

FREDDIE MAC
FINANCIAL REPORT FOR THE THREE AND SIX MONTHS
ENDED JUNE 30, 2007

**Information Statement Supplement to the 2006 Information Statement
and Annual Report to Stockholders, dated March 23, 2007**

This Information Statement Supplement contains important financial and other information about Freddie Mac and supplements our Information Statement and Annual Report to Stockholders for the fiscal year ended December 31, 2006, dated March 23, 2007, or 2006 Information Statement. Our 2006 Information Statement is supplemented periodically. All available supplements, including this Information Statement Supplement, should be read together with our 2006 Information Statement. We also provide information about the securities we issue in the offering circular for each securities program and any supplement for each particular offering. You can obtain copies of our 2006 Information Statement, offering circulars, available supplements, financial reports and other similar information by visiting our website (www.freddiemac.com) or by writing or calling us at:

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THIS INFORMATION STATEMENT SUPPLEMENT IS DATED AUGUST 30, 2007

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This Information Statement Supplement includes forward-looking statements, which may include expectations and objectives related to our operating results, financial condition, business, remediation of internal controls, credit losses, market share and trends and other matters. You should not rely unduly on our forward-looking statements. Actual results might differ significantly from those described or implied in such forward-looking statements due to various factors and uncertainties, including those described in (i) "MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS," or MD&A, "FORWARD-LOOKING STATEMENTS" and "RISK FACTORS" in this Information Statement Supplement and in the comparably captioned sections of the 2006 Information Statement and (ii) the "BUSINESS" section of the 2006 Information Statement. These forward-looking statements are made as of the date of this Information Statement Supplement and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date of this Information Statement Supplement, or to reflect the occurrence of unanticipated events.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
EXECUTIVE SUMMARY**

Our Business

Freddie Mac is a stockholder-owned company chartered by Congress in 1970 to stabilize the nation's residential mortgage markets and expand opportunities for homeownership and affordable rental housing. Our mission is to provide liquidity, stability and affordability to the U.S. housing market. We fulfill our mission by purchasing residential mortgage loans and mortgage-related securities in the secondary mortgage market. We are one of the largest purchasers of mortgage loans in the U.S. We purchase mortgage loans and bundle them into mortgage-related securities that can be sold to investors. We can use the proceeds to purchase additional mortgage loans from primary market mortgage lenders, thus providing them with a continuous flow of funds. We also purchase mortgage loans and mortgage-related securities for our investments portfolio. We finance our purchases for our investments portfolio and manage associated interest-rate and other market risks primarily by issuing a variety of debt instruments and entering into derivative contracts in the capital markets.

Though we are chartered by Congress, our business is funded completely with private capital. We alone are responsible for making payments on our securities. Neither the U.S. government nor any other agency or instrumentality of the U.S. government is obligated to fund our mortgage purchase or financing activities or to guarantee our securities or other obligations.

We generate income primarily through two business activities — Retained portfolio investment activities and credit guarantee activities. To achieve our objective for long-term growth of the fair value of our net assets, we focus on three long-term business drivers — the profitability of new investment and guarantee business, growth in our investment and credit guarantee portfolios and market share. Our requirements and responsibilities under the Federal Home Loan Mortgage Corporation Act, which we refer to as our charter, and affordable housing goals and subgoals set for us by the U.S. Department of Housing and Urban Development, or HUD, require that we make trade-offs in our business that affect each of these drivers. Our purchases of mortgage loans benefiting low- and moderate-income families and neighborhoods are an integral part of our mission and business. We are committed to fulfilling the needs of these borrowers and markets.

Retained Portfolio Investment Activities

Through our Retained portfolio investment activities, we seek to maximize long-term growth in the fair value of our net assets while maintaining a disciplined approach to interest-rate risk management. We accomplish this primarily by opportunistically purchasing and, to a lesser extent, selling mortgage assets to improve investment returns, while meeting the requirements of our charter and supporting the affordable housing goals and subgoals set for us by HUD. We estimate our expected investment returns using a mortgage-to-debt option-adjusted spread, or OAS, approach. We select our investments for purchase and sale primarily based on these expected returns and our market expertise.

As discussed in our 2006 Information Statement, we currently manage our Retained portfolio under a voluntary temporary growth limit. The carrying value of our Retained portfolio was approximately \$703 billion at June 30, 2007, approximately \$21 billion below the voluntary temporary growth limit at that date. While operating under this limit, we continue to be selective about the new investments we make and securities we retain in an effort to enhance investment returns.

For the six months ended June 30, 2007, the unpaid principal balance of our Retained portfolio increased by two percent on an annualized basis. However, for the three months ended June 30, 2007, the unpaid principal balance of our Retained portfolio decreased at an annualized rate of one percent. Continued lower demand for mortgage-related

securities from depository institutions and foreign investors, along with heightened market uncertainty, has resulted in wider mortgage-to-debt OAS, while providing favorable investment opportunities in the market towards the end of June and into the third quarter of 2007.

In keeping with our strategy of maximizing mortgage-to-debt OAS returns on our Retained portfolio, we entered into sales of seasoned securities and purchase commitments for favorable investments. The sales of approximately \$31 billion in unpaid principal balances, which occurred primarily in June and July 2007, generated net losses which are included in Gains (losses) on investment activity for the six months ended June 30, 2007. We recognized losses on these sales because the securities sold had lower coupon rates than those available in the market at the time of sale. Less than \$1 million of these losses related to our non-agency mortgage-related securities backed by subprime loans. During June 2007, we entered into approximately \$40 billion of net purchase commitments that were settled in June 2007 or are scheduled to settle in the third quarter of 2007. Over the long term, we expect that these activities will result in higher economic returns and ultimately improve future net income.

Participants in the mortgage market often characterize single-family loans based on their overall credit quality at the time of origination, generally considering them to be prime, Alt-A, or subprime. Although there are no universally accepted definitions of Alt-A or subprime loans, these segments of the market primarily serve borrowers with poor credit payment histories and such loans typically have a mix of credit characteristics, such as high loan-to-value, or LTV, ratios, low credit scores or originations using lower underwriting standards such as limited or no documentation of a borrower's income.

At June 30, 2007 and December 31, 2006, we held investments of approximately \$119 billion and \$124 billion, respectively, of non-agency mortgage-related securities backed by subprime loans. These securities include significant credit enhancements, particularly through subordination, and approximately 99.9 percent of these securities held at June 30, 2007 were rated AAA at August 27, 2007. See "RISK MANAGEMENT — Credit Risks — *Mortgage Credit Risk — Subprime Loans*" for additional information regarding our subprime exposure.

At June 30, 2007 and December 31, 2006, we believe that \$55 billion and \$54 billion, respectively, of our single-family non-agency mortgage-related securities not backed by subprime loans are generally backed by Alt-A mortgage loans. These securities include significant credit enhancements, particularly through subordination. Approximately 99.9 percent of these securities held at June 30, 2007 were rated AAA at August 27, 2007. See "RISK MANAGEMENT — Credit Risks — *Mortgage Credit Risk — Alt-A Loans*" for additional information regarding Alt-A mortgage loans.

We fund our cash requirements, including the purchase of mortgage-related securities into the Retained portfolio, primarily by issuing short-term and long-term debt. During the six months ended June 30, 2007, demand for our debt securities remained strong, allowing us to maintain an average cost of funds significantly below the London Interbank Offered Rate, or LIBOR.

We use derivatives primarily to: (a) regularly adjust or rebalance our funding mix in order to more closely match changes in the interest-rate characteristics of our mortgage assets; (b) hedge forecasted issuances of debt and synthetically create callable and non-callable funding; and (c) hedge foreign currency exposure. For the six months ended June 30, 2007, we experienced losses on our derivatives portfolio not in hedge accounting relationships compared to gains for the six months ended June 30, 2006. Fluctuations in interest rates and a decline in implied volatility during the three months ended March 31, 2007 resulted in losses on our derivatives portfolio, which were only partially offset by increases in interest rates and implied volatility during the three months ended June 30, 2007. During the six months ended June 30, 2006, an increase in interest rates resulted in gains recorded to Derivatives gains (losses) within our U.S. generally accepted accounting principles, or GAAP, earnings.

Credit Guarantee Activities

We seek to grow our credit guarantee portfolio by issuing guarantees that we believe offer attractive long-term returns relative to anticipated credit costs. During the six months ended June 30, 2007, the credit markets were increasingly volatile and the securitization market continued to be competitive. As a result of competitive pressure on our guarantee fees, some of our new credit guarantee business was acquired below our normal expected return thresholds. See "CONSOLIDATED RESULTS OF OPERATIONS — Non-Interest Expense — *Losses on Certain Credit Guarantees*," for additional information.

Our purchase volumes are impacted by several factors, including origination volumes, mortgage product and underwriting trends, competition, customer-specific behavior and contract terms. For example, many of our larger customers have contracts that require them to sell, subject to certain conditions and exclusions, a specified minimum share of their government-sponsored enterprise, or GSE, business to us. Mortgage purchase volumes from individual customers can fluctuate significantly based on changes in their GSE business volumes. During the six months ended

June 30, 2007, more than 75 percent of our guaranteed securitization volume originated from our ten largest customers. One of our customers, which accounted for more than ten percent of our mortgage purchase volume for the six months ended June 30, 2007, reduced its minimum mortgage volume commitments to us upon renewal of its contract at July 1, 2007. In addition, ABN Amro Mortgage Group, Inc., which accounted for more than eight percent of our guaranteed securitization volume for the six months ended June 30, 2007, was acquired and therefore the contract will not be renewed when it expires in the third quarter of 2007.

During the six months ended June 30, 2007 and 2006, the annualized growth rates of our credit guarantee portfolio were 16 percent and 11 percent, respectively. We estimate that our share of the GSE securitization market increased to approximately 45 percent for the six months ended June 30, 2007 from approximately 43 percent for the six months ended June 30, 2006. Our GSE securitization market share is expected to decline in the second half of 2007 due to a decrease in future commitments with some of our major customers. However, we expect that our share of the overall mortgage securitization market should increase as mortgage originators tighten their credit standards.

We estimate that approximately \$2 billion, or 0.1 percent and \$3 billion, or 0.2 percent, of loans underlying our single-family mortgage portfolio, at June 30, 2007 and December 31, 2006, respectively, were backed by subprime mortgage loans. In addition, we estimate that approximately \$120 billion, or eight percent, of loans underlying our single-family mortgage portfolio at June 30, 2007, were backed by Alt-A mortgage loans. See “RISK MANAGEMENT — Credit Risks — *Mortgage Credit Risk*” for additional information regarding our subprime and Alt-A mortgage loans.

The U.S. residential mortgage market continued to weaken during the three and six months ended June 30, 2007, as the rate of home price appreciation generally continued to decline, with significant variations across regions and metropolitan areas. Estimates of nationwide home price appreciation for the full year of 2007 vary widely, with most indicating a slight overall decline in home prices and others indicating low or no growth. We expect this trend to continue into 2008. Home price appreciation is an important market indicator for us because it reflects the general trend in value associated with the single-family mortgage loans underlying our mortgage Participation Certificates, or PCs, and Structured Securities. As home prices decline, the risk of borrower defaults and the severity of credit losses generally will increase.

Turmoil in the mortgage market during the six months ended June 30, 2007 has led to an increase in mortgage and credit risk pricing which had a direct, negative impact on the valuation of our guarantee-related obligations. We expect further deterioration in the value of our guarantee-related obligations in the third quarter of 2007 as market conditions continue to worsen.

For the six months ended June 30, 2007 and 2006, the valuations of our guarantee-related obligations were reflected in our GAAP results as follows:

- Losses on PC residuals, a component of Gains (losses) on investment activity, of \$66 million and gains of \$289 million, respectively;
- Losses on certain credit guarantees of \$331 million and \$98 million, respectively; and
- Losses on loans purchased of \$375 million and \$42 million, respectively.

The losses experienced in the six months ended June 30, 2007 were partially offset by the impact of increases in interest rates on our guarantee-related assets for the six months ended June 30, 2007, which resulted in valuation gains primarily reflected in Gains (losses) on Guarantee asset.

The fair value of our guarantee-related obligations implies higher future credit losses than we expect to incur. We estimate the fair value of our Guarantee obligation based on the amount we would expect to pay a third party with comparable credit quality to assume the obligation under our guarantee contract. Losses on certain credit guarantees represent losses recognized upon the issuance of PCs in guarantor swap transactions when, for a particular pool of loans, the initial fair value of the Guarantee obligation exceeds the total of the initial fair value of the Guarantee asset, the initial fair value of any related credit enhancements, any buy-downs received or buy-ups paid and any credit fees received. We estimate fair value for delinquent loans we purchase out of PC pools based on prices we obtain from third-party market participants. We have not transferred any of our guarantee obligations or sold delinquent loans to third parties. Ultimate realization of these losses will be based on the actual credit losses we experience on the underlying portfolio.

We manage our mortgage credit risk on delinquent loans through the use of credit enhancements and loss mitigation activities. Our single-family loss mitigation strategy emphasizes early intervention for delinquent mortgage loans and provides alternatives to foreclosure. Other single-family loss mitigation activities include providing our single-family servicers with default management tools designed to help them manage non-performing loans more effectively and to assist borrowers in retaining their homes. See “MD&A — RISK MANAGEMENT — Credit Risks — *Mortgage Credit*

Risk — Loss Mitigation Activities” in our 2006 Information Statement for more information regarding our loss mitigation activities.

Recent declining home price appreciation has contributed to the increase in the weighted average current LTV ratio to 60 percent at June 30, 2007, as compared to 57 percent at December 31, 2006. The percent of loans in our portfolio with current LTV ratios above 90 percent was four percent at June 30, 2007, compared to two percent at December 31, 2006. Our portfolio remains geographically well-diversified. Despite an increase in the purchase of interest-only mortgages during the three and six months ended June 30, 2007, long-term fixed-rate mortgages comprised approximately 80 percent of our credit guarantee portfolio at June 30, 2007. Interest-only mortgages comprised approximately 25 percent of our mortgage loan purchases for the six months ended June 30, 2007 and approximately eight percent of our total credit guarantee portfolio at June 30, 2007, compared to approximately 13 percent of our mortgage loan purchases for the six months ended June 30, 2006 and approximately three percent of our total credit guarantee portfolio at June 30, 2006. The increase in purchases of interest-only mortgages reflects the increase in originations of this product in the market. Although we charge higher guarantee fees for interest-only mortgages, we have limited historical experience with this product.

For the six months ended June 30, 2007, our single-family credit guarantee portfolio continued to experience increases in the rate at which loans transitioned from delinquency to foreclosure and higher losses on a per-property basis. As a result of the observed credit deterioration, we increased our loan loss reserves by \$370 million to \$790 million at June 30, 2007 from \$420 million at December 31, 2006. We expect to make further additions to our loan loss reserves in future periods, particularly related to interest-only mortgages and mortgages originated in 2006 and 2007. The impact of the weakening housing market was most evident in areas of the country where unemployment rates continued to be high, such as the North Central region. While the impact of the weakening housing market in the East and West coastal regions of the country has generally been less than in other regions, we experienced an increase in delinquency rates and real estate owned, or REO, activity in those regions during the three months ended June 30, 2007.

We incur credit losses at or after the point of foreclosure through the time when we dispose of the property. This provides a view of how initial estimates of credit losses are ultimately incurred. For the three months ended June 30, 2007, our annualized credit losses were 2.0 basis points of the average Total mortgage portfolio, excluding non-Freddie Mac securities. This compares to an annualized credit loss of 1.3 basis points for the three months ended June 30, 2006 and 1.4 basis points for the year ended December 31, 2006. We expect our credit losses to continue to increase in 2007 and 2008, especially if conditions, such as home price appreciation rates, deteriorate.

Summary of Financial Results for the Three and Six Months Ended June 30, 2007

GAAP Results

For the three months ended June 30, 2007, we reported Net income of \$764 million, or \$1.02 per diluted share, compared to \$1.4 billion, or \$1.93 per diluted share, for the three months ended June 30, 2006. Lower Net income was primarily due to lower Net interest income and higher credit-related costs, partially offset by higher Non-interest income.

For the six months ended June 30, 2007, we reported Net income of \$553 million, or \$0.55 per diluted share, compared to \$3.4 billion, or \$4.73 per diluted share, for the six months ended June 30, 2006. Lower Net income was primarily due to Derivative gains (losses), Gains (losses) on investment activity and higher Non-interest expense.

Net interest income was \$973 million for the three months ended June 30, 2007, compared to \$1.2 billion for the three months ended June 30, 2006. Net interest income decreased to \$2.0 billion for the six months ended June 30, 2007 from \$2.3 billion for the six months ended June 30, 2006. The decline in Net interest income reflected higher replacement costs associated with funding of our Retained portfolio as our long-term debt interest costs increased. Our long-term debt costs increased as lower rate debt matured and was replaced by higher rate debt.

Management and guarantee income increased to \$474 million for the three months ended June 30, 2007 from \$389 million for the three months ended June 30, 2006, as the average balance of outstanding PCs increased 18 percent and the total guarantee fee rate increased to 15.7 basis points from 15.3 basis points. For the six months ended June 30, 2007 and 2006, Management and guarantee income increased to \$934 million from \$802 million and the total guarantee fee rate was 15.9 basis points for both periods.

For the three months ended June 30, 2007, other components of Non-interest income totaled \$808 million compared to \$590 million for the three months ended June 30, 2006. The other components of Non-interest income for the three months ended June 30, 2007 included \$822 million of valuation gains, compared to gains of \$504 million for the three months ended June 30, 2006. The other components of Non-interest income that are impacted by valuation gains (losses) primarily include Derivative gains (losses), Gains (losses) on Guarantee asset, Gains (losses) on PC residuals as well as Security impairments. The change in valuation gains (losses) was primarily attributable to the impact of increasing long-term interest rates, resulting in gains related to the Guarantee asset associated with our securitization activities.

For the six months ended June 30, 2007, other components of Non-interest income (loss) totaled \$(206) million compared to \$1.5 billion for the six months ended June 30, 2006. The other components of Non-interest income (loss) for the six months ended June 30, 2007 included \$232 million of valuation losses primarily due to derivatives, compared to gains of \$1.2 billion for the six months ended June 30, 2006. The change in valuation gains (losses) was primarily attributable to the impact of increasing long-term interest rates, resulting in derivatives losses.

For the three months ended June 30, 2007 and 2006, our Provision for credit losses and REO operations expense were \$336 million and \$63 million, respectively. For the three months ended June 30, 2007, our Provision for credit losses increased due to continued credit deterioration in our single-family credit guarantee portfolio as more loans transitioned from delinquency to foreclosure and the expected severity of losses on a per-property basis increased.

For the six months ended June 30, 2007 and 2006, our Provision for credit losses and REO operations expense were \$529 million and \$39 million, respectively. We experienced credit weakness and increased severity of losses on a per-property basis in the six months ended June 30, 2007. The Provision for credit losses for the six months ended June 30, 2006 included the reversal of \$84 million of reserves previously recorded for properties affected by Hurricane Katrina because related payment and delinquency experience on affected properties was better than expected.

Other non-interest expense includes Losses on certain credit guarantees and Losses on loans purchased, which totaled \$392 million for the three months ended June 30, 2007, compared to \$73 million for the three months ended June 30, 2006. Losses on certain credit guarantees and Losses on loans purchased totaled \$706 million for the six months ended June 30, 2007, compared to \$140 million for the six months ended June 30, 2006. These increases were primarily due to losses related to higher fair values of credit costs on certain guarantees associated with new business activity, a decline in the fair values of non-performing loans purchased out of PC pools and an increase in the volume of non-performing loan purchases. See “CONSOLIDATED RESULTS OF OPERATIONS — Non-Interest Expense — Losses on Certain Credit Guarantees,” for additional information.

For the three months ended June 30, 2007 and 2006, we reported income tax expense of \$113 million and \$40 million, respectively. For the six months ended June 30, 2007 and 2006, we reported income tax benefit of \$326 million and \$75 million, respectively. While both periods reflect benefits from our investments in low-income housing tax credit, or LIHTC, partnerships and interest earned on tax-exempt housing-related securities, the six months ended June 30, 2006 also benefited from our application of Financial Accounting Standards Board Interpretation No. 18, “Accounting for Income Taxes in Interim Periods, an interpretation of APB Opinion No. 28,” and tax reserve releases. See “NOTE 12: INCOME TAXES” to our consolidated financial statements for additional information about how our effective tax rate was determined.

Capital Management

Our primary objective in managing capital is preserving our safety and soundness. We also seek to have sufficient capital to support our business and mission. As appropriate, we will consider opportunities to return excess capital to stockholders and to optimize our capital structure. At June 30, 2007, our estimated regulatory core capital was \$36.3 billion, which is an estimated \$9.8 billion in excess of our regulatory minimum capital requirement and \$1.8 billion in excess of the 30 percent mandatory target capital surplus.

We completed two offerings of non-cumulative, perpetual preferred stock with aggregate proceeds of \$1.6 billion during the six months ended June 30, 2007. We also repurchased \$750 million (approximately 11.9 million shares) of outstanding common stock. Subsequent to June 30, 2007, we issued another \$500 million of non-cumulative, perpetual preferred stock in July 2007. We also repurchased an additional \$250 million (approximately 4.2 million shares) of common stock through August 6, 2007.

We paid a quarterly dividend per common share of \$0.50 for each of the first two quarters of 2007.

Fair Value Results

We use estimates of fair value on a routine basis to make decisions about our business activities. Our consolidated fair value measurements are a component of our risk management processes, as we use daily estimates of the changes in fair value to calculate our Portfolio Market Value Sensitivity, or PMVS, and duration gap measures. In addition, we use fair value-derived performance measures to establish corporate objectives and as a factor in determining management compensation.

During the three months ended June 30, 2007, the fair value of net assets attributable to common stockholders, before capital transactions, increased by \$0.8 billion, resulting in an annualized return on the average fair value of net assets attributable to common stockholders of approximately 12.4 percent, compared to a \$1.4 billion increase, or approximately 20.6 percent annualized return, during the three months ended June 30, 2006.

During the six months ended June 30, 2007, the fair value of net assets attributable to common stockholders, before capital transactions, increased by \$0.5 billion, resulting in an annualized return on the average fair value of net assets attributable to common stockholders of approximately 3.9 percent, compared to a \$2.4 billion increase, or approximately 17.7 percent annualized return, during the six months ended June 30, 2006.

Our attribution of changes in the fair value of net assets relies on models, assumptions and other measurement techniques that evolve over time. The following attribution of changes in fair value reflects our current estimate of the items presented (on a pre-tax basis) and excludes the effect of returns on capital and administrative expenses.

During the three months ended June 30, 2007, our investment activities decreased fair value by approximately \$0.8 billion. This estimate includes declines in fair value of approximately \$1.4 billion attributable to the net widening of mortgage-to-debt OAS.

During the six months ended June 30, 2007, our investment activities decreased fair value by approximately \$0.4 billion. This estimate includes declines in fair value of approximately \$1.7 billion attributable to the net widening of mortgage-to-debt OAS.

Our investment activities increased fair value by an estimated \$1.0 billion during the three months ended June 30, 2006. This estimate includes increases in fair value of approximately \$0.1 billion attributable to the net tightening of mortgage-to-debt OAS.

Our investment activities increased fair value by an estimated \$0.9 billion during the six months ended June 30, 2006. This estimate includes declines in fair value of approximately \$0.6 billion attributable to the net widening of mortgage-to-debt OAS.

Our credit guarantee activities increased fair value by an estimated \$1.8 billion during the three months ended June 30, 2007. This increase includes the receipt of cash primarily related to management, guarantee and other up-front fees. This increase also includes a fair value increase related to our single-family guarantee asset of approximately \$1.7 billion, primarily attributable to an increase in interest rates during the three months ended June 30, 2007. These increases were partially offset by an increase in the fair value of our single-family guarantee obligation of approximately \$0.6 billion.

Our credit guarantee activities increased fair value by approximately \$0.6 billion during the six months ended June 30, 2007. This increase includes the receipt of cash primarily related to management, guarantee and other up-front fees. This increase also includes a fair value increase related to our single-family guarantee asset of approximately \$1.9 billion, primarily attributable to an increase in interest rates during the period. These increases were partially offset by an increase in the fair value of our single-family guarantee obligation of approximately \$2.6 billion due in part to the increased uncertainty in the mortgage market during the six months ended June 30, 2007.

During the three months ended June 30, 2006, our credit guarantee activities increased fair value by an estimated \$1.2 billion. This estimate includes a fair value increase related to our single-family guarantee asset of approximately \$0.5 billion with the remainder primarily due to the receipt of cash related to management, guarantee and other up-front fees.

During the six months ended June 30, 2006, our credit guarantee activities increased fair value by an estimated \$2.3 billion. This estimate includes a fair value increase related to our single-family guarantee asset of approximately \$1.3 billion with the remainder primarily due to the receipt of cash related to management, guarantee and other up-front fees.

Business Outlook — Fair Value Returns

Our objective is to achieve long-term returns, before capital transactions, on the average fair value of net assets attributable to common stockholders in the low-to mid-teens, although period-to-period returns may fluctuate substantially due to market conditions. This long-term objective is based on assumptions regarding rates of growth in our business, spreads that we expect to earn and a return over a period of years to capital levels consistent with current statutory requirements, among other factors. Our assumptions do not contemplate that the challenging market conditions and competitive pressures we are currently experiencing will continue through the next several years. We have also made no assumptions regarding any potential impact of pending legislation or regulatory actions, discussed more extensively in “Legislative and Regulatory Matters.” Our actual results may differ materially from these expectations.

Risk Management

Our Retained portfolio investment and credit guarantee activities expose us to three broad categories of risk: (a) operational risks; (b) interest-rate risk and other market risks; and (c) credit risks. Risk management is a critical aspect of our business. We must effectively manage risk to accomplish our mission and generate revenue and long-term value. We continued to make progress on initiatives to improve our financial reporting infrastructure and remediate

material weaknesses and other deficiencies in our internal controls. We continue to have a significant number of material weaknesses and other internal control deficiencies that have not been fully remediated and considerable challenges remain. See “RISK MANAGEMENT — Operational Risks” for additional information regarding our remediation activities.

Our interest-rate risk remains low. For the three months ended June 30, 2007 and 2006, PMVS-Level, or PMVS-L, and duration gap averaged one percent and zero months, respectively.

See “RISK MANAGEMENT — Credit Risks” for additional information regarding our credit risk exposures.

Legislative and Regulatory Matters

GSE Oversight Legislation

We face a highly uncertain regulatory environment in light of GSE regulatory oversight legislation currently under consideration in Congress. We generate a significant portion of our Net income through our Retained portfolio. Currently, we have in place a voluntary temporary growth limit on our Retained portfolio. The House of Representatives passed GSE regulatory oversight legislation on May 22, 2007. This legislation would give our regulator substantial authority to assess our safety and soundness and to regulate our portfolio investments, including requiring reductions in those investments, consistent with our mission and safe and sound operations. This legislation includes provisions that would increase the regulator’s authority to require us to maintain higher minimum and risk-based capital levels and, for 2007 through 2011, require us to make an annual contribution to an affordable housing fund in an amount equal to 1.2 basis points of the average aggregate unpaid principal balance of our Total mortgage portfolio. This legislation also includes provisions that would give our regulator enhanced authority to regulate our business activities, which could constrain our ability to respond quickly to a changing marketplace. See “REGULATION AND SUPERVISION — GSE Regulatory Oversight Legislation” in our 2006 Information Statement for more information regarding this bill. We cannot predict the prospects for the enactment, timing or content of any final legislation. The provisions of this legislation could have a material adverse effect on our ability to fulfill our mission, future earnings, stock price and stockholder returns, rate of growth of fair value of net assets attributable to common stockholders and our ability to recruit and retain qualified officers and directors.

Guidance on Non-traditional Mortgage Product Risks and Subprime Mortgage Lending

The Office of Federal Housing Enterprise Oversight, or OFHEO, has directed us to adopt practices consistent with the risk management, underwriting and consumer protection principles of the “Interagency Guidance on Non-traditional Mortgage Product Risks,” or Interagency Guidance, and the “Statement on Subprime Mortgage Lending,” or the Subprime Statement, jointly issued by five federal financial institution regulatory agencies, for non-traditional mortgages and subprime short-term hybrid adjustable-rate mortgages, or ARMs, that we purchase or which back non-agency mortgage-backed securities in which we invest. In response, on July 13, 2007 we informed our customers of new underwriting and disclosure requirements for non-traditional mortgages. In the near future, we will be informing our customers and other counterparties of similar new requirements for subprime short-term hybrid ARMs we purchase and for both subprime short-term hybrid ARMs and non-traditional mortgages backing non-agency mortgage-backed securities in which we invest. These new requirements are also consistent with our announcement in February 2007 that we would implement stricter investment standards for certain subprime ARMs originated after September 1, 2007, and develop new mortgage products providing lenders with more choices to offer subprime borrowers. These changes could reduce the number of non-traditional and subprime mortgages available to us for purchase, potentially affecting our profitability or our ability to achieve our housing goals and subgoals.

SELECTED FINANCIAL DATA AND OTHER OPERATING MEASURES⁽¹⁾

	At or for the Six Months Ended June 30,		At or for the Year Ended December 31,				
	2007	2006	2006	2005	2004	2003	2002
	(unaudited)		(dollars in millions, except share-related amounts)				
Income Statement Data							
Net interest income	\$ 1,951	\$ 2,303	\$ 4,235	\$ 5,370	\$ 9,137	\$ 9,498	\$ 9,525
Non-interest income (loss)	728	2,326	915	199	(3,039)	(244)	7,154
Net income before cumulative effect of changes in accounting principles	553	3,406	2,211	2,189	2,937	4,816	10,090
Cumulative effect of changes in accounting principles, net of taxes	—	—	—	(59)	—	—	—
Net income	553	3,406	2,211	2,130	2,937	4,816	10,090
Net income available to common stockholders	\$ 362	\$ 3,284	\$ 1,936	\$ 1,907	\$ 2,727	\$ 4,600	\$ 9,851
Earnings per common share before cumulative effect of changes in accounting principles:							
Basic	\$ 0.55	\$ 4.74	\$ 2.84	\$ 2.84	\$ 3.96	\$ 6.69	\$ 14.22
Diluted	0.55	4.73	2.84	2.83	3.94	6.68	14.17
Earnings per common share after cumulative effect of changes in accounting principles:							
Basic	\$ 0.55	\$ 4.74	\$ 2.84	\$ 2.76	\$ 3.96	\$ 6.69	\$ 14.22
Diluted	0.55	4.73	2.84	2.75	3.94	6.68	14.17
Dividends per common share	\$ 1.00	\$ 0.94	\$ 1.91	\$ 1.52	\$ 1.20	\$ 1.04	\$ 0.88
Weighted average common shares outstanding (in thousands):							
Basic	657,103	692,290	680,856	691,582	689,282	687,094	692,727
Diluted	659,365	693,755	682,664	693,511	691,521	688,675	695,116
Balance Sheet Data							
Total assets	\$ 821,673	\$ 855,654	\$ 813,081	\$ 806,222	\$ 795,284	\$ 803,449	\$ 752,249
Senior debt due within one year	276,974	306,328	294,861	288,532	282,303	295,262	244,429
Senior debt due after one year	478,295	488,227	452,677	454,627	443,772	438,738	415,662
Subordinated debt due after one year	5,227	6,879	6,400	5,633	5,622	5,613	5,605
Miscellaneous liabilities ⁽²⁾	35,085	29,739	30,326	29,290	30,662	30,420	52,914
Minority interests in consolidated subsidiaries	282	746	516	949	1,509	1,929	2,309
Stockholders' equity	25,810	23,735	28,301	27,191	31,416	31,487	31,330
Portfolio Balances⁽³⁾							
Retained portfolio (unpaid principal balances) ⁽⁴⁾	\$ 712,136	\$ 722,538	\$ 703,959	\$ 710,346	\$ 653,261	\$ 645,767	\$ 567,366
Total Guaranteed PCs and Structured Securities issued (unpaid principal balances) ⁽⁵⁾	1,592,524	1,405,684	1,477,023	1,335,524	1,208,968	1,162,068	1,090,624
Total mortgage portfolio (unpaid principal balances)	1,952,949	1,759,767	1,826,720	1,684,546	1,505,531	1,414,700	1,316,703
Ratios							
Return on average assets ⁽⁶⁾	0.1%	0.8%	0.3%	0.3%	0.4%	0.6%	1.4%
Return on common equity ⁽⁷⁾	3.5	31.5	8.6	7.7	10.2	17.2	47.2
Return on total equity ⁽⁸⁾	4.1	26.8	8.0	7.3	9.3	15.3	39.6
Dividend payout ratio on common stock ⁽⁹⁾	183.1	20.0	67.7	56.4	30.7	15.6	6.2
Equity to assets ratio ⁽¹⁰⁾	3.3	3.1	3.4	3.7	3.9	4.0	3.7

(1) Effective January 1, 2007, we adopted Financial Accounting Standards Board, or FASB, Statement of Financial Accounting Standards No. 155, "Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140," or SFAS 155, and FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109," or FIN 48. See "SELECTED FINANCIAL DATA" in our 2006 Information Statement for information regarding accounting changes impacting periods prior to January 1, 2007.

(2) Includes: (a) Due to Participation Certificate investors; (b) Accrued interest payable; (c) Guarantee obligation; (d) Derivative liabilities, at fair value; (e) Reserve for guarantee losses on Participation Certificates; and (f) Other liabilities, as presented on our consolidated balance sheets.

(3) Excludes mortgage loans and mortgage-related securities traded, but not yet settled.

(4) The Retained portfolio presented on our consolidated balance sheets differs from the Retained portfolio in this table because the consolidated balance sheet caption includes valuation adjustments and deferred balances. See "CONSOLIDATED BALANCE SHEETS ANALYSIS — Table 10 — Characteristics of Mortgage Loans and Mortgage-Related Securities in the Retained Portfolio" for more information.

(5) Excludes Structured Securities where we have resecuritized PCs and other previously issued Structured Securities. These excluded Structured Securities do not increase our credit-related exposure and consist of single-class Structured Securities backed by PCs, Real Estate Mortgage Investment Conduits, or REMICs, and principal-only strips. The notional balances of interest-only strips are excluded because this line item is based on unpaid principal balance. Also excluded from this line item are modifiable and combinable REMIC tranches and interest and principal classes where the holder has the option to exchange the security tranches for other pre-defined security tranches.

(6) Year-to-date computations are computed as annualized year-to-date Net income divided by the simple average of the beginning and ending balances of Total assets.

(7) Year-to-date computations are computed as annualized year-to-date Net income available to common stockholders divided by the simple average of the beginning and ending balances of Stockholders' equity, net of preferred stock (at redemption value).

(8) Year-to-date computations are computed as annualized year-to-date Net income divided by the simple average of the beginning and ending balances of Stockholders' equity.

(9) Year-to-date computations are computed as year-to-date Common stock dividends declared divided by year-to-date Net income available to common stockholders.

(10) Year-to-date computations are calculated as the simple average of the beginning and ending balances of Stockholders' equity divided by the simple average of the beginning and ending balances of Total assets.

CONSOLIDATED RESULTS OF OPERATIONS

The following discussion of our consolidated results of operations should be read in conjunction with our consolidated financial statements, including the accompanying notes. Also see “CRITICAL ACCOUNTING POLICIES AND ESTIMATES” for more information concerning our more significant accounting policies and estimates applied in determining our reported financial position and results of operations.

Table 1 — Summary Consolidated Statements of Income

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Net interest income	\$ 973	\$1,172	\$ 1,951	\$ 2,303
Non-interest income:				
Management and guarantee income	474	389	934	802
Gains (losses) on Guarantee asset	739	61	329	221
Income on Guarantee obligation	281	217	493	412
Derivative gains (losses)	281	355	(247)	628
Gains (losses) on investment activity	(368)	(312)	(551)	(146)
Foreign currency losses, net	(333)	(30)	(530)	(33)
Other	208	299	300	442
Non-interest income	<u>1,282</u>	<u>979</u>	<u>728</u>	<u>2,326</u>
Non-interest expense	<u>(1,378)</u>	<u>(714)</u>	<u>(2,452)</u>	<u>(1,298)</u>
Income before income tax (expense) benefit	877	1,437	227	3,331
Income tax (expense) benefit	(113)	(40)	326	75
Net income	<u>\$ 764</u>	<u>\$1,397</u>	<u>\$ 553</u>	<u>\$ 3,406</u>

Net Interest Income

Table 2 presents an analysis of Net interest income, including average balances and related yields earned on assets and incurred on liabilities.

Table 2 — Net Interest Income/Yield and Average Balance Analysis

	Three Months Ended June 30,					
	2007			2006		
	Average Balance ⁽¹⁾⁽²⁾	Interest Income (Expense)	Average Rate	Average Balance ⁽¹⁾⁽²⁾	Interest Income (Expense)	Average Rate
	(dollars in millions)					
Interest-earning assets:						
Mortgage loans ⁽³⁾	\$ 67,994	\$ 1,079	6.35%	\$ 63,211	\$ 1,040	6.58%
Mortgage-related securities	647,094	8,960	5.54	661,747	8,878	5.37
Total Retained portfolio	715,088	10,039	5.62	724,958	9,918	5.47
Investments ⁽⁴⁾	49,106	634	5.11	59,576	707	4.69
Securities purchased under agreements to resell and Federal funds sold	24,887	332	5.33	32,840	412	5.02
Total interest-earning assets	<u>789,081</u>	<u>11,005</u>	5.58	<u>817,374</u>	<u>11,037</u>	5.40
Interest-bearing liabilities:						
Short-term debt	172,592	(2,249)	(5.16)	189,120	(2,241)	(4.69)
Long-term debt ⁽⁵⁾	581,482	(7,331)	(5.04)	595,030	(7,110)	(4.78)
Total debt securities	754,074	(9,580)	(5.07)	784,150	(9,351)	(4.75)
Due to Participation Certificate investors	9,061	(121)	(5.32)	8,082	(104)	(5.13)
Total interest-bearing liabilities	<u>763,135</u>	<u>(9,701)</u>	(5.07)	<u>792,232</u>	<u>(9,455)</u>	(4.76)
Expense related to derivatives	—	(331)	(0.17)	—	(410)	(0.21)
Impact of net non-interest-bearing funding	25,946	—	0.17	25,142	—	0.15
Total funding of interest-earning assets	<u>\$789,081</u>	<u>(10,032)</u>	(5.07)	<u>\$817,374</u>	<u>(9,865)</u>	(4.82)
Net interest income/yield		973	0.51		1,172	0.58
Fully taxable-equivalent adjustments ⁽⁶⁾		99	0.05		98	0.05
Net interest income/yield (fully taxable-equivalent basis)		<u>\$ 1,072</u>	0.56		<u>\$ 1,270</u>	0.63

	Six Months Ended June 30,					
	2007			2006		
	Average Balance ⁽¹⁾⁽²⁾	Interest Income (Expense)	Average Rate	Average Balance ⁽¹⁾⁽²⁾	Interest Income (Expense)	Average Rate
	(dollars in millions)					
Interest-earning assets:						
Mortgage loans ⁽³⁾	\$ 67,288	\$ 2,140	6.36%	\$ 62,994	\$ 2,080	6.60%
Mortgage-related securities	645,010	17,723	5.50	654,739	17,123	5.23
Total Retained portfolio	712,298	19,863	5.58	717,733	19,203	5.35
Investments ⁽⁴⁾	48,924	1,257	5.11	57,173	1,299	4.52
Securities purchased under agreements to resell and Federal funds sold	25,684	681	5.30	24,525	594	4.85
Total interest-earning assets	786,906	21,801	5.54	799,431	21,096	5.28
Interest-bearing liabilities:						
Short-term debt	171,921	(4,457)	(5.16)	188,939	(4,256)	(4.48)
Long-term debt ⁽⁵⁾	580,814	(14,507)	(4.99)	577,637	(13,543)	(4.69)
Total debt securities	752,735	(18,964)	(5.03)	766,576	(17,799)	(4.64)
Due to Participation Certificate investors	8,364	(224)	(5.35)	7,530	(195)	(5.16)
Total interest-bearing liabilities	761,099	(19,188)	(5.04)	774,106	(17,994)	(4.64)
Expense related to derivatives	—	(662)	(0.17)	—	(799)	(0.21)
Impact of net non-interest-bearing funding	25,807	—	0.17	25,325	—	0.15
Total funding of interest-earning assets	\$786,906	(19,850)	(5.04)	\$799,431	(18,793)	(4.70)
Net interest income/yield		1,951	0.50		2,303	0.58
Fully taxable-equivalent adjustments ⁽⁶⁾		194	0.05		190	0.05
Net interest income/yield (fully taxable-equivalent basis)		\$ 2,145	0.55		\$ 2,493	0.63

(1) Excludes mortgage loans and mortgage-related securities traded, but not yet settled.

(2) For securities classified as available-for-sale, we calculated average balances based on their unpaid principal balance plus their associated deferred fees and costs (e.g., premiums and discounts), but excluded the effects of mark-to-fair-value changes. For securities in the Retained portfolio classified as trading, we calculated average balances excluding the effects of mark-to-fair-value adjustments.

(3) Non-performing loans, where interest income is recognized when collected, are included in average balances.

(4) Consist of Cash and cash equivalents and non-mortgage-related securities.

(5) Includes current portion of long-term debt.

(6) The determination of Net interest income/yield (fully taxable-equivalent basis), which reflects fully taxable-equivalent adjustments to interest income, involves the conversion of tax-exempt sources of interest income to the equivalent amounts of interest income that would be necessary to derive the same net return if the investments had been subject to income taxes using our statutory tax rate of 35 percent.

Net interest income and net interest yield on a fully taxable-equivalent basis decreased for the three and six months ended June 30, 2007, compared to the three and six months ended June 30, 2006. During the three and six months ended June 30, 2007, we experienced higher funding costs for our Retained portfolio as our long-term debt interest costs increased, reflecting the replacement of maturing debt that we issued at lower interest rates during the past few years to fund our investments in fixed-rate mortgage-related investments. The decrease in Net interest income and net interest yield on a fully taxable-equivalent basis was partially offset by a reduction in our mortgage-related securities premium amortization expense due to increases in interest rates and a decrease in our closed hedge amortization expense.

Effective January 1, 2006, we enhanced our process for forecasting interest rates and estimating prepayments used to amortize discounts, premiums and deferred fees for assets held in our Retained portfolio. This change in estimate resulted in a \$93 million pre-tax reduction in Net interest income on mortgage-related securities for the six months ended June 30, 2006.

Non-Interest Income

Management and Guarantee Income

Table 3 provides summary information about Management and guarantee income. Management and guarantee income consists of contractual amounts due to us related to our management and guarantee fees as well as amortization of certain pre-2003 deferred fees, including credit and buy-down fees. Other guarantee-related revenue is deferred and recognized over time as a component of Income on Guarantee obligation.

Table 3 — Management and Guarantee Income⁽¹⁾

	Three Months Ended June 30,				Six Months Ended June 30,			
	2007		2006		2007		2006	
	Amount	Rate	Amount	Rate	Amount	Rate	Amount	Rate
	(dollars in millions, rates in basis points)							
Contractual management and guarantee fees	\$483	16.0	\$393	15.4	\$934	15.9	\$780	15.5
Amortization of credit and buy-down fees included in Other liabilities ⁽²⁾	(9)	(0.3)	(4)	(0.1)	—	—	22	0.4
Total Management and guarantee income	<u>\$474</u>	<u>15.7</u>	<u>\$389</u>	<u>15.3</u>	<u>\$934</u>	<u>15.9</u>	<u>\$802</u>	<u>15.9</u>
Unamortized balance of credit and buy-down fees included in Other liabilities, at period end	<u>\$138</u>		<u>\$172</u>		<u>\$138</u>		<u>\$172</u>	

(1) Excludes amounts related to PCs we held in our Retained portfolio, which are reported in Net interest income.

(2) A change in estimate resulted in a net pre-tax increase in the Amortization of credit and buy-down fees of \$18 million during the six months ended June 30, 2006.

The primary drivers affecting Management and guarantee income are the average outstanding balance of our PCs and Structured Securities and changes in guarantee fee rates. Contractual management and guarantee fees include adjustments to the contractual rates for buy-ups and buy-downs, whereby the fee rate of the mortgage asset is adjusted for up-front cash payments made (buy-up) or received (buy-down) by us at origination. Our average rates of Management and guarantee income are also affected by the mix of products we issue, competition in market pricing and customer preference for buy-up and buy-down fees.

Management and guarantee income increased for the three and six months ended June 30, 2007, primarily reflecting an increase in the average outstanding PCs and Structured Securities balances of 18 percent and 16 percent, respectively, on an annualized basis. The average contractual management and guarantee fee rate increased for the three and six months ended June 30, 2007, predominantly due to an increase in buy-up activity during each period.

Gains (Losses) on Guarantee Asset

Upon issuance of a guarantee of securitized assets to third parties, we record a Guarantee asset on our consolidated balance sheets representing the fair value of the guarantee fees we expect to receive over the life of the related PCs or Structured Securities. Subsequent changes in the fair value of the Guarantee asset are reported in current period income as Gains (losses) on Guarantee asset.

The change in fair value of the Guarantee asset reflects:

- reductions related to the management and guarantee fees received that are considered a return of our recorded investment in the Guarantee asset; and
- changes in the future management and guarantee fees we expect to receive over the life of the related PC or Structured Security.

Table 4 — Attribution of Change — Gains (Losses) on Guarantee Asset

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Management and guarantee fees due	\$ (448)	\$(359)	\$(867)	\$(710)
Portion of Management and guarantee fees due related to imputed interest income	111	125	218	232
Return of investment on Guarantee asset	(337)	(234)	(649)	(478)
Change in fair value of future management and guarantee fees	1,021	295	948	659
Change in estimate ⁽¹⁾	55	—	30	40
Gains (losses) on Guarantee asset	<u>\$ 739</u>	<u>\$ 61</u>	<u>\$ 329</u>	<u>\$ 221</u>

(1) Represents changes in estimates resulting from enhancing our approach for determining the fair value of the Guarantee asset for the three and six months ended June 30, 2006 and 2007.

The fair value of future management and guarantee fees is driven by expected changes in interest rates that affect the estimated life of the mortgages underlying the outstanding PCs and Structured Securities and related discount rates used to determine the net present value of the cash flows. Our valuation methodology for the Guarantee asset uses market-based information, including market values of excess servicing, interest-only securities, to determine the fair value of future cash flows associated with the Guarantee asset. Fair value gains on the Guarantee asset increased for the three and six months ended June 30, 2007, compared to the three and six months ended June 30, 2006, primarily due to increases in interest rates which extended the expected life of the Guarantee asset. The increase in fair value gains for the three months ended June 30, 2007, compared to the three months ended June 30, 2006, was also due to tightening of spreads on excess servicing, interest-only securities during the three months ended June 30, 2007, resulting in higher market values for these assets.

Management and guarantee fees due represents income receipts in the current period related to PCs and Structured Securities held by third parties with an established Guarantee asset. A portion of management and guarantee fees due is attributed to imputed interest income on the Guarantee asset. Management and guarantee fees due increased for the three and six months ended June 30, 2007 compared to the three and six months ended June 30, 2006, respectively. These increases are primarily a result of increases in the average outstanding balance of our PCs and Structured Securities.

Income on Guarantee Obligation

Upon issuance of a guarantee of securitized assets to third parties, we record a Guarantee obligation on our consolidated balance sheet representing the fair value of our obligation to perform under the terms of the guarantee. Our Guarantee obligation is amortized into income in relation to the decline in the unpaid principal balance on the mortgage loans underlying the PCs and Structured Securities. Our Guarantee obligation consists of the following:

- Performance and other related costs, which consist of: estimated default costs, including unrecoverable principal and interest over the expected life of the underlying mortgages; estimated foreclosure-related costs; and estimated administrative and other costs related to our guarantee; and
- Deferred guarantee income on newly-issued Guarantor Swap transactions, which represents the excess of compensation received on issued guarantees and the fair value of our related Guarantee asset, compared to the fair value of our corresponding Guarantee obligation. Compensation received includes credit and buy-down fees received at the time of securitization. Credit fees vary with the relative credit quality of the underlying mortgages and buy-down fees vary based on customer compensation payment preferences.

Table 5 provides information about the components of Income on Guarantee obligation.

Table 5 — Income on Guarantee Obligation

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(dollars in millions)			
Amortization income:				
Performance and other related costs	\$ 192	\$ 143	\$ 332	\$ 276
Deferred guarantee income	89	74	161	136
Total Income on Guarantee obligation	<u>\$ 281</u>	<u>\$ 217</u>	<u>\$ 493</u>	<u>\$ 412</u>
Ending Guarantee obligation	\$8,574	\$6,173	\$8,574	\$6,173
Liquidation rate for outstanding PCs and Structured Securities	16%	16%	16%	16%

Amortization income increased for the three and six months ended June 30, 2007, compared to the three and six months ended June 30, 2006. These increases reflect increases in the growth of the related Guarantee obligation associated with the average outstanding balance of our PCs and Structured Securities.

Derivative Overview

Table 6 presents the notional or contractual amounts for our derivatives, including each of our hedge accounting classifications, and the corresponding impact of those positions on our consolidated financial statements.

Table 6 — Summary of the Effect of Derivatives on Selected Consolidated Financial Statement Captions

Description	Consolidated Balance Sheets					
	June 30, 2007			December 31, 2006		
	Notional or Contractual Amount ⁽¹⁾	Fair Value (Pre-Tax) ⁽²⁾	AOCI (Net of Tax) ⁽³⁾	Notional or Contractual Amount ⁽¹⁾	Fair Value (Pre-Tax) ⁽²⁾	AOCI (Net of Tax) ⁽³⁾
	(in millions)					
Cash flow hedges-open	\$ 4,498	\$ (48)	\$ (31)	\$ 70	\$ —	\$ —
No hedge designation	986,902	6,914	—	757,127	7,729	—
Subtotal	991,400	6,866	(31)	757,197	7,729	—
Balance related to closed cash flow hedges	—	—	(4,543)	—	—	(5,033)
Total	<u>\$991,400</u>	<u>\$6,866</u>	<u>\$ (4,574)</u>	<u>\$757,197</u>	<u>\$7,729</u>	<u>\$ (5,033)</u>

Description	Consolidated Statements of Income			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	Derivative Gains (Losses)	Derivative Gains (Losses)	Derivative Gains (Losses)	Derivative Gains (Losses)
	(in millions)			
No hedge designation	\$281	\$355	\$(247)	\$628

(1) Notional or contractual amounts are used to calculate the periodic settlement amounts to be received and paid and generally do not represent actual amounts to be exchanged. Notional amounts are not recorded as assets or liabilities on our consolidated balance sheets.

(2) The fair values of derivatives (netted by counterparty) are presented as Derivative assets, at fair value and Derivative liabilities, at fair value on our consolidated balance sheets. Fair value does not include accrued interest payable or receivable.

(3) Derivatives that meet specific criteria may be accounted for as cash flow hedges. Changes in the fair value of the effective portion of open cash flow hedges are recorded in Accumulated other comprehensive income (loss), or AOCI, net of taxes. Net deferred gains and losses on closed cash flow hedges (*i.e.*, where the derivative is either terminated or redesignated) are also included in AOCI, net of taxes, until the related forecasted transaction affects earnings or is determined to be probable of not occurring.

As discussed in our 2006 Information Statement, by the end of 2006 we had discontinued nearly all of our cash flow hedge accounting relationships and all of our fair value hedge accounting relationships. At June 30, 2007, the only derivatives in cash flow hedge accounting relationships were certain commitments to forward sell mortgage-related securities. We record changes in the fair value of derivatives not in hedge accounting relationships as Derivative gains (losses) on our consolidated statements of income. See “NOTE 10: DERIVATIVES” to our consolidated financial statements for additional information about our derivatives.

Derivative Gains (Losses)

Table 7 provides a summary of the period-end notional or contractual amounts and the gains and losses related to derivatives that were not accounted for in hedge accounting relationships.

Table 7 — Derivatives Not in Hedge Accounting Relationships

	Notional or Contractual Amount		Derivative Gains (Losses)			
	June 30,		Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006	2007	2006
			(in millions)			
Call swaptions						
Purchased	\$236,752	\$166,000	\$(1,168)	\$ (667)	\$(1,721)	\$(1,980)
Written	3,400	—	48	—	50	—
Put swaptions						
Purchased	19,325	39,725	244	207	236	444
Written	2,600	—	(144)	—	(146)	—
Receive-fixed swaps	214,657	179,076	(3,500)	(1,270)	(3,241)	(2,490)
Pay-fixed swaps	284,927	206,305	4,531	2,266	4,053	5,147
Futures	113,000	103,934	(70)	(212)	(51)	(478)
Foreign currency swaps	22,709	782	332	30	530	34
Other ⁽¹⁾	89,532	61,690	(86)	(29)	(90)	(76)
Subtotal	986,902	757,512	187	325	(380)	601
Accrual of periodic settlements:						
Receive-fixed swaps ⁽²⁾			(37)	(73)	(95)	(79)
Pay-fixed swaps			155	106	303	109
Foreign currency swaps			(25)	(4)	(77)	(4)
Other			1	1	2	1
Total accrual of periodic settlements			94	30	133	27
Total	<u>\$986,902</u>	<u>\$757,512</u>	<u>\$ 281</u>	<u>\$ 355</u>	<u>\$ (247)</u>	<u>\$ 628</u>

(1) Consists of basis swaps, certain option-based contracts (including written options), interest-rate caps, forward purchase and sale commitments, credit derivatives and swap guarantee derivatives not accounted for in hedge accounting relationships.

(2) Includes imputed interest on zero-coupon swaps.

Derivative gains (losses) reflects the change in the fair value of and the accrual of periodic settlements of all derivatives not in hedge accounting relationships.

We use receive- and pay-fixed swaps to adjust the interest-rate characteristics of our debt funding in order to more closely match changes in the interest-rate characteristics of our mortgage-related assets. During the three months ended June 30, 2007, fair value gains on our pay-fixed swaps were partially offset by losses on our receive-fixed swaps as swap interest rates increased. We use swaptions and other option-based derivatives to adjust the characteristics of our debt in response to changes in the expected lives of mortgage-related assets in our Retained portfolio. The losses on our purchased call swaptions, which increased during the three months ended June 30, 2007, compared to the three months ended June 30, 2006, were primarily attributable to increasing swap interest rates, partially offset by an increase in implied volatility during the three months ended June 30, 2007.

Gains on foreign currency swaps increased from \$30 million and \$34 million for the three and six months ended June 30, 2006, respectively, to \$332 million and \$530 million for the three and six months ended June 30, 2007, respectively. The change in this gain was largely the result of our voluntary discontinuation of hedge accounting for \$28.6 billion notional amount of foreign currency swaps in December 2006. Also contributing to the increase in derivative gains on foreign currency swaps was an increase in interest rates and the weakening of the U.S. dollar against the Euro. These gains were offset by net foreign currency translation losses, primarily related to our foreign currency denominated debt, of \$333 million and \$530 million for the three and six months ended June 30, 2007, respectively.

During the six months ended June 30, 2007, fair value changes of our receive- and pay-fixed swaps were primarily driven by increases in swap interest rates across the yield curve. During 2006, we also voluntarily discontinued hedge accounting for our receive-fixed swaps. See “NOTE 10: DERIVATIVES” to our consolidated financial statements for additional information about our derivatives.

Gains (Losses) on Investment Activity

Table 8 summarizes the components of Gains (losses) on investment activity.

Table 8 — Gains (Losses) on Investment Activity

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Gains (losses) on trading securities	\$ 62	\$ (26)	\$ 93	\$ (72)
Gains (losses) on PC residuals, at fair value	114	103	(66)	289
Gains on sale of mortgage loans ⁽¹⁾	2	13	22	34
Gains (losses) on sale of available-for-sale securities	(201)	(180)	(150)	(34)
Security impairments	(325)	(218)	(428)	(351)
Lower-of-cost-or-market adjustments	(20)	(4)	(22)	(12)
Total Gains (losses) on investment activity	<u>\$(368)</u>	<u>\$(312)</u>	<u>\$(551)</u>	<u>\$(146)</u>

(1) Represents mortgage loans sold in connection with securitization transactions.

Gains (Losses) on Trading Securities

A shift in the composition of our trading securities toward interest-only mortgage-related securities combined with increases in long-term interest rates resulted in gains recognized on the interest-only mortgage-related securities classified as trading for the three and six months ended June 30, 2007, which more than offset the losses on the other mortgage-related securities classified as trading. Losses for the three and six months ended June 30, 2006 reflect the impact of increases in long-term interest rates on mortgage-related securities classified as trading.

Gains (Losses) on PC Residuals, at Fair Value

Gains (losses) on PC residuals relate to certain PCs and Structured Securities we hold in our Retained portfolio and represent the net fair value of the future cash inflows and outflows related to our guarantee of these securities. The fair value of PC residuals is affected by several factors including: (a) changes in interest rates, which affect the expected lives of the related PCs and Structured Securities; (b) default experience and loss severity trends related to our guarantees; and (c) risk premiums implied by third party information with respect to fair value.

Gains on PC residuals for the three months ended June 30, 2007 and 2006 were due primarily to increasing interest rates in both periods that extended the expected lives of the PCs and Structured Securities underlying the PC residuals. Losses on PC residuals for the six months ended June 30, 2007, compared to gains for the six months ended June 30, 2006, resulted from higher expected default costs and increased uncertainty in the mortgage market during 2007.

Gains (Losses) on Sale of Available-For-Sale Securities

Net losses on the sale of available-for-sale securities increased for the three and six months ended June 30, 2007, compared to the three and six months ended June 30, 2006. In keeping with our strategy of maximizing mortgage-to-debt OAS returns on our Retained portfolio, we entered into structuring transactions and sales of seasoned securities with unpaid principal balances of approximately \$21 billion during the three months ended June 30, 2007. These sales generated net losses recognized in Gains (losses) on investment activity because the securities sold had lower coupon rates than those available in the market at the time of sale. The losses for the three and six months ended June 30, 2006 reflect the impact of rising interest rates, which were partially offset by net gains of approximately \$38 million and \$174 million for the three and six months ended June 30, 2006, respectively, related to the sale of certain commercial mortgage-backed securities, or CMBS, that OFHEO previously directed us to divest.

Security Impairments

Security impairments increased for the three and six months ended June 30, 2007, compared to the three and six months ended June 30, 2006 primarily due to increased interest rates. During the three months ended June 30, 2007, security impairments included \$278 million related to seasoned securities with unpaid principal balances of approximately \$10 billion that we planned to sell in the third quarter of 2007 and thus we did not have the intent to hold these securities at June 30, 2007 until the losses would be recovered. These \$278 million of impairments were primarily the result of increased interest rates that reduced the fair value of our guaranteed securities below their amortized cost. Our non-agency mortgage-related securities backed by subprime loans contributed less than \$1 million to our security impairments during the three months ended June 30, 2007.

For the three months ended June 30, 2006, total security impairments included \$196 million related to declines in fair value below amortized cost due to increased interest rates and \$19 million related to impairments of certain CMBS. For the six months ended June 30, 2006, total security impairments included \$282 million related to declines in fair value below amortized cost due to increased interest rates and \$61 million related to impairments of certain CMBS.

Foreign Currency Losses, Net

We actively manage the foreign currency exposure associated with our foreign currency denominated debt through the use of derivatives. For the three months ended June 30, 2007, we recognized net foreign currency translation losses of \$333 million primarily due to the weakening of the U.S. dollar relative to the Euro during the period. Foreign currency losses offset an increase of \$332 million in the fair value of foreign currency-related derivatives during the period, recorded in Derivative gains (losses).

For the six months ended June 30, 2007, we recognized net foreign currency translation losses primarily related to our foreign currency denominated debt of \$530 million. Foreign currency losses offset an increase of \$530 million in the fair value of foreign currency-related derivatives during the period, recorded in Derivative gains (losses).

During 2006, we voluntarily discontinued hedge accounting for our foreign currency swaps. See “*Derivative Gains (Losses)*” and “NOTE 10: DERIVATIVES” to our consolidated financial statements for additional information about our derivatives.

Non-Interest Expense

Table 9 summarizes the components of Non-interest expense.

Table 9 — Non-Interest Expense

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Administrative expenses:				
Salaries and employee benefits	\$ 243	\$203	\$ 471	\$ 394
Professional services	117	118	225	218
Occupancy expense	16	15	30	29
Other administrative expenses	66	69	119	137
Total administrative expenses	442	405	845	778
Provision for credit losses	320	56	499	20
REO operations expense	16	7	30	19
Losses on certain credit guarantees	187	52	331	98
Losses on loans purchased	205	21	375	42
Low-income housing tax credit partnerships	135	104	243	219
Minority interests in earnings of consolidated subsidiaries	8	16	17	34
Other expenses	65	53	112	88
Total Non-interest expense	<u>\$1,378</u>	<u>\$714</u>	<u>\$2,452</u>	<u>\$1,298</u>

Administrative Expenses

Administrative expenses increased for the three months ended June 30, 2007, compared to the three months ended June 30, 2006, primarily due to higher salary costs caused by the addition of new employees to support our financial reporting, infrastructure and controls-related activities. For the six months ended June 30, 2007 and 2006, administrative expenses increased due to increased headcount.

Provision for Credit Losses

The provision for credit losses increased for the three and six months ended June 30, 2007, compared to the three and six months ended June 30, 2006, as continued weakness in the housing market affected our single-family portfolio. For the three and six months ended June 30, 2007, we recorded additional reserves for credit losses on our single-family portfolio as a result of:

- increased estimates of incurred losses on loans that are expected to experience higher default rates based on their year of origination, particularly those originated during 2006 and 2007, which do not have the benefit of significant home price appreciation;
- an observed increase in the rates at which loans transition through delinquency to foreclosure, and increases in the number of non-performing loans acquired through purchase in performance of our financial guarantees; and
- increases in the expected severity of losses on a per-property basis, driven in part by the expectation of low or slower home price appreciation in certain areas and higher loan balances associated with 2005 through 2007 originations.

In addition, for the six months ended June 30, 2006, we reversed \$84 million of our Provision for credit losses recorded in 2005 associated with Hurricane Katrina because the related payment and delinquency experience on affected properties was more favorable than expected. Absent the adjustment related to Hurricane Katrina, our Provision for credit losses would have been \$104 million for the six months ended June 30, 2006.

We expect that credit losses, which include net charge-offs and REO expenses, will continue to rise from the current level. We also expect to have further increases in our loan loss reserves over the remainder of 2007.

Losses on Certain Credit Guarantees

Losses on certain credit guarantees consists of losses recognized upon the issuance of PCs in Guarantor Swap transactions. We negotiate contracts with our customers in Guarantor Swap transactions based upon our view of the overall economics of the transaction, considering the volume and types of mortgage loans to be delivered to us and our estimates of the net present value of related future guarantee fees, credit costs and other associated cash flows. However, the accounting for our guarantee-related assets and liabilities is not determined at the level at which we negotiate contracts; rather, it is determined separately for each PC-related pool of loans. We determine the initial fair value of the pool-level guarantee-related assets and liabilities using methodologies that employ direct market-based information that may differ from the estimates we use to negotiate the guarantee fees we charge customers. This accounting based on pool-level measurement and our use of market-based information results in the recognition of Losses on certain credit guarantees.

Our guarantee fees with larger customers are periodically negotiated with contracts that remain in effect for up to one year. Although we expect most of our Guarantor Swap transactions under these contracts will generate positive economic returns over the lives of the related PCs, during periods where conditions in the mortgage credit market deteriorate, we may incur initial losses on certain transactions until such time as contract terms are changed or business conditions improve. While we continue to believe the fair value of the Guarantee obligation recorded exceeds the losses that we ultimately expect to incur, our expectation of losses has increased.

For the three months ended June 30, 2007 and 2006, we realized losses of \$187 million and \$52 million, respectively, on certain Guarantor Swap transactions entered into during those periods. For the six months ended June 30, 2007 and 2006, we realized losses of \$331 million and \$98 million, respectively, on certain Guarantor Swap transactions and we deferred gains on newly-issued guarantees of \$470 million and \$417 million, respectively, entered into during those periods. The increases in Losses on certain credit guarantees were driven by a combination of higher expected future credit costs implied by fair market values and competitive pressure impacting fair values of newly-issued Guarantee assets. These losses have also increased for interest-only mortgage products acquired during 2007 as our volume of these mortgage products has increased significantly and these products have greater than expected future credit costs implied by the market's fair values. As credit conditions worsen, we expect to have an increase in Losses on certain credit guarantees.

Losses on Loans Purchased

Losses on non-performing loans purchased from the mortgage loan pools underlying PCs and Structured Securities held by third parties occur when the acquisition basis of the purchased loan exceeds the estimated fair value of the loan on the date of purchase.

In the three and six months ended June 30, 2007, the market-based valuation of non-performing loans was adversely affected by the expectation of higher actual default costs and increased uncertainty in the mortgage market. The decrease in fair values of these loans, combined with an increase in the volume of purchases of non-performing loans, resulted in losses of \$205 million compared to \$21 million for the three months ended June 30, 2007 and 2006, respectively. Similarly, losses increased to \$375 million for the six months ended June 30, 2007, compared to \$42 million for the six months ended June 30, 2006. We expect to recover a portion of the losses on loans purchased over time as these market-based valuations imply future credit losses that are higher than we expect to ultimately incur. See "RISK MANAGEMENT — Credit Risks — Table 26 — Changes in Loans Purchased Under Financial Guarantees" for additional information about our purchases of non-performing loans.

Income Tax Expense

Our effective tax rate for the three months ended June 30, 2007 was 13 percent compared to 3 percent for the three months ended June 30, 2006. Our effective tax rate for the six months ended June 30, 2007 was (144) percent compared to (2) percent for the six months ended June 30, 2006. While tax benefits recognized related to our investments in LIHTC partnerships and interest earned on tax-exempt housing-related securities continue to have a favorable impact on our effective tax rate, fluctuations in pre-tax income are resulting in volatility in our effective tax rate. See "NOTE 12: INCOME TAXES" to our consolidated financial statements for additional information about limitations in our determination of our effective tax rate.

CONSOLIDATED BALANCE SHEETS ANALYSIS

The following discussion of our consolidated balance sheets should be read in conjunction with our consolidated financial statements, including the accompanying notes. Also see “CRITICAL ACCOUNTING POLICIES AND ESTIMATES” for more information concerning our more significant accounting policies and estimates applied in determining our reported financial position.

Retained Portfolio

As described in the “BUSINESS” section of our 2006 Information Statement, beginning July 1, 2006, we voluntarily limited the growth of our Retained portfolio. At June 30, 2007, the carrying value of the Retained portfolio was approximately \$703.3 billion, which was below the voluntary limit for the period of approximately \$724.5 billion.

Table 10 provides detail regarding the mortgage loans and mortgage-related securities in our Retained portfolio.

Table 10 — Characteristics of Mortgage Loans and Mortgage-Related Securities in the Retained Portfolio

	June 30, 2007			December 31, 2006		
	Fixed-Rate	Variable-Rate ⁽¹⁾	Total	Fixed-Rate	Variable-Rate ⁽¹⁾	Total
	(in millions)					
Mortgage loans	\$ 64,564	\$ 4,479	\$ 69,043	\$ 61,273	\$ 4,574	\$ 65,847
Guaranteed PCs and Structured Securities: ⁽²⁾						
Single-family	269,378	81,954	351,332	282,052	71,828	353,880
Multifamily	240	139	379	241	141	382
Total Guaranteed PCs and Structured Securities	<u>269,618</u>	<u>82,093</u>	<u>351,711</u>	<u>282,293</u>	<u>71,969</u>	<u>354,262</u>
Non-Freddie Mac mortgage-related securities:						
Agency mortgage-related securities: ⁽³⁾						
Federal National Mortgage Association, or Fannie Mae:						
Single-family	23,859	19,175	43,034	25,805	17,640	43,445
Multifamily	834	170	1,004	987	2	989
Government National Mortgage Association, or Ginnie Mae:						
Single-family	606	204	810	707	231	938
Multifamily	13	—	13	13	—	13
Total agency mortgage-related securities	<u>25,312</u>	<u>19,549</u>	<u>44,861</u>	<u>27,512</u>	<u>17,873</u>	<u>45,385</u>
Non-agency mortgage-related securities:						
Single-family ⁽⁴⁾	3,954	170,376	174,330	4,280	174,081	178,361
CMBS	26,698	29,808	56,506	23,768	20,992	44,760
Mortgage revenue bonds ⁽⁵⁾	14,181	69	14,250	13,760	74	13,834
Manufactured housing ⁽⁶⁾	1,323	112	1,435	1,381	129	1,510
Total non-agency mortgage-related securities ⁽⁷⁾	<u>46,156</u>	<u>200,365</u>	<u>246,521</u>	<u>43,189</u>	<u>195,276</u>	<u>238,465</u>
Total unpaid principal balance of Retained portfolio	<u>\$405,650</u>	<u>\$306,486</u>	712,136	<u>\$414,267</u>	<u>\$289,692</u>	703,959
Premiums, discounts, deferred fees, impairments of unpaid principal balances and other basis adjustments			(558)			103
Net unrealized gains (losses) on mortgage-related securities, pre-tax			(8,681)			(4,046)
Participation Certificate residuals, at fair value			497			597
Reserve for losses on mortgage loans held-for-investment			(108)			(70)
Total Retained portfolio per consolidated balance sheets			<u>\$703,286</u>			<u>\$700,543</u>

- (1) Variable-rate mortgage loans and mortgage-related securities include those with a contractual coupon rate that, prior to contractual maturity, is either scheduled to change or is subject to change based on changes in the composition of the underlying collateral. Mortgage loans also include mortgages with balloon/reset provisions.
- (2) For Guaranteed PCs and Structured Securities we issue, we are subject to the credit risk associated with the underlying mortgage loan collateral.
- (3) Agency mortgage-related securities are generally not separately rated by nationally recognized statistical rating organizations, but are viewed as having a level of credit quality at least equivalent to non-agency mortgage-related securities rated AAA or equivalent.
- (4) At June 30, 2007 and December 31, 2006, we held investments of approximately \$119 billion and \$124 billion, respectively, of single-family non-agency mortgage-related securities backed by subprime loans. These securities backed by subprime loans include significant credit enhancements, particularly through subordination, and approximately 99.9 percent of these securities held at June 30, 2007 were rated AAA at August 27, 2007. At June 30, 2007 and December 31, 2006, we believe that \$55 billion and \$54 billion, respectively, of our single-family non-agency mortgage-related securities that are not backed by subprime loans are generally backed by Alt-A mortgage loans. These securities backed by Alt-A mortgage loans include significant credit enhancements, particularly through subordination, and approximately 99.9 percent of these securities held at June 30, 2007 were rated AAA at August 27, 2007.
- (5) Consist of obligations of states and political subdivisions. Approximately 67 percent of these securities were AAA-rated at both June 30, 2007 and December 31, 2006.
- (6) At June 30, 2007 and December 31, 2006, 37 percent and 38 percent, respectively, of mortgage-related securities backed by manufactured housing were rated BBB– or above. For the same dates, 97 percent of these securities were supported by third-party credit enhancements (e.g., bond insurance) and other credit enhancements (e.g., deal structure through subordination). Approximately 29 percent and 30 percent of these securities were AAA-rated at June 30, 2007 and December 31, 2006, respectively.
- (7) Credit ratings for most non-agency mortgage-related securities are designated by at least two nationally recognized statistical rating organizations. At June 30, 2007 and December 31, 2006, approximately 97 percent and 96 percent, respectively, of total non-agency mortgage-related securities were AAA-rated.

Derivative Assets and Liabilities, at Fair Value

Table 11 shows the notional or contractual amounts and fair value for each derivative type and the maturity profile of the derivative positions. The fair values of the derivative positions are presented on a product-by-product basis, without netting by counterparty.

Table 11 — Derivative Fair Values and Maturities

	June 30, 2007					
	Notional or Contractual Amount	Total Fair Value	Fair Value ⁽¹⁾			
			Less than 1 Year	1 to 3 Years	Greater than 3 and up to 5 Years	In Excess of 5 Years
			(dollars in millions)			
Interest-rate swaps:						
Receive-fixed:						
Swaps	\$200,849	\$(2,424)	\$(175)	\$(237)	\$ (137)	\$(1,875)
Weighted-average fixed rate ⁽²⁾			4.69%	5.10%	5.20%	5.62%
Forward-starting swaps ⁽³⁾	13,808	(166)	—	(3)	(2)	(161)
Weighted-average fixed rate			—	4.78%	5.03%	5.54%
Total receive-fixed	<u>214,657</u>	<u>(2,590)</u>	<u>(175)</u>	<u>(240)</u>	<u>(139)</u>	<u>(2,036)</u>
Basis (floating to floating)	473	(6)	—	—	(1)	(5)
Pay-fixed:						
Swaps	205,441	2,352	64	308	571	1,409
Weighted-average fixed rate ⁽²⁾			4.79%	5.19%	5.18%	5.32%
Forward-starting swaps ⁽³⁾	79,486	53	—	—	(1)	54
Weighted-average fixed rate			—	—	5.67%	5.69%
Total pay-fixed	<u>284,927</u>	<u>2,405</u>	<u>64</u>	<u>308</u>	<u>570</u>	<u>1,463</u>
Total interest-rate swaps	<u>500,057</u>	<u>(191)</u>	<u>(111)</u>	<u>68</u>	<u>430</u>	<u>(578)</u>
Option-based:						
Call swaptions						
Purchased	236,752	2,354	2	348	930	1,074
Written	3,400	(18)	(6)	—	(12)	—
Put swaptions						
Purchased	19,325	895	—	65	191	639
Written	2,600	(69)	(41)	—	(28)	—
Other option-based derivatives ⁽⁴⁾	30,268	(24)	(8)	—	(1)	(15)
Total option-based	<u>292,345</u>	<u>3,138</u>	<u>(53)</u>	<u>413</u>	<u>1,080</u>	<u>1,698</u>
Futures	113,000	(21)	(27)	6	—	—
Foreign currency swaps	22,709	3,921	682	246	2,208	785
Forward purchase and sale commitments	59,281	22	22	—	—	—
Swap guarantee derivatives	1,072	(3)	—	—	—	(3)
Subtotal	<u>988,464</u>	<u>6,866</u>	<u>\$ 513</u>	<u>\$ 733</u>	<u>\$3,718</u>	<u>\$ 1,902</u>
Credit derivatives	2,936	—	—	—	—	—
Total	<u>\$991,400</u>	<u>\$ 6,866</u>				

(1) Fair value is categorized based on the years from June 30, 2007, until the contractual maturity of the derivative.

(2) Represents the notional weighted average rate for the fixed leg of the swaps.

(3) Represent interest-rate swap agreements that are scheduled to begin on future dates ranging from less than one year to ten years.

(4) Primarily represent written options, including guarantees of stated final maturity of issued Structured Securities and written call options on PCs we issued.

Table 12 summarizes the change in derivative fair values.

Table 12 — Changes in Derivative Fair Values

	Six Months Ended June 30,	
	2007	2006
	(in millions)	
Beginning balance — Net asset (liability)	\$7,729	\$ 6,507
Net change in:		
Forward purchase and sale commitments	7	58
Credit derivatives	1	—
Other derivatives ⁽¹⁾ :		
Changes in fair value	(272)	2,922
Fair value of new contracts entered into during the period ⁽²⁾	240	1,319
Contracts realized or otherwise settled during the period	(839)	(1,298)
Ending balance — Net asset (liability)	<u>\$6,866</u>	<u>\$ 9,508</u>

(1) Include fair value changes for interest-rate swaps, option-based derivatives, futures, foreign currency swaps and interest-rate caps.

(2) Consists primarily of cash premiums paid or received on options.

Table 13 provides information on our outstanding written and purchased swaption and option premiums at June 30, 2007 and December 31, 2006 based on the original premium receipts or payments.

Table 13 — Outstanding Written and Purchased Swaption and Option Premiums

	Original Premium Amount (Paid) Received	Original Weighted Average Life to Expiration (dollars in millions)	Remaining Weighted Average Life
Purchased:			
At June 30, 2007	\$(4,893)	7.6 years	5.9 years
At December 31, 2006	\$(5,316)	7.5 years	6.1 years
Written: ⁽¹⁾			
At June 30, 2007	\$ 81	2.0 years	1.8 years
At December 31, 2006	\$ 21	0.2 years	0.1 years

(1) Excludes written options on guarantees of stated final maturity of Structured Securities.

Guarantee Asset

See “CONSOLIDATED RESULTS OF OPERATIONS — Non-Interest Income — *Gains (Losses) on Guarantee Asset*” for a description of the Guarantee asset. Table 14 summarizes the changes in the Guarantee asset balance.

Table 14 — Changes in Guarantee Asset

	Six Months Ended June 30,	
	2007	2006
	(in millions)	
Beginning balance	\$6,070	\$5,083
Additions, net of repurchases	1,378	785
Return of investment on Guarantee asset	(649)	(478)
Changes in fair value of future cash flows	948	659
Change in estimate	30	40
Gains (losses) on Guarantee asset	329	221
Ending balance	<u>\$7,777</u>	<u>\$6,089</u>

See “CONSOLIDATED RESULTS OF OPERATIONS — Non-Interest Income — *Gains (Losses) on Guarantee Asset*” for an attribution of other changes in the Guarantee asset.

Guarantee Obligation

See “CONSOLIDATED RESULTS OF OPERATIONS — Non-Interest Income — *Income on Guarantee Obligation*” for a description of the components of the Guarantee obligation. Table 15 summarizes the changes in the Guarantee obligation balance.

Table 15 — Changes in Guarantee Obligation

	Six Months Ended June 30,	
	2007	2006
	(in millions)	
Beginning balance	\$7,117	\$5,541
Transfer-out to the loan loss reserve ⁽¹⁾	(16)	(3)
Additions, net of repurchases:		
Fair value of performance and other related costs of newly-issued guarantees	1,496	630
Deferred guarantee income of newly-issued guarantees	470	417
Amortization income:		
Performance and other related costs	(332)	(276)
Deferred guarantee income	(161)	(136)
Income on Guarantee obligation	(493)	(412)
Ending balance	<u>\$8,574</u>	<u>\$6,173</u>
Components of the Guarantee obligation, at period end:		
Unamortized balance of performance and other related costs	\$6,016	\$4,094
Unamortized balance of deferred guarantee income	2,558	2,079
Ending balance	<u>\$8,574</u>	<u>\$6,173</u>

(1) Represents portions of the Guarantee obligation that correspond to incurred credit losses reclassified to Reserve for guarantee losses on Participation Certificates.

The primary drivers affecting our Guarantee obligation balances are our credit guarantee business volumes, fair values of performance obligations on new guarantees, liquidation rates on the existing portfolio and expected profitability of new business at origination. The Guarantee obligation includes unamortized deferred credit and buy-down fees

received from counterparties in Guarantor Swap and similar transactions of \$1.5 billion and \$1.3 billion at June 30, 2007 and 2006, respectively.

Additions, net of repurchases, increased for the six months ended June 30, 2007, compared to the six months ended June 30, 2006. This increase reflects higher business volumes as the unpaid principal balance of Guaranteed PCs and Structured Securities outstanding increased by approximately \$118 billion and \$63 billion during the six months ended June 30, 2007 and 2006, respectively. The increase was also a result of higher expected performance costs on newly-issued guarantees, which have been negatively impacted by the expectation of higher default costs and increased uncertainty in the mortgage market. See “CONSOLIDATED RESULTS OF OPERATIONS — Non-Interest Income — *Income on Guarantee Obligation*” for a discussion of amortization income related to our Guarantee obligation.

Total Stockholders’ Equity

Total stockholders’ equity decreased \$2.5 billion during the six months ended June 30, 2007. This decrease was primarily a result of a \$3.1 billion net increase in unrealized losses on available-for-sale securities, which are a component of the AOCI balance, the repurchase of \$750 million of common stock and the common and preferred stock dividends declared. These reductions were partially offset by Net income of \$553 million and a net increase in the balance of non-cumulative, perpetual preferred stock. During the six months ended June 30, 2007, we issued \$1.6 billion of non-cumulative, perpetual preferred stock, consisting of \$1.0 billion toward the planned replacement of common stock with an equal amount of preferred stock and \$600 million to replace higher-cost preferred stock that we redeemed during the six months ended June 30, 2007.

The balance of AOCI at June 30, 2007 was a net loss of approximately \$10.5 billion, net of taxes, compared to a net loss of \$7.9 billion, net of taxes, at December 31, 2006. The increase in the net loss in AOCI was primarily the result of a \$3.1 billion net increase in unrealized losses on available-for-sale securities as medium- and long-term interest rates increased since December 31, 2006.

CONSOLIDATED FAIR VALUE BALANCE SHEETS ANALYSIS

Our consolidated fair value balance sheets include the estimated fair values of financial instruments recorded on our consolidated balance sheets prepared in conformity with GAAP, as well as off-balance sheet financial instruments that represent our assets or liabilities that are not recorded on our GAAP consolidated balance sheets. These off-balance sheet items predominantly consist of: (a) the unrecognized Guarantee asset and Guarantee obligation associated with our PCs issued through our Guarantor Swap program prior to the implementation of FASB Interpretation No. 45, “Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an interpretation of FASB Statements No. 5, 57, and 107 and rescission of FASB Interpretation No. 34” in 2003; (b) certain commitments to purchase mortgage loans; and (c) certain credit enhancements on manufactured housing asset-backed securities. The fair value balance sheets also include certain assets and liabilities that are not financial instruments at their carrying value in conformity with GAAP. During the six months ended June 30, 2007 and for the full year 2006, our fair value results were affected by several improvements in our approach for estimating the fair value of certain financial instruments. See “CRITICAL ACCOUNTING POLICIES AND ESTIMATES” as well as “NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES” and “NOTE 14: FAIR VALUE DISCLOSURES” to our consolidated financial statements for more information on fair values.

We use a number of financial models in the preparation of our consolidated fair value balance sheets. See “MD&A — RISK MANAGEMENT — Operational Risks” and “MD&A — RISK MANAGEMENT — Interest-Rate Risk and Other Market Risks” of our 2006 Information Statement for discussion concerning the risks associated with our use of these models.

Table 16 shows our summary consolidated fair value balance sheets.

Table 16 — Summary Consolidated Fair Value Balance Sheets⁽¹⁾

	June 30, 2007		December 31, 2006	
	Carrying Amount ⁽²⁾	Fair Value	Carrying Amount ⁽²⁾	Fair Value
	(in billions)			
Total assets.....	\$821.7	\$816.5	\$813.1	\$811.3
Total liabilities and minority interests.....	\$795.9	\$784.6	\$784.8	\$779.5
Net assets attributable to stockholders:				
Preferred stockholders.....	7.1	6.8	6.1	5.8
Common stockholders.....	18.7	25.1	22.2	26.0
Total net assets.....	25.8	31.9	28.3	31.8
Total liabilities, minority interests and net assets.....	\$821.7	\$816.5	\$813.1	\$811.3

- (1) The summary consolidated fair value balance sheets do not purport to present our net realizable, liquidation or market value as a whole. Furthermore, amounts we ultimately realize from the disposition of assets or settlement of liabilities may vary significantly from the fair values presented.
- (2) Equals the amount reported on our GAAP consolidated balance sheets.

Discussion of Fair Value Results

During the six months ended June 30, 2007, the fair value of net assets attributable to common stockholders, before capital transactions, increased by \$0.5 billion, resulting in an annualized return on the average fair value of net assets attributable to common stockholders of approximately 3.9 percent. During the six months ended June 30, 2006, the fair value of net assets attributable to common stockholders, before capital transactions, increased by \$2.4 billion, resulting in an annualized return on the average fair value of net assets attributable to common stockholders of approximately 17.7 percent. The fair value of net assets attributable to common stockholders at June 30, 2007 was \$25.1 billion, compared to \$26.0 billion at December 31, 2006. The payment of common stock dividends and the repurchase of common stock during the six months ended June 30, 2007 reduced total fair value by \$1.4 billion.

Estimated Impact of Changes in Mortgage-to-Debt OAS on Fair Value Results

For the six months ended June 30, 2007 and 2006, we estimated that on a pre-tax basis the change in the fair value of net assets attributable to common stockholders, before capital transactions, included decreases of approximately \$1.7 billion and \$0.6 billion, respectively, due to a net widening of mortgage-to-debt OAS.

We believe disclosing the estimated impact of changes in mortgage-to-debt OAS on the fair value of net assets is helpful to understanding our current period fair value results in the context of our long-term fair value return objective. Our long-term objective is to generate returns, before capital transactions, over time on the average fair value of net assets attributable to common stockholders in the low- to mid-teens. However, period-to-period returns may fluctuate substantially due to market conditions. These market conditions include changes in interest rates and other market factors that affect certain components of our fair value changes, including those which we do not attempt to hedge or actively manage, specifically, the change in mortgage-to-debt OAS with respect to our Retained portfolio and the change in the fair value of the single-family guarantee portfolio.

Our estimate of the periodic increases or decreases in the fair value of net assets associated with fluctuations in OAS provides insight into a component of our fair value results that we do not believe will significantly affect the long-term fair value of the Retained portfolio. This belief is based on our expectation that differences between the prepayments forecasted by our models and the actual prepayments we will experience are not likely to be significant.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity

Our business activities require that we maintain adequate liquidity to make payments upon the maturity or repurchase of our debt securities; purchase mortgage loans, mortgage-related securities and other investments; make payments of principal and interest on our debt securities and on our Guaranteed PCs and Structured Securities; make net payments on derivative instruments; fund our general operations; and pay dividends on and repurchase our preferred and common stock.

We fund our cash requirements primarily by issuing short-term and long-term debt. Other sources of cash include:

- receipts of principal and interest payments on securities we hold or mortgage loans we have securitized and sold;
- sales of securities we hold;
- borrowings against mortgage-related securities and other investment securities we hold;

- other cash flows from operating activities, including guarantee activities; and
- issuances of common and preferred stock.

Debt Securities

We fund our business activities primarily through the issuance of short-term and long-term debt. Table 17 summarizes the par value of the debt securities we issued, based on settlement dates, during the three and six months ended June 30, 2007 and 2006. We seek to maintain a variety of consistent, active funding programs that promote high-quality coverage by market makers and reach a broad group of institutional and retail investors. By diversifying our investor base and the types of debt securities we offer, we believe we enhance our ability to maintain continuous access to the debt markets under a variety of market conditions.

Table 17 — Debt Security Issuances by Product, at Par Value⁽¹⁾

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Short-term debt:				
Reference Bills [®] securities and discount notes	\$127,846	\$162,132	\$258,492	\$357,781
Medium-term Notes — Callable	300	997	2,200	2,097
Medium-term Notes — Non-callable	102	1,200	102	1,500
Total short-term debt issued	128,248	164,329	260,794	361,378
Long-term debt:				
Medium-term Notes — Callable ⁽²⁾	34,729	41,250	73,340	68,037
Medium-term Notes — Non-callable	6,951	4,566	21,215	14,306
U.S. dollar Reference Notes [®] securities — Non-callable	12,000	19,000	29,000	39,000
Freddie SUBS [®] securities	—	1,250	—	1,250
Total long-term debt issued	53,680	66,066	123,555	122,593
Total debt securities issued	<u>\$181,928</u>	<u>\$230,395</u>	<u>\$384,349</u>	<u>\$483,971</u>

(1) Exclude securities sold under agreements to repurchase and Federal funds purchased, swap collateral obligations, lines of credit and securities sold but not yet purchased.

(2) Include \$— million and \$100 million of Medium-term Notes — Callable issued for the three months ended June 30, 2007 and 2006, respectively, which were accounted for as debt exchanges. Include \$— million and \$100 million of Medium-term Notes — Callable issued for the six months ended June 30, 2007 and 2006, respectively, which were accounted for as debt exchanges.

Subordinated Debt

During the six months ended June 30, 2007, we called \$1.2 billion of Freddie SUBS[®] securities. At June 30, 2007 and December 31, 2006, the balance of our subordinated debt outstanding was \$5.2 billion and \$6.4 billion, respectively. Our subordinated debt in the form of Freddie SUBS[®] securities is a component of our risk management and disclosure commitments with OFHEO (described in “RISK MANAGEMENT AND DISCLOSURE COMMITMENTS”).

Credit Ratings

Our ability to access the capital markets and other sources of funding, as well as our cost of funds, are highly dependent upon our credit ratings. Table 18 indicates our credit ratings at August 1, 2007.

Table 18 — Freddie Mac Credit Ratings

	Nationally Recognized Statistical Rating Organization		
	Standard & Poor's	Moody's	Fitch
Senior long-term debt ⁽¹⁾	AAA	Aaa	AAA
Short-term debt ⁽²⁾	A-1+	P-1	F-1+
Subordinated debt ⁽³⁾	AA-	Aa2	AA-
Preferred stock	AA-	Aa3	AA-

(1) Includes Medium-term Notes, U.S. dollar Reference Notes[®] securities and €Reference Notes[®] securities.

(2) Includes Reference Bills[®] securities and discount notes.

(3) Includes Freddie SUBS[®] securities only.

Equity Securities

See “Capital Resources — Core Capital” and “UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS” for information about issuances and repurchases of our equity securities.

Cash and Investments Portfolio

We maintain a cash and investments portfolio that is important to our financial management and our ability to provide liquidity and stability to the mortgage market. At June 30, 2007, the investments in this portfolio consisted of liquid non-mortgage-related securities, principally asset-backed securities and other marketable assets, that we could sell or finance to provide us with an additional source of liquidity to fund our business operations. We also use the portfolio to

help manage recurring cash flows and meet our other cash management needs. In addition, we use the portfolio to hold capital on a temporary basis until we can deploy it into Retained portfolio investments or credit guarantee opportunities. We may also sell or finance the securities in this portfolio to maintain capital reserves to meet mortgage-funding needs, provide diverse sources of liquidity or help manage the interest-rate risk inherent in mortgage-related assets.

Capital Resources

Capital Adequacy

We estimated at June 30, 2007 that we exceeded each of our regulatory capital requirements, in addition to the 30 percent mandatory target capital surplus, based on our most recent submissions to OFHEO. See “NOTE 9: REGULATORY CAPITAL” to our consolidated financial statements for further information regarding our regulatory capital requirements and “NOTE 10: REGULATORY CAPITAL” to our consolidated financial statements in our 2006 Information Statement for further information regarding OFHEO’s capital monitoring framework.

Core Capital

During the six months ended June 30, 2007, we added approximately \$164 million to Core Capital, primarily from a net increase in the balance of non-cumulative, perpetual preferred stock of \$1.0 billion, Net income of \$553 million and the cumulative effect of a change in accounting principle of \$181 million, partially offset by the repurchase of common stock of \$750 million and the declaration of common stock and preferred stock dividends totaling \$847 million. See “NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES — Recently Adopted Accounting Standards — *Accounting for Uncertainty in Income Taxes*” to our consolidated financial statements for further information regarding the cumulative effect of a change in accounting principle.

We completed two non-cumulative, perpetual preferred stock offerings during the first six months of 2007. The proceeds from the first offering of \$1.1 billion were used to repurchase \$500 million of outstanding common stock to complete our stock repurchase plan authorized in October 2005 and to redeem \$600 million of higher-cost preferred stock. The proceeds from the second offering of \$500 million were used together with other funds to repurchase \$750 million of outstanding common stock under our \$1.0 billion stock repurchase plan authorized in March 2007. In July 2007, we issued an additional \$500 million of non-cumulative, perpetual preferred stock, \$250 million of which was used to complete the stock repurchase plan authorized in March 2007. We purchased a total of approximately 16.1 million shares of our outstanding common stock under the stock repurchase plan authorized in March 2007 at an average cost of \$62.04 per share.

RISK MANAGEMENT

We are exposed to risks that include operational risks, interest-rate and other market risks and credit risks, among others. See the “RISK FACTORS” section of our 2006 Information Statement and this Information Statement Supplement for further information regarding other risks. We manage risk through a framework, approved by our board of directors, that recognizes primary risk ownership and management by our business areas. Within this framework, our executive management committees and divisions responsible for independent risk oversight, which include Enterprise Risk Oversight, Corporate Compliance and Internal Audit, monitor performance against our risk management strategies and established risk limits, identify and assess potential issues and provide oversight regarding changes in business processes and activities. Our board of directors and its committees also provide oversight of risk management. Together, these groups assess the adequacy and effectiveness of the risk management functions across the company.

Operational Risks

Operational risks are inherent in all of our business activities and can become apparent in various ways, including accounting or operational errors, business interruptions, fraud, failures of the technology used to support our business activities and other operational challenges resulting from failed or inadequate internal controls. We face a number of significant operational risks, including material weaknesses and significant deficiencies in our internal control over financial reporting. These operational risks may expose us to financial loss, may delay or interfere with our ability to return to and sustain timely financial reporting or may result in other adverse consequences. Governance over the management of our operational risks takes place through the enterprise risk management framework described above. Business areas retain primary responsibility for identifying, assessing and reporting their operational risks.

Disclosure Controls and Procedures

Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that the information we are required to disclose in our financial reports is accumulated and communicated to senior management, as appropriate, to allow timely decisions regarding required disclosure. We have not completed the evaluation and testing of our disclosure controls and procedures.

Internal Control Over Financial Reporting

As discussed in “MD&A — RISK MANAGEMENT — Operational Risks” in our 2006 Information Statement, we have material weaknesses and significant deficiencies in our internal control over financial reporting. Based on the existence of the material weaknesses, our Chief Executive Officer and Chief Financial Officer concluded that our internal control over financial reporting was ineffective at December 31, 2006. Since that time, we have made a number of material changes to our internal control over financial reporting as described below. We believe our efforts to date to remediate our material weaknesses and significant deficiencies have continued to strengthen our control environment since December 31, 2006. However, material weaknesses and significant deficiencies continue to pose significant risk to our financial reporting in 2007. The complexity associated with the interdependent nature of key elements of our remediation efforts may also continue to affect the timing and impact of such efforts. As we continue our remediation activities, we may identify additional material weaknesses, significant deficiencies or other operational issues in our internal controls or conclude that significant deficiencies we have already identified should be regarded as material weaknesses, either individually or in the aggregate. Improvements to the processes and controls we put in place to remediate our control deficiencies need to operate for a period of time to enable us to evaluate their effectiveness. Additionally, the controls described below that we have put in place through our remediation efforts have not been subject to assessment by our external auditors in the course of their audit of our annual consolidated financial statements.

We performed extensive verification and validation procedures to provide reasonable assurance that our June 30, 2007 consolidated financial statements were prepared and are fairly stated in conformity with GAAP. We developed and have begun assessing our processes against a set of standards over internal controls for matters such as general ledger reconciliations, financial analytics and end-user computing. To assess the reliability of our financial results, we strengthened our monthly and quarterly analysis and review forums. In these forums, business area controllers, the Corporate Controller and the Chief Financial Officer review our periodic results, issues that arose in processing these results, our simplifying assumptions, the impact of process changes and the status and impact of control deficiencies. In view of these and other procedures we performed, we believe that the material weaknesses do not prevent us from preparing and fairly stating our June 30, 2007 consolidated financial statements in conformity with GAAP.

Overview of Progress Toward Remediation

Remediation of the material weaknesses and significant deficiencies in our financial reporting processes continues to be a top corporate priority in 2007. Our material weaknesses and planned remediation activities are described in our 2006 Information Statement. We report progress towards remediation of material weaknesses and significant deficiencies in the following stages:

- In process — We are in the process of designing and implementing controls to correct identified internal control deficiencies and conducting ongoing evaluations to ensure all deficiencies have been identified.
- Remediation activities implemented — We have designed and implemented the controls we believe necessary to remediate the identified internal control deficiencies.
- Remediated — After a sufficient period of operation of the controls implemented to remediate the control deficiencies, management has evaluated the controls and found them to be operating effectively.

Progress Toward Remediation of Material Weaknesses

At December 31, 2006, remediation activities were in process for all of our material weaknesses. Our progress toward remediation of the material weaknesses since the date of our 2006 Information Statement is summarized below.

<u>Material Weaknesses</u>	<u>Remediation Progress as of June 14, 2007</u>	<u>Remediation Progress as of August 30, 2007</u>
<p>Integration between Operations and Finance Systems and processes related to our operational and financial accounting systems and to our financial close process are not adequately integrated. The components of this weakness are:</p> <ul style="list-style-type: none"> • Data Hand-offs — Controls over data hand-offs between business units and from external providers need to be improved. • Financial Close Process — The financial close process needs better coordination between business unit accounting teams and corporate accounting and reporting teams, and improved monitoring of the process. • Complex Transactions Processing — Controls over the processing of complex structured securitization transactions need to be improved. • Accounting Policy Linkage — Processing performed by financial applications needs to be evaluated for appropriate linkage to accounting policies. 	<p>In process</p> <p>Remediation activities implemented</p> <p>In process</p> <p>In process</p>	<p>In process</p> <p>Remediation activities implemented</p> <p>Remediation activities implemented</p> <p>In process</p>
<p>Monitoring Controls within Financial Operations Monitoring controls and analytics within financial operations failed to detect significant errors and escalate issues to management prior to external disclosure of financial results.</p>	<p>In process</p>	<p>In process</p>
<p>Information Technology General Controls — Access to Data and Security Administration Controls over monitoring of users with direct access to data, segregation of duties and administration of user access to applications and data are not adequately designed and enforced.</p>	<p>In process</p>	<p>In process</p>
<p>Information Technology General Controls — Change Management Policies and procedures for making program and data changes are inadequate and controls over system development testing, approval and quality assurance are not operating effectively.</p>	<p>In process</p>	<p>In process</p>
<p>Management Self-Assessment Self-assessment processes do not enable management to timely identify, document and remediate control deficiencies within the financial reporting process.</p>	<p>In process</p>	<p>In process</p>
<p>Adequacy of Staffing Vacancies in leadership and key staff positions increase operational risk in our financial reporting processes. Individual accountability for risk management is not embedded in our corporate culture.</p>	<p>Remediated</p>	<p>Remediated</p>

Material Weakness We Have Remediated

Adequacy of Staffing — We adequately filled our leadership and critical staff position vacancies as well as made significant progress in resolving single-person critical dependencies. We also implemented an on-going process designed to identify and resolve critical vacancies in an expeditious manner through better coordination between our human resources professionals and our business units. In addition, we developed and have initiated a series of programs designed to enhance our management of human resources and to create and sustain a more effective culture of accountability. These programs include improvements to our performance management process, development of broad-based risk and control training programs and more effective workforce planning. We are continuing to implement programs and processes related to assuring adequate staffing and risk management accountability as part of our ongoing focus in this area.

Progress Toward Remediation of Other Material Weaknesses

The discussion below describes the actions that management has taken and is in the process of taking to remediate our remaining material weaknesses. Although we have made progress on remediation of these material weaknesses, additional work remains. As we continue our remediation activities, we may identify additional material weaknesses, significant deficiencies or other operational issues in our internal control over financial reporting or conclude that significant deficiencies we already identified should be regarded as material weaknesses, either individually or in the aggregate.

Integration between Operations and Finance — Our efforts to remediate the components of this material weakness are described below:

- 1) Data Hand-offs — Policies and standards have been developed to define control objectives related to hand-offs of information between people, processes and systems. An extensive “end-to-end” process review is currently in

progress to validate the controls over hand-offs that are in place and to identify potential design deficiencies in our existing system of internal controls. As specific control deficiencies are identified, remediation plans are being designed and implemented.

- 2) **Financial Close Process** — We have made significant improvements in the coordination and execution of and control over our financial close process. These include substantive enhancements to the coordination of close process activities among our business unit accounting teams and corporate accounting and reporting teams as well as improvements in monitoring controls around critical elements of the financial close process.
- 3) **Complex Transactions Processing** — We performed an in-depth review of our controls related to the processing and reporting of our more complex structured securitization transactions. For the specific deficiencies identified, we designed and implemented the controls we believe necessary for remediation.
- 4) **Accounting Policy Linkage** — We reviewed and ranked the relative risk of our financial applications for their impact on the application of accounting policy. High-risk financial applications are currently being evaluated to determine whether accounting policies are appropriately applied through the processing of those applications.

Monitoring Controls within Financial Operations — We are developing and implementing monitoring controls and standards to support the accounting processes at both the business unit and corporate levels, including a more structured, in-depth analytics process. These monitoring controls, combined with a newly implemented governance and review structure, are being designed to provide for detection, escalation and remediation of accounting and reporting issues prior to external disclosure of financial results.

Information Technology General Controls — Access to Data and Security Administration — We have substantially completed the design assessment of our information technology general controls over security administration utilizing the Information Technology Governance Institute's Control Objectives for Information Technology framework. We identified relevant control deficiencies and are implementing controls designed to ensure that data is secure and available only to authorized and appropriate users.

Information Technology General Controls — Change Management — We developed and deployed a new change management process and a new systems development life cycle process that are based on methodologies acquired from a third party. We now require adherence to these processes and related controls for new systems development projects. All pre-existing projects have transition plans to convert to the new systems development life cycle process. We are assessing financial application projects to determine whether they achieve the control objectives of the new systems development life cycle process. Additional remediation efforts will focus on developing and executing remediation plans for any control deficiencies identified in financial application projects and establishing a monitoring process to ensure that all changes introduced into a production environment are appropriately documented, approved and tested.

Management Self-Assessment — We designed a management self-assessment process that will provide more timely and effective identification, documentation and remediation of control deficiencies within the financial reporting process. We are currently conducting a pilot of the process within a portion of our business to validate the process and procedures for risk assessment, control effectiveness assessment, issue identification and remediation, and management attestation and reporting on internal control. We anticipate deploying the self-assessment process to each business area as the corresponding components of the end-to-end process review are completed.

Progress Toward Remediation of Significant Deficiencies

As discussed in “MD&A — RISK MANAGEMENT — Operational Risks” in our 2006 Information Statement, we previously remediated significant deficiencies related to our risk governance framework, security impairments accounting process and our amortization of deferred premiums, discounts and fees for assets held in our Retained portfolio. At December 31, 2006, remediation activities were in process for all of our remaining significant deficiencies. Our progress

toward remediation of the significant deficiencies since the date of our 2006 Information Statement is summarized below.

<u>Significant Deficiencies</u>	<u>Remediation Progress as of June 14, 2007</u>	<u>Remediation Progress as of August 30, 2007</u>
<p>Guarantee Asset/Guarantee Obligation Governance Our process for valuation of and accounting for guarantee assets and guarantee obligations is complex, manually intensive and dependent on end-user computing solutions, resulting in an unacceptable likelihood of risk of significant error.</p>	In process	In process
<p>End-User Computing Controls Our financial reporting processes rely on models and end-user computing solutions that are not subject to adequate controls over their development, nor are they currently subject to adequate change control procedures.</p>	In process	In process
<p>New Products Governance Our policies and procedures for the introduction of new products are insufficient and related governance processes do not adequately ensure adherence to policies and procedures.</p>	Remediated	Remediated
<p>Tax Basis Balance Sheet We do not maintain a tax basis balance sheet to support deferred tax accounting under GAAP, which could result in balance sheet misclassifications and potential income statement adjustments.</p>	In process	In process
<p>Controls over Data Quality Controls over the quality of data used in our financial reporting process are not effective.</p>	In process	In process
<p>Simplifying Assumptions Our financial reporting process is over-reliant on simplifying assumptions, or manual work around solutions, in the application of our accounting policies. In addition, we do not adequately monitor the potential impact of these simplifying assumptions on the financial statements.</p>	In process	Remediation activities implemented
<p>Oversight of Models and Model Applications Our model governance and monitoring procedures (other than those used in the Guarantee Asset/Guarantee Obligation Governance significant deficiency described above) do not effectively ensure that changes to and our use of models in our financial reporting process are appropriate.</p>	In process	Remediation activities implemented

Significant Deficiency We Have Remediated

New Products Governance — In completing the remediation of this significant deficiency, we redesigned the processes and controls over the introduction of new products, including improving our overall procedures, implementing enhanced governance and oversight, providing training to personnel involved in developing and implementing new products and deploying post-implementation monitoring.

Significant Deficiencies for which We Have Implemented Remediation Activities

Simplifying Assumptions — We redesigned and implemented processes and controls over simplifying assumptions, including enhanced governance and oversight, and procedures related to the identification and governance of new assumptions. We also provided training to responsible personnel on governance, oversight, monitoring and measurement processes. Additionally, we evaluated all simplifying assumptions to determine the feasibility of eliminating the assumptions by modifying our processes and implemented changes as appropriate.

Oversight of Models and Model Applications — We developed and implemented a governance structure for our core financial models and model application systems to monitor model risk and performance including requirements for documentation and change management controls. We prioritized our inventory of core models based on level of risk and implemented a review process to periodically evaluate each model for compliance with established policies and control requirements. Our governance and monitoring procedures over models used in the valuation of and accounting for our guarantee assets and guarantee obligations are addressed under the Guarantee Asset/Guarantee Obligation Governance significant deficiency.

Interest-Rate Risk and Other Market Risks

Our interest-rate risk management objective is to protect stockholder value consistent with our housing mission and safe and sound operations in all interest-rate environments. We believe a disciplined approach to interest-rate risk management is essential to maintaining a strong and durable capital base and uninterrupted access to debt and equity capital markets. See “MD&A — RISK MANAGEMENT — Interest-Rate Risk and Other Market Risks” in our 2006 Information Statement for more information.

PMVS and Duration Gap

Our primary interest-rate risk measures are PMVS and duration gap. PMVS measures the estimated sensitivity of our portfolio market value to parallel (PMVS-L) and non-parallel (PMVS-Yield Curve, or PMVS-YC) movements in interest rates.

PMVS Results

Table 19 provides estimated PMVS-L and PMVS-YC results. Table 19 also provides PMVS-L estimates assuming an immediate 100 basis point shift in the LIBOR yield curve. Because we do not hedge all prepayment risk, the duration of our mortgage assets changes more rapidly as changes in interest rates increase. Accordingly, as shown in Table 19, the PMVS-L results based on a 100 basis point shift in the LIBOR curve are disproportionately higher than the PMVS-L results based on a 50 basis point shift in the LIBOR curve.

Table 19 — Portfolio Market Value Sensitivity Assuming Shifts of the LIBOR Yield Curve

	Portfolio Market Value Sensitivity			Potential Pre-Tax Loss in Portfolio Market Value (in millions)		
	PMVS-YC	PMVS-L		PMVS-YC	PMVS-L	
	25 bps	50 bps	100 bps	25 bps	50 bps	100 bps
At:						
June 30, 2007	—%	1%	2%	\$ 8	\$129	\$453
December 31, 2006	—%	1%	2%	\$27	\$146	\$560

Derivatives have enabled us to keep our interest-rate risk exposure at consistently low levels in a wide range of interest-rate environments. By keeping PMVS-L and PMVS-YC low, we have been able to reduce the exposure of the fair value of our stockholders' equity to adverse changes in interest rates.

Table 20 shows that the low PMVS-L risk levels for the periods presented would generally have been higher if we had not used derivatives to manage our interest-rate risk exposure.

Table 20 — Derivative Impact on PMVS-L (50 bps)

	Before Derivatives	After Derivatives	Effect of Derivatives
At:			
June 30, 2007	4%	1%	(3)%
December 31, 2006	2%	1%	(1)%

Duration Gap Results

Our estimated average duration gap for the months of June 2007 and December 2006 was zero months.

Use of Derivatives and Interest-Rate Risk Management

Types of Derivatives

The derivatives we use to economically hedge interest-rate and foreign currency risk are common in the financial markets. We principally use the following types of derivatives:

- LIBOR- and Euribor-based interest-rate swaps;
- LIBOR- and Treasury-based exchange-traded futures;
- LIBOR- and Treasury-based purchased options (including purchased swaptions); and
- Foreign currency swaps.

Derivative Positions

In addition to swaps, futures and options, our derivative positions include the following:

Written Options and Swaptions. Written call and put swaptions are sold to counterparties allowing them the option to enter into receive- and pay-fixed swaps, respectively. Written call and put options on mortgage-related securities give the counterparty the right to execute a contract under specified terms, which generally occurs when we are in a liability position. We use these written options and swaptions to manage convexity risk over a wide range of interest rates. We may, from time to time, write other derivative contracts such as caps, floors and interest-rate futures.

Forward Purchase and Sale Commitments. We routinely enter into forward purchase and sale commitments for mortgage loans and mortgage-related securities. Most of these commitments are derivatives subject to the requirements of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended.

Swap Guarantee Derivatives. We guarantee the payment of principal and interest on: (a) multifamily mortgage loans that are originated and held by state and municipal housing finance agencies to support tax-exempt multifamily housing revenue bonds; (b) tax-exempt multifamily housing revenue bonds that support pass-through certificates issued by third parties; and (c) Freddie Mac pass-through certificates, which are backed by tax-exempt multifamily housing revenue bonds and related taxable bonds and/or loans. In connection with some of these guarantees, we may also guarantee the sponsor's or the borrower's performance as a counterparty on any related interest-rate swaps used to

mitigate interest-rate risk. Guarantees of these interest-rate swaps entered into after June 30, 2003 are treated as derivatives and are reported as swap guarantee derivatives.

Credit Derivatives. We have entered into credit derivatives during the six months ended June 30, 2007, including risk-sharing agreements. Under these risk-sharing agreements, default losses on specific mortgage loans delivered by sellers are compared to default losses on reference pools of mortgage loans with similar characteristics. Based upon the results of that comparison, we remit or receive payments based upon the default performance of the referenced pools of mortgage loans. In addition, we have entered into an agreement whereby we assume credit risk for mortgage loans held by third parties for up to a 90-day period in exchange for a monthly fee. Should the mortgage loans become delinquent we are obligated to purchase the loans. See “MD&A — RISK MANAGEMENT — Credit Risks — *Mortgage Credit Risk — Other Credit Risk Management Activities*” in our 2006 Information Statement for more information.

Derivative Counterparty Credit Risk

Table 21 summarizes our exposure to counterparty credit risk in our derivatives.

Table 21 — Derivative Counterparty Credit Exposure

Rating ⁽¹⁾	June 30, 2007					Collateral Posting Threshold
	Number of Counterparties ⁽²⁾	Notional or Contractual Amount	Total Exposure at Fair Value ⁽³⁾	Exposure, Net of Collateral ⁽⁴⁾	Weighted Average Contractual Maturity (in years)	
			(dollars in millions)			
AAA	2	\$ 1,121	\$ 144	\$129	4.1	Mutually agreed upon
AA+	3	122,507	510	25	4.7	\$10 million or less
AA	8	268,944	2,563	172	5.3	\$10 million or less
AA-	9	242,043	5,023	76	5.3	\$10 million or less
A+	5	144,093	1,108	59	6.2	\$1 million or less
A	1	210	—	—	4.5	\$1 million or less
Subtotal ⁽⁵⁾	28	778,918	9,348	461	5.4	
Other derivatives ⁽⁶⁾		152,129	—	—		
Forward purchase and sale commitments		59,281	153	153		
Swap guarantee derivatives		1,072	—	—		
Total derivatives		<u>\$991,400</u>	<u>\$9,501</u>	<u>\$614</u>		

- (1) We use the lower of Standard & Poor's, or S&P, and Moody's ratings to manage collateral requirements. In this table, the rating of the legal entity is stated in terms of the S&P equivalent.
- (2) Based on legal entities. Affiliated legal entities are reported separately.
- (3) For each counterparty, this amount includes derivatives with a net positive fair value (recorded as Derivative assets, at fair value) including the related accrued interest receivable/payable (net) (recorded in Accounts and other receivables, net or Accrued interest payable).
- (4) Total Exposure at Fair Value less collateral held as determined at the counterparty level.
- (5) Consists of over-the-counter derivative agreements for interest-rate swaps, option-based derivatives (excluding written options), certain credit derivatives, foreign currency swaps and purchased interest-rate caps. Written options do not present counterparty credit exposure, because we receive a one-time up-front premium in exchange for giving the holder the right to execute a contract under specified terms, which generally puts us in a liability position.
- (6) Consist primarily of exchange-traded contracts, written options and certain credit derivatives.

Credit Risks

Our credit guarantee portfolio is subject primarily to two types of credit risk: institutional credit risk and mortgage credit risk. Institutional credit risk is the risk that a counterparty that has entered into a business contract or arrangement with us will fail to meet its obligations. Mortgage credit risk is the risk that a borrower will fail to make timely payments on a mortgage we own or guarantee.

Institutional Credit Risk

Our primary institutional credit risk exposure, other than counterparty credit risk relating to derivatives, arises from agreements with the following entities: mortgage loan insurers; mortgage seller/servicers; issuers, guarantors or third party providers of credit enhancements; mortgage investors and originators; and issuers, guarantors and insurers of investments held in both our Retained portfolio and Cash and investments portfolio. Investments in our Retained portfolio expose us to institutional credit risk on non-Freddie Mac mortgage-related securities to the extent that servicers, issuers, guarantors, or third parties providing credit enhancements become insolvent or do not perform. Our non-Freddie Mac mortgage-related securities portfolio consists of both agency and non-agency mortgage-related securities. Agency securities present minimal institutional credit risk due to the prevailing view that these securities have a credit quality at least equivalent to non-agency securities rated AAA (based on the S&P or equivalent rating scale of other nationally recognized statistical rating organizations). We manage institutional credit risk on non-Freddie Mac mortgage-related securities by only purchasing securities that meet our investment guidelines and performing ongoing analysis to evaluate the creditworthiness of the issuers and servicers of these securities and the bond insurers that guarantee them. See “CONSOLIDATED BALANCE SHEETS ANALYSIS — Table 10 — Characteristics of Mortgage Loans and Mort-

gage-Related Securities in the Retained Portfolio” for more information on non-Freddie Mac securities within our Retained portfolio. See the “RISK MANAGEMENT” section in our 2006 Information Statement for more information on our institutional credit risks.

Mortgage Credit Risk

Mortgage credit risk is primarily influenced by the credit profile of the borrower on the mortgage, the features of the mortgage itself, the type of property securing the mortgage and the general economic environment. To manage our mortgage credit risk, we focus on three key areas: underwriting requirements and quality control standards; portfolio diversification; and portfolio management activities, including loss mitigation and the use of credit enhancements.

All mortgages that we purchase for our Retained portfolio or that we guarantee have an inherent risk of default. We seek to manage the underlying risk by adequately pricing for the risk we assume using our underwriting and quality control processes. Our underwriting process evaluates mortgage loans using several critical risk characteristics, such as credit score, loan-to-value ratio and occupancy type. Table 22 provides characteristics of our single-family mortgage loans purchased during the three and six months ended June 30, 2007 and 2006, and of our single-family mortgage portfolio at June 30, 2007 and December 31, 2006.

Table 22 — Characteristics of Single-Family Mortgage Portfolio⁽¹⁾

	Purchases During the Three Months Ended June 30,		Purchases During the Six Months Ended June 30,		June 30, 2007	December 31, 2006
	2007	2006	2007	2006		
Original LTV Ratio Range⁽²⁾						
Less than 60%	17%	20%	18%	20%	23%	24%
Above 60% to 70%	14	15	14	15	16	16
Above 70% to 80%	54	53	54	53	48	46
Above 80% to 90%	6	7	6	7	7	7
Above 90% to 100%	9	5	8	5	6	7
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>
Weighted average original LTV ratio	74%	72%	73%	72%	71%	70%
Estimated Current LTV Ratio Range⁽³⁾						
Less than 60%					47%	52%
Above 60% to 70%					17	18
Above 70% to 80%					21	20
Above 80% to 90%					11	8
Above 90% to 100%					3	2
Above 100%					1	—
Total					<u>100%</u>	<u>100%</u>
Weighted average estimated current LTV ratio					60%	57%
Credit Score⁽⁴⁾						
740 and above	42%	43%	42%	42%	45%	45%
700 to 739	23	24	23	24	23	23
660 to 699	19	19	19	20	18	18
620 to 659	10	10	10	10	9	9
Less than 620	5	4	5	4	4	4
Not available	1	—	1	—	1	1
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>
Weighted average credit score	719	722	719	720	724	725
Loan Purpose						
Purchase	47%	51%	46%	50%	38%	37%
Cash-out refinance	33	34	34	35	30	29
Other refinance	20	15	20	15	32	34
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>
Property Type						
1 unit	97%	98%	97%	97%	97%	97%
2-4 units	3	2	3	3	3	3
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>
Occupancy Type						
Primary residence	89%	89%	89%	89%	92%	92%
Second/vacation home	6	7	6	6	5	5
Investment	5	4	5	5	3	3
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

(1) Purchases and ending balances are based on the unpaid principal balance of the single-family mortgage portfolio (excluding certain Structured Transactions and loans purchased under financial guarantees). Purchases included in the data totaled \$118 billion and \$81 billion for the three months ended June 30, 2007 and 2006, respectively, and \$233 billion and \$174 billion for the six months ended June 30, 2007 and 2006, respectively. Ending balances included in the data totaled \$1,599 billion and \$1,482 billion at June 30, 2007 and December 31, 2006, respectively.

(2) Our charter requires that mortgage loans purchased with original LTV ratios above 80 percent be covered by mortgage insurance or other credit enhancements.

(3) Current market values are estimated by adjusting the value of the property at origination based on changes in the market value of homes since origination. Estimated current LTV ratio excludes certain Structured Transactions. Estimated current LTV ratio ranges are not applicable to purchases made during the period. We began using a new model for estimating current LTV ratios during the six months ended June 30, 2007. Prior period estimated current LTV ratios have been revised to conform to the current period presentation.

(4) Credit score data is as of mortgage loan origination for all loans within mortgage pools underlying our issued PCs and Structured Securities, as well as mortgage loans held in our Retained portfolio, and is based on the rating system scale developed by Fair, Isaac and Co., Inc., or FICO® scores.

Our charter requires that single-family mortgages with LTV ratios above 80 percent at the time of purchase be covered by one or more of the following: (a) mortgage insurance for mortgage amounts above the 80 percent threshold; (b) a seller's agreement to repurchase or replace any mortgage in default; or (c) retention by the seller of at least a 10 percent participation interest in the mortgages. In addition, we employ other types of credit enhancements, including pool insurance, indemnification agreements, collateral pledged by lenders and subordinated security structures. We also occasionally use credit enhancements to mitigate risk on multifamily mortgages.

Certain loan characteristics are often associated with a higher degree of credit risk. For example, mortgages with high LTV ratios and borrowers who have lower credit scores typically experience higher rates of delinquency, default and credit losses. We take a disciplined approach to the acquisition of mortgage loans and generally participate in these products when we believe we are appropriately compensated for the credit risk. For the 15 percent of single-family mortgages underlying our Guaranteed PCs and Structured Securities with greater than 80 percent estimated current LTV ratios the borrowers had a weighted average credit score at origination of 707 and 705 as of June 30, 2007 and December 31, 2006, respectively. Similarly, for the 14 percent of single-family mortgages underlying our Guaranteed PCs and Structured Securities where the average credit score at origination was less than 660, the average estimated current LTV ratios were 66 percent and 63 percent at June 30, 2007 and December 31, 2006, respectively.

The composition of our mortgage portfolio, as described in “Table 23 — Product Distribution,” at June 30, 2007 generally remained consistent with that at December 31, 2006, except for an increase in interest-only mortgages and a decrease in 15-year mortgages.

Table 23 summarizes the product distribution of our mortgage portfolio.

Table 23 — Product Distribution⁽¹⁾

	<u>June 30, 2007</u>	<u>December 31, 2006</u>
	(dollars in millions)	
<i>Single-family:</i>		
30-year amortizing fixed-rate ⁽²⁾	63%	63%
15-year amortizing fixed-rate	17	19
Adjustable-rate mortgages, or ARMs	6	7
Option ARMs	1	1
Interest-only	8	5
Balloon/Resets	1	1
Other	<u>1</u>	<u>1</u>
<i>Total single-family</i>	97%	97%
<i>Multifamily:</i>		
Conventional ⁽³⁾	<u>3%</u>	<u>3%</u>
<i>Total multifamily</i>	3%	3%
Total	<u><u>100%</u></u>	<u><u>100%</u></u>
Amounts related to:		
Guaranteed PCs and Structured Securities:		
Single-family	\$1,563,116	\$1,442,306
Multifamily	7,745	8,415
Structured Securities backed by non-Freddie Mac mortgage-related securities ⁽⁴⁾	21,663	26,302
Mortgage loans in the Retained portfolio:		
Single-family	21,434	20,640
Multifamily	<u>47,609</u>	<u>45,207</u>
Total	<u><u>\$1,661,567</u></u>	<u><u>\$1,542,870</u></u>

(1) Based on unpaid principal balances. Excludes non-Freddie Mac mortgage-related securities held in our Retained portfolio, but includes those that underlie Freddie Mac Structured Securities.

(2) Includes 40-year and 20-year fixed-rate mortgages.

(3) Includes Structured Transactions.

(4) Consists of Structured Transactions and that portion of Structured Securities that are backed by Ginnie Mae Certificates.

We periodically issue Structured Securities backed by mortgage loans or mortgage-related securities using collateral pools transferred to trusts that were specifically created for the purpose of issuing the securities. These trusts issue various senior interests, subordinated interests or both. We purchase interests, including senior interests, of the trusts and simultaneously issue and guarantee Structured Securities backed by these interests. We refer to these Structured Securities as Structured Transactions. Although Structured Transactions generally have underlying mortgage loans with higher risk characteristics, they may afford us credit protection from losses due to the underlying structure employed and additional credit enhancement features.

Subprime Loans

Participants in the mortgage market often characterize single-family loans based upon their overall credit quality at the time of origination, generally considering them to be prime or subprime. There is no universally accepted definition of subprime. The subprime segment of the mortgage market primarily serves borrowers with poorer credit payment histories and such loans typically have a mix of credit characteristics that indicate a higher likelihood of default and higher loss severities than prime loans. Such characteristics might include a combination of high loan-to-value ratios, low credit scores or originations using lower underwriting standards such as limited or no documentation of a borrower's income. The subprime market helps certain borrowers by broadening the availability of mortgage credit.

We estimate that approximately \$2 billion, or 0.1 percent, and \$3 billion, or 0.2 percent, of loans underlying our single-family mortgage portfolio, at June 30, 2007 and December 31, 2006, respectively, were classified as subprime mortgage loans.

With respect to our Retained portfolio, at June 30, 2007 and December 31, 2006, we held investments of approximately \$119 billion and \$124 billion, respectively, of non-agency mortgage-related securities backed by subprime loans. These securities include significant credit enhancement, particularly through subordination, and approximately 99.9 percent of these securities held at June 30, 2007, were rated AAA at August 27, 2007.

To support our mission, we announced on April 18, 2007 that we will purchase up to \$20 billion in fixed-rate and hybrid ARM products that will provide lenders with more choices to offer subprime borrowers. The products are intended to be consumer-friendly mortgages for borrowers that will limit payment shock by offering reduced adjustable-rate margins, longer fixed-rate terms and longer reset periods than existing similar products. We made our first purchase of \$106 million of mortgages pursuant to this commitment during July 2007. This first purchase of loans had an average credit score of 613 and consisted of mortgages on primary residence, single-family properties.

Alt-A Loans

Many mortgage market participants classify single-family loans that range between their prime and subprime categories as Alt-A because these loans have a combination of characteristics of each category or may be underwritten with lower or alternative documentation than a full documentation mortgage loan. Although there is no universally accepted definition of Alt-A, industry participants have used this classification principally to describe loans for which the underwriting process has been streamlined in order to reduce the documentation requirements of the borrower or allow alternative documentation.

We principally acquire mortgage loans originated as Alt-A from our traditional lenders that largely specialize in originating prime mortgage loans. These lenders typically originate Alt-A loans as a complementary product offering and generally follow an origination path similar to that used for their prime origination process. In determining our Alt-A exposure in loans underlying our single-family mortgage portfolio, we have classified mortgage loans as Alt-A if the lender that delivers them to us has classified the loans as Alt-A, or if the loans had reduced documentation requirements which indicate that the loan should be classified as Alt-A. We estimate that approximately \$120 billion, or eight percent, of loans underlying our single-family mortgage portfolio at June 30, 2007 were classified as Alt-A mortgage loans. For these loans, our average credit score was 715 and our estimated current LTV ratios were 71 percent.

We also invest in non-agency mortgage-related securities backed by Alt-A loans in our Retained portfolio. We have classified these securities as Alt-A if the securities were labeled as Alt-A when sold to us or we believe the underlying collateral includes a significant amount of Alt-A loans. We believe that \$55 billion and \$54 billion of our single-family non-agency mortgage-related securities that are not backed by subprime loans are generally backed by Alt-A mortgage loans at June 30, 2007 and December 31, 2006, respectively. We believe that our credit exposure to the Alt-A mortgage loans underlying the non-agency mortgage-related securities in our Retained portfolio is limited because we have focused our purchases on credit-enhanced, senior tranches of these securities, which provides additional protection due to subordination and approximately 99.9 percent of these securities held at June 30, 2007, were rated AAA at August 27, 2007.

Guidance on Non-traditional Mortgage Product Risks and Subprime Mortgage Lending

In October 2006, five federal financial institution regulatory agencies jointly issued the Interagency Guidance that updated earlier guidance and clarified how financial institutions should offer non-traditional mortgage products in a safe and sound manner and in a way that clearly discloses the risks that borrowers may assume. In June 2007, the same financial institution regulatory agencies published the final Subprime Statement, which addresses risks relating to subprime short-term hybrid ARMs. The Interagency Guidance and the Subprime Statement set forth principles that regulated financial institutions originating non-traditional mortgages and subprime short-term hybrid ARMs should follow with respect to their underwriting practices and should provide borrowers with clear and balanced information about the relative benefits and risks of these products sufficiently early in the process to enable them to make informed decisions.

OFHEO has directed us to adopt practices consistent with the risk management, underwriting and consumer protection principles of the Interagency Guidance and the Subprime Statement for non-traditional mortgages and subprime short-term hybrid ARMs that we purchase or which back non-agency mortgage-backed securities in which we invest. In response, on July 13, 2007 we informed our customers of new underwriting and disclosure requirements for non-traditional mortgages. In the near future, we will be informing our customers and other counterparties of similar new requirements for subprime short-term hybrid ARMs we purchase and for both subprime short-term hybrid ARMs and non-traditional mortgages backing non-agency mortgage-backed securities in which we invest. These new requirements

are also consistent with our announcement in February 2007 that we would implement stricter investment standards for certain subprime ARMs originated after September 1, 2007, and develop new mortgage products providing lenders with more choices to offer subprime borrowers. These changes could reduce the number of non-traditional and subprime mortgages available to us for purchase, potentially affecting our profitability, or our ability to achieve our housing goals and subgoals.

Credit Performance

Performing and Non-Performing Assets

We have classified single-family loans in our Total mortgage portfolio that are past due for 90 days or more (serious delinquency) or whose contractual terms have been modified due to the financial difficulties of the borrower as non-performing assets. Similarly, multifamily loans that are 60 days or more past due (serious delinquency) or where collectibility of principal and interest is not reasonably assured based on an individual loan level assessment are deemed non-performing assets. Table 24 provides detail of performing and non-performing assets within our Total mortgage portfolio.

Table 24 — Performing and Non-Performing Assets⁽¹⁾

	Performing ⁽²⁾ Assets	Non-Performing Assets		Total
		Less Than 90 Days Past Due ⁽³⁾	Seriously Delinquent ⁽⁴⁾	
June 30, 2007				
(in millions)				
<i>Mortgage Loans in Retained portfolio</i>				
Multifamily	\$ 47,316	\$ —	\$ —	\$ 47,316
Multifamily troubled debt restructurings	—	293	—	293
Subtotal, Mortgage Loans in Retained portfolio, multifamily	47,316	293	—	47,609
Single-family	12,945	—	744	13,689
Single-family loans purchased under financial guarantees ⁽⁵⁾	1,971	—	2,820	4,791
Single-family troubled debt restructurings	—	2,502	452	2,954
Subtotal, Mortgage Loans in Retained portfolio, single-family	14,916	2,502	4,016	21,434
Subtotal, Mortgage Loans in Retained portfolio	62,232	2,795	4,016	69,043
<i>Guaranteed PCs and Structured Securities Issued</i>				
Multifamily	7,663	—	30	7,693
Multifamily troubled debt restructurings	—	52	—	52
Single-family ⁽⁶⁾	1,561,067	—	2,049	1,563,116
Structured Securities backed by non-Freddie Mac mortgage-related securities ⁽⁷⁾	20,715	—	948	21,663
Subtotal, Guaranteed PCs and Structured Securities Issued	1,589,445	52	3,027	1,592,524
<i>Real Estate Owned, Net</i>	—	—	1,020	1,020
Totals	\$1,651,677	\$ 2,847	\$8,063	\$1,662,587
December 31, 2006				
(in millions)				
<i>Mortgage Loans in Retained portfolio</i>				
Multifamily	\$ 44,845	\$ —	\$ —	\$ 44,845
Multifamily troubled debt restructurings	—	362	—	362
Subtotal, Mortgage Loans in Retained portfolio, multifamily	44,845	362	—	45,207
Single-family	13,819	—	1,090	14,909
Single-family loans purchased under financial guarantees ⁽⁵⁾	1,180	—	1,862	3,042
Single-family troubled debt restructurings	—	2,219	470	2,689
Subtotal, Mortgage Loans in Retained portfolio, single-family	14,999	2,219	3,422	20,640
Subtotal, Mortgage Loans in Retained portfolio	59,844	2,581	3,422	65,847
<i>Guaranteed PCs and Structured Securities Issued</i>				
Multifamily	8,333	—	30	8,363
Multifamily troubled debt restructurings	—	52	—	52
Single-family ⁽⁶⁾	1,440,585	—	1,721	1,442,306
Structured Securities backed by non-Freddie Mac mortgage-related securities ⁽⁷⁾	25,305	—	997	26,302
Subtotal, Guaranteed PCs and Structured Securities Issued	1,474,223	52	2,748	1,477,023
<i>Real Estate Owned, Net</i>	—	—	743	743
Totals	\$1,534,067	\$ 2,633	\$6,913	\$1,543,613

(1) Based on unpaid principal balance.

(2) Consists of single-family loans that are less than 90 days past due and multifamily loans less than 60 days past due under the original terms of the mortgage.

(3) Includes loans previously reported as seriously delinquent for which the original loan terms have been modified.

(4) Consists of single-family loans 90 days or more delinquent or in foreclosure and multifamily loans 60 days or more delinquent. Delinquency status does not apply to REO; however, REO is included in non-performing assets.

- (5) Represents those loans purchased from the mortgage pools underlying PCs, Structured Securities or long-term standby agreements due to the borrower's delinquency. Generally, once we purchase a loan under our financial guarantee it is placed on non-accrual status as long as it remains greater than 90 days past due.
- (6) Once a loan in this category is delinquent for 120 days it generally is repurchased out of the security and becomes part of our Retained portfolio. Excludes Structured Securities that we classify separately as Structured Transactions.
- (7) Consists of Structured Transactions and that portion of Structured Securities that are backed by Ginnie Mae certificates. The unpaid principal balances of Structured Transactions were \$20.3 billion and \$24.8 billion at June 30, 2007 and December 31, 2006, respectively.

The amount of non-performing assets increased 14 percent during the six months ended June 30, 2007, to \$10,910 million from \$9,546 million at December 31, 2006, due to increases in the average size of seriously delinquent loans compared to 2006, as well as higher volume associated with portfolio growth. In addition, the delinquency transition rate, which is the percentage of delinquent loans that proceed to foreclosure or are modified as troubled debt restructurings, has increased during the six months ended June 30, 2007, compared to the same period in 2006. As a result, the balance of our REO, net, increased 37 percent during the six months ended June 30, 2007. The increase in the delinquency transition rate is more pronounced in mortgage loans originated in recent years, particularly mortgages originated during 2006 and 2007. Until the rate of nationwide housing appreciation increases or selected regional economies improve, we believe we will continue to experience higher delinquency transition rates than those experienced in 2006 and an increase in non-performing assets.

Delinquencies

We report single-family delinquency rate information based on the number of loans that are 90 days or more past due. For multifamily loans, we report the mortgage loans as delinquent when payment is 60 days or more past due. See "NOTE 5: LOAN LOSS RESERVES — Table 5.5 — Delinquency Performance" to our consolidated financial statements for the delinquency performance of our single-family and multifamily mortgage portfolios. Table 25 presents our single-family delinquency rates, by region.

Table 25 — Single-Family — Delinquency Rates — By Region⁽¹⁾

	June 30, 2007		December 31, 2006	
	Percent of UPB ⁽²⁾	Delinquency Rate ⁽³⁾	Percent of UPB ⁽²⁾	Delinquency Rate ⁽³⁾
Northeast	24%	0.25%	24%	0.24%
Southeast	18	0.33	18	0.30
North Central	21	0.33	21	0.32
Southwest	12	0.23	13	0.26
West	25	0.17	24	0.12
	<u>100%</u>		<u>100%</u>	
Total non-credit-enhanced — all regions		0.26		0.25
Total credit-enhanced — all regions		1.17		1.30
Total single-family portfolio		0.42		0.42

- (1) Presentation of non-credit-enhanced delinquency rates with the following regional designation: West (AK, AZ, CA, GU, HI, ID, MT, NV, OR, UT, WA); Northeast (CT, DE, DC, MA, ME, MD, NH, NJ, NY, PA, RI, VT, VA, WV); North Central (IL, IN, IA, MI, MN, ND, OH, SD, WI); Southeast (AL, FL, GA, KY, MS, NC, PR, SC, TN, VI); and Southwest (AR, CO, KS, LA, MO, NE, NM, OK, TX, WY).
- (2) Percentages are based on mortgage loans in the Retained portfolio and Total Guaranteed PCs and Structured Securities Issued, excluding that portion of Structured Securities that is backed by Ginnie Mae Certificates.
- (3) Percentages are based on mortgage loans in the Retained portfolio and Total Guaranteed PCs and Structured Securities Issued, excluding that portion of Structured Securities that is backed by Ginnie Mae Certificates and Structured Transactions. Structured Transactions generally have underlying mortgage loans with higher risk characteristics but may provide inherent credit protections from losses due to the underlying structure employed, including subordination, excess interest, over-collateralization and other features. Delinquency rates on Structured Transactions were 8.71 percent and 8.33 percent at June 30, 2007 and December 31, 2006, respectively. At June 30, 2007 and December 31, 2006, the unpaid principal balances of Structured Transactions were \$20.3 billion and \$24.8 billion, respectively, representing approximately 1 percent of our Total mortgage portfolio at both June 30, 2007 and December 31, 2006. The delinquency rate of the Total single-family portfolio, including Structured Transactions was 0.50 percent and 0.53 percent as of June 30, 2007 and December 31, 2006, respectively.

In the last half of 2006 and continuing for the six months ended June 30, 2007, there has been a significant decrease in the rate of home price appreciation and some regions have seen overall declines in home prices. In some geographical areas, particularly in the North Central region, this decline has been combined with increased rates of unemployment and weakness in other economic factors, which has resulted in increases in the rate of transition of delinquent mortgages into foreclosure status. The increase in transition rates from delinquency to foreclosure is most significant in mortgages originated in the last two years, when increasing home prices drove higher average balances for new originations without significant appreciation in home values after purchase. As a result of observed credit deterioration and higher severity of losses per loan, we have increased our loan loss reserves in 2007 reflecting the expectation that our credit losses will continue to rise in 2007 and 2008.

The delinquency rate on our Guaranteed PCs and Structured Securities portfolio, excluding that portion of Structured Securities that is backed by Ginnie Mae Certificates and Structured Transactions, was 0.42 percent at June 30, 2007 and reflects the strong housing and employment markets in the U.S. that have existed over the last several years. Minor improvement in delinquency rates occurred in all product types during the six months ended June 30, 2007,

except for interest-only mortgages. Delinquency rates for interest-only products, which represented approximately eight percent of our credit guarantee portfolio, increased to 76 basis points at June 30, 2007, compared with 44 basis points at December 31, 2006.

Table 26 presents activities related to loans purchased under financial guarantees for the three and six months ended June 30, 2007.

Table 26 — Changes in Loans Purchased Under Financial Guarantees

	Three Months Ended June 30, 2007			
	Contractual Loan Balance	Purchase Discount	Loan Loss Reserves	Net Investment
	(in millions)			
Beginning balance, March 31, 2007	\$4,037	\$ (380)	\$ (6)	\$3,651
Purchases of loans	1,841	(307)	—	1,534
Provision for credit losses	—	—	(7)	(7)
Principal repayments	(441)	42	1	(398)
Troubled debt restructurings ⁽¹⁾	(166)	23	—	(143)
Foreclosures, transferred to REO	(480)	56	2	(422)
Ending balance, June 30, 2007 ⁽²⁾	<u>\$4,791</u>	<u>\$ (566)</u>	<u>\$ (10)</u>	<u>\$4,215</u>
	Six Months Ended June 30, 2007			
	Contractual Loan Balance	Purchase Discount	Loan Loss Reserves	Net Investment
	(in millions)			
Beginning balance, December 31, 2006	\$3,042	\$ (201)	\$ —	\$2,841
Purchases of loans	3,693	(546)	—	3,147
Provision for credit losses	—	—	(13)	(13)
Principal repayments	(745)	64	1	(680)
Troubled debt restructurings ⁽¹⁾	(312)	35	—	(277)
Foreclosures, transferred to REO	(887)	82	2	(803)
Ending balance, June 30, 2007 ⁽²⁾	<u>\$4,791</u>	<u>\$ (566)</u>	<u>\$ (10)</u>	<u>\$4,215</u>

(1) Consists of loans that have transitioned into troubled debt restructurings during the stated period.

(2) Includes \$1,217 million and \$1,098 million of contractual balance and net investment in loans, respectively, that have subsequently returned to current status under the original loan terms at June 30, 2007.

We have the right to purchase mortgages that back our PCs and Structured Securities from the loan pools when they have been past due for 120 days and in certain circumstances sooner, if there have been early indications of credit deterioration such as extraordinary personal or financial hardship events of the borrower. This right to repurchase collateral is known as our repurchase option. We record loans that we purchase out of PCs and Structured Securities held by third parties, in connection with our repurchase option, at fair value. We record Losses on loans purchased on our consolidated statements of income in order to reduce our net investment in the acquired loan to its fair value. Loans that we purchase out of PCs held by us, in connection with our repurchase option, are recorded at their carrying amount which generally approximates fair value because the related PC residual is generally accounted for at fair value with changes in market valuations recorded in our consolidated statements of income.

We expect that we will continue to incur losses on the purchase of non-performing loans during the remainder of 2007. However, the volume and severity of these losses is dependent on many factors, including house price appreciation and the changes in the market environment for non-performing assets. In the current market, we believe there is a disparity between fair values of these loans and the actual amounts we ultimately expect to recover. Based on the reperformance rate experienced on these loans as well as our access to credit enhancement remedies that are not considered in the market determination of the loan's fair value, we expect our recoveries to exceed the recorded net investment in these purchased loans, in the aggregate.

The recapture of losses previously recognized on purchased loans may occur when a borrower repays the loan or with the proceeds from the disposition of the REO obtained as a result of foreclosure. As indicated in Table 26, at December 31, 2006, there was a \$201 million purchase discount representing the difference between contractual loan balances and the prevailing market values at acquisition for those non-performing loans that we purchased from PC and mortgage loan pools in fulfillment of our guarantees. For loans purchased out of mortgage loan pools during 2006, we have recaptured greater than 47 percent of the purchase discount recorded on those loans. Loans acquired during the six months ended June 30, 2007 added \$546 million of purchase discount, which reflects: (a) \$171 million that was previously recorded on our consolidated balance sheets either as Reserve for guarantee losses on Participation Certificates, net Guarantee obligation, or PC residuals if the related PC was held in our Retained portfolio; and (b) \$375 million of Losses on loans purchased as shown on our consolidated statements of income.

The unpaid principal balance of non-performing loans that have been purchased under our financial guarantees and that have not been modified under troubled debt restructurings has increased approximately 58 percent during the six

months ended June 30, 2007. During this period, we purchased approximately \$3.7 billion in contractual balances of these loans with a fair value of \$3.1 billion. In resolution and disposition of loans purchased under financial guarantees during the six months ended June 30, 2007, \$887 million, or approximately 13 percent, of these loans proceeded to foreclosure and \$1.1 billion, or approximately 16 percent, were either repaid or were modified under a troubled debt restructuring. There were approximately 39,000 and 27,000 of these mortgages remaining at June 30, 2007 and December 31, 2006, respectively.

Credit Loss Performance

Some of the loans that are delinquent or in foreclosure result in credit losses. Table 27 provides detail on our credit loss performance associated with mortgage loans in our Retained portfolio, including those purchased out of PCs and Structured Securities.

Table 27 — Credit Loss Performance

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(dollars in millions)			
REO				
REO balances:				
Single-family	\$ 1,014	\$ 646	\$ 1,014	\$ 646
Multifamily	6	18	6	18
Total	<u>\$ 1,020</u>	<u>\$ 664</u>	<u>\$ 1,020</u>	<u>\$ 664</u>
REO activity ⁽¹⁾ (number of properties):				
Beginning property inventory	9,650	8,263	8,785	8,070
Properties acquired	5,013	4,163	9,651	8,214
Properties disposed	(4,403)	(4,124)	(8,176)	(7,982)
Ending property inventory	<u>10,260</u>	<u>8,302</u>	<u>10,260</u>	<u>8,302</u>
Average holding period ⁽²⁾ (in days)	169	175	170	182
REO operations expense:				
Single-family	\$ (16)	\$ (7)	\$ (30)	\$ (19)
Multifamily	—	—	—	—
Total	<u>\$ (16)</u>	<u>\$ (7)</u>	<u>\$ (30)</u>	<u>\$ (19)</u>
CHARGE-OFFS				
Single-family:				
Charge-offs, gross ⁽³⁾ (including \$87 million, \$80 million, \$169 million and \$152 million relating to loan loss reserves, respectively)	\$ (114)	\$ (80)	\$ (207)	\$ (152)
Recoveries	51	40	100	82
Single-family, net	<u>\$ (63)</u>	<u>\$ (40)</u>	<u>\$ (107)</u>	<u>\$ (70)</u>
Multifamily:				
Charge-offs, gross	\$ —	\$ —	\$ —	\$ —
Recoveries	—	—	—	—
Multifamily, net	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
Total charge-offs, net	<u>\$ (63)</u>	<u>\$ (40)</u>	<u>\$ (107)</u>	<u>\$ (70)</u>
CREDIT LOSSES⁽⁴⁾				
Single-family	\$ (79)	\$ (47)	\$ (137)	\$ (89)
Multifamily	—	—	—	—
Total	<u>\$ (79)</u>	<u>\$ (47)</u>	<u>\$ (137)</u>	<u>\$ (89)</u>
In basis points ⁽⁵⁾ (annualized):				
Single-family	(2.0)	(1.3)	(1.7)	(1.2)
Multifamily	—	—	—	—
Total	<u>(2.0)</u>	<u>(1.3)</u>	<u>(1.7)</u>	<u>(1.2)</u>

(1) Includes single-family and multifamily REO properties.

(2) Represents weighted average holding period for single-family and multifamily based on number of REO properties.

(3) Charge-offs represent the amount of the unpaid principal balance of a loan that has been discharged in order to remove the loan from our Retained portfolio at the time of resolution, regardless of when the impact of the credit loss was recorded on our consolidated statements of income through the Provision for credit losses or Losses on loans purchased. The amount of charge-offs for credit loss performance is generally derived as the contractual balance of a loan at the date it is discharged less the estimated value in final disposition.

(4) Equal to REO operations expense plus charge-offs, net.

(5) Calculated as annualized Credit losses divided by the average Total mortgage portfolio, excluding non-Freddie Mac mortgage-related securities and that portion of Structured Securities that is backed by Ginnie Mae Certificates.

Our credit loss performance is an indicator of the effectiveness of both risk management and loss mitigation strategies. However, this is a historical metric that measures losses at the conclusion of a delinquent loan resolution process, which may occur several years from the point of initial delinquency. While our credit losses have shown an increase from the prior year, our credit losses, net of recoveries, in basis points, remain low. The credit loss performance above does not include an estimate of probable incurred losses in the three and six month periods on mortgage loans held-

for-investment in the Retained portfolio and mortgages underlying PCs held by third parties. These unrealized losses are recorded in our Provision for credit losses and Losses on loans purchased in our consolidated financial statements.

OFF-BALANCE SHEET ARRANGEMENTS

We enter into certain business arrangements that are not recorded on our consolidated balance sheets or may be recorded in amounts that differ from the full contract or notional amount of the transaction. Most of these arrangements relate to our financial guarantee and securitization activity for which we record guarantee-related assets and obligations, but the related securitized assets are owned by third parties. See “MD&A — OFF-BALANCE SHEET ARRANGEMENTS” in our 2006 Information Statement for more discussion of our off-balance sheet arrangements.

As part of our credit guarantee business, we routinely enter into forward purchase and sale commitments for mortgage loans and mortgage-related securities. Some of these commitments are accounted for as derivatives. Their fair values are reported as either Derivative assets, at fair value or Derivative liabilities, at fair value on our consolidated balance sheets. Certain non-derivative commitments are related to commitments arising from mortgage swap transactions and commitments to purchase certain multifamily mortgage loans that will be classified as held-for-investment. These non-derivative commitments totaled \$228.6 billion and \$264.4 billion at June 30, 2007 and December 31, 2006, respectively. Such commitments are not accounted for as derivatives and are not recorded on our consolidated balance sheets.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in conformity with GAAP requires us to make a number of judgments, estimates and assumptions that affect the reported amounts of our assets, liabilities, income and expenses. Certain of our accounting policies, as well as estimates we make, are critical to the presentation of our financial condition and results of operations. They often require management to make difficult, complex or subjective judgments and estimates, at times, regarding matters that are inherently uncertain. Actual results could differ from our estimates and different judgments and assumptions related to these policies and estimates could have a material impact on the consolidated financial statements.

Our critical accounting policies and estimates relate to: (a) valuation of financial instruments; (b) issuances and transfers of PCs and Structured Securities; (c) derivative instruments and hedging activities; (d) credit losses; (e) amortization of cost basis adjustments using the effective interest method; and (f) impairment recognition on investments in securities. For additional information about our critical accounting policies and estimates and other significant accounting policies, including recently issued accounting pronouncements, see “MD&A — CRITICAL ACCOUNTING POLICIES AND ESTIMATES” and “NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES” to our consolidated financial statements in our 2006 Information Statement.

OUR PORTFOLIOS

Table 28 — Freddie Mac’s Total Mortgage Portfolio Based on Unpaid Principal Balances⁽¹⁾

	June 30, 2007		December 31, 2006	
	Amount	% of Total Mortgage Portfolio	Amount	% of Total Mortgage Portfolio
Outstanding Guaranteed PCs and Structured Securities ⁽²⁾	\$1,240,813	63%	\$1,122,761	61%
Retained portfolio:				
PCs and Structured Securities	351,711	18	354,262	19
Non-Freddie Mac mortgage-related securities:				
Agency mortgage-related securities	44,861	2	45,385	3
Non-agency mortgage-related securities	246,521	13	238,465	13
Total non-Freddie Mac mortgage-related securities	291,382	15	283,850	16
Mortgage loans	69,043	4	65,847	4
Total Retained portfolio ⁽³⁾	712,136	37	703,959	39
Total mortgage portfolio	<u>\$1,952,949</u>	<u>100%</u>	<u>\$1,826,720</u>	<u>100%</u>

(1) Excludes mortgage loans and mortgage-related securities traded, but not yet settled.

(2) Represent Guaranteed PCs and Structured Securities held by third parties.

(3) Differs from the Retained portfolio presented in our consolidated balance sheets because the amounts presented in our consolidated balance sheets include valuation adjustments and deferred balances. See “CONSOLIDATED BALANCE SHEETS ANALYSIS — Retained Portfolio — Table 10 — Characteristics of Mortgage Loans and Mortgage-Related Securities in the Retained Portfolio” for a reconciliation of the Retained portfolio amounts shown in this table to the amounts shown under such caption in conformity with GAAP on our consolidated balance sheets.

Due to changes in market conditions during the first six months of 2007, the GSEs have had greater opportunity to compete with the non-agency securitization market and consequently have collectively increased market share during the six months ended June 30, 2007. In addition, during the six months ended June 30, 2007 and 2006, we grew our portfolio of Guaranteed PCs and Structured Securities outstanding at an annualized rate of 21 percent and 13 percent, respectively. Although the demand by borrowers for non-traditional mortgages, such as interest-only and option ARMs, remained strong, we did not purchase any option ARM products during the six months ended June 30, 2007, in contrast to approximately \$6 billion of option ARM purchases during the six months ended June 30, 2006. Our purchases of interest-only mortgage loans during the six months ended June 30, 2007 and 2006, were 25 percent and 13 percent, respectively, of our total purchase volume. We impose risk management thresholds on purchases of certain new products for which we have limited historical experience.

Table 29 summarizes purchases into our Total mortgage portfolio.

Table 29 — Total Mortgage Portfolio Activity Detail⁽¹⁾

	Three Months Ended June 30,				Six Months Ended June 30,			
	2007		2006		2007		2006	
	Amount	% of Purchase Amounts	Amount	% of Purchase Amounts	Amount	% of Purchase Amounts	Amount	% of Purchase Amounts
	(dollars in millions)							
New business purchases:								
Single-family mortgage purchases:								
Conventional:								
Amortizing fixed-rate ⁽²⁾	\$ 81,940	67%	\$ 64,831	77%	\$162,439	68%	\$133,790	73%
ARMs/Variable-rate ⁽³⁾	4,513	4	4,317	5	8,974	3	10,098	6
Interest-only ⁽⁴⁾	31,771	26	10,236	12	60,910	25	23,792	13
Balloon/Resets ⁽⁵⁾	16	<1	135	<1	32	<1	319	<1
FHA/VA ⁽⁶⁾	18	<1	—	—	144	1	—	—
Rural Housing Service and other federally guaranteed loans	50	<1	49	<1	86	<1	77	<1
Total single-family	118,308	97	79,568	94	232,585	97	168,076	92
Multifamily:								
Conventional	2,515	2	3,079	4	5,654	2	6,587	4
Total multifamily	2,515	2	3,079	4	5,654	2	6,587	4
Total mortgage purchases	120,823	99	82,647	98	238,239	99	174,663	96
Non-Freddie Mac mortgage-related securities purchased for Structured Securities:								
Ginnie Mac Certificates	33	<1	16	<1	40	<1	34	<1
Structured Transactions ⁽⁷⁾	200	1	1,326	2	200	1	6,247	4
Total non-Freddie Mac mortgage-related securities purchased for Structured Securities	233	1	1,342	2	240	1	6,281	4
Total single-family and multifamily mortgage purchases and total non-Freddie Mac mortgage-related securities purchased for Structured Securities	121,056	100%	83,989	100%	238,479	100%	180,944	100%
Non-Freddie Mac mortgage-related securities purchased into the Retained portfolio:								
Agency securities:								
Single-family:								
Fixed-rate	782		1,837		1,103		3,796	
Variable-rate	2,738		3,482		3,729		4,548	
Total Agency	3,520		5,319		4,832		8,344	
Non-agency securities:								
<i>Mortgage-related securities, other:</i>								
Single-family:								
Fixed-rate	269		718		269		718	
Variable-rate	17,284		27,045		38,584		54,387	
Total mortgage-related securities, other	17,553		27,763		38,853		55,105	
CMBS:								
Fixed-rate	2,923		431		3,101		2,413	
Variable-rate	3,791		2,961		9,796		5,056	
Total CMBS	6,714		3,392		12,897		7,469	
Mortgage revenue bonds:								
Single-family:								
Fixed-rate	558		1,227		803		1,682	
Variable-rate	—		—		—		—	
Multifamily:								
Fixed-rate	—		40		—		60	
Variable-rate	—		—		—		—	
Total mortgage revenue bonds	558		1,267		803		1,742	
Total non-agency mortgage-related securities	24,825		32,422		52,553		64,316	
Total non-Freddie Mac mortgage-related securities purchased into the Retained portfolio	28,345		37,741		57,385		72,660	
Total new business purchases	\$149,401		\$121,730		\$295,864		\$253,604	
Mortgage purchases with credit enhancements	18%		15%		16%		17%	
Mortgage liquidations ⁽⁸⁾	\$ 87,691		\$ 87,525		\$168,752		\$164,540	
Mortgage liquidations rate ⁽⁸⁾	19%		20%		19%		20%	
Freddie Mac securities repurchased into the Retained portfolio:								
Single-family:								
Fixed-rate	\$ 21,439		\$ 31,023		\$ 37,983		\$ 48,740	
Variable-rate	7,799		7,800		18,330		17,310	
Total Freddie Mac securities repurchased into the Retained portfolio	\$ 29,238		\$ 38,823		\$ 56,313		\$ 66,050	

(1) Based on unpaid principal balances. Excludes mortgage loans and mortgage-related securities traded, but not yet settled.

(2) Includes 40-year, 30-year, 20-year and 15-year fixed-rate mortgages.

(3) Includes ARMs with 1-, 3-, 5-, 7- and 10-year initial fixed-rate periods.

(4) Represents loans where the borrower pays interest only for a period of time before the borrower begins making principal payments.

(5) Represents mortgages whose terms require lump sum principal payments on contractually determined future dates unless the borrower qualifies for and elects an extension of the maturity date with an adjusted interest-rate.

(6) Excludes FHA/VA loans that back Structured Transactions.

(7) Includes \$— million and \$1,326 million of option ARMs purchased for Structured Transactions during the three months ended June 30, 2007 and 2006, respectively; and \$— million and \$6,247 million of option ARMs purchased for Structured Transactions during the six months ended June 30, 2007 and 2006, respectively.

(8) Based on the Total mortgage portfolio.

Table 30 presents ending balance and issuance detail of our credit guarantee business activity.

Table 30 — Guaranteed PCs and Structured Securities⁽¹⁾

	June 30, 2007		December 31, 2006	
	Total Issued PCs and Structured Securities	Outstanding PCs and Structured Securities ⁽²⁾	Total Issued PCs and Structured Securities	Outstanding PCs and Structured Securities ⁽²⁾
	(in millions)			
Ending Balances				
PCs and Structured Securities				
Single-family:				
Conventional:				
30-year fixed-rate ⁽³⁾	\$1,061,290	\$ 869,914	\$ 956,842	\$ 763,563
15-year fixed-rate	275,231	198,309	290,314	202,747
ARMs/Variable-rate	203,659	136,595	169,254	116,910
Option ARMs	2,238	271	2,808	303
Balloons/Resets	19,272	18,370	21,551	20,508
FHA/VA	1,293	1,141	1,398	1,267
Rural Housing Service and other federally guaranteed loans	133	133	139	139
<i>Total single-family</i>	<u>1,563,116</u>	<u>1,224,733</u>	<u>1,442,306</u>	<u>1,105,437</u>
Multifamily:				
Conventional:				
Fixed-rate	3,039	2,799	3,449	3,208
Variable-rate	4,706	4,567	4,966	4,825
<i>Total multifamily</i>	<u>7,745</u>	<u>7,366</u>	<u>8,415</u>	<u>8,033</u>
Structured Securities backed by non-Freddie Mac mortgage-related securities:				
Ginnie Mae Certificates ⁽⁴⁾	1,395	1,370	1,510	1,481
Structured Transactions ⁽⁵⁾	20,268	7,344	24,792	7,810
<i>Total Structured Securities backed by Non-Freddie Mac mortgage-related securities</i>	<u>21,663</u>	<u>8,714</u>	<u>26,302</u>	<u>9,291</u>
Total	<u><u>\$1,592,524</u></u>	<u><u>\$1,240,813</u></u>	<u><u>\$1,477,023</u></u>	<u><u>\$1,122,761</u></u>

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Issuance Detail				
PCs and Structured Securities				
Single-family:				
Conventional:				
30-year fixed-rate ⁽³⁾	\$ 76,106	\$59,498	\$152,026	\$122,099
15-year fixed-rate	5,329	5,424	10,009	11,729
ARMs/Variable-rate	4,508	4,308	8,982	10,099
Interest-only	31,688	10,230	60,814	23,769
Balloon/Resets	16	127	26	307
FHA/VA	19	—	145	—
Rural Housing Service and other federally guaranteed loans	3	1	4	3
<i>Total single-family</i>	<u>117,669</u>	<u>79,588</u>	<u>232,006</u>	<u>168,006</u>
Multifamily:				
Conventional				
	<u>107</u>	<u>43</u>	<u>127</u>	<u>355</u>
<i>Total multifamily</i>	<u>107</u>	<u>43</u>	<u>127</u>	<u>355</u>
Structured Securities that are backed by non-Freddie Mac mortgage-related securities:				
Ginnie Mae Certificates ⁽⁴⁾	32	16	40	34
Structured Transactions ⁽⁵⁾⁽⁶⁾	200	1,326	200	6,247
<i>Total Structured Securities backed by non-Freddie Mac mortgage-related securities</i>	<u>232</u>	<u>1,342</u>	<u>240</u>	<u>6,281</u>
Total Guaranteed PCs and Structured Securities Issued	<u><u>\$118,008</u></u>	<u><u>\$80,973</u></u>	<u><u>\$232,373</u></u>	<u><u>\$174,642</u></u>
Resecuritization Activity:				
Multi-class	\$ 53,882	\$47,200	\$ 79,571	\$ 92,609
Single-class	70,894	50,292	136,601	96,838
Total activity	<u><u>\$124,776</u></u>	<u><u>\$97,492</u></u>	<u><u>\$216,172</u></u>	<u><u>\$189,447</u></u>

(1) Based on unpaid principal balances. Excludes mortgage loans and mortgage-related securities traded, but not yet settled.

(2) Represent PCs and Structured Securities held by third parties.

(3) Includes 40-year and 20-year fixed-rate mortgages.

(4) Ginnie Mae Certificates that underlie the Structured Securities are backed by FHA/VA loans.

(5) Represents Structured Securities backed by non-agency securities that include prime, FHA/VA and subprime mortgage loans.

(6) Includes \$— million and \$1,326 million of option ARMs purchased for Structured Transactions during the three months ended June 30, 2007 and 2006, respectively; and \$— million and \$6,247 million of Option ARMs purchased for Structured Transactions during the six months ended June 30, 2007 and 2006, respectively.

UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS AND ACCOMPANYING NOTES

FREDDIE MAC
CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(dollars in millions, except share-related amounts)			
<i>Interest income</i>				
Mortgage loans	\$ 1,079	\$ 1,040	\$ 2,140	\$ 2,080
Mortgage-related securities	8,960	8,878	17,723	17,123
Cash and investments	966	1,119	1,938	1,893
Total interest income	11,005	11,037	21,801	21,096
<i>Interest expense</i>				
Short-term debt	(2,249)	(2,241)	(4,457)	(4,256)
Long-term debt	(7,331)	(7,110)	(14,507)	(13,543)
Total interest expense on debt securities	(9,580)	(9,351)	(18,964)	(17,799)
Due to Participation Certificate investors	(121)	(104)	(224)	(195)
Total interest expense	(9,701)	(9,455)	(19,188)	(17,994)
Expense related to derivatives	(331)	(410)	(662)	(799)
<i>Net interest income</i>	973	1,172	1,951	2,303
<i>Non-interest income</i>				
Management and guarantee income (includes interest on Guarantee asset of \$111, \$125, \$218 and \$232, respectively)	474	389	934	802
Gains (losses) on Guarantee asset	739	61	329	221
Income on Guarantee obligation	281	217	493	412
Derivative gains (losses)	281	355	(247)	628
Gains (losses) on investment activity	(368)	(312)	(551)	(146)
Gains on debt retirement	89	244	96	308
Resecuritization fees	35	31	54	79
Foreign currency losses, net	(333)	(30)	(530)	(33)
Other income	84	24	150	55
<i>Non-interest income</i>	1,282	979	728	2,326
<i>Non-interest expense</i>				
Salaries and employee benefits	(243)	(203)	(471)	(394)
Professional services	(117)	(118)	(225)	(218)
Occupancy expense	(16)	(15)	(30)	(29)
Other administrative expenses	(66)	(69)	(119)	(137)
Total administrative expenses	(442)	(405)	(845)	(778)
Provision for credit losses	(320)	(56)	(499)	(20)
Real estate owned, or REO, operations expense	(16)	(7)	(30)	(19)
Losses on certain credit guarantees	(187)	(52)	(331)	(98)
Losses on loans purchased	(205)	(21)	(375)	(42)
Low-income housing tax credit partnerships	(135)	(104)	(243)	(219)
Other expenses	(73)	(69)	(129)	(122)
<i>Non-interest expense</i>	(1,378)	(714)	(2,452)	(1,298)
Income before income tax (expense) benefit	877	1,437	227	3,331
Income tax (expense) benefit	(113)	(40)	326	75
<i>Net income</i>	764	1,397	553	3,406
Preferred stock dividends and issuance costs on redeemed preferred stock (including \$—, \$—, \$6 and \$— of issuance costs on redeemed preferred stock, respectively)	(95)	(59)	(190)	(117)
Amount allocated to participating stock option holders	(2)	(3)	(1)	(5)
<i>Net income available to common stockholders</i>	\$ 667	\$ 1,335	\$ 362	\$ 3,284
Earnings per common share:				
Basic	\$ 1.02	\$ 1.93	\$ 0.55	\$ 4.74
Diluted	\$ 1.02	\$ 1.93	\$ 0.55	\$ 4.73
Weighted average common shares outstanding (in thousands)				
Basic	652,877	691,773	657,103	692,290
Diluted	655,784	693,026	659,365	693,755
Dividends per common share	\$ 0.50	\$ 0.47	\$ 1.00	\$ 0.94

The accompanying notes are an integral part of these unaudited consolidated financial statements.

**FREDDIE MAC
CONSOLIDATED BALANCE SHEETS**

	June 30, 2007 (unaudited)	December 31, 2006
	(in millions, except share-related amounts)	
Assets		
<i>Retained portfolio</i>		
Mortgage loans:		
Held-for-investment, at amortized cost	\$ 66,101	\$ 63,780
Reserve for losses on mortgage loans held-for-investment	(108)	(70)
Held-for-sale, at lower-of-cost-or-market	2,357	1,908
Mortgage loans, net of reserve	68,350	65,618
Mortgage-related securities:		
Available-for-sale, at fair value (includes \$17,777 and \$20,463, respectively, pledged as collateral that may be repledged)	622,364	626,731
Trading, at fair value	12,075	7,597
Participation Certificate residuals, at fair value	497	597
Total mortgage-related securities	634,936	634,925
<i>Retained portfolio</i>	703,286	700,543
<i>Cash and investments</i>		
Cash and cash equivalents	11,808	11,359
Investments:		
Non-mortgage-related securities:		
Available-for-sale, at fair value	41,746	45,586
Securities purchased under agreements to resell and Federal funds sold	27,502	23,028
<i>Cash and investments</i>	81,056	79,973
Accounts and other receivables, net	7,634	7,461
Derivative assets, at fair value	7,203	7,908
Guarantee asset, at fair value	7,777	6,070
REO, net	1,020	743
Other assets	13,697	10,383
<i>Total assets</i>	\$ 821,673	\$ 813,081
Liabilities and stockholders' equity		
<i>Debt securities, net</i>		
Senior debt:		
Due within one year	\$ 276,974	\$ 294,861
Due after one year	478,295	452,677
Subordinated debt, due after one year	5,227	6,400
<i>Total debt securities, net</i>	760,496	753,938
Due to Participation Certificate investors	13,261	11,123
Accrued interest payable	8,475	8,345
Guarantee obligation	8,574	7,117
Derivative liabilities, at fair value	337	179
Reserve for guarantee losses on Participation Certificates	682	350
Other liabilities	3,756	3,212
<i>Total liabilities</i>	795,581	784,264
Commitments and contingencies (Notes 2, 3, 11 and 12)		
Minority interests in consolidated subsidiaries	282	516
<i>Stockholders' equity</i>		
Preferred stock, at redemption value	7,109	6,109
Common stock, \$0.21 par value, 726,000,000 shares authorized, 725,863,886 shares issued and 650,138,001 shares and 661,254,178 shares outstanding, respectively	152	152
Additional paid-in capital	954	962
Retained earnings	32,064	32,177
Accumulated other comprehensive income (loss), or AOCI, net of taxes, related to:		
Available-for-sale securities	(5,869)	(2,749)
Cash flow hedge relationships	(4,574)	(5,033)
Defined benefit plans	(81)	(87)
Total AOCI, net of taxes	(10,524)	(7,869)
Treasury stock, at cost, 75,725,885 shares and 64,609,708 shares, respectively	(3,945)	(3,230)
<i>Total stockholders' equity</i>	25,810	28,301
<i>Total liabilities and stockholders' equity</i>	\$ 821,673	\$ 813,081

The accompanying notes are an integral part of these unaudited consolidated financial statements.

FREDDIE MAC
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(UNAUDITED)

	Six Months Ended June 30,			
	2007		2006	
	Shares	Amount	Shares	Amount
	(in millions)			
<i>Preferred stock, at redemption value</i>				
Balance, beginning of year	132	\$ 6,109	92	\$ 4,609
Preferred stock issuances	64	1,600	—	—
Preferred stock redemptions	(12)	(600)	—	—
<i>Preferred stock, end of period</i>	<u>184</u>	<u>7,109</u>	<u>92</u>	<u>4,609</u>
<i>Common stock, par value</i>				
Balance, beginning of year	726	152	726	152
<i>Common stock, end of period</i>	<u>726</u>	<u>152</u>	<u>726</u>	<u>152</u>
<i>Additional paid-in capital</i>				
Balance, beginning of year		962		924
Stock-based compensation		41		21
Income tax benefit from stock-based compensation		1		9
Preferred stock issuance costs		(16)		—
Common stock issuance		(27)		(10)
Real Estate Investment Trust, or REIT, preferred stock repurchase		(7)		—
<i>Additional paid-in capital, end of period</i>		<u>954</u>		<u>944</u>
<i>Retained earnings</i>				
Balance, beginning of year		32,177		31,559
Cumulative effect of change in accounting principle, net of taxes		181		(13)
Balance, beginning of year, as adjusted		32,358		31,546
Net income		553		3,406
Preferred stock dividends declared		(184)		(117)
Common stock dividends declared		(663)		(657)
<i>Retained earnings, end of period</i>		<u>32,064</u>		<u>34,178</u>
<i>AOCI, net of taxes</i>				
Balance, beginning of year		(7,869)		(8,773)
Changes in unrealized gains (losses) related to available-for-sale securities, net of reclassification adjustments		(3,120)		(6,300)
Changes in unrealized gains (losses) related to cash flow hedge relationships, net of reclassification adjustments		459		685
Changes in defined benefit plans		6		—
<i>AOCI, net of taxes, end of period</i>		<u>(10,524)</u>		<u>(14,388)</u>
<i>Treasury stock, at cost</i>				
Balance, beginning of year	65	(3,230)	33	(1,280)
Common stock issuances	(1)	35	(1)	20
Common stock repurchases	12	(750)	9	(500)
<i>Treasury stock, end of period</i>	<u>76</u>	<u>(3,945)</u>	<u>41</u>	<u>(1,760)</u>
<i>Total stockholders' equity</i>		<u>\$25,810</u>		<u>\$23,735</u>
<i>Comprehensive income (loss)</i>				
Net income		\$ 553		\$ 3,406
Changes in other comprehensive income, net of taxes, net of reclassification adjustments		(2,655)		(5,615)
<i>Total comprehensive income (loss)</i>		<u>\$(2,102)</u>		<u>\$(2,209)</u>

The accompanying notes are an integral part of these unaudited consolidated financial statements.

FREDDIE MAC
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Six Months Ended June 30,	
	2007	2006
	(in millions)	
Cash flows from operating activities		
Net income	\$ 553	\$ 3,406
Adjustments to reconcile net income to net cash provided by operating activities:		
Hedge accounting losses	—	11
Derivative losses (gains)	379	(602)
Asset related amortization — premiums, discounts and hedging basis adjustments	(68)	60
Debt related amortization — premiums and discounts on certain debt securities and hedging basis adjustments	5,391	5,617
Net discounts paid on retirements of debt	(4,240)	(3,435)
Gains on debt retirement	(96)	(308)
Provision for credit losses	499	20
Low-income housing tax credit partnership losses	243	219
Losses on loans purchased	375	42
Losses on investment activity	511	473
Foreign currency losses, net	530	33
Deferred income taxes	(1,268)	188
Purchases of held-for-sale mortgages	(9,886)	(8,962)
Sales of held-for-sale mortgages	9,156	9,006
Repayments of held-for-sale mortgages	57	39
Net (purchases) proceeds of trading securities	(2,159)	385
Change in accounts and other receivables, net	(570)	(728)
Change in amounts due to Participation Certificate investors, net	2,336	634
Change in accrued interest payable	154	536
Change in income taxes payable	335	(1,457)
Change in Guarantee asset, at fair value	(1,708)	(1,007)
Change in Guarantee obligation	1,466	611
Change in Participation Certificate residuals, at fair value	(25)	(323)
Other, net	337	470
<i>Net cash provided by operating activities</i>	2,302	4,928
Cash flows from investing activities		
Purchases of available-for-sale securities	(157,291)	(214,529)
Proceeds from sales of available-for-sale securities	37,005	49,672
Proceeds from maturities of available-for-sale securities	120,382	147,131
Purchases of held-for-investment mortgages	(8,177)	(7,888)
Repayments of held-for-investment mortgages	4,979	5,233
Proceeds from mortgage insurance and sales of REO	813	748
Net increase in securities purchased under agreements to resell and Federal funds sold	(4,473)	(30,660)
Derivative premiums and terminations, net	688	(932)
Investments in low-income housing tax credit partnerships	(57)	(139)
<i>Net cash used for investing activities</i>	(6,131)	(51,364)
Cash flows from financing activities		
Proceeds from issuance of short-term debt	473,497	318,257
Repayments of short-term debt	(478,057)	(330,088)
Proceeds from issuance of long-term debt	118,775	119,280
Repayments of long-term debt	(108,517)	(56,833)
Repayments of minority interest in consolidated subsidiaries	(3)	(230)
Repurchase of Real Estate Investment Trust preferred stock	(231)	—
Proceeds from the issuance of preferred stock	1,584	—
Redemption of preferred stock	(600)	—
Proceeds from issuance of common stock	8	11
Repurchases of common stock	(750)	(500)
Payment of cash dividends on preferred stock and common stock	(847)	(774)
Excess tax benefits associated with stock-based awards	3	11
Payments of low-income housing tax credit partnerships notes payable	(568)	(728)
(Decrease) increase in cash overdraft	(16)	33
<i>Net cash provided by financing activities</i>	4,278	48,439
Net increase in cash and cash equivalents	449	2,003
Cash and cash equivalents at beginning of period	11,359	10,468
<i>Cash and cash equivalents at end of period</i>	\$ 11,808	\$ 12,471
Supplemental cash flow information		
Cash paid (received) for:		
Interest	\$ 18,728	\$ 16,177
Derivative interest carry, net	(165)	(133)
Income taxes	607	1,195
Non-cash investing and financing activities:		
Held-for-sale mortgages securitized and retained as available-for-sale securities	169	13
Transfers from mortgage loans to REO	1,147	774
Investments in low-income housing tax credit partnerships financed by notes payable	117	138
Transfers from held-for-sale mortgages to held-for-investment mortgages	40	63
Transfers from held-for-investment mortgages to held-for-sale mortgages	—	950
Transfers from Retained portfolio Participation Certificates to held-for-investment mortgages	828	670

The accompanying notes are an integral part of these unaudited consolidated financial statements.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

We are a stockholder-owned government-sponsored enterprise, or GSE, established by Congress in 1970 to provide a continuous flow of funds for residential mortgages. Our obligations are ours alone and are not insured or guaranteed by the U.S. government, or any other agency or instrumentality of the U.S. We play a fundamental role in the U.S. housing finance system, linking the domestic mortgage market and the global capital markets. Our participation in the secondary mortgage market includes providing our credit guarantee on securities backed by residential mortgages originated by mortgage lenders and investing in mortgage loans and mortgage-related securities that we hold in our Retained portfolio. Through our credit guarantee activities, we securitize mortgage loans by issuing Mortgage Participation Certificates, or PCs, to third-party investors. We also resecuritize mortgage-related securities that are issued by us or the Government National Mortgage Association, or Ginnie Mae, as well as non-agency entities. We also guarantee the payment of principal and interest with respect to multifamily mortgage loans that support housing revenue bonds issued by third parties. Securitized mortgage-related assets that back PCs and Structured Securities that are held by third parties are not reflected as our assets. In return for providing our guarantee on issued PCs and Structured Securities, we may earn a management and guarantee fee that is paid to us over the life of the related PCs and Structured Securities. Our guarantee of the payment of principal and interest on outstanding PCs and Structured Securities is reflected in our consolidated financial statements through the recognition of a Guarantee asset and Guarantee obligation.

Basis of Presentation

The accompanying unaudited consolidated financial statements include our accounts and those of our subsidiaries, and should be read in conjunction with the audited consolidated financial statements and related notes included in our Information Statement and Annual Report to Stockholders for the fiscal year ended December 31, 2006 dated March 23, 2007, or 2006 Information Statement.

Certain financial information that is normally included in annual financial statements prepared in conformity with U.S. generally accepted accounting principles, or GAAP, but is not required for interim reporting purposes has been condensed or omitted. Certain amounts in prior periods' consolidated financial statements have been reclassified to conform to the current presentation. In the opinion of management, all adjustments, which include only normal recurring adjustments, have been recorded for a fair statement of our unaudited consolidated financial statements in conformity with GAAP.

Changes in Estimates and Accounting Principles

The preparation of financial statements requires the use of estimates and assumptions. See "NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES" to our consolidated financial statements in our 2006 Information Statement for a discussion of our estimates and assumptions.

Table 1.1 shows the impact of the changes in estimates in our consolidated statements of income:

Table 1.1 — Summary of Changes in Estimates

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Interest income	\$ —	\$—	\$ —	\$(93)
<i>Non-interest income</i>				
Management and guarantee income	—	—	—	18
Gains (losses) on Guarantee asset	55	—	30	40
Gains (losses) on investment activity	5	—	6	47
Total Non-interest income	<u>60</u>	<u>—</u>	<u>36</u>	<u>105</u>
<i>Non-interest expense</i>				
Provision for credit losses	(33)	—	(33)	—
Losses on certain credit guarantees	1	—	1	—
Total Non-interest expense	<u>(32)</u>	<u>—</u>	<u>(32)</u>	<u>—</u>
Total pre-tax impact of changes in estimates	<u>\$ 28</u>	<u>\$—</u>	<u>\$ 4</u>	<u>\$ 12</u>
Total after-tax impact of changes in estimates	<u>\$ 18</u>	<u>\$—</u>	<u>\$ 3</u>	<u>\$ 8</u>

Changes in estimates increased Net income for the three months ended June 30, 2007 and 2006 by approximately \$18 million and \$— million (after-tax), or \$0.03 and \$— per diluted common share, respectively. Changes in estimates increased Net income for the six months ended June 30, 2007 and 2006 by approximately \$3 million and \$8 million (after-tax), or \$0.00 and \$0.01 per diluted common share, respectively. The increases for the three and six months ended June 30, 2007 were due to enhancements to our approach for estimating prepayments impacting our Guarantee asset and

Guarantee obligation. Those enhancements were partially offset by enhancements to our approach for estimating the Reserve for losses on mortgage loans held-for-investment and the Reserve for guarantee losses on Participation Certificates, including increased rates at which loans transition from delinquency to foreclosure.

Effective January 1, 2006, we enhanced our process for forecasting interest rates and estimating prepayments used to amortize discounts, premiums and deferred fees for assets held in our Retained portfolio. This change resulted in a \$49 million (after-tax) reduction in Net income for the six months ended June 30, 2006, including the effect of the amortization of deferred credit fees. Also, effective January 1, 2006, we enhanced our approach for Guarantee asset and Guarantee obligation valuations primarily with respect to applying dealer prices in estimating the fair value of our guarantee-related assets. We also enhanced our approach for applying loan characteristics in the valuation of our Guarantee obligation. These changes resulted in a \$57 million (after-tax) increase in Net income for the six months ended June 30, 2006.

Effective January 1, 2006, we made a change to our method of amortization for certain types of non-agency securities resulting in a \$13 million (after-tax) reduction to the beginning balance of retained earnings.

Net income included after-tax adjustments of approximately \$13 million of expense and \$41 million of income, for the six months ended June 30, 2007 and 2006, respectively, to correct certain immaterial errors related to previously reported periods.

Recently Adopted Accounting Standards

Accounting for Uncertainty in Income Taxes

On January 1, 2007, we adopted Financial Accounting Standard Board, or FASB, Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109," or FIN 48. FIN 48 provides a single model to account for uncertain tax positions and clarifies accounting for income taxes by prescribing a minimum threshold that a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. As a result of the adoption of FIN 48, we recorded a \$181 million increase to retained earnings as of January 1, 2007. See "NOTE 12: INCOME TAXES" for additional information related to FIN 48.

Accounting for Certain Hybrid Instruments

On January 1, 2007, we adopted Statement of Financial Accounting Standards, or SFAS, No. 155, "Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140," or SFAS 155. SFAS 155 permits fair value measurement for any hybrid financial instrument with an embedded derivative that otherwise would require bifurcation. In addition, this statement establishes a requirement to evaluate interests in securitized financial assets to identify instruments that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation. We adopted SFAS 155 prospectively, and, therefore, there is no cumulative effect of a change in accounting principle. In connection with the adoption of SFAS 155 on January 1, 2007, we elected to measure newly acquired interests in securitized financial assets that contain embedded derivatives at fair value, with changes in fair value reflected in our consolidated statements of income. See "NOTE 4: RETAINED PORTFOLIO AND CASH AND INVESTMENTS PORTFOLIO" for additional information.

Recently Issued Accounting Standards, Not Yet Adopted

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements," or SFAS 157. This statement defines fair value, establishes a framework for measuring fair value in conformity with GAAP and expands disclosures about fair value measurements. SFAS 157 provides clarity to other accounting pronouncements that require or permit fair value measurements, but does not change existing guidance as to whether a financial asset or liability is carried at fair value. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. We do not expect our adoption of SFAS 157 to result in a material increase or decrease to our fair value measurements.

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of FASB Statement No. 115," or SFAS 159. This statement permits companies to choose to measure certain financial assets and liabilities at fair value with changes in fair value recognized in earnings as they occur. The objective is to improve financial reporting by providing entities with the opportunity to measure both assets and liabilities at fair value without having to apply complex hedge accounting provisions. SFAS 159 is effective as of the beginning of an entity's first fiscal year beginning after November 15, 2007. We have not yet determined the impact, if any, that the adoption of this standard will have on our consolidated financial statements.

Offsetting of Amounts Related to Certain Contracts

In April 2007, the FASB issued FASB Staff Position FIN 39-1, “Amendment of FASB Interpretation No. 39,” or FSP FIN 39-1. The position amends FASB Interpretation No. 39, “Offsetting of Amounts Related to Certain Contracts, an interpretation of APB Opinion No. 10 and FASB Statement No. 105,” to permit a reporting entity to offset fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral against fair value amounts recognized for derivative instruments executed with the same counterparty under a master netting agreement. When offsetting of fair value amounts recognized for derivative instruments is elected, as permitted under a master netting agreement, the position requires the offsetting of amounts recognized for cash collateral held or posted when the collateral represents “fair value amounts.” FSP FIN 39-1 is effective for financial statements issued for fiscal years beginning after November 15, 2007. We have determined that the adoption of FSP FIN 39-1 will result in the reclassification of certain amounts in our consolidated financial statements.

NOTE 2: FINANCIAL GUARANTEES AND SECURITIZED INTERESTS IN MORTGAGE-RELATED ASSETS

Financial Guarantees

We provide a variety of financial guarantees. For a discussion of these guarantees see “NOTE 2: TRANSFERS OF SECURITIZED INTERESTS IN MORTGAGE-RELATED ASSETS” and “NOTE 4: FINANCIAL GUARANTEES” to our consolidated financial statements in our 2006 Information Statement. Table 2.1 below presents our maximum potential amount of future payments, our recognized liability and the maximum remaining term of these guarantees.

Table 2.1 — Financial Guarantees

	June 30, 2007			December 31, 2006		
	Maximum Exposure	Recognized Liability	Maximum Remaining Term	Maximum Exposure	Recognized Liability	Maximum Remaining Term
	(dollars in millions, terms in years)					
Financial Guarantees:						
Guaranteed PCs and Structured Securities held by third parties ⁽¹⁾	\$1,240,813	\$8,574	40	\$1,122,761	\$7,117	40
Derivative instruments	37,241	114	28	27,917	13	28
Servicing-related premium guarantees	36	—	5	44	—	5

(1) Include long-term standby commitments and exclude mortgage loans and mortgage-related securities traded, but not yet settled. Due to timing differences in our receipt of principal and interest payments from mortgage servicers and subsequent pass-through of payments to PC investors, the unpaid principal balances of the underlying mortgage loans do not equal the unpaid principal balances of issued PCs and Structured Securities.

With the exception of interest-rate swap guarantees included in derivative instruments in Table 2.1, maximum exposure represents the contractual amounts that could be lost under the guarantees if guaranteed parties defaulted, without consideration of possible recoveries under recourse provisions or from collateral held or pledged. The maximum exposure related to interest-rate swap guarantees is based on contractual rates and without consideration of recovery under recourse provisions. Maximum exposure disclosed above is not representative of the actual loss we are likely to incur, based on our historical loss experience.

Guaranteed PCs and Structured Securities

We guarantee the payment of principal and interest on issued PCs and Structured Securities that are secured by pools of mortgage loans. At June 30, 2007 and December 31, 2006, we guaranteed \$1,592.5 billion and \$1,477.0 billion of PCs and Structured Securities, respectively, of which \$351.7 billion and \$354.3 billion were held in our Retained portfolio at June 30, 2007 and December 31, 2006, respectively. There were \$1,379.4 billion and \$1,240.2 billion at June 30, 2007 and December 31, 2006, respectively, of Structured Securities backed by resecuritized PCs and other previously issued Structured Securities. These restructured securities do not increase our credit-related exposure and consist of single-class and multi-class Structured Securities backed by PCs, Real Estate Mortgage Investment Conduits and principal-only strips.

The recognized liability associated with our guarantee of PCs and Structured Securities held by third parties represents our Guarantee obligation. At June 30, 2007 and December 31, 2006 our Guarantee obligation includes our estimate of performance and other related costs of \$6.0 billion and \$4.9 billion, respectively, and deferred guarantee income of \$2.6 billion and \$2.2 billion, respectively. In addition to our Guarantee obligation, we recognized a Reserve for guarantee losses on Participation Certificates that totaled \$682 million and \$350 million at June 30, 2007 and December 31, 2006, respectively.

At June 30, 2007 and December 31, 2006, approximately 95 percent and 94 percent, respectively, of issued PCs and Structured Securities (excluding securities we issued that are backed by Ginnie Mae Certificates) had a corresponding Guarantee asset, Guarantee obligation or PC residual recognized on our consolidated balance sheets. With respect to

outstanding guarantees held by third parties at June 30, 2007 and December 31, 2006, 96 percent and 95 percent, respectively, had a related Guarantee asset and Guarantee obligation established.

Derivative Instruments

Derivative instruments include written options, written swaptions, interest-rate swap guarantees and guarantees of stated final maturity of Structured Securities. Derivative instruments also include short-term default guarantee commitments that we account for as credit derivatives.

Servicing-Related Premium Guarantees

We provide guarantees to reimburse servicers for premiums paid to acquire servicing in situations where the original seller is unable to perform under its separate servicing agreement. The liability associated with these agreements was not material.

Other Financial Commitments

As part of the guarantee arrangements pertaining to multifamily housing revenue bonds, we provided commitments to advance funds, commonly referred to as “liquidity guarantees,” totaling \$5.2 billion and \$5.8 billion at June 30, 2007 and December 31, 2006, respectively. These guarantees enable others to repurchase the tendered tax-exempt and related taxable pass-through certificates and housing revenue bonds that are unable to be remarketed. Any repurchased securities could be pledged to us to secure funding until the time when the securities could be remarketed. We have not made any payments to date under these liquidity guarantees.

Valuation of Recognized Guarantee Asset

Recognized Guarantee Asset

Our approach for estimating the fair value of the Guarantee asset utilizes third-party market data as practicable. For approximately 75 percent of the fair value of the Guarantee asset at June 30, 2007, the valuation approach involved obtaining dealer quotes on proxy securities with collateral similar to aggregated characteristics of our portfolio. Effectively, the Guarantee asset approximates the current, or “spot,” market values for excess servicing, interest-only securities, which trade at a discount to trust interest-only security prices. The remaining 25 percent of the Guarantee asset, which relates to underlying loan products without readily available market prices, is valued using an expected cash flow approach with market input assumptions extracted from the dealer quotes provided on the more liquid products, reduced by an estimated liquidity discount.

Key Assumptions Used in the Valuation of the Guarantee Asset

Table 2.2 summarizes the key assumptions associated with the fair value measurements of the recognized Guarantee asset. The fair values at the time of securitization and the subsequent fair value measurements were estimated using third party information. However, the assumptions included in this table for those periods are those implied by our fair value estimates, with the internal rates of return, or IRRs, adjusted where necessary to align our internal models with estimated fair values determined using third party information. Prepayment rates are presented as implied by our internal models and have not been similarly adjusted.

At June 30, 2007, our Guarantee asset totaled \$7,777 million on our consolidated balance sheets, of which approximately \$160 million, or approximately 2 percent, related to PCs and Structured Securities backed by multifamily mortgage loans. The key assumptions utilized in fair value measurements of the Guarantee asset presented in Table 2.2 and the sensitivity analysis presented in Table 2.3 relate solely to the Guarantee asset associated with PCs and Structured Securities backed by single-family mortgage loans.

Table 2.2 — Key Assumptions Utilized in Fair Value Measurements of the Guarantee Asset

Valuation Assumptions	Three Months Ended June 30,				Six Months Ended June 30,			
	2007		2006		2007		2006	
	Range ⁽¹⁾	Mean ⁽²⁾	Range ⁽¹⁾	Mean ⁽²⁾	Range ⁽¹⁾	Mean ⁽²⁾	Range ⁽¹⁾	Mean ⁽²⁾
IRRs ⁽³⁾	1.0% – 12.6%	6.3%	5.7% – 13.4%	8.8%	1.0% – 12.6%	6.6%	5.5% – 13.5%	8.9%
Prepayment rates ⁽⁴⁾	7.9% – 64.6%	17.1%	7.4% – 51.0%	14.0%	7.9% – 64.6%	17.5%	7.4% – 51.0%	14.5%
Weighted average lives (years)	1.5 – 8.6	5.3	1.8 – 9.0	6.0	1.5 – 8.6	5.2	1.8 – 9.0	5.8

- (1) Lower and higher ranges of IRR and Prepayment rate assumptions represent the first and ninety-ninth percentile of rate assumptions, respectively, throughout the three and six months ended June 30, 2007 and 2006. Weighted average lives range assumptions reflect Prepayment rate assumptions.
- (2) Mean values represent the weighted average of all IRR, Prepayment rate and Weighted average lives assumptions throughout the three and six months ended June 30, 2007 and 2006.
- (3) IRR range and mean assumptions represent an unpaid principal balance weighted average of the discount rates inherent in the fair value of the recognized Guarantee asset. Mean Weighted average lives assumptions reflect Prepayment rate assumptions.
- (4) Although Prepayment rates are simulated monthly, the range and mean rate assumptions above represent annualized Prepayment rates based on unpaid principal balances.

Table 2.3 — Sensitivity Analysis of the Guarantee Asset (Single-Family Mortgages)

	June 30, 2007	December 31, 2006
	(dollars in millions)	
Fair value ⁽¹⁾	\$7,617	\$5,905
Weighted average IRR assumptions:	7.6%	7.0%
Impact on fair value of 100 bps unfavorable change	\$ (308)	\$ (224)
Impact on fair value of 200 bps unfavorable change	\$ (592)	\$ (431)
Weighted average prepayment rate assumptions:	14.5%	18.4%
Impact on fair value of 10% unfavorable change	\$ (339)	\$ (298)
Impact on fair value of 20% unfavorable change	\$ (646)	\$ (565)

(1) At June 30, 2007 and December 31, 2006, our Guarantee asset totaled \$7,777 million and \$6,070 million, respectively, on our consolidated balance sheets. Of those amounts, approximately \$160 million and \$165 million, or approximately two percent and three percent, related to PCs backed by multifamily mortgage loans at June 30, 2007 and December 31, 2006, respectively. The sensitivity analysis relates solely to the Guarantee asset associated with the PCs backed by single-family mortgage loans.

Valuation of Other Retained Interests

Other retained interests include securities that were issued by us as part of a securitization transaction, which was recorded as a sale. The majority of these securities are classified as available-for-sale. The fair value of other retained interests is generally based on independent price quotations obtained from third-party pricing services or dealer marks.

To report the hypothetical sensitivity of the carrying value of other retained interests, we used internal models adjusted where necessary to align with the fair values. The sensitivity analysis in Table 2.4 illustrates hypothetical adverse changes in the fair value of other retained interests for changes in key assumptions based on these models.

Table 2.4 — Sensitivity Analysis of Other Retained Interests⁽¹⁾

	June 30, 2007	December 31, 2006
	(dollars in millions)	
Fair value	\$116,692	\$127,490
Weighted average IRR assumptions:	5.8%	5.6%
Impact on fair value of 100 bps unfavorable change	\$ (4,599)	\$ (4,551)
Impact on fair value of 200 bps unfavorable change	\$ (8,884)	\$ (8,813)
Weighted average prepayment rate assumptions:	9.6%	11.0%
Impact on fair value of 10% unfavorable change	\$ (40)	\$ (66)
Impact on fair value of 20% unfavorable change	\$ (97)	\$ (132)

(1) The sensitivity analysis includes only other retained interests whose fair value is impacted as a result of changes in IRR and prepayment assumptions. At June 30, 2007 and December 31, 2006, the fair values of other retained interests not included in the sensitivity analysis above were \$44 million and \$51 million, respectively.

Gains and Losses on Transfers of PCs and Structured Securities that are Accounted for as Sales

We recognized gains (losses) on transfers of PCs and Structured Securities that were accounted for as sales under SFAS 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities — a replacement of FASB Statement No. 125." For the three months ended June 30, 2007 and 2006, these net pre-tax gains (losses) were approximately \$(165) million and \$(95) million, respectively. For the six months ended June 30, 2007 and 2006, these net pre-tax gains (losses) were approximately \$(96) million and \$(56) million, respectively.

Cash Flows on Transfers of Securitized Interests and Corresponding Retained Interests

Table 2.5 below summarizes cash flows on retained interests.

Table 2.5 — Details of Cash Flows

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2007	2006	2007	2006
	(in millions)			
Cash flows from:				
Transfers of Freddie Mac securities that were accounted for as sales	\$21,267	\$21,699	\$34,464	\$34,900
Payments received on the Guarantee asset ⁽¹⁾	448	359	867	710
Other retained interests principal and interest	6,059	5,911	12,058	11,537

(1) Represent contractual guarantee-related cash flows received by us in connection with the recognized Guarantee asset.

Credit Protection and Other Forms of Recourse

In connection with our outstanding guarantees of PCs and Structured Securities held by third parties, we have recourse in the form of primary mortgage insurance, pool insurance, recourse to lenders, credit enhancements and other forms of credit protection. As of June 30, 2007 and December 31, 2006, we had recorded \$549 million and \$466 million, respectively, within Other assets on our consolidated balance sheets related to these credit enhancements on securitized mortgages. Table 2.6 presents the amounts of potential loss recovery by type of credit protection.

Table 2.6 — Credit Protection and Other Forms of Recourse⁽¹⁾

	June 30, 2007	December 31, 2006
	(in millions)	
PCs and Structured Securities:		
Single-family:		
Primary mortgage insurance	\$33,812	\$30,720
Pool insurance and other credit enhancements	3,125	3,178
Recourse to lenders	9,447	8,875
Multifamily:		
Credit enhancements	826	1,104
Structured Securities backed by Ginnie Mae Certificates ⁽²⁾	1,370	1,481

(1) Exclude credit enhancements related to outstanding Structured Transactions, which had unpaid principal balances that totaled \$7.3 billion and \$7.8 billion at June 30, 2007 and December 31, 2006, respectively.

(2) Ginnie Mae Certificates are backed by the full faith and credit of the U.S. government.

Indemnifications

In connection with certain business transactions, we may provide indemnification to counterparties for claims arising out of breaches of certain obligations (*e.g.*, those arising from representations and warranties) in contracts entered into in the normal course of business. For a discussion of these indemnifications see “NOTE 4: FINANCIAL GUARANTEES” to our consolidated financial statements in our 2006 Information Statement. Our assessment is that the risk of any material loss from such a claim for indemnification is remote and there are no probable and estimable losses associated with these contracts. Therefore, we have not recorded any liabilities related to these indemnifications on our consolidated balance sheets at June 30, 2007 and December 31, 2006.

NOTE 3: VARIABLE INTEREST ENTITIES

We are a party to numerous entities that are considered to be variable interest entities, or VIEs. Our investments in VIEs include low-income housing tax credit, or LIHTC, partnerships, certain Structured Securities transactions and a mortgage reinsurance entity. In addition, we buy the highly-rated senior securities in certain securitization trusts that are VIEs. Our investments in these securities do not represent a significant variable interest in the securitization trusts as the securities issued by these trusts are not designed to absorb a significant portion of the variability in the trust. Accordingly, we do not consolidate these securities.

Low-Income Housing Tax Credit Partnerships

We invest as a limited partner in LIHTC partnerships formed for the purpose of providing funding for affordable multifamily rental properties. Most of these LIHTC partnerships are VIEs. A general partner operates the partnership, identifying investments and obtaining debt financing as needed to finance partnership activities. Although these partnerships generate operating losses, we realize a return on our investment through reductions in income tax expense that result from tax credits and the deductibility of the operating losses of these partnerships. The partnership agreements are typically structured to meet a required 15-year period of occupancy by qualified low-income tenants. These investments were made between 1989 and 2007. At June 30, 2007 and December 31, 2006, we did not guarantee any obligations of these partnerships and our exposure was limited to the amount of our investments. At June 30, 2007 and December 31, 2006, we were the primary beneficiary of investments in six LIHTC partnerships and we consolidated these investments. The investors in the obligations of the consolidated LIHTC partnerships have recourse only to the assets of those VIEs and do not have recourse to us.

VIEs Not Consolidated

Low-Income Housing Tax Credit Partnerships

At June 30, 2007 and December 31, 2006, we had unconsolidated investments in 181 and 179 LIHTC partnerships, respectively, in which we had a significant variable interest. The size of these partnerships at June 30, 2007 and December 31, 2006, as measured in total assets, was \$9.9 billion and \$8.9 billion, respectively. These partnerships are accounted for using the equity method. As a limited partner, our maximum exposure to loss equals the undiscounted book value of our equity investment. At both June 30, 2007 and December 31, 2006, our maximum exposure to loss on unconsolidated LIHTC partnerships, in which we had a significant variable interest, was \$3.7 billion.

Structured Transactions

We periodically issue securities in Structured Transactions, which are backed by mortgage loans or mortgage-related securities using collateral pools transferred to trusts specifically created for the purpose of issuing securities. These trusts issue various senior interests, subordinated interests or both. We purchase interests, including senior interests, of the trusts and simultaneously issue and guarantee Structured Securities backed by these interests. The subordinated interests are generally either held by the seller or other party or sold in the capital markets. Generally, the structure of the transactions and the trusts as qualifying special purpose entities exempts them from the scope of FASB Interpretation

No. 46 (revised December 2003), “Consolidation of Variable Interest Entities, an interpretation of ARB No. 51,” or FIN 46(R). However, at both June 30, 2007 and December 31, 2006, we had investments or guarantees related to two Structured Transactions that did not fall within this scope exception and in which we had a significant variable interest. At June 30, 2007 and December 31, 2006, we were not the primary beneficiary of any such transactions.

Our involvement in these two Structured Transactions began in 1996 and 2002, respectively. The size of these two transactions at June 30, 2007 and December 31, 2006, as measured in total assets, was \$58 million and \$67 million, respectively. At June 30, 2007 and December 31, 2006, our maximum exposure to loss on these transactions, in which we had a significant variable interest, was \$47 million and \$55 million, respectively, consisting of the book value of our investments plus incremental guarantees of the senior interests that are held by third parties.

NOTE 4: RETAINED PORTFOLIO AND CASH AND INVESTMENTS PORTFOLIO

Table 4.1 summarizes amortized cost, estimated fair values and corresponding gross unrealized gains and gross unrealized losses for available-for-sale securities by major security type.

Table 4.1 — Available-For-Sale Securities

<u>June 30, 2007</u>	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
	(in millions)			
<i>Retained portfolio</i>				
Mortgage-related securities issued by:				
Freddie Mac	\$341,388	\$1,127	\$ (7,206)	\$335,309
Federal National Mortgage Association, or Fannie Mae	42,894	213	(835)	42,272
Ginnie Mae	617	14	(9)	622
Other	232,264	298	(2,375)	230,187
Obligations of states and political subdivisions	14,063	145	(234)	13,974
Total mortgage-related securities	<u>631,226</u>	<u>1,797</u>	<u>(10,659)</u>	<u>622,364</u>
<i>Cash and investments portfolio</i>				
Non-mortgage-related securities:				
Asset-backed securities	32,435	12	(57)	32,390
Commercial paper	8,245	—	—	8,245
Obligations of states and political subdivisions	1,111	—	—	1,111
Total non-mortgage-related securities	<u>41,791</u>	<u>12</u>	<u>(57)</u>	<u>41,746</u>
Total available-for-sale securities	<u>\$673,017</u>	<u>\$1,809</u>	<u>\$ (10,716)</u>	<u>\$664,110</u>
<u>December 31, 2006</u>				
<i>Retained portfolio</i>				
Mortgage-related securities issued by:				
Freddie Mac	\$347,700	\$1,753	\$ (5,365)	\$344,088
Fannie Mae	44,223	323	(660)	43,886
Ginnie Mae	720	17	(4)	733
Other	224,642	553	(1,096)	224,099
Obligations of states and political subdivisions	13,622	334	(31)	13,925
Total mortgage-related securities	<u>630,907</u>	<u>2,980</u>	<u>(7,156)</u>	<u>626,731</u>
<i>Cash and investments portfolio</i>				
Non-mortgage-related securities:				
Asset-backed securities	32,179	23	(80)	32,122
Commercial paper	11,191	—	—	11,191
Obligations of states and political subdivisions	2,273	—	—	2,273
Total non-mortgage-related securities	<u>45,643</u>	<u>23</u>	<u>(80)</u>	<u>45,586</u>
Total available-for-sale securities	<u>\$676,550</u>	<u>\$3,003</u>	<u>\$ (7,236)</u>	<u>\$672,317</u>

We have the ability and intent to hold available-for-sale securities that may be currently in an unrealized loss position for a period of time sufficient to recover all unrealized losses. Based on our ability and intent to hold these available-for-sale securities, we have concluded that the impairment of these securities is temporary.

Table 4.2 below illustrates the gross realized gains and gross realized losses from the sale of available-for-sale securities.

Table 4.2 — Gross Realized Gains and Gross Realized Losses on Available-For-Sale Securities

	<u>Three Months Ended June 30,</u>		<u>Six Months Ended June 30,</u>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
	(in millions)			
Gross realized gains	\$ 87	\$ 77	\$ 147	\$ 269
Gross realized (losses)	(288)	(257)	(297)	(303)
Net realized gains (losses)	<u>\$(201)</u>	<u>\$(180)</u>	<u>\$(150)</u>	<u>\$(34)</u>

For the three months ended June 30, 2007 and 2006, we recorded impairments related to investments in securities of \$325 million and \$218 million, respectively. For the six months ended June 30, 2007 and 2006, we recorded impairments related to investments in securities of \$428 million and \$351 million, respectively.

Table 4.3 presents the changes in AOCI, net of taxes, related to available-for-sale securities. The Net unrealized holding losses, net of tax, represents the net fair value adjustments recorded on available-for-sale securities throughout the period, after the effects of our statutory tax rate of 35 percent. The Net reclassification adjustment for net realized losses, net of tax, represents the amount of those fair value adjustments, after the effects of our statutory tax rate of 35 percent, that have been recognized in earnings due to the sale of an available-for-sale security or the recognition of an impairment loss.

Table 4.3 — AOCI, Net of Taxes, Related to Available-For-Sale Securities

	Six Months Ended June 30,	
	2007	2006
(in millions)		
Beginning balance	\$(2,749)	\$(2,485)
Net unrealized holding losses, net of tax ⁽¹⁾	(3,491)	(6,541)
Net reclassification adjustment for realized losses, net of tax ⁽²⁾⁽³⁾	371	241
Ending balance	<u>\$(5,869)</u>	<u>\$(8,785)</u>

- (1) Net of tax benefit of \$1,880 million and \$3,522 million for the six months ended June 30, 2007 and 2006, respectively. Include the fair value adjustments of available-for-sale Participation Certificate residuals, net of tax.
- (2) Net of tax benefit of \$200 million and \$130 million for the six months ended June 30, 2007 and 2006, respectively.
- (3) Includes the reversal of previously recorded unrealized losses that have been recognized as impairment losses on available-for-sale securities of \$274 million and \$224 million, net of tax, for the six months ended June 30, 2007 and 2006, respectively.

Table 4.4 summarizes the estimated fair values by major security type for trading securities in our Retained portfolio.

Table 4.4 — Trading Securities in the Retained Portfolio

	June 30, 2007	December 31, 2006
	(in millions)	
Mortgage-related securities issued by:		
Freddie Mac	\$10,401	\$6,573
Fannie Mae	1,476	802
Ginnie Mae	198	222
Total trading securities in the Retained portfolio	<u>\$12,075</u>	<u>\$7,597</u>

For the three months ended June 30, 2007 and 2006, we recorded net unrealized gains (losses) on trading securities held at June 30, 2007 and 2006 of \$26 million and \$(29) million, respectively. For the six months ended June 30, 2007 and 2006, we recorded net unrealized gains (losses) on trading securities held at June 30, 2007 and 2006 of \$55 million and \$(81) million, respectively.

Total trading securities in the Retained portfolio include \$2.2 billion of SFAS 155 related assets. Gains (losses) on trading securities include losses of \$95 million related to these SFAS 155 trading securities for both the three and the six months ended June 30, 2007.

Retained Portfolio Voluntary Growth Limit

Effective July 1, 2006, we voluntarily limited the growth of our Retained portfolio to no more than 2.0 percent annually on a cumulative basis (and 0.5 percent quarterly) based on its carrying value as reported in our minimum capital report to the Office of Federal Housing Enterprise Oversight, or OFHEO, filed on July 28, 2006, which was \$710.3 billion. This voluntary, temporary growth limit was put in place in response to a request from OFHEO. At June 30, 2007, the carrying value of the Retained portfolio as reported on our consolidated balance sheets was approximately \$703.3 billion, below the voluntary limit of approximately \$724.5 billion at that time.

Collateral Pledged

Collateral Pledged to Freddie Mac

Our counterparties are required to pledge collateral for reverse repurchase transactions and most interest-rate swap transactions subject to collateral posting thresholds generally related to a counterparty's credit rating. Although it is our practice not to repledge assets held as collateral, a portion of the collateral may be repledged based on master agreements related to our interest-rate swap transactions. At June 30, 2007 and December 31, 2006, we did not have collateral in the form of securities pledged to and held by us under interest-rate swap agreements.

Collateral Pledged by Freddie Mac

We are also required to pledge collateral for margin requirements with third-party custodians in connection with secured financings, interest-rate swap agreements, futures and daily trade activities with some counterparties. The level of collateral pledged related to our interest-rate swap agreements is determined after giving consideration to our credit rating. In 2006, we opened three uncommitted intraday lines of credit with third-parties, two of which are secured, in connection with the Federal Reserve Board's revised payments system risk policy, which restricts or eliminates daylight overdrafts by GSEs, including us, in connection with our use of the Fedwire system. In certain limited circumstances, the line of credit agreements give the secured parties the right to repledge the securities underlying our financing to other third parties, including the Federal Reserve Bank. We pledge collateral to meet these requirements upon a demand by the respective counterparty.

Table 4.5 summarizes all securities pledged as collateral by us, including assets that the secured party may repledge and those that may not be repledged.

Table 4.5 — Collateral in the Form of Securities Pledged

	<u>June 30, 2007</u>	<u>December 31, 2006</u>
	(in millions)	
Securities pledged with ability for secured party to repledge (parenthetically disclosed on our consolidated balance sheets):		
Available-for-sale	\$17,777	\$20,463
Securities pledged without ability for secured party to repledge:		
Available-for-sale	804	225
Total securities pledged	<u>\$18,581</u>	<u>\$20,688</u>

NOTE 5: LOAN LOSS RESERVES

We maintain separate loan loss reserves for mortgage loans in our Retained portfolio that we classify as held-for-investment and for credit-related losses associated with certain mortgage loans that underlie Guaranteed PCs and Structured Securities held by third parties.

Table 5.1 summarizes loan loss reserve activity during the periods presented.

Table 5.1 — Detail of Loan Loss Reserves Balance

	Three Months Ended June 30,					
	2007			2006		
	Reserves related to:		Total Loan Loss Reserves	Reserves related to:		Total Loan Loss Reserves
	Retained Mortgages	PCs Outstanding		Retained Mortgages	PCs Outstanding	
	(in millions)					
Beginning balance	\$ 92	\$453	\$545	\$119	\$226	\$345
Provision for credit losses	52	268	320	30	26	56
Charge-offs ⁽¹⁾⁽²⁾	(87)	—	(87)	(80)	—	(80)
Recoveries ⁽¹⁾	51	—	51	40	—	40
Transfers-out ⁽³⁾	—	(53)	(53)	—	(10)	(10)
Other transfers ⁽⁴⁾	—	14	14	—	—	—
Ending balance	<u>\$108</u>	<u>\$682</u>	<u>\$790</u>	<u>\$109</u>	<u>\$242</u>	<u>\$351</u>
	Six Months Ended June 30,					
	2007			2006		
	Reserves related to:		Total Loan Loss Reserves	Reserves related to:		Total Loan Loss Reserves
	Retained Mortgages	PCs Outstanding		Retained Mortgages	PCs Outstanding	
	(in millions)					
Beginning balance	\$ 70	\$350	\$ 420	\$ 119	\$295	\$ 414
Provision for credit losses	107	392	499	60	(40)	20
Charge-offs ⁽¹⁾⁽²⁾	(169)	—	(169)	(152)	—	(152)
Recoveries ⁽¹⁾	100	—	100	82	—	82
Transfers-out ⁽³⁾	—	(76)	(76)	—	(16)	(16)
Other transfers ⁽⁴⁾	—	16	16	—	3	3
Ending balance	<u>\$ 108</u>	<u>\$682</u>	<u>\$ 790</u>	<u>\$ 109</u>	<u>\$242</u>	<u>\$ 351</u>

- (1) It is our practice to purchase mortgage loans from the pools that underlie PCs principally at the point a mortgage loan is identified as being 120 days past due. Because credit losses related to off-balance sheet PCs are preceded by the purchase of a delinquent mortgage loan from the PC pool, charge-offs or recoveries are presented in the Retained Mortgages columns above.
- (2) Represent the amount of the unpaid principal balance of a loan that has been discharged using the reserve balance to remove the loan from our Retained portfolio at the time of resolution. Exclude \$27 million for the three months ended June 30, 2007 and \$38 million for the six months ended June 30, 2007 related to reserve amounts previously transferred to reduce the carrying value of loans purchased under financial guarantees.
- (3) Consist of the transfer of reserves, including amounts attributable to uncollectible interest, associated with non-performing loans purchased from mortgage pools underlying PCs, Structured Securities and long-term standby agreements to establish the initial recorded investment in these loans at the date of our purchase.
- (4) Represent transfers of a portion of the initial Guarantee obligation associated with credit losses reclassified to the reserve balance allocated to PCs outstanding.

Impaired Loans

Single-family impaired loans include performing and non-performing troubled debt restructurings, as well as delinquent loans that were purchased from mortgage collateral pools underlying PCs and Structured Securities and long-term standby agreements. Multifamily impaired loans are defined as troubled debt restructuring loans, non-credit-enhanced loans greater than 60 days delinquent and certain mortgage loans identified as individually impaired. Recorded investment on impaired loans includes the unpaid principal balance plus amortized basis adjustments, which are modifications to the loan's carrying value.

Total loan loss reserves, as presented in "Table 5.1 — Detail of Loan Loss Reserves Balance," consist of a specific valuation allowance related to impaired loans, which is presented in Table 5.2, and a reserve for other probable incurred losses.

Our recorded investment in impaired loans and the related valuation allowance are summarized in Table 5.2.

Table 5.2 — Impaired Loans

	June 30, 2007			December 31, 2006		
	Recorded Investment	Specific Reserve	Net Investment	Recorded Investment	Specific Reserve	Net Investment
	(in millions)					
Impaired loans having:						
Related valuation allowance	\$ 403	\$(17)	\$ 386	\$ 86	\$(6)	\$ 80
No related valuation allowance ⁽¹⁾	7,083	—	7,083	5,869	—	5,869
Total	<u>\$7,486</u>	<u>\$(17)</u>	<u>\$7,469</u>	<u>\$5,955</u>	<u>\$(6)</u>	<u>\$5,949</u>

- (1) Impaired loans with no related valuation allowance primarily represent performing single-family troubled debt restructuring loans and those delinquent loans purchased out of PC pools that have not been impaired subsequent to acquisition.

The average investment in impaired loans was \$6,753 million and \$4,215 million for the six months ended June 30, 2007 and for the year ended December 31, 2006, respectively. The increase in impaired loans for the six months ended

June 30, 2007 is attributed to higher serious delinquency rates for loans originated in 2006 and 2007, which have been principally purchased out of PCs and Structured Securities.

Interest income and management and guarantee income foregone on impaired loans approximated \$56 million and \$11 million for the six months ended June 30, 2007 and 2006, respectively.

Loans Acquired in a Transfer

We have the option to purchase mortgage loans from the loan pools that underlie our guarantees and standby commitments under certain circumstances, such as to resolve an existing or impending delinquency or default. Our general practice is to purchase the mortgage loans after the loans are 120 days delinquent. Loans purchased that underlie our guarantees and standby commitments held by third parties are recorded at fair value. We record Losses on loans purchased on our consolidated statements of income in order to reduce our net investment in the acquired loan to its fair value. Loans purchased out of PCs held by us are recorded at their carrying amount, which approximates fair value because the related PC residual is generally accounted for at fair value with changes in market valuations recorded in our consolidated statements of income. At June 30, 2007 and December 31, 2006, the outstanding balance of these loans was \$4.8 billion and \$3.0 billion, respectively, while the carrying amount of these loans was \$4.2 billion and \$2.8 billion, respectively.

The following table provides details on loans acquired under financial guarantees.

Table 5.3 — Loans Acquired Under Financial Guarantees

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Contractual principal and interest payments at acquisition	\$2,060	\$1,102	\$4,127	\$2,512
Non-accretable difference	(82)	(36)	(142)	(82)
Cash flows expected to be collected at acquisition	1,978	1,066	3,985	2,430
Accretable balance	(444)	(138)	(838)	(307)
Initial investment in acquired loans at acquisition	<u>\$1,534</u>	<u>\$ 928</u>	<u>\$3,147</u>	<u>\$2,123</u>

The excess of contractual principal and interest over the undiscounted amount of cash flows we expect to collect represents a non-accretable difference that is not accreted to interest income nor displayed in the consolidated balance sheets. The amount that may be accreted into interest income on such loans is limited to the excess of our estimate of undiscounted expected principal, interest and other cash flows from the loan over our initial investment in the loan. We consider estimated prepayments when calculating the accretable balance and the non-accretable difference. While these loans are seriously delinquent, no amounts are accreted to interest income. Subsequent changes in estimated future cash flows to be collected related to interest-rate changes are recognized prospectively in interest income over the remaining contractual life of the loan. Decreases in estimated future cash flows to be collected due to further credit deterioration are recognized as Provision for credit losses and increase our loan loss reserve. Subsequent to the acquisition of these loans, we recognized an increase in Provision for credit losses of \$7 million and \$13 million for the three and six months ended June 30, 2007, respectively.

The following table provides changes in the accretable balance of these loans.

Table 5.4 — Changes in Accretable Balance

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(in millions)			
Beginning balance	\$ 883	\$183	\$ 593	\$ —
Additions from new acquisitions	444	138	838	307
Accretion during the period	(70)	(8)	(70)	(11)
Reductions ⁽¹⁾	(64)	(11)	(99)	(15)
Change in estimated cash flows ⁽²⁾	(6)	(5)	(58)	5
Reclassifications to or from nonaccretable difference	(25)	5	(42)	16
Ending balance	<u>\$1,162</u>	<u>\$302</u>	<u>\$1,162</u>	<u>\$302</u>

(1) Represent the recapture of losses previously recognized due to borrower repayment or foreclosure on the loan.

(2) Represents the change in expected cash flows due to troubled debt restructurings or change in prepayment assumptions of the related loans.

Delinquency Rates

Table 5.5 summarizes the delinquency performance for our Total mortgage portfolio, excluding non-Freddie Mac mortgage-related securities and that portion of Structured Securities backed by Ginnie Mae Certificates.

Table 5.5 — Delinquency Performance

	<u>June 30, 2007</u>	<u>December 31, 2006</u>
Delinquencies, end of period:		
<i>Single-family</i> : ⁽¹⁾		
Non-credit-enhanced portfolio — excluding Structured Transactions:		
Delinquency rate	0.26%	0.25%
Total number of delinquent loans	25,310	22,677
Credit-enhanced portfolio — excluding Structured Transactions:		
Delinquency rate	1.17%	1.30%
Total number of delinquent loans	22,603	24,106
Total portfolio — excluding Structured Transactions:		
Delinquency rate	0.42%	0.42%
Total number of delinquent loans	47,913	46,783
Structured Transactions ⁽²⁾ :		
Delinquency rate	8.71%	8.33%
Total number of delinquent loans	10,502	12,079
Total portfolio:		
Delinquency rate	0.50%	0.53%
Total number of delinquent loans	58,415	58,862
<i>Multifamily</i> : ⁽³⁾		
Total portfolio:		
Delinquency rate	0.05%	0.05%
Net carrying value of delinquent loans (in millions)	\$ 30	\$ 30

(1) Based on the number of mortgages 90 days or more delinquent or in foreclosure.

(2) Structured Transactions generally have underlying mortgage loans with higher risk characteristics but may provide inherent credit protections from losses due to underlying subordination, excess interest, overcollateralization and other features.

(3) Based on net carrying value of mortgages 60 days or more delinquent.

NOTE 6: REAL ESTATE OWNED

For periods presented below, the weighted average holding period for our disposed properties was less than one year. Table 6.1 provides a summary of our REO activity.

Table 6.1 — REO

	<u>Three Months Ended June 30,</u>					
	<u>2007</u>			<u>2006</u>		
	<u>REO, Gross</u>	<u>Valuation Allowance</u>	<u>REO, Net</u>	<u>REO, Gross</u>	<u>Valuation Allowance</u>	<u>REO, Net</u>
	(in millions)					
Beginning balance	\$ 1,021	\$(143)	\$ 878	\$ 774	\$(120)	\$ 654
Additions	575	(35)	540	363	(20)	343
Dispositions and write-downs	(416)	18	(398)	(354)	21	(333)
Ending balance	<u>\$1,180</u>	<u>\$(160)</u>	<u>\$1,020</u>	<u>\$ 783</u>	<u>\$(119)</u>	<u>\$ 664</u>
	<u>Six Months Ended June 30,</u>					
	<u>2007</u>			<u>2006</u>		
	<u>REO, Gross</u>	<u>Valuation Allowance</u>	<u>REO, Net</u>	<u>REO, Gross</u>	<u>Valuation Allowance</u>	<u>REO, Net</u>
	(in millions)					
Beginning balance	\$ 871	\$(128)	\$ 743	\$ 744	\$(115)	\$ 629
Additions	1,066	(64)	1,002	717	(40)	677
Dispositions and write-downs	(757)	32	(725)	(678)	36	(642)
Ending balance	<u>\$1,180</u>	<u>\$(160)</u>	<u>\$1,020</u>	<u>\$ 783</u>	<u>\$(119)</u>	<u>\$ 664</u>

We realized losses of \$18 million and \$11 million for the three months ended June 30, 2007 and 2006, respectively, and \$33 million and \$25 million for the six months ended June 30, 2007 and 2006, respectively, on REO dispositions, which are included in REO operations expense. The volume of properties that was added to our REO inventory increased by 20 percent during the three months ended June 30, 2007, compared to the three months ended June 30, 2006, consistent with the growth of our outstanding guaranteed PCs and Structured Securities. Our REO additions have continued to be greatest in the North Central region of the U.S. and more than one-half of our REO balance relates to properties located in this region.

NOTE 7: DEBT SECURITIES AND SUBORDINATED BORROWINGS

Debt securities are classified as either due within one year or due after one year based on their remaining contractual maturity. Table 7.1 summarizes the balances and effective interest rates for debt securities and subordinated borrowings.

Table 7.1 — Total Debt Securities, Net

	June 30, 2007			December 31, 2006		
	Par Value	Balance, Net ⁽¹⁾	Effective Rate ⁽²⁾	Par Value	Balance, Net ⁽¹⁾	Effective Rate ⁽²⁾
	(dollars in millions)					
Senior debt, due within one year:						
Reference Bills® securities and discount notes	\$161,537	\$159,083	5.14%	\$159,503	\$157,553	5.14%
Medium-term Notes	4,077	4,077	5.29	9,832	9,832	5.16
Swap collateral obligations	9,016	9,055	5.31	9,552	9,597	5.17
Short-term debt securities	174,630	172,215	5.15	178,887	176,982	5.14
Current portion of long-term debt	104,074	104,759	4.29	117,972	117,879	4.10
Senior debt, due within one year	<u>278,704</u>	<u>276,974</u>	4.83	<u>296,859</u>	<u>294,861</u>	4.73
Senior debt, due after one year ⁽³⁾	514,705	478,295	5.23	484,397	452,677	5.08
Subordinated debt, due after one year ⁽³⁾	5,532	5,227	5.76	6,714	6,400	5.86
Senior and subordinated debt, due after one year	<u>520,237</u>	<u>483,522</u>	5.24	<u>491,111</u>	<u>459,077</u>	5.09
Total debt securities, net	<u>\$798,941</u>	<u>\$760,496</u>		<u>\$787,970</u>	<u>\$753,938</u>	

- (1) Represents par value, net of associated discounts, premiums and foreign currency-related and hedging-related basis adjustments. Swap collateral obligations include the related accrued interest payable.
- (2) Represents the approximate weighted average effective rate for each instrument outstanding at the end of the period, which includes the amortization of discounts or premiums and issuance costs, but excludes the amortization of hedging-related basis adjustments.
- (3) Balance, Net for Senior debt, due after one year includes callable debt of \$232,981 million and \$220,758 million at June 30, 2007 and December 31, 2006, respectively. Balance, Net for Subordinated debt, due after one year includes callable debt of \$747 million and \$1,928 million at June 30, 2007 and December 31, 2006, respectively.

NOTE 8: STOCKHOLDERS' EQUITY

Stock Repurchase and Issuance Programs

During the six months ended June 30, 2007, we completed two non-cumulative, perpetual preferred stock offerings with aggregate proceeds of \$1.6 billion. We issued \$500 million of 5.66 percent non-cumulative, perpetual preferred stock and repurchased \$750 million (approximately 11.9 million shares) of outstanding common stock in connection with our plan announced in March 2007 to replace \$1.0 billion of common stock with an equal amount of preferred stock. In addition, we issued \$1.1 billion of 5.57 percent non-cumulative, perpetual preferred stock, consisting of \$500 million to complete our plan announced in October 2005 to replace \$2.0 billion of common stock with an equal amount of preferred stock and \$600 million to replace higher-cost preferred stock that we redeemed. In accordance with OFHEO's capital monitoring framework, we obtained OFHEO's approval for the preferred stock redemption. Subsequent to June 30, 2007, in connection with the \$1.0 billion authorization noted above, we issued another \$500 million of 6.02 percent non-cumulative, perpetual preferred stock during July 2007 and repurchased \$250 million (approximately 4.2 million shares) of common stock through August 6, 2007 to complete our plan to replace \$1.0 billion of common stock with an equal amount of preferred stock.

Dividends Declared During the Six Months Ended June 30, 2007

On March 2, 2007 and June 8, 2007, respectively, our board of directors declared quarterly dividends on our common stock of \$0.50 per share and dividends on our preferred stock consistent with the contractual rates and terms shown in "NOTE 9: STOCKHOLDERS' EQUITY — Table 9.1 — Preferred Stock" in our 2006 Information Statement, excluding the redeemed 6.14 percent issuance and including the 5.57 percent and 5.66 percent issuances, as applicable, referenced above.

NOTE 9: REGULATORY CAPITAL

Table 9.1 summarizes our regulatory capital requirements and surpluses.

Table 9.1 — Regulatory Capital Requirements⁽¹⁾

	June 30, 2007	December 31, 2006
	(in millions)	
<i>Minimum capital requirement</i>	\$26,580	\$25,844
Core capital	36,334	36,170
Minimum capital surplus	9,754	10,326
<i>Critical capital requirement</i>	\$13,637	\$13,237
Core capital	36,334	36,170
Critical capital surplus	22,697	22,933
<i>Risk-based capital requirement⁽²⁾</i>	N/A	\$15,320
Total capital ⁽²⁾	N/A	36,742
Risk-based capital surplus ⁽²⁾	N/A	21,422

(1) OFHEO is the authoritative source of the capital calculations that underlie our capital classifications. The minimum and critical capital values for June 30, 2007 reflect the amounts we reported to OFHEO.

(2) OFHEO determines the amounts reported with respect to our risk-based capital requirement. Amounts for the three months ended June 30, 2007 are not yet available.

Table 9.2 summarizes our compliance with our subordinated debt commitment.

Table 9.2 — Subordinated Debt Commitment⁽¹⁾

	June 30, 2007	December 31, 2006
	(in millions)	
Total on-balance sheet assets and guaranteed PCs and Structured Securities outstanding target ⁽²⁾	\$38,452	\$37,576
Total capital plus qualifying subordinated debt	41,767	42,602
Surplus	3,315	5,026

(1) The values for June 30, 2007 reflect the amounts we reported to OFHEO.

(2) Equals the sum of 0.45 percent of outstanding guaranteed PCs and Structured Securities and 4 percent of on-balance sheet assets.

Table 9.3 summarizes our compliance with the mandatory target capital surplus portion of OFHEO's monitoring framework.

Table 9.3 — Mandatory Target Capital Surplus⁽¹⁾

	June 30, 2007	December 31, 2006
	(in millions)	
Minimum capital requirement plus 30% add-on	\$34,555	\$33,597
Core capital	36,334	36,170
Surplus	1,779	2,573

(1) The values for June 30, 2007 are based on amounts we reported to OFHEO.

NOTE 10: DERIVATIVES

By the end of 2006, we had discontinued nearly all of our cash flow hedge accounting relationships and all of our fair value hedge accounting relationships. We record changes in the fair value of derivatives not in hedge accounting relationships as Derivative gains (losses) on our consolidated statements of income. Any associated interest received or paid is recognized on an accrual basis and also recorded in Derivative gains (losses) on our consolidated statements of income.

For a derivative accounted for as a cash flow hedge, changes in fair value are reported in AOCI, net of taxes, on our consolidated balance sheets to the extent the hedge is effective.

Table 10.1 presents the changes in AOCI, net of taxes, related to derivatives designated as cash flow hedges. The Net change in fair value related to cash flow hedging activities, net of tax represents the net change in the fair value of the derivatives that were designated as cash flow hedges, after the effects of our statutory tax rate of 35 percent, to the extent the hedges were effective. The Net reclassifications of losses to earnings, net of tax represents the AOCI amount, after the effects of our statutory tax rate of 35 percent, that was recognized in earnings as the originally hedged forecasted transactions affected earnings. If it is probable that the forecasted transaction will not occur, then the entire deferred gain or loss associated with the hedge related to the forecasted transaction is reclassified into earnings immediately. The total AOCI, net of taxes, related to cash flow hedge relationships was a loss of \$4.6 billion and \$5.6 billion at June 30, 2007 and 2006, respectively, primarily composed of deferred net losses on closed cash flow hedges. Closed cash flow hedges involve derivatives that have been terminated or are no longer designated as cash flow hedges. Fluctuations in prevailing market interest rates have no impact on the deferred portion of AOCI relating to losses on closed cash flow hedges.

Over the next 12 months, we estimate that approximately \$920 million, net of taxes, of the \$4.6 billion of cash flow hedging losses in AOCI, net of taxes, at June 30, 2007 will be reclassified into earnings. The maximum remaining length

of time over which we have hedged the exposure related to the variability in future cash flows on forecasted transactions, primarily forecasted debt issuances, is 26 years. However, over 70 percent and 90 percent of AOCI, net of taxes, relating to cash flow hedges at June 30, 2007, will be reclassified to earnings over the next five and ten years, respectively.

At June 30, 2007, the only derivatives accounted for as open cash flow hedges were certain commitments to forward sell mortgage-related securities with a notional amount of \$4.5 billion and a fair value of \$(48) million.

Table 10.1 — AOCI, Net of Taxes, Related to Cash Flow Hedge Relationships

	Six Months Ended June 30,	
	2007	2006
	(in millions)	
Beginning balance ⁽¹⁾	\$(5,033)	\$(6,287)
Net change in fair value related to cash flow hedging activities, net of tax ⁽²⁾	(36)	31
Net reclassifications of losses to earnings, net of tax ⁽³⁾	495	654
Ending balance ⁽¹⁾	<u>\$(4,574)</u>	<u>\$(5,602)</u>

(1) Represents the effective portion of the fair value of open derivative contracts (*i.e.*, net unrealized gains and losses) and net deferred gains and losses on closed (*i.e.*, terminated or redesignated) cash flow hedges.

(2) Net of tax (benefit) expense of \$(20) million and \$16 million for the six months ended June 30, 2007 and 2006, respectively.

(3) Net of tax benefit of \$266 million and \$352 million for the six months ended June 30, 2007 and 2006, respectively.

NOTE 11: LEGAL CONTINGENCIES

We are involved as a party to a variety of legal proceedings arising from time to time in the ordinary course of business, including among other things, contractual disputes, personal injury claims, employment-related litigation and other legal proceedings incidental to our business. We are frequently involved, directly or indirectly, in litigation involving mortgage foreclosures. From time to time, we are also involved in proceedings arising from our termination of a seller/servicer's eligibility to sell mortgages to us and service mortgages for us. In these cases, the former seller/servicer sometimes seeks damages against us for wrongful termination under a variety of legal theories. In addition, we are sometimes sued in connection with the origination or servicing of mortgages. These suits typically involve claims alleging wrongful actions of seller/servicers. Our contracts with our seller/servicers generally provide for indemnification against liability arising from their wrongful actions.

We are subject to various other legal proceedings, including regulatory investigations and administrative and civil litigation, arising from the restatement of our previously issued consolidated financial statements for the years 2000 and 2001 and the first three quarters of 2002 and the revision of fourth quarter and full-year consolidated financial statements for 2002 (collectively referred to as the "restatement"). In 2005, we recorded a \$339 million expense related to our litigation reserves for legal settlements, including our settlement of the securities class action lawsuits and the shareholder derivative lawsuits, discussed below. We maintain reserves for the amount of the estimated probable loss in connection with the remaining legal proceedings related to the restatement. During 2006, we recorded a \$25 million reduction in our reserves for this loss contingency. Litigation and claims resolution are subject to many uncertainties and are not susceptible to accurate prediction. Any additional losses that might result from the adverse resolution of any of the remaining legal proceedings could be greater than our current reserves.

SEC Investigation. In June 2003, the SEC initiated a formal investigation of Freddie Mac in connection with the restatement. On August 18, 2004, we announced that we had received a "Wells Notice" from the staff of the SEC. The Wells Notice advised us that the SEC staff is considering recommending that the SEC initiate a civil injunctive action against us for possible violations of federal securities laws, including Section 10(b) of the Securities Exchange Act of 1934 and the SEC's Rule 10b-5, as well as Sections 17(a)(1), (2) and (3) of the Securities Act of 1933. The Wells Notice also indicated that the SEC staff may seek a permanent injunction and a civil money penalty in connection with the contemplated action. We continue to cooperate fully with the SEC's investigation.

Securities Class Action Lawsuits. In June 2003 and thereafter, securities class action lawsuits were brought in three separate federal courts against us and certain former executive officers on behalf of certain stockholders in connection with the restatement which were eventually consolidated in the U.S. District Court for the Southern District of New York. The plaintiffs claimed that the defendants improperly managed earnings to create a misleading impression of steady earnings by Freddie Mac, that they engaged in a number of improper transactions that violated GAAP and that they made false and misleading statements regarding the same. On October 26, 2006, the court approved a settlement of the securities class action lawsuits, as well as the shareholder derivative actions described below. The settlement of these actions included a cash payment of \$410 million. The settlement does not include any admission of wrongdoing by us.

Shareholder Derivative Lawsuits. Two shareholder derivative lawsuits were filed during 2003 against certain former and current executives and, in one of the suits, certain former and current members of the board of directors and five

counterparties. The plaintiffs alleged claims for breach of fiduciary duties, indemnification, waste of corporate assets, unjust enrichment and aiding and abetting breach of fiduciary duties in connection with the restatement. Both cases were ultimately assigned to the same judge in New York who handled the securities class action lawsuits described above. As described above, on October 26, 2006, the court approved a settlement of both shareholder derivative actions, as well as the securities class action lawsuits. The settlement of these cases was based in part on corporate governance reforms we instituted under our current management.

Antitrust Lawsuits. Consolidated lawsuits were filed against Fannie Mae and us in the U.S. District Court for the District of Columbia, originally filed on January 10, 2005, alleging that both companies conspired to establish and maintain artificially high guarantee fees. The complaint covers the period from January 1, 2001 to the present and asserts a variety of claims under federal and state antitrust laws, as well as claims under consumer-protection and similar state laws. The plaintiffs seek injunctive relief, unspecified damages (including treble damages with respect to the antitrust claims and punitive damages with respect to some of the state claims) and other forms of relief. We filed a motion to dismiss the action and are awaiting a ruling from the court. At present, it is not possible for us to predict the probable outcome of the consolidated lawsuit or any potential impact on our business, financial condition or results of operations.

Other Inquiries. We receive inquiries from the Internal Revenue Service, or IRS, in connection with its regular audits of our tax returns for prior years, some of which relate to matters connected with the restatement. We continue to respond to these inquiries.

NOTE 12: INCOME TAXES

For the three months ended June 30, 2007 and 2006, we reported Income tax expense of \$113 million and \$40 million, respectively, representing effective tax rates of 13 percent and 3 percent, respectively.

Our effective tax rate continues to be favorably impacted by our investments in LIHTC partnerships and interest earned on tax-exempt housing-related securities. During the three months ended June 30, 2006, we recorded higher pre-tax income than for the three months ended June 30, 2007. However, for the three months ended June 30, 2006, we also recognized an offsetting tax benefit as a result of our application of FIN 18, "Accounting for Income Taxes in Interim Periods, an interpretation of APB Opinion No. 28."

In 2006, and other years since the restatement, we did not release interim financial statements. As a result, for the three and six months ended June 30, 2006, we used our actual 2006 annual effective tax rate as our best estimate of our effective income tax rate for those periods. We cannot estimate our annual effective tax rate for 2007 as we are unable to produce a reliable forecast of book income for 2007. Therefore, for the three and six months ended June 30, 2007, we used our current period effective tax rate to account for income taxes, which represents our best estimate of our 2007 annual effective tax rate.

For the six months ended June 30, 2007 and 2006, we reported income tax benefit of \$326 million and \$75 million, respectively, representing effective tax rates of (144) percent and (2) percent, respectively. Our effective tax rate for the six months ended June 30, 2007 and 2006, benefited from our investments in LIHTC partnerships and interest earned on tax-exempt housing-related securities. Although we recognized pre-tax income for the six months ended June 30, 2006, the application of FIN 18 resulted in the allocation of tax benefit on pre-tax losses incurred in the last six months of 2006 to the first six months of 2006. In addition, the six months ended June 30, 2006 benefited from tax reserve releases.

We adopted the provisions of FIN 48 effective January 1, 2007 and as a result recorded a \$181 million increase to retained earnings. At January 1, 2007, we had total unrecognized tax benefits, exclusive of interest, of \$677 million. Included in the \$677 million were \$76 million of unrecognized tax benefits that, if recognized, would reduce our effective tax rate. The remaining \$601 million of unrecognized tax benefits related to tax positions for which ultimate deductibility is highly certain, but for which there is uncertainty as to the timing of such deductibility. Recognition of these tax benefits, other than applicable interest, would not affect our effective tax rate. There were no material changes in our unrecognized tax benefits during the three and six months ended June 30, 2007.

We continue to recognize interest and penalties, if any, in income tax expense. As of January 1, 2007, we recognized a net accrued interest receivable, net of tax effect, of approximately \$67 million. Amounts included in accrued interest relate to: (a) unrecognized tax benefits; (b) pending claims with the IRS for open tax years; (c) the tax benefit related to tax refund claims; and (d) the impact of payments made to the IRS in prior years in anticipation of potential tax deficiencies. Of the \$67 million of net accrued interest receivable, approximately \$105 million of accrued interest payable, net of tax effect, was allocable to unrecognized tax benefits. There were no material changes in our accrued interest during the three and six months ended June 30, 2007. We have no amount accrued for penalties.

The statute of limitations for federal income tax purposes is open on tax returns filed for years 1985 to 2005. The IRS is currently examining tax years 1998 to 2005. Tax years 1985 to 1997 are before the U.S. Tax Court. We are currently in settlement discussions with the IRS regarding the tax treatment of the customer relationship intangible asset recognized

upon our transition from non-taxable to taxable status in 1985. We believe it is reasonably possible that significant changes in the gross balance of unrecognized tax benefits may occur within the next 12 months; however, we cannot predict the amount of such change or the range of potential changes.

NOTE 13: EMPLOYEE BENEFITS

Table 13.1 presents the components of the net periodic benefit cost with respect to pension and postretirement health care benefits for the three and six months ended June 30, 2007 and 2006. Net periodic benefit cost is included in Salaries and employee benefits on our consolidated statements of income.

Table 13.1 — Net Periodic Benefit Cost Detail

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
(in millions)				
Pension Benefits				
Service cost	\$ 9	\$ 8	\$17	\$16
Interest cost on benefit obligation	7	6	15	13
Expected (return) loss on plan assets	(10)	(6)	(19)	(12)
Recognized net actuarial loss (gain)	1	2	2	3
Net periodic benefit cost	<u>\$ 7</u>	<u>\$10</u>	<u>\$15</u>	<u>\$20</u>
Postretirement Health Care Benefits				
Service cost	\$ 2	\$ 2	\$ 4	\$ 4
Interest cost on benefit obligation	2	1	4	3
Recognized net actuarial loss (gain)	—	1	—	1
Net periodic benefit cost	<u>\$ 4</u>	<u>\$ 4</u>	<u>\$ 8</u>	<u>\$ 8</u>

Table 13.2 presents the changes in AOCI, net of taxes, related to our defined benefit plans recorded to AOCI for the six months ended June 30, 2007, after the effects of our statutory tax rate of 35 percent.

Table 13.2 — AOCI, Net of Taxes, Related to Defined Benefit Plans

	Six Months Ended June 30, 2007
(in millions)	
Beginning balance	\$(87)
Amounts recognized in AOCI, net of tax:	
Recognized net gain (loss) ⁽¹⁾	5
Net reclassification adjustments, net of tax: ⁽²⁾	
Recognized net loss (gain) ⁽³⁾	1
Ending balance	<u>\$(81)</u>

(1) Represents the correction of deferred taxes related to previously recorded Medicare Part D subsidies from prior years.

(2) Represent amounts subsequently recognized as adjustments to other comprehensive income as those amounts are recognized as components of net periodic benefit cost.

(3) Net of tax benefit of \$1 million for the six months ended June 30, 2007.

Cash Flows Related to Defined Benefit Plans

Our general practice is to contribute to our Pension Plan an amount at least equal to the minimum required contribution, if any, but no more than the maximum amount deductible for federal income tax purposes each year. We have not yet determined whether a contribution to our Pension Plan is required for 2007.

NOTE 14: FAIR VALUE DISCLOSURES

The supplemental consolidated fair value balance sheets in Table 14.1 present our estimates of the fair value of our recorded financial assets and liabilities and off-balance sheet financial instruments at June 30, 2007 and December 31, 2006, respectively. The valuations of financial instruments on our consolidated fair value balance sheets are in conformity with GAAP fair value guidelines prescribed by SFAS No. 107, "Disclosures about Fair Value of Financial Instruments," or SFAS 107, and other relevant pronouncements.

Table 14.1 — Consolidated Fair Value Balance Sheets⁽¹⁾

	June 30, 2007		December 31, 2006	
	Carrying Amount ⁽²⁾	Fair Value ⁽³⁾	Carrying Amount ⁽²⁾	Fair Value ⁽³⁾
	(in billions)			
Assets				
Mortgage loans	\$ 68.4	\$ 66.1	\$ 65.6	\$ 65.4
Mortgage-related securities excluding PC residuals	634.4	634.4	634.3	634.3
PC residuals	0.5	0.5	0.6	0.6
Retained portfolio	703.3	701.0	700.5	700.3
Cash and cash equivalents	11.8	11.8	11.4	11.4
Investments	41.7	41.7	45.6	45.6
Securities purchased under agreements to resell and Federal funds sold	27.5	27.5	23.0	23.0
Derivative assets	7.2	7.2	7.9	7.9
Guarantee asset ⁽⁴⁾	7.8	8.1	6.1	6.4
Other assets ⁽⁵⁾	22.4	19.2	18.6	16.7
Total assets	<u>\$821.7</u>	<u>\$816.5</u>	<u>\$813.1</u>	<u>\$811.3</u>
Liabilities and minority interests				
Total debt securities, net	\$760.5	\$753.5	\$753.9	\$752.3
Guarantee obligation	8.6	6.0	7.1	4.7
Derivative liabilities	0.3	0.3	0.2	0.2
Reserve for guarantee losses on PCs	0.7	—	0.4	—
Other liabilities	25.5	24.6	22.7	21.8
Minority interests in consolidated subsidiaries	0.3	0.2	0.5	0.5
Total liabilities and minority interests	795.9	784.6	784.8	779.5
Net assets attributable to stockholders				
Preferred stockholders	7.1	6.8	6.1	5.8
Common stockholders	18.7	25.1	22.2	26.0
Total net assets	<u>25.8</u>	<u>31.9</u>	<u>28.3</u>	<u>31.8</u>
Total liabilities, minority interests and net assets	<u>\$821.7</u>	<u>\$816.5</u>	<u>\$813.1</u>	<u>\$811.3</u>

- (1) The consolidated fair value balance sheets do not purport to present our net realizable, liquidation or market value as a whole. Furthermore, amounts we ultimately realize from the disposition of assets or settlement of liabilities may vary significantly from the fair values presented.
- (2) Equals the amount reported on our GAAP consolidated balance sheets.
- (3) Methodologies employed to calculate fair values are periodically changed on a prospective basis to reflect improvements in the underlying estimation processes. The estimated impact of these improvements resulted in net after-tax changes to the fair value of Total net assets of approximately \$0.2 billion at June 30, 2007 and that rounded to zero at December 31, 2006.
- (4) The fair value of the Guarantee asset reported exceeds the carrying value primarily because the fair value includes the Guarantee asset related to some PCs held by third parties that are not recognized on our GAAP consolidated balance sheets because such PCs were issued prior to the implementation of FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," an interpretation of FASB Statements No. 5, 57, and 107 and rescission of FASB Interpretation No. 34" in 2003.
- (5) Fair values include estimated income taxes calculated using the 35 percent statutory rate on the difference between the consolidated fair value balance sheets net assets, including deferred taxes from our GAAP consolidated balance sheets, and the GAAP consolidated balance sheets equity attributable to common stockholders.

NOTE 15: EARNINGS PER COMMON SHARE

Because we have participating securities, we use the “two-class” method of computing earnings per share. Basic earnings per common share are computed by dividing Net income (loss) available to common stockholders by Weighted average common shares outstanding — Basic for the period. Diluted earnings per common share are computed as Net income (loss) available to common stockholders divided by Weighted average common shares outstanding — Diluted for the period, which consider the effect of dilutive common equivalent shares outstanding. The effect of dilutive common equivalent shares outstanding includes: (a) the weighted average shares related to stock options (including the Employee Stock Purchase Plan) that have an exercise price lower than the average market price during the period; (b) the weighted average of non-vested restricted shares; and (c) all restricted stock units. Such items are excluded from Weighted average common shares outstanding — Basic.

For the three months ended June 30, 2007 and 2006, there were approximately 2.9 million and 1.3 million, respectively, of dilutive common equivalent weighted average shares outstanding that could have potentially diluted earnings per common share. Options to purchase 0.7 million and 3.5 million weighted average shares of common stock were excluded from the computation of Diluted earnings per common share at June 30, 2007 and 2006, respectively, because the options’ exercise prices exceeded the average market price of the common stock for the three months ended June 30, 2007 and 2006.

For the six months ended June 30, 2007 and 2006, there were approximately 2.3 million and 1.5 million, respectively, of dilutive common equivalent weighted average shares outstanding that could have potentially diluted earnings per common share. Options to purchase 1.7 million and 2.0 million weighted average shares of common stock were excluded from the computation of Diluted earnings per common share at June 30, 2007 and 2006, respectively, because the options’ exercise prices exceeded the average market price of the common stock for the six months ended June 30, 2007 and 2006.

END OF UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS AND ACCOMPANYING NOTES

FORWARD-LOOKING STATEMENTS

We regularly communicate information concerning our business activities to investors, securities analysts, the news media and others as part of our normal operations. Some of these communications, including this Information Statement Supplement, contain “forward-looking statements” pertaining to our current expectations and objectives for financial reporting, remediation efforts, future business plans, market conditions, market share, credit losses, prepayments, results of operations and financial condition on both a GAAP and fair value basis, and market trends and developments. Forward-looking statements are often accompanied by, and identified with, terms such as “objective,” “seek,” “will,” “may,” “might,” “can,” “could,” “expect,” “trend,” “assumptions,” “judgments,” “estimate,” “anticipate,” “future,” “continue,” “affect,” “uncertainty,” “long-term,” “ultimate,” “believe,” “ability,” “models,” “develop,” “current,” “generally,” “designed,” “priorities,” “implies,” “evolve,” “remains,” “plan,” “outlook,” “maintain,” “consider,” “opportunities,” “initiatives,” “over time,” “potentially,” “would,” “likely,” “efforts,” “in the process of,” “enable,” “intended,” and similar phrases. These statements are not historical facts, but rather represent our expectations based on current information, plans, judgments, assumptions, estimates and projections. Forward-looking statements involve known and unknown risks, uncertainties and other factors, some of which are beyond our control. You should not unduly rely on our forward-looking statements. All risks, uncertainties and other factors described in our 2006 Information Statement and this Information Statement Supplement should be considered in relying on any forward-looking statements. Actual results may differ materially from the expectations expressed in these and other forward-looking statements we make as a result of various factors, including those factors described in the “RISK FACTORS” section of this Information Statement Supplement and the comparably captioned section in our 2006 Information Statement and:

- changes in applicable legislative or regulatory requirements, including regulation of the subprime or non-traditional mortgage product markets, enactment of GSE oversight legislation, changes to our charter, changes to affordable housing goals regulation, changes to regulatory capital requirements or the exercise or assertion of regulatory or administrative authority beyond historical practice;
- our ability to effectively identify, assess, evaluate, manage, mitigate or remediate control deficiencies and risks, including material weaknesses and significant deficiencies, in our internal control over financial reporting and disclosure controls and procedures;
- our ability to effectively implement our business strategies and manage the risks in our business, including our efforts to improve the supply and liquidity of, and demand for, our products;
- our ability to effectively identify and manage interest-rate and other market risks, including the levels and volatilities of interest rates, as well as the shape and slope of the yield curves;
- our ability to effectively identify and manage credit risk and/or changes to the credit environment;
- volatility of reported results due to changes in the fair value of certain instruments or assets;
- changes to legislative, regulatory or voluntary limits on the growth of any aspect of our business activities, including our Retained portfolio;
- changes in our judgments, assumptions, forecasts or estimates regarding rates of growth in our business, spreads we expect to earn, required capital levels and the timing and impact of capital transactions;
- our ability to effectively manage and implement changes, developments or impacts of accounting or tax standards and interpretations or changes to our accounting policies or estimates;
- the availability of debt financing and equity capital in sufficient quantity and at attractive rates to support growth in our Retained portfolio, to refinance maturing debt and to meet regulatory capital requirements;
- changes in pricing, valuation or other methodologies, models, assumptions, judgments, estimates and/or other measurement techniques or their respective reliability;
- changes in general regional, national or international economic, business or market conditions and competitive pressures, including consolidation of mortgage originators, employment rates and home price appreciation;
- changes in mortgage-to-debt option-adjusted spread;
- the availability of options, interest-rate and currency swaps and other derivative financial instruments of the types and quantities and with acceptable counterparties needed for investment funding and risk management purposes;
- the rate of growth in total outstanding U.S. residential mortgage debt and the size of the U.S. residential mortgage market;
- preferences of originators in selling into the secondary market;
- borrower preferences for fixed-rate mortgages or ARMs;
- changes to our underwriting and disclosure requirements or investment standards for mortgage-related products;

- investor preferences for mortgage loans and mortgage-related and debt securities compared to other investments;
- the ability of our financial, accounting, data processing and other operating systems or infrastructure and those of our vendors to process the complexity and volume of our transactions;
- incomplete or inaccurate information provided by customers and counterparties, or adverse changes in the financial condition of our customers and counterparties;
- the occurrence of a major natural or other disaster in geographic areas in which portions of our Total mortgage portfolio are concentrated;
- other factors and assumptions described in this Information Statement Supplement or 2006 Information Statement, including in the “MD&A” section;
- our assumptions and estimates regarding the foregoing and our ability to anticipate the foregoing factors and their impacts; and
- market reactions to the foregoing.

We undertake no obligation to update forward-looking statements we make to reflect events or circumstances after the date of this Information Statement Supplement or to reflect the occurrence of unanticipated events.

CONTROLS AND PROCEDURES

See “MD&A — RISK MANAGEMENT — Operational Risks — *Disclosure Controls and Procedures*” and “— *Internal Control Over Financial Reporting*” for information regarding our remediation efforts.

LEGAL PROCEEDINGS

We are involved as a party to a variety of legal proceedings arising from time to time in the ordinary course of business. For a description of certain of our legal proceedings, see “NOTE 11: LEGAL CONTINGENCIES” to our consolidated financial statements for more information regarding our involvement as a party to various legal proceedings.

RISK FACTORS

Our 2006 Information Statement describes certain risk factors that may impact our future results. Such description is supplemented by the following:

Market uncertainty and volatility may adversely affect our business and results of operations.

The mortgage credit markets experienced difficult conditions and volatility during the first six months of 2007. These deteriorating conditions in the mortgage market resulted in a decrease in availability of corporate credit and liquidity within the mortgage industry in the third quarter of 2007 and have caused disruptions to normal operations of major mortgage originators, including some of our largest customers. These conditions resulted in less liquidity, greater volatility, widening of credit spreads and a lack of price transparency. We operate in these markets through exposures in securities, loans, derivatives and other mortgage commitments with our customers. While it is difficult to predict how long these conditions will exist and how our markets or products will ultimately be affected, these factors could adversely impact our business and results of operations.

The loss of business volume from key lenders could result in a decline in our market share and revenues.

Our business depends on our ability to acquire a steady flow of mortgage loans from the originators of those loans. We purchase a significant percentage of our single-family mortgages from several large mortgage originators. During the six months ended June 30, 2007, more than 75 percent of our guaranteed mortgage securities issuances originated from purchase volume associated with our ten largest customers. Two of our customers each accounted for greater than ten percent of our mortgage securitization volume for the six months ended June 30, 2007. We enter into mortgage purchase volume commitments with many of our customers that are renewed annually and provide for a minimum level of mortgage volume that these customers will deliver to us. One of our customers, which accounted for more than ten percent of our mortgage purchase volume for the six months ended June 30, 2007, has reduced its minimum mortgage volume commitments to us upon renewal of its contract at July 1, 2007. In addition, ABN Amro Mortgage Group, Inc., which accounted for more than eight percent of our guaranteed securitization volume for the six months ended June 30, 2007, was acquired and therefore the contract will not be renewed when it expires in the third quarter of 2007. The mortgage industry has been consolidating and a decreasing number of large lenders originate most single-family mortgages. The loss of business from any one of our major lenders could adversely affect our market share, our revenues and the performance of our guaranteed mortgage-related securities.

Regulation and initiatives regarding non-traditional and subprime mortgage products may adversely affect our profitability or our ability to achieve our affordable housing goals and subgoals.

The actions we are taking in connection with the Interagency Guidance and the Subprime Statement are described in “MD&A — RISK MANAGEMENT — Credit Risks — *Mortgage Credit Risk — Guidance on Non-traditional Mortgage Product Risks and Subprime Mortgage Lending.*” These changes to our underwriting and disclosure requirements and investment standards could reduce the number of these mortgage products available to us for purchase. Reductions in our purchases of these mortgage products may adversely affect our profitability and are likely to make it more difficult to achieve our affordable housing goals and subgoals.

Furthermore, in April 2007, we committed to purchase up to \$20 billion of the new products we began developing in February 2007. In July 2007, we purchased approximately \$106 million of these mortgage products pursuant to this commitment. These initiatives may also adversely affect our profitability or our ability to achieve our affordable housing goals and subgoals.

UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Recent Sales of Unregistered Securities

The securities we issue are “exempted securities” under the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended. As a result, we do not file registration statements with the SEC with respect to offerings of our securities.

During the six months ended June 30, 2007, we completed two preferred stock offerings. On January 16, 2007, we sold 44 million shares of 5.57 percent non-cumulative, perpetual preferred stock in an offering underwritten by a syndicate of dealers headed by Goldman, Sachs and Co. and J.P. Morgan Securities Inc. for aggregate offering proceeds of \$1.1 billion and an aggregate underwriting discount of \$11 million. On April 16, 2007, we sold 20 million shares of 5.66 percent non-cumulative, perpetual preferred stock in an offering underwritten by a syndicate of dealers headed by Banc of America Securities LLC and Morgan Stanley & Co. Inc for aggregate offering proceeds of \$500 million and an aggregate underwriting discount of \$5 million. See “NOTE 8: STOCKHOLDERS’ EQUITY” to our consolidated financial statements for more information regarding our preferred stock offerings.

We regularly provide stock compensation to our employees and members of our board of directors. We have three stock-based compensation plans under which grants are currently being made: (a) the Employee Stock Purchase Plan, or ESPP; (b) the 2004 Stock Compensation Plan, or 2004 Employee Plan; and (c) the 1995 Directors' Stock Compensation Plan, as amended and restated, or Directors' Plan. Prior to the stockholder approval of the 2004 Employee Plan, employee stock-based compensation was awarded in accordance with the terms of the 1995 Stock Compensation Plan, or 1995 Employee Plan. Although grants are no longer made under the 1995 Employee Plan, we currently have awards outstanding under this plan. We collectively refer to the 2004 Employee Plan and 1995 Employee Plan as the Employee Plans.

During the six months ended June 30, 2007, options for 308,929 shares of common stock were exercised and no stock options were granted under our Employee Plans and Directors' Plan. Under our ESPP, options to purchase 108,181 shares of common stock were exercised and options to purchase 122,167 shares of common stock were granted during the six months ended June 30, 2007. Further, for the six months ended June 30, 2007, under the Employee Plans and Directors' Plan, 1,442,214 restricted stock units were granted and restrictions lapsed on 515,949 restricted stock units. See "NOTE 11: STOCK-BASED COMPENSATION" to our consolidated financial statements in our 2006 Information Statement for more information.

See "NOTE 10: REGULATORY CAPITAL" to our consolidated financial statements in our 2006 Information Statement for a description of our regulatory capital requirements and possible regulatory restrictions on our ability to pay dividends.

Issuer Purchases of Equity Securities

During the three months ended June 30, 2007, we repurchased common stock in connection with our \$1.0 billion stock repurchase plan authorized in March 2007. Table 31 sets forth our common share repurchase activity during the three months ended June 30, 2007. See "MD&A — LIQUIDITY AND CAPITAL RESOURCES — Capital Resources" for additional information.

Table 31 — Common Share Repurchase Activity for the Three Months Ended June 30, 2007

Period	Total Number of Shares Purchased (in millions)	Average Price Paid per Share	Total Number of Shares Purchased as Part of a Publicly Announced Program (in millions)	Approximate Dollar Value of Shares That May Yet be Purchased Under the Program ⁽¹⁾ (in millions)
April	7.7	\$61.57	7.7	\$529
May	4.2	66.22	4.2	250
June	—	—	—	250
Total	<u>11.9</u>	<u>\$63.23</u>	<u>11.9</u>	

(1) On March 23, 2007, we announced that our board of directors had authorized us to repurchase up to \$1 billion of outstanding shares of common stock.

SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The following matters were submitted to a vote by stockholders at our annual meeting held on June 8, 2007:

(a) election of 13 members to our board of directors, each for a term ending on the date of our next annual meeting of stockholders; (b) ratification of the appointment of PricewaterhouseCoopers LLP as our independent auditors for 2007; and (c) approval of the amendment and restatement of the 1995 Directors' Stock Compensation Plan.

As shown in Table 32 below, the following persons were elected to our board of directors at the meeting by the respective votes indicated:

Table 32 — Election of Directors

	<u>Votes For</u>	<u>Votes Withheld</u>
Barbara T. Alexander	561,436,121	21,859,693
Geoffrey T. Boisi	539,697,402	43,598,412
Michelle Engler	542,296,545	40,999,269
Robert R. Glauber	558,360,092	24,935,722
Richard Karl Goeltz	518,695,847	64,599,967
Thomas S. Johnson	517,330,244	65,965,570
William M. Lewis, Jr.	563,828,592	19,467,222
Eugene M. McQuade	563,855,562	19,440,252
Shaun F. O'Malley	502,534,996	80,760,818
Jeffrey M. Peek	563,803,570	19,492,244
Nicolas P. Retsinas	576,351,457	6,944,357
Stephen A. Ross	505,937,942	77,357,872
Richard F. Syron	558,787,116	24,508,698

The appointment by the Audit Committee of PricewaterhouseCoopers LLP was ratified at the meeting by the following votes:

<u>Votes For</u>	<u>Votes Against</u>	<u>Abstentions</u>
575,138,200	4,445,217	3,712,397

The amendment and restatement of the 1995 Directors' Stock Compensation Plan was approved at the meeting by the following votes:

<u>Votes For</u>	<u>Votes Against</u>	<u>Abstentions</u>	<u>Broker Non-Votes</u>
461,759,928	38,495,235	4,214,641	78,826,010

RISK MANAGEMENT AND DISCLOSURE COMMITMENTS

In October 2000, we announced our voluntary adoption of a series of commitments designed to enhance market discipline, liquidity and capital. In September 2005, we entered into a written agreement with OFHEO that updated these commitments and set forth a process for implementing them. The letters between the company and OFHEO dated September 1, 2005 constituting the written agreement are available on the Investor Relations page of our website at www.freddiemac.com/investors/reports.html#commit. As noted in these letters, disclosures may be affected by situations for which current financial statements are not available. The status of our commitments at June 30, 2007 follows:

Description	Status
<p>1. <i>Periodic Issuance of Subordinated Debt:</i></p> <ul style="list-style-type: none"> • We will issue Freddie SUBS[®] securities for public secondary market trading that are rated by no less than two nationally recognized statistical rating organizations. • Freddie SUBS[®] securities will be issued in an amount such that the sum of Total capital (Core capital plus general allowance for losses) and the outstanding balance of “Qualifying subordinated debt” will equal or exceed the sum of (i) 0.45 percent of outstanding PCs and Structured Securities we guaranteed; and (ii) four percent of total on-balance sheet assets. Qualifying subordinated debt is discounted by one-fifth each year during the instrument’s last five years before maturity; when the remaining maturity is less than one year, the instrument is entirely excluded. We will take reasonable steps to maintain outstanding subordinated debt of sufficient size to promote liquidity and reliable market quotes on market values. • Each quarter, we will submit to OFHEO calculations of the quantity of qualifying Freddie SUBS[®] securities and Total capital as part of our quarterly capital report. • Every six months, we will submit to OFHEO a subordinated debt management plan that includes any issuance plans for the six months following the date of the plan. 	<ul style="list-style-type: none"> • During the six months ended June 30, 2007, we did not issue any Freddie SUBS[®] securities; however, we called \$1.2 billion of Freddie SUBS[®] securities. • We reported to OFHEO that at June 30, 2007, we had \$41.8 billion in Total capital plus qualifying subordinated debt, resulting in a surplus of \$3.3 billion. We have submitted our June 30, 2007 quarterly Total capital plus qualifying subordinated debt report to OFHEO. • We have submitted our semi-annual subordinated debt management plan to OFHEO.
<p>2. <i>Liquidity Management and Contingency Planning:</i></p> <ul style="list-style-type: none"> • We will maintain a contingency plan providing for at least three months’ liquidity without relying upon the issuance of unsecured debt. We will also periodically test the contingency plan in consultation with OFHEO. 	<ul style="list-style-type: none"> • We have in place a liquidity contingency plan, upon which we report to OFHEO on a weekly basis. We periodically test this plan in accordance with our agreement with OFHEO.
<p>3. <i>Interest-Rate Risk Disclosures:</i></p> <ul style="list-style-type: none"> • We will provide public disclosure of our duration gap, PMVS-L and PMVS-YC interest-rate risk sensitivity results on a monthly basis. See “MD&A — RISK MANAGEMENT — Interest-Rate Risk and Other Market Risks — <i>Portfolio Market Value Sensitivity and Measurement of Interest-Rate Risk</i>” in our 2006 Information Statement for a description of these metrics. 	<ul style="list-style-type: none"> • For the six months ended June 30, 2007, our duration gap averaged zero months, PMVS-L averaged one percent and PMVS-YC averaged zero percent. Our 2007 monthly average duration gap, PMVS results and related disclosures are provided in our Monthly Volume Summary which is available on our website, www.freddiemac.com/investors/volsum.

Description	Status																																												
<p>4. <i>Credit Risk Disclosures:</i></p> <ul style="list-style-type: none"> We will make quarterly assessments of the expected impact on credit losses from an immediate 5 percent decline in single-family home prices for the entire U.S. We will disclose the impact in present value terms and measure our estimated losses both before and after receipt of private mortgage insurance claims and other credit enhancements. 	<ul style="list-style-type: none"> Our quarterly credit risk sensitivity estimates are as follows: <table border="1" style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th rowspan="2"></th> <th colspan="2" style="text-align: center;">Before Receipt of Credit Enhancements⁽¹⁾</th> <th colspan="2" style="text-align: center;">After Receipt of Credit Enhancements⁽²⁾</th> </tr> <tr> <th style="text-align: center;">Net Present Value, or NPV⁽³⁾</th> <th style="text-align: center;">NPV Ratio⁽⁴⁾</th> <th style="text-align: center;">NPV⁽³⁾</th> <th style="text-align: center;">NPV Ratio⁽⁴⁾</th> </tr> </thead> <tbody> <tr> <td colspan="5" style="text-align: center;">(dollars in millions)</td> </tr> <tr> <td>At:</td> <td></td> <td></td> <td></td> <td></td> </tr> <tr> <td>06/30/07</td> <td style="text-align: right;">\$1,768</td> <td style="text-align: right;">11.0 bps</td> <td style="text-align: right;">\$1,292</td> <td style="text-align: right;">8.1 bps</td> </tr> <tr> <td>03/31/07</td> <td style="text-align: right;">\$1,327</td> <td style="text-align: right;">8.6 bps</td> <td style="text-align: right;">\$ 929</td> <td style="text-align: right;">6.0 bps</td> </tr> <tr> <td>12/31/06</td> <td style="text-align: right;">\$1,128</td> <td style="text-align: right;">7.6 bps</td> <td style="text-align: right;">\$ 770</td> <td style="text-align: right;">5.2 bps</td> </tr> <tr> <td>09/30/06</td> <td style="text-align: right;">\$1,071</td> <td style="text-align: right;">7.4 bps</td> <td style="text-align: right;">\$ 724</td> <td style="text-align: right;">5.0 bps</td> </tr> <tr> <td>06/30/06</td> <td style="text-align: right;">\$1,018</td> <td style="text-align: right;">7.2 bps</td> <td style="text-align: right;">\$ 686</td> <td style="text-align: right;">4.9 bps</td> </tr> </tbody> </table> <p>(1) Assumes that none of the credit enhancements currently covering our mortgage loans has any mitigating impact on our credit losses. (2) Assumes we collect amounts due from credit enhancement providers after giving effect to certain assumptions about counterparty default rates. (3) Based on single-family mortgage portfolio, excluding Structured Securities backed by Ginnie Mae Certificates. (4) Calculated as the ratio of net present value of increase in credit losses to the single-family Total mortgage portfolio, defined in footnote (3) above.</p> 		Before Receipt of Credit Enhancements ⁽¹⁾		After Receipt of Credit Enhancements ⁽²⁾		Net Present Value, or NPV ⁽³⁾	NPV Ratio ⁽⁴⁾	NPV ⁽³⁾	NPV Ratio ⁽⁴⁾	(dollars in millions)					At:					06/30/07	\$1,768	11.0 bps	\$1,292	8.1 bps	03/31/07	\$1,327	8.6 bps	\$ 929	6.0 bps	12/31/06	\$1,128	7.6 bps	\$ 770	5.2 bps	09/30/06	\$1,071	7.4 bps	\$ 724	5.0 bps	06/30/06	\$1,018	7.2 bps	\$ 686	4.9 bps
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<p>5. <i>Public Disclosure of Risk Rating:</i></p> <ul style="list-style-type: none"> We will seek to obtain a rating, that will be continuously monitored by at least one nationally recognized statistical rating organization, assessing our “risk-to-the-government” or independent financial strength. 	<ul style="list-style-type: none"> At both August 1, 2007 and June 30, 2007, our “risk-to-the-government” rating from S&P was “AA–” and Moody’s Bank Financial Strength Rating for us was “A–”. 																																												

EXHIBITS
CERTIFICATION*

I, Richard F. Syron, certify that:

1. I have reviewed this Information Statement Supplement of Freddie Mac;
2. Based on my knowledge, this Information Statement Supplement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Information Statement Supplement; and
3. Based on my knowledge, the unaudited consolidated financial statements, and other financial information included in this Information Statement Supplement, fairly present in all material respects the financial condition, results of operations and cash flows of Freddie Mac as of, and for, the periods presented in this Information Statement Supplement.

Date: August 30, 2007



Richard F. Syron
Chairman and Chief Executive Officer

CERTIFICATION*

I, Anthony S. Pizsel, certify that:

1. I have reviewed this Information Statement Supplement of Freddie Mac;
2. Based on my knowledge, this Information Statement Supplement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Information Statement Supplement; and
3. Based on my knowledge, the unaudited consolidated financial statements, and other financial information included in this Information Statement Supplement, fairly present in all material respects the financial condition, results of operations and cash flows of Freddie Mac as of, and for, the periods presented in this Information Statement Supplement.

Date: August 30, 2007



Anthony S. Pizsel
Executive Vice President and Chief Financial Officer

* For a discussion of our progress with respect to our internal control over financial reporting and disclosure controls and procedures, see “MD&A — RISK MANAGEMENT — Operational Risks — *Internal Control over Financial Reporting*” and the comparably captioned section of our 2006 Information Statement.

RATIO OF EARNINGS TO FIXED CHARGES

	Six Months Ended		Year Ended December 31,				
	June 30,						
	2007	2006	2006	2005	2004	2003	2002
	(dollars in millions)						
Net income (loss) before cumulative effect of changes in accounting principles	\$ 553	\$ 3,406	\$ 2,211	\$ 2,189	\$ 2,937	\$ 4,816	\$10,090
Add:							
Income tax expense (benefit)	(326)	(75)	(108)	367	790	2,202	4,713
Minority interests in earnings of consolidated subsidiaries	17	34	58	96	129	157	184
Low-income housing tax credit partnerships	243	219	407	320	281	200	160
Total interest expense	19,188	17,994	37,270	29,899	26,566	26,509	26,876
Interest factor in rental expenses	3	3	6	6	6	5	5
Earnings, as adjusted	<u>\$19,678</u>	<u>\$21,581</u>	<u>\$39,844</u>	<u>\$32,877</u>	<u>\$30,709</u>	<u>\$33,889</u>	<u>\$42,028</u>
Fixed charges:							
Total interest expense	\$19,188	\$17,994	\$37,270	\$29,899	\$26,566	\$26,509	\$26,876
Interest factor in rental expenses	3	3	6	6	6	5	5
Capitalized interest	—	—	—	—	1	—	1
Total fixed charges	<u>\$19,191</u>	<u>\$17,997</u>	<u>\$37,276</u>	<u>\$29,905</u>	<u>\$26,573</u>	<u>\$26,514</u>	<u>\$26,882</u>
Ratio of earnings to fixed charges ⁽¹⁾	<u>1.03</u>	<u>1.20</u>	<u>1.07</u>	<u>1.10</u>	<u>1.16</u>	<u>1.28</u>	<u>1.56</u>

(1) Ratio of earnings to fixed charges is computed by dividing Earnings, as adjusted by Total fixed charges.

RATIO OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED STOCK DIVIDENDS

	Six Months Ended		Year Ended December 31,				
	June 30,						
	2007	2006	2006	2005	2004	2003	2002
	(dollars in millions)						
Net income (loss) before cumulative effect of changes in accounting principles	\$ 553	\$ 3,406	\$ 2,211	\$ 2,189	\$ 2,937	\$ 4,816	\$10,090
Add:							
Income tax expense (benefit)	(326)	(75)	(108)	367	790	2,202	4,713
Minority interests in earnings of consolidated subsidiaries	17	34	58	96	129	157	184
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Fixed charges:							
Total interest expense	\$19,188	\$17,994	\$37,270	\$29,899	\$26,566	\$26,509	\$26,876
Interest factor in rental expenses	3	3	6	6	6	5	5
Capitalized interest	—	—	—	—	1	—	1
Preferred stock dividends ⁽¹⁾	184	117	270	261	266	315	351
Total fixed charges including preferred stock dividends	<u>\$19,375</u>	<u>\$18,114</u>	<u>\$37,546</u>	<u>\$30,166</u>	<u>\$26,839</u>	<u>\$26,829</u>	<u>\$27,233</u>
Ratio of earnings to combined fixed charges and preferred stock dividends ⁽²⁾	<u>1.02</u>	<u>1.19</u>	<u>1.06</u>	<u>1.09</u>	<u>1.14</u>	<u>1.26</u>	<u>1.54</u>

(1) Preferred stock dividends represent pre-tax earnings required to cover any preferred stock dividend requirements using our effective tax rate for the relevant periods.

(2) Ratio of earnings to combined fixed charges and preferred stock dividends is computed by dividing Earnings, as adjusted by Total fixed charges including preferred stock dividends.