OFFERING CIRCULAR

Freddie Mac

5,000,000 Shares

Federal Home Loan Mortgage Corporation

Variable Rate, Non-Cumulative Preferred Stock

Dividend Rate:	$\frac{(\text{3-Month LIBOR} + 1.0\%)}{1.377}$
Dividend Rate Cap:	9.00%
Payment Dates:	March 31, June 30, September 30 and December 31 of each year, beginning June 30, 1996
Dividend Reset Frequency:	Quarterly
Dividend Adjustment:	Dividend amount subject to adjustment upon certain adverse changes to dividends-received deduction prior to April 26, 1998
Liquidation Preference:	$50 per share plus current dividends
Optional Redemption:	On or after June 30, 2001
Issue Date:	On or about April 26, 1996
Initial Dividend Rate:	4.7091% (from April 26, 1996 through June 30, 1996)
Listing:	New York Stock Exchange

FREDDIE MAC'S OBLIGATIONS UNDER THE TERMS OF THE PREFERRED STOCK ARE OBLIGATIONS OF FREDDIE MAC ONLY AND ARE NOT OBLIGATIONS OF, OR GUARANTEED BY, THE UNITED STATES OR ANY AGENCY OR INSTRUMENTALITY OF THE UNITED STATES OTHER THAN FREDDIE MAC.

	Initial Public Offering Price(1)	Underwriting Discount(2)	Proceeds to Freddie Mac(1)(3)
Per Share	$50.00	$.875	$49.125
Total(4)	$250,000,000	$4,375,000	$245,625,000

(1) Plus accrued dividends, if any, from April 26, 1996.
(2) Freddie Mac has agreed to indemnify the several Underwriters against certain liabilities. See "Underwriting."
(3) Before deducting expenses payable by Freddie Mac estimated at $200,000.
(4) Freddie Mac has granted the Underwriters an option to purchase up to an additional 500,000 shares to cover overallotments. If all such shares are purchased, the total Initial Public Offering Price, Underwriting Discount and Proceeds to Freddie Mac will be $275,000,000, $4,812,500 and $270,187,500, respectively. See "Underwriting."

Goldman, Sachs & Co.

Bear, Stearns & Co. Inc.

Salomon Brothers Inc

The date of this Offering Circular is April 23, 1996.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE PREFERRED STOCK AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH TRANSACTIONS MAY BE EFFECTED ON THE NEW YORK STOCK EXCHANGE, IN THE OVER-THE-COUNTER MARKET OR OTHERWISE. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

ADDITIONAL INFORMATION

This Offering Circular should be read in conjunction with, and is qualified in its entirety by:

- the Certificate of Creation, Designation, Powers, Preferences, Rights, Privileges, Qualifications, Limitations, Restrictions, Terms and Conditions (the "Certificate of Designation") relating to the Variable Rate, Non-Cumulative Preferred Stock (the "Preferred Stock"), which will be in substantially the form attached as Appendix A to this Offering Circular,
- recent unaudited financial information of Freddie Mac attached as Appendix B to this Offering Circular, which information was contained in materials originally released on April 15, 1996, and
- Freddie Mac's Information Statement dated March 29, 1996 (the "Information Statement") attached to this Offering Circular.

Freddie Mac furnishes its stockholders with annual reports containing financial information audited by independent public accountants and quarterly reports containing unaudited financial information.

The shares of Preferred Stock are exempt from the registration requirements of the Securities Act of 1933 and are "exempted securities" within the meaning of the Securities Exchange Act of 1934. Accordingly, no registration statement has been filed with the Securities and Exchange Commission, and Freddie Mac does not file periodic reports with the Securities and Exchange Commission.

Copies of Freddie Mac's most recent annual and quarterly reports and its most recent proxy statement are available, and copies of the Certificate of Designation as executed will be available, without charge from Shareholder Relations, Federal Home Loan Mortgage Corporation, 8200 Jones Branch Drive, McLean, VA 22102, telephone 800/424-5401, ext. 2581.

Dividends paid on the Preferred Stock have no exemption under federal law from federal, state or local taxation.

The distribution of this Offering Circular and the offer, sale and delivery of the Preferred Stock in certain jurisdictions may be restricted by law. Persons who receive this Offering Circular should inform themselves about and observe any such restrictions.

OFFERING SUMMARY

Issuer	Federal Home Loan Mortgage Corporation ("Freddie Mac" or the "Corporation").
Security Offered	5,000,000 shares (assuming the Underwriters' over-allotment option is not exercised) of Variable Rate, Non-Cumulative Preferred Stock (the "Preferred Stock"), with a redemption price and liquidation preference of $50 per share.
Dividends:	
Rate	$\frac{(\text{3-Month LIBOR} + 1.0\%)}{1.377}$ Dividends will accrue from April 26, 1996 and will reset quarterly. For information about how and when LIBOR will be determined, see "Description of Preferred Stock — Determination of LIBOR."
Initial Rate	4.7091% (from April 26, 1996 through June 30, 1996).
Rate Cap	9.00%.
Calculation Agent	Freddie Mac.
Frequency	Quarterly, when, as and if declared by the Board of Directors.
Payment Dates	March 31, June 30, September 30 and December 31 of each year, beginning June 30, 1996.
DRD Protection	If, prior to April 26, 1998, certain amendments to the Internal Revenue Code of 1986, as amended (the "Code"), are enacted that reduce the percentage of the dividends-received deduction below 70%, the amount of dividends payable in respect of the Preferred Stock will be adjusted to offset the effect of such reduction. However, no adjustment will be made to the extent that the percentage of the dividends-received deduction is reduced below 50%. Such adjustment may result in a dividend rate in excess of 9% per annum.
Preferences	The Preferred Stock will be entitled to a preference, both as to dividends and upon liquidation, over the common stock (and any other junior stock) of Freddie Mac. The Preferred Stock will rank on a parity, both as to dividends and upon liquidation, with other currently outstanding series of Freddie Mac preferred stock.
Optional Redemption	Beginning June 30, 2001, Freddie Mac will have the option to redeem the Preferred Stock at any time, in whole or in part, at the redemption price of $50 per share plus the dividend for the then-current quarterly dividend period accrued through the redemption date.
Liquidation Rights	In the event of any dissolution or liquidation of Freddie Mac, holders of the Preferred Stock will be entitled to receive, out of any assets available for distribution to stockholders, up to $50 per share plus the dividend for the then-current quarterly dividend period accrued through the liquidation payment date.
Voting Rights	None, except with respect to certain changes in the terms of the Preferred Stock.
Preemptive and Conversion Rights	None.

Use of Proceeds . . . . . To be added to the working capital of Freddie Mac and used for general corporate purposes, including the purchase of residential mortgages and repayment of outstanding debt.

Transfer Agent, Dividend Disbursing Agent and Registrar . . . . . First Chicago Trust Company, New York, New York.

NYSE Listing . . . . . The Preferred Stock has been approved for listing on the New York Stock Exchange (the "NYSE").

SUMMARY SELECTED FINANCIAL DATA

	At or For the Quarter Ended March 31,		At or For the Year Ended December 31,				
	1996	1995	1995	1994	1993	1992	1991
	(dollars in millions, except per share amounts)						
BALANCE SHEET							
Retained portfolio	$117,420	$ 77,313	$107,424	$ 72,828	$ 55,698	$ 33,896	$ 27,046
Total assets	$143,792	$113,625	$137,181	$ 106,199	$ 83,880	$ 59,502	$ 46,860
Primary capital base(1)	$ 6,701	$ 6,075	$ 6,546	$ 5,895	$ 5,197	$ 4,355	$ 3,303
Adjusted total capital base(2)	$ 7,342	$ 7,309	$ 7,179	$ 7,121	$ 6,680	$ 5,813	$ 5,265
MORTGAGE PURCHASE AND FINANCING ACTIVITIES							
Mortgage purchases	$ 36,231	$ 13,400	$ 98,386	$ 124,246	$ 229,706	$ 191,126	$ 99,965
Number of mortgages purchased	338,951	121,115	933,559	1,256,549	2,315,162	1,969,851	1,061,942
Mortgage security settlements(3)	$ 32,741	$ 11,214	$ 85,877	$ 117,110	$ 208,724	$ 179,207	$ 92,479
Mortgage Participation Certificates ("PCs")(4)	$524,327	$492,194	$515,051	$ 491,325	$ 454,906	$ 407,514	$ 359,163
INCOME STATEMENT							
Net interest income on earning assets(5)	$ 387	$ 293	$ 1,298	$ 1,047	$ 808	$ 695	$ 683
Management and guarantee income(5)	$ 305	$ 295	$ 1,185	$ 1,174	$ 1,077	$ 936	$ 792
Net income	$ 301	$ 258	$ 1,091	$ 983	$ 786	$ 622	$ 555
Earnings per common share(6)	$ 1.60	$ 1.34	$ 5.69	$ 5.08	$ 4.07	$ 3.29	$ 3.08
Dividends per common share(6)	$ 0.35	$ 0.30	$ 1.20	$ 1.04	$ 0.88	$ 0.76	$ 0.67
Return on common equity	22%	22%	22%	23%	22%	21%	24%

(1) "Stockholders' equity" and "Reserves for losses on mortgages."
(2) "Primary capital base" and "Subordinated borrowings."
(3) Single-class Mortgage Participation Certificates.
(4) Includes balances of Freddie Mac PCs held in the retained portfolio. Data for 1993 through 1995 have been restated to reflect this revised reporting implemented in first quarter 1996.
(5) Guarantee fee income on mortgages underlying Freddie Mac PCs held in the retained portfolio is no longer included in net interest income on earning assets, but is included in management and guarantee income. Data for 1993 through 1995 have been restated to reflect this revised reporting implemented in first quarter 1996.
(6) In April 1992, Freddie Mac effected a three-for-one split of its Common Stock. All earnings per share and dividends per share amounts have been adjusted retroactively to reflect the three-for-one stock split.

FEDERAL HOME LOAN MORTGAGE CORPORATION

Freddie Mac is a shareholder-owned government-sponsored enterprise ("GSE") chartered on July 24, 1970 pursuant to the Federal Home Loan Mortgage Corporation Act, Title III of the Emergency Home Finance Act of 1970, as amended (the "Freddie Mac Act"). Freddie Mac's statutory purposes are (i) to provide stability in the secondary market for residential mortgages, (ii) to respond appropriately to the private capital market, (iii) to provide ongoing assistance to the secondary market for residential mortgages (including activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities) and (iv) to promote access to mortgage credit throughout the United States (including central cities, rural areas and underserved areas) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing.

The principal activity of Freddie Mac consists of the purchase of first lien, conventional, residential mortgages, including both whole loans and participation interest in such mortgages. Its mortgage purchases are primarily financed by sales of single-class guaranteed mortgage-related securities, primarily various types of mortgage participation certificates ("PCs"). Freddie Mac guarantees the payment of interest due on PCs and the principal of the underlying mortgages. Freddie Mac also finances mortgage purchases with debt securities, other liabilities and equity capital.

Freddie Mac is subject to two primary types of risk in the conduct of its business: credit risk associated with the mortgages it purchases and the institutions with which it does business; and interest-rate risk that principally results from mortgage prepayments that may create mismatches in the Corporation's assets and liabilities associated with its mortgage portfolio. For a discussion of the impact and management of these risks, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management" in the Information Statement.

The principal office of Freddie Mac is in McLean, Virginia. Freddie Mac has regional offices that are primarily responsible for the performance of various marketing activities and quality control procedures. These offices are located in Atlanta, Georgia; Chicago, Illinois; Dallas, Texas; McLean, Virginia; New York, New York and Woodland Hills, California.

A more detailed discussion of the business of the Corporation appears under "Business" in the Information Statement. The preceding description of the business of Freddie Mac is qualified in its entirety by that discussion.

USE OF PROCEEDS

The Corporation will apply the net proceeds from the sale of Preferred Stock to its general funds to be used for general corporate purposes, including the purchase of residential mortgages and the repayment of outstanding indebtedness. The precise amounts and timing of the application of the proceeds will depend upon the funding requirements of the Corporation.

The Corporation engages in financing transactions continuously. The amount and nature of such transactions are dependent upon a number of factors, including the volume of mortgage prepayments and mortgages purchased by the Corporation, as well as general market conditions.

CAPITALIZATION

The following table sets forth the capitalization of the Corporation at March 31, 1996 and as adjusted to reflect the sale of the Preferred Stock offered hereby. This table should be read in conjunction with the financial statements of the Corporation and other information contained in the Information Statement.

	March 31, 1996	
	Actual	As Adjusted(1)
	(dollars in millions)	
Debt Securities:		
Notes and bonds payable due within one year:		
Discount notes, mortgage securities sold under agreements to repurchase, and medium-term notes	$ 56,522	$ 56,522
Current portion of long-term debt	10,531	10,531
	67,053	67,053
Notes and bonds payable due after one year	56,584	56,584
Total debt securities, net	123,637	123,637
Subordinated Borrowings	641	641
Stockholders' Equity:		
Preferred Stock, $1.00 par value and $25.00 liquidation value	35	35
Preferred Stock, $1.00 par value and $50.00 liquidation value	—	5
Common Stock, $0.84 par value	152	152
Additional paid-in capital	910	1,150
Retained earnings	5,107	5,107
Net unrealized gain on securities reported at fair value	16	16
Less: treasury stock, at cost	(208)	(208)
Total stockholders' equity	6,012	6,257
Total Capitalization	$130,290	$130,535

(1) "As adjusted" reflects anticipated proceeds of $250 million from the issuance of 5 million shares of Preferred Stock and the deduction of $5 million in estimated transaction costs. The actual costs may differ.

See Notes 7, 8 and 9 to the 1995 Consolidated Financial Statements included in the Information Statement for further information about Freddie Mac's debt securities, subordinated borrowings and stockholders' equity. Amounts of debt securities and subordinated borrowings are net of unamortized discounts, premiums, hedging gains or losses and debt issuance costs.

The Corporation engages in transactions affecting stockholders' equity (including repurchases of its common stock) from time to time and issues or retires debentures, notes and other debt obligations on an ongoing basis. Accordingly, on any date subsequent to March 31, 1996, stockholders' equity may differ, and the amount of debt obligations outstanding will differ, and may differ substantially, from the figures contained in the capitalization table above.

SELECTED FINANCIAL DATA

The following selected financial data for the years 1991 through 1995 have been summarized or derived from the audited financial statements or the internal accounting records of the Corporation. These data are qualified in their entirety by, and should be read in conjunction with, the detailed information, audited financial statements and notes to financial statements that are presented in the Information Statement. The following selected financial data for the quarters ended March 31, 1996 and March 31, 1995 have been summarized or derived from unaudited financial statements (which are included in Appendix B to this Offering Circular) or from internal accounting records, but in the opinion of management of the Corporation, all adjustments necessary for a fair presentation have been included. Adjustments included herein are of a normal, recurring nature.

	At or For the Quarter Ended March 31,		At or For the Year Ended December 31,				
	1996	1995	1995	1994	1993	1992	1991
			(dollars in millions, except per share amounts)				
Balance Sheet							
Retained portfolio	$117,420	$ 77,313	$107,424	$ 72,828	$ 55,698	$ 33,896	$ 27,046
Total assets	$143,792	$113,625	$137,181	$ 106,199	$ 83,880	$ 59,502	$ 46,860
Debt securities, net	$123,637	$100,439	$119,328	$ 92,053	$ 48,510	$ 28,173	$ 28,300
Total liabilities	$136,753	$106,608	$130,297	$ 99,368	$ 77,406	$ 53,795	$ 41,725
Capital base:							
Stockholders' equity	$ 6,012	$ 5,351	$ 5,863	$ 5,162	$ 4,437	$ 3,570	$ 2,566
Reserves for losses on mortgages(1)	689	724	683	733	760	785	737
Primary capital base	$ 6,701	$ 6,075	$ 6,546	$ 5,895	$ 5,197	$ 4,355	$ 3,303
Subordinated borrowings	641	1,234	633	1,226	1,483	1,458	1,962
Adjusted total capital base	$ 7,342	$ 7,309	$ 7,179	$ 7,121	$ 6,680	$ 5,813	$ 5,265
Mortgage Participation Certificates ("PCs")(2)	$524,327	$492,194	$515,051	$ 491,325	$ 454,906	$ 407,514	$ 359,163
Freddie Mac PCs held in retained portfolio	$ 63,138	$ 33,441	$ 56,006	$ 30,669	$ 15,877	N/A	N/A
Primary capital ratio(3)	1.11%	1.06%	1.10%	1.04%	0.99%	0.93%	0.81%
Adjusted total capital ratio(4)	1.21%	1.28%	1.20%	1.26%	1.28%	1.24%	1.30%
Return on common equity(5)	22%	22%	22%	23%	22%	21%	24%
Return on average assets and average contingencies(6)	0.20%	0.18%	0.19%	0.18%	0.16%	0.14%	0.15%
Mortgage Purchase and Financing Activities							
Mortgage purchases	$ 36,231	$ 13,400	$ 98,386	$ 124,246	$ 229,706	$ 191,126	$ 99,965
Number of mortgages purchased	338,951	121,115	933,559	1,256,549	2,315,162	1,969,851	1,061,942
Mortgage PC settlements:							
Single-class	$ 32,741	$ 11,214	$ 85,877	$ 117,110	$ 208,724	$ 179,207	$ 92,479
Multiclass (REMICs)	$ 5,153	$ 2,956	$ 15,372	$ 73,131	$ 143,336	$ 131,284	$ 72,032
Long-term debt:							
Issued	$ 9,084	$ 6,050	$ 29,643	$ 22,744	$ 24,784	$ 9,660	$ 4,346
Retired	$ (9,784)	(1,312)	(11,082)	(6,462)	(9,924)	(5,159)	(2,652)
Net	$ (700)	$ 4,738	$ 18,561	$ 16,282	$ 14,860	$ 4,501	$ 1,694
Income Statement							
Net interest income on earning assets(7)	$ 387	$ 293	$ 1,298	$ 1,047	$ 808	$ 695	$ 683
Management and guarantee income(7)	$ 305	$ 295	$ 1,185	$ 1,174	$ 1,077	$ 936	$ 792
Income before income taxes	$ 440	$ 375	$ 1,586	$ 1,482	$ 1,128	$ 901	$ 800
Net income	$ 301	$ 258	$ 1,091	$ 983	$ 786	$ 622	$ 555
Earnings per common share(8)	$ 1.60	$ 1.34	$ 5.69	$ 5.08	$ 4.07	$ 3.29	$ 3.08
Weighted average common shares outstanding (in thousands)(8)	178,413	180,760	180,322	180,666	180,421	180,165	180,095
Dividends per common share(8)	$ 0.35	$ 0.30	$ 1.20	$ 1.04	$ 0.88	$ 0.76	$ 0.67
Dividend payout ratio on common stock	21.91%	22.41%	21.09%	20.47%	21.63%	23.14%	21.62%
Ratio of earnings to fixed charges(9)	1.22:1	1.24:1	1.23:1	1.31:1	1.32:1	1.32:1	1.28:1
Ratio of earnings to combined fixed charges and preferred stock dividends(9)	1.21:1	1.23:1	1.22:1	1.30:1	1.30:1	1.30:1	N/A

(1) "Reserve for losses on retained mortgages" and "Reserve for losses on sold mortgages."
(2) Includes balances of Freddie Mac PCs held in the retained portfolio. Data for 1993 through 1995 have been restated to reflect this revised reporting implemented in first quarter 1996.
(3) "Primary capital base" divided by "Total assets" and "PCs" less Freddie Mac PCs held in the retained portfolio.
(4) "Adjusted total capital base" divided by "Total assets" and "PCs" less Freddie Mac PCs held in the retained portfolio.
(5) "Net income" (annualized for the quarterly periods) less preferred stock dividends, divided by the simple average of the beginning and ending balances of "Stockholders' equity," net of par and additional paid-in capital of preferred stock, for the reporting period.
(6) Contingencies consist of PCs, less Freddie Mac's PCs held in the retained portfolio.
(7) Guarantee fee income on mortgages underlying Freddie Mac PCs held in the retained portfolio is no longer included in net interest income on earning assets, but is included in management and guarantee income. Data for 1993 through 1995 have been restated to reflect this revised reporting implemented in first quarter 1996.
(8) In April 1992, Freddie Mac effected a three-for-one split of its Common Stock. All earnings per share and dividends per share amounts and weighted average shares outstanding have been adjusted retroactively to reflect the three-for-one stock split.
(9) Earnings represent consolidated pretax income plus consolidated fixed charges, less interest capitalized. Fixed charges include interest (including amounts capitalized) and the portion of net rental expense deemed representative of interest.

RESULTS OF OPERATIONS

The following is a summary of Freddie Mac's results of operations for the three months ended March 31, 1996, as compared to the three months ended March 31, 1995. For a discussion of Freddie Mac's results of operations for the year ended December 31, 1995, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Information Statement.

Year-to-Date Earnings

Earnings per common share rose 19 percent, from $1.34 for the first quarter of 1995 to $1.60 for the first quarter of 1996. Freddie Mac's net income increased 17 percent, from $258 million in the first quarter of 1995 to $301 million in the first quarter of 1996.

Revenues

Freddie Mac's revenues reached $701 million in the first quarter of 1996 compared with $601 million in the first quarter of 1995, an increase of 17 percent.

Net Interest Income on Earning Assets

Net interest income on earning assets increased from $293 million in the first quarter of 1995 to $387 million in the first quarter of 1996. The $94 million, or 32 percent, increase in net interest income was due to a 32 percent increase in average total earning assets, driven by growth of 52 percent in average retained portfolio balances. The retained portfolio increased by $10 billion during the first quarter of 1996.

Management and Guarantee Income

Management and guarantee income totaled $305 million for the first quarter of 1996 compared to $295 million for the first quarter of 1995. The $10 million increase over the first quarter of 1995 reflects an increase of $30 billion in the average balance of total PCs, partially offset by a 0.6 basis point decrease in the average guarantee fee rate. The increase in the total PC balance reflects the favorable effect of lower interest rates on business volumes during the latter half of 1995 and the first quarter of 1996. Declining mortgage rates during these periods resulted in an increase in refinancing activity and a shift in demand from ARMs toward fixed-rate mortgages, which are less likely than ARMs to be retained in lenders' portfolios. The decrease in the average guarantee fee rate reflects lower rates on new PC issuances than on existing PCs combined with the ongoing liquidation of existing PCs at the comparatively higher fee rates.

Freddie Mac's purchase market share during the first quarter of 1996 was 44 percent, unchanged from the first quarter of 1995.

Other Income, net

Other income, net, totaled $9 million for the first quarter of 1996, compared to $13 million in the first quarter of 1995.

Credit

Total credit-related expenses, consisting of the provision for mortgage losses and REO operations expense, were $156 million in the first quarter of 1996, an increase of 21 percent from $129 million in the first quarter of 1995. Specifically, Freddie Mac increased its provision for mortgage losses to $80 million for the first quarter of 1996, compared to $60 million for the first quarter of 1995. Total mortgage charge-offs increased from $69 million to $74 million. The increases in credit-related expenses and charge-offs were due to continued economic weakness in California and increased loss mitigation activities.

The February 1996 delinquency rate for single-family at-risk mortgages was 0.61 percent, up 6 basis points from March 1995. The February 1996 delinquent multifamily balances were $219 million, down from $248 million at the end of March 1995.

Administrative Expenses

Administrative expenses for the first quarter of 1996 totaled $105 million compared to $97 million in the first quarter of 1995. The ratio of administrative expenses to revenues was 15 percent for the first quarter of 1996, down slightly from 16 percent for the first quarter of 1995. Annualized administrative expenses as a proportion of the average total mortgage portfolio for the first quarter of 1996 remained unchanged from the first quarter of 1995 at 7.3 basis points.

REGULATION AND GOVERNMENTAL RELATIONSHIPS

From time to time, Freddie Mac's statutory, structural and regulatory relationships with the federal government may be subject to review or modification. While Freddie Mac's GSE status is often advantageous for the Corporation, proposals have been advanced that could adversely affect Freddie Mac's fulfillment of its statutory purposes, as well as the Corporation's results of operations. A more detailed discussion of Freddie Mac's regulatory and governmental relationships appears under "Regulation and Governmental Relationships" in the Information Statement.

DESCRIPTION OF PREFERRED STOCK

The description of the Preferred Stock set forth below does not purport to be complete and is qualified in its entirety by the Certificate of Designation, which will be in substantially the form attached as Appendix A.

General

Under §306(f) of the Freddie Mac Act, Freddie Mac is authorized to issue an unlimited number of shares of preferred stock. The shares of Preferred Stock being offered hereby will have a par value of $1.00 per share. The Preferred Stock is created pursuant to the Certificate of Designation.

First Chicago Trust Company, New York, New York, will be the transfer agent, dividend disbursing agent and registrar for the Preferred Stock.

Authorized Issuance

Freddie Mac has been authorized by its Board of Directors to issue the 5,000,000 shares of Preferred Stock offered hereby. The Board of Directors may increase the authorized number of shares at any time, without the consent of the holders of Preferred Stock.

Dividends

Dividends on shares of the Preferred Stock will not be mandatory. Holders of Preferred Stock will be entitled to receive non-cumulative, quarterly cash dividends which will accrue from but not including April 26, 1996 and will be payable on March 31, June 30, September 30 and December 31 of each year (each, a "Dividend Payment Date"), commencing June 30, 1996 when, as and if declared by the Board of Directors in its sole discretion, out of funds legally available therefor. Dividends will accrue at a variable per annum rate (not greater than 9% per annum) equal to (a) the sum of LIBOR, determined quarterly as described under "Determination of LIBOR," and 1.0%, divided by (b) 1.377, with the resulting dividend per share being rounded to the nearest cent (with one-half cent rounded up). If a Dividend Payment Date is not a "Business Day," the related dividend will be paid on the next Business Day with the same force and effect as though paid on the Dividend Payment Date, without any increase to account for the period from such Dividend Payment Date through the date of actual payment. For these purposes, "Business Day" means a day other than (i) a Saturday or a Sunday, (ii) a day on which New York City banks are closed or (iii) a day on which the offices of Freddie Mac are closed. Dividends will be paid to holders of record on the record date fixed by the Board of Directors, not to be earlier than 45 days or later than 10 days preceding the applicable Dividend Payment Date. If declared, the initial dividend, which will be for the period from but not including April 26, 1996 through and including June 30, 1996, will be 4.7091% or $.43 per share and will be payable on July 1, 1996. Thereafter, the

dividend payable to holders of Preferred Stock will vary from Dividend Period to Dividend Period. The "Dividend Period" relating to a Dividend Payment Date will be the period from but not including the preceding Dividend Payment Date through and including the related Dividend Payment Date. Freddie Mac will calculate the dividend rate for each Dividend Period based on LIBOR determined as of two London Business Days (defined as any day, other than a Saturday or Sunday, on which banks are open for business in London) prior to the first day of such Dividend Period (each, a "Determination Date"). Each dividend will be calculated on the basis of the actual number of days elapsed, assuming a year of 360 days, and the dividend rate will be applied to the $50 per share redemption value.

The Preferred Stock will rank prior to the Voting Common Stock, par value $0.84 per share, of Freddie Mac (the "Common Stock") with respect to dividends, to the extent provided in the Certificate of Designation. No dividend may be declared or paid or set apart for payment on the Common Stock (or any other junior stock) unless dividends have been declared and paid or set apart (or ordered to be set apart) on the Preferred Stock in respect to the then-current Dividend Period. The Preferred Stock will rank on a parity with the 6.72% Non-Cumulative Preferred Stock (the "1993 Preferred Stock") issued on August 2, 1993 and currently outstanding and the 7.90% Non-Cumulative Preferred Stock (the "1992 Preferred Stock") issued on April 27, 1992 and currently outstanding (together, the "Existing Preferred Stock") with respect to dividends.

Dividends on the Preferred Stock will not be cumulative. If a dividend is not paid on the Preferred Stock, the holders of the Preferred Stock will have no claim in respect of such non-payment so long as no dividend is paid on the Common Stock (or any other junior stock) or the Existing Preferred Stock for the then-current period.

The Board of Directors may, in its discretion, choose to pay dividends on the Preferred Stock without the payment of any dividends on the Common Stock.

No dividends will be declared or paid or set apart for payment on any shares of the Preferred Stock if at the same time any arrears or default exists in the payment of dividends on any outstanding class or series of stock of Freddie Mac ranking prior to the Preferred Stock with respect to the payment of dividends. At the time of issuance of the Preferred Stock, no class or series of stock of Freddie Mac ranking prior to the Preferred Stock will exist.

Holders of shares of the Preferred Stock will not be entitled to any dividends, whether payable in cash or property, other than as described above and will not be entitled to interest, or any sum in lieu of interest, in respect of any dividend payment. See "Regulatory Matters" for a description of possible regulatory restrictions on Freddie Mac's payment of dividends.

Changes in the Dividends-Received Percentage

If, prior to April 26, 1998, one or more amendments to the Code are enacted that reduce the percentage of the dividends-received deduction (currently 70 percent) as specified in section 243(a)(1) of the Code or any successor provision (the "Dividends-Received Percentage"), certain adjustments may be made in respect of the dividends payable by the Corporation, and Post Declaration Date Dividends and Retroactive Dividends (as such terms are defined below) may become payable, as described below.

The amount of each dividend payable (if declared) per share of Preferred Stock for dividend payments made on or after the effective date of such change in the Code will be adjusted by multiplying the amount of the dividend payable described above under "Dividends" (before adjustment) by a factor, which will be the number determined in accordance with the following formula (the "DRD Formula"), and rounding the result to the nearest cent (with one-half cent rounded up):

$$\frac{1-.35(1-.70)}{1-.35(1-DRP)}$$

For the purposes of the DRD Formula, "DRP" means the Dividends-Received Percentage (expressed as a decimal) applicable to the dividend in question; *provided, however,* that if the Dividends-Received

Percentage applicable to the dividend in question is less than 50%, then the DRP will equal .50. If the amount of any dividend payable on the Preferred Stock is adjusted through such application of the DRD Formula, the resulting dividend rate may exceed 9% per annum. No amendment to the Code, other than a change in the percentage of the dividends-received deduction set forth in section 243(a)(1) of the Code or any successor provision, will give rise to an adjustment. Notwithstanding the foregoing provisions, if, with respect to any such amendment, the Corporation receives either an unqualified opinion of nationally recognized independent tax counsel selected by the Corporation or a private letter ruling or similar form of assurance from the Internal Revenue Service (the "IRS") to the effect that such an amendment does not apply to a dividend payable on the Preferred Stock, then such amendment will not result in the adjustment provided for pursuant to the DRD Formula with respect to such dividend. The opinion referenced in the previous sentence must be based upon the legislation amending or establishing the DRP or upon a published pronouncement of the IRS addressing such legislation. Unless the context otherwise requires, references to dividends in this Offering Circular will mean dividends as adjusted by the DRD Formula. The Corporation's calculation of the dividends payable as so adjusted shall be final and not subject to review.

Notwithstanding the foregoing, if any such amendment to the Code is enacted after the dividend payable on a Dividend Payment Date has been declared but before such dividend is paid, the amount of the dividend payable on such Dividend Payment Date will not be increased; instead, additional dividends (the "Post Declaration Date Dividends"), equal to the excess, if any, of (x) the product of the dividend paid by the Corporation on such Dividend Payment Date and the DRD Formula (where the DRP used in the DRD Formula would be equal to the greater of the Dividends-Received Percentage applicable to the dividend in question and .50) over (y) the dividend paid by the Corporation on such Dividend Payment Date, will be payable (if declared) to holders of Preferred Stock on the record date applicable to the next succeeding Dividend Payment Date, in addition to any other amounts payable on such date.

If any such amendment to the Code is enacted and the reduction in the Dividends-Received Percentage retroactively applies to a Dividend Payment Date as to which the Corporation previously paid dividends on the Preferred Stock (each, an "Affected Dividend Payment Date"), the Corporation will pay (if declared) additional dividends (the "Retroactive Dividends") to holders of Preferred Stock on the record date applicable to the next succeeding Dividend Payment Date (or, if such amendment is enacted after the dividend payable on such Dividend Payment Date has been declared, to Holders of Preferred Stock on the record date applicable to the second succeeding Dividend Payment Date following the date of enactment) in an amount equal to the excess of (x) the product of the dividend paid by the Corporation on each Affected Dividend Payment Date and the DRD Formula (where the DRP used in the DRD Formula would be equal to the greater of the Dividends-Received Percentage and .50 applied to each Affected Dividend Payment Date) over (y) the sum of the dividend paid by the Corporation on each Affected Dividend Payment Date. The Corporation will make only one payment of Retroactive Dividends for any such amendment. Notwithstanding the foregoing provisions, if, with respect to any such amendment, the Corporation receives either an unqualified opinion of nationally recognized independent tax counsel selected by the Corporation or a private letter ruling or similar form of assurance from the IRS to the effect that such amendment does not apply to a dividend payable on an Affected Dividend Payment Date for the Preferred Stock, then such amendment will not result in the payment of Retroactive Dividends with respect to such Affected Dividend Payment Date. The opinion referenced in the previous sentence must be based upon the legislation amending or establishing the DRP or upon a published pronouncement of the IRS addressing such legislation.

Notwithstanding the foregoing, no adjustment in the dividends payable by the Corporation will be made, and no Post Declaration Date Dividends or Retroactive Dividends will be payable by the Corporation, in respect of the enactment of any amendment to the Code on or after April 26, 1998.

In the event that the amount of dividends payable per share of the Preferred Stock is adjusted pursuant to the DRD Formula and/or Post Declaration Date Dividends or Retroactive Dividends are to be paid, the Corporation will give notice of each such adjustment and, if applicable, any Post Declaration Date Dividends and Retroactive Dividends to the holders of Preferred Stock.

See "Certain Federal Income Tax Consequences — Dividends — Recent Proposals" for a discussion of certain proposals to reduce the Dividends-Received Percentage.

Determination of LIBOR

"LIBOR" means, with respect to a Dividend Period relating to a Dividend Payment Date (in the following order of priority):

(i) the rate (expressed as a percentage per annum) for Eurodollar deposits having a three-month maturity that appears on Telerate Page 3750 as of 11:00 a.m. (London time) on the related Determination Date;

(ii) if such rate does not appear on Telerate Page 3750 as of 11:00 a.m. (London time) on the related Determination Date, LIBOR will be the arithmetic mean (if necessary rounded upwards to the nearest whole multiple of 1/128%) of the rates (expressed as percentages per annum) for Eurodollar deposits having a three-month maturity that appear on Reuters Monitor Money Rates Page LIBO ("Reuters Page LIBO") as of 11:00 a.m. (London time) on such Determination Date;

(iii) if such rate does not appear on Reuters Page LIBO as of 11:00 a.m. (London time) on the related Determination Date, Freddie Mac will request the principal London offices of four leading banks in the London interbank market to provide such banks' offered quotations (expressed as percentages per annum) to prime banks in the London interbank market for Eurodollar deposits having a three-month maturity as of 11:00 a.m. (London time) on such Determination Date. If at least two quotations are provided, LIBOR will be the arithmetic mean (if necessary rounded upwards to the nearest whole multiple of 1/128%) of such quotations;

(iv) if fewer than two such quotations are provided as requested in clause (iii) above, Freddie Mac will request four major New York City banks to provide such banks' offered quotations (expressed as percentages per annum) to leading European banks for loans in Eurodollars as of 11:00 a.m. (London time) on such Determination Date. If at least two such quotations are provided, LIBOR will be the arithmetic mean (if necessary rounded upwards to the nearest whole multiple of 1/128%) of such quotations; and

(v) if fewer than two such quotations are provided as requested in clause (iv) above, LIBOR will be LIBOR determined with respect to the Dividend Period immediately preceding such current Dividend Period.

If the rate for Eurodollar deposits having a three-month maturity that initially appears on Telerate Page 3750 or Reuters Page LIBO, as the case may be, as of 11:00 a.m. (London time) on the related Determination Date is superseded on Telerate Page 3750 or Reuters Page LIBO, as the case may be, by a corrected rate before 12:00 noon (London time) on such Determination Date, the corrected rate as so substituted on the applicable page will be the applicable LIBOR for such Determination Date.

Absent manifest error, Freddie Mac's determination of LIBOR and its calculation of the applicable dividend rate for each Dividend Period will be final and binding. Investors may obtain the dividend rates for the current and preceding Dividend Periods by writing or calling the Investor Inquiry Department at Freddie Mac at 8200 Jones Branch Drive, McLean, Virginia 22102 (outside Washington, D.C. metropolitan area, phone 800/336-FMPC; within Washington, D.C. metropolitan area, phone 703/450-3777).

Optional Redemption

The Preferred Stock will not be redeemable prior to June 30, 2001. On or after that date and subject to any further limitations which may be imposed by law, Freddie Mac may redeem the Preferred Stock, in whole or in part, at any time or from time to time, out of funds legally available

therefor, at the redemption price of $50.00 per share plus an amount equal to the dividend (calculated as provided in the Certificate of Designation) for the then-current Dividend Period accrued through and including the date of such redemption. If less than all of the outstanding shares of the Preferred Stock are to be redeemed, Freddie Mac will select shares to be redeemed from the outstanding shares not previously called for redemption by lot or pro rata (as nearly as possible) or by any other method which Freddie Mac in its sole discretion deems equitable.

Freddie Mac will give notice of any such redemption by mail to holders of the Preferred Stock not less than 30 days and not more than 60 days prior to the date fixed by the Board of Directors for such redemption. Each such notice will state the number of shares of Preferred Stock being redeemed, the redemption price, the redemption date and the place at which a holder's certificate(s) representing shares of the Preferred Stock must be presented upon such redemption.

See "Regulatory Matters" for a description of possible regulatory restrictions on Freddie Mac's redemption of the Preferred Stock.

From and after the redemption date, the shares of Preferred Stock called for redemption will no longer be deemed outstanding, and all rights of the holders thereof as holders of the Preferred Stock will cease.

Regulatory Matters

Neither Freddie Mac's right to declare dividends on nor its right to redeem the Preferred Stock is currently subject to prior regulatory approval. Under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the "GSE Act"), the exercise of these rights may be subject to regulatory approval only if the Corporation fails to meet applicable capital standards.

The GSE Act established minimum capital, critical capital and risk-based capital standards for the Corporation.

The GSE Act has required the Corporation to maintain "core capital" in an amount that equals or exceeds the levels established under the minimum and critical capital standards since the GSE Act was enacted. The Director (the "Director") of the Office of Federal Housing Enterprise Oversight ("OFHEO") has issued a proposed minimum capital regulation that interprets the minimum capital standard and that proposes to implement a calculation methodology that is similar to the methodology OFHEO has applied on an interim basis since the GSE Act was enacted. The Director has stated that a final minimum capital regulation will be issued in 1996.

The GSE Act does not require the Corporation to maintain "total capital" at a level that equals or exceeds the risk-based capital standard until the Director issues a final risk-based capital regulation establishing the risk-based capital stress test (and the risk-based capital level cannot be determined from the GSE Act alone). The Director has stated that OFHEO expects to publish for comment in 1996 and 1997 a proposed regulation, in two parts, establishing the risk-based capital test, and subsequently to issue a final risk-based capital regulation. The final risk-based capital regulation becomes effective when issued but, until the risk-based capital regulation has been in effect for one year, the Director must base any determination of the Corporation's capital adequacy solely on whether the core capital of the Corporation is equal to or exceeds the minimum and critical capital levels.

Subject to the applicability of the risk-based capital standard described above, the Corporation may pay a dividend without prior OFHEO approval if the payment would not decrease the total capital of the Corporation to an amount less than the risk-based capital level for the Corporation and would not decrease the core capital level to an amount less than the minimum capital level for the Corporation. Beginning one year after the final risk-based capital regulation is issued, if the Corporation's total capital is less than the risk-based capital level, but its core capital equals or exceeds the minimum capital level, the Corporation is prohibited from making a dividend payment that would decrease its core capital to an amount less than the minimum capital level. At any time, if the Corporation's core capital is less than the minimum capital level, the Corporation may make a dividend payment only if the Director determines that the dividend payment satisfies certain statutory standards and if the Director

approves the payment, and under these circumstances the Corporation is prohibited from making any dividend payment that would decrease the Corporation's core capital to less than the critical capital level.

In addition to the preceding requirements that relate directly to the payment of dividends, the Director has authority, under certain conditions, to require the Corporation to submit for the Director's approval a capital restoration plan or to restrict the Corporation's activities, either of which also could affect the payment of dividends. Specifically if the Director determines, after the risk-based capital regulation has been in effect for one year, that the Corporation fails to meet the risk-based capital standard, or if the Director determines, at any time, that the Corporation fails to meet the minimum capital standard, the Corporation will be required to submit for the Director's approval a capital restoration plan setting forth a feasible plan for restoring the Corporation's capital level. In addition, if the Corporation at any time fails to meet the minimum capital standard, the Director is authorized to impose various limitations on the Corporation's activities. If, at any time, the Director determines that the Corporation fails to meet the critical capital standard, the Director must appoint a conservator for the Corporation.

If the Director does not approve a required capital restoration plan or determines that the Corporation has failed to make reasonable efforts to comply with such a plan, then the Director may treat the Corporation as not meeting capital standards that it otherwise meets and take the actions authorized when the Corporation does not meet such standards. Similarly, if the Director determines that the Corporation is engaging in conduct not approved by the Director that could result in a rapid depletion of core capital or that the value of the property subject to mortgages held or securitized by the Corporation has decreased significantly, the Director is authorized to treat the Corporation as not meeting capital standards that it otherwise meets.

If the Corporation fails to meet or is treated by the Director as not meeting applicable capital standards and the Director has reasonable cause to believe that the Corporation or any executive officer or director of the Corporation is engaging in or about to engage in any conduct (which could include the payment of dividends) that threatens to result in a material depletion of the Corporation's core capital, then the Director is authorized to commence proceedings pursuant to which, after a hearing, the Director could issue a cease and desist order prohibiting such conduct. If the Director determines that the conduct in question is likely to cause a significant depletion of core capital, the Director can issue such an order without a hearing, which would be effective until completion of the cease-and-desist proceedings, and can do so without regard to whether the Corporation meets all applicable capital standards.

The Director has the authority to require the Corporation to submit a report to the Director regarding any capital distribution (including any dividend) declared by the Corporation before the Corporation makes the distribution.

The foregoing discussion with respect to the payment of dividends is equally applicable to Freddie Mac's redemption of the Preferred Stock and is based on Freddie Mac's understanding and interpretations of the relevant provisions of the GSE Act. OFHEO has not yet issued any definitive guidance as to its interpretations of these provisions of the Act. Until OFHEO has provided such guidance, there can be no assurance that the foregoing discussion will be consistent with OFHEO's interpretation in every respect. A more detailed discussion of the regulatory oversight of Freddie Mac's capitalization and the terms used above appears under "Regulation and Governmental Relationships — Regulation of Freddie Mac — OFHEO Oversight" in the Information Statement.

No Preemptive Rights and No Conversion

No holder of the Preferred Stock will have any preemptive right to purchase or subscribe for any other shares, rights, options or other securities of any class of Freddie Mac which at any time may be sold or offered for sale by Freddie Mac. The holders of shares of Preferred Stock will not have any right to convert such shares into or exchange such shares for any other class or series of stock or obligations of Freddie Mac.

No Voting Rights

Section 306(f) of the Freddie Mac Act prohibits the holders of Preferred Stock from voting with respect to the election of any member of the Board of Directors. Except as set forth under "Amendments" below, the holders of the Preferred Stock will not be entitled to vote.

Liquidation Rights

Upon any voluntary or involuntary dissolution, liquidation or winding up of Freddie Mac, after payment or provision for the liabilities of Freddie Mac and the expenses of such dissolution, liquidation or winding up, the holders of the outstanding shares of the Preferred Stock will be entitled to receive out of the assets of Freddie Mac available for distribution to stockholders, before any payment or distribution is made on the Common Stock (or any other junior stock), the amount of $50.00 per share plus an amount equal to the dividend (calculated as provided in the Certificate of Designation) for the then-current quarterly Dividend Period accrued through and including the date of such liquidation payment. In the event of the dissolution, liquidation or winding up of Freddie Mac, the rights of the Preferred Stock are on a parity with those of the Existing Preferred Stock. If the assets of Freddie Mac available for distribution in such event are insufficient to pay in full the aggregate amount payable to holders of the Preferred Stock, the Existing Preferred Stock and any other class or series of stock ranking on a parity upon liquidation with the Preferred Stock and the Existing Preferred Stock, the assets will be distributed to the holders of Preferred Stock, the Existing Preferred Stock and such parity stock pro rata, based on the amounts to which they are entitled.

Nothwithstanding the foregoing, holders of the Preferred Stock will not be entitled to be paid any amount in respect of a dissolution, liquidation or winding up of Freddie Mac until holders of any classes or series of stock of Freddie Mac ranking prior to the Preferred Stock upon liquidation have been paid all amounts to which such classes or series are entitled.

A consolidation, merger or combination of Freddie Mac with or into any other corporation or entity, or the sale of all or substantially all of the property or business of Freddie Mac, will not be deemed to be a liquidation, dissolution or winding up of Freddie Mac for purposes of these provisions on liquidation rights.

Additional Classes or Series of Stock

Freddie Mac will have the right to create and issue additional classes or series of stock ranking prior to, on a parity with or junior to the Preferred Stock, as to dividends, liquidation or otherwise, without the consent of holders of the Preferred Stock.

Amendments

Without the consent of the holders of the Preferred Stock, Freddie Mac will have the right to amend, alter, supplement or repeal any terms of the Preferred Stock to cure any ambiguity, to correct or supplement any term which may be defective or inconsistent with any other term or to make any other provisions so long as such action does not materially and adversely affect the interests of the holders of the Preferred Stock. Otherwise, the terms of the Preferred Stock may be amended, altered, supplemented or repealed only with the consent of the holders of at least two-thirds of the outstanding shares of Preferred Stock. On matters requiring their consent, holders of the Preferred Stock will be entitled to one vote per share.

NYSE Listing

The Preferred Stock has been approved for listing on the NYSE. The NYSE symbol for the Preferred Stock is FREprB.

CERTAIN FEDERAL INCOME TAX CONSEQUENCES

The Preferred Stock and payments thereon are generally subject to taxation by the United States and other taxing jurisidictions to the same extent and in the same manner as stock of and payments thereon by any other corporation. The following discussion addresses some of the U.S. federal income tax consequences that may result from ownership of the Preferred Stock by a U.S. person who holds the Preferred Stock as a capital asset. For this purpose, a U.S. person is an individual who is a citizen or resident of the United States for federal income tax purposes, a corporation, partnership or other type of entity organized under the laws of the United States or any political subdivision thereof, or an estate or trust the income of which, regardless of its source, is subject to U.S. federal taxation. This discussion does not purport to address all rules which may apply to particular investors. Investors are encouraged to consult their own tax advisors regarding the federal, state, local and foreign tax considerations applicable to an investment in the Preferred Stock.

This discussion reflects current federal income tax laws and regulations and administrative and judicial interpretations thereof. Changes to any of these subsequent to the date of this Offering Circular may affect the tax consequences described herein.

Dividends

Current Law

Distributions on the Preferred Stock which are paid out of current earnings and profits, or earnings and profits accumulated after 1984, generally constitute dividends taxable as ordinary income. To the extent that the amount of any distribution paid on a share of Preferred Stock exceeds the current or accumulated earnings and profits for federal income tax purposes attributable to that share, such excess will be treated first as a return of capital (rather than as ordinary income) and will be applied against and reduce the holder's adjusted tax basis in that share of Preferred Stock. Any such amount in excess of the holder's adjusted tax basis will then be taxed as capital gain. For purposes of the remainder of this discussion, it is assumed that dividends paid with respect to the Preferred Stock will constitute dividends for U.S. federal income tax purposes.

Dividends received by corporations generally will be eligible for the dividends-received deduction. The dividends-received deduction is available only with respect to a dividend received on stock held for more than 45 days (or more than 90 days in the case of a dividend on preferred stock attributable to periods aggregating in excess of 366 days), including the day of disposition, but excluding the day of acquisition or any day which is more than 45 days (or 90 days) after the date on which the Preferred Stock becomes ex-dividend. The length of time that a corporate shareholder is deemed to have held stock for these purposes is reduced for periods during which the shareholder's risk of loss with respect to the stock is diminished by reason of the existence of certain options, contracts to sell, short sales or other similar transactions. The amount of such deduction generally will equal 70 percent of the amount of the dividends received, subject to reduction in certain events, including where a holder has indebtedness outstanding that is directly attributable to an investment in the Preferred Stock. For this purpose, indebtedness of a depository institution attributable to deposits received in the ordinary course of its business is not treated as indebtedness directly attributable to an investment in the Preferred Stock.

For purposes of the corporate alternative minimum tax, alternative minimum taxable income is increased by 75 percent of the amount by which a corporation's adjusted current earnings exceeds its alternative minimum taxable income prior to the addition of the applicable tax preference item. The amount of any dividend that is included in a corporate shareholder's adjusted current earnings will not be reduced by any dividends-received deduction otherwise allowable with respect to that dividend.

Recent Proposals

On March 19, 1996, the Clinton Administration submitted to Congress a proposed fiscal 1997 budget. This proposed budget contains certain tax proposals (the "Proposals") which, if enacted, could adversely affect holders of the Preferred Stock.

Under the Proposals, the 70-percent dividends-received deduction generally available to corporate shareholders, as discussed above under "Current Law," would be reduced from 70 percent to 50 percent for dividends received or accrued after the thirtieth day after the date of enactment of the provision. If this provision or a similar provision is enacted prior to April 26, 1998, the amount of dividends payable per share of Preferred Stock will be adjusted as discussed above under "Description of Preferred Stock — Changes in the Dividends-Received Percentage." Additionally, the Proposals would change the holding period required for eligibility for the dividends-received deduction, effective for dividends received or accrued after the thirtieth day after the date of enactment. The holder would be required to hold the stock for at least 46 days during the 90-day period beginning on the date that is 45 days before the date on which the shares become ex-dividend with respect to such dividend. In the case of a dividend on preferred stock attributable to periods aggregating in excess of 366 days, the shares must have been held for at least 91 days during the 180-day period beginning on the date that is 90 days before the ex-dividend date.

It is impossible to predict whether the Proposals will be enacted either in their current form or in some other form.

Dispositions, Including Redemptions

Any sale, exchange, redemption (except as discussed below) or other disposition of the Preferred Stock generally will result in taxable gain or loss equal to the difference between the amount received and the shareholder's adjusted tax basis in the Preferred Stock. Such gain or loss generally will be capital gain or loss and will be long-term capital gain or loss if the holding period for the Preferred Stock exceeds one year.

A redemption of Preferred Stock may be treated as a dividend, rather than as payment in exchange for the Preferred Stock, unless the redemption is "not essentially equivalent to a dividend" with respect to the holder within the meaning of section 302(b)(1) of the Code. In applying this standard, the holder must take into account not only the Preferred Stock and other stock of Freddie Mac that it owns directly, but also the Preferred Stock and other stock of Freddie Mac that it constructively owns within the meaning of section 318 of the Code. A redemption payment made to a holder will be "not essentially equivalent to a dividend" if it results in a "meaningful reduction" in the holder's aggregate stock interest in Freddie Mac. Because of the ambiguities in applying this rule, each holder should consult its tax advisor to determine whether a redemption of Preferred Stock will be treated as a dividend or as payment in exchange for the Preferred Stock. If the redemption payment is treated as a dividend, the rules discussed above under "Dividends" apply.

Information Reporting and Backup Withholding

Payments of dividends on shares of Preferred Stock held of record by U.S. persons other than corporations and other exempt holders are required to be reported to the IRS.

Backup withholding of U.S. federal income tax at a rate of 31 percent may apply to payments made with respect to shares of Preferred Stock, as well as payments of proceeds from the sale of shares of Preferred Stock, to holders that are not "exempt recipients" and that fail to provide certain identifying information (such as the taxpayer identification number of the holder) in the manner required. Individuals generally are not exempt recipients, whereas corporations and certain other entities generally are exempt recipients.

LEGALITY OF INVESTMENT

National banks may deal in, underwrite and purchase for their own accounts the shares of Preferred Stock without regard to limitations generally applicable to investment securities. 12 U.S.C. §24, seventh paragraph. The Preferred Stock is subject to a 100% risk weighting for capital adequacy purposes. Office of the Comptroller of the Currency, Interpretive Letter No. 581, Federal Banking Law Reporter, 1992-1993 Transfer Binder ¶83,402 (April 6, 1992).

Federal savings associations and federal savings banks may invest in the shares of Preferred Stock without regard to limitations generally applicable to investments. 12 U.S.C. §1464(c)(1)(E). Preferred Stock held by a federal savings association or federal savings bank is subject to a 100% risk weighting for capital adequacy purposes. 12 C.F.R. §567.6(a)(1)(iv)(T).

Federally insured state-chartered banks, state-chartered banks which are members of the Federal Reserve System, and federally insured state-chartered savings banks and state-chartered savings and loan associations may invest in the shares of Preferred Stock to the extent permitted by SMMEA (as defined below) and by applicable state law, after complying with any procedures imposed by the state. Preferred Stock held by such an institution is subject to a 100% risk weighting for federal capital adequacy purposes. 12 C.F.R. Part 325, Appendix A; 12 C.F.R. Part 208, Appendix A; 12 C.F.R. §567.6(a)(1)(iv)(T).

Federal credit unions may purchase the shares of Preferred Stock without regard to limitations generally applicable to investments. 12 U.S.C. §1757(7)(E).

The shares of Preferred Stock are "stock . . . of a corporation which is an instrumentality of the United States" within the meaning of §7701(a)(19)(C)(ii) of the Internal Revenue Code of 1986 for purposes of the 60 percent of assets limitation applicable to domestic building and loan associations.

In addition to the specific authorizations discussed above, §106 of the Secondary Mortgage Market Enhancement Act of 1984 ("SMMEA") provides that any person, trust, corporation, partnership, association, business trust or business entity created pursuant to or existing under the laws of the United States or any state (including the District of Columbia and Puerto Rico) is authorized to purchase, hold and invest in securities issued or guaranteed by Freddie Mac (including the shares of Preferred Stock) to the same extent that the investor is authorized to purchase, hold or invest in obligations issued or guaranteed as to principal and interest by the United States or any agency or instrumentality thereof. Prior to October 4, 1991, states were authorized by SMMEA to enact legislation which specifically referred to §106 and either prohibited or limited an investor's authority to purchase, hold or invest in securities issued or guaranteed by Freddie Mac. 15 U.S.C. §77r-1. To the best of Freddie Mac's knowledge, 18 states currently have legislation limiting to varying extents the ability of certain entities (in most cases, insurance companies) to invest in securities issued or guaranteed by Freddie Mac, including the shares of Preferred Stock.

Notwithstanding the preceding paragraphs, investors should consult their legal advisors to determine whether and to what extent the shares of Preferred Stock constitute legal investments for such investors or are eligible to be used as security for borrowings. The foregoing does not take into consideration the application of statutes, regulations, orders, guidelines or agreements generally governing investments made by a particular investor, including but not limited to "prudent investor" provisions, safety and soundness conditions and percentage-of-assets limits. The regulatory authorities that administer the statutes or regulations discussed or referred to above generally reserve discretion whether securities, such as the Preferred Stock, that are otherwise acceptable for investment may be purchased or pledged by the institutions subject to their jurisdiction. An institution under the jurisdiction of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of Thrift Supervision, the National Credit Union Administration, the Department of the Treasury or any other federal or state agency with similar authority should review any applicable regulations, policy statements and guidelines before purchasing the Preferred Stock.

UNDERWRITING

Subject to the terms and conditions set forth in an underwriting agreement (the "Underwriting Agreement"), the Corporation has agreed to sell to each of the Underwriters named below, and each of the Underwriters, for whom Goldman, Sachs & Co., Bear, Stearns & Co. Inc. and Salomon Brothers Inc are acting as representatives (the "Representatives"), has severally agreed to purchase from the Corporation the respective number of shares of Preferred Stock set forth opposite its name below.

Underwriter	Number of Shares of Preferred Stock
Goldman, Sachs & Co.	950,000
Bear, Stearns & Co. Inc.	950,000
Salomon Brothers Inc	950,000
Lehman Brothers Inc.	200,000
Merrill Lynch, Pierce, Fenner & Smith Incorporated	200,000
Morgan Stanley & Co. Incorporated	200,000
Oppenheimer & Co., Inc.	200,000
PaineWebber Incorporated	200,000
Prudential Securities Incorporated	200,000
Smith Barney Inc.	200,000
Blaylock & Partners L.P.	62,500
J.C. Bradford & Co.	62,500
Craigie Incorporated	62,500
A.G. Edwards & Sons, Inc.	62,500
Interstate/Johnson Lane Corporation	62,500
McDonald & Company Securities, Inc.	62,500
Morgan Keegan & Company, Inc.	62,500
Piper Jaffray Inc.	62,500
Pryor, McClendon, Counts & Co., Inc.	62,500
Redwood Securities Group, Inc.	62,500
Muriel Siebert & Co., Inc.	62,500
Wheat, First Securities, Inc.	62,500
Total	5,000,000

Under the terms of the Underwriting Agreement, the several Underwriters are committed to take and pay for all of the shares of Preferred Stock offered hereby, if any are taken.

The Underwriters propose to offer the Preferred Stock in part directly to the public at the initial offering price set forth on the cover page of this Offering Circular and in part to certain dealers at such price less a concession not in excess of $.60 per share. The Underwriters may allow, and such dealers may reallow, a concession not in excess of $.30 per share on sales to certain brokers and dealers. After the shares of Preferred Stock are released for sale to the public, the offering price and other selling terms may from time to time be varied by the representatives.

The Corporation has granted the Underwriters an option exercisable for 30 days after the date of this Offering Circular to purchase up to an aggregate of 500,000 additional shares of Preferred Stock solely to cover overallotments, if any. If the Underwriters exercise their overallotment option, the Underwriters have severally agreed, subject to certain conditions, to purchase approximately the same percentage thereof that the number of shares to be purchased by each of them, as shown in the foregoing table, bears to the 5,000,000 shares of Preferred Stock offered.

Prior to this offering, there has been no public market for the Preferred Stock. The Preferred Stock has been approved for listing on the NYSE. Trading of the Preferred Stock on the NYSE is expected to commence within a fourteen-day period after the initial delivery of the Preferred Stock. The Representatives have advised the Corporation that they intend to make a market in the Preferred Stock prior to the commencement of trading on the NYSE, but are not obliged to do so and may discontinue any such market making at any time without notice.

The Corporation has agreed to indemnify the Underwriters against certain liabilities in connection with the offering and sale of the Preferred Stock.

Certain of the Underwriters, dealers or agents may engage in transactions with, and perform services for, the Corporation in the ordinary course of business.

INDEPENDENT PUBLIC ACCOUNTANTS

The Consolidated Financial Statements of the Corporation included in the Information Statement, have been audited by Arthur Andersen LLP, independent public accountants, as indicated in their report with respect thereto.

LEGAL MATTERS

The validity of the Preferred Stock will be passed upon for the Corporation by Maud Mater, Esq., Senior Vice President-General Counsel and Secretary of the Corporation. As of March 31, 1996, Ms. Mater was the beneficial owner of 14,107 shares of Common Stock and options covering an additional 26,110 shares of Common Stock. Ms. Mater has been nominated to fill a vacancy on Freddie Mac's Board of Directors until an external candidate is identified for recommendation for election at the Annual Shareholders' Meeting or substitution by the Board of Directors. Certain legal matters relating to the Preferred Stock will be passed upon for the Underwriters by Cleary, Gottlieb, Steen & Hamilton. Certain federal income tax consequences of the Preferred Stock will be passed upon for Freddie Mac by Cadwalader, Wickersham & Taft.

FEDERAL HOME LOAN MORTGAGE CORPORATION

CERTIFICATE OF CREATION, DESIGNATION, POWERS, PREFERENCES, RIGHTS, PRIVILEGES, QUALIFICATIONS, LIMITATIONS, RESTRICTIONS, TERMS AND CONDITIONS

of

VARIABLE RATE, NON-CUMULATIVE PREFERRED STOCK (Par Value $1.00 Per Share)

KNOW ALL PERSONS BY THESE PRESENTS, that I, MAUD MATER, Secretary of the Federal Home Loan Mortgage Corporation, a government-sponsored enterprise of the United States of America ("Freddie Mac"), do hereby certify that, pursuant to authority vested in the Board of Directors of Freddie Mac by Section 306(f) of the Federal Home Loan Mortgage Corporation Act, as amended (12 U.S.C. §1455(f)), said Board of Directors on March 1, 1996, adopted the following resolution, effective as of the close of business on April 23, 1996, on which date, pursuant to FHLMC Resolution 96-05, the Chairman and Chief Executive Officer approved the final terms of the public issuance and sale of the preferred stock of Freddie Mac designated above, which resolution is now, and at all times since such date has been, in full force and effect:

RESOLVED, that, the Variable Rate, Non-Cumulative Preferred Stock shall have the following designation, powers, preferences, rights, privileges, qualifications, limitations, restrictions, terms and conditions:

1. Designation, Par Value, Number of Shares and Seniority

The class of preferred stock of Freddie Mac created hereby (the "Non-Cumulative Preferred Stock") shall be designated "Variable Rate, Non-Cumulative Preferred Stock," shall have a par value of $1.00 per share and shall consist of 5 million shares. The Board of Directors shall be permitted to increase the authorized number of such shares at any time. The Non-Cumulative Preferred Stock shall rank prior to the Voting Common Stock of Freddie Mac (the "Common Stock") to the extent provided in this Certificate and shall rank, both as to dividends and upon liquidation, on a parity with the 6.72% Preferred Stock issued on August 2, 1993 and the 7.90% Non-Cumulative Preferred Stock issued on April 27, 1992 (together, the "Existing Preferred Stock").

2. Dividends

(a) The holders of outstanding shares of Non-Cumulative Preferred Stock shall be entitled to receive, ratably, when, as and if declared by the Board of Directors, in its sole discretion, out of funds legally available therefor, non-cumulative, cash dividends at a variable per annum rate (not greater than 9% per annum) equal to (i) the sum of LIBOR (as defined in clause (b) below) and 1.0%, divided by (ii) 1.377, with the resulting dividend per share being rounded to the nearest cent (with one-half cent being rounded up), without taking into account any adjustments referred to in clause (c) below. Dividends on the Non-Cumulative Preferred Stock shall accrue from April 26, 1996 and are payable when, as and if declared by the Board of Directors quarterly on March 31, June 30, September 30 and December 31 of each year (each, a "Dividend Payment Date") commencing on June 30, 1996. If a Dividend Payment Date is not a "Business Day," the related dividend shall be paid on the next Business Day with the same force and effect as though paid on the Dividend Payment Date, without any increase to account for the period from such Dividend Payment Date through the date of actual payment. For these purposes, "Business Day" means a day other than (i) a Saturday or Sunday, (ii) a day on which New York City banks are closed or (iii) a day on which the offices of Freddie Mac are closed. If declared, the initial dividend, which will be for the period from but not including April 26, 1996 through and including June 30, 1996, will be 4.7091% or $.43 per share and will be payable on July 1, 1996. Thereafter, the dividend payable to holders of Non-Cumulative Preferred Stock will vary from Dividend Period to Dividend Period. The "Dividend Period" relating to a Dividend Payment Date shall

be the period from but not including the preceding Dividend Payment Date through and including the related Dividend Payment Date. Freddie Mac will calculate the dividend rate for each Dividend Period based on LIBOR determined as of two London Business Days (defined as any day, other than a Saturday or Sunday, on which banks are open for business in London) prior to the first day of such Dividend Period (each a "Determination Date"). Each dividend shall be calculated on the basis of the actual number of days elapsed, assuming a year of 360 days, and the dividend rate shall be applied to the $50 per share redemption value. Each such dividend shall be paid to the holders of record of outstanding shares of the Non-Cumulative Preferred Stock as they appear in the books and records of Freddie Mac on such record date as shall be fixed in advance by the Board of Directors, not to be earlier than 45 days nor later than 10 days preceding the applicable Dividend Payment Date. No dividends shall be declared or paid or set apart for payment on the Common Stock or any other class or series of stock ranking junior to or (except as hereinafter provided) on a parity with the Non-Cumulative Preferred Stock with respect to the payment of dividends unless dividends have been declared and paid or set apart (or ordered by the Board of Directors to be set apart) for payment on the outstanding Non-Cumulative Preferred Stock in respect of the then-current Dividend Period; provided, however, that the foregoing dividend preference shall not be cumulative and shall not in any way create any claim or right in favor of the holders of Non-Cumulative Preferred Stock in the event that Freddie Mac shall not have declared or paid or set apart (or the Board of Directors shall not have ordered to be set apart) dividends on the Non-Cumulative Preferred Stock in respect of any prior Dividend Period. In the event that Freddie Mac shall not pay any one or more dividends or any part thereof on the Non-Cumulative Preferred Stock, the holders of the Non-Cumulative Preferred Stock shall not have any claim in respect of such non-payment so long as no dividend is paid on any junior or parity stock in violation of the next preceding sentence.

(b) "LIBOR" means, with respect to a Dividend Period relating to a Dividend Payment Date (in the following order of priority):

(i) the rate (expressed as a percentage per annum) for Eurodollar deposits having a three-month maturity that appears on Telerate Page 3750 as of 11:00 a.m. (London time) on the related Determination Date;

(ii) if such rate does not appear on Telerate Page 3750 as of 11:00 a.m. (London time) on the related Determination Date, LIBOR shall be the arithmetic mean (if necessary rounded upwards to the nearest whole multiple of 1/128%) of the rates (expressed as a percentage per annum) for Eurodollar deposits having a three-month maturity that appear on Reuters Monitor Money Rates Page LIBO ("Reuters Page LIBO") as of 11:00 a.m. (London time) on such Determination Date;

(iii) if such rate does not appear on Reuters Page LIBO as of 11:00 a.m. (London time) on the related Determination Date, Freddie Mac shall request the principal London offices of four leading banks in the London interbank market to provide such banks' offered quotations (expressed as percentages per annum) to prime banks in the London interbank market for Eurodollar deposits having a three-month maturity as of 11:00 a.m. (London time) on such Determination Date. If at least two quotations are provided, LIBOR shall be the arithmetic mean (if necessary rounded upwards to the nearest whole multiple of 1/128%) of such quotations;

(iv) if fewer than two such quotations are provided as requested in clause (iii) above, Freddie Mac shall request four major New York City banks to provide such banks' offered quotations (expressed as percentages per annum) to leading European banks for loans in Eurodollars as of 11:00 a.m. (London time) on such Determination Date. If at least two such quotations are provided, LIBOR will be the arithmetic mean (if necessary rounded upwards to the nearest whole multiple of 1/128%) of such quotations; and

(v) if fewer than two such quotations are provided as requested in clause (iv) above, LIBOR shall be LIBOR determined with respect to the Dividend Period immediately preceding such current Dividend Period.

If the rate for Eurodollar deposits having a three-month maturity that initially appears on Telerate Page 3750 or Reuters Page LIBO, as the case may be, as of 11:00 a.m. (London time) on the related

Determination Date is superseded on Telerate Page 3750 or Reuters Page LIBO, as the case may be, by a corrected rate before 12:00 noon (London time) on such Determination Date, such corrected rate as so substituted on the applicable page shall be the applicable LIBOR for such Determination Date.

(c) If, prior to April 26, 1998, one or more amendments to the Internal Revenue Code of 1986, as amended (the "Code"), are enacted that reduce the percentage of the dividends-received deduction as specified in section 243(a)(1) of the Code or any successor provision (the "Dividends-Received Percentage"), certain adjustments may be made in respect of the dividends payable by the Corporation, and Post Declaration Date Dividends and Retroactive Dividends (as such terms are defined below) may become payable, as described below.

The amount of each dividend payable (if declared) per share of Non-Cumulative Preferred Stock for dividend payments made on or after the effective date of such change in the Code will be adjusted by multiplying the amount of the dividend payable pursuant to clause (a) of this Section 2 (before adjustment) by a factor, which shall be the number determined in accordance with the following formula (the "DRD Formula"), and rounding the result to the nearest cent (with one-half cent rounded up):

$$\frac{1-.35(1-.70)}{1-.35(1-DRP)}$$

For the purposes of the DRD Formula, "DRP" means the Dividends-Received Percentage (expressed as a decimal) applicable to the dividend in question; provided, however, that if the Dividends-Received Percentage applicable to the dividend in question is less than 50%, then the DRP shall equal .50. In the event an adjustment to any dividend payable on the Non-Cumulative Preferred Stock is made pursuant to this Section 2(c), the resulting dividend rate may exceed 9% per annum. No amendment to the Code, other than a change in the percentage of the dividends-received deduction set forth in section 243(a)(1) of the Code or any successor provision, shall give rise to an adjustment.

Notwithstanding the foregoing provisions, if, with respect to any such amendment, the Corporation receives either an unqualified opinion of nationally recognized independent tax counsel selected by the Corporation or a private letter ruling or similar form of assurance from the Internal Revenue Service (the "IRS") to the effect that such an amendment does not apply to a dividend payable on the Non-Cumulative Preferred Stock, then such amendment shall not result in the adjustment provided for pursuant to the DRD Formula with respect to such dividend. The opinion referenced in the previous sentence shall be based upon the legislation amending or establishing the DRP or upon a published pronouncement of the IRS addressing such legislation. Unless the context otherwise requires, references to dividends herein shall mean dividends as adjusted by the DRD Formula. The Corporation's calculation of the dividends payable as so adjusted shall be final and not subject to review.

Notwithstanding the foregoing, if any such amendment to the Code is enacted after the dividend payable on a Dividend Payment Date has been declared but before such dividend is paid, the amount of the dividend payable on such Dividend Payment Date shall not be increased. Instead, additional dividends (the "Post Declaration Date Dividends"), equal to the excess, if any, of (x) the product of the dividend paid by the Corporation on such Dividend Payment Date and the DRD Formula (where the DRP used in the DRD Formula would be equal to the greater of the Dividends-Received Percentage applicable to the dividend in question and .50) over (y) the dividend paid by the Corporation on such Dividend Payment Date, shall be payable (if declared) to holders on the record date applicable to the next succeeding Dividend Payment Date in addition to any other amounts payable on such date.

If any such amendment to the Code is enacted and the reduction in the Dividends-Received Percentage retroactively applies to a Dividend Payment Date as to which the Corporation previously paid dividends on the Non-Cumulative Preferred Stock (each, an "Affected Dividend Payment Date"), the Corporation shall pay (if declared) additional dividends (the "Retroactive Dividends") to holders on the record date applicable to the next succeeding Dividend Payment Date (or, if such amendment is enacted after the dividend payable on such Dividend Payment Date has been declared, to Holders on the record date applicable to the second succeeding Dividend Payment Date following the date of enactment) in an amount equal to the excess of (x) the product of the dividend paid by the Corporation

on each Affected Dividend Payment Date and the DRD Formula (where the DRP used in the DRD Formula would be equal to the greater of the Dividends-Received Percentage and .50 applied to each Affected Dividend Payment Date) over (y) the sum of the dividend paid by the Corporation on each Affected Dividend Payment Date. The Corporation shall make only one payment of Retroactive Dividends for any such amendment. Notwithstanding the foregoing provisions, if, with respect to any such amendment, the Corporation receives either an unqualified opinion of nationally recognized independent tax counsel selected by the Corporation or a private letter ruling or similar form of assurance from the IRS to the effect that such amendment does not apply to a dividend payable on an Affected Dividend Payment Date for the Non-Cumulative Preferred Stock, then such amendment shall not result in the payment of Retroactive Dividends with respect to such Affected Dividend Payment Date. The opinion referenced in the previous sentence shall be based upon legislation amending or establishing the DRP or upon a published pronouncement of the IRS addressing such legislation.

In the event that the amount of dividends payable per share of Non-Cumulative Preferred Stock is adjusted pursuant to the DRD Formula and/or Post Declaration Date Dividends or Retroactive Dividends are to be paid, the Corporation will cause notice of each such adjustment and, if applicable, Post Declaration Date Dividends and Retroactive Dividends to be given as soon as practicable to the holders of Non-Cumulative Preferred Stock.

(d) Notwithstanding any other provision of this Certificate, the Board of Directors, in its discretion, may choose to pay dividends on the Non-Cumulative Preferred Stock without the payment of any dividends on the Common Stock or any other class or series of stock from time to time outstanding ranking junior to the Non-Cumulative Preferred Stock with respect to the payment of dividends.

(e) No dividend shall be declared or paid or set apart for payment on any shares of the Non-Cumulative Preferred Stock if at the same time any arrears or default exists in the payment of dividends on any outstanding class or series of stock of Freddie Mac ranking prior to or (except as provided herein) on a parity with the Non-Cumulative Preferred Stock with respect to the payment of dividends. If and whenever dividends, having been declared, shall not have been paid in full, as aforesaid, on shares of the Non-Cumulative Preferred Stock and on the shares of any other class or series of stock of Freddie Mac ranking on a parity with the Non-Cumulative Preferred Stock with respect to the payment of dividends, all such dividends that have been declared on shares of the Non-Cumulative Preferred Stock and on the shares of any such other class or series shall be paid pro rata, so that the respective amounts of dividends paid per share on the Non-Cumulative Preferred Stock and on such other class or series shall in all cases bear to each other the same ratio that the respective amounts of dividends declared but unpaid per share on the shares of the Non-Cumulative Preferred Stock (including any adjustments due to changes in the Dividends-Received Percentage) and on the shares of such other class or series bear to each other.

(f) Holders of shares of the Non-Cumulative Preferred Stock shall not be entitled to any dividends, in cash or in property, other than as herein provided and shall not be entitled to interest, or any sum in lieu of interest, on or in respect of any dividend payment.

3. Optional Redemption

(a) The Non-Cumulative Preferred Stock shall not be redeemable prior to June 30, 2001. Subject to this limitation and to any further limitations which may be imposed by law, Freddie Mac may redeem the Non-Cumulative Preferred Stock, in whole or in part, at any time or from time to time, out of funds legally available therefor, at the redemption price of $50.00 per share, plus an amount, determined in accordance with Section 2 above, equal to the dividend, if any, otherwise payable for the then-current Dividend Period accrued through and including the date of such redemption. If less than all of the outstanding shares of the Non-Cumulative Preferred Stock are to be redeemed, Freddie Mac shall select shares to be redeemed from the outstanding shares not previously called for redemption by lot or pro rata (as nearly as possible) or by any other method which Freddie Mac in its sole discretion deems equitable.

(b) In the event Freddie Mac shall redeem any or all of the Non-Cumulative Preferred Stock as aforesaid, notice of such redemption shall be given by Freddie Mac by first class mail, postage prepaid, mailed neither less than 30 nor more than 60 days prior to the redemption date, to each holder of record of the shares of the Non-Cumulative Preferred Stock being redeemed, at such holder's address as the same appears in the books and records of Freddie Mac. Each such notice shall state the number of shares being redeemed, the redemption price, the redemption date and the place at which such holder's certificate(s) representing shares of the Non-Cumulative Preferred Stock must be presented for cancellation or exchanges, as the case may be, upon such redemption. Failure to give notice, or any defect in the notice, to any holder of the Non-Cumulative Preferred Stock shall not affect the validity of the proceedings for the redemption of shares of any other holder of Non-Cumulative Preferred Stock being redeemed.

(c) Notice having been mailed as aforesaid, from and after the redemption date specified therein and upon payment of the consideration set forth in Section 3(a) above, said shares of the Non-Cumulative Preferred Stock shall no longer be deemed to be outstanding, and all rights of the holders thereof as holders of the Non-Cumulative Preferred Stock shall cease, with respect to shares so redeemed.

(d) Any shares of the Non-Cumulative Preferred Stock which shall have been redeemed shall, after such redemption, no longer have the status of authorized, issued or outstanding shares.

4. No Voting Rights

Except as set forth in Section 9(h) below, the shares of the Non-Cumulative Preferred Stock shall not have any voting powers, either general or special.

5. No Conversion or Exchange Rights

The holders of shares of the Non-Cumulative Preferred Stock shall not have any right to convert such shares into or exchange such shares for any other class or series of stock or obligations of Freddie Mac.

6. No Preemptive Rights

No holder of the Non-Cumulative Preferred Stock shall as such holder have any preemptive right to purchase or subscribe for any other shares, rights, options or other securities of any class of Freddie Mac which at any time may be sold or offered for sale by Freddie Mac.

7. Liquidation Rights and Preference

(a) Except as otherwise set forth herein, upon the voluntary or involuntary dissolution, liquidation or winding up of Freddie Mac, after payment of or provision for the liabilities of Freddie Mac and the expenses of such dissolution, liquidation or winding up, the holders of the outstanding shares of the Non-Cumulative Preferred Stock shall be entitled to receive out of the assets of Freddie Mac available for distribution to stockholders, before any payment or distribution shall be made on the Common Stock or any other class or series of stock of Freddie Mac ranking junior to the Non-Cumulative Preferred Stock upon liquidation, the amount of $50.00 per share plus an amount, determined in accordance with Section 2 above, equal to the dividend, if any, otherwise payable for the then-current Dividend Period accrued through and including the date of payment in respect of such dissolution, liquidation or winding up, and the holders of the outstanding shares of any class or series of stock of Freddie Mac ranking on a parity with the Non-Cumulative Preferred Stock upon liquidation shall be entitled to receive out of the assets of Freddie Mac available for distribution to stockholders, before any such payment or distribution shall be made on the Common Stock or any other class or series of stock of Freddie Mac ranking junior to the Non-Cumulative Preferred Stock and to such parity stock upon liquidation, any corresponding preferential amount to which the holders of such parity stock may, by the terms thereof, be entitled; provided, however, that if the assets of Freddie Mac available for distribution to stockholders shall be insufficient for the payment of the full amounts to which the holders of the outstanding shares of the

Non-Cumulative Preferred Stock and the holders of the outstanding shares of such parity stock shall be entitled to receive upon such dissolution, liquidation or winding up of Freddie Mac as aforesaid, then, subject to paragraph (b) of this Section 7, all of the assets of Freddie Mac available for distribution to stockholders shall be distributed to the holders of outstanding shares of the Non-Cumulative Preferred Stock and to the holders of outstanding shares of such parity stock pro rata, so that the amounts so distributed to holders of the Non-Cumulative Preferred Stock and to holders of such classes or series of such parity stock, respectively, shall bear to each other the same ratio that the respective distributive amounts to which they are so entitled (including any adjustment due to changes in the Dividends-Received Percentage) bear to each other. After the payment of the aforesaid amounts to which they are entitled, the holders of outstanding shares of the Non-Cumulative Preferred Stock and the holders of outstanding shares of any such parity stock shall not be entitled to any further participation in any distribution of assets of Freddie Mac.

(b) Notwithstanding the foregoing, upon the dissolution, liquidation or winding up of Freddie Mac, the holders of shares of the Non-Cumulative Preferred Stock then outstanding shall not be entitled to be paid any amounts to which such holders are entitled pursuant to paragraph (a) of this Section 7 unless and until the holders of any classes or series of stock of Freddie Mac ranking prior upon liquidation to the Non-Cumulative Preferred Stock shall have been paid all amounts to which such classes or series are entitled pursuant to their respective terms.

(c) Neither the sale of all or substantially all of the property or business of Freddie Mac, nor the merger, consolidation or combination of Freddie Mac into or with any other corporation or entity, shall be deemed to be a dissolution, liquidation or winding up for the purpose of this Section 7.

8. Additional Classes or Series of Stock

The Board of Directors shall have the right at any time in the future to authorize, create and issue, by resolution or resolutions, one or more additional classes or series of stock of Freddie Mac, and to determine and fix the distinguishing characteristics and the relative rights, preferences, privileges and other terms of the shares thereof. Any such class or series of stock may rank prior to or on a parity with or junior to the Non-Cumulative Preferred Stock as to dividends or upon liquidation or otherwise.

9. Miscellaneous

(a) Any stock of any class or series of Freddie Mac shall be deemed to rank:

(i) prior to the shares of the Non-Cumulative Preferred Stock, either as to dividends or upon liquidation, if the holders of such class or series shall be entitled to the receipt of dividends or of amounts distributable upon dissolution, liquidation or winding up of Freddie Mac, as the case may be, in preference or priority to the holders of shares of the Non-Cumulative Preferred Stock;

(ii) on a parity with shares of the Non-Cumulative Preferred Stock, either as to dividends or upon liquidation, whether or not the dividend rates or amounts, dividend payment dates or redemption of liquidation prices per share, if any, be different from those of the Non-Cumulative Preferred Stock, if the holders of such class or series shall be entitled to the receipt of dividends or of amounts distributable upon dissolution, liquidation or winding up of Freddie Mac, as the case may be, in proportion to their respective dividend rates or amounts or liquidation prices, without preference or priority, one over the other, as between the holders of such class or series and the holders of shares of the Non-Cumulative Preferred Stock; and

(iii) junior to shares of the Non-Cumulative Preferred Stock, either as to dividends or upon liquidation, if such class or series shall be Common Stock, or if the holders of shares of the Non-Cumulative Preferred Stock shall be entitled to receipt of dividends or of amounts distributable upon dissolution, liquidation or winding up of Freddie Mac, as the case may be, in preference or priority to the holders of shares of such class or series.

(b) Freddie Mac and any agent of Freddie Mac may deem and treat the holder of a share or shares of Non-Cumulative Preferred Stock, as shown in Freddie Mac's books and records, as the absolute

owner of such share or shares of Non-Cumulative Preferred Stock for the purpose of receiving payment of dividends in respect of such share or shares of Non-Cumulative Preferred Stock and for all other purposes whatsoever, and neither Freddie Mac nor any agent of Freddie Mac shall be affected by any notice to the contrary. All payments made to or upon the order of any such person shall be valid and, to the extent of the sum or sums so paid, effectual to satisfy and discharge liabilities for moneys payable by Freddie Mac on or with respect to any such share or shares of Non-Cumulative Preferred Stock.

(c) The shares of the Non-Cumulative Preferred Stock, when duly issued, shall be fully paid and non-assessable.

(d) The Non-Cumulative Preferred Stock shall be issued, and shall be transferable on the books of Freddie Mac, only in whole shares, it being intended that no fractional interests in shares of Non-Cumulative Preferred Stock shall be created or recognized by Freddie Mac.

(e) For purposes of this Certificate, the term "Freddie Mac" means the Federal Home Loan Mortgage Corporation and any successor thereto by operation of law or by reason of a merger, consolidation or combination.

(f) This Certificate and the respective rights and obligations of Freddie Mac and the holders of the Non-Cumulative Preferred Stock with respect to such Non-Cumulative Preferred Stock shall be construed in accordance with and governed by the laws of the United States, provided that the law of the Commonwealth of Virginia shall serve as the federal rule of decision in all instances except where such law is inconsistent with Freddie Mac's enabling legislation, its public purposes or any provision of this Certificate.

(g) Any notice, demand or other communication which by any provision of this Certificate is required or permitted to be given or served to or upon Freddie Mac shall be given or served in writing addressed (unless and until another address shall be published by Freddie Mac) to the Federal Home Loan Mortgage Corporation, 8200 Jones Branch Drive, McLean, Virginia 22102, Attn: Senior Vice President-General Counsel and Secretary. Such notice, demand or other communication to or upon Freddie Mac shall be deemed to have been sufficiently given or made only upon actual receipt of a writing by Freddie Mac. Any notice, demand or other communication which by any provision of this Certificate is required or permitted to be given or served by Freddie Mac hereunder may be given or served by being deposited first class, postage prepaid, in the United States mail addressed (i) to the holder as such holder's name and address may appear at such time in the books and records of Freddie Mac or (ii) if to a person or entity other than a holder of record of the Non-Cumulative Preferred Stock, to such person or entity at such address as appears to Freddie Mac to be appropriate at such time.

(h) Freddie Mac, by or under the authority of the Board of Directors, may amend, alter, supplement or repeal any provision of this Certificate pursuant to the following terms and conditions:

(i) Without the consent of the holders of the Non-Cumulative Preferred Stock, Freddie Mac may amend, alter, supplement or repeal any provision of this Certificate to cure any ambiguity, to correct or supplement any provision herein which may be defective or inconsistent with any other provision herein, or to make any other provisions with respect to matters or questions arising under this Certificate, provided that such action shall not materially and adversely affect the interests of the holders of the Non-Cumulative Preferred Stock.

(ii) The consent of the holders of at least 66⅔% of all of the shares of the Non-Cumulative Preferred Stock at the time outstanding, given in person or by proxy, either in writing or by a vote at a meeting called for the purpose at which the holders of shares of the Non-Cumulative Preferred Stock shall vote together as a class, shall be necessary for authorizing, effecting or validating the amendment, alteration, supplementation or repeal of the provisions of this Certificate if such amendment, alteration, supplementation or repeal would materially and adversely affect the powers, preferences, rights, privileges, qualifications, limitations, restrictions, terms or conditions of the Non-Cumulative Preferred Stock. The creation and issuance of any other class or series of stock, or the issuance of additional shares of any existing class or series of stock of Freddie Mac (including the Non-Cumulative Preferred Stock), whether ranking prior to, on a parity with or

junior to the Non-Cumulative Preferred Stock, shall not be deemed to constitute such an amendment, alteration, supplementation or repeal.

(iii) Holders of the Non-Cumulative Preferred Stock shall be entitled to one vote per share on matters on which their consent is required pursuant to subparagraph (ii) of this paragraph (h). In connection with any meeting of such holders, the Board of Directors shall fix a record date, neither earlier than 60 days nor later than 10 days prior to the date of such meeting, and holders of record of shares of the Non-Cumulative Preferred Stock on such record date shall be entitled to notice of and to vote at any such meeting and any adjournment. The Board of Directors, or such person or persons as it may designate, may establish reasonable rules and procedures as to the solicitation of the consent of holders of the Non-Cumulative Preferred Stock at any such meeting or otherwise, which rules and procedures shall conform to the requirements of any national securities exchange on which the Non-Cumulative Preferred Stock may be listed at such time.

(i) RECEIPT AND ACCEPTANCE OF A SHARE OR SHARES OF THE NON-CUMULATIVE PREFERRED STOCK BY OR ON BEHALF OF A HOLDER SHALL CONSTITUTE THE UNCONDITIONAL ACCEPTANCE BY THE HOLDER (AND ALL OTHERS HAVING BENEFICIAL OWNERSHIP OF SUCH SHARE OR SHARES) OF ALL OF THE TERMS AND PROVISIONS OF THIS CERTIFICATE. NO SIGNATURE OR OTHER FURTHER MANIFESTATION OF ASSENT TO THE TERMS AND PROVISIONS OF THIS CERTIFICATE SHALL BE NECESSARY FOR ITS OPERATION OR EFFECT AS BETWEEN FREDDIE MAC AND THE HOLDER (AND ALL SUCH OTHERS).

IN WITNESS WHEREOF, I have hereunto set my hand and the seal of Freddie Mac this 23rd day of April 1996.

[Seal]

Maud Mater, *Secretary*

RECENT UNAUDITED FINANCIAL INFORMATION

FEDERAL HOME LOAN MORTGAGE CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(unaudited)
(dollars in millions, except per share amounts)

	Quarter Ended		
	March 31, 1996	December 31, 1995	March 31, 1995
Interest income:			
Mortgages	$ 820	$ 803	$ 770
Guaranteed mortgage securities	1,238	1,075	612
Investments and mortgage securities purchased under agreements to resell	369	405	455
	2,427	2,283	1,837
Interest expense on debt securities:			
Short-term debt	(517)	(525)	(587)
Long-term debt	(1,398)	(1,302)	(927)
	(1,915)	(1,827)	(1,514)
Interest expense due to security program cycles	(125)	(93)	(30)
	(2,040)	(1,920)	(1,544)
Net interest income on earning assets	387	363	293
Management and guarantee income	305	300	295
Other income, net	9	9	13
Total revenues	701	672	601
Provision for mortgage losses	(80)	(70)	(60)
REO operations expense	(76)	(76)	(69)
Administrative expenses	(105)	(102)	(97)
Total non-interest expenses	(261)	(248)	(226)
Income before income taxes	440	424	375
Provision for income taxes	(139)	(133)	(117)
Net income	$ 301	$ 291	$ 258
Preferred stock dividends	(16)	(17)	(16)
Net income available to common stockholders	$ 285	$ 274	$ 242
Earnings per common share	$ 1.60	$ 1.53	$ 1.34
Weighted average common shares outstanding (thousands)	178,413	179,473	180,760

FEDERAL HOME LOAN MORTGAGE CORPORATION
CONSOLIDATED BALANCE SHEETS
(unaudited)
(dollars in millions)

	March 31, 1996	December 31, 1995	March 31, 1995
Assets			
Retained portfolio:			
Mortgages	$ 45,208	$ 43,753	$ 41,309
Reserve for losses on retained mortgages	(303)	(295)	(292)
	44,905	43,458	41,017
Guaranteed mortgage securities	72,212	63,671	36,004
Unamortized purchase and sale premiums, discounts and fees	224	282	302
Retained portfolio, net	117,341	107,411	77,323
Cash and cash equivalents	5,423	7,483	17,158
Investments	3,971	4,745	7,905
Mortgage securities purchased under agreements to resell	8,260	9,217	6,824
Accounts receivable and other assets	7,979	7,525	3,467
Real estate owned, net	818	800	948
	$143,792	$137,181	$113,625
Liabilities and Stockholders' Equity			
Debt securities, net			
Due within one year	$ 67,053	$ 62,141	$ 51,093
Due after one year	56,584	57,187	49,346
Total debt securities, net	123,637	119,328	100,439
Principal and interest due to Mortgage Participation Certificate (PC) investors	11,069	8,806	4,743
Other liabilities	2,047	2,163	1,426
	136,753	130,297	106,608
Reserve for losses on sold mortgages	386	388	432
Guarantees:			
Mortgage Participation Certificates	524,327	515,051	492,194
Less—Underlying mortgages	(524,327)	(515,051)	(492,194)
	—	—	—
Subordinated borrowings	641	633	1,234
Stockholders' equity	6,012	5,863	5,351
	$143,792	$137,181	$113,625

Information Statement

Freddie Mac

Federal Home Loan Mortgage Corporation

The Federal Home Loan Mortgage Corporation ("Freddie Mac" or the "corporation") is a shareholder-owned government-sponsored enterprise ("GSE") established by Congress in 1970 to provide a continuous flow of funds for residential mortgages. Freddie Mac performs this function principally through the purchase of residential mortgage loans from mortgage originators on a continuous basis under all market conditions. To finance its mortgage purchase activities, Freddie Mac offers and sells its securities to investors directly and through selected dealers, underwriters and underwriting syndicates. The corporation's securities are exempt from registration under the federal securities laws, including the Securities Act of 1933 and the Securities Exchange Act of 1934. Freddie Mac makes available information for the securities it issues, including the terms of the securities, the distribution or selling arrangements and other pertinent information, in the Offering Circular and any Offering Circular Supplement applicable to each particular offering. Neither the United States nor any agency or instrumentality of the United States is obligated, either directly or indirectly, to fund the mortgage purchase or financing activities of Freddie Mac.

This Information Statement contains important financial and other information concerning Freddie Mac and should be read carefully by investors in, and prospective purchasers of, Freddie Mac securities. This Information Statement should be read in conjunction with the Offering Circular and any Offering Circular Supplement for the particular securities being offered and in conjunction with any supplements to this Information Statement made available by Freddie Mac, including supplements for calendar quarters ending after December 31, 1995. Freddie Mac also periodically makes available statistical information on its mortgage purchase and securities sales volume as well as other relevant information about Freddie Mac. Copies of available supplements, reports and information can be obtained by writing or calling Freddie Mac's Investor Inquiry Department at 8200 Jones Branch Drive, McLean, Virginia 22102 (outside the Washington, D.C. metropolitan area, telephone (800) 336-FMPC; within the Washington, D.C. metropolitan area, telephone (703) 450-3777).

The principal office of Freddie Mac is located at 8200 Jones Branch Drive, McLean, Virginia 22102 (telephone (703) 903-2000).

This Information Statement describes the business and operations of Freddie Mac as of March 29, 1996, and the financial condition of Freddie Mac as of the date of the financial statements included herein. Recipients of this Information Statement should retain it for future reference until a subsequent Information Statement is made available by Freddie Mac, but delivery or retention of this Information Statement shall not create any implication that the information provided is correct at any time after the date hereof.

INFORMATION STATEMENT DATED MARCH 29, 1996

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FEDERAL HOME LOAN MORTGAGE CORPORATION

Freddie Mac was chartered on July 24, 1970 pursuant to the Federal Home Loan Mortgage Corporation Act, Title III of the Emergency Home Finance Act of 1970, as amended (the "Freddie Mac Act"). Freddie Mac's statutory purposes are (i) to provide stability in the secondary market for residential mortgages, (ii) to respond appropriately to the private capital market, (iii) to provide ongoing assistance to the secondary market for residential mortgages (including activities relating to mortgages on housing for low- and moderate-income families involving a reasonable economic return that may be less than the return earned on other activities) and (iv) to promote access to mortgage credit throughout the United States (including central cities, rural areas and underserved areas) by increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing. To meet these statutory purposes, Freddie Mac continuously purchases residential mortgages from mortgage originators, and finances such purchases under all market conditions. Freddie Mac strives to fulfill these purposes through the purchase of investment-quality mortgages from all communities and geographic segments of the United States, and thereby improve the quality of life by making the American dream of decent accessible housing a reality.

The principal office of Freddie Mac is located in McLean, Virginia. Freddie Mac has regional offices located in Atlanta, Georgia; Chicago, Illinois; Dallas, Texas; McLean, Virginia; New York, New York; and Woodland Hills, California.

BUSINESS

General

As a GSE chartered by Congress principally to provide a reliable source of funds for residential mortgages, Freddie Mac engages in a single line of business operations: the purchase of residential mortgages and the financing of those purchases primarily through the sale of mortgage-related securities and unsecured debt. In addition, Freddie Mac can engage in activities that are incidental to and supportive of its primary line of business. The corporation's success in pursuing this unitary business operation is dependent largely upon the skills of its management and employees in responding to conditions prevailing in the mortgage markets and the general capital markets. In its 25 years of operations, Freddie Mac has been very successful. Specifically, it routinely has been able to generate profitable returns and achieve a sound financial condition while operating in a wide variety of economic and market environments. If these or other factors should change in a manner that adversely affects the corporation's business prospects, limitations within Freddie Mac's charter which prevent the corporation from diversifying into new business endeavors unrelated to the fulfillment of its statutory purposes limit Freddie Mac's flexibility to respond to such changes.

Freddie Mac is subject to two primary types of risk in the conduct of its business: credit risk associated with the mortgages it purchases and the institutions with which it does business; and interest-rate risk that principally results from mortgage prepayments that may create mismatches in the corporation's assets and liabilities associated with its mortgage portfolio. For a discussion of the impact and management of these risks, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management."

Freddie Mac purchases first-lien, conventional residential mortgages, including both whole loans and participation interests in such mortgages (referred to collectively as "mortgages"). Freddie Mac purchases both fixed-rate mortgages and adjustable-rate mortgages ("ARMs"). A conventional mortgage is a mortgage that does not have the benefit of any guarantee or insurance by the United States or any of its agencies or instrumentalities. A mortgage secured by a property with one to four living units is referred to as a "single-family" mortgage, and a mortgage secured by a property with five or more living units is referred to as a "multifamily" mortgage. To a lesser extent, Freddie Mac also purchases mortgages that are fully insured by the Federal Housing Administration ("FHA") or guaranteed, in part, by the Department of Veterans Affairs (collectively, "FHA/VA" mortgages) and subordinate lien mortgages ("second" mortgages) on single-family properties. Currently, substantially all of the single-family

mortgages purchased by the corporation may be repaid by the borrower, in whole or in part, at any time prior to maturity without penalty. By contrast, the multifamily mortgages purchased by the corporation often may be repaid prior to maturity only upon payment of a prepayment premium or, in some cases, are subject to contractual restrictions on prepayment for a period of time following origination.

The corporation finances mortgage purchases principally by sales of guaranteed mortgage-related securities, including various types of mortgage participation certificates ("PCs"). Freddie Mac also finances mortgage purchases with debt securities, other liabilities (primarily cash temporarily held pending disbursement to security holders) and equity capital. Mortgages financed by PCs sold to investors are referred to as the "sold portfolio." Mortgages and mortgage-related securities held for investment by Freddie Mac and financed by debt securities, other liabilities and equity capital are referred to as the "retained portfolio." The sold and retained portfolios are collectively referred to as the "total mortgage portfolio." Freddie Mac's mortgage purchase and mortgage-related securities sales programs are described below.

Mortgage Purchases

Freddie Mac purchases a variety of single-family mortgages with fixed or adjustable interest rates or interest rate reset features. Single-family mortgages acquired by Freddie Mac are purchased mainly from mortgagees approved by the Secretary of Housing and Urban Development ("HUD") for participation in mortgage insurance programs under the National Housing Act (primarily mortgage bankers) or from federally insured financial institutions (primarily commercial banks and thrift institutions). Freddie Mac purchases multifamily mortgages with fixed interest rates or interest-rate reset features from a limited network of multifamily mortgage originators, including federally insured financial institutions, mortgage bankers, investment bankers and insurance companies.

Freddie Mac fulfills its statutory purposes of providing a reliable and low-cost source of mortgage funding for the benefit of a diverse range of homeowners and renters primarily through the purchase of conventional, conforming single-family mortgages, as well as through its multifamily mortgage purchase programs and other initiatives. See "Regulation and Governmental Relationships — Regulation of Freddie Mac" and "Management's Discussion and Analysis of Financial Condition and Results of Operations — Regulatory Matters — Housing Goals." Freddie Mac views the financing of affordable housing as an integral part of its mission and business. Accordingly, the corporation purchases most single-family and multifamily mortgages in support of affordable housing through its standard mortgage purchase programs and under the same credit standards as its other mortgage purchases. In addition, Freddie Mac has initiated a variety of targeted programs to develop experience in order to better serve this segment of the residential mortgage market with the ultimate goal of incorporating these programs into its standard mortgage purchase programs. See "— Recent Initiatives — Expanding Markets and Community Development Lending."

Freddie Mac Act Mortgage Purchase Requirements

The Freddie Mac Act imposes limits, which are subject to annual adjustment, on the maximum original principal amount of any type of mortgage that Freddie Mac may purchase. For 1996 the maximum original principal amount of a first-lien conventional single-family mortgage is $207,000 for a one-family dwelling, $264,750 for a two-family dwelling, $320,050 for a three-family dwelling and $397,800 for a four-family dwelling. Separate limits, expressed on a per-unit basis, apply to the maximum original principal amount of multifamily mortgages purchased by Freddie Mac. These per-unit limits may be increased by 92 percent for properties located in HUD-designated "high cost" areas. The applicable loan purchase limits for both single-family and multifamily mortgages are 50 percent higher for properties located in Alaska, Guam, Hawaii or the U.S. Virgin Islands.

The Freddie Mac Act also provides that Freddie Mac may not purchase a first-lien conventional single-family mortgage if the outstanding principal balance at the time of purchase exceeds 80 percent of the value of the real property securing the mortgage unless one of several conditions is met. These conditions generally provide credit enhancement to Freddie Mac (and therefore limit Freddie Mac's exposure to loss) or incentives for sellers to deliver only mortgages of acceptable quality. They consist of

mortgage insurance from a Freddie Mac-approved mortgage insurer, recourse to the seller or equivalent forms of credit enhancement as determined by Freddie Mac, or the retention of at least a 10 percent participation interest in the mortgages by the seller. Comparable conditions apply to the purchase of conventional single-family second mortgages where the total loan-to-value ratio exceeds 80 percent, but not to the purchase of conventional multifamily mortgages or FHA/VA mortgages.

Finally, the Freddie Mac Act provides that Freddie Mac may purchase, so far as practicable, only mortgages that Freddie Mac deems to be of such quality, type and class as to meet, generally, the purchase standards of private institutional mortgage investors. This aspect of the Freddie Mac Act requires that the mortgages purchased be readily marketable to institutional mortgage investors.

Single-Family Mortgage Purchases

Freddie Mac purchases single-family mortgages for cash and in exchange for PCs. In addition to the requirements of the Freddie Mac Act, single-family mortgages purchased under these programs generally are subject to the corporation's credit, appraisal, underwriting and other purchase guidelines set forth in its *Single-Family Seller/Servicer Guide.* Freddie Mac may modify these guidelines or grant waivers with respect to the purchase of specific mortgages.

Freddie Mac purchases single-family 15-year, 20-year and 30-year fixed-rate mortgages, ARMs and Balloon/Reset mortgages. Balloon/Reset mortgages typically have original terms to maturity of either five or seven years and provide for level payments of principal and interest during the original term with principal payments typically based on a 30-year amortization schedule. At the expiration of the original term, the then-remaining unpaid principal balance of the mortgage is payable in full, although the borrower may elect to extend the mortgage term with an interest-rate adjustment if the borrower satisfies certain conditions associated with such an extension. Freddie Mac began purchasing Balloon/Reset mortgages in 1989. Approximately $12.8 billion in Balloon/Reset mortgages are scheduled to reset in 1996 and 1997.

Freddie Mac purchases single-family mortgages for cash primarily for resale as PCs to parties other than the sellers of the mortgages. Freddie Mac generally coordinates the volume of and effective interest rates on its cash mortgage purchase commitments with its commitments to sell PCs. This procedure effectively enables Freddie Mac to reduce interest-rate risk and realize income on a portion of the difference in rates between mortgages purchased and PCs sold. The remaining cash mortgage purchases are held for investment and financed by debt securities, equity capital and other liabilities. Sellers typically choose to sell mortgages for cash if they have relatively straightforward secondary market needs and prefer to sell mortgages as soon as they have been originated without having to accumulate the volume generally needed for efficient securitization, and also without requiring the operational support necessary for participation in the securities markets. Freddie Mac's cash purchase prices for mortgages generally reflect the prices at which Freddie Mac can sell the related PCs; as a result sellers can realize certain of the benefits of securitization without incurring all of the associated costs.

Freddie Mac also purchases mortgages in exchange for PCs representing interests in the mortgages purchased from one or more sellers. Sellers may choose to exchange mortgages for PCs for several reasons. Owning PCs rather than the underlying mortgages may reduce the exposure of an institution to credit risk and increase the financial flexibility and liquidity of the institution, which may use the PCs as collateral for repurchase agreement transactions and other borrowings and for other purposes. In addition, in the case of depository institutions, regulatory capital requirements generally favor holding mortgage assets in securitized form.

Sellers with relatively complex secondary market needs and the desire and capability to participate actively in the securities market may prefer to sell mortgages in exchange for PCs when the sale or other utilization of PCs provides a greater flexibility or overall return than is available through a sale of mortgages for cash. Sellers that originate a volume of mortgages sufficient for efficient securitization and that prefer to determine the particular mortgages included in each pool may choose to sell mortgages for PCs. Sellers that prefer to sell mortgages in smaller amounts rather than in bulk, but that also want to take advantage of a securities execution, often can accomplish both of these objectives by exchanging mortgages, together with other sellers, in exchange for PCs. Such PCs may be available as soon as the next business day, thereby enabling these mortgage sellers to reduce their use of warehouse credit lines and lower their borrowing costs.

Multifamily Mortgage Purchases

Under its multifamily mortgage purchase programs, Freddie Mac purchases multifamily mortgages from approved lenders in exchange for cash or multifamily mortgage-related securities. Freddie Mac generally does not purchase individual multifamily mortgages with an original aggregate principal amount exceeding $50 million.

In addition to the statutory requirements for the purchase of multifamily mortgages set forth in the Freddie Mac Act, the corporation has established multifamily mortgage purchase standards, including credit, appraisal and underwriting guidelines as set forth in its *Multifamily Seller/Servicer Guide.* From time to time, Freddie Mac modifies its non-statutory mortgage purchase standards. Freddie Mac may also grant waivers or modifications to these standards in connection with the purchase of specific mortgages when compensating factors (such as high debt coverage ratios, low loan-to-value ratios ("LTV ratios") or credit enhancements) are present.

Freddie Mac purchases for cash conventional multifamily mortgages with terms generally ranging from 5 to 25 years. Multifamily mortgages purchased for cash which have terms of 20 years or longer generally are fully amortizing. Each mortgage generally may be paid in full or in part prior to maturity, sometimes subject to payment of a prepayment premium which may be in the form of a yield maintenance fee based on a benchmark interest rate at the time of prepayment, or a percentage of the amount prepaid. The corporation also purchases for cash multifamily mortgages that provide refinancing of multifamily mortgages held by the corporation in its sold or retained portfolio that are in danger of defaulting. The refinancing of existing multifamily mortgages allows borrowers to reduce their debt burdens by permitting more of the cash flow to be used for property maintenance. In 1995, these refinancings represented approximately 6 percent of Freddie Mac's multifamily mortgage purchases.

In 1996, Freddie Mac initiated a program for the purchase of multifamily mortgages with rate reset features ("Multifamily Rate Reset Mortgages"). Multifamily Rate Reset Mortgages provide for 5 years of level payments of principal and interest based on an amortization schedule of up to 25 years, with a borrower option to extend the term of the mortgage for an additional 5 years at a new fixed rate. The interest rate applicable during the second 5-year period is set at a predetermined spread over a comparable 5-year Treasury security available at the end of the original mortgage term.

Also in 1996, Freddie Mac introduced the Multifamily PC One Program. Under this program, Freddie Mac purchases multifamily mortgages for cash with the expectation that it will securitize those mortgages as single-loan PCs promptly following purchase. Mortgages purchased under the PC One Program have similar features to mortgages purchased under the Multifamily Conventional Cash Program.

Freddie Mac regularly purchases seasoned multifamily mortgages in exchange for PCs. Freddie Mac may also purchase newly originated multifamily mortgages in exchange for PCs or other multifamily mortgage-related securities in certain negotiated transactions. The multifamily mortgages purchased for PCs may be fully amortizing mortgages, amortizing balloon mortgages or, in the case of certain negotiated transactions, interest-only balloon mortgages. Fully amortizing mortgages generally have original terms of from 10 to 30 years and provide for level monthly payments of principal and interest sufficient to amortize the mortgages over their original terms. Amortizing balloon mortgages have original terms of from 5 to 15 years, provide for level monthly payments of principal and interest sufficient to amortize the mortgages over a period of up to 30 years and require a balloon payment at maturity. Interest-only balloon mortgages have original terms of from 3 to 10 years, provide for interest-only monthly payments during their terms and require a balloon payment at maturity.

Conventional multifamily mortgages purchased by Freddie Mac in exchange for mortgage-related securities may allow prepayment at any time, or, in some cases, may be subject to contractual restrictions on prepayment. In certain cases, prepayment of multifamily mortgages purchased in exchange for mortgage-related securities may require the payment of a mortgage prepayment premium.

Recent Initiatives

Freddie Mac continually examines and modifies its programs and policies in order to broaden its markets and increase the attractiveness and competitiveness of its mortgage purchase programs and mortgage-related securities. Freddie Mac endeavors to develop products and services that are attractive to different types of mortgage sellers and security investors.

Expanding Markets and Community Development Lending. In 1994, Freddie Mac introduced the Expanding Markets initiative to promote affordable lending, fair lending and community development lending. The initiative produced a package of single-family mortgage products, programs, services and tools designed to bring the benefits of the secondary market to more people, and expand access to mortgage credit for underserved communities. Expanding Markets products and services include: (1) Affordable Gold with the 3/2 Option—a program designed to help homebuyers who need assistance with downpayment and closing costs; (2) Affordable Seconds—an automated checklist to help lenders work with governments, non-profit organizations and other housing finance agencies to find and create secondary financing terms for their potential borrowers; (3) Fair Lending: an Introduction to Self Evaluation—a guide for lenders considering a self-evaluation program to assess their fair lending performance; (4) Gold Measure—an automated worksheet tool to help lenders evaluate risks and compensating factors to assess a borrower's ability to manage mortgage debt; (5) Discover Gold Through Expanding Markets—a booklet of over 100 case studies and product information to guide lenders and illustrate the flexibility of Freddie Mac's underwriting standards; and (6) Discover Gold Through Homeownership Education—a publication that offers best practices in homeownership education to help lenders select suitable homeownership education and counseling programs and that includes a "how-to" booklet for potential borrowers on conducting a consumer home inspection.

In addition to these initiatives, the corporation has undertaken a number of pilot projects to gain experience with particular mortgage products, borrower groups or lender groups in order to incorporate successfully the features of these transactions into its standard mortgage purchase programs. These pilots include a lease-purchase program, an FHA rehabilitation mortgage purchase program and a 2- to 4-unit affordable lending program. Other negotiated offerings include HUD and FHA Native American purchase programs, and the U.S. Department of Agriculture's Rural Housing and Community Development Service Guaranteed Housing purchase program. These initiatives are intended to expand access to the secondary market for non-traditional lenders, including housing finance agencies and community development and non-profit organizations.

Also in 1995, the corporation began a community development lending approach which includes national alliances with national non-profit housing organizations and national minority religious organizations with local affiliates and other housing finance participants. Under the terms of these national alliances, Freddie Mac provides the national organization with seed capital to enable the national organization and its local affiliates in targeted communities to establish homebuyer readiness programs, create local alliances with a variety of community resources, and connect potential homebuyers with lenders offering Freddie Mac mortgage products for purchase by the corporation.

*Loan Prospector*SM. In January 1995, Freddie Mac commercially introduced Loan ProspectorSM, an automated single-family mortgage underwriting service that evaluates a mortgage loan application in minutes and determines if the mortgage is eligible for sale to Freddie Mac. The service includes four components: (i) a product eligibility determination for the sale of the mortgage to Freddie Mac; (ii) a credit evaluation to assess a borrower's creditworthiness; (iii) an optional collateral assessment to determine the adequacy of the mortgaged property to serve as collateral for the mortgage; and (iv) an optional mortgage insurance component to facilitate the insurance of mortgages with LTV ratios over 80 percent with the insurer of choice.

Loan ProspectorSM provides lenders with the ability to evaluate mortgage application materials electronically. The service uses statistical models and underwriting guidelines to generate purchase decisions from Freddie Mac in a matter of minutes. Mortgage applications that do not receive favorable purchase decisions are referred to the originator's underwriters for manual underwriting, with feedback from Loan ProspectorSM about the issues that caused the loan to be referred.

In 1995, approximately 180 mortgage sellers signed up to use Loan Prospector℠; approximately 39,000 mortgages were underwritten through Loan Prospector℠ for credit purposes; approximately 4,600 of these mortgages were also the subject of collateral assessment; and more than $1 billion in mortgages underwritten through Loan Prospector℠ were purchased by the corporation. Loan Prospector℠ is an open system capable of underwriting mortgages sold to purchasers other than Freddie Mac, including mortgages processed in a pilot program in which the loan amount may exceed the corporation's individual loan purchase limits, or that do not conform to the corporation's underwriting criteria. Freddie Mac earns a fee on all mortgages underwritten through Loan Prospector℠.

GoldWorks®. In July 1995, Freddie Mac commercially introduced GoldWorks®, an electronic information network for the mortgage industry. GoldWorks® provides mortgage market participants with a single link with Freddie Mac and other parties involved in the mortgage origination and purchase process, such as credit bureaus and mortgage insurers. GoldWorks® also is an open system through which Freddie Mac customers may conduct business with the corporation as well as access third party services such as services for tracking, sharing and transferring title documents; disseminating mortgage rate sheets and product announcements; and selling mortgage products not purchased by the corporation to third-party investors. Freddie Mac earns fees on services offered and used through GoldWorks®.

Mortgage Purchase Volume

Set forth below is a summary of Freddie Mac's mortgage purchase activity for the years shown.

Purchases of Mortgages
(dollars in millions)

	Year ended December 31,				
	1995	1994	1993	1992	1991
Single-family 30-year fixed-rate(1)	$58,244	$ 70,390	$115,375	$ 85,200	$61,275
Single-family 15-year fixed-rate	13,806	25,543	68,471	62,203	18,190
Single-family 5- and 7-year Balloon/Reset	3,822	9,984	24,497	28,184	12,471
Single-family adjustable-rate(2)	20,949	17,482	21,172	15,512	7,793
Multifamily	1,565	847	191	27	236
Total	$98,386	$124,246	$229,706	$191,126	$99,965

(1) Includes single-family 20-year fixed-rate mortgages and mortgage revenue bonds.
(2) Includes FHA/VA mortgages purchased and held in Freddie Mac's retained mortgage portfolio in securitized form (*i.e.*, Government National Mortgage Association ("GNMA" or "Ginnie Mae") Certificates).

Freddie Mac purchases single-family mortgages primarily by issuing commitments pursuant to which it agrees in advance to purchase specified dollar amounts of mortgages for delivery for cash or securities over a specified period of time such as three, six or twelve months. These contracts are called "master commitments." Sellers enter into master commitments to assure a secondary market outlet for the mortgages they expect to originate and sell over the term of the contract and to lock in the underwriting standards that will apply to those mortgages, and in some cases, to lock in the management and guarantee fees payable to Freddie Mac. Freddie Mac commits to purchase mortgages for either mandatory or optional delivery. By entering into master commitments with sellers, Freddie Mac seeks to assure that it will receive a competitive share of the mortgages the sellers originate over the contract term. As of December 31, 1995, Freddie Mac had approximately $31.4 billion in outstanding master commitments to purchase mortgages, of which approximately $20.4 billion provided for mandatory delivery (or the payment of pair-off fees in the event of non-delivery) and approximately $11 billion provided for delivery at the option of mortgage sellers. Master commitments normally are fulfilled by successive separate deliveries of mortgages by sellers. Offers to sell mortgages also are considered on a negotiated basis outside of the master commitment process. During 1995, as in 1994, Freddie Mac increased its purchases of mortgages through large transactions with major originators and competed for (but was not awarded) other similar transactions.

Freddie Mac's mortgage purchase activities have historically been concentrated in the single-family fixed-rate segment of the mortgage market. In part, this is because most borrowers in the conforming conventional market prefer fixed-rate mortgages to ARMs, particularly in lower interest-rate environments. It also reflects the preference shown by many large depository institutions for holding ARMs in their own portfolios at least during the first several years after originating them, rather than promptly selling them in the secondary market as they routinely do with most of their new fixed-rate originations. The ability of such institutions to fund ARMs with relatively low-cost deposit liabilities provides them with an attractive spread and enables them to compete effectively for ARM originations against mortgage bankers and other originators, which tend to have higher funding costs and to be less deeply capitalized than depository institutions. As a result, the percentage of ARMs available for purchase by Freddie Mac has been and continues to be considerably smaller than the percentage of fixed-rate mortgages.

Financing of Mortgage Purchases

Freddie Mac finances its mortgage purchases by securitizing mortgages as PCs, and with short- and long-term debt securities, other liabilities and equity capital. The relative amounts of mortgages that are retained or securitized are determined in accordance with the corporation's overall capital and interest-rate risk management strategies. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Results of Operations — Net Interest Income on Earning Assets."

The following table presents the relative proportions of the total mortgage portfolio represented by the sold and retained portfolios as of December 31 for each of the years shown.

Sold and Retained Portfolios

	As of December 31,				
	1995	1994	1993	1992	1991
Sold Portfolio					
Single-Class PCs	37.4%	36.9%	35.4%	43.2%	56.0%
Multiclass PCs	43.6	49.6	53.6	49.6	38.2
Total Sold Portfolio	81.0%	86.5%	89.0%	92.8%	94.2%
Retained Portfolio	19.0%	13.5%	11.0%	7.2%	5.8%
Total Mortgage Portfolio	100.0%	100.0%	100.0%	100.0%	100.0%

Mortgage-Related Securities
(dollars in billions)

	Year ended December 31,				
	1995	1994	1993	1992	1991
Original Issue PCs(1)					
Single-family 30-year fixed-rate(2)	$54.4	$ 65.8	$103.1	$ 80.2	$57.3
Single-family 15-year fixed-rate	13.1	24.6	61.7	57.9	16.2
Single-family 5- and 7-year Balloon/Reset	3.7	9.9	23.1	25.9	11.4
Single-family adjustable-rate	14.3	16.6	20.8	15.2	7.6
Multifamily	0.4	0.2	—	—	—
Total	$85.9	$117.1	$208.7	$179.2	$92.5
Exchanges: 75-day PCs to Gold PCs®	$ 1.2	$ 1.0	$ 4.1	$ 9.2	$16.2
Resecuritized PCs(3)					
Multiclass PCs	$15.4	$ 73.1	$143.4	$131.3	$72.0
Giant PCs	20.0	37.5	41.3	22.0	12.6
Total	$35.4	$110.6	$184.7	$153.3	$84.6

(1) Original issue PCs include both single- and multiple-class PCs backed by mortgages, rather than previously issued PCs.
(2) Includes PCs backed by single-family 20-year fixed-rate mortgages.
(3) Includes GNMA certificates resecuritized as Freddie Mac Multiclass and Giant PCs.

The following table sets forth Freddie Mac's original issue settlement activity for its PCs by PC type during the years shown.

PC Settlements
(dollars in billions)

	Year ended December 31,				
	1995	1994	1993	1992	1991
Gold PCs®	$71.6	$100.5	$187.9	$63.8	$81.7
75-day PCs(1)	14.3	16.6	20.8	15.4	10.8
Total	$85.9	$117.1	$208.7	$79.2	$92.5

(1) PCs issued under the corporation's 75-day PC programs include all PCs backed by ARMs, graduated payment, tiered-payment, and growing equity mortgages and certain Multifamily PCs.

Single-Class Securities

PCs and Multifamily PCs. The majority of single-family mortgages acquired by Freddie Mac are sold as PCs. Freddie Mac also sells Multifamily PCs backed by multifamily mortgages acquired in both cash and structured transactions. PCs are original issue single-class securities that represent undivided interests in first-lien or second-lien, fixed-rate or adjustable-rate, conventional or FHA/VA single-family mortgages and provide for monthly payment of interest and pass-through of principal due or collected on the underlying mortgages. Freddie Mac receives a management and guarantee fee with respect to its outstanding PCs. Freddie Mac guarantees the payment of interest due on PCs and the principal of the underlying mortgages.

Giant PCs. Giant Mortgage Participation Certificates ("Giant PCs") are resecuritized single-class mortgage-related securities. Giant PCs provide a means for combining existing PCs to meet a market need, and for aggregating single-family PCs into larger pools, thereby creating a more liquid security. Giant PCs represent beneficial ownership interests in pools consisting primarily of PCs or other Giant PCs. Freddie Mac's guarantees with respect to Giant PCs are economically equivalent to the guarantees on the underlying PCs.

Multiple-Class Securities

Freddie Mac has issued a number of types of securities that divide the cash flows of the underlying mortgages, PCs or other securities into classes having a variety of features. These features include, among other things, variations relating to (i) expected maturities or weighted average lives; (ii) whether principal and interest, principal only or interest only is to be received and (iii) whether the coupon (if any) on the class is fixed or variable rate (and if variable rate, the index to which the variable rate relates). Freddie Mac's multiple-class mortgage-related securities include Multiclass Mortgage Participation Certificates ("Multiclass PCs"), Multiclass GNMA-Backed Securities, Stripped Giant Mortgage Participation Certificates ("Stripped Giant PCs") and Stripped Giant GNMA-Backed Securities. Multiple-class securities backed directly or indirectly by PCs provide a means for improving the liquidity and value of PCs.

Multiclass PCs. Freddie Mac's principal activity in the area of multiple-class securities is the issuance and sale of Multiclass PCs that qualify for treatment as Real Estate Mortgage Investment Conduits ("REMICs") under the Internal Revenue Code. To date, Freddie Mac has issued Multiclass PCs representing beneficial ownership interests in pools consisting of PCs, Giant PCs, Stripped Giant PCs, other Multiclass PCs, multifamily mortgages, manufactured housing installment sale contracts and REMIC securities issued by issuers other than Freddie Mac. Multiclass PCs are issued in series, with each series consisting of two or more classes. Freddie Mac also issues Multiclass GNMA-Backed Securities that qualify for REMIC treatment. Multiclass GNMA-Backed Securities are similar to Multiclass PCs in most respects. The primary difference is that the pools underlying Multiclass GNMA-Backed Securities consist of GNMA Certificates, Giant GNMA-Backed Securities or securities issued under GNMA's REMIC program.

Stripped Giant PCs. Stripped Giant PCs are resecuritized securities issued in classes or "strips," each of which is entitled to receive interest only, principal only or a specified portion of the principal and interest payments received on an underlying pool of securities. Freddie Mac issues Stripped Giant PCs backed by PCs, Giant PCs and classes of Multiclass PCs including Gold MACS® (Modifiable And Combinable Securities). Gold MACS® are multiple-class stripped securities that are issued with various coupons and that permit a holder to exchange with Freddie Mac a class or classes of a Gold MACS® series for a different class or classes of the same Gold MACS® series, thereby changing the coupons of the securities held.

Market Conditions and Competition

The volume of Freddie Mac's mortgage purchases depends primarily on the volume of conforming conventional mortgages originated in the primary market, the share of conforming conventional mortgages sold into the secondary market and the share of those mortgages sold to Freddie Mac rather than its principal competitor, Fannie Mae. Freddie Mac is limited in its mortgage purchases to conforming mortgages that satisfy mortgage principal amount limits and credit-related standards mandated by statute.

Freddie Mac estimates that approximately $575 billion of conventional single-family mortgages were originated in 1995; a total of approximately $220 billion, or 38 percent of that amount, were sold to Freddie Mac and Fannie Mae. Freddie Mac and Fannie Mae purchased a combined total of approximately 47 percent and 54 percent of the conventional single-family mortgages originated in 1994 and 1993, respectively.

Freddie Mac and Fannie Mae generally compete for the purchase of the same types of mortgages. The two companies are structured similarly and have the same business lines. Freddie Mac competes on the basis of its products, services and business processes, the liquidity of its securities in the secondary mortgage markets and its pricing strategies and credit standards. Once a decision to sell a conforming mortgage is made by a mortgage originator, the entity to which the mortgage is sold depends on the originator's assessment of, among other things, the relative attractiveness of Freddie Mac's and Fannie Mae's products, services and prices. That assessment is reflected in the relative market shares of the two companies. Freddie Mac's share of the conventional single-family mortgages sold to the two entities in

1995 was approximately $91 billion, or 42 percent. In 1994 and 1993, Freddie Mac's share of secondary market sales of newly originated mortgages to the two entities was 44 percent and 45 percent, respectively.

The markets for Freddie Mac's original issue and resecuritized securities are closely interrelated. The issuance of resecuritized mortgage securities by Freddie Mac supports the market for PCs. Although interest rates are generally the most significant determinant of PC prices, significant resecuritization activity also tends to increase the prices (and thus reduce the yields) of both PCs and mortgages. When demand for Multiclass PCs and other resecuritized securities diminishes (as it did in 1994 and 1995), PC prices may be adversely affected.

Following rapid interest rate increases in early 1994, certain types of multiple-class mortgage-related securities experienced substantial decreases in liquidity. As a result of the difficulty experienced by some investors in such securities in finding acceptable opportunities to liquidate their investments, and following investment losses incurred by such investors, market demand for multiple-class mortgage-related securities generally has decreased. These developments also have led to legislative proposals and regulatory initiatives that have tended to decrease demand for multiple-class mortgage-related securities. These developments may represent cyclical phases rather than permanent changes in the character of the markets for these securities, and future changes in the market and general economy may stimulate investor appreciation for the risk/reward opportunities provided by such securities.

The level of Freddie Mac's Multiclass PC issuances in future periods may be adversely affected by increasing activity by other issuers of multiple-class securities similar to those of Freddie Mac and Fannie Mae (including GNMA as well as private issuers of mortgage-related and other asset-backed securities). To date, there has been only a limited number of GNMA multiple-class securities transactions. Investors have tended to favor these GNMA securities over Freddie Mac's Multiclass GNMA-Backed Securities. The competitive effect of a GNMA program on the volume and fees of Freddie Mac's multiple-class securities program backed by its own securities cannot be assessed at this time, although management believes a material effect is unlikely. However, in 1995 the volume of mortgage-related securities issued by private issuers exceeded the combined volume of multiple class securities issued by both Freddie Mac and Fannie Mae.

Competition is also a consideration in connection with the issuance of Freddie Mac's non-mortgage-related debt securities. Freddie Mac competes for funds raised through the issuance of unsecured debt in the "agency" debt market with other GSEs, including Fannie Mae, the Student Loan Marketing Association, the Federal Home Loan Bank ("FHLB") system, and other governmental and non-governmental issuers. Increases in the issuance of unsecured debt by other GSEs generally, and the issuance of callable debt in particular, may have an adverse effect on the issuance of Freddie Mac's unsecured debt, or result in the issuance of such debt at higher interest rates than would otherwise be the case. In addition, the availability and cost of funds raised through the issuance of certain types of unsecured debt may be affected adversely by regulatory initiatives that tend to reduce investments by certain depository institutions in unsecured debt with greater than normal volatility or interest-rate sensitivity. See "Regulation and Governmental Relationships — Regulations Affecting Mortgage-Related and Debt Securities."

Freddie Mac and Fannie Mae enjoy significant advantages because of their economies of scale and long-term market presence in the secondary market for conforming mortgages. However, an increasing number of mortgage originators, including members of the FHLB system, retain newly originated mortgages for at least some period of time (in particular, ARMs prior to their initial rate adjustments). The ability of such portfolio lenders to finance mortgage originations by means other than through sales of mortgages into the secondary market has heightened competition for mortgage purchases. This source of competition becomes more significant in rising interest rate environments when market conditions tend to favor ARM originations.

The Secretary of HUD, Congress and others have proposed significant changes in the role and structure of FHA. FHA provides insurance for both single-family and multifamily housing. The reform proposals have generally addressed only the single-family FHA program. The single-family FHA

insurance program insures the full principal amount of individual mortgages with original principal amounts up to a maximum of $155,250, depending upon property location. Most mortgages insured under the FHA single-family program have LTV ratios in excess of 90 percent and are underwritten to standards that are often less stringent than those used by Freddie Mac. The reform proposals have ranged from privatizing FHA and expanding its authority to insure different types of mortgage products, to restricting its authority by limiting the FHA to providing pool insurance on mortgages held by Freddie Mac or other market participants. Modifying FHA's structure and expanding its authority could place additional competitive pressures on Freddie Mac. Alternatively, restricting FHA's authority could increase the share of mortgages originated by the conventional market.

In late 1995 and early 1996, market uncertainty arose over the federal government's willingness and ability to make scheduled payments on U.S. Treasury securities and other debts in the event the Congressionally authorized ceiling on outstanding government debt was not raised. Because Freddie Mac's debt and other fixed-income securities are priced and trade by reference to Treasury securities, the corporation's access to the capital markets, its funding and investment operations, and other activities potentially could be disrupted in the event of a default on, or downgrading or interruption in the issuance of, U.S. Treasury securities.

Defaults, Foreclosures and REO

General

In the normal course of business, certain of the mortgages retained or securitized by Freddie Mac will default and be foreclosed upon. In most of these cases, Freddie Mac acquires the real estate securing such mortgages as real estate owned ("REO"). Defaults that lead to foreclosure and/or acquisition of property as REO often result in losses to Freddie Mac because the amount realized upon ultimate disposition of a property and/or recoveries under applicable mortgage insurance policies or from other sources may not be sufficient to pay all principal, financing costs, foreclosure expenses and other costs related to holding the property pending disposition. The remaining defaults generally involve either repurchases by sellers of conventional mortgages or FHA/VA mortgages on which Freddie Mac receives insurance or guaranty payments.

For those mortgages that default, significant periods of time may elapse after default and foreclosure before Freddie Mac acquires title to, and may exercise its right to sell, REO. Foreclosure proceedings on single-family mortgages typically are not initiated until a mortgage has been delinquent for at least 90 days. State law imposes varying notice and other requirements with respect to foreclosure actions (including, in some states with judicial foreclosure procedures, a requirement for time-consuming court proceedings at several stages of the foreclosure process). In addition, some state statutes grant to borrowers rights to redeem properties for periods of up to two years after foreclosure. Freddie Mac generally does not acquire clear title to these properties until the expiration of any such right.

For those properties that become REO, Freddie Mac's policy generally is to dispose of such properties at market value as quickly as possible, taking into consideration local market conditions. Consistent with prudent management, Freddie Mac occasionally rents acquired properties pending sale in order to reduce its carrying costs and losses. Freddie Mac also may make repairs prior to sale in order to increase the value of the acquired property and, in the case of a multifamily property, in order to increase the cash flow on the property.

Due to the time and expense of acquiring, managing and disposing of property, foreclosure is not always the most effective method of resolving problems associated with non-performing mortgages. As a result, Freddie Mac has increased its use of alternative loss mitigation strategies for single-family and multifamily mortgages. These strategies include pre-foreclosure sales (in which the corporation accepts less than the full principal balance outstanding on the mortgage), loan modifications and other forms of refinancing, forbearance and other foreclosure alternatives. Foreclosure alternatives have tended to accelerate charge-offs for affected properties, but are expected to reduce overall credit costs by eliminating costs associated with acquisition, management and disposition of properties taken in foreclosure. Accordingly, the corporation expects that the increasing use of foreclosure alternatives ultimately will reduce the number of foreclosed properties and the overall level of credit-related expenses. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Credit Risk — Non-performing Assets."

Freddie Mac manages the risk of loss from defaults, foreclosure and REO activities by monitoring and managing the various factors that influence this risk. The most significant of these factors are the quality and effectiveness of the corporation's mortgage purchase underwriting standards; the sensitivity of the total mortgage portfolio to changing economic conditions; and the corporation's ability to resolve and dispose of its REO assets on terms advantageous to Freddie Mac. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Credit Risk."

REO Activities

Freddie Mac's REO activities during 1995 and 1994 are reflected in the table below.

Single-Family REO

	Number of REO properties in inventory as of January 1	Number of property acquisitions	Number of property dispositions	Number of REO properties in inventory as of December 31	Average holding period (in days)	Average net loss per property disposition(1)
1995	8,632	15,530	16,116	8,046	210	$39,266 (35% loss rate)
1994	7,670	15,289	14,327	8,632	200	$35,353 (33% loss rate)

Multifamily REO

	Number of REO properties in inventory as of January 1	Number of property acquisitions	Number of property dispositions	Number of REO properties in inventory as of December 31	Average holding period (in days)	Average net loss per property disposition(1)
1995	170	47	121	96	463	$829,902 (57% loss rate)
1994	218	171	219	170	400	$614,641 (55% loss rate)

(1) Cumulative net mortgage and REO-related losses with respect to properties disposed of in the indicated year. Comprised principally of mortgage charge-offs, uncollected interest, REO holding period income and expenses, REO valuation adjustments and REO disposition gains or losses. Excludes net losses on facilitated sales of defaulted mortgages prior to foreclosure.

Note 6 of Notes to Consolidated Financial Statements summarizes Freddie Mac's REO activity for the years ended 1995, 1994, and 1993. For further information concerning Freddie Mac's single-family and multifamily REO, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Credit Risk — Credit Performance."

Economic weakness in California has led to increased REO acquisitions of single-family properties in that area by Freddie Mac and other financial institutions. While REO acquisitions by Freddie Mac increased in 1995 (and may increase further in future periods), they are expected to remain a small percentage of Freddie Mac's overall asset base. Freddie Mac anticipates, however, that its ability to dispose of REO properties in a timely manner and/or at advantageous prices in the near future may be adversely affected, particularly in the West, by the increasing volume of REO properties in that region offered for sale by the corporation and by other financial institutions.

Set forth below is a five-year mortgage loss analysis of the total mortgage portfolio.

Mortgage Loss Analysis(1)

	1995	1994	1993	1992	1991
Total Servicing Portfolio:			(dollars in millions)		
Average portfolio balance, net	$543,982	$522,189	$465,138	$407,500	$356,876
Year-end portfolio balance, net	566,751	533,376	494,725	441,376	386,067
Net charge-offs	305	227	325	367	290
Provision for mortgage losses	255	200	300	425	407
Year-end reserve for losses on mortgages	683	733	760	785	737
Net charge-offs to average portfolio balance	0.06%	0.04%	0.07%	0.09%	0.08%

(1) Information prior to 1994 does not include pro forma adjustments to reflect the adoption in 1994 of a change in the reporting of uncollectible interest on single-family mortgages.

For financial reporting purposes, the majority of credit costs are recognized at the time of foreclosure in the form of charge-offs and provisions for estimated selling expenses. At foreclosure, the mortgage is transferred to REO at fair value with any excess of the cost basis in the loan over the fair value of the property being recorded as a charge-off to the Reserve for mortgage losses. Also at foreclosure, estimated costs to sell single-family properties are recognized as REO operations expense. Estimated costs to sell multifamily properties are accounted for through provisions to the Reserve for mortgage losses. Subsequent to foreclosure, market conditions, property damage and other factors may cause the estimated fair value of the property to decrease during the time the property is held by Freddie Mac. Such losses are recognized currently as REO operations expense.

On January 1, 1995, Freddie Mac adopted Statement of Financial Accounting Standards ("SFAS") No. 114, "Accounting by Creditors for Impairment of a Loan," as amended by SFAS No. 118, "Accounting by Creditors for Impairment of a Loan — Income Recognition and Disclosures." Under SFAS No. 114, loans are transferred to REO at foreclosure, the point at which the corporation obtains physical possession of the property. Prior to SFAS No. 114, loans were transferred to REO prior to foreclosure when the borrower had minimal equity in the underlying collateral, repayment was expected to come only from the operation or sale of the collateral, and the borrower had effectively abandoned control of the collateral. Prior period multifamily mortgage and REO balances have been restated to reflect the adoption of SFAS No. 114. The adoption of SFAS No. 114 did not have a material effect on results of operations.

Litigation

Freddie Mac is involved as a party to a variety of legal proceedings arising from time to time in the normal course of its business. Freddie Mac is most frequently involved, directly or indirectly, in litigation involving mortgage foreclosures. Another type of proceeding arises out of the termination by the corporation of a seller/servicer's eligibility to sell mortgages to and service mortgages for Freddie Mac. In these cases, the former seller/servicer sometimes seeks damages against Freddie Mac for wrongful termination under a variety of legal theories. In addition, Freddie Mac is sometimes sued in connection with the origination or servicing of mortgages. These suits generally involve claims alleging wrongful actions of seller/servicers. The contracts between Freddie Mac and its seller/servicers generally provide for indemnification of the corporation for liability arising from wrongful actions by such seller/servicers.

Another type of dispute arises from Freddie Mac's ownership of properties after foreclosure as REO. Certain liability risks associated primarily with Freddie Mac's multifamily and 2- to 4-unit REO, such as tort liability to third parties and compliance with applicable environmental requirements, are typical of those associated with property ownership generally. Among the tort claims with which the corporation is currently dealing are claims involving alleged injury to juvenile tenants caused by the exposure to lead-based paint. In addition, Freddie Mac is named as a defendant in a class action lawsuit involving alleged lead paint hazards in certain buildings it owns in New York City. *German v. FHLMC, et al.*, 93 Civ. 6941 (S.D.N.Y.). Although this litigation is in its early procedural stages and it is not

possible to predict the outcome, Freddie Mac does not believe that the litigation would have a material adverse effect on the corporation's financial condition or results of operations.

Litigation and claims resolution are subject to many uncertainties and are not susceptible to assurable predictability. Nevertheless, management believes that the outcome of all currently pending claims will not have a material adverse effect on the corporation's financial condition or results of operations.

REGULATION AND GOVERNMENTAL RELATIONSHIPS

From time to time, Freddie Mac's statutory, structural and regulatory relationships with the federal government may be subject to review or modification. While Freddie Mac's GSE status is often advantageous for the corporation, on occasion proposals have been advanced that could adversely affect Freddie Mac's fulfillment of its statutory purposes, as well as the corporation's results of operations.

Regulation of Freddie Mac

Freddie Mac is subject to oversight by three agencies of the federal government; the Office of Federal Housing Enterprise Oversight ("OFHEO"), an independent office within HUD created by the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the "GSE Act"); the Secretary of HUD and the Secretary of the Treasury.

OFHEO Oversight

The GSE Act provided for the creation of a separate office within HUD, substantially independent of the Secretary of HUD, headed by a director (the "Director"), appointed by the President of the United States and confirmed by the Senate, for a five-year term. The Director has exclusive regulatory authority for ensuring the adequate capitalization and safe operation of Freddie Mac in accordance with the GSE Act. The Director is required, among other things, to conduct an annual on-site examination of both Freddie Mac and Fannie Mae to determine the condition of each enterprise for the purpose of ensuring its financial safety and soundness. The Director is authorized to levy annual assessments, payable semiannually, on the two enterprises to cover OFHEO's reasonable expenses.

The Director is required under the GSE Act to establish and monitor compliance with three separate capital standards applicable to both Freddie Mac and Fannie Mae. These capital standards consist of a minimum capital measure, a critical capital measure and a risk-based capital measure.

The minimum capital standard requires Freddie Mac to maintain "core capital" equal to the sum of 2.50 percent of its aggregate on-balance sheet assets, determined in accordance with GAAP, and 0.45 percent of its aggregate off-balance sheet obligations (consisting of the unpaid principal balance of outstanding mortgage-related securities and substantially equivalent instruments issued or guaranteed by it, other off-balance sheet obligations and one-half of its average mortgage purchase commitments). In the case of other off-balance sheet obligations and mortgage purchase commitments, the Director is required to adjust the percentage to reflect differences in the credit risk of those obligations and commitments in relation to mortgage-related securities. In June 1995, OFHEO issued a proposed minimum capital regulation, which would not change significantly OFHEO's current implementation of the minimum capital standard. OFHEO has announced that it expects to issue a final minimum capital regulation in 1996.

The critical capital requirement involves the same structure as the minimum capital standard except that the percentages for on-balance sheet assets and off-balance sheet obligations are 1.25 and 0.25, respectively.

The risk-based standard includes credit risk and interest-rate risk components and an additional amount of capital for management and operations risk. Together, the credit risk component and the interest-rate risk component consist of an amount of "total capital" determined by the Director to be sufficient for Freddie Mac to maintain positive capital for a period of ten years under specified highly stressful economic scenarios. Total capital consists of "core capital" (defined to include the sum of the

par value of outstanding stock, paid-in capital and retained earnings, as determined in accordance with GAAP), unallocated reserves for mortgage and certain foreclosure losses and any other amounts from sources of funds available to absorb losses that the Director determines to be appropriate to include in determining total capital. Freddie Mac has utilized an internal risk-based capital model for asset-liability management purposes for several years.

In February 1995, the Director published an Advance Notice of Proposed Rulemaking ("ANPR") soliciting written public comments prior to publication of a proposed risk-based capital standard. The ANPR discussed a substantial number of issues and policy alternatives raised by the Director under the statutory risk-based capital requirement, and requested comments on the appropriate capital measurement of credit risk, interest-rate risk and related issues. The Director has stated that a proposed risk-based capital regulation will be issued for public comment in 1996 and that, due to the complexity of the subject, the proposed regulation likely will be issued in the form of two separate proposals. Following the submission and consideration of public comments, a final risk-based capital regulation will be issued. Under the GSE Act, the final regulation will become effective immediately upon issuance.

The GSE Act provides that Freddie Mac must be classified at least quarterly within one of four levels of capital adequacy. Currently, OFHEO bases its capital classifications on whether Freddie Mac's core capital level meets the minimum and critical capital standards. One year after the effective date of a final risk-based capital regulation, OFHEO also will base its capital classifications on whether Freddie Mac's total capital level meets the risk-based capital standard.

In the event that Freddie Mac is classified as less than adequately capitalized, the GSE Act requires the Director to take a number of mandatory remedial measures and provides the Director with discretionary authority to take various optional measures depending on the category in which Freddie Mac is classified. The remedial measures are similar to those available to regulators of other federally chartered or insured financial institutions. Freddie Mac will not be subject to any of the remedial measures if it is classified as adequately capitalized, although certain violations of law, or practices that could lead to a rapid depletion of the corporation's capital, also would be subject to sanctions under other provisions of the GSE Act.

In its first classification of Freddie Mac, the Director classified Freddie Mac as "adequately capitalized" as of June 30, 1993, and the Director has classified Freddie Mac as "adequately capitalized" in each of its subsequent classifications to date.

HUD Oversight

Affordable Housing Goals. The GSE Act requires the Secretary of HUD to establish three mortgage purchase goals for Freddie Mac: a goal for the purchase of mortgages on housing for low- and moderate-income borrowers (the "Low- and Moderate-Income Goal"); a goal for the purchase of mortgages on housing located in central cities, rural areas and other underserved areas; and a special affordable housing goal for the purchase of mortgages on housing for low-income persons in low-income areas and for very low-income persons (the "Special Affordable Goal"). In October 1993, the Secretary of HUD established interim housing goals for the transition period of 1993 and 1994. In November 1994, the Secretary extended the interim housing goals through 1995, pending the adoption of final regulations. During the transition period, the goal for the purchase of mortgages on housing located in central cities, rural areas and other underserved areas included only purchases of mortgages on housing located in areas designated as central cities by the United States Office of Management and Budget (the "Central Cities Goal").

In December 1995, the Secretary of HUD issued final regulations establishing new affordable housing goals for years 1996 through 1999. Under the final regulations, HUD redefined the goal for the purchase of mortgages on housing located in central cities, rural areas and other underserved areas to measure mortgage purchases based on the income and minority composition of targeted metropolitan and rural areas (the "Underserved Areas Goal"). The new goals provide that 40 percent of the total number of dwelling units financed by the corporation's mortgage purchases meet the Low- and Moderate-Income Goal in 1996 and 42 percent in each of 1997, 1998, and 1999; 21 percent of the total

number of dwelling units financed by the corporation's mortgage purchases meet the Underserved Areas Goal in 1996 and 24 percent in each of 1997, 1998 and 1999, and 12 percent of the total number of dwelling units financed by the corporation's mortgage purchases meet the Special Affordable Goal in 1996 and 14 percent in each of 1997, 1998 and 1999, including at least $981 million in qualifying multifamily mortgage purchases in each year from 1996 through 1999.

Under the GSE Act, if the Secretary of HUD finds that Freddie Mac has failed to meet or there is a substantial probability that Freddie Mac will not meet any of the housing goals and that the goals are "feasible," the Secretary of HUD may require Freddie Mac to prepare a "housing plan" that describes the specific actions Freddie Mac will take to achieve the goal for the next calendar year or to make improvements as are reasonable in the remainder of the current year. The Secretary of HUD is empowered to issue cease and desist orders or to assess civil money penalties upon a finding, after a hearing on the merits, that Freddie Mac has failed to make a timely submission of a housing plan complying with the GSE Act or to make a good faith effort to comply with a housing plan approved by the Secretary of HUD. For further information on Freddie Mac's performance under these affordable housing goals, see "Management's Discussion and Analysis of Financial Condition and Results of Operations — Results of Operations — Regulatory Matters — Housing Goals."

In 1995, the Secretary requested Freddie Mac to file a housing plan, in accordance with the GSE Act, based on Freddie Mac's failure to meet the Central Cities Goal for 1994. Freddie Mac filed this plan in accordance with the Secretary's request, detailing the corporation's efforts to increase its mortgage purchases in underserved areas, including OMB-designated central cities.

By letter dated March 4, 1996, the Secretary notified Freddie Mac of his determination that the corporation failed to meet the 1995 Central Cities Goal, that the corporation had up to 30 days to comment on that determination, and that the Secretary proposed to require Freddie Mac to submit a housing plan describing the specific actions that Freddie Mac will take to meet the 1996 Underserved Areas Goal.

Fair Lending. Freddie Mac is subject to the anti-discrimination provisions of the Fair Housing Act. In addition, the GSE Act requires the Secretary of HUD to adopt regulations prohibiting Freddie Mac from engaging in discriminatory practices in its mortgage purchase activities and periodically to review and comment on Freddie Mac's underwriting and appraisal guidelines for consistency with the Fair Housing Act and the GSE Act. The GSE Act also requires the Secretary of HUD to direct the enterprises to (i) submit data to HUD to assist HUD in investigating whether a mortgage lender with which the enterprise does business has failed to comply with the Fair Housing Act or the Equal Credit Opportunity Act and (ii) undertake remedial actions, including suspension, probation, reprimand or settlement, against lenders that are found to have engaged in discriminatory lending practices in violation of the Fair Housing Act or the Equal Credit Opportunity Act ("ECOA") pursuant to a final adjudication and after opportunity for an administrative hearing. In December 1995, HUD issued final regulations implementing the fair housing provisions of the GSE Act.

New Program Approval. Under the GSE Act, Freddie Mac must obtain the approval of the Secretary of HUD for any new Freddie Mac program before implementing the program. The law defines a "new program" as a program for the purchasing, servicing, selling, lending on the security of, or otherwise dealing in, conventional mortgages that (i) is significantly different from programs that were approved or engaged in by Freddie Mac before the date the GSE Act was enacted or (ii) represents a material expansion of programs above limits expressly contained in any prior approval. There have been no such HUD-imposed limits applicable to Freddie Mac's mortgage programs. The Secretary of HUD is required to approve any new program unless the Secretary of HUD determines that the new program is not authorized under the Freddie Mac Act or that the program is not in the public interest. In addition, the GSE Act also provides new program approval authority to the Director of OFHEO for a transition period ending 12 months after the risk-based capital regulations become effective.

In December 1995, HUD issued final regulations implementing the new program approval authority granted under the GSE Act. Under the regulations, HUD may request information about any program which it believes may be subject to prior approval. Freddie Mac is required to seek prior approval only for new programs that are "significantly different" from current activities. The term "significantly different" is not defined in the regulations. In adopting these regulations, the Secretary indicated his intention to implement his new program approval authority under the GSE Act in a manner that avoids the creation of undue burdens on the GSEs and fosters competition.

Treasury Oversight

The Secretary of the Treasury must approve the issuance of, including the interest rates and maturities on, all notes, debentures and substantially identical types of unsecured debt obligations of Freddie Mac, as well as the issuance of types of mortgage-related securities not issued prior to the enactment of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"). The Secretary of the Treasury performs this function by coordinating GSE and agency debt offerings with Treasury Department funding activities.

Regulations Affecting Mortgage-Related and Debt Securities

In addition to being subject to governmental regulation of its own business activities, Freddie Mac's issuance and sale of mortgage-related and debt securities is affected by a broad array of legislative and regulatory actions related to the activities of banks, savings institutions, insurance companies, securities dealers and other regulated entities that comprise a significant part of Freddie Mac's customer base for these securities. As is the case with the regulation of many businesses, certain aspects of the regulations affecting its customers are beneficial to Freddie Mac (for example, the generally favorable treatment of mortgage-related securities as compared with unsecuritized mortgages under risk-based capital regulations applicable to depository institutions). Other provisions (for example, limitations on the ability of regulated institutions to purchase and own certain types of mortgage-related securities based upon concerns about the prepayment sensitivity and illiquidity of such securities) may have a constraining effect on the marketability of the corporation's securities. The more significant of these regulatory provisions are summarized below.

Risk-Based Capital Regulations

Risk-based capital regulations adopted by the various federal bank and savings association regulatory agencies affect Freddie Mac's single-class and multiple-class securities programs. Among other things, these regulations assign lower credit-risk weights to most mortgage-related securities issued or guaranteed by Freddie Mac and Fannie Mae than to the underlying mortgages themselves, thereby requiring regulated financial institutions to maintain higher levels of capital for a given quantity of unsecuritized mortgages than would be required for an equivalent quantity of mortgage-related securities.

Risk-based capital regulations applicable to insured depository institutions also may affect the market for mortgage-related securities issued by Freddie Mac and others. These regulations generally assign Freddie Mac and Fannie Mae mortgage-related securities, including those backed by GNMA Certificates, to the second lowest risk weight, while GNMA-guaranteed securities are assigned the lowest risk weight, thereby eliminating the need to maintain any risk-weighted capital in support of GNMA securities. Accordingly, the capital costs of holding Freddie Mac and Fannie Mae securities as investments are higher for federally insured depository institutions than the costs of holding comparable GNMA-guaranteed securities.

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") mandated that each of the federal bank and savings association regulatory agencies revise their risk-based capital standards to ensure that those standards adequately take into account interest-rate risk. Under these standards, financial institutions with high levels of measured risk are subject to increased capital requirements. To a certain extent, these rules have an adverse effect on the market for certain types of mortgage-related securities that increase the capital requirements for insured depository institutions.

Conversely, certain aspects of these rules permit (and may even facilitate) purchases of certain types or combinations of mortgage-related securities that tend to reduce the interest-rate risk exposure of a particular institution.

Most mortgages sold to Freddie Mac are sold "without recourse" for purposes of the financial institution risk-based capital regulations. Under these regulations, sales of mortgages to Freddie Mac that involve recourse to the seller generally have been treated as if the mortgages had not been sold. By requiring banking and savings institutions to maintain the same capital levels as would be required if the mortgages had not been sold, these regulations discourage such institutions from selling mortgages in the secondary market on a recourse basis. Sellers may provide credit enhancements that protect Freddie Mac from credit risk in forms other than recourse. Depending upon the particular arrangement involved, these credit enhancements may or may not be treated for regulatory purposes as recourse sales.

In the first quarter of 1995, the Federal Reserve Board and the Federal Deposit Insurance Corporation ("FDIC") adopted amendments to their risk-based capital guidelines for assets sold with specified low levels of recourse. Under these amendments, when a bank sells a mortgage with such limited recourse, its risk-based capital requirement would reflect only the amount of risk actually remaining with the bank. This may encourage banks to sell mortgages with limited recourse in the future. In addition, comprehensive revisions to the risk-based capital requirements for mortgages sold with recourse are under consideration by other banking regulatory agencies. If adopted, these revisions could increase or decrease the amount of capital particular banks and savings institutions would be required to hold under various circumstances.

Similarly, the National Association of Insurance Commissioners ("NAIC") has issued risk-based capital guidelines for life insurance and related companies. Under the guidelines, capital requirements applicable to mortgage-related securities with a rating of "A" or better (including Freddie Mac mortgage-related securities) are significantly lower than capital requirements applicable to the underlying mortgages themselves.

Other Regulations Affecting Financial Institutions

FFIEC Policy Statement. The Federal Financial Institutions Examination Council ("FFIEC"), whose members include several agencies that regulate depository institutions, adopted a Supervisory Policy Statement on Securities Activities (the "Policy Statement") that, among other things, sets forth guidelines for investing in certain types of mortgage-related securities. Under the Policy Statement, a security that, under certain tests, exhibits greater price volatility than a standard 30-year fixed-rate mortgage-related security or fails to meet certain estimated weighted-average-life criteria generally is not a suitable investment for depository institutions. Although these investments may be used as interest-rate risk reduction tools by institutions with well-managed portfolios and specific interest-rate risk policies, implementation of the Policy Statement generally has had a negative effect on the market among depository institutions for certain types of multiple-class mortgage-related securities that Freddie Mac issues.

Advisories on Structured Notes. In 1994, each of the federal bank regulatory agencies issued an advisory setting forth supervisory policies with respect to purchases of "structured notes." These advisories indicate that debt securities whose cash flows are dependent on one or more indices in ways that create the risk characteristics of forward contracts or options may be inappropriate holdings for many depository institutions. These characteristics include substantial price sensitivity, complexity, illiquidity and high amounts of leverage relative to fixed-income instruments with comparable face values. The advisories stress the need for appropriate supervision and review of investments in structured notes and indicate that it may be considered an unsafe and unsound practice to invest in these securities without the knowledge and ability to measure, monitor and manage the risks. Although these advisories potentially may have an adverse effect on the market among depository institutions for certain types of Freddie Mac debt securities, investor demand for certain complex structured notes is limited, at present, and Freddie Mac has issued a relatively small amount of this type of unsecured debt in the past two years.

Accounting Standards

The Financial Accounting Standards Board ("FASB"), the organization responsible for promulgating financial accounting and reporting standards followed by most U.S. public companies in connection with the preparation of financial statements, recently has issued a number of accounting pronouncements or proposals affecting the market for mortgage-related securities.

Mark-to-Market Accounting. SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," requires banks, savings associations, other financial institutions and other public companies that maintain investment portfolios generally to value a portion of those portfolios, including mortgage-related securities, at their actual market value, rather than at their amortized cost. SFAS No. 115 requires this "mark-to-market" adjustment to be recorded, for securities that are not "held-to-maturity," either in the reporting company's earnings or directly in its capital accounts.

Prior to the adoption of SFAS No. 115, financial institutions often classified their investments in Freddie Mac mortgage-related securities as "held-to-maturity" and valued these investments at their amortized cost. Under SFAS 115, in order to classify an investment as held-to-maturity, an investor must show both the ability and the intent to hold the investment until maturity. Sales of securities classified in the "held-to-maturity" category may result in the reclassification of all "held-to-maturity" securities and require such securities to be marked-to-market. The combined effects of SFAS No. 115 and the FFIEC Policy Statement generally have had a negative effect on the market for both original issue and resecuritized mortgage-related securities.

Accounting for Mortgage Servicing. In 1995, FASB issued SFAS No. 122, "Accounting for Mortgage Servicing Rights." SFAS No. 122, which is effective for fiscal years beginning after December 15, 1995, requires mortgage banking enterprises to recognize the right to service mortgage loans as a separate asset when an originated mortgage loan is sold or securitized with servicing rights retained, and to subsequently account for those mortgage servicing rights at the lower of cost or market value. Previously, the value of originated mortgage servicing rights was recognized over the life of the mortgage loan as net servicing income. While SFAS No. 122 does not directly affect Freddie Mac, it may have an impact on the market for mortgage-related securities to the extent SFAS No. 122 changes the motivations of financial institutions to enter into transactions in mortgage-related securities.

Accounting for Transfers of Assets. Also in 1995, FASB issued Proposed Statement of Financial Accounting Standards, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." The proposed standard on transfers of assets, which would be effective for transfers of assets occurring after December 31, 1996, would require certain transactions involving the sale and repurchase of mortgage-related securities to be accounted for as sales of assets with gains and losses on such transactions recognized immediately. Currently, these transactions often are accounted for as financing transactions. This proposed standard, if it becomes effective, could adversely affect the market for mortgage-related securities if market participants are discouraged from entering into such transactions due to the adverse accounting effects for certain investors of the treatment of such transactions as sales rather than financings.

Government Securities Dealer Regulations

The Government Securities Act Amendments of 1993 ("GSA") authorized the National Association of Securities Dealers ("NASD") and bank regulators, for the first time, to adopt sales practice rules applicable to the marketing of government securities, including securities issued by Freddie Mac and Fannie Mae. These rules, which are intended to regulate the conduct of government securities dealers and brokers, will become applicable only after the NASD, or the appropriate banking regulator, has adopted regulations implementing the authority conferred under the GSA. In 1995, the NASD reproposed certain amendments to its Rules of Fair Practice that would apply its existing sales practice rules to transactions by its members in government securities. To date, financial institution regulatory authorities have not published comparable rules applicable to sales of government securities by financial institution government securities dealers. It is unclear what effect, if any, such rules may have on the market for the corporation's securities.

State Laws

The Secondary Mortgage Market Enhancement Act of 1984 ("SMMEA") provides, among other things, that certain investors are authorized to purchase, hold and invest in securities issued or guaranteed by Freddie Mac and Fannie Mae to the same extent that the investor is authorized to purchase, hold or invest in obligations issued or guaranteed as to principal and interest by the United States or any agency or instrumentality thereof. SMMEA also provided that, prior to October 4, 1991, a state could enact legislation that prohibited or limited an investor's authority to invest in securities issued or guaranteed by Freddie Mac or Fannie Mae. Pursuant to SMMEA, 18 states currently have legislation in effect that limits the ability of certain entities chartered by such states (principally insurance companies) to invest in Freddie Mac securities. Freddie Mac does not believe that such legislation has had or will have a material adverse effect on the markets for Freddie Mac mortgage-related securities.

Certain states recently have enacted or introduced legislation that would restrict the ability of state and/or local government agencies and various state-regulated entities to invest in certain types of securities, including mortgage-related securities. It is unclear, in light of the expiration of the period for state legislative action under SMMEA, whether these states have the authority to enact or enforce any such legislation at this time, and what effect, if any, the passage of such legislation would have on the market for Freddie Mac mortgage-related securities.

In 1995, the NAIC published a proposed Investments of Insurers Model Act (the "Model Act") that would set forth guidelines for investments by insurers, including investments in mortgage-related securities, and impose additional restrictions on investments by certain insurance companies in certain mortgage-related securities. The Model Act is expected to be published in final form in 1996, and would be applicable in any particular state only in the form and to the extent adopted by that state's legislature.

Governmental Relationships

In order to support its statutory purposes, Freddie Mac's GSE status affords the corporation certain benefits such as the corporation's exemption from the registration requirements of the federal securities laws, favorable treatment of the corporation's securities under various legal investment laws and other regulations, and access to the Federal Reserve Bank of New York's book-entry system for the corporation's mortgage-related and debt securities. In addition, the Secretary of the Treasury has discretionary authority to purchase obligations issued by Freddie Mac up to a maximum of $2.25 billion outstanding at any one time. Finally, Freddie Mac also is exempt from state and local taxes, except real property tax on real estate which it owns.

From time to time, proposals have been made to change the relationship of GSEs such as Freddie Mac to the federal government. For example, various legislative and regulatory proposals have advocated the partial or complete elimination of the exemptions from registration under federal securities laws of securities issued by the GSEs, including Freddie Mac. Similarly, both federal and local government officials have proposed that the income of the GSEs be subjected to taxation by the District of Columbia or other states. In addition, from time to time other policy changes (such as the modification or elimination of the mortgage interest tax deduction) have been suggested that may affect the mortgage markets, including the secondary mortgage market. Finally, legislative and other proposals have recommended the imposition of certain fees ("user fees") by the federal government on securities issued by Freddie Mac, Fannie Mae and other GSEs. All or a portion of the proposed user fees might be passed on in the form of higher fees on newly purchased mortgages, and could cause the GSEs to shift funding of mortgage purchases away from the issuance of certain types of securities.

Separately, legislation has been introduced in Congress that would regulate the "derivatives activities" of Freddie Mac and other companies. Certain aspects of these legislative proposals would subject Freddie Mac to new or additional capital requirements, accounting requirements, risk management requirements, supervisory oversight and other substantive regulation of its present business

activities with respect to certain transactions (such as forward sales and repurchase agreements involving mortgage-related securities, and interest-rate swaps).

Under the GSE Act, the Secretary of HUD, the Comptroller General of the United States, the Secretary of the Treasury and the Director of the Congressional Budget Office were each directed to conduct and submit to Congress a study analyzing the effect of eliminating any federal sponsorship of Freddie Mac and Fannie Mae, and allowing each corporation to continue to operate as a fully private entity. Both Freddie Mac and Fannie Mae will have the opportunity to comment on these reports and express their views to Congress. In Freddie Mac's view, elimination of any federal sponsorship of Freddie Mac would be contrary to the best interests of the corporation, the secondary market for residential mortgages, and America's homeowners and renters.

Elimination or modification of Freddie Mac's various exemptions, new or additional fees or substantive regulation of Freddie Mac's business activities, any further alteration or elimination of Freddie Mac's major ties to the federal government or any significant amendments to the Freddie Mac Act or other federal legislation bearing on Freddie Mac could require or cause Freddie Mac to change the nature and/or extent of its business activities, and could adversely affect the scope of its activities and results of operations. Any modification of Freddie Mac's relationship to the federal government, including assessment of user fees, repeal of its exemptions, or any modification of the present tax treatment of mortgage interest payments, would require legislation to be passed by Congress and signed by the President. Legislation that adversely affects Freddie Mac or its shareholders, if challenged, would be subject to judicial review to ensure its conformity with the requirements of the United States Constitution (including the Fifth Amendment's ban on uncompensated takings of property). To date, Congress has not enacted any such proposals.

CUSTOMER AND MARKET SUPPORT ACTIVITIES

Securities Sales and Trading Group

Freddie Mac makes a market in its own mortgage-related and debt securities by distributing these securities to, and trading these securities with, Freddie Mac's customers and other counterparties, including mortgage sellers, investors and dealers in such securities. Trading services are organized and provided through Freddie Mac's Securities Sales and Trading Group ("SS&TG"). SS&TG buys, sells and exchanges Freddie Mac fixed-income securities in various financial transactions (including forward sales and reverse repurchase agreements) that use mortgage pass-through, debt and resecuritized securities. Such transactions are subject to limits established by the Board of Directors.

The positions in securities maintained by SS&TG, as well as the interest-rate risks of these financial transactions, are hedged with purchases and sales of Freddie Mac securities, or in certain cases with transactions in Treasury securities and mortgage pass-through securities of Fannie Mae and Ginnie Mae. To manage customer credit risk, SS&TG analyzes and monitors the financial condition and trading positions of all customers and establishes trading limits consistent with such reviews. In addition, SS&TG has established overall policies, trading procedures and controls, that are reviewed on an ongoing basis, to manage credit, interest-rate and operations risk.

Reverse Repurchase Program

Freddie Mac engages in reverse repurchase ("reverse repo") transactions through SS&TG with approved seller/servicers, depository institutions and other financial institutions and investors. In these transactions, SS&TG customers sell PCs or other Freddie Mac securities to Freddie Mac and agree to repurchase them at a later date. As of December 31, 1995, the outstanding balance of reverse repo agreements between SS&TG and its customers was approximately $6.3 billion.

Under a reverse repo agreement, Freddie Mac lends funds to its customers on the security of PCs or other securities to which the repurchase obligation relates. The customer sells the securities to Freddie Mac for cash and agrees to repurchase them on a specified future date at an agreed price that is higher than the price at which the securities were sold to Freddie Mac. The difference between the purchase price paid by Freddie Mac and the repurchase price payable by the customer represents the

"interest" component of the transaction. The customer is required to maintain collateral for its borrowings with a value equal to the outstanding indebtedness owed to Freddie Mac plus a specified margin to provide overcollateralization.

In the event of reverse repo borrower default by reason of a failure to provide additional collateral, as required by Freddie Mac, or a failure to meet repurchase obligations, Freddie Mac is entitled to liquidate the collateral. If there were a delay in liquidating the collateral following a reverse repo borrower's default, losses could result to Freddie Mac.

Distribution Activities

From time to time, SS&TG assists Freddie Mac in the distribution of its securities by acquiring securities directly at issuance from Freddie Mac for sale to investors and other market participants. Distribution activities may include participation in dealer auctions of Freddie Mac securities, conversions of 75-day PCs for Gold PCs, resecuritization of outstanding Freddie Mac securities and other transactions.

PC Price Performance

Freddie Mac supports the market for its PCs and PC prices relative to prices for Fannie Mae pass-through securities and other comparable securities, in a variety of ways including the acquisition of PCs for resecuritization as REMICs and other securities; market-making activities of SS&TG; and the purchase of PCs for Freddie Mac's retained portfolio and for other corporate purposes. Recent market support activities have included the use of several external money management firms to actively manage and trade a relatively small portion of Freddie Mac's retained portfolio, the participation by SS&TG in the dollar roll market for Freddie Mac PCs, and the initiation of a focused marketing effort to present to dealers and investors the relative advantages of trading and investing in Freddie Mac PCs. From time to time Freddie Mac awards business to dealers or other market participants based upon their levels of support in trading and making active, liquid secondary markets in PCs. Freddie Mac anticipates undertaking additional activities to support the market for PCs in the future, although it may determine to increase, reduce or discontinue all or any one of its efforts at any time.

PROPERTIES AND EMPLOYEES

Freddie Mac owns a 75 percent interest in a limited partnership that constructed Freddie Mac's corporate headquarters near Tysons Corner in McLean, Virginia. The project contemplates a five-phase development. The first phase was completed in 1991 and accommodates approximately 1,000 employees and a variety of corporate facilities in a single building comprising approximately 390,000 square feet, with the remaining headquarters functions located at Freddie Mac's other sites in Washington, D.C. and in Reston and Tysons Corner, Virginia.

In 1995, Freddie Mac completed the second and third phases of the corporate headquarters project. Freddie Mac has expended approximately $150 million to design and construct these two new buildings comprising an aggregate of approximately 454,000 square feet. These buildings accommodate a total of approximately 1,500 additional Freddie Mac employees formerly situated in leased facilities. Although Freddie Mac's occupancy expenses increased when these two new buildings were occupied, over time the corporation expects to realize savings over the cost of leasing comparable facilities.

As of December 31, 1995, Freddie Mac had 3,216 full-time and 104 part-time employees.

CAPITALIZATION

The following table sets forth Freddie Mac's capitalization as of December 31, 1995. Dollars are in millions.

Debt securities:	
Notes and bonds payable due within one year:	
Discount notes, mortgage securities sold under agreements to repurchase and medium-term notes	$ 51,458
Current portion of long-term debt	10,637
Multiclass debt securities due within one year	46
	62,141
Notes and bonds payable due after one year:	
Debentures	55,994
Medium-term notes	749
Multiclass debt securities due after one year	444
	57,187
Total debt securities, net	119,328
Subordinated borrowings due after one year, net	633
Stockholders' equity	5,863
Total capitalization	$125,824

See Notes 7, 8 and 9 to Consolidated Financial Statements for further information about Freddie Mac's debt securities, subordinated borrowings and stockholders' equity. Amounts of debt securities and subordinated borrowings are net of unamortized discounts, premiums, hedging gains or losses and debt issuance costs.

EQUITY SECURITIES

Freddie Mac is authorized to issue preferred stock and common stock in the manner and amount, and, in the case of voting common stock, subject to any limitations on concentration of ownership, as may be prescribed by the Board of Directors of Freddie Mac. There is no limitation on the number of shares of preferred stock or of voting common stock that Freddie Mac is authorized to issue.

Freddie Mac had issued and outstanding 178,790,007 shares of its voting common stock (the "Common Stock") as of December 31, 1995. Each share of the Common Stock has a par value of $0.84 per share. In June 1995, the Board of Directors authorized the repurchase by the corporation of up to $200 million in Common Stock, which amount was repurchased between June 1995 and February 1996 in open market transactions. On March 1, 1996, the Board of Directors authorized the repurchase of up to $1 billion in additional shares of Common Stock. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Recent Events — Capital Authorizations."

Freddie Mac has issued and outstanding 22.5 million shares of its 7.90% Non-Cumulative Preferred Stock (the "1992 Preferred Stock") and 12 million shares of its 6.72% Non-Cumulative Preferred Stock (the "1993 Preferred Stock"). Each share of the 1992 Preferred Stock and the 1993 Preferred Stock has a par value of $1.00 per share. The 1992 Preferred Stock and the 1993 Preferred Stock are collectively referred to as the "Preferred Stock." On March 1, 1996, the Board of Directors authorized the issuance of up to $500 million of additional non-cumulative preferred stock on terms to be determined by Freddie Mac's management at the time of issuance. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Recent Events — Capital Authorizations."

Under Section 303(b)(2) of the Freddie Mac Act, Freddie Mac's right to declare dividends on, and its right to redeem, any of its stock is subject to prior regulatory approval by the Director if such "capital distribution" (as defined in the GSE Act) would decrease Freddie Mac's capital below the risk-based capital level for Freddie Mac established in the GSE Act or would decrease its core capital to an amount less than the minimum capital level Freddie Mac is required to maintain by the GSE Act. See "Regulation and Governmental Relationships — Regulation — OFHEO Oversight." In addition, pursuant to the GSE Act, the Director may require Freddie Mac to submit a report to the Director after the declaration of, and before making, any such capital distribution.

The descriptions of the Common Stock and the Preferred Stock set forth below do not purport to be complete and are qualified in their entirety by the respective Certificates of Designation for such securities.

Common Stock

Authorized Issuance. The Board of Directors may increase the authorized number of shares of Common Stock at any time without the consent of the holders of the Common Stock.

Dividends. Dividends on shares of the Common Stock are not mandatory. Subject to the dividend priority of the Preferred Stock described below, holders of outstanding shares of Common Stock are entitled to receive cash dividends when, as and if declared by the Board of Directors.

No Optional Redemption. The Common Stock is not subject to optional redemption by Freddie Mac.

No Preemptive Rights and No Conversion Rights. No holder of the Common Stock has any preemptive right to purchase or subscribe for any other shares, rights, options or other securities of any class of stock of Freddie Mac that at any time may be sold or offered for sale by Freddie Mac. The holders of shares of the Common Stock do not have any right to convert such shares into or exchange such shares for any other class or series of stock or obligations of Freddie Mac.

Voting Rights. Holders of Common Stock are entitled to one vote per share in the election of non-appointed Directors and on all other matters presented to them for their vote.

Additional Classes or Series of Stock. Freddie Mac has the right to create and issue additional classes or series of stock ranking prior to, on a parity with or junior to the Common Stock, as to dividends, liquidation or otherwise, without the consent of the holders of the Common Stock.

Amendments. Without the consent of the holders of the Common Stock, Freddie Mac has the right to amend, alter, supplement or repeal any terms of the Common Stock to cure any ambiguity, to correct or supplement any term that may be defective or inconsistent with any other term or to make any other provisions so long as such action does not materially and adversely affect the interests of the holders of the Common Stock. Otherwise, the terms of the Common Stock may be amended, altered, supplemented or repealed only with the consent of the holders of at least two-thirds of the outstanding shares of the Common Stock.

Ownership Reporting System. The Board of Directors has adopted an ownership reporting system similar to the disclosure system applicable to public companies that have a class of securities registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934. Beneficial owners of more than 5 percent of the outstanding shares of Common Stock are required to file ownership reports with Freddie Mac's Shareholder Relations Department and with the New York and Pacific Stock Exchanges, on which the stock is listed. Freddie Mac may impose sanctions upon shareholders for failure to comply with its beneficial ownership reporting system, including forfeiture of voting rights for the portion of the stock that is held in excess of the reporting threshold. Freddie Mac's policy is to make available copies of ownership reports filed with the corporation upon request to the Shareholder Relations Department. In addition, information regarding the stock ownership of certain shareholders is provided on an annual basis in Freddie Mac's proxy statement.

Short-swing Transactions. Freddie Mac has a short-swing trading policy for transactions in the corporation's common and preferred stock by directors and certain officers ("insiders") similar to the short-swing transaction reporting provisions applicable to insiders of public companies with equity securities registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934. Under the corporation's policy, insiders must file initial reports of beneficial ownership of the corporation's equity securities, and reports of changes in beneficial ownership, with the corporation's legal division. Purchases and sales, or sales and purchases, of any Freddie Mac equity security of the same class beneficially owned by an insider within a six-month period generally are prohibited by the policy. Freddie Mac will make available to the public copies of ownership reports filed under the policy upon request to the corporation's Shareholder Relations Department.

General. The Common Stock is identified by the ticker symbol "FRE" on the New York and Pacific Stock Exchanges. From time to time, the Common Stock may be admitted to unlisted trading status on other national securities exchanges. Put and call options with respect to the Common Stock are traded on the American Stock Exchange. The transfer agent for the Common Stock is First Chicago Trust Company of New York, Mail Suite 2589, P.O. Box 2536, Jersey City, N.J., 07303-2536.

Preferred Stock

Authorized Issuance. The Board of Directors may increase the authorized number of shares of Preferred Stock at any time, without the consent of the holders of the Preferred Stock.

Dividends. Dividends on shares of the Preferred Stock are not mandatory. Holders of Preferred Stock are entitled to receive non-cumulative, quarterly cash dividends that are payable on March 31, June 30, September 30 and December 31 of each year (each, a "Dividend Payment Date"), at the annual rate of $1.975 per share for the 1992 Preferred Stock and $1.68 per share for the 1993 Preferred Stock when, as and if declared by the Board of Directors in its sole discretion, out of funds legally available for payment of dividends. Dividends will be paid to holders of record on the record date fixed by the Board of Directors, not to be earlier than 45 days or later than 10 days preceding the applicable payment date.

The Preferred Stock ranks prior to the Common Stock with respect to dividends, to the extent provided in the Certificate of Designation for the Preferred Stock. No dividend can be declared or paid or set apart for payment on the Common Stock unless dividends have been declared and paid or set apart on the Preferred Stock in respect of the then-current quarterly dividend period. The 1992 Preferred Stock and the 1993 Preferred Stock rank on a parity with each other with respect to dividends. Dividends on the Preferred Stock are not cumulative.

Optional Redemption. The 1992 Preferred Stock is not redeemable prior to June 30, 1997. The 1993 Preferred Stock is not redeemable prior to September 30, 1998. On or after such dates and subject to the limitation on capital distributions described above and any further limitations that may be imposed by law or regulation, Freddie Mac may redeem the Preferred Stock, in whole or in part, at any time at the redemption price of $25.00 per share plus an amount equal to the dividend for the then-current quarterly dividend period accrued through and including the date of redemption.

Other Provisions. Additional information about the liquidation preferences and other rights, terms and provisions of the Preferred Stock may be obtained upon request to Freddie Mac's Shareholder Relations Department.

Short-swing Transactions. Freddie Mac's short-swing transaction policy also applies to transactions in Freddie Mac's preferred stock.

General. The 1992 Preferred Stock is identified by the ticker symbol "FREpr" and the 1993 Preferred Stock is identified by the ticker symbol "FREpra" on the New York and Pacific Stock Exchanges. The transfer agent, dividend disbursing agent and registrar for the Preferred Stock is First Chicago Trust Company of New York, Mail Suite 2589, P.O. Box 2536, Jersey City, N.J., 07303-2536.

Dividends

From 1990 through 1995, Freddie Mac paid aggregate dividends of approximately $820 million on the outstanding shares of Common Stock. From 1992 through 1995, Freddie Mac paid aggregate dividends of approximately $212 million on the outstanding shares of Preferred Stock. Freddie Mac will pay approximately $62.3 million in aggregate dividends on the Common Stock and $16.1 million in aggregate dividends on the Preferred Stock for the first quarter of 1996.

MANAGEMENT

Freddie Mac's Board of Directors consists of 18 members, including 13 members elected annually by the holders of the Common Stock and five members appointed annually by the President of the United States. The Presidential appointees must include at least one person from each of the mortgage lending, home building and real estate industries and one person from a consumer or community interest organization or who has demonstrated a career commitment to the provision of low-income housing. All directors serve for a term ending on the date of each annual meeting of stockholders, unless they are re-elected or reappointed, as applicable, and have identical fiduciary duties to the corporation's stockholders.

Information concerning the directors of Freddie Mac, compensation of certain executive officers and of directors, stock ownership of management and any person or group owning more than 5 percent of the Common Stock and related matters may be found in the Proxy Statement (the "Proxy Statement") for the Annual Meeting of Stockholders of Freddie Mac to be held on May 14, 1996. The Proxy Statement, as and when available, is incorporated by reference into this Information Statement.

Freddie Mac will provide a copy of the Proxy Statement, without charge, to each person to whom this Information Statement has been delivered, upon the written or oral request of that person. Such requests should be addressed to Shareholder Relations, Freddie Mac, 8200 Jones Branch Drive, McLean, Virginia 22102 (outside the Washington, D.C. metropolitan area, telephone (800) 424-5401, ext. 2581; within the Washington, D.C. metropolitan area, telephone (703) 903-2581).

Executive Officers

As of March 29, 1996, the executive officers of Freddie Mac are as follows:

Name	Age	Year of Affiliation	Position
Leland C. Brendsel	53	1982	Chairman and Chief Executive Officer
David W. Glenn	52	1987	President and Chief Operating Officer
John P. Gibbons	44	1991	Executive Vice President and Chief Financial Officer (Interim)
Michael K. Stamper	49	1982	Executive Vice President—Risk Management
David A. Andrukonis	38	1980	Senior Vice President and General Manager—Seller Division
Henry J. Cassidy	52	1984	Senior Vice President—Single-Family Risk Management
John D. Fisk	39	1983	Senior Vice President—Investor and Dealer Services
John P. Harding	51	1995	Senior Vice President—Planning and Research
Stephen T. Hopkins	45	1976	Senior Vice President and National Sales Director
Melvin M. Kann	55	1993	Senior Vice President and General Auditor
William I. Ledman	47	1994	Senior Vice President—Information Systems and Services
Ronald J. Majewicz	46	1988	Senior Vice President and Corporate Controller
Maud Mater	48	1976	Senior Vice President—General Counsel and Secretary
Candice D. Mendenhall	46	1995	Senior Vice President—Human Resources
Gregory J. Parseghian	35	1996	Senior Vice President—Corporate Finance
Paul T. Peterson	46	1989	Senior Vice President—Servicer Division
Ann B. Schnare	48	1993	Senior Vice President—Corporate Relations (Interim)
Thomas J. Watt	56	1991	Senior Vice President—Multifamily Housing

The following is a brief biographical description of each executive officer of Freddie Mac.

Leland C. Brendsel was elected Chairman and Chief Executive Officer in November 1989. He served as President and Chief Executive Officer from September 1987 to November 1989, Acting President—Chief Executive Officer from September 1985 to September 1987 and Executive Vice President—Finance and Chief Financial Officer from September 1982 to September 1985.

David W. Glenn was appointed President and Chief Operating Officer in March 1990. He served as Executive Vice President—Chief Operating Officer from November 1989 to March 1990 and Executive Vice President—Finance and Chief Financial Officer from November 1987 to November 1989. Prior to joining Freddie Mac, Mr. Glenn was Senior Vice President of CalFed, Inc., and California Federal Savings and Loan Association (currently California Federal Bank, FSB) from August 1984 to October 1987.

John P. Gibbons was appointed Executive Vice President and Chief Financial Officer (Interim) in January 1996. Mr. Gibbons had served as Senior Vice President—Corporate Relations since June 1994 and as Assistant to the Chairman since May 1993. He served as Acting Chief Financial Officer from May 1993 to June 1994. Prior to that, Mr. Gibbons served as Vice President—Financial Research from July 1991 to May 1993. Prior to joining Freddie Mac, Mr. Gibbons served in several capacities with Merrill Lynch & Co. from 1985 to June 1991, including Director of Mortgage Finance and Vice President of the Mortgage Research Group.

Michael K. Stamper was appointed Executive Vice President—Risk Management in February 1990. Mr. Stamper served as National Sales Director and head of the Marketing and Sales Division from January 1989 to February 1990. From August 1985 to January 1989 he served as General Manager of SS&TG. Prior to that time, Mr. Stamper served as Vice President—Market Analysis from July 1984 to July 1985 and Vice President—Corporate Planning and Development from November 1982 to July 1984.

David A. Andrukonis was appointed Senior Vice President and General Manager—Seller Division in March 1994. From May 1993 to March 1994, he was Senior Vice President—Competitive Advantage Program. Mr. Andrukonis served as Vice President—Mortgage Finance from January 1991 to May 1993 and Director of Product Development and Pricing from June 1988 to January 1991 and held various other positions at Freddie Mac between the time he joined the corporation in June 1980 and June 1988.

Henry J. Cassidy was appointed Senior Vice President—Single-Family Risk Management in January 1996. Prior to that Mr. Cassidy served as Vice President—Mortgage Credit Policy since March 1990. From October 1986 to March 1990 he served as Vice President—Corporate Finance and held various other positions at Freddie Mac since the time he joined the corporation in 1984.

John D. Fisk was appointed Senior Vice President—Investor and Dealer Services in May 1993. Mr. Fisk served as Vice President—Structured Finance from August 1992 to May 1993, General Manager and Vice President—SS&TG from January 1989 to August 1992 and Head Trader for SS&TG from July 1987 to January 1989 and held various other positions at Freddie Mac between the time he joined the corporation in February 1983 and July 1987.

John P. Harding was appointed Senior Vice President—Planning and Research in May 1995. From 1989 to 1995 Mr. Harding worked on and completed his Ph.D. in Real Estate and Finance and taught various courses at the University of California at Berkeley. Prior to that, Mr. Harding was Senior Vice President and Chief Financial Officer for H.F. Holdings, Inc., a savings and loan holding company, from 1986 to 1989.

Stephen T. Hopkins was appointed Senior Vice President and National Sales Director in October 1994. Mr. Hopkins had been Acting Senior Vice President and National Sales Director since April 1994. Prior to that appointment, Mr. Hopkins served as Vice President—Marketing and Sales for Freddie Mac's North Central region since September 1983, and as regional director of that region since 1979. Mr. Hopkins joined Freddie Mac in 1976.

Melvin M. Kann was appointed Senior Vice President and General Auditor in August 1993. Prior to joining Freddie Mac, Mr. Kann served as Senior Vice President of Bank United of Texas, FSB from 1991 to 1993 and as Senior Vice President of Southeast Banking Corporation in Miami, Florida from 1983 to 1991.

William I. Ledman was appointed Senior Vice President—Information Systems and Services effective January 1995. He had been Vice President—Computer and Network Operations since he joined Freddie Mac in February 1994. Prior to joining Freddie Mac, Mr. Ledman held a variety of information systems-related positions with GEICO, a property-casualty insurance company, between 1974 and 1994, the most recent being Vice President—Systems and Data Processing.

Ronald J. Majewicz was appointed Senior Vice President and Corporate Controller in January 1992 and served as Acting Senior Vice President—Human Resources from September 1994 to May 1995. Mr. Majewicz served as Vice President—Internal Audit from June 1988 to January 1992. Prior to joining Freddie Mac, Mr. Majewicz served as Vice President of Auditing and Director of Auditing for the National Life Insurance Company from 1978 to 1988.

Maud Mater was appointed Senior Vice President—General Counsel and Secretary in June 1984. Prior to that time, Ms. Mater served as Vice President—General Counsel and Secretary from October 1982 to June 1984.

Candice D. Mendenhall was appointed Senior Vice President—Human Resources in June 1995. Before joining Freddie Mac, Ms. Mendenhall held several positions at Manchester, Inc., a large outplacement firm, between 1992 and 1995, the most recent being Executive Vice President of Operations. Prior to that, Ms. Mendenhall was Vice President and Chief Administrative Officer for The Hair Cuttery, a large, privately-owned retail chain, from 1988 to 1992. From 1983 to 1987, Ms. Mendenhall was Senior Vice President of Employee Relations at Mellon Bank.

Gregory J. Parseghian was appointed Senior Vice President—Corporate Finance in February 1996. Prior to joining Freddie Mac, Mr. Parseghian was a managing director, chief fixed-income strategist and head of collateralized mortgage obligations and mortgage derivatives trading at Salomon Brothers, Inc. Prior to that, Mr. Parseghian was a partner and senior portfolio manager at BlackRock Financial Management, Inc. Mr. Parseghian worked at First Boston Corporation from 1982 through 1993, most recently as managing director and head of fixed-income research.

Paul T. Peterson was appointed Senior Vice President—Servicer Division in July 1995 and served as Acting Senior Vice President—Servicer Division since January 1995. Prior to that, he had served as Senior Vice President—Corporate Finance from January 1992 to January 1995, as Vice President—Corporate Finance from March 1990 to January 1992 and as Director of Portfolio Management from April 1989 to March 1990. Prior to joining Freddie Mac, Mr. Peterson served as President of Market Street Mortgage Corporation from 1986 to 1989 and as President and Chief Executive Officer of Cal America Savings and Loan Association from 1983 to 1986.

Ann B. Schnare was appointed Senior Vice President—Corporate Relations (Interim) in January 1996. Ms. Schnare has served as Vice President—Housing Economics since 1993. Prior to joining the corporation, Ms. Schnare served as Senior Vice President of ICF-Kaiser International, Inc., an international engineering, construction and consulting services company, from 1987 to 1993.

Thomas J. Watt was appointed Senior Vice President—Multifamily Housing in May 1991. Prior to joining Freddie Mac, Mr. Watt served as Managing Director—Real Estate for State House Capital Management, a subsidiary of Connecticut Mutual Life Insurance Company, from 1989 to 1991. From 1984 to 1989 Mr. Watt served as Senior Vice President for CIGNA Investments, Inc.

INDEPENDENT PUBLIC ACCOUNTANTS

The Consolidated Financial Statements and the supplemental Consolidated Fair Value Balance Sheets of the corporation included in this Information Statement have been audited by Arthur Andersen LLP, independent public accountants, as stated in their report appearing herein.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

HIGHLIGHTS OF 1995

In 1995, Freddie Mac generated record revenues and earnings. Revenues increased 10 percent, to $2.5 billion from $2.3 billion in 1994, and Net income increased 11 percent, to $1.091 billion from $983 million in 1994. Earnings per common share were up 12 percent, to $5.69 from $5.08. The corporation's return on common equity was 22 percent in 1995, the fourteenth consecutive year this rate of return exceeded 20 percent. Freddie Mac achieved record revenues and solid earnings growth despite lower business volumes and a challenging credit environment.

Freddie Mac's 1995 revenues and earnings growth were driven by continued disciplined expansion of the corporation's retained mortgage portfolio. The retained portfolio, which surpassed $100 billion during the fourth quarter, grew by $35 billion, or 48 percent, in 1995 and now comprises approximately 19 percent of the corporation's total mortgage portfolio. The corporation's net interest income doubled from 1992 to 1995 as a result of retained portfolio growth, including the repurchase of outstanding PCs, and increased interest-free funding related to capital growth.

Freddie Mac's total mortgage portfolio grew at a rate of 6 percent during 1995, approximately equal to the estimated growth in outstanding residential mortgage debt. In recent years, Freddie Mac's total mortgage portfolio has generally grown at a faster rate than the growth in outstanding residential mortgage debt, but did not exceed that growth rate in 1995 due in part to borrower preference for adjustable-rate mortgages (ARMs) during the early part of the year. ARMs are less likely than fixed-rate mortgages to be sold into the secondary market at, or for a period of time after, origination. The volume of mortgage originations continually increased during 1995 as declining mortgage rates spurred originations both for the purchase of homes and for refinancings. Demand for ARMs declined and the volume of fixed-rate mortgage originations increased.

Administrative expenses increased modestly at the rate of 4 percent in 1995, reflecting Freddie Mac's continued commitment to corporate cost management.

Credit-related expenses increased by 27 percent, from $425 million in 1994 to $541 million in 1995. Because mortgages generally experience their peak default period approximately three to five years after origination, credit-related expenses in 1995 were primarily related to mortgages originated prior to 1992. California loans account for approximately 25 percent of Freddie Mac's total mortgage portfolio, but contributed 63 percent of total credit losses in 1995. California experienced a deep economic recession in the early 1990s, with significant declines in employment levels and house prices. The increase in credit-related expenses was also attributable to the corporation's increased use of loss mitigation strategies, particularly foreclosure alternatives, which tend to accelerate the recognition of credit-related expenses through charge-offs.

In the next two to three years, Freddie Mac's credit performance will increasingly depend upon the performance of mortgages originated in 1992 and 1993. These are primarily refinanced fixed-rate mortgages with relatively low loan-to-value (LTV) ratios. These mortgages were originated after Freddie Mac tightened its underwriting guidelines to significantly reduce the purchase of higher-risk loans such as low-documentation and negative amortization mortgages. In addition, house prices have been stable or improving in most regions in the period since these mortgages were originated. As a result, 1992 and 1993 mortgage purchases are expected to experience lower average percentage loss rates than pre-1992 purchases. However, these mortgages, which are entering the peak default period, comprise the largest portion of the corporation's total mortgage portfolio. Therefore, small proportional changes in the credit performance of these mortgages can have a significant dollar impact on the corporation's results of operations.

The major underwriting changes instituted by Freddie Mac since 1991 along with continued significant advances in underwriting capabilities, the most significant being the successful introduction of Freddie Mac's automated underwriting service, Loan Prospector℠, have built the foundation for improved credit performance in the future. In addition, Freddie Mac has continued to develop its strategies for reducing credit losses normally associated with non-performing mortgages.

The record earnings achieved in 1995 further strengthened the corporation's capital base. The Office of Federal Housing Enterprise Oversight (OFHEO) classified Freddie Mac "adequately capitalized," OFHEO's highest classification, in its most recent capital classification. Disciplined capital deployment underlies all of Freddie Mac's business activities. The corporation invests capital only when expected long-term returns and related risks are acceptable. Freddie Mac's common share repurchase program, initiated during 1995, allows the return of capital to shareholders during periods when there are fewer opportunities to invest capital at attractive returns.

Freddie Mac produced solid earnings growth in 1995 at a time when total mortgage portfolio growth and growth in credit-related expenses diverged from longer-term trend lines. By aggressively managing risks, prudently deploying capital and maintaining a strong market position, Freddie Mac has built a solid foundation for future growth in its total mortgage portfolio, revenues and earnings.

BUSINESS AND MARKET OVERVIEW

Business Overview

The principal business activity of Freddie Mac is the purchase or securitization of single-family and multifamily residential mortgages from mortgage lenders, which include both depository institutions and mortgage bankers. Freddie Mac uses two principal methods to finance its mortgage purchases, each of which generates a different source of revenue for the corporation.

Under the first method, mortgages are securitized and issued to investors as guaranteed mortgage pass-through securities called Mortgage Participation Certificates or "PCs." Mortgages financed by the issuance of PCs are referred to as the "sold portfolio." Freddie Mac guarantees the payment of principal and interest on PCs and bears the risk of borrower default on the mortgages backing the PCs. For assuming this risk, and as compensation for administration of principal and interest payments, the corporation receives fee income which is recorded as "Management and guarantee income" over the lives of the underlying mortgages. The amount of this fee income is the difference between the effective interest rate received by Freddie Mac on mortgages it purchases and the effective interest rate paid to PC holders.

Under the second method, purchased mortgages and mortgage-related securities are held for investment by Freddie Mac and financed with debt, equity and other liabilities. Mortgage assets held by Freddie Mac are referred to as the "retained portfolio." The corporation recognizes net interest income on the retained portfolio, which is the interest income earned on these assets net of the interest expense on the liabilities funding them. The corporation's ability to grow the retained portfolio is dependent on the availability of spreads between asset yields and financing costs that generate attractive returns on capital, which may not prevail in all interest-rate environments.

The retained and sold portfolios together comprise the "total mortgage portfolio." During 1995, the total mortgage portfolio grew 6 percent from $533 billion to $566 billion. At December 31, 1995, the retained portfolio accounted for $107 billion, or 19 percent, of the total mortgage portfolio with the remaining $459 billion, or 81 percent, in the sold portfolio. The retained portfolio is comprised of $44 billion in mortgages and $63 billion in mortgage-related securities, including $56 billion of repurchased PCs.

A portion of the PCs issued by Freddie Mac is resecuritized and reissued as multiclass PCs that qualify for treatment as real estate mortgage investment conduits (REMICs) under the Internal Revenue Code of 1986. Because substantially all REMICs are formed by resecuritizing existing PCs and other mortgage securities already guaranteed by Freddie Mac, they do not increase credit risk to the corporation or the size of the sold portfolio. A single REMIC series consists of multiple classes with varying maturities and interest rates and is designed to appeal to the needs of a variety of investors. For Freddie Mac, the issuance of multiclass securities responds to investor needs, supports market prices for PCs and generates additional fee income, which is recorded as other income.

Freddie Mac also maintains a non-mortgage investment portfolio primarily for liquidity and working capital purposes. The investment portfolio, which totaled approximately $21 billion at December 31, 1995, consists principally of federal funds sold, reverse repurchase agreements and highly rated, short-term investments, the majority of which are funded with debt or other funding sources of maturities similar to those of the assets being financed. The corporation recognizes net interest income on the investment portfolio which is the interest income earned on the investment assets net of the interest expense associated with the liabilities funding them.

Freddie Mac employs three financial disciplines in managing the corporation. The first is disciplined credit risk management. Credit risk management has become even more critical as intense competition in the primary market, shifts in product mix and increases in average LTV ratios have increased the credit risk of new mortgage originations over the past two years.

Freddie Mac also adheres to a strong interest-rate risk management discipline. The primary objective is to keep the risk of decline in the value of the corporation or its earnings within acceptable levels. In doing so, Freddie Mac continually reassesses its funding mix in light of changes in market conditions and asset composition.

Lastly, Freddie Mac invests shareholder capital in a disciplined fashion. The company seeks to invest capital only when long-term returns exceed certain thresholds and are appropriate given the risks of the investment. This discipline means Freddie Mac will not pursue growth, market share or short-term earnings at the cost of unacceptable returns on capital.

Market Overview

Freddie Mac competes directly with the Federal National Mortgage Association (Fannie Mae) for purchases of residential mortgages (primarily "conventional" mortgages that are not insured or guaranteed by agencies of the U.S. government) in the conforming mortgage market. "Conforming" mortgages are those mortgages having original principal amounts that do not exceed statutory loan limits based on housing prices, as established annually by Freddie Mac and Fannie Mae as required by their charters, and which meet other statutory requirements. The one-unit single-family loan limit is tied to an increase in the average purchase price of single-family conventionally financed homes as reported by the Federal Housing Finance Board. As a result of the 1995 index increase, Freddie Mac and Fannie Mac raised their single-family one-unit conforming loan limits to $207,000 effective January 1996.

Freddie Mac estimates that approximately $575 billion of conventional single-family mortgages were originated in 1995. Of that amount approximately $220 billion, or 38 percent, were sold to Freddie Mac and Fannie Mae. Freddie Mac and Fannie Mae purchased a combined total of approximately 47 percent and 54 percent of the conventional single-family mortgages originated in 1994 and 1993, respectively.

The percentage of conventional single-family mortgages sold into the secondary market declined sharply in 1994 and early 1995 due in part to the high proportion of residential mortgage originations represented by ARMs during this period. Depository institutions, which originate a large share of ARMs, tend to retain these mortgages in their portfolios because ARMs present generally lower exposure to interest-rate risk than fixed-rate mortgages. The decline in secondary market share of primary market originations also reflected a cyclical contraction similar to that experienced in 1988 after a period of high mortgage refinancing. Depository portfolio lenders also entered 1995 with strong deposit and capital levels, which allowed them to originate mortgages at competitive prices and take on the additional credit risk of holding more loans in their portfolios. The secondary market purchase share increased during the second half of 1995 as declining interest rates made fixed-rate mortgages more attractive to borrowers compared to ARMs.

Freddie Mac and Fannie Mae compete for mortgages on the basis of the relative strength of their respective mortgage purchase programs and security products, customer service, technological innovations and price. Price is of particular importance to originators in deciding whether to sell mortgages to Freddie Mac or Fannie Mae.

Price differences or "spreads" between Freddie Mac PCs and competing securities reflect, in part, the different remittance cycles of these securities. Because Freddie Mac's Gold PC, with a 45-day payment delay, offers a faster remittance of mortgage principal and interest payments to investors than Fannie Mae securities with a similar coupon and maturity,

Gold PCs generally trade at higher prices. However, factors such as differences in liquidity, temporary supply and demand imbalances and investor perceptions can cause the price premiums on Gold PCs to fall below the level that reflects the full value of the Gold PC's faster remittance.

In 1995, as in 1994, the spreads between Freddie Mac and Fannie Mae pass-through securities did not reflect the full value of this faster remittance. Management believes this is due to investor concerns that Freddie Mac PCs have less liquidity than comparable Fannie Mae securities, as well as a shift in the primary purchasers of mortgage securities from buy and hold investors to investors who more actively trade their portfolios. Continuing concerns over the liquidity of PCs, and changes in the market and investor base for mortgage securities, may continue to adversely affect spreads, contributing to competitive pressures.

Freddie Mac supports the market for its PCs and PC spreads relative to Fannie Mae pass-through securities and other comparable securities in a variety of ways, including the acquisition of PCs for resecuritization as REMICs and other securities; the purchase of PCs for Freddie Mac's retained portfolio and for other corporate purposes; and through other market-related activities. In 1995, market support activities included the use of several external money management firms to actively trade a relatively small portion of Freddie Mac's retained portfolio, and the initiation of a focused marketing effort to educate dealers and investors about the relative advantages of trading and investing in Freddie Mac PCs. The trading activities of external money management firms did not have a material effect on Freddie Mac's 1995 net earnings. Freddie Mac may undertake additional activities to support the market for PCs in the future, although it also may determine to increase, reduce or discontinue all or any one of its efforts at any time.

Freddie Mac's market share, as a percentage of combined Freddie Mac and Fannie Mae purchases, was approximately 42 percent for the full year 1995, compared to approximately 43 percent in 1994. As in 1994, market share continued to be influenced by the level of large purchases from individual lenders' existing portfolios. The extent to which Freddie Mac and Fannie Mac make these large portfolio purchases can cause significant fluctuations in their respective purchase volumes and market share over relatively short time periods. Market share also may be affected by Freddie Mac's credit and capital deployment disciplines to the extent the corporation declines, or is not awarded, certain transactions on the basis of credit or pricing terms.

The corporation fully re-entered the multifamily purchase market in 1994 and has purchased approximately $2.4 billion of multifamily mortgages over the past two years.

RISK MANAGEMENT

Freddie Mac is subject to two primary business risks: credit risk and interest-rate risk. The management of these risks affects both the level and stability of the corporation's earnings, capital base and long-term value.

Credit Risk

Freddie Mac's primary credit risk is the risk that the corporation will not receive amounts due from mortgage borrowers, potentially resulting in a loss if Freddie Mac is unable to sell the mortgaged property at a price sufficient to pay the amount owed on the mortgage and related disposition costs. Borrower default on a single-family mortgage can occur as a result of various adverse events affecting a borrower after origination, or because the mortgage is made to a borrower unable or unwilling to support the economic obligations of the mortgage. A credit loss also occurs if a seller/servicer fails to pass through borrower payments to Freddie Mac, most commonly in connection with insolvency of that mortgage servicer. For multifamily mortgages, the principal factors affecting default risk are the level of debt coverage, the property condition and LTV ratios of the mortgaged properties. To a lesser extent, Freddie Mac also is exposed to credit risk on its non-mortgage investment portfolio and off-balance sheet financial instruments.

Freddie Mac's management of credit risk comprises three broad areas: underwriting standards, sensitivity of mortgage default rates to changes in economic conditions and other risk factors and the resolution of non-performing assets. The effectiveness of Freddie Mac's credit risk management is reflected primarily in the levels of mortgage delinquencies and charge-offs, real estate owned (REO) balances and associated expenses. Freddie Mac strives to be the industry leader in credit risk management by building and maintaining a high-quality portfolio, and by providing low-cost credit processes and achieving continuous process improvement.

Underwriting standards: Freddie Mac seeks to ensure, through effective underwriting standards, that the mortgages it purchases are protected by adequate borrower income and equity in the underlying collateral, and by the borrower's willingness and ability to repay the mortgage obligation. In addition, the corporation purchases mortgages only from seller/servicers that maintain approved underwriting and servicing standards and sufficient net worth as required by Freddie Mac. For single-family mortgages, Freddie Mac generally obtains warranties from each of its sellers that purchased mortgages meet the corporation's underwriting criteria and other contractual commitments. The corporation also monitors seller/servicers' compliance with these standards through quality control reviews, on-site audits and institutional eligibility enforcement, and actively investigates situations involving possible fraud. For multifamily mortgages, Freddie Mac relies on a combination of an intensive, individualized underwriting process, restrictions on the types of mortgage sellers that are eligible to participate in Freddie Mac's multifamily programs and, to a lesser extent, seller warranties.

One measure Freddie Mac uses to determine the effectiveness of its single-family underwriting standards is the ratio of early payment defaults (EPDs) on "at-risk" single-family mortgages (those mortgages for which the corporation has assumed primary default risk) in relation to the total single-family mortgage portfolio. Specifically, EPDs represent at-risk single-family mortgages that become 90 or more days delinquent within 12 months of purchase and ultimately enter the foreclosure process. Management believes EPDs serve as a measure of portfolio quality because they historically have been predictive of default rates in future years. While the rate of EPDs for 1994 mortgage purchases has increased, the rate is lower than those experienced in 1990 and early 1991. Management believes the decline in EPDs is the result of the high proportion of refinanced mortgages purchased from 1992 to

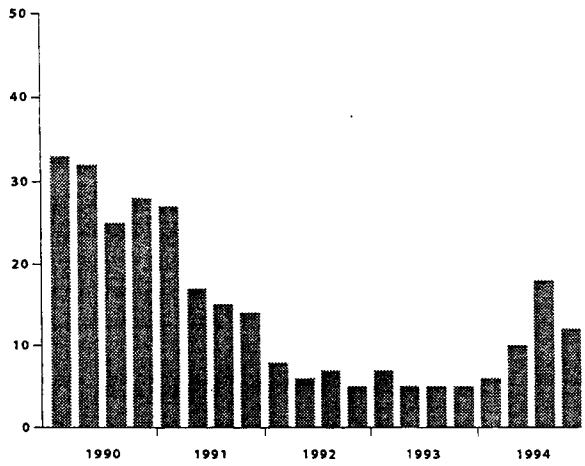
mid-1994, improved underwriting standards initiated in the early 1990s, as well as the corporation's increased focus on fraud detection and mitigation and generally improved economic and market conditions.

The higher EPD rates of 1990 and 1991 single-family purchases have translated into higher annual default rates over time. The corporation improved mortgage purchase quality during the early 1990s by suspending purchases of low-documentation mortgages and mortgages that rely on house price appreciation or inflation, such as graduated payment mortgages. During this time, the corporation also established stricter mortgage purchase standards with respect to third-party originated mortgages, improved quality control procedures and removed many underperforming seller/servicers from its customer base.

Refinanced mortgages purchased from 1992 to mid-1994 generally have lower LTV ratios and other characteristics associated with enhanced credit quality. Freddie Mac's 1992 and 1993 single-family mortgage purchases, which account for over 50 percent of the corporation's current total mortgage portfolio, had significantly better EPD rates and are showing dramatically lower annual default rates. Although the rate of EPDs for 1994 mortgage purchases is higher, the lower volume of mortgages purchased that year makes it likely that the higher EPD rates on these mortgages will have a relatively smaller impact on the corporation's overall default rates.

EARLY PAYMENT DEFAULTS

Basis Points by Funding Quarters



The upturn in EPD rates on 1994 mortgage purchases has been driven by rising LTV ratios associated with the decline in refinancings, and some deterioration in single-family borrower credit quality. Freddie Mac continues to implement new initiatives to improve underwriting effectiveness and reduce credit risk, especially in light of increasing credit challenges in the primary market. Examples include increased mortgage insurance requirements during 1994 and 1995 for most high-LTV mortgages, increased use of credit enhancements on new mortgage purchases and establishment of additional insurance requirements for purchases of mortgages on certain properties located in areas prone to earthquakes or floods.

Freddie Mac is leading the mortgage industry in the use of certain credit scores as a single-family underwriting tool. These credit scores use a borrower's credit history to assess ability and willingness to make timely mortgage payments. The corporation's research has shown a strong correlation between certain credit scores and mortgage performance. Mortgage defaults tend to rise significantly as these credit scores weaken. Loan Prospector℠ combines certain credit scores, LTV ratios and other loan characteristics, providing lenders with a comprehensive underwriting tool to evaluate overall loan risk. Management believes these underwriting enhancements will translate into improved credit performance in the future.

Portfolio Sensitivity: In addition to borrower credit quality, the primary factors influencing the sensitivity of the single-family mortgage portfolio to changes in economic conditions are LTV ratios, mortgage product mix and geographic concentrations.

Freddie Mac's default experience has shown that mortgages with high LTV ratios are more sensitive to changes in economic conditions than mortgages with low LTV ratios. Freddie Mac monitors both the LTV ratios of new purchases (market LTV ratios) and estimated current LTV ratios of the total mortgage portfolio. The current LTV ratio compares the current unpaid principal balance of the mortgage to the estimated current value of the property collateralizing the mortgage. Current market values are estimated using regional house-price appreciation and depreciation data and adjusting the value of the property at origination by the estimated change in price since origination. The weighted average current LTV ratio of the corporation's single-family portfolio at December 31, 1995 was 64 percent, compared to 65 percent at December 31, 1994. The distribution of purchase LTV ratios and estimated current LTV ratios of the total single-family (1- to 4-family) portfolio by current LTV range is set forth below.

Average Purchase LTV Ratio Range

Year ended December 31,	1995	1994	1993
0% to 70%	26%	34%	41%
Above 70% to 80%	42	39	40
Above 80% to 90%	18	18	15
Above 90% to 95%	14	9	4
Above 95%	–	–	–
Total	100%	100%	100%

Estimated Current LTV Ratio Range

As of December 31,	1995	1994	1993
0% to 70%	60%	57%	54%
Above 70% to 80%	19	21	24
Above 80% to 90%	12	13	14
Above 90% to 95%	4	4	4
Above 95%	5	5	4
Total	100%	100%	100%

Market LTV ratios on mortgages originated for the purchase of a home (purchase money mortgages) have increased in recent years, although this trend was partially masked by the high volume of refinancings from 1992 to mid-1994. Refinanced single-family mortgages generally have lower LTV ratios than purchase money mortgages because refinancing borrowers usually have increased their equity in the underlying properties through the combined effects of house-price appreciation and principal amortization. Rising interest rates during 1994 caused a significant decline in refinancing activity from 1993. Although interest rates declined throughout most of 1995, refinancing activity did not increase significantly from the overall 1994 level. In response to the increase in originations of higher LTV purchase money mortgages, Freddie Mac increased mortgage insurance requirements during 1994 and 1995 for most high-LTV mortgages. The increasing proportion of purchase money mortgages caused the average LTV ratios of mortgages purchased by Freddie Mac to increase from 74 percent in 1994 to 77 percent in 1995.

Mortgage Purchase Characteristics	**1995**	**1994**	**1993**
Percentage of purchases represented by refinancings	35%	55%	72%
Average LTV of purchases:			
Refinancings	68%	68%	67%
Purchase money mortgages	81%	81%	79%
Total purchases	77%	74%	70%

The following table sets forth default rates with respect to single-family mortgages of all types in Freddie Mac's total mortgage portfolio within the indicated ranges of origination LTV ratios. The rates shown relate to the total original unpaid principal balance of single-family first-lien mortgages that defaulted during the designated year, expressed as percentages of the aggregate original unpaid principal balance as of the beginning of each year.

Origination LTV Ratio Range of Defaulted Single-Family Mortgages

Year ended December 31,	**1995**	**1994**
0% to 75%	0.24%	0.26%
Above 75% to 80%	0.45	0.49
Above 80% to 85%	0.50	0.44
Above 85% to 90%	0.83	0.82
Above 90% to 95%	0.49	0.63

Another factor affecting single-family mortgage risk is product mix. Freddie Mac has experienced generally higher default rates on ARMs than on fixed-rate mortgages, and lower default rates on 15-year fixed-rate mortgages than on 30-year fixed-rate mortgages. ARMs present greater credit risk in part because the mortgage coupon is tied to a specified index, and borrower payments rise and fall, within limits, with changes in the index. Generally, 15-year fixed-rate mortgages pose a lower default risk than 30-year fixed-rate mortgages due in part to the faster principal amortization inherent in the 15-year product. Balloon/reset mortgages generally have default rates above those of 30-year fixed-rate mortgages but less than those of ARMs. Balloon/reset mortgages, which Freddie Mac began purchasing in late 1989, are mortgages that amortize on a 30-year fixed-rate schedule, but require full repayment or refinancing in 5 or 7 years. Freddie Mac generally receives higher management and guarantee fees for these higher-risk mortgage products.

Freddie Mac also has experienced generally higher default losses on 2- to 4-unit single-family mortgages and multifamily mortgages than on one-unit single-family mortgages, largely because these multi-unit mortgages generally have higher average balances, are at least in part non-owner occupied and tend to experience the adverse effects of economic weakness more than one-unit single-family mortgages. In addition, 2- to 4-unit properties are located primarily in urban areas that have experienced significant economic distress in recent years. Approximately 3 percent of Freddie Mac's total mortgage portfolio consists of 2- to 4-unit single-family mortgages.

Multifamily mortgages present different credit risks from owner-occupied, single-family mortgages where borrowers often will continue to make mortgage payments to avoid loss of a residence even when the unpaid principal balance of the mortgage exceeds the market value of the underlying property. Like 2- to 4-unit properties, multifamily properties often are located in urban areas that have experienced economic distress. In addition, the values of multifamily properties are sensitive to factors not applicable to single-family mortgages, such as changes in certain tax laws and rent control regulations. Because multifamily properties primarily are viewed by borrowers as investments, and generally do not involve recourse to an individual for the mortgage debt or private mortgage insurance (as is the case for single-family mortgages), the performance of multifamily mortgages largely depends upon the net cash flow generated from the property, as well as the property's market value. In Freddie Mac's experience, the principal factor in default risk for multifamily mortgages is the level of debt service coverage of the property securing the mortgage. LTV ratios also provide a measure of potential loss severity. In light of these factors, Freddie Mac generally receives higher management and guarantee fees for multifamily mortgages than single-family mortgages.

The composition of Freddie Mac's mortgage purchases and total mortgage portfolio by product type is presented in the following tables.

Year ended December 31,	1995	1994	1993
(dollars in millions)			
Purchases of mortgages:[1]			
30-year single-family fixed-rate[2]	$ 58,244	$ 70,390	$115,375
15-year single-family fixed-rate	13,806	25,543	68,471
5- and 7-year balloon/resets	3,822	9,984	24,497
Adjustable-rate	20,949	17,482	21,172
Multifamily	1,565	847	191
Total	$ 98,386	$124,246	$229,706
Credit risk distribution:			
Freddie Mac at-risk[3]	$ 76,619	$108,838	$220,989
Credit-enhanced or guaranteed[4]	21,767	15,408	8,717

December 31,	1995	1994	1993
(dollars in millions)			
Outstanding portfolio balances:			
30-year single-family fixed-rate[2]	$318,003	$288,350	$261,807
15-year single-family fixed-rate	128,443	130,701	125,629
5- and 7-year balloon/resets	44,780	47,805	46,812
Adjustable-rate	68,578	60,331	53,175
Multifamily	6,665	6,297	7,304
Total	$566,469	$533,484	$494,727
Credit risk distribution:			
Freddie Mac at-risk[3]	$511,777	$495,218	$468,673
Credit-enhanced or guaranteed[4]	54,692	38,266	26,054

(1) Excludes repurchased Freddie Mac PCs since repurchases do not affect the unpaid principal balance of the total mortgage portfolio.

(2) Includes 20-year single-family fixed-rate mortgages.

(3) Includes those mortgages for which Freddie Mac has assumed primary default risk.

(4) Includes mortgages and mortgage-related securities for which the lender or issuer has retained primary default risk by pledging collateral or agreeing to repurchase mortgages that default. Lender risk may be limited to a certain portion of the mortgages delivered.

The shift toward originations of higher-risk single-family mortgage products such as ARMs, particularly in the latter half of 1994 and early 1995, had no significant impact on the overall product mix of the total mortgage portfolio. This was primarily due to the low volume of mortgage purchases during that period. The corporation's current mortgage portfolio consists largely of low-coupon, fixed-rate mortgages.

Shifts in the types of single-family mortgage products originated by lenders significantly affect the product mix of Freddie Mac purchases. During 1994, rising interest rates increased the proportion of primary market originations represented by ARMs, while borrower demand for fixed-rate mortgage products decreased. Declining interest rates during 1995 have made 30-year fixed-rate mortgages increasingly more attractive to borrowers compared with ARMs. At the end of 1995, ARMs comprised only about one-quarter of total primary market originations, down from approximately one-half at the beginning of 1995. Freddie Mac manages the credit risk related to higher-risk mortgage products by making appropriate adjustments to its own mortgage products and underwriting standards, and by requiring additional compensation or credit enhancements on higher-risk mortgages.

Freddie Mac increasingly has utilized credit enhancements to address the increased risk of loss inherent in higher LTV ratio single-family mortgage originations and less stringent primary market underwriting. Credit enhancements require the lender to retain primary default risk either by pledging collateral or through a recourse agreement in which the lender agrees to repurchase mortgages that default. The increased use of credit enhancement types other than recourse provisions tends to lessen Freddie Mac's exposure to institutional credit risk, the risk that a seller/servicer does not perform or defaults on its payment obligations to the corporation. The corporation especially has used credit enhancements in large purchases of seasoned ARMs from lenders' existing portfolios.

As of December 31, 1995, approximately 10 percent of Freddie Mac's outstanding mortgage portfolio carried some type of credit enhancement or were government guaranteed mortgages or mortgage-related securities. This compares to 7 percent of the outstanding mortgage portfolio at December 31, 1994. Approximately 81 percent of 1995 credit-enhanced purchases used non-recourse loss protection compared to 69 percent in 1994. The portion of the total mortgage portfolio for which Freddie Mac has assumed primary default risk, through the absence of credit enhancements or government guarantees, is designated as "at-risk" by Freddie Mac. The corporation believes supplemental reporting of at-risk data presents a more meaningful discussion of credit risk and provides additional comparability with the reporting of other secondary market institutions.

Geographic diversification mitigates the effect of changing regional and national economic conditions on Freddie Mac's total mortgage portfolio. The geographic distribution of Freddie Mac's total mortgage portfolio is generally reflective of the distribution of outstanding residential mortgage debt in the United States. The diversification of Freddie Mac's portfolio, however, cannot insulate it entirely from weak economic conditions in geographic regions in which Freddie Mac has a relatively larger proportion of its total mortgage portfolio. As discussed in "Credit Performance," persistent economic weakness in California and the Northeast region has continued to adversely affect Freddie Mac's overall credit performance. Information about regional and significant state credit concentrations is provided in Note 10 to the Consolidated Financial Statements.

Non-performing Assets: The amounts recovered by Freddie Mac on delinquent mortgages and REO are affected by the corporation's strategies to manage the resolution of non-performing assets. Freddie Mac works with servicers to manage and resolve delinquencies as they occur and measures servicer effectiveness by monitoring mortgage delinquency rates and other credit performance measures.

When it becomes apparent that a borrower will not be able to repay a mortgage, the principal method of collection historically has been foreclosure. However, foreclosure is not always the most effective resolution method because of the time and expense related to acquiring, managing and disposing of the property. As a result, Freddie Mac has been prudently increasing its loss mitigation activities, primarily the use of early intervention alternatives to foreclosure. Foreclosure alternatives are central to Freddie Mac's overall loss mitigation strategies that are designed to reduce the number of foreclosed properties and ultimately the level of total credit-related costs and expenses. However, the use of foreclosure alternatives tends to accelerate the recognition of credit-related expenses by shifting losses related to delinquent mortgages and REO from net interest income and REO operations expense to charge-offs. Freddie Mac expects to improve the efficiency and increase the use of foreclosure alternatives in 1996. The two foreclosure alternatives most frequently employed by Freddie Mac are pre-foreclosure sales and loan modifications.

A pre-foreclosure sale is a transaction in which Freddie Mac accepts less than a full payoff of the unpaid principal balance of a defaulted mortgage from the sale of a home prior to foreclosure. Pre-foreclosure sales are Freddie Mac's most commonly utilized foreclosure alternative and result in average losses that are approximately 60 percent of the average loss incurred if a property ultimately is acquired by the corporation through foreclosure and becomes REO.

A loan modification is a loan agreement that changes one or more of the original terms of a mortgage, usually the borrower's interest rate or payment period. Freddie Mac expects that, on average, loan modifications will avoid approximately 75 percent of the loss normally incurred if a property were to go through the foreclosure process.

While potential savings from loan modifications can be significant, losses could be incurred by the corporation from their overuse. These losses can occur in the loan modification process as a result of modifying a loan that is likely to redefault at a later time or modifying a loan that ultimately would have returned to performing status. Freddie Mac's loan modification policies limit the circumstances in which loan modifications are used in order to avoid these errors.

Freddie Mac's loss mitigation efforts also provide incentives, mortgage performance data and specialized training to mortgage servicers to improve the management of non-performing mortgages. The corporation also seeks to leverage its Loan Prospector℠ technology and is developing more sophisticated decision support tools that can be integrated into its loss mitigation programs. These tools provide assessments of the economic costs associated with available foreclosure alternatives as well as information on the probability of a loan going to foreclosure.

Freddie Mac also has been improving the processes involved in acquiring, managing and disposing of REO properties. The goal of these efforts is to maximize REO sales proceeds and reduce operating expenses. During 1995, the corporation improved its property valuation process to help ensure that the highest potential sales proceeds are received. In some cases, this includes performing minor repairs or upgrades to properties.

Loss mitigation is a key component of Freddie Mac's strategy for managing non-performing assets and lowering future credit losses. These activities reinforce Freddie Mac's commitment to protect and enhance the value of its portfolio by enhancing the capabilities of servicers and mortgage loan processing technology, and should have an increasingly positive impact on credit performance over the next several years.

Credit Performance: The following table summarizes mortgage delinquencies, REO activity and charge-offs for 1995 as compared to 1994.

Year ended December 31,	**1995**	**1994**[1]
(dollars in millions)		
Delinquencies, end of period		
Single-family:[2]		
Total portfolio	0.61%	0.57%
Freddie Mac at-risk[3]	0.60%	0.55%
Multifamily[4]	2.88%	3.79%
REO, end of period		
Single-family	$ 713	$ 781
Multifamily	87	167
Total	$ 800	$ 948
REO activity for period:		
Properties in inventory – beginning of period	8,802	7,888
Properties acquired	15,577	15,460
Properties disposed of	(16,237)	(14,546)
Properties in inventory – end of period	8,142	8,802
Number of foreclosure alternatives settled[5]	5,945	3,452
Charge-offs for period		
Single-family:		
Foreclosure alternatives[5]	$ 85	$ 38
REO acquisitions	200	155
	285	193
Multifamily	20	34
Total	$ 305	$ 227

(1) Multifamily delinquencies and REO balances reflect the implementation of Statement of Financial Accounting Standards No. 114, which requires the reclassification and transfer from REO to delinquencies of mortgages previously classified as in-substance foreclosures.

(2) Based on the number of mortgages 90 days or more delinquent.

(3) Includes those mortgages for which Freddie Mac has assumed primary default risk. Excludes mortgages for which the lender or issuer has retained primary default risk by pledging collateral or agreeing to repurchase mortgages that default. Lender risk may be limited to a certain portion of the mortgages delivered.

(4) Based on the net carrying value of mortgages 60 or more days delinquent. Excludes mortgages in litigation that are less than 60 days delinquent.

(5) Primarily consist of pre-foreclosure sales and loan modifications.

Delinquencies: The overall increase in single-family delinquencies (based on the number of mortgages delinquent 90 days or more), from 0.57 percent at December 31, 1994 to 0.61 percent at December 31, 1995, primarily reflected a 9 basis point increase in the delinquency rate for the West region, which continues to experience areas of economic weakness, particularly in California. Continued economic weakness in California and, to a lesser extent, the Northeast is expected to cause the delinquency rates for those areas to remain at high levels relative to the delinquency rates in other areas. The single-family delinquency rate on Freddie Mac's at-risk portfolio increased from 0.55 percent at December 31, 1994 to 0.60 percent at December 31, 1995.

The multifamily delinquency rate of 2.88 percent (based on the net carrying value of mortgages delinquent 60 days or more) and the balance of non-performing multifamily mortgages both decreased from December 31, 1994. The decrease in non-performing multifamily mortgages resulted from successful asset resolution efforts and general economic improvements in the multifamily market. As of December 31, 1995, none of the multifamily mortgages purchased since Freddie Mac's full re-entry into this market in 1994 have defaulted.

Mortgage Charge-offs and REO: The $92 million increase in single-family charge-offs from 1994 resulted primarily from increased REO acquisitions. Increased REO acquisitions were driven by continued economic weakness and declining average house prices in California and certain areas within the Northeast region. The increase in single-family charge-offs also reflected the increased use of loss mitigation strategies, particularly foreclosure alternatives, which tend to accelerate the recognition of credit losses in the short term. Foreclosure alternatives are intended to reduce the number of delinquent mortgages proceeding to foreclosure, and ultimately reduce total credit-related expenses and costs by eliminating the expense of acquiring, carrying and subsequently disposing of REO properties (see also "Results of Operations — Credit-Related Expenses").

As previously mentioned, the corporation has experienced weaker credit performance on single-family mortgages purchased before 1992. Pre-1992 mortgage purchases currently comprise approximately 20 percent of the total single-family mortgage portfolio, but account for approximately 80 percent of current single-family credit losses, which consist of charge-offs and REO operations expense. The corporation has experienced generally stronger credit performance from its post-1991 mortgage purchases, which consist primarily of lower-coupon, fixed-rate mortgages. Although the corporation has experienced somewhat higher EPD rates on 1994 mortgage purchases, it generally expects the performance of post-1991 mortgage purchases, along with the increasing level of credit-enhanced mortgage purchases, to positively influence overall credit results over time.

The dollar amount and number of single-family REO properties decreased from December 31, 1994, as dispositions outpaced acquisitions during the year. Although REO property acquisitions and dispositions both increased compared to 1994, dispositions outpaced acquisitions as a result of intensive efforts to reduce the average REO inventory age and reduce the percentage of REO held longer than one year. The majority of REO additions continues to consist of foreclosed California properties, although there remains a significant inflow of properties from the Northeast region.

The volume of single-family REO additions may increase in 1996 as current delinquencies, primarily California properties, proceed through the foreclosure process. In addition, the corporation's growing emphasis on loss mitigation strategies will continue the accelerated recognition of credit losses. Based on management's current expectations for delinquency rates, the transition of mortgages through the delinquency pipeline, average loss rates, the level of loss mitigation activities and total mortgage portfolio growth, single-family credit losses in 1996 are expected to increase in dollar terms, but remain at roughly current levels as a percentage of the single-family mortgage portfolio. Should economic conditions such as interest rates, employment rates or house-price appreciation rates vary materially from management's expectations, or if management changes its strategy for loss mitigation transactions, credit losses could vary from expected levels.

Multifamily charge-offs decreased $14 million from 1994 due to a decrease in REO acquisitions, which reflected strengthening real estate values in certain areas combined with successful loss mitigation strategies. The multifamily REO balance decreased by $80 million from December 31, 1994, as a result of declining acquisitions and active disposition activity during 1995.

The corporation adopted Statement of Financial Accounting Standards (SFAS) No. 114 effective January 1, 1995. This statement requires that impaired loans be valued based on the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if the loan is collateral dependent. In addition, under SFAS No. 114, multifamily loans deemed to be in-substance foreclosed are no longer transferred to REO, but rather continue to be carried in the retained mortgage portfolio until the foreclosure process is complete. As a result, prior period multifamily delinquencies and REO balances have been restated to reflect the adoption of SFAS No. 114. The adoption of SFAS No. 114 did not have a material effect on reported results of operations or financial position. Additional information regarding REO is provided in Note 6 to the Consolidated Financial Statements.

Reserves for Losses on Mortgages: Management maintains the corporation's reserves for mortgage losses at levels it deems are adequate to absorb losses incurred on the retained and sold portfolios. In estimating losses incurred on the single-family mortgage portfolio, management evaluates numerous factors, including general and regional economic conditions, expected future default experience and mortgage collateral values. The multifamily reserve valuation process is based on the determination of collateral deficiencies reflecting assessments of current market values and incorporates assumptions regarding default probabilities. Management also considers uncertainties related to estimations in the reserve setting process. The combined reserves for mortgage losses for the retained and sold portfolios were $683 million and $733 million at December 31, 1995 and 1994, respectively.

Other Credit Risks: Freddie Mac is subject to credit risk from potential undercapitalization or mismanagement of institutional counterparties. A significant form of institutional credit risk faced by Freddie Mac arises in connection with insolvencies of mortgage servicers. Freddie

Mac is also subject to credit risk from possible financial instability of mortgage insurers. To protect the corporation against such risks, Freddie Mac requires servicers to meet minimum net worth and other eligibility requirements, conducts quality control checks and on-site audits, and institutes remedial actions against seller/servicers that fail to comply with these standards. Similarly, Freddie Mac limits acceptable mortgage insurers to financially sound entities.

From time to time, Freddie Mac faces risk in connection with major natural disasters. In most cases, credit losses experienced by Freddie Mac on properties securing its mortgages within disaster areas have exhibited no material increase from levels in comparable areas not affected by natural disasters. This experience is partly attributable to the fact that homeowner losses often are mitigated by property insurance and by federal and state disaster relief programs. Freddie Mac's own policies extending forbearance to borrowers with properties damaged by natural disasters also may contribute to fewer defaults. Freddie Mac revised its single-family mortgage servicing standards in 1995 to require servicers to ensure that borrowers whose mortgages have been sold to Freddie Mac obtain flood insurance when their dwellings are located in Special Flood Hazard Areas. Also, Freddie Mac changed its underwriting standards in 1995 to require earthquake insurance or similar protection on certain condominium and multifamily properties in designated areas of California. Freddie Mac continues to pursue avenues to mitigate risks associated with natural disasters.

Freddie Mac is also subject to credit risk relating to its non-mortgage investment portfolio and off-balance sheet financial instruments. Credit risk exists to the extent the counterparties to these transactions do not fulfill their obligations to Freddie Mac under the terms of the specific security or contract. The credit risk inherent in the investment portfolio is mitigated to a great extent through Freddie Mac's policy of investing in highly-rated instruments and through the short-term, highly liquid nature of the assets in the corporation's investment portfolio. At December 31, 1995, the portfolio consisted primarily of federal funds sold, reverse repurchase agreements, Eurodollar time deposits and obligations of states and municipalities. Freddie Mac's management of the credit risk associated with off-balance sheet financial instruments is discussed in "Risk Management — Interest-Rate Risk — Off-balance Sheet Financial Instruments."

INTEREST-RATE RISK

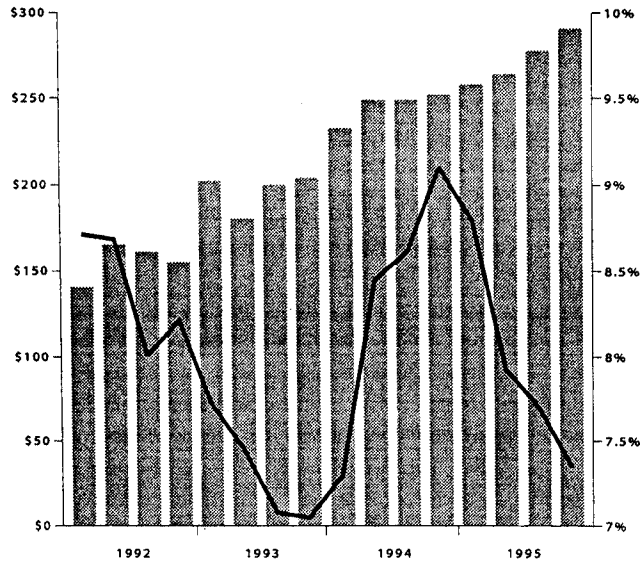
Interest-rate risk is the risk that changes in interest rates could materially change the long-term value or short-term earnings of the corporation. Freddie Mac is subject to interest-rate risk primarily as a result of the ability of borrowers to prepay their mortgages, in most cases without penalty, before the scheduled maturities. Mortgage prepayments can cause fluctuations in earnings if they create mismatches between the maturities of the corporation's assets and liabilities, including the sold portfolio and related contingent guarantee liability. Changing prepayment rates also may require changes in the rate of amortization of deferred income and expense balances.

Freddie Mac's primary interest-rate risk management objective is to maintain the risk of decline in the corporation's value or earnings within acceptable levels. The corporation's interest-rate risk management strategies are designed to manage the risk of the corporation as a whole rather than individual components. Freddie Mac's proprietary computer-based financial models estimate the value of the corporation, and its earnings and capital levels under many interest-rate scenarios. These models help the corporation monitor and manage interest-rate risk, and assist in determining appropriate funding for the retained mortgage portfolio. The substantial growth in the retained portfolio in recent years has made this the primary focus of Freddie Mac's interest-rate risk management activities. The corporation seeks to fund newly purchased mortgage assets to meet risk/return objectives, while at the same time ensuring that the overall portfolio meets risk/return targets. Consequently, Freddie Mac regularly reevaluates its funding strategies with interest-rate risk objectives in mind, and adjusts its mix of debt instruments to suit portfolio rebalancing needs.

The graph below illustrates the stable growth of Freddie Mac's earnings in a wide variety of mortgage rate environments.

EARNINGS vs. MORTGAGE RATES

(dollars in millions)



**30-year single-family fixed-rate mortgages*

Repricing and Prepayment Risk: The corporation's net interest income can increase or decrease whenever mortgage assets in the retained portfolio are repaid faster or slower than expected and the costs of the liabilities funding these assets cannot be correspondingly adjusted.

Freddie Mac is also exposed to interest-rate risk related to principal and interest payments on mortgages underlying the sold portfolio. Timing differences between Freddie Mac's receipt of principal and interest payments from servicers and the subsequent pass-through to PC investors result in the liability "Principal and Interest Due to Mortgage Participation Certificate Investors" (P&I Due). The aggregate balance of P&I Due is determined by the size of the sold portfolio, prepayment rates, mortgage coupon rates and the rates of scheduled amortization.

P&I Due consists of an interest-free component and an interest-bearing component. The interest-free component arises from the pass-through of scheduled principal and interest payments. The interest-bearing component, known as the PC Variance, arises from the pass-through of principal prepayments, and bears a rate equal to the average coupon on the PCs backed by the prepaying mortgages.

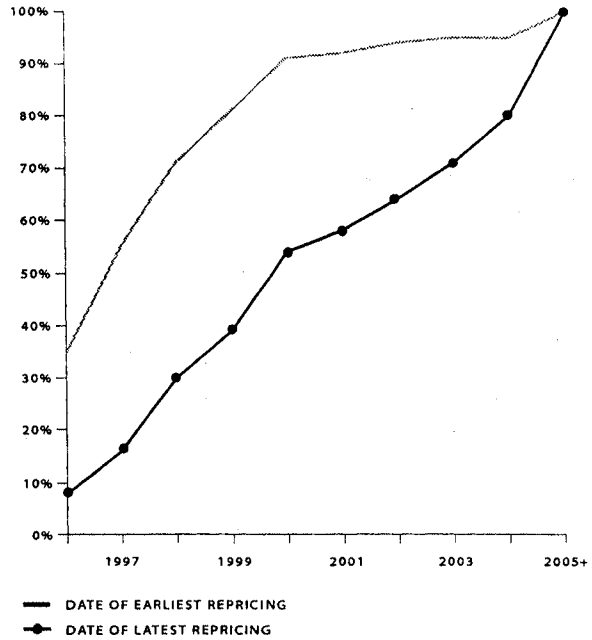
The cash balances associated with the P&I Due liability are held for periods that range from less than one week to over two months. While the aggregate cash balance associated with P&I Due varies with prepayment levels and other factors, there is a core level below which this cash balance is highly unlikely to fall. The corporation generally uses this core cash balance as a source of long-term funding for the retained mortgage portfolio. The variable amount of cash balances above this core level is generally invested in short-term money market instruments or used as a substitute for short-term debt.

Freddie Mac is exposed to interest-rate risk on P&I Due because changes in prepayment rates, short-term interest rates and other factors can cause material fluctuations in the interest expense paid on the PC Variance and the interest income (or reduction in interest expense) on cash balances associated with P&I Due. Countervailing changes in other components of the corporation's asset/liability mix, or the corporation's asset/liability rebalancing, may partially or totally offset these fluctuations. However, in certain environments, these fluctuations can cause material changes in the corporation's short-term net interest income and earnings.

Freddie Mac manages repricing and prepayment risk by funding the retained mortgage portfolio with a mixture of liabilities designed to match the expected cash flow characteristics of the financed mortgages, while allowing the corporation to adjust debt maturities in response to changes in prepayment rates. This is largely accomplished through the issuance of long-term callable debt and through the use of off-balance sheet interest-rate contracts that effectively create long-term debt with downward interest-rate adjustment features. The use of these debt instruments provides interest-rate risk protection over a wide range of both increasing and decreasing interest-rate environments by allowing the corporation to reprice its funding costs as interest rates decline and mortgages prepay, or keep its funding costs stable as interest rates rise and mortgages remain in the portfolio. At December 31, 1995, approximately 73 percent of Freddie Mac's effective long-term debt funding consisted of debt with call protection or downward interest rate adjustment features.

Freddie Mac's financing strategies emphasize long final maturities on debt, coupled with call options allowing the corporation to refinance the debt prior to maturity. Callable debt allows the corporation to use longer final maturities than would be prudent without the call option. The following graph illustrates the earliest and latest available maturities of Freddie Mac's outstanding long-term debt as of December 31, 1995. The solid line illustrates the cumulative amount of the corporation's long-term debt that is available for repricing either through maturity or the exercise of the call option in each year for the next ten years and beyond. These earliest repricing opportunities provide substantial protection against prepayment risk. The dotted line shows the cumulative final maturity of the corporation's long-term debt, without regard to call features. These long final maturities provide protection if prepayments slow and the lives of the corporation's assets extend.

COMPOSITION OF LONG-TERM DEBT FUNDING



The percentage of effective long-term debt with call or downward rate adjustment features decreased to approximately 73 percent from approximately 81 percent at December 31, 1994. During 1995, the corporation purchased for the retained portfolio Freddie Mac PCs with underlying mortgage note rates that were below prevailing current coupon mortgage rates. Lower coupon mortgages reduce prepayment risk and thus decrease the need for callable debt.

In its efforts to reduce debt costs, Freddie Mac expanded the investor base for its debt issuances during 1995 by creating a global debt facility to improve the corporation's access to the international bond markets. Freddie Mac's international funding program is separate from the corporation's domestic funding programs because it incorporates elements required or preferred by bond investors outside of the United States. Freddie Mac issued approximately $1.5 billion of callable bonds during 1995 through its global debt facility.

Freddie Mac also uses short-term liabilities to finance a portion of the retained mortgage portfolio expected to prepay in the short term. The corporation increases the level of short-term funding when prepayment levels rise to reflect the effective shortening of the maturities of the retained mortgage portfolio. This also tends to offset the increase in PC Variance expense that generally occurs when prepayment rates rise. The objective of this debt funding strategy is to minimize the impact of changes in interest rates and prepayment rates on net interest income. The corporation's purchases of ARMs are primarily funded by the issuance of floating-rate debt.

Deferred Items: The corporation receives fees and incurs costs at the time mortgages are purchased or sold. These fees and costs are deferred and amortized over the estimated weighted average lives of the mortgages to result in a level yield. The amount of amortization charged to interest income and Management and guarantee income may vary from period to period, depending on the difference between the actual and expected lives of the mortgages. The corporation manages the interest-rate risk associated with deferred purchase and sale premiums, discounts, fees and costs, in part, through other on-balance sheet instruments that exhibit opposite behavior in response to changing prepayment rates.

Coupon Distribution: The low interest rates that prevailed in the refinancing wave during 1993 and early 1994 caused the coupon rate distribution of Freddie Mac's total mortgage portfolio to shift downward. This shift has reduced the susceptibility of Freddie Mac's portfolio to future refinancing waves. The following table shows the distribution of the total mortgage portfolio by coupon range.

Coupon Range

December 31,	1995	1994	1993
0% to 6.99%	19.3%	22.2%	18.9%
7% to 7.99%	40.6	38.5	33.9
8% to 8.99%	25.0	22.3	23.0
9% to 9.99%	9.4	9.8	13.3
10% to 10.99%	4.5	5.6	8.6
11% or greater	1.2	1.6	2.3
Total	100.0%	100.0%	100.0%
Weighted Average Coupon	7.81%	7.79%	8.03%

Off-balance Sheet Financial Instruments: The corporation enters into certain off-balance sheet financial transactions, primarily interest-rate swaps, caps, floors and corridors, as an "end user" and not for trading or speculative purposes. Interest-rate swaps are contractual agreements between two parties for the exchange of periodic payments based on a notional principal amount and agreed-upon fixed and variable interest rates. Interest-rate caps and floors are contracts under which one party, in exchange for a one-time up-front payment, is entitled to receive from a counterparty one or more periodic future payments based on a notional amount when interest rates exceed the cap rate or fall below the floor rate. Interest-rate corridors combine purchased and sold interest-rate caps or floors to effectively reduce the cost of the interest-rate cap or floor protection. Currently, all of the interest-rate corridors entered into by Freddie Mac involve interest-rate caps.

The primary objective of these transactions is to lower the corporation's financing costs as well as reduce the corporation's exposure to interest-rate risk. To a lesser extent, the corporation also enters into interest-rate contracts to increase yields on specific assets held in both the corporation's retained portfolio and investment portfolio. The corporation's use of interest-rate contracts is expected to grow as funding requirements for its retained portfolio continue to increase. Currently, all of the corporation's interest-rate contracts are U.S. dollar denominated. As of December 31, 1995, approximately 15 percent of the notional contract amount of the corporation's interest-rate contracts involved non-U.S. counterparties. In certain cases, the obligations of some U.S. counterparties have been guaranteed by their foreign affiliates. The following table summarizes the notional or contractual amounts of interest-rate contracts and other hedging instruments along with their remaining contractual maturities.

	Notional or Contractual Amount	
December 31,	**1995**	**1994**
(dollars in millions)		
Outstanding at period end:		
Debt-linked swaps	$37,277	$17,333
Asset-linked swaps	7,107	1,661
Interest-rate swaps	1,000	2,840
Interest-rate caps	4,448	3,145
Interest-rate floors	6,078	4,950
Corridors	2,529	908
Spread-lock agreements	24	–
Total	$58,463	$30,837
Contractual maturity:[1]		
Under one year	$ 6,763	$ 6,893
From one to five years	28,977	15,043
From five to ten years	19,982	7,883
Over ten years	2,741	1,018
Total	$58,463	$30,837

(1) Certain of the corporation's interest-rate contracts contain provisions permitting termination prior to contractual maturity. In addition, interest-rate contracts generally may be terminated by mutual consent of the parties, or effectively canceled by entering into an offsetting transaction.

The majority of Freddie Mac's interest-rate agreements are interest-rate swap agreements executed in conjunction with debt financing (debt-linked swaps). Debt-linked swaps effectively convert longer-term debt to short-term variable-rate financing or convert short-term variable-rate financing to longer-term fixed-rate debt, as appropriate. During 1994 and 1995, most debt-linked swap transactions involved the receipt of variable-rate amounts that reprice or adjust within one year and payment of fixed-rate amounts over the terms of the swaps, which generally range from two to ten years. Freddie Mac also enters into asset-linked swaps that are linked to specific assets held in the corporation's retained mortgage or investment portfolios. Debt-linked and asset-linked swaps, when combined with the underlying asset or liability, synthetically create debt instruments and interest-earning assets that achieve a lower effective financing cost or higher effective asset yield than those available on alternative instruments and reduce

the corporation's exposure to interest-rate risk. Similarly, interest-rate caps, floors and corridors produce lower effective debt costs and higher asset yields when combined with short-term debt issuances and asset purchases by limiting the impact of significant interest-rate changes on these instruments. To a lesser extent, the corporation uses short sales of Treasury securities and spread-lock agreements to hedge against the effects of changes in interest rates on the cost of debt used to finance the retained portfolio.

During 1995, the corporation entered into $38.0 billion notional amount of interest-rate agreements, $6.6 billion notional amount of interest-rate agreements matured and $3.7 billion notional amount were called prior to contractual maturity. Interest-rate agreements were called prior to contractual maturity at their par values and thus no gains or losses were deferred or recorded to income. The notional principal amount of outstanding interest-rate agreements increased to $58.5 billion at December 31, 1995, from $30.8 billion at December 31, 1994. The increase in the notional principal amount of interest-rate agreements compared to December 31, 1994 primarily reflects increased funding needs associated with continued growth of the retained mortgage portfolio during 1995. Notional amounts serve only as a factor in determining periodic interest amounts to be received and paid and do not themselves represent actual amounts to be exchanged. Thus, they do not directly reflect the corporation's exposure to credit and market risks.

Failure of a counterparty to perform under the terms of an interest-rate agreement exposes the corporation to credit risk. The corporation's aggregate exposure to credit loss for interest-rate agreements can be estimated by calculating the cost to replace at current market values all outstanding agreements for each counterparty with which the corporation was in a net gain position. The corporation's estimate of its aggregate exposure to credit risk for transactions in a gain position was $27 million at December 31, 1995, compared to $828 million at December 31, 1994. The substantial decrease in credit loss exposure reflects a general decrease in interest rates since early 1995, which caused the payment obligations of counterparties under interest-rate agreements where Freddie Mac receives a variable-rate obligation to decrease.

Freddie Mac manages the counterparty credit risk associated with interest-rate agreements by dealing only with institutions that meet high credit standards, limiting its exposure to any one counterparty, regularly monitoring financial positions and requiring collateral in many cases. At December 31, 1995, four counterparties, each with a credit rating of A+ or better from one or more nationally recognized credit rating agencies, accounted for approximately 52 percent of the notional amount of the corporation's outstanding interest-rate agreements. Collateral supporting the corporation's net gain positions at December 31, 1995 had an estimated market value of $3 million, compared to $498 million at December 31, 1994. Substantially all of the corporation's uncollateralized net gain position of $24 million at December 31, 1995 resulted from positions taken with counterparties having among the highest credit ratings available from major rating agencies. The corporation's policy for requiring collateral from counterparties to interest-rate agreements is based on independent credit ratings, estimated credit loss exposure on net gain positions and assessments of counterparty credit quality. Freddie Mac has not set aside specific reserves for counterparty credit exposure and does not believe such reserves are necessary at this time given the corporation's collateral and counterparty policy requirements. To date, Freddie Mac has not incurred any counterparty defaults relating to interest-rate agreements.

Although Freddie Mac's interest-rate risk management strategies are designed to minimize the corporation's exposure to market risk resulting from changes in interest rates, Freddie Mac's exposure to credit loss can fluctuate from period to period due to changes in interest rates. Further information regarding off-balance sheet financial transactions is included in Note 10 to the Consolidated Financial Statements.

AVERAGE BALANCE SHEETS AND RATE/VOLUME ANALYSIS

The table on the following page presents average balance sheets for the years ended December 31, 1995, 1994 and 1993, as well as information with respect to yields earned on assets and rates paid on liabilities for these periods.

Monthly weighted average balances are calculated for interest-earning assets, interest-bearing liabilities and contingencies. When monthly weighted average balance information is not available, a simple month-to-month average balance is calculated. The accompanying rate/volume analysis details the changes to Net interest income on earning assets and Management and guarantee income during 1995, 1994 and 1993 resulting from changes in average balances and interest rates.

AVERAGE BALANCE SHEETS

Year ended December 31,	1995			1994			Pro Forma 1993[1]		
(dollars in millions)	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate
Assets									
Interest-earning assets:									
Retained mortgages, net	$ 86,506	$6,505	7.52%	$ 62,474	$4,528	7.25%	$ 41,865	$3,216	7.68%
Investments:									
Cash and investments	24,146	1,437	5.96[2]	22,110	973	4.40[2]	25,732	838	3.26[2]
Mortgage securities purchased under agreements to resell	7,397	451	6.10	7,515	314	4.18	8,783	289	3.30
	31,543	1,888	5.99	29,625	1,287	4.34	34,515	1,127	3.27
Total interest-earning assets	118,049	8,393	7.11	92,099	5,815	6.31	76,380	4,343	5.69
All other assets	3,412			3,189			3,061		
Total assets	$121,461			$ 95,288			$ 79,441		
Liabilities and Stockholders' Equity									
Interest-bearing liabilities:									
Debt securities, net:[3]									
Short-term notes and bonds	$ 47,502	2,898	6.10	$ 35,303	1,644	4.66	$ 26,837	858	3.20
Long-term notes and bonds	59,058	3,780	6.40	40,940	2,476	6.05	23,305	1,492	6.41
Subordinated borrowings	945	86	9.07	1,430	143	9.99	1,473	149	10.07
	107,505	6,764	6.29	77,673	4,263	5.49	51,615	2,499	4.84
Due to PC investors	3,982	233	5.86	6,383	440	6.90	12,856	1,072	8.34
Total interest-bearing liabilities	111,487	6,997	6.28	84,056	4,703	5.60	64,471	3,571	5.54
All other liabilities	4,430			6,420			10,983		
Stockholders' equity	5,544			4,812			3,987		
Total liabilities and stockholders' equity	$121,461			$ 95,288			$ 79,441		
Net interest income/yield		$1,396	1.18%		$1,112	1.21%		$ 772	1.01%
Net interest yield (fully taxable equivalent basis)			1.23%			1.25%			1.02%
Sold portfolio									
Management and guarantee income/spread	$457,476	$1,087	23.8bp	$459,715	$1,108	24.1bp	$423,273	$1,009	23.8bp

(1) 1993 is presented on a pro forma basis for comparative purposes to reflect the adoption in 1994 of a change in the reporting of uncollectible interest on single-family mortgages.

(2) Rates computed on a fully taxable equivalent basis are 6.18%, 4.54% and 3.34% for the years ended December 31, 1995, 1994 and 1993, respectively.

(3) Average balances and average rates do not include the effect of off-balance sheet interest-rate agreements.

RATE/VOLUME ANALYSIS

(dollars in millions)	1995 vs. 1994 Increase or (Decrease) Due To[1]			1994 vs. 1993 Increase or (Decrease) Due To[1]		
	Rate	Volume	Total	Rate	Volume	Total
Income from interest-earning assets:						
Retained mortgages, net	$175	$1,802	$1,977	$(191)	$1,503	$1,312
Investments	514	87	601	335	(175)	160
Total income from interest-earning assets	$689	$1,889	$2,578	$ 144	$1,328	$1,472
Expense on interest-bearing liabilities:						
Debt securities, net	$690	$1,811	$2,501	$ 369	$1,395	$1,764
Due to PC investors	(59)	(148)	(207)	(161)	(471)	(632)
Total expense on interest-bearing liabilities	$631	$1,663	$2,294	$ 208	$ 924	$1,132
Change in Net interest income[2]	$(23)	$ 307	$ 284	$ 165	$ 175	$ 340
Change in Management and guarantee income	$(15)	$ (6)	$ (21)	$ 12	$ 87	$ 99

(1) Combined rate/volume variances, a third element of the calculation, are allocated based on the relative size of the rate and volume variances.

(2) Reflects changes in total interest-earning assets and net interest yield.

SUMMARY OF RESULTS

Year Ended December 31,	1995	1994	1995 vs. 1994 Dollar Change	1995 vs. 1994 % Change	Pro Forma 1993[1]	1994 vs. 1993 Dollar Change	1994 vs. 1993 % Change
(dollars in millions, except per share amounts)							
Net interest income on earning assets	$1,396	$1,112	$ 284	26 %	$ 772	$ 340	44 %
Management and guarantee income	1,087	1,108	(21)	(2)	1,009	99	10
Other income, net	39	66	(27)	(41)	128	(62)	(48)
Total Revenues	$2,522	$2,286	$ 236	10 %	$1,909	$ 377	20 %
Credit-related expenses	$ 541	$ 425	$ 116	27 %	$ 420	$ 5	1 %
Administrative expenses	395	379	16	4	361	18	5
Total Non-interest expenses	$ 936	$ 804	$ 132	16 %	$ 781	$ 23	3 %
Net income	$1,091	$ 983	$ 108	11 %	$ 786	$ 197	25 %
Earnings per common share	$ 5.69[2]	$ 5.08[2]	$0.61	12 %	$ 4.07[2]	$1.01	25 %
Total mortgage portfolio (dollars in billions)	$566.5	$533.5	$33.0	6 %	$494.7	$38.8	8 %

(1) In 1994, Freddie Mac changed the way it reports uncollectible interest on single-family mortgages. As a result of the change, the Provision for mortgage losses and the sum of Net interest income on earning assets and Management and guarantee income are reduced by approximately equal amounts, with no material effect on net income. For comparative purposes, 1993 amounts are reported on a pro forma basis, as if the new method had been in effect for that year. The discussion that follows is based on the pro forma amounts resulting from the single-family reporting change, where applicable.

(2) After payments of preferred stock dividends of $65 million, $65 million and $52 million for 1995, 1994 and 1993, respectively.

RESULTS OF OPERATIONS

Freddie Mac had net income of $1.091 billion on revenues of $2.522 billion in 1995. Net income in 1995 represented an 11 percent increase from $983 million reported for 1994. Revenues increased $236 million, or 10 percent, from $2.286 billion in 1994. Earnings per common share were $5.69 in 1995, up 12 percent over $5.08 in 1994. Net income for 1994 was up 25 percent over $786 million in 1993, and earnings per common share increased 25 percent over $4.07 in 1993.

Net Interest Income on Earning Assets

Net interest income on earning assets increased by $284 million, or 26 percent, from $1.112 billion in 1994 to $1.396 billion in 1995. Growth in net interest income primarily reflects a $26.0 billion, or 28 percent, increase in average interest-earning assets. The increase in average interest-earning assets was driven by growth of $24.0 billion, or 38 percent, in the average balance of the retained mortgage portfolio. In addition, the average investment portfolio balance increased by $1.9 billion, or 6 percent from 1994.

Net additions to the retained portfolio totaled $35 billion during 1995. Freddie Mac's substantial retained portfolio growth was made possible by a relatively large supply of mortgages and mortgage-related securities available for purchase by the corporation at attractive mortgage asset-to-debt spreads. Declining interest rates and the resulting shift in demand from ARMs to fixed-rate mortgages during the year increased sales of mortgages into the secondary market. In addition to purchasing and retaining an increasing volume of mortgages, Freddie Mac was able to make substantial additions to the retained portfolio by purchasing PCs, REMICs and other mortgage-related securities throughout 1995 as attractive spreads became available.

Growth in net interest income was tempered by a 2 basis point decrease in the Net interest yield on earning assets on a fully taxable equivalent basis. The decrease in net interest yield compared to 1994 resulted primarily from a lower average level of non-interest-bearing funding in proportion to the overall funding mix. In a period when interest-earning assets are growing faster than non-interest-bearing funding, a higher proportion of total funding is interest-bearing which, in turn, results in some compression of net interest yield. While the corporation's net interest yield may experience some compression when non-interest-bearing funding as a proportion of interest-earning assets decreases, overall net interest income can continue to grow. Net interest yield also may experience some compression as short-term interest rates rise because a small portion of the retained portfolio is funded with short-term debt.

Lower initial net yields on retained portfolio purchases during 1995 also reduced net interest yield. The lower initial net yields resulted from a flatter yield curve in 1995 as compared to much of 1994. In a steeper yield curve environment, Freddie Mac's funding strategy generally results in the purchase of mortgage assets with relatively higher initial net yields that decline more rapidly over time. In a flatter yield curve environment, this same funding strategy results in lower initial net yields that are more stable over time. Freddie Mac's funding strategy is intended to facilitate purchases of mortgage assets that provide acceptable rates of return on equity in a wide range of yield curve environments.

The decrease in net interest yield was partially offset by an increase in the proportion of interest-earning assets represented by mortgages and mortgage-related securities as opposed to shorter term non-mortgage investments. The average balance of retained mortgages and mortgage-related securities increased 38 percent compared to 1994 while the average balance of the investment portfolio increased 6 percent. This shift in the mix of interest-earning assets tends to increase net interest yield since mortgage assets usually generate higher net yields than short-term investments. The disciplined growth of the retained portfolio combined with the corporation's common stock repurchase program initiated in 1995 (see "Liquidity and Capital Adequacy — Capital Adequacy") were the primary drivers of the shift in the mix of interest-earning assets. As the corporation repurchases outstanding common shares and returns capital to its shareholders, the portfolio of short-term investments is decreased over time.

Management expects the majority of growth in interest-earning assets in 1996 to be in the retained mortgage portfolio rather than in the non-mortgage investment portfolio. Based on market conditions in early 1996, the retained portfolio is expected to grow substantially during the year. Actual growth in the retained portfolio will depend on the availability of attractive returns on capital invested in mortgage assets for the retained portfolio. These returns are a function of the difference between the expected yield on the mortgage assets and the expected cost of debt financing, as well as the amount of capital supporting these investments. Both the expected yield on mortgage assets and the expected cost of debt financing can vary over the life of the investment depending primarily on changes in interest rates and mortgage prepayment speeds. The cost of debt can also vary with changes in the supply of and demand for both Freddie Mac debt securities and callable debt securities generally. Future growth in the retained portfolio is expected to continue to be funded with a mix of debt instruments, primarily long-term callable debt, designed to maximize expected return on equity while limiting interest-rate risk. Any changes in investor preferences, funding costs or other factors that reduce the market demand for callable debt securities generally, could result in a slower rate of growth for the retained portfolio and could increase the corporation's exposure to interest-rate risk on its existing mortgage assets.

The primary drivers of the corporation's net interest yield in 1996 will be the declining net yield on the existing portfolio, the volume and initial net yields of retained portfolio purchases in 1996, the mix of mortgage assets versus non-mortgage investments and the relative growth rates of interest-earning assets versus non-interest-bearing funding.

Interest income on retained mortgage assets does not include interest deemed uncollectible on non-performing mortgages. If these non-performing mortgages had been fully performing, they would have contributed an additional $105 million, $153 million and $138 million to retained mortgage portfolio interest income in 1995, 1994 and 1993, respectively.

In the third quarter of 1995, the corporation modified its method of reporting PC Variance expense. During the time between receipt of principal and interest payments from seller/servicers and the subsequent pass-through to PC investors, Freddie Mac earns interest income from the investment of these funds (investment income) and incurs interest expense on the funds owed but not yet paid to investors (PC Variance expense).

Float balances arising from mortgage prepayments are invested and interest income is earned from the date proceeds are remitted to Freddie Mac through the date Freddie Mac remits these proceeds to PC investors, which is generally 38 to 68 days, depending on the type of security and the remittance agreement between the seller and Freddie Mac. Previously, interest expense on PC variance balances was recognized for an average of 30 days following receipt of prepayment proceeds. Under the revised method of reporting, the same dollar amount of PC Variance expense is recognized over the 38 to 68 day period, consistent with the corresponding period during which investment income will be earned.

The corporation believes that this modification more appropriately matches the recognition of the expense with the corresponding investment income, and provides more comparable period-to-period net interest yields. The modification did not have a material effect on 1995 results.

The $340 million, or 44 percent, increase in net interest income on earning assets between 1993 and 1994 reflected a 21 percent increase in average interest-earning assets driven by retained portfolio growth of 49 percent. In addition, net interest income was enhanced by a 23 basis point increase in the Net interest yield on earning assets on a fully taxable equivalent basis. The increase in net interest yield was due to both an increase in the proportion of interest-earning assets represented by mortgages and growth in non-interest-bearing funding approximately equal to the rate of growth in interest-earning assets.

Management and Guarantee Income

Management and guarantee income, the fee Freddie Mac earns for administering payments and providing its credit guarantee on mortgages in the sold mortgage portfolio, decreased $21 million, or 2 percent from 1994 due to a 0.3 basis point decrease in the average guarantee fee rate coupled with a $2.2 billion decrease in the average sold portfolio balance. The decrease in the average sold portfolio balance reflects a reduction in primary market mortgage originations from 1994 to 1995, the cyclical decline in the secondary market purchase share of these originations, and purchases of outstanding PCs and REMICs for the corporation's retained mortgage portfolio.

The average guarantee fee rate continues to be impacted by lower fee rates on new additions to the sold portfolio combined with the ongoing liquidation of existing balances having comparatively higher fee rates. The lower guarantee fee rates on new additions primarily are due to an increasing proportion of mortgage purchases since the latter half of 1994 that carry some type of credit enhancement (see "Risk Management — Credit Risk Management — Portfolio Sensitivity"). The increase in mortgage purchases with lower guarantee fee rates also has resulted from an increase during 1995 in the proportion of purchases of seasoned loans from lenders' existing portfolios in credit-enhanced transactions.

The increase in the proportion of credit-enhanced purchases moderates short-term revenue growth while the associated decreases in credit-related expenses are not realized until several years after purchase when mortgages normally reach their peak period of default. In addition, many credit-enhanced transactions produce significant amounts of float income, as a result of remittance agreements between the mortgage seller and Freddie Mac, which is recognized as interest income primarily at the time of mortgage prepayment. Despite the impact on short-term earnings growth, credit-enhanced purchases can provide attractive returns on equity since the lower guarantee fee rates are expected to be more than offset by lower credit-related expenses over time.

Management and guarantee income does not include interest deemed uncollectible on non-performing mortgages. If these non-performing mortgages had been fully performing, they would have contributed an additional $23 million, $32 million and $24 million to Management and guarantee income in 1995, 1994 and 1993, respectively.

The $99 million, or 10 percent, increase in Management and guarantee income from 1993 to 1994 was due to a $36.4 billion, or 9 percent, increase in the average sold portfolio balance coupled with a 0.3 basis point increase in the average guarantee fee rate. The increase in the average guarantee fee rate reflected a $30 million acceleration of deferred expense amortization in 1993 resulting from high levels of mortgage prepayments that occurred in that year.

Year ended December 31,	1995	1994	1993
(dollars in millions)			
Issuances of original issue securities:[1]			
30-year single-family fixed-rate[2]	$54,426	$ 65,750	$103,103
15-year single-family fixed-rate	13,110	24,673	61,741
5- and 7-year balloon/resets	3,719	9,889	23,052
Adjustable-rate	14,267	16,589	20,828
Multifamily	355	209	-
Total[3]	$85,877	$117,110	$208,724
Exchanges of 75-day PCs to Gold PCs	$ 1,117	$ 1,022	$ 4,139
Issuances of resecuritized PCs:			
Multiclass PCs	$15,372	$ 73,131	$143,336
Giant PCs	19,979	37,479	41,321
Total	$35,351	$110,610	$184,657

(1) Original issue securities include PCs and REMICs backed by newly purchased mortgages, rather than previously existing PCs.

(2) Includes 20-year single-family fixed-rate mortgages.

(3) Includes issuances of $71.6 billion, $100.5 billion and $187.9 billion of Gold PCs and $14.3 billion, $16.6 billion and $20.8 billion of 75-day PCs in 1995, 1994 and 1993, respectively.

Other Income, Net

Other income, net, decreased $27 million compared to 1994 primarily due to lower REMIC fee income attributable to a significant decline in REMIC settlement volumes. REMIC volumes have been adversely affected by decreases in mortgage originations and PC settlements from 1994 to 1995, as well as reduced investor demand for certain REMIC securities in response to rising interest rates during 1994 and early 1995 and the resulting relative lack of liquidity of these REMIC securities.

The remaining components of Other income, net, increased $5 million compared to 1994. These components, consisting largely of income related to securities market activities, fee for service activities and other fees collected from seller/servicers, tend to fluctuate from period to period. Freddie Mac experienced modest increases in revenues and expenses relating to Loan Prospector℠ during 1995, but the effect of these changes on net income is not material.

Other income, net, decreased $62 million between 1993 and 1994 due primarily to lower REMIC fee income attributable to the sharp decline in REMIC issuances in 1994.

Credit-Related Expenses

Total credit-related expenses consist of the Provision for mortgage losses and REO operations expense. The Provision for mortgage losses is charged against income in an amount considered appropriate to maintain the corporation's reserves for mortgage losses at levels that management deems adequate to absorb losses incurred on the retained and sold mortgage portfolios. REO operations expense includes foreclosure-related costs, REO valuation adjustments and other income and expense items related to operating and disposing of acquired properties.

Total credit-related expenses increased $116 million, or 27 percent, from $425 million in 1994 to $541 million in 1995. The Provision for mortgage losses increased from $200 million in 1994 to $255 million in 1995. The provision was increased during 1995 to cover increased single-family charge-offs. As discussed in "Risk Management — Credit Risk — Credit Performance — Mortgage Charge-offs and REO," single-family charge-offs increased due to increased REO acquisition losses resulting from economic weakness and declining average house prices in California and certain areas within the Northeast region, as well as increased loss mitigation activities which tend to shift losses from net interest income and REO operations expense to charge-offs.

Single-family REO operations expense increased $73 million, from $181 million in 1994 to $254 million in 1995. This increase was due to costs related to higher REO acquisitions along with higher holding and disposition costs resulting from declining average house prices in the areas mentioned above. Multifamily REO operations expense decreased $12 million, from $44 million in 1994 to $32 million in 1995, reflecting the decreasing REO balance.

Administrative Expenses

The major components of administrative expenses are costs related to personnel, occupancy and equipment. Administrative expenses increased $16 million, or 4 percent, from $379 million in 1994 to $395 million in 1995. The rate of administrative expense growth in 1995 was less than the rate of revenue growth and approximately equal to average total mortgage portfolio growth. The ratio of administrative expenses to revenues declined from approximately 17 percent in 1994 to approximately 16 percent in 1995. Administrative expenses as a percentage of the average total mortgage portfolio were 7.3 basis points for 1995, unchanged from 1994. Administrative expenses are expected to increase in 1996 with technology initiatives and credit risk management being primary areas of investment. Direct development costs related to significant technological initiatives have been capitalized and are expensed over relatively short periods of time.

Administrative expenses increased $18 million, or 5 percent, from 1993 to 1994, less than both revenue growth and average total mortgage portfolio growth during that period.

Other Items

Effective January 1, 1996, the corporation will revise the method by which it reports balances and associated income for Freddie Mac PCs held in the retained mortgage portfolio. This reporting change has no impact on total revenues or net income. The change is designed to more clearly portray portfolio balances and associated revenues for Freddie Mac's two principal revenue sources: mortgage portfolio investment and credit guarantee.

Prior to 1996, PCs held in the retained portfolio were included in the retained portfolio balance and excluded from the sold portfolio balance. Both the PC coupon interest and Management and guarantee income on these securities were included in Net interest income as a component of interest earned on the retained portfolio.

Under the new reporting presentation, these PCs will continue to be included in the retained portfolio as guaranteed mortgage security investments, but will also be included in total PCs outstanding (sold portfolio). The total mortgage portfolio balance can be calculated as the sum of the retained portfolio and the sold portfolio, less PCs held in the retained portfolio.

The guarantee fee income on these PCs will now be reported as part of Management and guarantee income. The PC coupon interest will continue to be reported as part of Net interest income on earning assets.

The following table provides pro forma information relating to this reporting change for 1995, 1994 and 1993, respectively.

Year ended December 31,	**1995**	**1994**	**1993**
(dollars in millions)			
Retained portfolio:			
Mortgages	$ 43,753	$ 40,970	$ 39,357
Guaranteed mortgage securities	63,671	31,858	16,341
Ending portfolio balance	$107,424	$ 72,828	$ 55,698
Average portfolio balance	$ 86,872	$ 62,990	$ 43,573
Net interest income	$ 1,297	$ 1,047	$ 728
Net interest yield	1.10%	1.12%	0.93%
Total PCs outstanding:			
Ending balance	$515,051	$491,325	$454,906
Average balance	$497,246	$481,434	$435,274
Management and guarantee income	$ 1,186	$ 1,174	$ 1,053
Average guarantee fee rate	23.9 bp	24.4 bp	24.2 bp

In March 1994, the corporation received from the Internal Revenue Service (IRS) a Revenue Agent Report for its 1985 and 1986 federal income tax returns. In anticipation that this report would assert a deficiency, management previously had established reserves for additional taxes and related interest.

Positions taken by the IRS resolved several open issues, including hedging issues that were treated in a manner consistent with regulations issued by the IRS in October 1993. The resolution of these issues allowed the corporation to reduce its existing reserves for contingent taxes and report a one-time reduction in its 1994 provision for income taxes of $16 million, and also to reduce its reserves for related contingent interest.

In conjunction with this reduction in reserves, several actions were taken by management. First, along with the change in the reporting of uncollectible interest on single-family mortgages implemented in 1994, the corporation wrote off $120 million of accrued but uncollectible interest that had previously been provided for in mortgage loss reserves. The balance of mortgage loss reserves was not reduced by this transaction. Second, the corporation retired high-cost debt, generating $16 million, or $0.08 per common share, of after-tax extraordinary losses. These actions and the reduction in tax and interest reserves had no effect on 1994 net income.

The corporation also recorded an additional $28 million after-tax extraordinary loss on retirement of high-cost debt in addition to the actions described above. In total, 1994 after-tax extraordinary losses on debt retirements amounted to $44 million, or $0.24 per common share.

During 1993, the corporation recorded a $20 million after-tax extraordinary loss associated with the retirement of high-cost debt.

Effective January 1, 1993, Freddie Mac adopted SFAS No. 109, "Accounting for Income Taxes." The $20 million net benefit from adopting the standard was reported as a cumulative effect of a change in accounting

principle for 1993. The net benefit resulted from adjusting deferred tax amounts to reflect the federal statutory income tax rate of 34 percent in effect at January 1, 1993, as opposed to the higher tax rates that were in effect when the associated timing differences originated.

During 1993, the corporation recognized a one-time tax benefit of $17 million for the remeasurement of its net deferred tax asset at the higher federal statutory income tax rate of 35 percent established by the Omnibus Budget Reconciliation Act of 1993 (OBRA). Taxes associated with 1993 earnings were $11 million higher due to the increased statutory income tax rate. Thus, the adoption of OBRA provided a net benefit of $6 million to 1993 earnings.

Regulatory Matters

Capital Standards: Under the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the GSE Act), Freddie Mac is subject to certain minimum and risk-based capital standards. In its most recent classification, the Director of OFHEO classified Freddie Mac "adequately capitalized," OFHEO's highest classification. As of December 31, 1995, Freddie Mac's core capital was $5.8 billion.

The Director of OFHEO is developing a regulation that will implement the risk-based capital standard using a stress test model. Freddie Mac has used stress test models for internal assessments of capital adequacy for several years. Freddie Mac believes that a reasonable interpretation of the risk-based capital standard would not require the corporation to substantially increase its capitalization, and that the corporation has adequate access to the capital markets to raise any necessary additional capital. While the risk-based capital standard can have a significant impact on the corporation, it is impossible to determine at this time what, if any, impact the final regulations will have on Freddie Mac. See Note 9 to the Consolidated Financial Statements for further information regarding regulatory capital standards.

Housing Goals: The GSE Act requires the Secretary of the Department of Housing and Urban Development (HUD) to establish three mortgage purchase goals for Freddie Mac — a goal for the purchase of mortgages on housing for low- and moderate-income borrowers (the "Low- and Moderate-Income Goal"); a goal for the purchase of mortgages on housing located in central cities, rural areas and other underserved areas; and a goal for the purchase of mortgages on housing for low-income borrowers in low-income areas and for very low-income borrowers (the "Special Affordable Goal"). In October 1993, the Secretary established interim housing goals for the transition period of 1993 and 1994. In November 1994, the Secretary extended the interim housing goals through 1995, pending adoption of final regulations. During the transition period, the goal for the purchase of mortgages on housing located in central cities, rural areas and other underserved areas included only purchases of mortgages on housing located in areas designated as central cities by the United States Office of Management and Budget (the "Central Cities Goal").

Freddie Mac met the Low- and Moderate-Income Goal of 28 percent in 1993 and 30 percent in 1994 and 1995, with low- and moderate-income purchases of 29 percent, 37 percent and 39 percent of the corporation's qualifying mortgage purchases in each year, respectively. Freddie Mac did not meet its Central Cities Goal of 26 percent in 1993 and 30 percent in 1994 and 1995, with qualifying mortgage purchases of 24 percent, 25 percent and 23 percent in each year, respectively. Freddie Mac met its Special Affordable Goal of $11.9 billion for the two-year period of 1993 and 1994 with $12.7 billion of qualifying purchases, but did not meet the $750 million multifamily portion of this goal with $495 million of qualifying multifamily purchases. Freddie Mac met its Special Affordable Goal of $3.357 billion for 1995, including the $375 million multifamily portion of this goal, with over $5.4 billion of qualifying purchases, including over $1.0 billion of qualifying multifamily mortgage purchases.

In December 1995, the Secretary issued final regulations establishing new affordable housing goals for the years 1996 through 1999. Under the final regulations, HUD redefined the goal for the purchase of mortgages on housing located in central cities, rural areas and other underserved areas to measure mortgage purchases based on the income and minority composition of targeted metropolitan and rural areas (the "Underserved Areas Goal"). The new goals provide that 40 percent of the total number of dwelling units financed by the corporation's mortgage purchases meet the Low- and Moderate-Income Goal in 1996 and 42 percent in each of 1997, 1998 and 1999; 21 percent of the total number of dwelling units financed by the corporation's mortgage purchases meet the Underserved Areas Goal in 1996 and 24 percent in each of 1997, 1998 and 1999; and 12 percent of the total number of dwelling units financed by the corporation's mortgage purchases meet the Special Affordable Goal in 1996 and 14 percent in each of 1997, 1998 and 1999, including at least $981 million in qualifying multifamily mortgage purchases in each year from 1996 through 1999.

Management views the purchases of mortgages benefiting low- and moderate-income families and neighborhoods as an integral part of Freddie Mac's mission and business and remains committed to profitably fulfilling the needs of underserved borrowers and markets. Freddie Mac expects to purchase the majority of its single-family and multifamily mortgages counted toward the housing goals through its standard purchase programs.

LIQUIDITY AND CAPITAL ADEQUACY

Liquidity

Freddie Mac's primary business programs present significant liquidity demands that are driven by the maturities of debt, purchases of mortgages, payments to security holders and general operations. The corporation's sources of cash to meet these needs include short- and long-term borrowings, mortgage repayments and cash flows from operations. Because of its strong financial performance, regular and significant participation as an issuer in the capital markets, and status as a government-sponsored enterprise, the corporation has had ready access to debt and other funding markets to meet its liquidity needs. Freddie Mac also expanded its funding capabilities during 1995 by issuing callable debt outside of the United States.

In addition to debt issuances, the corporation maintains an investment portfolio of highly rated and marketable short-term investments to draw upon as necessary. At December 31, 1995 and 1994, Freddie Mac held approximately $21 billion and $29 billion, respectively, of highly rated marketable assets, including cash and cash equivalents, short-term investments and reverse repurchase agreements.

Capital Adequacy

Freddie Mac maintains capital as a cushion to absorb unforeseen losses that might arise in fulfilling its mortgage guarantee obligations and conducting its business programs and to meet regulatory capital requirements. The primary method by which Freddie Mac assesses its capital adequacy for internal purposes is through the use of internally developed stress test models that measure the corporation's survival in response to severe changes in interest-rate and credit environments.

The corporation maintains its primary capital base, which is the sum of Stockholders' equity and Reserves for losses on mortgages, at a level management believes is sufficient to absorb unforeseen losses while permitting the payment of dividends at appropriate levels. Over the past three years, the corporation has added $2.2 billion to its primary capital base and increased its primary capital ratio (primary capital as a percentage of total assets and PCs) from 0.93 percent at December 31, 1992 to 1.10 percent at December 31, 1995. The increase was driven by strong earnings and a preferred stock issuance during that time period. The following table summarizes the components of Freddie Mac's capital base.

December 31,	1995	1994	1993
(dollars in millions)			
Common stock (par)	$ 152	$ 152	$ 152
Preferred stock (par)	35	35	35
Additional paid-in capital	916	913	911
Retained earnings	4,884	4,074	3,344
Net unrealized gain (loss) on securities reported at fair value	33	(7)	-
Treasury stock, at cost	(157)	(5)	(5)
Stockholders' equity	$5,863	$5,162	$4,437
Reserves for losses on mortgages	683	733	760
Primary capital base	$6,546	$5,895	$5,197
Subordinated borrowings	633	1,226	1,483
Adjusted total capital base	$7,179	$7,121	$6,680

In June 1995, Freddie Mac announced its intention to purchase up to $200 million of its common stock in open market purchases over a twelve-month period. This repurchase program is intended to return to shareholders equity capital that currently is invested in short-term non-mortgage investments. The repurchase program has a modest impact on Freddie Mac's capital growth, but is not expected to adversely affect growth in the retained or sold mortgage portfolios or the corporation's overall capital adequacy. As of December 31, 1995, Freddie Mac had purchased approximately $151 million of its common stock in conjunction with the repurchase program.

RECENT EVENTS

Board of Directors

On January 5, 1996, President Clinton appointed Joel I. Ferguson to the Board of Directors of Freddie Mac. Mr. Ferguson is president and co-owner of F&S Development Company in Lansing, Michigan, a developer of multifamily properties, and co-owner of First Housing Corporation, a real estate management company.

On January 17, 1996, Barbara C. Jordan, a member of Freddie Mac's Board of Directors for the past six years, passed away. Ms. Jordan, a noted public figure and a former member of Congress, was Professor of Public Service at the University of Texas at the time of her death.

Capital Authorizations

On March 1, 1996, the Board of Directors of Freddie Mac authorized management to issue up to $500 million of preferred stock and repurchase up to $1 billion of common stock. The preferred stock issuance is intended to provide capital to support asset growth in attractive market environments, and the common stock repurchase authorization provides the flexibility to return capital to shareholders in periods when fewer growth opportunities are available.

It is expected that most or all of the preferred stock will be issued in one or more public offerings in 1996. Based on management's current expectations for asset growth and capital resources, relatively little of the additional common stock repurchase authority is likely to be utilized during 1996. If attractive opportunities for asset growth decrease significantly during the year, 1996 repurchases could occur at a faster rate.

EFFECT OF NEW ACCOUNTING STANDARDS

In March 1995, the Financial Accounting Standards Board (FASB) issued SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." This statement provides guidance on the carrying value of long-lived assets, including REO, and is effective January 1, 1996. Management believes that adoption of SFAS No. 121 will not have a material effect on reported results of operations or financial position.

In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation," which requires entities to measure compensation costs related to awards of stock-based compensation using either the fair value method or the intrinsic value method. Under the fair value method, compensation expense is measured at the grant date based on the fair value of the award. Under the intrinsic value method, compensation expense is equal to the excess, if any, of the quoted market price of the stock at the grant date over the amount the employee must pay to acquire the stock. Entities electing to measure compensation costs using the intrinsic value method must make pro forma disclosures, beginning after the effective date of January 1, 1996, of net income and earnings per share as if the fair value method had been applied. Freddie Mac has elected to account for stock-based compensation programs using the intrinsic value method consistent with existing accounting policies and, therefore, the standard will have no effect on the consolidated financial statements.

FIVE-YEAR FINANCIAL HIGHLIGHTS

December 31,	1995	1994	1993	1992	1991
(dollars in millions, except per share amounts)					
Balance Sheet					
Retained portfolio[1]	$107,424	$ 72,828	$ 55,698	$ 33,896	$ 27,046
Total assets	$137,181	$ 106,199	$ 83,880	$ 59,502	$ 46,860
Debt securities, net	$119,328	$ 92,053	$ 48,510	$ 28,173	$ 28,300
Total liabilities	$130,297	$ 99,368	$ 77,406	$ 53,795	$ 41,725
Capital base:					
Stockholders' equity	$ 5,863	$ 5,162	$ 4,437	$ 3,570	$ 2,566
Reserves for losses on mortgages[2]	683	733	760	785	737
Primary capital base	$ 6,546	$ 5,895	$ 5,197	$ 4,355	$ 3,303
Subordinated borrowings	633	1,226	1,483	1,458	1,962
Adjusted total capital base	$ 7,179	$ 7,121	$ 6,680	$ 5,813	$ 5,265
Mortgage Participation Certificates (PCs)	$459,045	$ 460,656	$ 439,029	$ 407,514	$ 359,163
Primary capital ratio[3]	1.10%	1.04%	0.99%	0.93%	0.81%
Adjusted total capital ratio[4]	1.20%	1.26%	1.28%	1.24%	1.30%
Total mortgage portfolio	$566,469	$ 533,484	$ 494,727	$ 441,410	$ 386,209
Mortgage Purchase and Financing Activities					
Mortgage purchases	$ 98,386	$ 124,246	$ 229,706	$ 191,126	$ 99,965
Number of mortgages purchased	933,559	1,256,549	2,315,162	1,969,851	1,061,942
Mortgage PC settlements:					
Single-class	$ 85,877	$ 117,110	$ 208,724	$ 179,207	$ 92,479
Multiclass (REMICs)	$ 15,372	$ 73,131	$ 143,336	$ 131,284	$ 72,032
Long-term debt:					
Issued	$ 29,643	$ 22,744	$ 24,784	$ 9,660	$ 4,346
Retired	(11,082)	(6,462)	(9,924)	(5,159)	(2,652)
Net	$ 18,561	$ 16,282	$ 14,860	$ 4,501	$ 1,694
Income Statement and Performance Ratios					
Net interest income on earning assets[5]	$ 1,396	$ 1,112	$ 852	$ 695	$ 683
Management and guarantee income[5]	$ 1,087	$ 1,108	$ 1,033	$ 936	$ 792
Total revenues[5]	$ 2,522	$ 2,286	$ 2,013	$ 1,687	$ 1,506
Income before income taxes	$ 1,586	$ 1,482	$ 1,128	$ 901	$ 800
Net income	$ 1,091	$ 983	$ 786	$ 622	$ 555
Earnings per common share[6]	$ 5.69	$ 5.08	$ 4.07	$ 3.29	$ 3.08
Dividends per common share[6]	$ 1.20	$ 1.04	$ 0.88	$ 0.76	$ 0.67
Dividend payout ratio on common stock	21.09%	20.47%	21.63%	23.14%	21.62%
Weighted average common shares outstanding (in thousands)[6]	180,322	180,666	180,421	180,165	180,095
Return on common equity[7]	22%	23%	22%	21%	24%
Return on stockholders' equity[8]	20%	21%	20%	20%	24%
Return on average assets and contingencies	0.19%	0.18%	0.16%	0.14%	0.15%
Ratio of earnings to fixed charges[9]	1.23:1	1.31:1	1.32:1	1.32:1	1.28:1
Ratio of earnings to combined fixed charges and preferred stock dividends[9]	1.22:1	1.30:1	1.30:1	1.30:1	N/A

(1) Prior years data have been restated to reflect the transfer of multifamily in-substance foreclosures from real estate owned to the retained portfolio pursuant to the adoption of Statement of Financial Accounting Standards No. 114 in 1995.

(2) "Reserve for losses on retained mortgages" and "Reserves for losses on sold mortgages."

(3) "Primary capital base" divided by "Total assets" and "Mortgage Participation Certificates."

(4) "Adjusted total capital base" divided by "Total assets" and "Mortgage Participation Certificates."

(5) Prior years amounts do not include pro forma adjustments to reflect the adoption in 1994 of a change in the reporting of uncollectible interest on single-family mortgages.

(6) In April 1992, Freddie Mac effected a three-for-one split of its common stock. All earnings per common share, dividends per common share and weighted average common shares outstanding have been adjusted retroactively to reflect the three-for-one stock split.

(7) "Net income" less preferred stock dividends divided by the simple average of the beginning and ending balances of "Stockholders' equity," net of par and additional paid-in capital of preferred stock.

(8) Net income divided by the simple average of the beginning and ending balances of "Stockholders' equity."

(9) Earnings represent consolidated pretax income plus consolidated fixed charges, less interest capitalized. Fixed charges include interest (including amounts capitalized) and the portion of net rental expense deemed representative of interest.

CONSOLIDATED STATEMENTS OF INCOME

Year ended December 31,	1995	1994	1993
(dollars in millions, except per share data)			
Interest income:			
Retained mortgage portfolio	$ 6,505	$ 4,528	$ 3,296
Investments and mortgage securities purchased under agreements to resell	1,888	1,287	1,127
	8,393	5,815	4,423
Interest expense on debt securities:			
Short-term notes and bonds	(2,898)	(1,644)	(858)
Long-term notes and bonds	(3,866)	(2,619)	(1,641)
	(6,764)	(4,263)	(2,499)
Interest expense due to security program cycles	(233)	(440)	(1,072)
	(6,997)	(4,703)	(3,571)
Net interest income on earning assets	1,396	1,112	852
Management and guarantee income	1,087	1,108	1,033
Other income, net	39	66	128
Total revenues	2,522	2,286	2,013
Provision for mortgage losses	(255)	(200)	(300)
REO operations expense	(286)	(225)	(224)
Administrative expenses	(395)	(379)	(361)
Total non-interest expenses	(936)	(804)	(885)
Income before income taxes, extraordinary item and cumulative effect of change in accounting principle	1,586	1,482	1,128
Provision for income taxes:			
Current	(387)	(423)	(509)
Deferred	(108)	(32)	167
Total provision for income taxes	(495)	(455)	(342)
Income before extraordinary item, net of taxes, and cumulative effect of change in accounting principle	1,091	1,027	786
Extraordinary loss on retirement of debt, net of taxes	—	(44)	(20)
Cumulative effect of change in accounting principle	—	—	20
Net income	$ 1,091	$ 983	$ 786
Preferred stock dividends	(65)	(65)	(52)
Net income available to common stockholders	$ 1,026	$ 918	$ 734
Earnings per common share	$ 5.69	$ 5.08	$ 4.07

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED BALANCE SHEETS

December 31,	1995	1994
(dollars in millions)		
Assets		
Retained mortgage portfolio	$107,424	$ 72,828
Unamortized purchase and sale premiums, discounts and fees	282	343
Reserve for losses on retained mortgages	(295)	(290)
Total mortgages, net	107,411	72,881
Cash and cash equivalents	7,483	11,442
Investments	4,745	11,895
Mortgage securities purchased under agreements to resell	9,217	5,913
Accounts receivable and other assets	6,769	2,689
Real estate owned, net	800	948
Accrued interest receivable	756	431
	$137,181	$106,199
Liabilities and Stockholders' equity		
Debt securities, net:		
Due within one year	$ 62,141	$ 47,307
Due after one year	57,187	44,746
Total debt securities, net	119,328	92,053
Accrued interest and other accrued expenses	2,078	1,358
Income taxes payable	85	72
Principal and interest due to Mortgage Participation Certificate (PC) investors	8,806	5,885
	130,297	99,368
Reserve for losses on sold mortgages	388	443
Contingencies:		
Single-class Mortgage Participation Certificates	459,045	460,656
Less-Underlying mortgages sold	(459,045)	(460,656)
	—	—
Subordinated borrowings	633	1,226
Stockholders' equity:		
Common stock, $0.84 par value, 181,500,000 shares authorized, 181,028,603 and 180,837,618 shares issued, respectively	152	152
Non-cumulative 7.90% preferred stock $1.00 par value, 30,000,000 shares authorized, 22,500,000 shares issued and outstanding	23	23
Non-cumulative 6.72% preferred stock, $1.00 par value, 12,000,000 shares authorized, issued and outstanding	12	12
Additional paid-in capital	916	913
Retained earnings	4,884	4,074
Net unrealized gain (loss) on securities reported at fair value	33	(7)
Treasury stock, at cost, 2,238,596 and 75,338 shares, respectively	(157)	(5)
Total Stockholders' equity	5,863	5,162
	$137,181	$106,199

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years ended December 31, 1995, 1994 and 1993

(dollars in millions, except per share amounts)	Common Stock	7.90% Non-cumulative Preferred Stock	6.72% Non-cumulative Preferred Stock	Additional Paid-in Capital	Retained Earnings	Net Unrealized Gain (Loss) on Securities Available for Sale, Net of Tax	Treasury Stock at Cost	Total Stockholders' Equity
Balance, December 31, 1992	$151	$23	$—	$629	$2,769	$—	$ (2)	$3,570
Net Income					786			786
Cash dividends declared:								
Common stock ($0.88 per share)					(159)			(159)
7.90% Non-cumulative preferred stock ($1.98 per share)					(44)			(44)
6.72% Non-cumulative preferred stock ($0.69 per share)					(8)			(8)
Proceeds on common and treasury stock transactions, net	1			1			(3)	(1)
Proceeds on preferred stock issuance, net			12	281				293
Balance, December 31, 1993	152	23	12	911	3,344	—	(5)	4,437
Net income					983			983
Cash dividends declared:								
Common stock ($1.04 per share)					(188)			(188)
7.90% Non-cumulative preferred stock ($1.98 per share)					(44)			(44)
6.72% Non-cumulative preferred stock ($1.68 per share)					(21)			(21)
Change in net unrealized gain (loss) on available-for-sale securities, net of tax						(7)		(7)
Proceeds on common and treasury stock transactions, net				2				2
Balance, December 31, 1994	152	23	12	913	4,074	(7)	(5)	5,162
Net income					1,091			1,091
Cash dividends declared:								
Common stock ($1.20 per share)					(216)			(216)
7.90% Non-cumulative preferred stock ($1.98 per share)					(44)			(44)
6.72% Non-cumulative preferred stock ($1.68 per share)					(21)			(21)
Change in net unrealized gain (loss) on available-for-sale securities, net of tax						40		40
Proceeds on common and treasury stock transactions, net				3			(152)	(149)
Balance, December 31, 1995	$152	$23	$ 12	$916	$4,884	$ 33	$(157)	$5,863

See accompanying Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Year ended December 31,	1995	1994	1993
(dollars in millions)			
Cash Flows from Operating Activities:			
Net income	$ 1,091	$ 983	$ 786
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Amortization of mortgage purchase and sale premiums, discounts and fees	95	167	273
Amortization of deferred debt issuance costs	71	99	86
Provision for mortgage losses	255	200	300
Provision for REO disposition losses	102	111	135
Provision (benefit) for deferred federal income taxes	108	32	(167)
Net change in payables and receivables	3,573	(32,683)	(2,028)
	4,204	(32,074)	(1,401)
Mortgages purchased for resale	(27,716)	(24,577)	(66,277)
PCs sold	24,173	41,081	77,498
	(3,543)	16,504	11,221
Net cash provided by (used in) operating activities	1,752	(14,587)	10,606
Cash Flows from Investing Activities:			
Mortgages purchased and held as investments	(41,618)	(21,850)	(32,666)
Mortgage principal repayments	5,839	2,113	5,093
Net (increase) decrease in investments	7,194	2,137	(6,007)
Mortgage securities purchased under agreements to resell	(29,847)	(27,993)	(42,225)
Repayments on mortgage securities purchased under agreements to resell	26,543	26,278	42,087
Net cash used in investing activities	(31,889)	(19,315)	(33,718)
Cash Flows from Financing Activities:			
Notes and bonds issued	29,643	22,744	24,784
Notes and bonds retired	(11,082)	(6,462)	(9,924)
	18,561	16,282	14,860
Short-term borrowings issued	835,927	707,682	474,148
Short-term borrowings retired	(827,877)	(681,585)	(469,214)
	8,050	26,097	4,934
Proceeds from stock transactions, net	(152)	2	292
Dividends paid	(281)	(253)	(211)
Net cash provided by financing activities	26,178	42,128	19,875
Net increase (decrease) in cash and cash equivalents	(3,959)	8,226	(3,237)
Cash and cash equivalents at January 1,	11,442	3,216	6,453
Cash and cash equivalents at December 31,	$ 7,483	$ 11,442	$ 3,216

Supplemental Cash Flow Information

Year ended December 31,	1995	1994	1993
(dollars in millions)			
Cash paid during the year for:			
Interest	$ 6,492	$ 4,298	$ 3,413
Taxes	376	437	460
Non-cash financing activities:			
PCs issued under Guarantor program	61,742	77,286	131,470
Giant PCs issued	19,979	37,479	41,321
Multiclass PCs issued	15,372	73,131	143,336
Transfers to real estate owned	1,206	1,517	1,170

See accompanying Notes to Consolidated Financial Statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Federal Home Loan Mortgage Corporation (Freddie Mac or the corporation) is a federally chartered and stockholder-owned corporation. The principal activity of Freddie Mac is the purchase of residential mortgages from mortgage lenders to increase the availability of funds for home ownership. Freddie Mac finances a majority of these purchases by securitizing and selling the mortgages to investors as guaranteed mortgage pass-through securities called Mortgage Participation Certificates (PCs). Mortgages financed by the issuance of PCs are referred to as the "sold portfolio." To a lesser extent, Freddie Mac finances mortgage purchases with debt, equity and other liabilities. Mortgages and mortgage-related securities held as investments are referred to as the "retained portfolio." Together, the retained and sold portfolio comprise the "total mortgage portfolio."

Freddie Mac's financial reporting and accounting policies conform to generally accepted accounting principles (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Certain prior year amounts have been reclassified to conform to current year presentation. The following is a summary of the corporation's significant accounting policies.

Consolidation

The consolidated financial statements include the accounts of the corporation and its majority-owned subsidiary, the West*Mac Associates Limited Partnership, which is the owner and developer of Freddie Mac's corporate headquarters buildings. The interests of the minority partners are immaterial in relation to the consolidated financial statements and are included in "Accrued interest and other accrued expenses." Material intercompany transactions have been eliminated in consolidation.

Mortgages

Freddie Mac classifies mortgages and mortgage-related securities as held for investment and reports them at amortized cost when it has the positive intent and ability to hold them to maturity. Mortgages that Freddie Mac does not intend to hold to maturity are classified as held for sale and are reported at the lower of cost or market value as determined based on outstanding sale commitments or current market prices for mortgages not subject to forward sale commitments. Substantially all of the mortgages held for sale at December 31, 1995 and 1994 were subject to forward sale commitments. The lower of cost or market value is calculated based on the aggregate of all mortgages held for sale. Mortgage-related securities that Freddie Mac does not have the positive intent to hold to maturity are classified as available-for-sale and are reported at fair value with unrealized gains and losses reported in Stockholders' equity on a net of tax basis.

Freddie Mac discontinues recognizing interest income on mortgages when collection of interest is doubtful. Interest income is recognized on such mortgages only to the extent cash payments are received. Effective January 1, 1994, the corporation changed the way it reports uncollectible interest on single-family mortgages to be more consistent with industry practices. Previously, accrued but uncollected interest was reflected as a charge-off against reserves for losses on mortgages. Under the current method, uncollectible interest is charged directly against interest income. As a result of the change, loss provisions, charge-offs and Net interest income on earning assets and Management and guarantee income are reduced by approximately equal amounts, with no material effect on net income. Uncollectible interest on multifamily mortgages has historically been charged against interest income. Previously reported amounts in the financial statements do not reflect the change in reporting of uncollectible interest on single-family mortgages.

On January 1, 1995, the corporation adopted Statement of Financial Accounting Standards (SFAS) No. 114, "Accounting by Creditors for Impairment of a Loan," as amended by SFAS No. 118, "Accounting by Creditors for Impairment of a Loan-Income Recognition and Disclosures." Under SFAS No. 114, loans deemed to be in-substance foreclosures are no longer transferred to real estate owned (REO), but rather continue to be carried in the mortgage portfolio until Freddie Mac obtains physical possession of the collateral, which is normally when the foreclosure process is completed. As a result, prior period mortgage and REO balances have been restated to reflect the adoption of SFAS No. 114. The adoption of SFAS No. 114 did not have a material effect on results of operations.

Securitization and Resecuritization Activity

Freddie Mac sells or issues single-class PCs representing undivided interests in primarily conventional mortgages. Because Freddie Mac guarantees payment on the mortgages underlying the PCs, the PCs are reflected as contingent liabilities. To compensate it for assuming this risk, and as compensation for administration of principal and interest payments, Freddie Mac receives fee income recorded as "Management and guarantee income" over the lives of the PCs. Freddie Mac recognizes losses currently on PC issuances and outstanding PC issuance commitments when the underlying mortgages fail to generate management and guarantee fee income sufficient to cover all anticipated expenses and probable credit losses to be incurred by Freddie Mac over the life of the securities.

Freddie Mac also issues multiclass PCs, referred to as real estate mortgage investment conduits (REMICs), representing beneficial ownership interests in specific pools of single-class PCs, mortgages or other REMICs. A majority of the fees received from issuing REMICs is recognized as "Other income, net" in the period the fees are received with the remaining portion, which is equivalent to the future costs related to managing the REMICs, being deferred and amortized over the weighted average life of the REMICs.

Unamortized Purchase and Sale Premiums, Discounts and Fees

"Unamortized purchase and sale premiums, discounts and fees" associated with acquiring mortgages and issuing single-class PCs are amortized over the estimated weighted average lives of the related mortgages using the effective interest method. Amortization of purchase premiums, discounts, and fees for retained mortgages and mortgage-related securities is included in interest income on the retained mortgage portfolio. Amortization of sale premiums, discounts and fees on PCs and purchase premiums, discounts and fees on mortgages underlying PCs is included in "Management and guarantee income."

The corporation uses actual prepayment experience and estimates of future prepayments to determine the constant yield needed to apply the effective interest method. Weighted average life estimates and associated amortization amounts are periodically revised to account for changes in actual and expected prepayment experience.

Reserves for Losses on Mortgages

Reserves for losses are maintained at levels that, in the opinion of management, are adequate to absorb credit losses incurred on mortgages in the retained and sold portfolios. These levels are estimated by management based on an evaluation of numerous factors including, but not limited to, general and regional economic conditions, prior and expected future default experience and mortgage collateral values. Reserves are increased through periodic provisions charged to expense and decreased by charge-offs, net of recoveries.

As noted above, Freddie Mac adopted SFAS No. 114 on January 1, 1995. Under SFAS No. 114, multifamily loans that will not be repaid in accordance with their contractual terms are measured for impairment based on the fair value of the collateral less estimated selling expenses. When the value of the collateral is less than the recorded investment in the loan, the impairment is recorded through a valuation allowance. This method of accounting for impairment of multifamily loans is consistent with the methods used by Freddie Mac prior to the adoption of SFAS No. 114. Single-family mortgages are excluded from the scope of the standard, with the exception of troubled debt restructurings. Single-family troubled debt restructurings are measured for impairment by discounting the estimated cash flows to be received under the restructured terms. When the present value is less than the carrying amount of the loan, the difference is recorded as a charge-off to the Reserve for losses on mortgages. Previously, losses on troubled debt restructurings were recognized to the extent the sum of estimated cash flows was less than the carrying amount of the loan. The adoption of SFAS No. 114 did not have a material effect on the results of operations.

Effective January 1, 1994, Freddie Mac changed the way it reports uncollectible interest on single-family mortgages such that uncollectible interest is no longer charged to the Reserve for losses on mortgages. See "Summary of Significant Accounting Policies — Mortgages" for further discussion of this reporting change.

Investments

At December 31, 1995 and 1994, non-mortgage investments were classified as available-for-sale since the corporation does not have the positive intent to hold these securities to maturity. Available-for-sale securities are reported at fair value with unrealized gains and losses reported in Stockholders' equity on a net of tax basis.

Real Estate Owned

REO is carried at the lower of cost or fair value less estimated selling costs. Accordingly, provisions for estimated REO disposition costs and for losses occurring subsequent to foreclosure due to changes in the fair value of the property are recognized through the REO valuation allowance with a corresponding charge to "REO operations expense." REO-related expenses and income during the holding period are also included as part of REO operations expense.

As noted previously, prior period multifamily REO and mortgage balances have been restated to reflect the adoption of SFAS No. 114, which was effective January 1, 1995. The adoption of SFAS No. 114 did not have a material effect on results of operations.

Debt Issuance Costs

Debt issuance costs are deferred and amortized over the period during which the related indebtedness is outstanding using the effective interest method.

Security Program Variances

Timing differences between Freddie Mac's receipt of principal and interest payments from seller/servicers and subsequent pass-through to PC investors results in the liability "Principal and interest due to Mortgage Participation Certificate investors" (P&I Due). P&I Due balances arising from the pass-through of prepaid mortgages are interest-bearing at the PC coupon rate from the date of prepayment until the date the PC security balance is reduced (an average of 30 days) and non-interest-bearing from the date the PC security balance is reduced to the date of payment to the PC investor (an additional 8 to 38 days depending on the type of security). Interest expense resulting from P&I Due balances is reported as "Interest expense due to security program cycles."

In 1995, the corporation revised its method of recognizing interest expense on P&I Due balances. Previously, interest expense on P&I Due balances was recognized from the date of prepayment to the date the PC security balance was reduced. Under the revised accounting method, the same dollar amount of interest expense is recognized over the period between the date of prepayment and the date of payment to the PC investor, consistent with the corresponding period during which investment income is earned on the prepayment proceeds. The change in accounting method did not have a material effect on the consolidated financial statements. Previously reported amounts in the financial statements do not reflect the change in reporting of interest expense on P&I Due balances.

Income Taxes

Effective January 1, 1993, Freddie Mac adopted SFAS No. 109, "Accounting for Income Taxes," and reported the effect of adopting the standard as a cumulative effect of a change in accounting principle in 1993. SFAS No. 109 required a change from the deferred method required by Accounting Principles Board Opinion (APB) No. 11, which the corporation used in accounting for income taxes prior to 1993, to the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized based upon the expected future tax consequences of existing differences between the financial reporting and tax reporting basis of assets and liabilities using enacted statutory tax rates. To the extent tax rates change, deferred tax assets and liabilities are adjusted in the period the tax rate change is enacted. Deferred tax expense represents the net change in the deferred tax asset or liability balance during the year. This amount, together with income taxes payable for the current year represents the total "Provision for income taxes" for the year.

Earnings Per Share

Earnings per common share are based on net income less dividends declared on "6.72% Non-cumulative preferred stock" and "7.90% Non-cumulative preferred stock," divided by the weighted average number of shares of common stock outstanding during the year. Stock options are not included in the weighted average number of shares outstanding because they do not have a material dilutive effect.

Interest-Rate Agreements and Other Hedging Instruments

Freddie Mac uses certain off-balance sheet financial instruments, primarily interest-rate swaps, caps, floors and corridors, as an "end user" with the objective of lowering the corporation's financing costs or increasing investment yields, as well as reducing the corporation's exposure to interest-rate risk. When these instruments meet specific criteria, they are accounted for as hedges on either a deferral or an accrual basis, depending upon the nature of the hedge strategy.

Interest-rate agreements — The net differential received or paid under interest-rate agreements is recognized as an adjustment to interest income or expense on the associated assets or liabilities on an accrual basis. Net premiums paid for interest-rate agreements are included in "Accounts receivable and other assets" and are amortized to interest income or expense over the terms of the agreements. Gains and losses on terminated interest-rate agreements are deferred over the remaining lives of the hedged items. As of December 31, 1995 and 1994, the unamortized balance of deferred gains and losses was not material to the consolidated financial statements.

Other hedging instruments — To hedge against fluctuations in interest rates that may affect the cost of certain debt issuances, the corporation enters into short sales of Treasury securities and spread-lock agreements. Gains and losses resulting from these transactions that are designated and perform effectively as hedges are deferred and amortized as adjustments to interest expense over the lives of the hedged borrowings. Gains and losses resulting from transactions that do not perform effectively as hedges are recognized currently. As of December 31, 1995 and 1994, the unamortized balance of deferred gains and losses was not material to the consolidated financial statements.

Consolidated Statements of Cash Flows

For purposes of reporting cash flows, Freddie Mac considers federal funds and highly liquid investment securities with original maturities of three months or less to be cash equivalents. Freddie Mac's Consolidated Statements of Cash Flows are prepared using the indirect method of presentation.

Freddie Mac enters into non-cash transactions involving the securitization of mortgages, resecuritization of existing PCs and foreclosure on defaulted mortgages. Non-cash mortgage securitization and PC resecuritization transactions include: (1) the exchange of mortgages with a seller for a like amount of PCs, backed by the identical mortgages (Guarantor Program); (2) the exchange of existing Freddie Mac PCs with a seller for an interest in a Freddie Mac PC, backed by a group of PCs exchanged under the program (Giant PC Program); and (3) the exchange of existing single-class PCs with a seller for a like amount of multiclass PCs, backed by the identical single-class PCs.

New Accounting Pronouncements

In March 1995, the Financial Accounting Standards Board (FASB) issued SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of." This standard provides guidance on the carrying value of long lived assets, including REO, and is effective January 1, 1996. Management believes that adopting the new standard will not have a material effect on the consolidated financial statements.

In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation," which requires entities to measure compensation costs related to awards of stock-based compensation using either the fair value method or the intrinsic value method. Under the fair value method, compensation expense is measured at the grant date based on the fair value of the award. Under the intrinsic value method, compensation expense is equal to the excess, if any, of the quoted market price of the stock at the grant date over the amount the employee must pay to acquire the stock. Entities electing to measure compensation costs using the intrinsic value method must make pro forma disclosures, beginning after the effective date of January 1, 1996, of net income and earnings per share as if the fair value method had been applied. Freddie Mac has elected to account for stock-based compensation programs using the intrinsic value method consistent with existing accounting policies and, therefore, the standard will have no effect on the consolidated financial statements.

2. MORTGAGES

The following is a summary of the components of the retained mortgage portfolio.

December 31,	1995	1994
(dollars in millions)		
Single-family:		
30-year fixed-rate[1]	$ 71,653	$44,633
15-year fixed-rate	15,692	16,609
Balloon/resets	5,585	6,157
Adjustable-rate	10,642	2,464
Multifamily	3,852	2,965
Total	$107,424	$72,828

(1) Includes 20-year fixed-rate mortgages, second mortgages and mobile home loans.

At December 31, 1995 and 1994, the retained mortgage portfolio included $1.2 billion and $0.4 billion, respectively, of mortgages held for sale. The market value of mortgages held for sale at December 31, 1995 and 1994 approximated their carrying value.

The retained mortgage portfolio also includes Freddie Mac PCs, REMICs and other mortgage-related securities. These mortgage-related securities have been classified in the table above based on the underlying mortgages. The estimated fair value and corresponding gross unrealized gains and losses of mortgage-related securities held in the retained mortgage portfolio are summarized in the table on the following page. No available-for-sale securities were sold during 1995.

December 31,	1995				1994			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(dollars in millions)								
Held to maturity	$57,678	$1,935	$ –	$59,613	$31,316	$28	$(2,090)	$29,254
Available-for-sale	5,848	190	(148)	5,890	–	–	–	–
Total	$63,526	$2,125	$(148)	$65,503	$31,316	$28	$(2,090)	$29,254

In November 1995, the FASB issued "A Guide to Implementation of Statement 115 on Accounting for Certain Investments in Debt and Equity Securities." Freddie Mac implemented the report on December 31, 1995, and in doing so transferred $6 billion of mortgage-related securities from held to maturity to available-for-sale which resulted in a $27 million unrealized gain, net of tax, being recorded to Stockholders' equity.

3. RESERVES FOR LOSSES ON MORTGAGES

Freddie Mac maintains reserves to provide for credit losses on the retained and sold mortgage portfolios. The following is a combined analysis of these reserves for losses on mortgages for the years ended December 31, 1995, 1994 and 1993.

	1995	1994	1993
(dollars in millions)			
Beginning balance	$ 733	$ 760	$ 785
Provision	255	200	300
Charge-offs, net	(305)	(227)	(325)
Ending balance	$ 683	$ 733	$ 760

At December 31, 1995, the reserve balance consisted of a general reserve available to absorb losses on the total mortgage portfolio and a specific valuation allowance related to impaired loans pursuant to SFAS No. 114, as discussed in Note 1. At December 31, 1995, the corporation's recorded investment in impaired loans and the related valuation allowance were as follows:

	Recorded Investment	Valuation Allowance	Net Investment
(dollars in millions)			
Impaired loans for which:			
Valuation allowance required	$449	$(67)	$382
No valuation allowance required	453	–	453
Total	$902	$(67)	$835

For the year ended December 31, 1995, the average recorded investment in impaired loans was $938 million and the related interest income recognized was $74 million.

4. INVESTMENTS

Presented below are the amortized cost and estimated market values of non-mortgage investments at December 31, 1995 and 1994. Estimated fair values and corresponding gross unrealized gains and losses in the following table include the effect of interest-rate agreements which, when linked to specific investments, enable the corporation to achieve a specific investment objective at a desired yield (see Note 10).

December 31,	1995				1994			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
(dollars in millions)								
Federal Funds	$ 105	$ –	$ –	$ 105	$ 5,533	$ –	$ –	$ 5,533
Eurodollar time deposits	5	–	–	5	1,727	–	–	1,727
Obligations of states and municipalities	1,040	6	(3)	1,043	1,715	3	(10)	1,708
Auction rate preferred stock	446	–	–	446	1,064	–	–	1,064
Medium-term notes	1,196	16	(11)	1,201	1,237	12	(15)	1,234
Other securities	1,943	14	(12)	1,945	630	9	(10)	629
Total	$4,735	$36	$(26)	$4,745	$11,906	$24	$(35)	$11,895

At December 31, 1995 and 1994, all investments were classified as available-for-sale. Included in Stockholders' equity at December 31, 1995 and 1994 were net unrealized gains (losses) on available-for-sale non-mortgage investments, net of tax, totaling $6 million and $(7) million, respectively. Sales of investment securities were immaterial in 1995, 1994 and 1993.

The remaining contractual maturities of investments at December 31, 1995 and 1994 were as follows:

Remaining maturity at December 31,	1995		1994	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
(dollars in millions)				
Due within one year	$3,849	$3,853	$11,246	$11,238
Due after one year through five years	886	892	660	657
Total	$4,735	$4,745	$11,906	$11,895

5. MORTGAGE SECURITIES PURCHASED UNDER AGREEMENTS TO RESELL

Mortgage securities purchased under agreements to resell (reverse repurchase agreements) are collateralized lending transactions in which Freddie Mac purchases PCs with an agreement to sell back the exact same security. The following table provides information regarding the balances of reverse repurchase agreements in 1995 and 1994.

	1995	1994
(dollars in millions)		
Average outstanding during the year	$ 7,398	$7,531
Maximum month-end outstanding balance	13,584	8,163
Due within one year	$ 8,139	$5,861
Due after one year through five years	1,078	52
Balance, December 31	$ 9,217	$5,913

The amount a customer can borrow under a reverse repurchase agreement is limited to approximately 97 percent of the market value of the securities collateralizing the agreement, depending on the type of collateral and/or the credit quality of the customer. The master agreements governing reverse repurchase agreement transactions provide for the delivery of securities collateralizing the agreements to Freddie Mac (or its custodian bank) and provide that Freddie Mac has the right to sell the collateral in the event of a borrower default. All reverse repurchase agreements permit Freddie Mac to obtain additional collateral as margin if the market value of the securities subject to the reverse repurchase agreement declines.

6. REAL ESTATE OWNED

The following table provides an analysis of Freddie Mac's REO activity for the years ended December 31, 1995, 1994 and 1993.

	REO, Gross	Valuation Allowance	REO, Net
(dollars in millions)			
Balance, December 31, 1992	$ 537	$ (5)	$ 532
Additions	1,170	(116)	1,054
Dispositions and write downs	(844)	29	(815)
Balance, December 31, 1993	863	(92)	771
Additions	1,517	(102)	1,415
Dispositions and write downs	(1,348)	110	(1,238)
Balance, December 31, 1994	1,032	(84)	948
Additions	1,206	(102)	1,104
Dispositions and write downs	(1,357)	105	(1,252)
Balance, December 31, 1995	$ 881	$ (81)	$ 800

7. NOTES AND BONDS PAYABLE

The following tables do not include the effect of interest-rate agreements (see Note 10). Notes and bonds payable consists of the following:

December 31,	1995		1994	
	Balance, Net[1]	Effective Rate[2]	Balance, Net[1]	Effective Rate[2]
(dollars in millions)				
Due within one year:				
Discount notes, mortgage securities sold under agreements to repurchase and medium-term notes	$ 51,458	5.65%	$43,408	5.80%
Current portion of long-term debt	10,683	5.68	3,899	5.85
Total due within one year	62,141	5.66	47,307	5.80
Due after one year (maturing between 1997 – 2022)	57,187	6.74	44,746	6.41
Total	$119,328		$92,053	

(1) Net of unamortized discounts or premiums, hedging gains or losses and debt issuance costs totaling $111 million and $63 million at December 31, 1995 and 1994, respectively.

(2) Represents the weighted average effective rate at the end of the period, and includes the amortization of discounts, premiums, hedging gains or losses and debt issuance costs.

The following table provides additional information related to amounts due within one year.

	1995				1994			
	Balance, Net	Average Balance Outstanding During the Year	Effective Rate	Maximum Balance Outstanding at Any Month End	Balance, Net	Average Balance Outstanding During the Year	Effective Rate	Maximum Balance Outstanding at Any Month End
(dollars in millions)								
Discount notes	$49,024	$45,491	5.89%	$49,024	$42,989	$33,280	4.36%	$42,989
Mortgage securities sold under agreements to repurchase	–	11	–	106	19	520	2.34	2,260
Medium-term notes	2,434	2,000	6.49	2,501	400	918	2.92	1,265

Mortgage securities sold under agreements to repurchase are collateralized borrowing transactions in which Freddie Mac sells PCs with an agreement to repurchase PCs that are substantially the same. These agreements require the underlying PCs to be delivered to the dealers who arranged the transactions. At December 31, 1994, the book value, including accrued interest, of the PCs underlying the agreements was $20 million. The market values of these PCs approximated their book value.

A significant portion of Freddie Mac's long-term debt is callable. Callable debt gives Freddie Mac the option to redeem the debt security in whole or in part at anytime on or after a specified date. The following table summarizes the amounts, average interest rates and call periods of callable debt as of December 31, 1995.

Call Period Inception Date	Maturity	Balance, Net of Discount	Effective Rate
(dollars in millions)			
1996	1996–2010	$29,185	6.04%
1997	1998–2007	8,960	7.29
1998	2000–2008	8,744	7.21
1999	2002–2009	3,248	7.54
2000	2005–2010	2,060	7.24
2001	2010	25	8.35
Total		$52,222	6.59%

The following table summarizes the principal amounts, net, at December 31, 1995 of short- and long-term notes and bonds payable and subordinated borrowings (see Note 8) scheduled to mature in the years 1996-2005 and thereafter, assuming callable debt is (1) paid at scheduled maturity, and (2) is redeemed at the initial call date.

	Scheduled Maturity	Assuming Callable Debt is Redeemed at Initial Call Date
(dollars in millions)		
1996	$ 59,647	$ 85,107
1997	6,442	11,856
1998	11,055	10,258
1999	7,123	5,707
2000	10,083	4,163
2001	2,009	570
2002	3,005	216
2003	4,263	534
2004	5,891	134
2005	7,716	668
Thereafter	2,727	748
Total	$119,961	$119,961

8. SUBORDINATED BORROWINGS

Subordinated borrowings consist of the following:

December 31,		1995		1994	
	Maturity	Balance	Effective Rate[1]	Balance	Effective Rate[1]
(dollars in millions)					
Capital debentures	1995	$ –	–%	$ 225	10.95%
	1996	150	10.27	150	10.27
	2000	–	–	400	9.22
	2016	200	8.40	200	8.40
		350		975	
Unamortized discounts and fees		(8)		(13)	
		342		962	
Zero coupon capital debentures	2019	3,178	10.26	3,178	10.26
Unamortized discounts and fees		(2,887)		(2,914)	
		291		264	
Total subordinated borrowings		$ 633		$ 1,226	

(1) Represents the weighted average effective rate at the end of the period, and includes the amortization of discounts, premiums, hedging gains or losses and debt issuance costs.

The capital debentures and zero coupon capital debentures are subordinated to all obligations and liabilities of Freddie Mac, including obligations of others that Freddie Mac has guaranteed, whether existing at the date of issuance or thereafter incurred or created. The zero coupon capital debentures rank equally with the capital debentures.

In 1994, the corporation extinguished $68 million ($887 million face value and 10.26% average rate) of zero coupon capital debentures. As a result, Freddie Mac recorded extraordinary losses of $67 million ($44 million after taxes, or $0.24 per common share) in 1994.

9. STOCKHOLDERS' EQUITY

Non-cumulative, Fixed-Rate Preferred Stock

Freddie Mac issued 22.5 million shares of 7.90 percent preferred stock on April 27, 1992 and 12.0 million shares of 6.72 percent preferred stock on August 2, 1993. Both the 7.90 percent and 6.72 percent non-cumulative fixed-rate preferred stocks are redeemable at the corporation's option at any time after five years from the date of issuance at $25 per share plus accrued dividends. Both classes of preferred stock carry a liquidation value of $25 per share plus accrued dividends and no significant voting rights or rights to purchase other Freddie Mac stock or securities.

Employee Stock Purchase Plan

Freddie Mac has established an Employee Stock Purchase Plan (ESPP) under which up to 3.0 million shares of common stock may be issued to qualified employees. In 1995, employees pledged to purchase 247,073 shares on July 31, 1996. The purchase price under the ESPP will be equal to 85 percent of the fair market value of the stock on July 1, 1995 or July 31, 1996, whichever is lower. Employees purchased 190,985 shares and 194,615 shares for the years ended December 31, 1995 and December 31, 1994, respectively, under the ESPP. The ESPP qualifies as an "employee stock purchase plan" under Section 423 of the Internal Revenue Code of 1986, as amended. No shares may be issued under the current ESPP after December 31, 2004.

Stock Compensation Plan

Under Freddie Mac's 1995 Stock Compensation Plan (the Stock Plan), the corporation is permitted to grant stock options (with or without dividend rights), restricted stock, stock appreciation rights (SARs) and various other performance awards that are based on or related to common stock to employees. To date, no SARs or performance awards have been granted. The corporation has the right to impose performance conditions with respect to any awards to employees under the Stock Plan. The maximum number of shares of common stock which may be granted to employees under the Stock Plan is 8.4 million shares.

Freddie Mac has also established a Directors' Stock Compensation Plan (the Directors' Plan). Under the Directors' Plan, the corporation is permitted to grant stock options and restricted stock to members of the Board of Directors who are non-employees. The maximum number of shares of common stock which may be granted under the Directors' Plan is 600,000 shares.

At December 31, 1995, 4,842,234 shares remained available for grant under the 1995 Stock Plan and the Directors' Plan. The common stock delivered under these plans may be shares held in Freddie Mac's treasury, authorized but previously unissued shares, or shares purchased by Freddie Mac on the open market. No awards may be made under these plans after December 31, 2004.

Stock options allow for the purchase of Freddie Mac's common stock at a price equal to the fair market value on the grant date. Because the option price is equal to the fair market value on the grant date, the options do not result in compensation expense. Options may be exercised for a period of 10 years from the grant date, subject to a vesting schedule generally commencing one year from the grant date. The following is a summary of the status of stock options.

	Available for Exercise	Outstanding	Price Per Share
December 31, 1992	630,401	2,244,552	$14.10 – $45.81
Granted		476,740	49.06 – 51.44
Exercised		(232,839)	14.10 – 40.69
Canceled		(78,425)	20.19 – 49.06
December 31, 1993	1,083,988	2,410,028	14.10 – 51.44
Granted		509,660	50.94 – 60.44
Exercised		(307,194)	14.10 – 53.44
Canceled		(131,240)	27.83 – 60.38
December 31, 1994	1,359,353	2,481,254	14.10 – 60.44
Granted		539,730	58.69 – 77.75
Exercised		(230,782)	16.29 – 60.38
Canceled		(47,467)	39.06 – 68.13
December 31, 1995	1,391,153	2,742,735	$24.96 – $77.75

Dividend rights provide participants the right to receive, at the time stock options are exercised, an amount equal to dividends paid on the stock from the date the options were granted. Compensation expense related to dividend rights charged to operations in 1995, 1994, and 1993 was $3.0 million, $2.4 million, and $2.0 million, respectively.

Restricted stock entitles participants to all the rights of a stockholder, except that the shares awarded are subject to a risk of forfeiture and may not be disposed of by the participant until the end of the restriction period established by the corporation. The value of shares awarded is amortized to compensation expense over the restricted or vesting period. Compensation expense charged to operations was $2.2 million, $1.8 million, and $1.7 million in 1995, 1994, and 1993, respectively. During 1995, 43,480 shares of restricted stock were granted. At December 31, 1995, 129,416 shares of restricted stock remained outstanding.

Regulatory Capital

The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (the GSE Act) established risk-based and minimum capital standards for Freddie Mac. The risk-based capital standard will require Freddie Mac to maintain an amount of "total capital" sufficient for the corporation to maintain positive total capital for a ten-year period under highly stressful economic scenarios. Total capital includes "core capital" and general reserves for mortgage and foreclosure losses and certain other amounts available to absorb losses. Core capital consists of the par or stated values of outstanding common and perpetual preferred stock, paid-in capital and retained earnings, measured under GAAP.

The minimum capital standard is an amount of core capital equal to the sum of 2.50 percent of aggregate on-balance sheet assets, measured under GAAP, 0.225 percent of its average mortgage purchase commitments and, generally, 0.45 percent of its other aggregate off-balance sheet obligations, including the aggregate unpaid principal balance of the corporation's PCs.

As of December 31, 1995, Freddie Mac's core capital amounted to approximately $5.8 billion, which exceeded the minimum capital requirement under the GSE Act. Freddie Mac believes that a reasonable interpretation of the risk-based capital standard would not require the corporation to substantially increase its capitalization, and that the corporation has adequate access to the capital markets to raise any necessary additional capital.

10. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK AND CONCENTRATIONS OF CREDIT RISK

Financial Instruments with Off-Balance Sheet Risk

In the normal course of business the corporation is a party to transactions involving financial instruments with off-balance sheet risk. These financial instruments include PCs, commitments to purchase mortgages, commitments to sell PCs, and interest-rate agreements and other hedging instruments. These instruments expose the corporation to credit risk and market risk in excess of the amounts reported in the balance sheet. The following summarizes financial instruments with off-balance sheet risk at December 31, 1995 and 1994.

December 31,	1995	1994
(dollars in millions)		
Financial instruments whose contractual amounts represent credit risk:		
Guaranteed PCs[1]	$459,045	$460,656
Commitments to purchase mortgages	32,730	40,256
Financial instruments whose notional or contractual amounts exceed the amount of credit risk:		
Commitments to sell PCs	1,659	652
Interest-rate agreements and other hedging instruments	58,463	30,837

(1) Excludes $12.4 billion and $14.1 billion at December 31, 1995 and 1994, respectively, of Freddie Mac REMIC securities collateralized by Government National Mortgage Association (GNMA) securities. Also excludes $56.0 billion and $30.7 billion at December 31, 1995 and 1994, respectively, of PCs held in the retained mortgage portfolio.

Guaranteed Mortgage Participation Certificates

Freddie Mac guarantees to PC holders the timely payment of interest at the PC coupon rate, and the timely payment of principal on mortgages underlying Gold PCs or the ultimate payment of principal on mortgages underlying 75-day PCs. Several types of credit risk are associated with the issuance and guarantee of PCs. These include the risk of loss from: (1) borrower default on the mortgage; (2) the failure of institutions holding monthly remittances payable to Freddie Mac; and (3) mortgage fraud. These credit risks are mitigated through Freddie Mac's uniform underwriting and servicing criteria and warranties obtained from sellers. Freddie Mac also requires collateral in the form of security interests in the underlying real estate supporting the mortgages backing the PCs, as well as mortgage insurance for mortgages exceeding certain loan-to-value (LTV) ratios. Certain transactions may also include other forms of credit enhancement provided by the seller. Management continually monitors the corporation's credit exposure and provides for probable losses incurred through the "Reserve for losses on sold mortgages." As of December 31, 1995 and 1994, this reserve stood at $388 million and $443 million, respectively (see Note 3).

As part of administering its PC programs, Freddie Mac is required to repurchase the mortgages backing PCs when certain events occur. Specifically, Freddie Mac may be required under certain conditions to repurchase balloon/reset mortgages, convertible adjustable-rate mortgages (CARMs), and mortgages in default. Under the balloon/reset and the CARM programs, the mortgagor has the option, if certain conditions are met, to reset or convert the mortgage to a market-based fixed-rate mortgage. If the mortgagor elects to reset or convert the mortgage rate, Freddie Mac is obligated to repurchase the mortgage from the security pool and may either place the mortgage in its retained portfolio or securitize and sell the mortgage as part of a pool underlying a new PC. Freddie Mac is also required to repurchase mortgages collateralizing PCs when the mortgages are deemed to be in default as defined in the security offering documents.

Commitments

Freddie Mac can incur market risk — the risk of adverse interest-rate movements — between the time it commits to purchase mortgages under the Cash Program and the time it finances those purchases either by issuing PCs collateralized by mortgages purchased under the Cash Program or by issuing debt. Freddie Mac manages market risk under the Cash Program by committing to issue PCs at substantially the same time it commits to purchase mortgages similar to the Guarantor Program. Issuing PCs under the Guarantor Program does not expose the corporation to market risk because the purchase of mortgages and issuance of PCs occur simultaneously. Market risk related to financing mortgage purchases with debt is mitigated through the use of hedging instruments as discussed in "Interest-Rate Agreements and Other Hedging Instruments."

At the time a commitment to purchase is entered into, Freddie Mac is subject to credit risk similar to that of its PC programs (see above). In addition, Freddie Mac is exposed to a loss if a party to a mandatory purchase commitment fails to deliver mortgages which Freddie Mac has committed to sell as PCs under a mandatory delivery agreement. The loss in such an event is equal to the change in market value of the mortgages to be delivered to Freddie Mac, and is offset by the pair-off fee payable to Freddie Mac by the mortgage seller. The maximum delivery period for mandatory purchase commitments is 90 days for fixed rate mortgages and 105 days for adjustable-rate mortgages (ARMs). If a party fails to deliver mortgages under a mandatory purchase commitment, the corporation fulfills its mandatory sale commitments with retained mortgages held for sale.

The following table summarizes Freddie Mac's outstanding commitments to purchase mortgages.

December 31,	**1995**	**1994**
(dollars in millions)		
Commitments to Purchase:		
Cash Program		
Mandatory	$ 827	$ 297
Optional	1	1
Guarantor Program		
Mandatory	36	1,050
Optional	445	213
Master Commitments		
Mandatory	20,445	30,141
Optional	10,976	8,554

Under the optional commitment programs, lenders may or may not exercise their commitment option. Under the mandatory programs, the lender may buy back the commitment at any time by paying a pair-off fee. A master commitment is a contract between Freddie Mac and a mortgage lender which sets forth the terms and conditions under which Freddie Mac will purchase mortgages from approved seller/servicers. A master commitment may provide for the purchase of mortgages under one or more purchase programs with various product attributes, e.g., conventional fixed-rate or conventional ARMs.

Interest-Rate Agreements and Other Hedging Instruments

The corporation enters into interest-rate swaps, caps, floors and corridors and, to a lesser extent, short sales of Treasury securities and spread-lock agreements to lower financing costs or increase investment yields and to hedge against fluctuations in interest rates. The corporation is an "end user" and does not use these instruments to generate trading profits or for speculative purposes. All of the corporation's interest-rate agreements are currently U.S. dollar denominated. In addition, the corporation is not a party to leveraged hedging instruments. The table on the following page summarizes the notional or contractual amounts of these instruments and their related fair values.

	1995			
	Notional or contractual amount at year end	Average notional or contractual amount outstanding during year	Gross positive fair values	Gross negative fair values
(dollars in millions)				
Debt-linked swaps	$37,277	$28,505	$219	$(710)
Asset-linked swaps	7,107	4,361	5	(114)
Interest-rate swaps	1,000	1,468	2	(2)
Interest-rate caps	4,448	3,804	53	–
Interest-rate floors	6,078	5,413	45	(16)
Interest-rate corridors	2,529	2,485	40	(13)
Short sales of Treasury securities and spread-lock agreements	24	51	–	–
Total	$58,463	$46,087	$364	$(855)

	1994			
	Notional or contractual amount at year end	Average notional or contractual amount outstanding during year	Gross positive fair values	Gross negative fair values
(dollars in millions)				
Debt-linked swaps	$17,333	$14,521	$712	$(138)
Asset-linked swaps	1,661	814	20	(9)
Interest-rate swaps	2,840	3,157	9	(33)
Interest-rate caps	3,145	1,762	227	–
Interest-rate floors	4,950	4,110	3	–
Interest-rate corridors	908	134	51	(14)
Short sales of Treasury securities and spread-lock agreements	–	153	–	–
Total	$30,837	$24,651	$1,022	$(194)

Interest-rate swaps — Interest-rate swaps are contractual agreements between two parties for the exchange of periodic payments based on a notional principal amount and agreed-upon fixed and variable rates. The majority of Freddie Mac's interest-rate swap agreements are executed in conjunction with debt issuances (debt-linked swaps) or asset purchases (asset-linked swaps). These swaps, when combined with the underlying liability or asset, synthetically create debt and asset yields that produce lower effective debt costs or higher effective asset yields than those available on direct debt issuances or asset purchases. To a lesser extent, the corporation is also a party to interest-rate swaps that stabilize the effective costs or yields on short-term debt and investment transactions related to the monthly mortgage and security payment remittance cycle.

Interest-rate caps and floors — Interest-rate caps and floors are agreements in which one party makes a one-time up-front premium payment to another party in exchange for the right to receive interest payments based on a particular notional amount and the difference between the agreed-upon index rate over a specified "cap" or "floor" strike rate. Interest-rate caps and floors can be structured as corridors. A corridor combines a purchased and sold interest-rate cap or floor to effectively reduce the cost of the interest-rate cap or floor protection. Currently, all of the interest-rate corridors entered into by Freddie Mac involve interest-rate caps.

Similar to debt- and asset-linked swaps, interest-rate caps and floors produce lower effective debt costs and higher investment yields when combined with short-term debt issuances and investments by limiting the impact of interest rate changes on these instruments.

Short sales of Treasury securities and spread-lock agreements — Short sales of Treasury securities represent obligations to deliver, at a future date, securities that have not yet been purchased. Spread-lock agreements are agreements that duplicate the effect of purchases of Treasury securities but do not actually involve the purchase of Treasury securities. Both short sales of Treasury securities and spread-lock agreements are used to hedge against the effects of changes in interest rates on the cost of debt used to finance retained mortgages.

Notional amounts serve as a factor in determining periodic interest amounts to be received and paid and do not themselves represent actual amounts to be exchanged. Although the notional amounts of hedging instruments may be indicative of the extent to which the corporation uses these financial instruments in managing its interest-rate risk exposure, they do not directly represent the corporation's exposure to credit and market risks.

Failure of a counterparty to perform under the terms of a hedging instrument exposes the corporation to credit risk. The corporation reduces counterparty risk by dealing only with institutions that meet certain credit guidelines, requiring collateral in certain circumstances and continuously

monitoring credit risk exposure. The corporation's policy for requiring collateral from counterparties in interest-rate agreements is based on independent credit ratings, estimated credit loss exposure on net gain positions and internal assessments of counterparty credit quality. Freddie Mac has not set aside specific reserves for counterparty credit exposure and does not believe such reserves are necessary at this time based on the corporation's collateral and counterparty policy requirements.

The exposure to credit losses on hedging instruments can be estimated by calculating the cost to replace at current market values all hedging instruments outstanding with each counterparty for which the corporation was in a net gain position. The corporation's estimate of the exposure to credit losses for hedging instruments in a net gain position was $27 million at December 31, 1995. Collateral supporting the corporation's net gain position at December 31, 1995 had an estimated aggregate market value of $3 million. Substantially all of the corporation's uncollateralized net gain position of $24 million at December 31, 1995 resulted from positions taken with counterparties having among the highest credit ratings available from major rating agencies. Although hedging instruments are utilized to reduce the corporation's exposure to interest-rate risk, Freddie Mac's exposure to credit risk can fluctuate from period to period due to changes in interest-rates.

At December 31, 1995, receivable and payable amounts resulting from hedging transactions totaled $534 million and $610 million, respectively.

Concentrations of Credit Risk

The following tables summarize the total mortgage portfolio by geographical distribution and mortgage product type. Excluded from the total mortgage portfolio at December 31, 1995 and 1994 are $7.1 billion and $0.8 billion, respectively, of GNMA mortgage securities since these securities do not represent a credit risk to the corporation.

December 31,	1995		1994	
By Region[1]	**Amount**	**Percentage**	**Amount**	**Percentage**
(dollars in millions)				
West	$186,664	33.37%	$180,463	33.88%
Northeast	148,026	26.46	146,054	27.42
North Central	99,822	17.85	92,608	17.38
Southeast	70,919	12.68	64,942	12.19
Southwest	53,932	9.64	48,630	9.13
	$559,363	100.00%	$532,697	100.00%
By State				
California	$136,610	24.42%	$135,645	25.46%
New York	32,163	5.75	31,891	5.99
Illinois	27,510	4.92	26,444	4.97
Florida	23,791	4.25	22,553	4.23
New Jersey	23,782	4.25	23,659	4.44
All others	315,507	56.41	292,505	54.91
	$559,363	100.00%	$532,697	100.00%

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

December 31,	1995		1994	
By Product Type	**Amount**	**Percentage**	**Amount**	**Percentage**
(dollars in millions)				
Single Family:				
30-year fixed-rate[1]	$318,003	56.85%	$288,350	54.13%
15-year fixed-rate	128,443	22.96	130,701	24.53
ARMs	61,472	10.99	59,544	11.18
Balloon/Resets	44,780	8.01	47,805	8.98
Multifamily	6,665	1.19	6,297	1.18
	$559,363	100.00%	$532,697	100.00%

(1) Includes 20-year fixed-rate mortgages, second mortgages and mobile home loans.

11. INCOME TAXES

The components of the "Provision for income taxes" consist of the following:

Year Ended December 31,	1995	1994	1993
(dollars in millions)			
Current tax provision	$387	$423	$ 509
Deferred tax provision (benefit):			
Amortization of debt discounts and issuance costs	16	14	26
Amortization of mortgage purchase and sale premiums, discounts and fees	15	(55)	(96)
Provision for mortgage and REO losses in excess of deductions	46	32	(24)
Amortization of deferred hedging gains and losses	(11)	(4)	(12)
Capitalization of development costs	(5)	(5)	(13)
Other items, net	47	50	(48)
Total deferred tax provision (benefit)	108	32	(167)
Total provision for income taxes	$495	$455	$ 342

Deferred tax assets and liabilities reflect the tax effect of temporary differences between the amounts of assets and liabilities for financial reporting purposes and the tax basis of those assets and liabilities. The net deferred tax asset is included in "Accounts receivable and other assets." Management believes that it is more likely than not that the total deferred tax asset will be realized in future periods. The table on the following page summarizes the composition of the deferred tax asset and liability as of December 31, 1995 and 1994.

December 31,	1995	1994
(dollars in millions)		
Deferred tax assets:		
Unamortized purchase and sale premiums, discounts and fees	$ 478	$ 537
Reserve for losses on mortgages	732	823
Accrued interest and other accrued expenses	182	150
Other	19	–
Total deferred tax asset	1,411	1,510
Deferred tax liabilities:		
Accounts receivable and other assets	110	91
Real estate owned, net	589	475
Multiclass debt securities	108	130
Other	–	83
Total deferred tax liability	807	779
Net deferred tax asset	$ 604	$ 731

The Omnibus Budget Reconciliation Act (OBRA), which became law on August 10, 1993, increased the maximum federal tax rate for corporations from 34 percent to 35 percent, effective January 1, 1993. The remeasurement of the net deferred tax asset at the higher tax rate resulted in a $17 million benefit, while the taxes associated with 1993 earnings were $11 million higher. Thus, the adoption of OBRA resulted in a $6 million net decrease in the 1993 "Provision for income taxes."

The following table reconciles the expected federal statutory tax provision to the effective provision for income taxes.

Year Ended December 31,	1995	1994	1993
(dollars in millions)			
Provision for income taxes at the statutory rate	$555	$519	$395
Tax-exempt interest and dividends received deductions	(36)	(33)	(24)
Tax credits	(24)	(15)	(12)
Reduction in reserve for contingent taxes	–	(16)	–
Remeasurement of the net deferred tax asset due to OBRA	–	–	(17)
Total provision for income taxes	$495	$455	$342
Statutory tax rate	35.0%	35.0%	35.0%
Effective tax rate	31.2%	30.7%	30.3%

Freddie Mac is exempt from state and local taxes, with the exception of real estate taxes.

In March 1994, the corporation received from the Internal Revenue Service (IRS) a Revenue Agent Report for its 1985 and 1986 federal income tax returns. In anticipation that this report would assert a deficiency, management had previously established reserves for additional taxes and related interest. Positions taken by the IRS resolved several open issues, including hedging issues that were treated in a manner consistent with regulations issued by the IRS in October 1993. The resolution of these issues allowed the corporation to reduce its existing reserves for contingent taxes and thus report a one-time reduction in its 1994 provision for income taxes of $16 million and also to reduce its reserves for related contingent interest.

During 1994, the IRS completed its examination of Freddie Mac's federal income tax returns for the years 1987 and 1988 and began its examination of the years 1989 and 1990. In the opinion of management, adequate provision has been made for all income taxes and related interest. Management believes that additional tax liability, if any, that may arise for prior periods as a result of IRS adjustments will not have a material adverse impact on Freddie Mac's consolidated financial statements.

12. EMPLOYEE BENEFITS

Freddie Mac maintains a defined benefit pension plan (the Plan) covering substantially all of its employees. Benefits are based on years of service and the employee's highest compensation over any three consecutive years of employment. It is Freddie Mac's policy to contribute the maximum amount deductible for federal income tax purposes each year. Plan assets consist primarily of corporate bonds and listed stocks.

In addition to the Plan, Freddie Mac maintains nonqualified, unfunded defined benefit pension plans for officers of the corporation. The related retirement benefits are paid from Freddie Mac's assets.

Consolidated net periodic pension costs related to defined benefit pension plans consisted of the following:

Year Ended December 31,	1995	1994	1993
(dollars in thousands)			
Service cost of current period	$ 5,201	$ 6,370	$ 4,662
Interest on projected benefit obligation	5,276	5,204	4,749
Actual return on plan assets	(16,718)	780	(4,837)
Net amortization and deferral	12,255	(4,465)	1,785
Net periodic pension cost	$ 6,014	$ 7,889	$ 6,359

Freddie Mac calculates pension costs using assumptions as of the beginning of the year and calculates the funded status of the plans using assumptions as of the end of the year. The following table sets forth the funded status, the assumptions used to calculate the funded status and amounts recognized in Freddie Mac's Consolidated Balance Sheets.

December 31,	1995	1994
(dollars in thousands)		
Actuarial present value of benefit obligations:		
Vested benefits	$ 52,644	$ 37,395
Non-vested benefits	7,200	5,154
Accumulated benefit obligation	$ 59,844	$ 42,549
Pension liability:		
Projected benefit obligation	$ 88,182	$ 62,718
Plan assets at fair value	(73,701)	(53,421)
Projected benefit obligation in excess of plan assets	14,481	9,297
Unrecognized net actuarial gain (loss)	(3,778)	445
Unrecognized prior service cost	(528)	(541)
Initial unrecognized net asset being recognized over 17 years	(1,349)	(1,392)
Pension liability included in Accrued interest and other accrued expenses	$ 8,826	$ 7,809
Major assumptions:		
Assumed discount rate	7.5%	8.5%
Rate of increase in compensation levels[1]	4.5 to 5.5%	5.0 to 6.0%
Consumer price index	3.5%	4.0%
Expected long-term rate of return on plan assets	9.0%	8.0%

(1) Range of rates based on employee age.

Freddie Mac also offers a Thrift/401(k) Savings Plan (the Savings Plan) to employees who have worked full-time at Freddie Mac for at least one year. Under the Savings Plan, employees may contribute from 1 percent to 12 percent of their annual salaries, but not to exceed $9,240 in 1995 and 1994. Freddie Mac matches employees' contributions to the Savings Plan up to 6 percent of their annual salaries depending upon the length of service. In addition, Freddie Mac is authorized to make an annual contribution to a profit sharing account in the Savings Plan on behalf of each eligible employee based on salary level. Freddie Mac made contributions to the Savings Plan of $10.3 million, $9.0 million, and $6.9 million in 1995, 1994 and 1993, respectively.

The corporation is required to accrue the estimated cost of retiree benefits, other than pensions, as employees render the services necessary to earn their postretirement benefits. Freddie Mac provides postretirement health care benefits to retired employees on a contributory basis after attaining age 55, who have rendered at least five years of service after age 35. The corporation's postretirement health care plan currently is not funded. The following table provides the status of the plan at December 31, 1995 and 1994.

December 31,	1995	1994
(dollars in thousands)		
Accumulated postretirement benefit obligation (APBO):		
Retirees	$ 809	$ 630
Fully eligible, active plan participants	1,663	970
Unrecognized net gain	2,761	2,692
Other active plan participants	7,288	6,244
Net postretirement benefit liability included in Accrued interest and other accrued expenses	$12,521	$10,536

The components of net periodic postretirement benefits are as follows:

Year Ended December 31,	1995	1994	1993
(dollars in thousands)			
Service cost, benefits attributed to employee service during the year	$1,503	$1,537	$1,584
Interest cost on accumulated postretirement benefit obligation	664	537	522
Net amortization and deferral	(110)	(42)	–
Net periodic postretirement benefits cost	$2,057	$2,032	$2,106

The assumed discount rate was 7.5 percent and 8.5 percent at December 31, 1995 and 1994, respectively. The assumed health care cost trend rate used in measuring the accumulated postretirement benefit obligation was 11.0 percent in 1995, gradually declining to 6.5 percent in the year 2003 and remaining at that level thereafter. A one-percent increase in the assumed health care cost trend rate would increase the APBO by approximately 22 percent. The effect of this change on the sum of the service cost and interest cost components of net periodic postretirement benefit cost would be an increase of 24 percent.

13. FAIR VALUE DISCLOSURES

The Consolidated Fair Value Balance Sheets present Freddie Mac's estimates of the fair value of the corporation's existing assets and liabilities, including rights to future cash flows from these existing assets and liabilities. These balance sheets were prepared on the fair value basis of accounting, which is a comprehensive basis of accounting other than GAAP, to provide relevant financial information that is not provided by the historical cost financial statements. These disclosures satisfy the requirements of SFAS No. 107, "Disclosures about Fair Value of Financial Instruments," which generally requires companies to disclose fair value information about their financial instruments.

Limitations

The "Net fair value after tax" represents the difference between the estimated fair values of assets and liabilities. This estimate does not attempt to present Freddie Mac's value as a going concern or the value of anticipated future business. Therefore, net fair value does not represent an estimate of the aggregate fair value of Freddie Mac's common stock or Freddie Mac as a whole.

Consolidated Fair Value Balance Sheets

December 31,	1995		1994	
	Cost	Fair Value	Cost	Fair Value
(dollars in millions)				
Assets				
Mortgages, net	$107,400	$109,200	$ 72,900	$ 66,800
Cash and cash equivalents	7,500	7,500	11,400	11,400
Investments and mortgage securities purchased under agreements to resell	14,000	13,900	17,800	17,800
Real estate owned, net	800	800	1,000	1,000
Other assets	7,500	7,300	3,100	2,900
Off-balance sheet items:				
Guarantee fees on sold mortgages, net	–	1,200	–	3,200
Outstanding commitments to purchase and sell mortgages	–	100	–	100
Interest-rate agreements and other hedging instuments	–	100	–	300
	$137,200	$140,100	$106,200	$103,500
Liabilities and Net Fair Value				
Debt securities, net:				
Due within one year	$ 62,100	$ 61,400	$ 47,300	$ 46,700
Due after one year	57,200	57,000	44,800	42,100
Total debt securities, net	119,300	118,400	92,100	88,800
Principal and interest due to PC investors	8,800	8,800	5,900	5,900
Other liabilities	2,600	2,600	1,800	600
Subordinated borrowings	600	600	1,200	1,300
	131,300	130,400	101,000	96,600
Estimated income taxes on differences between fair values and GAAP values	–	1,300	–	600
Net fair value after tax	5,900	8,400	5,200	6,300
	$137,200	$140,100	$106,200	$103,500

VALUATION METHODS AND ASSUMPTIONS

The following methods and assumptions were used to estimate the fair values of Freddie Mac's existing assets and liabilities.

Mortgages, net

The retained mortgage portfolio consists of retained mortgages and mortgage-related securities. The fair value for mortgage-related securities is based on quoted market prices. The fair value of retained mortgages is estimated using an option-adjusted spread (OAS) model. The process involves calculating an OAS, a constant spread that, when added to each period's Treasury rate used for discounting, equates the present value of the expected cash flows to the market price of a benchmark Freddie Mac PC. The OAS is then applied to specific Freddie Mac assets benchmarked to that security to determine their estimated value. In this way, the estimated value of retained mortgages is calibrated to the actual market price of a benchmark security. The estimated present value of default costs is subtracted to arrive at the net fair value of the retained mortgage portfolio.

Cash and cash equivalents; Investments and mortgage securities purchased under agreements to resell; Real estate owned, net; Other assets; Principal and interest due to PC investors; Other liabilities; and Subordinated borrowings

For these assets and liabilities, the carrying amount is either fair value or a reasonable estimate of fair value.

Debt securities, net

For debt securities with an original maturity of less than one year, the carrying amount approximates fair value. For debt securities with an original maturity exceeding one year, the fair values are based on quoted market prices. Fair value estimates include the fair values of associated interest-rate agreements (see Note 10).

Guarantee fees on sold mortgages, net

The fair value is approximated using the OAS model described under "Mortgages, net." Interest-only stripped securities (IOs) serve as the benchmark security for valuing the guarantee fee stream because the cash flow pattern of IOs, which is calculated as a fixed percentage of the outstanding mortgage balance, resembles that of guarantee fees. The fair value of the guarantee fee stream includes estimated reinvestment income earned during the period between remittance of mortgage principal and interest to Freddie Mac and disbursement of funds to security holders, and is net of estimated administrative costs. The present value of future default costs on the underlying sold mortgage portfolio is deducted from the fair value of the guarantee fee stream.

Outstanding commitments to purchase and sell mortgages

The fair value of mandatory commitments is estimated as the total pair-off fees the seller must pay if the mortgages are not delivered. Optional purchase commitments are assumed to have a fair value of zero.

Interest-rate agreements and other hedging instruments

The fair values are based on quoted market prices. The estimated fair values of debt- and asset-linked swaps are included in the estimated fair values of the associated debt or assets (see Note 10).

Estimated income taxes on difference between fair values and GAAP values

Freddie Mac will eventually pay income taxes on the future earnings derived from current assets and liabilities. Therefore, the fair value balance sheet includes an estimate of additional income taxes by applying the statutory tax rate (35 percent for 1995 and 1994) to the excess of net fair value over stockholders' equity measured under GAAP.

QUARTERLY RESULTS OF OPERATIONS *(unaudited)*

	1995				1994			
	4th	3rd	2nd	1st	4th	3rd	2nd	1st
(dollars in millions)								
Interest on retained mortgages	$ 1,899	$ 1,694	$ 1,513	$ 1,399	$ 1,284	$ 1,163	$1,073	$1,008
Interest on investments	405	518	510	455	382	334	277	294
	2,304	2,212	2,023	1,854	1,666	1,497	1,350	1,302
Interest on debt securities	(1,827)	(1,764)	(1,659)	(1,514)	(1,335)	(1,151)	(960)	(817)
Interest expense due to security program cycles	(83)	(80)	(42)	(28)	(45)	(64)	(120)	(211)
Net interest income on earning assets	394	368	322	312	286	282	270	274
Management and guarantee income	269	270	272	276	278	282	276	272
Other income, net	9	7	10	13	8	6	16	36
Total revenues	672	645	604	601	572	570	562	582
Provision for mortgage losses	(70)	(65)	(60)	(60)	(50)	(50)	(50)	(50)
REO operations expense	(76)	(73)	(68)	(69)	(56)	(56)	(58)	(55)
Administrative expenses	(102)	(99)	(97)	(97)	(97)	(95)	(95)	(92)
Income before income taxes and extraordinary item	424	408	379	375	369	369	359	385
Provision for income taxes	(133)	(130)	(115)	(117)	(117)	(120)	(110)	(108)
Extraordinary item, net of taxes	–	–	–	–	–	–	–	(44)
Net income	$ 291	$ 278	$ 264	$ 258	$ 252	$ 249	$ 249	$ 233
Net income available to common stockholders	$ 274	$ 262	$ 248	$ 242	$ 235	$ 233	$ 233	$ 217

TOTAL PORTFOLIO LIQUIDATION[1] *(annualized) (unaudited)*

	Quarter Ended				
Year	March 31,	June 30,	September 30,	December 31,	Annual
1995	8.1%	10.7%	15.0%	14.3%	12.0%
1994	27.4	17.0	12.0	9.9	16.4
1993	22.3	41.3	39.3	48.4	38.0
1992	29.8	33.8	29.7	40.0	33.3
1991	9.8	16.1	14.1	18.1	14.6

(1) Liquidation rates on mortgages sold under the PC programs as well as those retained by Freddie Mac.

MORTGAGE DELINQUENCY STATISTICS *(unaudited)*

SINGLE-FAMILY MORTGAGES[1]

Date	Total Number of Mortgages	Three or more Delinquent Payments	Foreclosures Approved and In Process	Total	Freddie Mac At-Risk[2]
12/95	7,080,208	0.27%	0.34%	0.61%	0.60%
12/94	6,835,730	0.25%	0.32%	0.57%	0.55%
12/93	6,585,430	0.27%	0.34%	0.61%	N/A
12/92	6,388,896	0.30%	0.34%	0.64%	N/A
12/91	6,098,626	0.30%	0.31%	0.61%	N/A

(1) Numbers and percentages include all 1- to 4-family mortgages sold under the PC programs as well as those retained by Freddie Mac.
(2) Includes those mortgages for which Freddie Mac has assumed primary default risk.

MULTIFAMILY MORTGAGES[1][2]

(dollars in millions) Date	Total Dollars of Mortgages	Two or more Delinquent Payments[3]	Foreclosures Approved and In Process	Total	Total Dollars of Non-Performing Mortgages
12/95	$ 6,665	1.12%	1.76%	2.88%	$192
12/94	$ 6,297	0.83%	2.96%	3.79%	$239
12/93	$ 7,374	0.86%	5.06%	5.92%	$437
12/92	$ 8,967	2.02%	4.79%	6.81%	$610
12/91	$10,321	1.52%	3.90%	5.42%	$560

(1) Numbers and percentages include all conventional multifamily fixed-rate mortgages sold under the PC programs as well as those retained by Freddie Mac.
(2) Prior years data have been restated to reflect the transfer of multifamily in-substance foreclosures from real estate owned to the retained portfolio pursuant to the adoption of Statement of Financial Accounting Standards No. 114.
(3) Excludes mortgages in litigation that are less than 60 days delinquent.

MANAGEMENT'S REPORT ON THE FINANCIAL STATEMENTS AND INTERNAL CONTROL STRUCTURE

The management of the Federal Home Loan Mortgage Corporation (the corporation or Freddie Mac) is responsible for the preparation, integrity, and fair presentation of the corporation's annual consolidated financial statements. The annual consolidated financial statements presented have been prepared in accordance with generally accepted accounting principles, and, as such, include amounts based on judgments and estimates made by management. Management has also prepared the other information included in this annual report, and is responsible for its accuracy and consistency with the consolidated financial statements.

The annual consolidated financial statements referred to above have been audited by Arthur Andersen LLP, independent public accountants, who have been given unrestricted access to all financial records and related data, including minutes of all meetings of stockholders, the Board of Directors, and committees of the Board. Management believes that all representations made to Arthur Andersen LLP during the audit were valid and appropriate.

In addition, management is responsible for establishing and maintaining an internal control structure over financial reporting, including controls over the safeguarding of assets. The objective of the internal control structure is to provide reasonable assurance to management and the Board of Directors as to the preparation of the financial statements in accordance with generally accepted accounting principles.

Management has made its own assessment of the effectiveness of the corporation's internal control structure over financial reporting, including controls over the safeguarding of assets, as of December 31, 1995, in relation to the criteria described in "Internal Control — Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management believes that, as of December 31, 1995, the corporation's internal control structure was effective in achieving the objective stated above.

However, there are inherent limitations in the effectiveness of any internal control structure, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even an effective internal control structure can provide only reasonable assurance with respect to the reliability of the financial statements. Furthermore, the effectiveness of any internal control structure can change with changes in circumstances.

Management also recognizes its responsibility for fostering a strong ethical climate so that Freddie Mac's affairs are conducted according to the highest standards of personal and corporate conduct. This responsibility is characterized and reflected in Freddie Mac's ethical standards policy, which is publicized throughout the corporation. The ethical standards policy addresses, among other things, potential conflicts of interests, acceptable employee activities conducted outside of Freddie Mac, acceptable financial activities, confidentiality of proprietary information, and ethical business conduct, including compliance with selected laws and regulations. Freddie Mac maintains a systematic program to assess compliance with these policies.

The corporation has an Internal Audit Department whose responsibilities include monitoring compliance with established policies and procedures and evaluating Freddie Mac's internal control structure. The Internal Audit Department is independent of the activities it reviews. Operational and special audits are conducted, and internal audit reports are submitted to appropriate management and the audit committee of Freddie Mac's Board of Directors.

The Audit Committee of the Board of Directors meets periodically with management, internal auditors, and Freddie Mac's independent public accountants to review matters relating to financial accounting and reporting policies and control procedures. Both Arthur Andersen LLP and the Internal Audit Department have full and free access, with and without management present, to the Audit Committee.

Leland C. Brendsel

Leland C. Brendsel
Chairman and Chief Executive Officer

John P. Gibbons

John P. Gibbons
Executive Vice President and
Chief Financial Officer (Interim)

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS ON MANAGEMENT'S ASSERTION ABOUT THE EFFECTIVENESS OF THE INTERNAL CONTROL STRUCTURE OVER FINANCIAL REPORTING

To the Federal Home Loan Mortgage Corporation: We have examined management's assertion that the Federal Home Loan Mortgage Corporation maintained an effective internal control structure over financial reporting, including controls over the safeguarding of assets, as of December 31, 1995, included in the accompanying Management's Report on the Financial Statements and Internal Control Structure.

Our examination was made in accordance with standards established by the American Institute of Certified Public Accountants and, accordingly, included obtaining an understanding of the internal control structure over financial reporting, testing, and evaluating the design and operating effectiveness of the internal control structure, and such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Because of inherent limitations in any internal control structure, errors or irregularities may occur and not be detected. Also, projections of any evaluation of the internal control structure over financial reporting to future periods are subject to the risk that the internal control structure may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assertion that the Federal Home Loan Mortgage Corporation maintained an effective internal control structure over financial reporting, including controls over the safeguarding of assets, as of December 31, 1995, is fairly stated, in all material respects, based upon criteria established in "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Arthur Andersen LLP

Washington, D.C.
January 12, 1996

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS ON CONSOLIDATED FINANCIAL STATEMENTS

To the Federal Home Loan Mortgage Corporation: We have audited the accompanying Consolidated Balance Sheets of the Federal Home Loan Mortgage Corporation, a federally chartered corporation, (the "corporation"), as of December 31, 1995 and 1994, and the related Consolidated Statements of Income, Stockholders' Equity and Cash Flows for each of the three years in the period ended December 31, 1995. These financial statements are the responsibility of the corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Federal Home Loan Mortgage Corporation as of December 31, 1995 and 1994, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles.

We have also audited, in accordance with generally accepted auditing standards, the supplemental Consolidated Fair Value Balance Sheets of the Federal Home Loan Mortgage Corporation as of December 31, 1995 and 1994. As described in Note 13, the supplemental Consolidated Fair Value Balance Sheets have been prepared by management to present relevant financial information that is not provided by the Consolidated Balance Sheets referred to above and are not intended to be a presentation in conformity with generally accepted accounting principles. In addition, the supplemental Consolidated Fair Value Balance Sheets do not purport to present the net realizable, liquidation, or market value of the corporation as a whole. Furthermore, amounts ultimately realized by the corporation from the disposal of assets and settlement of liabilities may vary significantly from the fair values presented. In our opinion, the supplemental Consolidated Fair Value Balance Sheets referred to above present fairly, in all material respects, the information set forth therein as described in Note 13.

Arthur Andersen LLP

Washington, D.C.
January 12, 1996