FEDERAL HOME LOAN MORTGAGE CORP
Form 10-Q
May 08, 2014
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended March 31, 2014
or

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

For the transition period from to
Commission File Number: 001-34139

Federal Home Loan Mortgage Corporation
(Exact name of registrant as specified in its charter)
Freddie Mac

Federally chartered corporation	8200 Jones Branch Drive McLean, Virginia 22102-3110	52-0904874	(703) 903-2000 (Registrant's telephone number, including area code)
(State or other jurisdiction of incorporation or organization)	(Address of principal executive offices, including zip code)	(I.R.S. Employer Identification No.)	

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports); and (2) has been subject to such filing requirements for the past 90 days. ý Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ý Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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

As of April 24, 2014, there were 650,040,391 shares of the registrant's common stock outstanding.

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FINANCIAL STATEMENTS

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PART I — FINANCIAL INFORMATION

We continue to operate under the conservatorship that commenced on September 6, 2008, under the direction of FHFA as our Conservator. The Conservator succeeded to all rights, titles, powers and privileges of Freddie Mac, and of any shareholder, officer or director thereof, with respect to the company and its assets. The Conservator has delegated certain authority to our Board of Directors to oversee, and management to conduct, business operations so that the company can continue to operate in the ordinary course. The directors serve on behalf of, and exercise authority as directed by, the Conservator. See "BUSINESS — Conservatorship and Related Matters" in our Annual Report on Form 10-K for the year ended December 31, 2013, or 2013 Annual Report, for information on the terms of the conservatorship, the powers of the Conservator, and related matters, including the terms of our Purchase Agreement with Treasury.

This Quarterly Report on Form 10-Q includes forward-looking statements that are based on current expectations and are subject to significant risks and uncertainties. These forward-looking statements are made as of the date of this Form 10-Q and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date of this Form 10-Q. Actual results might differ significantly from those described in or implied by such statements due to various factors and uncertainties, including those described in: (a) the "FORWARD-LOOKING STATEMENTS" sections of this Form 10-Q and our 2013 Annual Report; and (b) the "RISK FACTORS" and "BUSINESS" sections of our 2013 Annual Report.

Throughout this Form 10-Q, we use certain acronyms and terms that are defined in the "GLOSSARY."

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read this MD&A in conjunction with our consolidated financial statements and related notes for the three months ended March 31, 2014 included in "FINANCIAL STATEMENTS" and our 2013 Annual Report.

EXECUTIVE SUMMARY

Overview

Freddie Mac is a GSE chartered by Congress in 1970 with a public mission to provide liquidity, stability, and affordability to the U.S. housing market. We have maintained a consistent market presence since our inception, providing essential mortgage liquidity in a wide range of economic environments. We are working to support the continued recovery of the housing market and the nation's economy by: (a) providing America's families with access to mortgage funding at low rates while helping distressed borrowers keep their homes and avoid foreclosure, where possible; and (b) providing consistent liquidity to the multifamily mortgage market, which includes providing financing for affordable rental housing. At the same time, we are working with FHFA, our customers and the industry to build a stronger housing finance system for the nation.

Conservatorship and Government Support for Our Business

We continue to operate in conservatorship that began in September 2008, under the direction of FHFA, as our Conservator. The conservatorship and related matters continue to have a wide-ranging impact on us, including our management, business, financial condition, and results of operations. There is significant uncertainty as to our future, as conservatorship has no specified termination date, and it is unknown what changes may occur to our business model during or following conservatorship, including whether we will continue to exist.

We are also subject to certain constraints on our business activities imposed by Treasury due to the terms of, and Treasury's rights under, the Purchase Agreement. We are dependent upon the continued support of Treasury and FHFA in order to continue operating our business. We cannot over the long term build and retain capital from the earnings generated by our business operations, or return capital to stockholders other than Treasury.

For more information on the conservatorship and government support for our business, including the Purchase Agreement, see "BUSINESS — Conservatorship and Related Matters" and "NOTE 2: CONSERVATORSHIP AND RELATED MATTERS" in our 2013 Annual Report.

Consolidated Financial Results

During the first quarter of 2014, home price growth moderated compared to early periods of 2013. Comprehensive income was $4.5 billion for the first quarter of 2014 compared to $7.0 billion for the first quarter of 2013. Comprehensive income for the first quarter of 2014 consisted of $4.0 billion of net income and $0.5 billion of other comprehensive income. Our results for the first quarter of 2014 include: (a) pre-tax income of $4.5 billion primarily related to settlements of lawsuits regarding our investments in certain residential non-agency mortgage-related securities; partially offset by (b) declines in the fair value of our derivatives due to the decrease in longer-term interest rates. Our total equity was $6.9 billion at March 31, 2014. As a result of our positive net worth at March 31, 2014, no draw is being requested from Treasury under the Purchase Agreement for the first quarter of 2014. Through March 31, 2014, we have paid aggregate cash dividends to Treasury that exceed our aggregate draws received under the Purchase Agreement by $10.4 billion. At March 31, 2014, our aggregate funding received from Treasury under the Purchase Agreement was $71.3 billion.

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Sustainability of Earnings

The level of earnings we have experienced in recent periods is not sustainable over the long term. Our recent financial results, particularly the level of loan loss provisioning, has benefited significantly from strong home price appreciation, which is beginning to moderate. Our 2013 financial results also included a significant benefit related to the release of the deferred tax asset valuation allowance. Additionally, our 2013 and 2014 financial results included settlements of both residential non-agency mortgage-related securities litigation and representation and warranty claims. Our settlements of representation and warranty claims related to pre-conservatorship loan originations are largely complete while residential non-agency mortgage-related securities litigation is ongoing and additional settlements are expected in the remainder of 2014. In addition, declines in the size of our mortgage-related investments portfolio, as required by FHFA and the Purchase Agreement with Treasury, will reduce earnings over time. Our financial results will also continue to be affected by changes in interest rates, yield curves, and mortgage spreads, which can cause significant earnings and net worth variability from period to period.

Our Primary Business Objectives

We are focused on the following primary business objectives: (a) reducing taxpayer exposure to losses by reducing and managing our overall risk profile, especially to mortgage-related risks; (b) supporting U.S. homeowners and renters by providing lenders with a constant source of liquidity for mortgage products even when other sources of financing are scarce; (c) building a commercially strong and efficient business enterprise; and (d) positioning the company, in particular our people and infrastructure, to succeed in a to-be-determined "future state."

Reducing Taxpayer Exposure to Losses by Reducing and Managing Our Overall Risk Profile, Especially to Mortgage-Related Risks

We continue to actively manage and reduce the high credit risk related to our 2005-2008 Legacy single-family book by: (a) providing homeowners with alternatives that allow them to stay in their homes; (b) maximizing the proceeds from short sales and REO sales; (c) actively managing our servicers; (d) pursuing our rights with our sellers; (e) enforcing our rights with other counterparties; and (f) reducing our mortgage-related investments portfolio over time. The 2005-2008 Legacy single-family book represented 15% of our single-family credit guarantee portfolio at March 31, 2014, but comprised 77% of our credit losses in the first quarter of 2014 compared to 81% in the full-year of 2013.

Providing Homeowners with Alternatives that Allow Them to Stay in Their Homes

We establish guidelines for our servicers to follow and provide them default management programs to use, in part, in determining which type of loan workout would be expected to provide us with an opportunity to manage our exposure to credit losses. Our servicers pursue repayment plans and loan modifications for borrowers facing financial or other hardships because the level of recovery on a reperforming loan may often be much higher than would be the case with a foreclosure or a foreclosure alternative. Since 2009, we have helped approximately 987,000 borrowers experiencing hardship complete a loan workout. Under our loan workout programs, our servicers contact borrowers experiencing hardship with a goal of helping them stay in their homes or avoid foreclosure. Across all of our modification programs, we modified $3.8 billion and $4.5 billion in UPB of loans in the first quarters of 2014 and 2013, respectively. Our servicers seek and also facilitate the completion of foreclosure alternatives when a home retention solution is not possible.

Beginning in 2009, we introduced a variety of borrower-assistance programs, including HAMP, to help keep families in their homes. Our relief refinance initiative, including HARP (which is the portion of our relief refinance initiative for loans with LTV ratios above 80%), is another key program used by our seller/servicers to help keep families in their homes. In the first quarters of 2014 and 2013, we purchased or guaranteed $9.1 billion and $32.9 billion in UPB of relief refinance loans, respectively, which included $5.2 billion and $21.5 billion in UPB of HARP loans, respectively. We have purchased HARP loans provided to nearly 1.3 million borrowers since the initiative began in 2009, including approximately 30,000 borrowers during the first quarter of 2014. See "Table 34 — Single-Family Relief Refinance Loans" for more information about the volume of our relief refinance purchases.

As of March 31, 2014, the borrower's monthly payment for all of our completed HAMP modifications was reduced on average by an estimated $530, which amounts to an average of $6,360 per year, and a total of $1.5 billion in annual reductions (these amounts are calculated by multiplying the number of completed modifications by the average reduction in monthly payment, and have not been adjusted to reflect the actual performance of the loans following modification).

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The table below presents our single-family loan workout activities for the last five quarterly periods.

Table 1 — Total Single-Family Loan Workout Volumes[(1)]

(1) Based on workouts completed with borrowers for loans within our single-family credit guarantee portfolio. Excludes those modification, repayment, and forbearance activities for which the borrower has started the required process, but the actions have not been made permanent or effective, such as loans in modification trial periods. Also excludes certain loan workouts where our single-family seller/servicers have executed agreements in the current or prior periods, but these have not been incorporated into certain of our operational systems due to delays in processing. These categories are not mutually exclusive and a loan in one category may also be included within another category in the same period.

(2) As of March 31, 2014, approximately 22,000 borrowers were in modification trial periods, including approximately 18,000 borrowers in trial periods for our non-HAMP modification.

(3) Excludes loans with long-term forbearance under a completed loan modification. Many borrowers enter into a short-term forbearance agreement before another loan workout is pursued or completed. We only report forbearance activity for a single loan once during each quarterly period within the year; however, a single loan may be included under separate forbearance agreements in separate periods.

While we believe our home retention programs have been largely successful, many borrowers still need our assistance. See “RISK MANAGEMENT — Credit Risk — Mortgage Credit Risk — Single-Family Mortgage Credit Risk” for more information about loss mitigation activities and our efforts to keep families in their homes, including through our loan modification initiatives and our relief refinance mortgage initiative.

Maximizing the Proceeds from Short Sales and REO Sales

In cases where repayment plans and loan modifications are not possible or successful, a short sale transaction typically provides us with a comparable or higher level of recovery than a foreclosure and subsequent property sale from our REO inventory. In large part, the benefit of a short sale is that we avoid costs we would otherwise incur to complete the foreclosure and dispose of the property, including maintenance, property taxes, and other expenses associated with holding REO property.

We believe our REO disposition and short sale severity ratios in the first quarter of 2014 were positively affected by changes made in 2012 to our process for evaluating the market value of impaired loan collateral and determining the list price for our REO properties when we offer them for sale.

Actively Managing our Servicers

We continue to face challenges with respect to the performance of certain of our single-family servicers in managing our seriously delinquent loans. Our servicers represent and warrant to us that loans serviced on our behalf will be serviced in accordance with our servicing contract. These contractual obligations provide us with remedies for breaches in servicing. These contractual remedies include the ability to require the servicer to pay compensatory or other fees, repurchase the loan at its current UPB, and/or reimburse us for losses realized. Beginning in 2013, we increased our review of servicing related violations, which included issuing notices of defect to our servicers for certain violations of our servicing standards. As of March 31, 2014, we had: (a) $0.4 billion of outstanding repurchase requests; and (b) $0.4 billion of outstanding notices of defect, with our servicers, based on the UPB of the related loans. We also recognized $131 million of compensatory fees in the first quarter of 2014 primarily for servicer failures to complete a foreclosure within our timelines.

We continue to have a large population of seriously delinquent loans, many of which have been delinquent for more than one year; these loans tend to be more challenging to resolve. As of March 31, 2014, our serious delinquency rate for the aggregate of those states that require a judicial foreclosure and all other states was 3.07% and 1.49%, respectively. Foreclosures generally take longer to complete in states where judicial foreclosures are required, compared to other states. In the first quarter of 2014, the average time to foreclose on properties in states that require a judicial foreclosure was 1,033 days compared to 637 days in all other states for loans in our single-family credit guarantee portfolio, excluding those underlying our Other Guarantee Transactions. These averages are based on the loans completing foreclosure during the period.

As part of our efforts to maximize foreclosure alternatives, increase problem loan workouts, and mitigate our credit losses, we have continued to facilitate the transfer of servicing for certain pools of loans with higher credit risk from underperforming servicers to other servicers that specialize in workouts of problem loans. In the first quarter of 2014, we facilitated the transfer of servicing for $7.1 billion in UPB of loans from our primary servicers to specialty servicers.

Pursuing Our Rights with Our Sellers

We have contractual arrangements with our sellers under which they agree to sell us mortgage loans, and represent and warrant that those loans have been originated under specified underwriting standards. If we subsequently discover that the representations and warranties were breached (i.e., that contractual standards were not followed), we can exercise certain contractual remedies to mitigate our actual or potential credit losses. These remedies include the ability to require the seller to repurchase the loan at its current UPB and/or reimburse us for losses realized. Our exposure to single-family mortgage seller/servicers has been high in recent years with respect to their repurchase obligations arising from breaches of representations and warranties made to us for loans they underwrote and sold to us. In 2013, we substantially achieved the goal set for us (in the 2013 Conservatorship Scorecard) to complete our requests for remedies for breaches of seller representations and warranties related to pre-conservatorship loan activity. We continue to recover credit losses from seller/servicers in the normal course of business related to breaches of representations and warranties for loans they sold to us or service for us. In the first quarter of 2014, we recovered amounts from seller/servicers with respect to $1.0 billion in UPB of loans subject to our repurchase requests, including $0.4 billion in UPB related to settlement agreements. Approximately 17% of the $1.0 billion in UPB associated with repurchase requests in the first quarter of 2014 were satisfied by the reimbursement of losses (excluding amounts related to settlement agreements). As of March 31, 2014 and December 31, 2013, we had $0.8 billion and $1.6 billion, respectively, of outstanding repurchase requests with sellers, based on UPB of the loans.

Enforcing Our Rights with Other Counterparties

We continue to pursue claims for coverage under mortgage insurance policies. We also continue to actively pursue settlements with mortgage insurance counterparties. We use mortgage insurance, which is a form of credit enhancement, to mitigate our credit loss exposure. Primary mortgage insurance is generally required to be purchased at loan origination, typically at the borrower’s expense, for certain mortgages with LTV ratios greater than 80%, from an insurer that is typically selected by the lender.

We received payments under primary and other mortgage insurance of $0.4 billion during both the first quarter of 2014 and the first quarter of 2013. Although the financial condition of certain of our mortgage insurers has improved in recent periods, there is still significant risk that some of these counterparties may fail to fully meet their obligations. We expect to receive substantially less than full payment of our claims from three of our seven larger mortgage insurance counterparties, as they are only permitted to partially pay claims under orders of their regulators.

Our ability to manage our exposure to mortgage insurers is limited as: (a) certain of our mortgage insurers are operating below our eligibility thresholds; and (b) our ability to revoke a mortgage insurer's status as an eligible insurer requires FHFA approval under certain circumstances. We consider the collectability of our claims against our mortgage insurers when determining the carrying amount of our receivables and estimating our loan loss reserves on our consolidated balance sheets.

We are working with FHFA and Fannie Mae to improve mortgage insurance standards. We are developing counterparty risk management standards for mortgage insurers that include revised eligibility requirements. In December 2013, FHFA announced that we and Fannie Mae, in collaboration with our mortgage insurers, had completed development of new master policies, for which the mortgage insurers are expected to seek state regulatory approval. These changes to the master policies are intended to provide greater certainty of coverage, facilitate timely claims processing, and help address the significant problems we faced in recent years in resolving repurchase requests related to mortgage insurance rescission. We expect to implement the new master policies and eligibility standards (including capital requirements) for mortgage insurers during 2014.

At the direction of our Conservator, we are also working to enforce our rights as an investor with respect to the non-agency mortgage-related securities we hold, and are engaged in various efforts, in some cases in conjunction with other investors, to mitigate or recover losses on our investments in these securities. In the first quarter of 2014, we and FHFA reached settlements with a number of institutions pursuant to which we received an aggregate of $4.5 billion. In April 2014, we and

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FHFA entered into agreements with two other institutions to settle FHFA-led litigation related to certain residential non-agency mortgage-related securities we hold. Under these agreements, we will be paid $275 million, which will be reflected in our consolidated financial results for the second quarter of 2014. Lawsuits against a number of large institutions are currently pending. See “NOTE 15: CONCENTRATION OF CREDIT AND OTHER RISKS” for more information about our recent agreements with non-agency mortgage-related security issuers.

We have also worked to enforce our rights in the Lehman bankruptcy. In February 2014, we reached a settlement with Lehman Brothers Holdings Inc. pursuant to which we received $767 million to resolve our claims related to Lehman’s bankruptcy. The majority of this settlement amount was reflected as an adjustment to our December 31, 2013 estimate of the expected recoveries of our short-term lending receivable. The remaining portion of this settlement related to claims for repurchase requests associated with loans sold to us by Lehman and is included in our results for the first quarter of 2014. For more information, see “NOTE 17: LEGAL CONTINGENCIES."

Reducing Our Mortgage-Related Investments Portfolio Over Time

During the first quarter of 2014, the size of our mortgage-related investments portfolio declined by 6% (or 23% on an annualized basis), or $26.6 billion, to $434.4 billion at March 31, 2014 compared to December 31, 2013. Our less liquid assets (i.e., assets less liquid than agency securities) accounted for $13.1 billion of this decline primarily due to liquidations and $2.4 billion of sales (excluding sales of: (a) multifamily held-for-sale loans; and (b) single-family loans purchased for cash). We plan to continue reducing the balance of our less liquid assets, although we continue to purchase certain of these assets as part of our business strategies (e.g., removal of seriously delinquent loans from PC pools).

Supporting U.S. Homeowners and Renters by Providing Lenders with a Constant Source of Liquidity for Mortgage Products even when Other Sources of Financing are Scarce

We maintain a consistent market presence by providing lenders with a constant source of liquidity for mortgage products even when other sources of financing are scarce. This liquidity provides our customers with confidence to continue lending even in difficult environments. In the first quarters of 2014 and 2013, we purchased or issued other guarantee commitments for $49.2 billion and $131.9 billion in UPB of single-family conforming mortgage loans, respectively, representing approximately 244,000 and 636,000 homes, respectively. Origination volumes in the U.S. residential mortgage market declined significantly during the first quarter of 2014, as compared to the first quarter of 2013, driven by a significant decline in the volume of refinance mortgages. We attribute this decline to higher mortgage interest rates in the 2014 period than in the 2013 period. We estimate that we, Fannie Mae, and Ginnie Mae collectively guaranteed approximately 90% of the single-family conforming mortgages originated in the first quarter of 2014. During the first quarter of 2014, our multifamily new business activity totaled $3.0 billion, and provided financing for 239 properties amounting to approximately 51,000 apartment units. More than 90% of these units were affordable to families earning at or below the median income in their area.

Building a Commercially Strong and Efficient Business Enterprise

Single-Family Guarantee Segment Strategies

Our single-family business is our core business line. We continue to take steps to build a stronger, profitable business model for our ongoing business. Our goal is to strengthen the business model in order to run the business efficiently and effectively in support of homeowners and taxpayers and, if required as part of a future state for the enterprise, to be able to promptly return to private sector ownership.

Our Single-family Guarantee segment is focused on strengthening our business model by:

- Leveraging the fundamentals: We are leveraging our existing product offerings to better meet the needs of an evolving mortgage market. This includes working to reduce repurchase requests and penalties, in the form of fees, by providing greater certainty for seller/servicers that the loans they sell to us or service for us meet our requirements. We are doing this by enhancing the tools we make available to our customers (including Loan Prospector, Loan Quality Advisor, and Home Value Estimator), and expanding and leveraging the data standards of the Uniform Mortgage Data Program. We intend to continue to simplify, streamline, and strengthen our operations, while keeping pace with regulatory requirements, such as those implemented under the Dodd-Frank Act.
- Better serving our customers: Our customers are our sellers, servicers, and investor/dealers. Based on feedback we have received directly from our customers through our Customer Advisory Boards, surveys, and ongoing

conversations, we are enhancing our processes and programs to improve our customers' experience when doing business with us.

- Managing the credit risk of the single-family credit guarantee portfolio: We are managing our credit risk by setting our underwriting standards at a level commensurate with the long-term credit risk appetite of the company. We use a process of delegated underwriting for the single-family mortgages we purchase or securitize. In this process, our contracts with seller/servicers describe mortgage eligibility and underwriting standards, and the seller/servicers represent and warrant to us that the mortgages sold to us meet these standards. Beginning in 2009, we have made various changes to our credit policies, including changes to improve our underwriting standards, purchased fewer loans with higher risk characteristics, and assisted in improving our mortgage insurers' and lenders' underwriting

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practices. As a result, the credit quality of the New single-family book is significantly better than that of the 2005-2008 Legacy single-family book, as measured by original LTV ratios, FICO scores, and the proportion of loans underwritten with full documentation, as well as delinquency rates and credit losses. However, in recent periods, as refinancing volumes have declined, the composition of our loan purchase activity has been shifting to a higher proportion of purchase-type loans and our sellers have sold us this type of loan with generally higher original LTV ratios and lower credit scores, in aggregate, than the purchase-type loans sold to us during 2010 through 2012.

- Transferring the credit risk of the single-family credit guarantee portfolio: We consider risk transfer transactions to be a prudent way to manage risk in our business. In addition to three transactions completed in 2013, we executed one transaction during the first quarter of 2014 that transferred a mezzanine credit loss position on certain groups of loans in the New single-family book. These transactions shift mortgage credit risk from us to private investors. While these transactions have been relatively small compared to our overall mortgage credit risk exposure, we believe they have attracted broad interest in the market. We will continue to seek to expand and refine our offerings of credit risk transfer transactions in the future.
- Optimizing the economics of the single-family credit guarantee portfolio: We strive to achieve the highest economic returns on our portfolio while considering and balancing our: (a) customer diversification; (b) housing mission and goals; and (c) customers' liquidity needs. We also align our mortgage-related securities offerings and disclosures with customer needs and investor demand to balance the achievement of the above objectives while considering the relative performance of our securities in the market.

Investments Segment Strategies

Our Investments segment is a key business operation, which has certain objectives in 2014, including:

- Maintaining a presence in the agency mortgage-related securities market. Our activities in this market may include outright purchases and sales, dollar roll transactions, and structuring activities (e.g., resecuritizing existing agency securities into REMICs) and selling some or all of the tranches.
- Maintaining a portfolio of liquid securities consistent with our liquidity management guidelines. In managing the reduction of our mortgage-related investments, we evaluate the liquidity of these investments based on two categories: (a) single-class and multiclass agency securities; and (b) assets that are less liquid than agency securities. We are focusing our efforts on reducing the balance of less liquid assets in the mortgage-related investments portfolio. Our liquid assets collectively represented approximately 39% of UPB of the portfolio at March 31, 2014, compared to 40% at December 31, 2013.
- Managing the single-family performing loans obtained through our cash purchase program. We purchase loans from lenders for cash and, in conjunction with the single-family business, securitize the majority of these loans into Freddie Mac agency securities that may be sold to dealers or investors, or retained in our mortgage investments portfolio as agency securities.
- Managing single-family re-performing loans and performing modified loans. This includes securitizing loans, and could include selling loans or other disposition strategies in the future.
- Managing single-family delinquent loans along with the single-family business. This includes removing seriously delinquent loans from PC pools and could include selling loans, securitizing loans, or other disposition strategies in the future.
- Reducing the overall balance of our holdings of non-agency mortgage-related securities through liquidations and sales, subject to a variety of constraints, including market conditions.
- Managing the treasury function, including funding and liquidity, for the overall company, through the issuance of short-term and long-term unsecured debt. We maintain a liquidity and contingency portfolio of cash and non-mortgage investments for short-term liquidity management.
- Managing the interest-rate risk for the overall company through the use of derivatives and unsecured debt.

Multifamily Segment Strategies

Our Multifamily business is also a key business operation focusing on financing multifamily rental housing. We provide financing for affordable housing for renters nationwide and are a consistent source of liquidity to the multifamily mortgage market. We maintain a strong credit and capital management discipline while seeking to generate positive Segment Earnings comprehensive income. We accomplish this primarily by focusing on our business model of purchasing, aggregating, and securitizing mortgage loans in order to transfer the expected credit risk associated with the loans to third-party investors. The Multifamily business model aligns with our objective that private investors absorb the first and predominant losses before any taxpayer exposure. We plan to continue to provide and support a consistent supply of affordable rental housing while reducing our exposure to credit risk through securitization. During the first quarter of 2014, we continued our K Certificate securitizations in the multifamily market with K Certificate transactions of $3.9 billion in UPB. In addition to our risk transfers

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though K Certificate transactions, we are seeking to introduce innovative ways to further expand our offerings in support of affordable rental housing while limiting our exposure to mortgage credit risk.

Positioning the Company, in Particular Our People and Infrastructure, to Succeed in a to-be-determined “future state”

Development of a New Secondary Mortgage Market

Under the direction of FHFA, we continue various efforts to build the infrastructure for a future housing finance system, including the following:

- Common Securitization Platform: We continue to work with FHFA and Fannie Mae on the development of a future new common securitization platform. In October 2013, Common Securitization Solutions, LLC (which is equally owned by us and Fannie Mae) was formed to build and operate the platform.
- Contractual and Disclosure Framework: FHFA directed us to work with Fannie Mae to implement a set of uniform contractual terms and standards for transparency that can inform the single-family mortgage securitization market in the future. During 2013, a team from Freddie Mac and Fannie Mae performed analysis and developed preliminary recommendations for: (a) fully-guaranteed (GSE) mortgage-related securities; (b) non- or partially guaranteed (GSE) mortgage-related securities; and (c) new master trust agreements for these types of securities.
- Uniform Mortgage Data Program: We and Fannie Mae are collaborating with the industry to develop and implement uniform data standards for single-family mortgages. We have made significant progress by completing initial phases of this program, including: (a) standard appraisal data elements; (b) the Uniform Collateral Data Portal, which allows us to aggregate this data from sellers; (c) the Uniform Loan Delivery Dataset, which defines common data elements for each loan we acquire or guarantee; and (d) the Uniform Closing Dataset, to support the Consumer Financial Protection Bureau's (or CFPB) new mortgage closing disclosure form.
- Lender placed insurance standards: As part of the servicing alignment initiative, we announced changes in our servicing standards for situations in which our servicers obtain property hazard insurance on properties securing single-family loans we own or guarantee. As a result, effective June 1, 2014, our seller/servicers may not receive compensation or other payment from insurance carriers nor may they use their own or affiliated entities to insure or reinsure a property.

In addition, we also worked to help our seller/servicers improve their underwriting processes for loans that they sell to us. As part of these efforts we made progress in the following areas during the first quarter of 2014:

- Continued our initiative for enhanced early-risk assessment by seller/servicers through the use of Loan Quality Advisor, an automated tool for use in evaluating the credit eligibility of loans and identifying non-compliance issues;
- Implemented requirements for our seller/servicers in response to certain final rules from the CFPB, including rules concerning the requirements for borrowers' ability to repay and high-cost mortgages. See “BUSINESS — Legislative and Regulatory Developments — Dodd-Frank Act” in our 2013 Annual Report for further information on the final rules;
- Adhered to recently implemented standard timelines, appeal requirements, and alternative remedies for resolution of repurchase obligations as part of our efforts to enhance post-delivery quality control practices and transparency associated with our new representation and warranty framework; and
- Continued to execute our loan review sampling strategy, specifically focusing on newly purchased mortgage loans, to evaluate compliance with our standards.

Investing in Human, Technology and Other Resources

We continue to make strategic investments to maintain and improve our ability to operate the company for the foreseeable future in conservatorship and potentially afterwards. Our human capital risks have stabilized in recent periods, as increased levels of voluntary turnover experienced in 2011 have abated. The possibility remains that we may experience increased turnover again in the future as the Administration and Congress continue to debate our future business model.

Our information technology risk also continues to decline. For example, in 2013, we completed a three-year multimillion dollar project to move our key legacy applications and infrastructure to current, supported technology. We are investing each year to maintain our technology and are focused on standardizing and simplifying the technology portfolio. We continue to focus on emerging information security risks. We are reviewing our information technology architecture design with a focus on simplifying our information technology environment. We are also building our out-of-region disaster recovery capabilities.

Streamlining, Simplifying and Strengthening Operations

We continue to strengthen our operations. Beginning in mid-2012 and continuing in 2013 and 2014, we took steps to enhance management's focus on control issues by elevating awareness of those issues across the company and stressing timely remediation. As a result, the number of outstanding control issues reached its lowest level since conservatorship. We also continue to work to improve our operating efficiency. In 2013, we began a multi-year project focused on simplifying our control structure and eliminating redundant control activities. We updated our risk and control framework to increase our

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emphasis on risk management and are conducting detailed operational controls design reviews to identify ways to simplify our controls structure.

Mortgage Market and Economic Conditions

Overview

The U.S. real gross domestic product rose by 0.1% on an annualized basis during the first quarter of 2014, compared to 2.6% in the fourth quarter of 2013 and 1.1% in the first quarter of 2013, according to the Bureau of Economic Analysis. The national unemployment rate was 6.7% in March 2014, the same as in December 2013, based on data from the U.S. Bureau of Labor Statistics. An average of approximately 190,000 monthly net new jobs (non-farm) were added to the economy during the first quarter of 2014, which shows evidence of a slow, but steady positive trend for the economy and the labor market. The average interest rate on new 30-year fixed-rate conforming mortgages largely held steady over the past two quarters, averaging 4.29% during the fourth quarter of 2013 and 4.36% during the first quarter of 2014, based on our weekly Primary Mortgage Market Survey. This compares with the first quarter of 2013, when the average rate on new 30-year fixed-rate conforming mortgages was 3.50%. Higher mortgage interest rates in recent periods, including the first quarter of 2014, contributed to a relatively low volume of single-family refinance mortgage activity in the market during the first quarter of 2014.

Single-Family Housing Market

Although home prices increased on a national basis in the first quarter of 2014 (based on our index), the single-family housing market continued to be affected by weakness in the employment market and a significant inventory of seriously delinquent loans and REO properties in the market.

Based on data from the National Association of Realtors, sales of existing homes in the first quarter of 2014 were 4.60 million (on a seasonally-adjusted annual basis), declining 7% from 4.94 million in the fourth quarter of 2013. Based on data from the U.S. Census Bureau and HUD, sales of new homes in the first quarter of 2014 were approximately 434,000 (on a seasonally-adjusted annual basis), declining 3% from approximately 446,000 in the fourth quarter of 2013. Home prices increased during the first quarter of 2014, with our nationwide index registering approximately a 1.2% increase from December 2013 through March 2014 and a 7.5% increase from March 2013 to March 2014. Despite these increases, our national home price index reflects a cumulative decline of 14.7% since June 2006. These estimates were based on our own price index of mortgage loans on one-family homes funded by us or Fannie Mae. Other indices of home prices may have different results, as they are determined using different pools of mortgage loans and calculated under different conventions than our own.

Multifamily Housing Market

The multifamily market continued to experience positive trends during the first quarter of 2014. The most recent preliminary data reported by Reis, Inc. indicated that the national apartment vacancy rate was 4.0% during the first quarter of 2014, representing the lowest level since 2001. In addition, Reis, Inc. reported that effective rents grew by 0.6% during the first quarter of 2014. Vacancy rates and effective rents are important to loan performance because multifamily loans are generally repaid from the cash flows generated by the underlying property and these factors significantly influence those cash flows. According to the latest information available from Moody's Analytics, Inc. and Real Capital Analytics, Inc., apartment prices continued to increase at the national level in the first quarter of 2014 and are now higher than the peak values observed in 2007. As a result, the multifamily sector continued to experience strong investor interest and continued to outperform most other commercial real estate sectors in the first quarter of 2014.

Outlook

Forward-looking statements involve known and unknown risks and uncertainties, some of which are beyond our control. These statements are not historical facts, but rather represent our expectations based on current information, plans, judgments, assumptions, estimates, and projections. Actual results may differ significantly from those described in or implied by such forward-looking statements due to various factors and uncertainties. For example, a number of factors could cause the actual performance of the housing and mortgage markets and the U.S. economy in the near term to be significantly worse than we expect, including adverse changes in national or international economic conditions and changes in the federal government’s fiscal or monetary policies. See “FORWARD-LOOKING STATEMENTS” for additional information.

Although national home prices have increased in recent periods, home prices at March 31, 2014 remained significantly below their peak levels in many geographical areas. Declines in the market’s inventory of vacant housing have supported stabilization and increases in home prices in a number of metropolitan areas. We believe that home prices will not continue at the same growth rate experienced in 2013, but will continue to gradually moderate during the remainder of 2014 and will return towards growth rates that are consistent with long-term historical averages (approximately 2 to 5 percent growth on an annual basis). To the extent a large volume of loans completes the foreclosure process in a short period, the resulting increase in the market’s inventory of homes for sale could have a negative effect on home prices.

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Single-Family

We continue to expect key macroeconomic drivers of the economy, such as income growth, employment, and inflation, will affect the performance of the housing and mortgage markets during the remainder of 2014. Since we expect that economic growth will continue and mortgage interest rates will remain relatively low compared to historical levels, but trend slowly upward during the remainder of 2014, we believe that housing affordability will remain relatively high in most metropolitan housing markets during the remainder of 2014 for potential home buyers. We expect that the volume of home sales in 2014 will likely remain at about the same level as in 2013. Important factors that we believe will continue to negatively affect single-family housing demand are the relatively high unemployment rate and relatively modest family income growth.

We expect the UPB of our single-family credit guarantee portfolio will be relatively unchanged at the end of 2014 compared to the end of 2013, as an expected decline in purchase volume is expected to be offset by a decline in prepayments. We expect 2014 mortgage origination volumes, including refinancings, to be at the lowest level since 2000. Our loan purchase activity in the first quarter of 2014 declined to $49.2 billion in UPB compared to $131.9 billion in UPB during the first quarter of 2013. Our expectation is for this trend to continue in the remainder of 2014 as refinancing volumes continue to decline. During the first quarter of 2014, refinancings, including HARP, comprised approximately 53% of our single-family purchase and issuance volume compared with 84% in the first quarter of 2013. We expect HARP activity to continue to decline during the remainder of 2014 since the pool of borrowers eligible to participate in the program has declined and mortgage interest rates moved higher in recent periods.

Our charge-offs declined significantly during the first quarter of 2014 compared to the first quarter of 2013. We expect our charge-offs and credit losses to continue to be lower than the level we experienced in 2013 but to remain elevated in the remainder of 2014 in part due to the substantial number of delinquent and underwater mortgage loans in our single-family credit guarantee portfolio that will likely be resolved. For the near term, we also expect:

- REO disposition and short sale severity ratios to remain high. However, our recovery rates have been positively affected by recent improvements in home prices and home sales; and
- The number of seriously delinquent loans and the volume of our loan workouts to continue to decline.

Our guarantee fee rate charged on new acquisitions is significantly higher than that of our Legacy single-family books as a result of two across-the-board increases in guarantee fees implemented in 2012. In December 2013, FHFA directed us to make additional changes to our management and guarantee fee rates in 2014. In January 2014, FHFA announced it was delaying the implementation of these changes. FHFA may direct us to implement further changes in our guarantee fees in the future.

Multifamily

We expect that, at the national level, new supply of multifamily housing will not significantly exceed market demand in the near term due to constraints, such as rising construction costs. We expect that demand growth, driven by a strengthening economy and positive demographics, will generally be sufficient for the increase in supply. However, there may be certain local markets where new supply may outpace demand, which would be evidenced by excess supply and rising vacancy rates. As multifamily market fundamentals improved in recent years, other market participants increased their activities in the multifamily market. As a result, we face increased competition and we believe that our portion of new business in the multifamily market will not increase during the full-year 2014 compared to the level in 2013.

As a result of the positive market fundamentals and continuing strong portfolio performance, we expect our credit losses and delinquency rates to remain low during the remainder of 2014. We believe the long-term outlook for the national multifamily market continues to be favorable as strong demand will support healthy cash flows for multifamily properties.

Limits on Investment Activity and Our Mortgage-Related Investments Portfolio

Our mortgage-related investments portfolio consists of agency securities, single-family non-agency mortgage-related securities, CMBS, housing revenue bonds, and single-family and multifamily unsecuritized mortgage loans. Our ability to acquire and sell mortgage assets is significantly constrained by limitations under the Purchase Agreement and those imposed by FHFA. Under the Purchase Agreement and FHFA regulation, the UPB of our mortgage-related

investments portfolio is subject to a cap that decreases by 15% each year until the portfolio reaches $250 billion. FHFA has indicated that such portfolio reduction targets should be viewed as minimum reductions and has encouraged us to reduce the mortgage-related investments portfolio at a faster rate than required, while indicating that the pace of reducing the portfolio may be moderated by conditions in the housing and financial markets. The reduction in the mortgage-related investments portfolio will result in a decline in income from this portfolio over time.
The table below presents the UPB of our mortgage-related investments portfolio, for purposes of the limit imposed by the Purchase Agreement and FHFA regulation.

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Table 2 — Mortgage-Related Investments Portfolio[1]

	March 31, 2014	December 31, 2013
	(in millions)	
Investments segment — Mortgage investments portfolio	$312,613	$331,071
Single-family Guarantee segment — Single-family unsecuritized mortgage loans[2]	34,825	37,726
Multifamily segment — Mortgage investments portfolio	86,960	92,227
Total mortgage-related investments portfolio	$434,398	$461,024
Mortgage-related investments portfolio cap[3]	$469,625	$552,500

(1) Based on UPB.
(2) Represents unsecuritized seriously delinquent single-family loans.
(3) Represents the portfolio cap as discussed above at December 31, 2014 and 2013, respectively.

The UPB of our mortgage-related investments portfolio at March 31, 2014 was $434.4 billion, a decline of 23% on an annualized basis, compared to $461.0 billion at December 31, 2013. We evaluate the liquidity of the assets in our mortgage-related investments portfolio based on two categories: (a) single-class and multiclass agency securities; and (b) assets that are less liquid than agency securities. The reduction in UPB resulted primarily from liquidations (i.e., principal repayments).

During the first quarter of 2014, the UPB of our less liquid assets declined $13.1 billion and collectively represented approximately 61% of the UPB of the portfolio at March 31, 2014 compared to 60% at December 31, 2013. Assets that we consider to be less liquid than agency securities include unsecuritized performing single-family mortgage loans, multifamily mortgage loans, CMBS, housing revenue bonds, unsecuritized seriously delinquent and modified single-family mortgage loans which we removed from PC trusts, and our investments in non-agency mortgage-related securities backed by subprime, option ARM, and Alt-A and other loans. During the first quarter of 2014, we sold $2.4 billion of assets (excluding sales of: (a) multifamily held-for-sale loans; and (b) single-family loans purchased for cash) that are less liquid than agency securities.

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SELECTED FINANCIAL DATA

The selected financial data presented below should be reviewed in conjunction with MD&A and our consolidated financial statements and related notes.

Table 3 — Selected Financial Data[1]

	Three Months Ended March 31, 2014	2013
	(dollars in millions, except share-related amounts)	
Statements of Comprehensive Income Data		
Net interest income	$3,510	$4,265
(Provision) benefit for credit losses	(85)	503
Non-interest income (loss)	3,111	402
Non-interest expense	(771)	(624)
Income tax (expense) benefit	(1,745)	35
Net income	4,020	4,581
Comprehensive income	4,499	6,971
Loss attributable to common stockholders[2]	(479)	(2,390)
Loss per common share – basic and diluted	(0.15)	(0.74)
Cash dividends per common share	—	—
Weighted average common shares outstanding (in millions) – basic and diluted[3]	3,237	3,239

	March 31, 2014	December 31, 2013
	(dollars in millions)	
Balance Sheets Data		
Mortgage loans held-for-investment, at amortized cost by consolidated trusts (net of allowances for loan losses)	$1,533,106	$1,529,905
Total assets	1,921,538	1,966,061
Debt securities of consolidated trusts held by third parties	1,446,477	1,433,984
Other debt	453,848	506,767
All other liabilities	14,314	12,475
Total Freddie Mac stockholders' equity	6,899	12,835
Portfolio Balances[4]		
Mortgage-related investments portfolio	$434,398	$461,024
Total Freddie Mac mortgage-related securities[5]	1,595,933	1,592,511
Total mortgage portfolio[6]	1,903,507	1,914,661
TDRs on accrual status[7]	80,725	78,708
Non-accrual loans[7]	39,764	43,469

	Three Months Ended March 31, 2014	2013
Ratios[8]		
Return on average assets[9]	0.8 %	0.9 %
Allowance for loans losses as percentage of mortgage loans, held-for-investment[10]	1.4	1.7
Equity to assets ratio[11]	0.5	0.5

(1) See "NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES" in our 2013 Annual Report and in this Form 10-Q for information regarding our accounting policies and the impact of new accounting policies on our

consolidated financial statements.

(2) For a discussion of how the senior preferred stock dividend is determined and how it affects net income (loss) attributable to common stockholders, see "NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES — Earnings Per Common Share" in our 2013 Annual Report.

(3) Includes the weighted average number of shares that are associated with the warrant for our common stock issued to Treasury as part of the Purchase Agreement, because it is unconditionally exercisable by the holder at a cost of $0.00001 per share.

(4) Based on UPB.

(5) See ''Table 25 — Freddie Mac Mortgage-Related Securities'' for the composition of this line item.

(6) See ''Table 10 — Composition of Segment Mortgage Portfolios and Credit Risk Portfolios'' for the composition of our total mortgage portfolio.

(7) Based on UPB of the mortgage loans.

(8) The dividend payout ratio on common stock is not presented because the amount of cash dividends per common share is zero for all periods presented. The return on common equity ratio is not presented because the simple average of the beginning and ending balances of total stockholders' equity, net of preferred stock (at redemption value) is less than zero for all periods presented.

(9) Ratio computed as net income (loss) divided by the simple average of the beginning and ending balances of total assets.

(10) Ratio computed as the allowance for loan losses divided by the total recorded investment of held-for-investment mortgage loans.

(11) Ratio computed as the simple average of the beginning and ending balances of total stockholders' equity divided by the simple average of the beginning and ending balances of total assets.

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CONSOLIDATED RESULTS OF OPERATIONS

The following discussion of our consolidated results of operations should be read in conjunction with our consolidated financial statements, including the accompanying notes. Also see "CRITICAL ACCOUNTING POLICIES AND ESTIMATES" in our 2013 Annual Report for information concerning certain significant accounting policies and estimates applied in determining our reported results of operations.

Table 4 — Summary Consolidated Statements of Comprehensive Income

	Three Months Ended March 31,	
	2014	2013
	(in millions)	
Net interest income	$3,510	$4,265
(Provision) benefit for credit losses	(85)	503
Net interest income after (provision) benefit for credit losses	3,425	4,768
Non-interest income (loss):		
Gains (losses) on extinguishment of debt securities of consolidated trusts	12	34
Gains (losses) on retirement of other debt	7	(32)
Derivative gains (losses)	(2,351)	375
Impairment of available-for-sale securities:		
Total other-than-temporary impairment of available-for-sale securities	(331)	(21)
Portion of other-than-temporary impairment recognized in AOCI	(33)	(22)
Net impairment of available-for-sale securities recognized in earnings	(364)	(43)
Other gains (losses) on investment securities recognized in earnings	766	(276)
Other income (loss)	5,041	344
Total non-interest income (loss)	3,111	402
Non-interest expense:		
Administrative expenses	(468)	(432)
REO operations income (expense)	(59)	(6)
Temporary Payroll Tax Cut Continuation Act of 2011 expense	(178)	(93)
Other expenses	(66)	(93)
Total non-interest expense	(771)	(624)
Income before income tax (expense) benefit	5,765	4,546
Income tax (expense) benefit	(1,745)	35
Net income	4,020	4,581
Other comprehensive income (loss), net of taxes and reclassification adjustments:		
Changes in unrealized gains (losses) related to available-for-sale securities	427	2,280
Changes in unrealized gains (losses) related to cash flow hedge relationships	52	90
Changes in defined benefit plans	—	20
Total other comprehensive income (loss), net of taxes and reclassification adjustments	479	2,390
Comprehensive income	$4,499	$6,971

Net Interest Income

The table below presents an analysis of net interest income, including average balances and related yields earned on assets and incurred on liabilities.

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Table 5 — Net Interest Income/Yield and Average Balance Analysis

	Three Months Ended March 31,					
	2014			2013		
	Average Balance[1]	Interest Income (Expense)	Average Rate	Average Balance[1]	Interest Income (Expense)	Average Rate
	(dollars in millions)					
Interest-earning assets:						
Cash and cash equivalents	$19,641	$—	— %	$35,436	$7	0.07 %
Federal funds sold and securities purchased under agreements to resell	48,155	5	0.05	35,925	11	0.13
Mortgage-related securities:						
Mortgage-related securities[2]	271,646	2,607	3.84	328,241	3,417	4.16
Extinguishment of PCs held by Freddie Mac	(116,588)	(1,097)	(3.77)	(122,280)	(1,262)	(4.13)
Total mortgage-related securities, net	155,058	1,510	3.90	205,961	2,155	4.19
Non-mortgage-related securities[2]	5,870	—	0.02	14,980	2	0.06
Mortgage loans held by consolidated trusts[3]	1,532,416	14,484	3.78	1,495,202	14,504	3.88
Unsecuritized mortgage loans[3]	178,220	1,662	3.73	219,067	2,009	3.67
Total interest-earning assets	$1,939,360	$17,661	3.64	$2,006,571	$18,688	3.73
Interest-bearing liabilities:						
Debt securities of consolidated trusts including PCs held by Freddie Mac	$1,547,682	$(13,340)	(3.45)	$1,518,006	$(13,292)	(3.50)
Extinguishment of PCs held by Freddie Mac	(116,588)	1,097	3.77	(122,280)	1,262	4.13
Total debt securities of consolidated trusts held by third parties	1,431,094	(12,243)	(3.42)	1,395,726	(12,030)	(3.45)
Other debt:						
Short-term debt	126,521	(41)	(0.13)	119,691	(44)	(0.15)
Long-term debt[4]	348,631	(1,788)	(2.05)	416,520	(2,218)	(2.13)
Total other debt	475,152	(1,829)	(1.54)	536,211	(2,262)	(1.69)
Total interest-bearing liabilities	1,906,246	(14,072)	(2.95)	1,931,937	(14,292)	(2.96)
Expense related to derivatives[5]	—	(79)	(0.02)	—	(131)	(0.03)
Impact of net non-interest-bearing funding	33,114	—	0.05	74,634	—	0.11
Total funding of interest-earning assets	$1,939,360	$(14,151)	(2.92)	$2,006,571	$(14,423)	(2.88)
Net interest income/yield		$3,510	0.72		$4,265	0.85

(1) We calculate average balances based on amortized cost.

(2) Interest income (expense) includes accretion of the portion of impairment charges recognized in earnings where we expect significant increases in cash flows from the impaired securities.

(3) Mortgage loans on non-accrual status, where interest income is generally recognized when collected, are included in average balances.

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

(5) Represents changes in fair value of derivatives in closed cash flow hedge relationships that were previously deferred in AOCI and have been reclassified to earnings as the associated hedged forecasted issuance of debt affects earnings.

Net interest income decreased by $755 million to $3.5 billion for the three months ended March 31, 2014 compared to $4.3 billion for the three months ended March 31, 2013. Net interest yield decreased by 13 basis points to 72 basis points for the three months ended March 31, 2014 compared to 85 basis points for the three months ended March 31, 2013. The decrease in net interest income and net interest yield was primarily due to the negative impact of the reduction in the balance of higher-yielding mortgage-related assets due to continued liquidations. Excluding the impact of the legislated 10 basis point increase in guarantee fees, which was implemented in April 2012, net interest income decreased by $835 million for the three months ended March 31, 2014 compared to the three months ended March 31, 2013. Net interest income includes $172 million and $91 million for the three months ended March 31, 2014 and 2013, respectively, related to this increase in guarantee fees.

We recognize interest income on non-accrual mortgage loans only when cash payments are received. We refer to the interest income that we do not recognize as foregone interest income (i.e., interest income we would have recorded if the loan had been current in accordance with its terms). Foregone interest income and reversals of previously recognized interest income, net of cash received, related to non-accrual mortgage loans was $0.4 billion and $0.6 billion during the three months ended March 31, 2014 and 2013, respectively. These amounts have declined primarily because of the reduction in the number of loans on non-accrual status.

The objectives set for us under our charter and conservatorship, restrictions in the Purchase Agreement and restrictions imposed by FHFA have negatively impacted, and will continue to negatively impact, our net interest income. For example, our mortgage-related investments portfolio is subject to a cap that decreases by 15% each year until the portfolio reaches $250 billion. This decline in asset balances will cause a reduction in our interest income from this portfolio over time. For more information on the various restrictions and limitations on our investment activity and our mortgage-related investments portfolio, see “BUSINESS — Conservatorship and Related Matters — Limits on Investment Activity and Our Mortgage-Related Investments Portfolio” in our 2013 Annual Report.

During the three months ended March 31, 2014, we had sufficient access to the debt markets. For more information, see “LIQUIDITY AND CAPITAL RESOURCES — Liquidity.”

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(Provision) Benefit for Credit Losses

We maintain loan loss reserves at levels we believe are appropriate to absorb probable incurred losses on mortgage loans held-for-investment and loans underlying our financial guarantees. Our loan loss reserves are increased through the provision for credit losses and are reduced by net charge-offs. The provision for credit losses primarily reflects our estimate of incurred losses for newly impaired loans as well as changes in our estimates of incurred losses for previously impaired loans. Assuming that all other factors remain the same, home price growth can reduce the likelihood that loans will default and may also reduce the amount of credit losses on the loans that do default.

Our (provision) benefit for credit losses was $(0.1) billion in the first quarter of 2014 compared to $0.5 billion in the first quarter of 2013. The provision for credit losses in the first quarter of 2014 reflects incurred losses associated with newly delinquent loans that were partially offset by moderate home price growth. The benefit for credit losses in the first quarter of 2013 reflects a more significant increase in home prices that was partially offset by incurred losses associated with newly delinquent loans.

Our provision for credit losses in the first quarter of 2014 also reflects $0.3 billion of benefit related to settlement agreements with certain sellers to release specified loans from certain repurchase obligations in exchange for one-time cash payments primarily associated with our Legacy single-family books. However, we do not expect future settlement agreements with seller/servicers to have a significant effect on our financial results.

Our provision for credit losses and amount of charge-offs in the future will be affected by a number of factors, including: (a) the actual level of mortgage defaults, including default rates among borrowers that participated in HARP and HAMP; (b) the effect of the MHA Program, the servicing alignment initiative, and other current and future loss mitigation efforts; (c) any government actions or programs that affect the ability of borrowers to refinance underwater mortgages or obtain modifications; (d) changes in property values; (e) regional economic conditions, including unemployment rates; (f) additional delays in the foreclosure process; and (g) third-party mortgage insurance coverage and recoveries.

During the first quarter of 2014, our charge-offs, net of recoveries for single-family loans, were significantly lower than those recorded in the first quarter of 2013 primarily due to: (a) lower volumes of foreclosures and foreclosure alternatives; and (b) improvements in home prices in many of the areas in which we have had significant foreclosure and short sale activity. Our recoveries in the first quarters of 2014 and 2013 included approximately $0.4 billion and $0.3 billion, respectively, related to repurchase requests from our seller/servicers (including $0.3 billion in the first quarter of 2014 with respect to settlement agreements related to repurchase requests from certain sellers). We continue to experience a high volume of foreclosures and foreclosure alternatives as compared to periods prior to 2008. As a result, we expect our credit losses will continue to remain elevated during the remainder of 2014 even if the volume of new seriously delinquent loans continues to decline.

The total number of single-family seriously delinquent loans declined approximately 8% and 7% during the first quarters of 2014 and 2013, respectively. As of March 31, 2014 and March 31, 2013, the UPB of our single-family loans classified as TDRs was $98.7 billion and $90.0 billion, respectively. However, these amounts include $80.1 billion and $68.5 billion, respectively, of single-family TDRs that were no longer seriously delinquent. Loans that have been classified as TDRs remain categorized as such throughout the remaining life of the loan regardless of whether the borrower makes payments which return the loan to a current payment status. See “RISK MANAGEMENT — Credit Risk — Mortgage Credit Risk” for further information on our single-family credit guarantee portfolio, including credit performance, seriously delinquent loans, charge-offs, REO assets, our loan loss reserves balance, TDRs, and non-accrual loans.

Non-Interest Income (Loss)

Gains (Losses) on Extinguishment of Debt Securities of Consolidated Trusts

During the three months ended March 31, 2014 and 2013, we extinguished debt securities of consolidated trusts with a UPB of $7.9 billion and $5.9 billion, respectively (representing our purchase of single-family PCs with a corresponding UPB amount). Purchases of single-family PCs increased in 2014 primarily due to investment opportunities. See “Table 18 — Mortgage-Related Securities Purchase Activity” for additional information regarding purchases of mortgage-related securities, including those issued by consolidated PC trusts.

Gains (Losses) on Retirement of Other Debt

Gains (losses) on retirement of other debt were $7 million and $(32) million during the three months ended March 31, 2014 and 2013, respectively. We recognized gains on the retirement of other debt during the three months ended March 31, 2014 primarily as a result of exercising our call option for other debt held at premiums. We recognized losses on the retirement of other debt during the three months ended March 31, 2013 primarily due to the repurchase of higher-cost other debt securities at premiums. For more information, see "LIQUIDITY AND CAPITAL RESOURCES — Liquidity — Other Debt Securities."

Derivative Gains (Losses)

The table below presents derivative gains (losses) reported in our consolidated statements of comprehensive income. See "NOTE 9: DERIVATIVES — Table 9.2 — Gains and Losses on Derivatives" for information about gains and losses related to specific categories of derivatives. Changes in fair value and interest accruals on derivatives not in hedge accounting

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relationships are recorded as derivative gains (losses) in our consolidated statements of comprehensive income. At March 31, 2014 and December 31, 2013, we did not have any derivatives in hedge accounting relationships; however, there are amounts recorded in AOCI related to closed cash flow hedges. Amounts recorded in AOCI associated with these closed cash flow hedges are reclassified to earnings when the forecasted transactions affect earnings. If it is probable that the forecasted transaction will not occur, then the deferred gain or loss associated with the forecasted transaction is reclassified into earnings immediately.

While derivatives are an important aspect of our strategy to manage interest-rate risk, they could increase the volatility of reported net income because, while fair value changes in derivatives from fluctuations in interest rates and yield curves affect net income, fair value changes in several of the types of assets and liabilities being hedged do not affect net income. Therefore, there can be timing mismatches affecting current period earnings, which may not be reflective of the economics of our business.

Table 6 — Derivative Gains (Losses)

	Derivative Gains (Losses) Three Months Ended March 31,	
	2014	2013
	(in millions)	
Interest-rate swaps	$(1,770)	$1,574
Option-based derivatives[1]	69	(437)
Other derivatives[2]	28	144
Accrual of periodic settlements	(678)	(906)
Total	$(2,351)	$375

(1) Primarily includes purchased call and put swaptions and purchased interest-rate caps and floors.

(2) Primarily includes futures, foreign-currency swaps, commitments, credit derivatives and swap guarantee derivatives. Our last foreign-currency swaps matured in January 2014.

Gains (losses) on derivatives are principally driven by changes in: (a) interest rates and implied volatility; and (b) the mix and balance of products in our derivative portfolio.

During the three months ended March 31, 2014, we recognized a net loss on derivatives of $2.4 billion. We recognized: (a) fair value losses on our pay-fixed swaps of $3.2 billion primarily driven by a decline in longer-term interest rates; and (b) a net loss of $0.7 billion related to the accrual of periodic settlements on interest-rate swaps as we were a net payer on our interest-rate swaps based on the coupons of the instruments. These losses were partially offset by net gains on our receive-fixed swaps of $1.4 billion.

During the three months ended March 31, 2013, we recognized gains on derivatives of $0.4 billion primarily as a result of an increase in longer-term interest rates. We recognized fair value gains on our pay-fixed swaps of $3.9 billion, which were largely offset by: (a) fair value losses on our receive-fixed swaps of $2.3 billion; (b) net losses of $0.9 billion related to the accrual of periodic settlements on interest-rate swaps as we were a net payer on our interest-rate swaps based on the coupons of the instruments; and (c) fair value losses of $0.4 billion on our option-based derivatives resulting from losses on our purchased call swaptions.

Investment Securities-Related Activities

Impairments of Available-For-Sale Securities

We recorded net impairments of available-for-sale securities recognized in earnings, which were related to non-agency mortgage-related securities, of $364 million and $43 million during the three months ended March 31, 2014 and 2013, respectively. During the three months ended March 31, 2014, these impairments were primarily driven by an increase in the population of available-for-sale securities in an unrealized loss position that we intend to sell. The majority of the impairments recognized in earnings from securities where our intent to sell changed relate to a non-agency mortgage-related securities settlement where a counterparty agreed to purchase these securities as part of the settlement. See “CONSOLIDATED BALANCE SHEETS ANALYSIS — Investments in Securities — Mortgage-Related Securities — Other-Than-Temporary Impairments on Available-For-Sale Mortgage-Related Securities,” as well as “NOTE 7: INVESTMENTS IN SECURITIES” and "NOTE 15: CONCENTRATION OF CREDIT

AND OTHER RISKS — Non-Agency Mortgage-Related Security Issuers" for additional information.

Other Gains (Losses) on Investment Securities Recognized in Earnings

Other gains (losses) on investment securities recognized in earnings consists of gains (losses) on trading securities and gains (losses) on sales of available-for-sale securities. With the exception of principal-only securities, our agency securities, classified as trading, were valued at a net premium (i.e., net fair value was higher than UPB) as of March 31, 2014.

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We recognized \$(7) million and \$(377) million related to losses on trading securities during the three months ended March 31, 2014 and 2013, respectively. The losses on trading securities during both periods were primarily due to the movement of securities with unrealized gains towards maturity.

We recognized \$773 million and \$101 million of gains on sales of available-for-sale securities during the three months ended March 31, 2014 and 2013, respectively. The increase in gains during the three months ended March 31, 2014 resulted from increased sales related to our structuring activity.

Other Income (Loss)

The table below summarizes the significant components of other income.

Table 7 — Other Income (Loss)

	Three Months Ended March 31,	
	2014	2013
	(in millions)	
Other income (loss):		
Non-agency mortgage-related securities settlements	\$4,533	\$6
Gains (losses) on mortgage loans	254	9
Recoveries on loans impaired upon purchase[1]	50	74
Guarantee-related income, net[2]	33	90
All other	171	165
Total other income (loss)	\$5,041	\$344

(1) Our recoveries principally relate to impaired loans purchased prior to 2010. Consequently, our recoveries on these loans will generally decline over time.

(2) Most of our guarantee-related income relates to securitized multifamily mortgage loans where we have not consolidated the securitization trusts on our consolidated balance sheets.

Non-Agency Mortgage-Related Securities Settlements

Non-agency mortgage-related securities settlements were \$4.5 billion in the first quarter of 2014 compared to \$6 million in the first quarter of 2013. We had settlements with five counterparties in the first quarter of 2014, while we had one settlement in the first quarter of 2013. For information on the settlements in 2014, see “NOTE 15: CONCENTRATION OF CREDIT AND OTHER RISKS — Non-Agency Mortgage-Related Security Issuers.”

Gains (Losses) on Mortgage Loans

In the first quarters of 2014 and 2013, we recognized gains on mortgage loans of \$254 million and \$9 million, respectively. The substantial majority of these amounts relate to multifamily loans which we designated for securitization and elected to carry at fair value. The gains in the first quarter of 2014 were due to favorable interest rate movements. During the first quarters of 2014 and 2013, we sold \$3.9 billion and \$5.6 billion, respectively, in UPB of multifamily loans primarily through K Certificate transactions.

All Other

All other income includes income recognized from transactional fees, fees assessed to our servicers for technology use and late fees or other penalties, changes in fair value of STACR debt notes, and other miscellaneous income. All other income was \$171 million in the first quarter of 2014 compared to \$165 million in the first quarter of 2013. This slight increase was primarily due to: (a) higher compensatory fees assessed in the first quarter of 2014 on servicers that failed to meet our timelines to complete a foreclosure of a loan; partially offset by (b) fair value losses on STACR debt notes during the first quarter of 2014 (which we began issuing during the third quarter of 2013). We elected the fair value option on STACR debt notes, and recorded fair value losses on these notes during the first quarter of 2014 due to an increase in market prices for these notes.

Non-Interest Expense

The table below summarizes the components of non-interest expense.

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Table 8 — Non-Interest Expense

	Three Months Ended March 31,	
	2014	2013
	(in millions)	
Administrative expenses:		
Salaries and employee benefits	$233	$208
Professional services	138	109
Occupancy expense	13	13
Other administrative expense	84	102
Total administrative expenses	468	432
REO operations (income) expense	59	6
Temporary Payroll Tax Cut Continuation Act of 2011 expense	178	93
Other expenses(1)	66	93
Total non-interest expense	$771	$624

(1) Includes HAMP servicer incentive fees, c