UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended February 28, 2015
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: 1-7102

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION
(Exact name of registrant as specified in its charter)

District of Columbia	52-0891669
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)
20701 Cooperative Way, Dulles, Virginia	20166
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (703) 467-1800

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x 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). Yes x 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.
(Check one): Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x 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 x
The Registrant does not issue capital stock because it is a tax-exempt cooperative.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements defined by the Securities Act of 1933, as amended, and the Exchange Act of 1934, as amended. Forward-looking statements, which are based on certain assumptions and describe our future plans, strategies and expectations, are generally identified by our use of words such as "intend," "plan," "may," "should," "will," "project," "estimate," "anticipate," "believe," "expect," "continue," "potenti and similar expressions, whether in the negative or affirmative. All statements about future expectations or projections, including statements about loan volume, the adequacy of the loan loss allowance, operating income and expenses, leverage and debt-to-equity ratios, borrower financial performance, impaired loans, and sources and uses of liquidity, are forward-looking statements. Although we believe that the expectations reflected in our forward-looking statements are based on reasonable assumptions, actual results and performance could materially differ. Factors that could cause future results to vary from current expectations include, but are not limited to, general economic conditions, legislative changes including those that could affect our tax status, governmental monetary and fiscal policies, demand for our loan products, lending competition, changes in the quality or composition of our loan portfolio, changes in our ability to access external financing, changes in the credit ratings on our debt, valuation of collateral supporting impaired loans, charges associated with our operation or disposition of foreclosed assets, regulatory and economic conditions in the rural electric industry, nonperformance of counterparties to our derivative agreements and the costs and effects of legal or governmental proceedings involving National Rural Utilities Cooperative Finance Corporation ("CFC") or its members. Some of these and other factors are discussed in our annual and quarterly reports previously filed with the U.S. Securities and Exchange Commission ("SEC"). Except as required by law, we undertake no obligation to update or publicly release any revisions to forward-looking statements to reflect events, circumstances or changes in expectations after the date on which the statement is made.

INTRODUCTION

CFC is a member-owned cooperative association incorporated under the laws of the District of Columbia in April 1969. CFC's principal purpose is to provide its members with financing to supplement the loan programs of the Rural Utilities Service ("RUS") of the United States Department of Agriculture ("USDA"). CFC makes loans to its rural electric members so they can acquire, construct and operate electric distribution, generation, transmission and related facilities. CFC also provides its members with credit enhancements in the form of letters of credit and guarantees of debt obligations. As a cooperative, CFC is owned by and exclusively serves its membership, which consists of not-for-profit entities or subsidiaries or affiliates of not-for-profit entities. CFC is exempt from federal income taxes. As a member-owned cooperative, CFC has no publicly held equity securities outstanding. CFC funds its activities primarily through a combination of publicly and privately held debt securities and member investments. As a member-owned cooperative, CFC's objective is not to maximize profit, but rather to offer its members cost-based financial products and services consistent with sound financial management. CFC annually allocates its net earnings, which consist of net income excluding the effect of certain non-cash accounting entries, to (i) a cooperative educational fund, (ii) a members' capital reserve, (iii) a general reserve, if necessary, and (iv) members based on each member's patronage of CFC's loan programs during the year.

Our financial statements include the consolidated accounts of CFC, Rural Telephone Finance Cooperative ("RTFC"), National Cooperative Services Corporation ("NCSC") and certain entities created and controlled by CFC to hold foreclosed assets and accommodate loan securitization transactions. RTFC was established to provide private financing for the rural telecommunications industry. NCSC was established to provide financing to members of CFC and the for-profit and nonprofit entities that are owned, operated or controlled by, or provide significant benefits to Class A, B and C members of CFC. The entities controlled by CFC that hold foreclosed assets include Caribbean

Asset Holdings, LLC (“CAH”) and Denton Realty Partners, LP (“DRP”). CAH is a holding company for various U.S. Virgin Islands, British Virgin Islands and St. Maarten-based telecommunications operating entities that provide local, long-distance and wireless telephone, cable television and internet services to residential and commercial customers. DRP holds a land development loan and limited partnership interests in certain receivables related to a real estate development. Unless stated otherwise, references to “we,”

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"our" or "us" relate to CFC and its consolidated entities. All references to members within this document include members, associates and affiliates of CFC and its consolidated entities.

Management monitors a variety of key indicators to evaluate our business performance. The following MD&A is intended to provide the reader with an understanding of our results of operations, financial condition and liquidity by focusing on changes from period to period in certain key measures used by management to evaluate performance, such as leverage ratios, growth and credit quality metrics. MD&A is provided as a supplement to, and should be read in conjunction with, our unaudited condensed consolidated financial statements and related notes in this Report, the more detailed information contained in our Annual Report on Form 10-K for the fiscal year ended May 31, 2014 ("2014 Form 10-K"), including the risk factors discussed under "Part I—Item 1A. Risk Factors" in our 2014 Form 10-K, and the risk factors under "Part II—Item 1A. Risk Factors" in this Report.

SUMMARY OF SELECTED FINANCIAL DATA

Table 1 provides a summary of selected financial data for the three and nine months ended February 28, 2015 and 2014, and as of February 28, 2015 and May 31, 2014. In addition to financial measures determined in accordance with generally accepted accounting principles in the United States ("GAAP"), management also evaluates performance based on certain non-GAAP measures, which we refer to as "adjusted" measures. Our key non-GAAP metrics consist of adjusted times interest earned ratio ("TIER") and adjusted debt-to-equity ratio. The most comparable GAAP measures are TIER and debt-to-equity ratio, respectively. The primary adjustments we make to calculate these non-GAAP measures consist of (i) adjusting interest expense and net interest income to include the impact of net periodic derivative cash settlements; (ii) adjusting net income, senior debt and total equity to exclude the non-cash impact of the accounting for derivative financial instruments; (iii) adjusting senior debt to exclude the amount that funds CFC member loans guaranteed by the RUS, subordinated deferrable debt and members' subordinated certificates; and (iv) adjusting total equity to include subordinated deferrable debt and members' subordinated certificates. See "Non-GAAP Financial Measures" for a detailed reconciliation of these adjusted measures to the most comparable GAAP measures. We believe our adjusted non-GAAP metrics, which are not a substitute for GAAP and may not be consistent with similarly titled non-GAAP measures used by other companies, provide meaningful information and are useful to investors because the financial covenants in our revolving credit agreements and debt indentures are based on these adjusted metrics.

Table 1: Summary of Selected Financial Data

	Three Months Ended February 28,			Nine Months Ended February 28,		
(Dollars in thousands)	2015	2014	Change	2015	2014	Change
Statement of operations						
Interest income	$238,740	$238,732	—	$711,266	$719,057	(1) %
Interest expense	(156,850)	(163,534)	(4)	(471,677)	(496,464)	(5)
Net interest income	81,890	75,198	9	239,589	222,593	8
Provision for loan losses	(2,304)	(787)	193	3,475	(3,161)	(210)
Fee and other income	5,020	5,702	(12)	19,249	14,983	28
Derivative gains (losses), net [1]	(98,770)	(31,623)	212	(223,209)	43,981	(608)
Results of operations of foreclosed assets[2]	(1,369)	(1,164)	18	(33,059)	(8,482)	290
Operating expenses[3]	(18,008)	(17,183)	5	(54,788)	(54,371)	1
Other non-interest expense	(710)	(1,359)	(48)	(653)	(1,699)	(62)
Income (loss) before income taxes	(34,251)	28,784	(219)	(49,396)	213,844	(123)
Income tax (expense) benefit	55	(243)	(123)	(100)	(2,045)	(95)
Net income (loss)	$(34,196)	$28,541	(220) %	$(49,496)	$211,799	(123) %
Adjusted statement of operations						
Adjusted interest expense[4]	$(178,362)	$(182,322)	(2) %	$(535,054)	$(551,408)	(3) %
Adjusted net interest income[4]	60,378	56,410	7	176,212	167,649	5
Adjusted net income[4]	43,062	41,376	4	110,336	112,874	(2)
Ratios						
Fixed-charge coverage ratio/TIER [5]	—	1.17	NA	—	1.43	NA
Adjusted TIER[4]	1.24	1.23	1 bps	1.21	1.20	1 bps

	As of February 28, 2015	May 31, 2014	Change
Balance sheet			
Cash, investments and time deposits	$769,229	$944,412	(19)%
Loans to members[6]	21,212,092	20,476,642	4
Allowance for loan losses	(53,114)	(56,429)	(6)
Loans to members, net	21,158,978	20,420,213	4
Total assets	22,648,921	22,232,743	2
Short-term borrowings	3,213,860	4,099,331	(22)
Long-term debt	15,861,011	14,513,284	9
Subordinated deferrable debt	400,000	400,000	—
Members’ subordinated certificates	1,526,452	1,612,227	(5)
Total debt outstanding	21,001,323	20,624,842	2
Total liabilities	21,764,417	21,262,369	2
Total equity	884,504	970,374	(9)
Guarantees	987,833	1,064,822	(7)

Ratios

Leverage ratio(7)	25.72	23.01	271	bps
Adjusted leverage ratio(4)	6.41	6.24	17	
Debt-to-equity ratio(8)	24.61	21.91	270	
Adjusted debt-to-equity ratio(4)	6.10	5.90	20	

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— Change is less than one percent or not meaningful.

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(1)Consists of derivative cash settlements and derivative forward value amounts. Derivative cash settlement amounts represent net periodic contractual interest accruals related to derivatives not designated for hedge accounting. Derivative forward value amounts represent changes in fair value during the period, excluding net periodic contractual accruals, related to derivatives not designated for hedge accounting and expense amounts reclassified into income related to the cumulative transition loss recorded in accumulated other comprehensive income ("AOCI") at June 1, 2001 as a result of adoption of the derivative accounting guidance that required derivatives to be reported at fair value on the balance sheet.
(2) Includes non-cash impairment charge of $27 million for the nine months ended February 28, 2015 related to certain identifiable intangible assets and goodwill of CAH.
(3)Consists of salaries and employee benefits and other general and administrative expenses.
(4) See "Non-GAAP Financial Measures" for details on the calculation of these adjusted non-GAAP ratios and the reconciliation to the most comparable GAAP measures.
(5)Calculated based on net income plus interest expense for the period divided by interest expense for the period. The fixed-charge coverage ratios and TIER were the same for the three and nine months ended February 28, 2015 and 2014 because we did not have any capitalized interest during these periods. We reported a net loss of $34 million and $49 million for the three and nine months ended February 28, 2015, respectively; therefore, the TIER for these periods is below 1.00.
(6)Consists of outstanding principal balance of member loans and deferred loan origination costs of $10 million as of both February 28, 2015 and May 31, 2014.
(7)Calculated based on total liabilities and guarantees at period end divided by total equity at period end.
(8)Calculated based on total liabilities at period end divided by total equity at period end.

EXECUTIVE SUMMARY

Our primary objective as a member-owned cooperative lender is to provide cost-based financial products to our rural electric members, while maintaining sound financial results required for investment-grade credit ratings on our debt instruments. Our objective is not to maximize net income; therefore, the rates we charge our member-borrowers reflect our adjusted interest expense plus a spread to cover our operating expenses, a provision for loan losses and earnings sufficient to achieve interest coverage to meet our financial objectives. Our goal is to earn an annual minimum adjusted TIER of 1.10 and to achieve and maintain an adjusted debt-to-equity ratio below 6.00-to-1.

Financial Performance

Reported Results

We reported a net loss of $34 million and TIER below 1.00 for the quarter ended February 28, 2015 ("current quarter"), compared with net income of $29 million and TIER of 1.17 for the quarter ended February 28, 2014 ("prior year quarter"). We reported a net loss of $49 million and TIER below 1.00 for the nine months ended February 28, 2015, compared with net income of $212 million and TIER of 1.43 for the same prior year period. Our debt-to-equity ratio increased to 24.61-to-1 as of February 28, 2015, from 21.91-to-1 as of May 31, 2014. Our reported results for the current quarter and nine months ended February 28, 2015 reflect the impact of significantly higher net derivative losses, which more than offset an increase in net interest income. In addition, our results for the nine months ended February 28, 2015 include a non-cash impairment charge of $27 million related to certain identifiable intangible assets and goodwill of CAH, which resulted in the write down of the carrying value of CAH in the second quarter of fiscal year 2015. We provide additional information on the CAH impairment charge below under "Consolidated Results of Operations" and in "Note 4—Foreclosed Assets."

We expect volatility from period to period in our reported GAAP results due to changes in market conditions that result in periodic fluctuations in the estimated fair value of our derivative instruments, which we mark to market through earnings. As previously noted, we therefore use adjusted non-GAAP measures to evaluate our performance and for compliance with our debt covenants.

Adjusted Non-GAAP Results

Our adjusted net income totaled $43 million and $41 million for the three months ended February 28, 2015 and 2014, respectively, and our adjusted TIER was 1.24 and 1.23, respectively. Our adjusted net income totaled $110 million and $113 million for the nine months ended February 28, 2015 and 2014, respectively, and our adjusted TIER was 1.21 and 1.20, respectively. Our adjusted debt-to-equity ratio increased to 6.10-to-1 as of February 28, 2015, from 5.90-to-1 as of May 31, 2014.

Our adjusted net income for the current quarter and nine months ended February 28, 2015 reflected improvements in our core operations resulting from strategic actions taken to reduce our funding costs, which generated higher adjusted net interest income as the reduction in our average debt cost more than offset a decrease in the average yield on our interest-earning assets. Our adjusted results for the nine months ended February 28, 2015 also include the favorable impact of higher fee and other non-interest income and a reduction in the allowance for loan losses, which resulted in a negative provision for loan losses for the nine months ended February 28, 2015. The decrease in adjusted net income during the nine months ended February 28, 2015 from the same prior year period was driven by the CAH impairment charge of $27 million recorded in the second quarter of 2015, which more than offset the favorable impact from the improvement in our core operations.

Lending Activity

Total loans outstanding, which consists of the unpaid principal balance and excludes deferred loan origination costs, was $21,202 million as of February 28, 2015, an increase of $735 million, or 4%, from May 31, 2014. The increase was primarily due to an increase in CFC distribution and power supply loans of $740 million and $162 million, respectively, which was attributable to members refinancing with us loans issued by other lenders and member advances for capital investments. This increase was partially offset by a decrease in NCSC loans of $112 million and a decrease in RTFC loans of $48 million.

CFC had long-term fixed-rate loans totaling $1,026 million that repriced during the nine months ended February 28, 2015. Of this total, $862 million repriced to a new long-term fixed rate; $100 million repriced to a long-term variable rate; and $64 million were repaid in full.

Funding Activity

Our debt volume generally increases and decreases in response to member loan demand. As outstanding loan balances increased during the nine months ended February 28, 2015, our debt volume also increased. Total debt outstanding was $21,001 million as of February 28, 2015, an increase of $376 million, or 2%, from May 31, 2014. The increase reflected the issuance of $300 million aggregate principal amount of collateral trust bonds in November 2014 and $900 million in January 2015, which was partially offset by a $789 million reduction in our dealer commercial paper as part of our strategy to reduce our short-term wholesale funding risk. Significant funding-related developments during the current quarter are discussed below.

On January 27, 2015, we issued $400 million aggregate principal amount of 2.00% collateral trust bonds due 2020 and $500 million of aggregate principal amount of 2.85% collateral trust bonds due 2025. We used these funds to reduce our outstanding dealer commercial paper, which totaled $1,974 million as of May 31, 2014, to $1,185 million as of February 28, 2015.

On January 8, 2015, the commitment amount under the revolving note purchase agreement with Farmer Mac was increased by $600 million to $4,500 million, and the draw period was extended by four years to January 11, 2020.

During fiscal year 2014, the CFC Board of Directors authorized management to execute the call of the outstanding $387 million of 7.5% member capital securities and offer members the option to invest in a new series of member capital securities that currently have a 5% interest rate. As of February 28, 2015, all $387 million of the 7.5% member capital securities had been redeemed. Members invested $219 million in the new series of member capital securities as of February 28, 2015.

On January 20, 2015, subsequent to our significant reduction in outstanding dealer commercial paper to manage our short-term wholesale funding risk, S&P restored CFC’s outlook to “stable” from “negative.” CFC’s rating outlook by both

S&P and Moody’s was stable as of April 10, 2015 and February 28, 2015. Below we discuss our expectations for the next 12 months and actions we believe will help maintain our stable ratings outlook.

Outlook for the Next 12 Months

We expect the amount of new long-term loan advances to exceed scheduled loan repayments over the next 12 months. We anticipate a continued increase in earnings from our core lending operations over the next 12 months based on our expectation of an increase in long-term loans outstanding.

As of February 28, 2015, we had $1,703 million of long-term debt scheduled to mature over the next 12 months. We believe that we have sufficient liquidity from the combination of existing cash and time deposits, member loan repayments, committed loan facilities and our ability to issue debt in the capital markets, to our members and in private placements, to meet the demand for member loan advances and satisfy our obligations to repay long-term debt maturing over the next 12 months. As of February 28, 2015, we had $684 million in cash and time deposits, up to $750 million available under committed loan facilities from the Federal Financing Bank, $3,418 million available under committed revolving lines of credit with a syndicate of banks and, subject to market conditions, up to $2,580 million available under a revolving note purchase agreement with Farmer Mac. We also have the ability to issue collateral trust bonds and medium-term notes in the capital markets and medium-term notes to members.

We believe we can continue to roll over the member outstanding short-term debt of $2,029 million as of February 28, 2015, based on our expectation that our members will continue to reinvest their excess cash in our commercial paper, daily liquidity fund and select notes. We believe we can also continue to roll over our dealer commercial paper of $1,185 million as of February 28, 2015. We intend to manage our short-term wholesale funding risk by maintaining our dealer commercial paper within an approximate range between $1,000 million and $1,250 million for the foreseeable future. We expect to continue to be in compliance with the covenants under our revolving credit agreements, which will allow us to mitigate our roll-over risk as we can draw on these facilities to repay dealer or member commercial paper that cannot be rolled over due to potential adverse changes in market conditions.

Our goal is to maintain the adjusted debt-to-equity ratio at or below 6.00-to-1. However, because of the increase in outstanding loan balances during the third quarter of fiscal 2015 and the expected further increase during the remainder of the fiscal year, we anticipate additional borrowings to support our loan growth. As a result, our adjusted debt-to-equity ratio will likely continue to be higher than 6.00-to-1 in the near term.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with GAAP requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expenses in the consolidated financial statements. Understanding our accounting policies and the extent to which we use management judgment and estimates in applying these policies is integral to understanding our financial statements. We provide a discussion of our significant accounting policies under “Note 1—General Information and Accounting Policies” in our 2014 Form 10-K.

We have identified the allowance for loan losses and fair value as our most critical accounting policies because they require significant judgments and assumptions about highly complex and inherently uncertain matters and the use of reasonably different estimates and assumptions could have a material impact on our reported results of operations or financial condition. We evaluate our critical accounting estimates and judgments on an ongoing basis and update them, as necessary, based on changing conditions. Management has discussed our critical accounting policies and estimates with the Audit Committee of the Board of Directors. We provide information on the methodologies and key assumptions used in our critical accounting policies and estimates under “MD&A—Critical Accounting Policies and Estimates” in our 2014 Form 10-K.

ACCOUNTING CHANGES AND DEVELOPMENTS

See “Note 1—Summary of Significant Accounting Policies” for information on accounting standards adopted during the nine months ended February 28, 2015, as well as recently issued accounting standards not yet required to be adopted and the expected impact of these accounting standards. To the extent we believe the adoption of new accounting standards has had or will have a material impact on our results of operations, financial condition or liquidity, we discuss the impacts in the applicable section(s) of MD&A.

CONSOLIDATED RESULTS OF OPERATIONS

The section below provides a comparative discussion of our condensed consolidated results of operations for the three and nine months ended February 28, 2015 and 2014. Following this section, we provide a comparative analysis of our condensed consolidated balance sheets as of February 28, 2015 and May 31, 2014. You should read these sections together with our

"Executive Summary—Outlook for the Next 12 Months" where we discuss trends and other factors that we expect will affect our future results of operations.

Net Interest Income

Net interest income represents the difference between the interest income and applicable fees earned on our interest-earning assets, which include loans and investment securities, and the interest expense on our interest-bearing liabilities. Our net interest yield represents the difference between the yield on our interest-earning assets and the cost of our interest-bearing liabilities plus the impact from non-interest bearing funding. We expect net interest income and our net interest yield to fluctuate based on changes in interest rates and changes in the amount and composition of our interest-earning assets and interest-bearing liabilities. We do not fund each individual loan with specific debt. Rather, we attempt to minimize costs and maximize efficiency by funding large aggregated amounts of loans.

Table 2 presents our average balance sheets for the three and nine months ended February 28, 2015 and 2014, and for each major category of our interest-earning assets and interest-bearing liabilities, the interest income earned or interest expense incurred, and the average yield or cost. Table 2 also presents non-GAAP adjusted interest expense, adjusted net interest income and adjusted net interest yield, which reflect the inclusion of net periodic derivative cash settlements in interest expense. We provide reconciliations of our non-GAAP adjusted measures to the most comparable GAAP measures under "Non-GAAP Financial Measures."

Table 2: Average Balances, Interest Income/Interest Expense and Average Yield/Cost

	Three Months Ended February 28,					
(Dollars in thousands)	2015			2014		
Assets:	Average Balance	Interest Income/Expense	Average Yield/Cost	Average Balance	Interest Income/Expense	Average Yield/Cost
Long-term fixed-rate loans	$19,134,746	$ 221,856	4.70 %	$18,376,969	$ 220,227	4.86 %
Long-term variable-rate loans	667,788	4,836	2.94	763,410	5,217	2.77
Line of credit loans	1,159,097	6,707	2.35	1,365,352	8,302	2.47
Restructured loans	7,534	—	—	7,584	—	—
Nonperforming loans	1,690	—	—	11,017	—	—
Interest-based fee income[1]	—	2,946	—	—	3,054	—
Total loans	20,970,855	236,345	4.57	20,524,332	236,800	4.68
Cash, investments and time deposits	761,963	2,395	1.27	1,007,430	1,932	0.78
Total interest-earning assets	$21,732,818	$ 238,740	4.46 %	$21,531,762	$ 238,732	4.50 %
Other assets, less allowance for loan losses	597,952			1,007,744		
Total assets	$22,330,770			$22,539,506		