

Federal Home Loan Bank of Chicago
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A
Amendment No. 1

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2009

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 No. 000-51401
FEDERAL HOME LOAN BANK OF CHICAGO
(Exact name of registrant as specified in its charter)

Federally chartered corporation

36-6001019

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

**200 East Randolph Drive
Chicago, IL**

60601

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: **(312) 565-5700**

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 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 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 (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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes No

There were 27,989,683 shares of registrant's capital stock outstanding as of July 31, 2009.

Federal Home Loan Bank of Chicago

Explanatory Note

The Federal Home Loan Bank of Chicago is filing this Form 10-Q/A for the quarter ended June 30, 2009 to reflect the restatement of our Condensed Statement of Cash Flows for the six months ended June 30, 2009. Management became aware of calculation errors in the cash flows from certain derivative and investment activities in the Condensed Statements of Cash Flows which led to an overstatement of “Net cash provided by operating activities” of \$274 million, an understatement of “Net cash provided by investing activities” of \$282 million, and an understatement of “Net cash used in financing activities” of \$8 million for the six months ended June 30, 2009. The restatement does not affect the “Net increase (decrease) in cash and due from banks” and has no impact on our Statement of Condition, Statement of Income and Statement of Capital as presented in the Form 10-Q for the quarter ended June 30, 2009. See the Restatement Note to the Financial Statements for further information related to the restatement.

We have performed a review of subsequent events through February 16, 2010, the date the financial statements were issued, and concluded there were no events or transactions occurring during this period that required the recognition or disclosure in our financial statements. Information not affected by the restatement is unchanged and reflects the disclosures made at the time of the original filing of the Form 10-Q with the Securities and Exchange Commission on August 12, 2009. The following items have been amended as a result of the restatement:

- Part I – Item 1 – Financial Statements
- Part I – Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations – Liquidity, Funding & Capital Resources – Liquidity and Funding – Sources of Funding
- Part I – Item 4T – Controls and Procedures
- Part II – Item 6 – Exhibits

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Federal Home Loan Bank of Chicago

PART I

Item 1. Financial Statements

Statements of Condition (unaudited)

(Dollars in millions, except par value)

	June 30, 2009	December 31, 2008
Assets		
Cash and due from banks	\$ 19	\$ 130
Federal Funds sold and securities purchased under agreement to resell	8,790	1,580
Investment securities -		
Trading (\$82 and \$761 pledged)	1,659	866
Available-for-sale (\$793 and \$546 pledged)	11,095	2,142
Held-to-maturity ¹ (\$1,122 and \$995 pledged)	13,655	16,595
Advances (\$0 and \$201 carried at fair value option)	27,192	38,140
MPF Loans held in portfolio, net of allowance for credit losses (\$9 and \$5)	26,964	32,087
Accrued interest receivable	287	367
Derivative assets	55	102
Software and equipment, net	25	26
Other assets	129	94
Total Assets	\$ 89,870	\$ 92,129
Liabilities and Capital		
Liabilities		
Deposits -		
Interest bearing (\$8 and \$9 from other FHLBs)	\$ 890	\$ 602
Non-interest bearing	296	155
Total deposits	1,186	757
Securities sold under agreements to repurchase	1,200	1,200
Consolidated obligations, net -		
Discount notes	40,286	29,466
Bonds (\$2,116 and \$0 carried at fair value option)	40,999	55,305
Total consolidated obligations, net	81,285	84,771
Accrued interest payable	355	567
Mandatorily redeemable capital stock	426	401
Derivative liabilities	864	1,067
Affordable Housing Program assessment payable	24	23
Resolution Funding Corporation assessment payable	16	-
Investment securities traded but not yet settled	1,759	-
Other liabilities	57	56
Subordinated notes	1,000	1,000
Total Liabilities	88,172	89,842
Commitments and contingencies (Note 15)		
Capital		
Capital stock - putable (\$100 par value per share) issued and outstanding shares - 24 million shares for both periods	2,375	2,386
Retained earnings	837	540
Accumulated other comprehensive income (loss)	(1,514)	(639)
Total Capital	1,698	2,287
Total Liabilities and Capital	\$ 89,870	\$ 92,129

¹ Fair values of held-to-maturity securities: \$13,951 and \$15,728 at June 30, 2009 and December 31, 2008.

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

Federal Home Loan Bank of Chicago

Statements of Income (unaudited)

(In millions)

	Three months ended June 30,		Six months ended June 30,	
	2009	2008	2009	2008
Interest income	\$ 753	\$ 903	\$ 1,541	\$ 1,901
Interest expense	594	881	1,238	1,848
Net interest income before provision for credit losses	159	22	303	53
Provision for credit losses	2	-	5	-
Net interest income	157	22	298	53
Non-interest income (loss) on -				
Total other-than-temporary impairment losses	(244)	-	(1,286)	-
Portion of loss recognized in other comprehensive income	120	-	1,076	-
Net impairment losses ¹	(124)	-	(210)	-
Realized loss on other-than-temporarily-impaired securities ¹	-	(30)	-	(63)
Trading securities	(2)	(15)	(11)	-
Realized net gain (loss) on the sale of available-for-sale securities	-	-	19	-
Derivatives and hedging activities	122	(20)	50	(82)
Instruments held under fair value option	(1)	-	(2)	-
Early extinguishment of debt, incl. losses of \$(5) and \$0 from debt transferred to other FHLBs	-	-	(5)	-
Other, net	3	2	6	4
Total non-interest income (loss)	(2)	(63)	(153)	(141)
Non-interest expense -				
Compensation and benefits	16	18	30	34
Professional service fees	3	5	5	7
Amortization and depreciation of software and equipment	4	4	8	9
Finance Agency/Finance Board and Office of Finance expenses	2	1	3	2
Other expense	4	5	12	12
Total non-interest expense	29	33	58	64
Income (loss) before assessments	126	(74)	87	(152)
Assessments -				
Affordable Housing Program	7	-	7	-
Resolution Funding Corporation	16	-	16	-
Total assessments	23	-	23	-
Net income (loss)	\$ 103	\$ (74)	\$ 64	\$ (152)

¹ Due to adoption of new accounting guidance effective January 1, 2009. See **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations.**

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

Federal Home Loan Bank of Chicago

Statements of Capital (unaudited)

(Dollars and shares in millions)

	Capital Stock - Putable		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Capital
	Shares	Par Value			
Balance December 31, 2007	27	\$ 2,661	\$ 659	\$ (251)	\$ 3,069
Net income (loss)			(152)		(152)
Other comprehensive income (loss) (Note 12)				(11)	(11)
Total comprehensive income (loss)					<u>(163)</u>
Proceeds from issuance of capital stock	-	52			52
Reclassification of capital stock to mandatorily redeemable	<u>(2)</u>	<u>(165)</u>			<u>(165)</u>
Balance June 30, 2008	<u>25</u>	<u>\$ 2,548</u>	<u>\$ 507</u>	<u>\$ (262)</u>	<u>\$ 2,793</u>
Balance December 31, 2008	<u>24</u>	<u>\$ 2,386</u>	<u>\$ 540</u>	<u>\$ (639)</u>	<u>\$ 2,287</u>
January 1, 2009, cumulative effect non-credit impairment adjustment ¹			233	(233)	-
Net income (loss)			64		64
Other comprehensive income (loss) (Note 12)				(642)	(642)
Total comprehensive income (loss)					<u>(578)</u>
Proceeds from issuance of capital stock	1	100			100
Reclassification of capital stock to mandatorily redeemable	<u>(1)</u>	<u>(111)</u>			<u>(111)</u>
Balance June 30, 2009	<u>24</u>	<u>\$ 2,375</u>	<u>\$ 837</u>	<u>\$ (1,514)</u>	<u>\$ 1,698</u>

¹ Due to adoption of new accounting guidance effective January 1, 2009. See Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations.

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

Federal Home Loan Bank of Chicago

Condensed Statements of Cash Flows (unaudited)

(In millions)

Six months ended June 30,		2009	2008
<u>Net cash provided by (used in) operating activities</u>		<u>As Restated</u>	
Operating Activities		\$ (68)	\$ (101)
Investing Activities	Net change in Federal Funds sold and securities purchased under agreements to resell	(7,210)	3,021
	Net change in advances	10,752	(4,432)
	MPF Loans -		
	Principal collected	5,023	2,989
	Purchases, incl. \$0 and \$(9) from other FHLBs	(15)	(2,148)
	Trading securities -		
	Proceeds from maturities, sales and paydowns	303	6
	Purchases	(1,106)	(20)
	Held-to-maturity (HTM) securities -		
	Net proceeds from maturities and purchases on short-term HTM securities ¹	305	(1,036)
	Proceeds from maturities on longer-term HTM securities ²	1,512	741
	Purchases of longer-term HTM securities ²	(12)	(3,274)
	Available-for-sale (AFS) securities -		
	Proceeds from maturities and sales	645	448
	Purchases	(7,778)	(267)
	Proceeds from sale of foreclosed assets	26	18
	Capital expenditures for software and equipment	(4)	(3)
	Net cash provided by (used in) investing activities	<u>2,441</u>	<u>(3,957)</u>
Financing Activities	Net change in deposits, incl. \$(1) and \$(2) from other FHLBs	428	(314)
	Net proceeds from issuance of consolidated obligations -		
	Discount notes	453,155	714,170
	Bonds	3,708	21,041
	Payments for maturing and retiring consolidated obligations -		
	Discount notes	(442,334)	(713,801)
	Bonds, incl. \$(112) and \$0 transferred to other FHLBs	(17,411)	(17,082)
	Net proceeds (payments) on derivative contracts with financing element	(44)	-
	Proceeds from issuance of capital stock	100	52
	Redemptions of mandatorily redeemable capital stock	(86)	(7)
	Net cash provided by (used in) financing activities	<u>(2,484)</u>	<u>4,059</u>
	Net increase (decrease) in cash and due from banks	(111)	1
	Cash and due from banks at beginning of year	130	17
	Cash and due from banks at end of year	<u>\$ 19</u>	<u>\$ 18</u>
Supplemental Disclosures	Interest paid	\$ 1,386	\$ 1,826
	Affordable Housing Program assessments paid	7	11
	Resolution Funding Corporation assessments paid	-	10
	Capital stock reclassified to mandatorily redeemable capital stock	111	165
	Transfer of MPF Loans to real estate owned	45	31

¹ Short-term HTM securities consist of commercial paper that has a maturity of less than 90 days when purchased.

² Longer-term HTM securities consist of securities with maturities of 90 days or more.

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

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Restatement Note

Subsequent to filing our Form 10-Q for the quarter ended September 30, 2009, and as a result of ongoing enhancement to our Statement of Cash Flow preparation process, management became aware of calculation errors in the cash flows from certain derivative and investment activities which led to the misclassification of certain items on our Condensed Statement of Cash Flows for the period. Following review and analysis, it was determined that cash provided by operating activities was overstated, cash provided by investing activities was understated, and cash used in financing activities was understated due to the incorrect classification of the above errors. Therefore, we restated the following components of our Statement of Cash Flows for the six months ended June 30, 2009:

For the six months ended June 30, 2009	<u>As Reported</u>	<u>As Restated</u>
Net cash provided by (used in) operating activities	\$ 206	\$ (68)
Net cash provided by (used in) investing activities		
Net change in advances	10,754	10,752
Purchases of trading securities	(1,101)	(1,106)
Net proceeds from maturities and purchases on short-term HTM securities	300	305
Proceeds from maturities on longer-term HTM securities	1,720	1,512
Proceeds from maturities and sales of AFS securities	636	645
Purchases of AFS securities	(8,261)	(7,778)
Net cash provided by (used in) financing activities		
Net proceeds from issuance of consolidated obligations discount notes	453,166	453,155
Payments for maturing and retiring consolidated obligations bonds, incl. \$(112) transferred to other FHLBs	(17,414)	(17,411)

Note 1 – Background and Basis of Presentation

The Federal Home Loan Bank of Chicago¹ is a federally chartered corporation and one of 12 Federal Home Loan Banks (the FHLBs) that, with the Office of Finance, comprise the Federal Home Loan Bank System (the System). The FHLBs are government-sponsored enterprises (GSE) of the United States of America and were organized under the Federal Home Loan Bank Act of 1932, as amended (FHLB Act), in order to improve the availability of funds to support home ownership. Each FHLB operates as a separate entity with its own management, employees, and board of directors. Each FHLB is a member-owned cooperative with members from a specifically defined geographic district. Our defined geographic district consists of the states of Illinois and Wisconsin.

With the enactment of the Housing and Economic Recovery Act of 2008 (Housing Act), the Federal Housing Finance Agency (FHFA) was established and became the new federal regulator of the FHLBs effective July 30, 2008. On October 27, 2008, the staff of the Federal Housing Finance Board (Finance Board), the federal regulator of the FHLBs prior to the creation of the FHFA, was merged into the FHFA. The Finance Board was abolished on July 29, 2009, one year after enactment of the Housing Act. We remain subject to existing regulations, orders, determinations, and resolutions until new ones are issued or made.

We provide credit to members principally in the form of secured loans called advances. We also provide funding for home mortgage loans to members approved as Participating Financial Institutions (PFIs) through the Mortgage Partnership Finance[®] (MPF[®]) Program².

These programs help us accomplish our mission to deliver value to our members, and promote and support their growth and success, by providing:

- highly reliable liquidity;
- secured advances, wholesale mortgage financing, and other products and services designed to meet members' needs; and
- direct financial support for members' affordable housing and community investment programs.

¹ Unless otherwise specified, references to "we," "us," "our," and "the Bank" are to the Federal Home Loan Bank of Chicago.

² "Mortgage Partnership Finance," "MPF," "MPF Shared Funding," and "eMPF" are registered trademarks of the Federal Home Loan Bank of Chicago. "MPF Xtra" is a trademark of the Federal Home Loan Bank of Chicago.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Note 2 – Summary of Significant Accounting Policies

Basis of Presentation – Our accounting and financial reporting policies conform to generally accepted accounting principles in the United States of America (GAAP). The preparation of the unaudited financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, as well as the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses. Actual results could differ from those estimates. Certain amounts in the prior period have been reclassified to conform to the current presentation. In particular, effective March 31, 2009 we changed the presentation of our statement of cash flows to present net cash flows from operating activities as a single line item as permitted by the Securities and Exchange Commission (SEC) guidance governing interim financial statements. As a result, we also made the change to our prior year statement of cash flows disclosed for comparative purposes in order to have a consistent presentation.

In the opinion of management, all normal recurring adjustments have been included for a fair statement of this interim financial information. Subsequent events have been evaluated through the time of filing on August 12, 2009, which is the time and date that these financial statements have been issued.

These unaudited financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2008, included in our Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC).

Consolidation – We apply consolidation accounting principles to our investments in variable interest entities. Our investments in variable interest entities include MPF Shared Funding securities, investments in mortgage-backed securities (MBS), and investments in Federal Family Education Loan Program (FFELP) student loan asset-backed securities (ABS).

MPF Shared Funding securities are MBS secured by pools of mortgage loans that meet the eligibility requirements of the MPF Program and FHFA regulations. We are a non-transferor investor in the MPF Shared Funding program in that the MPF Shared Funding securities do not contain any assets that were transferred by us. We hold two MPF Shared

Funding securities that were issued by special purpose entities (SPE) that were sponsored by One Mortgage Partners Corp., a subsidiary of JPMorgan Chase. We do not act as servicer for the mortgage loans held by the SPE. The MPF Shared Funding securities are classified as held-to-maturity and are not publicly traded or guaranteed by any FHLB. We do not provide any liquidity or credit support to our investments in MPF Shared Funding securities. Our maximum loss exposure to these MPF Shared Funding securities is limited to the carrying value of these securities.

We hold various senior interests in MBS. We are a non-transferor investor in these MBS, in that the MBS investment does not contain any assets that were transferred from us. We did not sponsor these securities nor are we the servicer. Our MBS are primarily classified as held-to-maturity but some are classified as available-for-sale. We do not provide any liquidity or credit support to our investments in MBS. Our maximum loss exposure to our investments in MBS is limited to the carrying value of these securities.

We also hold various senior interests in FFELP student loan ABS. We are a non-transferor investor in these investments. We did not sponsor these investments nor are we the servicer of the student loans collateralizing these ABS. FFELP student loan ABS are classified as available-for-sale. We do not provide any liquidity or credit support for these investments. Our maximum loss exposure to our investments in FFELP student loan ABS is limited to the carrying value of these securities.

Under consolidation accounting principals, the variable interest holder that is considered the primary beneficiary is responsible for consolidating the variable interest entity. An enterprise is considered the primary beneficiary if that enterprise has a variable interest (or combination of variable interests) that will absorb a majority of the variable interest entity's expected losses, receive a majority of its expected residual returns, or both. We do not consolidate our investments in MPF Shared Funding securities, securitized MBS, and FFELP student loan ABS since we are not the sponsor or the primary beneficiary of these variable interest entities, as we hold the senior, rather than residual, interest in these securities.

Cash Flows – For purposes of the statements of cash flows, we consider cash and due from banks as cash and cash equivalents.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations

Accounting Principles Adopted in 2009:

Other-Than-Temporary Impairments (OTTI)

On April 9, 2009, the FASB released new accounting guidance on the recognition and presentation of OTTI, amending the prior guidance for investment securities classified as available-for-sale (AFS) and held-to-maturity (HTM). The objective of the new guidance is to make OTTI guidance more operational and to improve the presentation and disclosure of OTTI on debt and equity securities in the financial statements. The most significant change to our previous OTTI accounting relates to the amount of OTTI that is recognized into earnings.

Prior to the new guidance, if OTTI was determined to exist, we recognized an OTTI charge into earnings in an amount equal to the entire difference between the security's amortized cost basis and its fair value as of the balance sheet date of the reporting period. Under the new guidance, if OTTI has been incurred, and it is more likely than not that we will not sell the investment security before the recovery of its amortized cost basis, then the OTTI is separated into (a) the amount representing the credit loss and (b) the amount related to all other factors.

On April 28, 2009 and May 7, 2009, the FHFA provided the FHLBs with guidance on the process for determining OTTI with respect to private-label MBS and our adoption of recent FASB guidance governing the accounting for OTTI in the first quarter of 2009. The goal of the FHFA guidance is to promote consistency in the determination of OTTI for private-label MBS among all FHLBs. Recognizing that many of the FHLBs desired to early adopt the FASB OTTI guidance, the FHFA guidance also required that all FHLBs early adopt the FASB OTTI guidance in order to achieve consistency among the 12 FHLBs and to follow certain guidelines for determining OTTI. We adopted the FASB guidance, applied in accordance with the FHFA guidance as further described in **Note 5 – Investment Securities**, effective January 1, 2009.

Cumulative Effect Adjustment Impact

We adopted the new OTTI accounting guidance applied in accordance with the FHFA guidance, effective January 1, 2009. The cumulative effect on retained earnings was calculated using accounting guidance creditors apply when determining the impairment of a loan. See **Note 5 – Investment Securities** for further details.

The following table summarizes the effect on our financial statements. It should be noted that this comparison is limited to the change in accounting principle with respect

to the amount of OTTI that is recognized in the statements of income. This adjustment had no impact on our AHP or REFCORP expense or accruals.

Year ended December 31, 2008 Total OTTI losses	\$ 292
OTTI accreted into income	<u>6</u>
Net OTTI related charges	286
OTTI credit loss portion	<u>53</u>
Increase to beginning retained earnings	<u>\$ 233</u>

Components of January 1, 2009 reclassification -

Charge to AOCI - AFS securities	\$ 56
Charge to AOCI - HTM securities	<u>177</u>
Increase to beginning retained earnings	<u>\$ 233</u>

Regulatory capital amount -

Before cumulative effect adjustment	\$ 4,327
After cumulative effect adjustment	<u>4,560</u>

Regulatory capital ratio -

Before cumulative effect adjustment	4.70%
After cumulative effect adjustment	<u>4.95%</u>

Estimating Fair Value

On April 9, 2009, the FASB released new accounting guidance for determining fair value when the volume and level of activity for the asset or liability has significantly decreased and identifying transactions that are not orderly. This guidance emphasizes that despite significant decreases in volume and level of activity, and regardless of the valuation technique(s) used for the asset or liability, the fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions.

We adopted this new accounting guidance effective January 1, 2009. The guidance had no effect on our financial statements at the time of adoption.

Disclosures about Fair Value

On April 9, 2009, the FASB released new guidance which amended disclosures about fair values of financial instruments to require entities to disclose, among other things, the methods and significant assumptions used to estimate the fair value of financial instruments in both interim and annual financial statements. We adopted the new disclosure guidance effective January 1, 2009. See **Note 14 – Estimated Fair Value** for further details.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Fair Values on Nonfinancial Assets and Liabilities

Pursuant to FASB guidance issued February 12, 2008, we adopted new fair value measurement requirements for nonfinancial assets and nonfinancial liabilities effective January 1, 2009. Examples of nonfinancial assets within the scope of this guidance are long-lived assets or asset groups measured at fair value for an impairment assessment such as real estate owned. At the date of adoption, the new guidance did not have a significant effect on our financial statements. See **Note 14 – Estimated Fair Value** for further details.

Derivative Instruments and Hedging Activities

In March of 2008, the FASB issued new guidance on disclosures about derivative instruments and hedging activities, which amends and expands the previously established derivative instrument disclosure requirements.

This new disclosure guidance requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. We adopted this new guidance effective January 1, 2009. Disclosures were not required retrospectively for prior reporting periods. There was no effect to our financial statements upon initial adoption because this new guidance only addresses disclosure requirements. See **Note 13– Derivatives and Hedging Activities** for further details.

Subsequent Events

On May 28, 2009, the FASB issued new accounting guidance pertaining to subsequent events. The new guidance defines subsequent events as events or transactions that occur after the balance sheet date but before our financial statements are issued or filed with the SEC. There are two types of subsequent events:

- The first type consists of events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. We are required to recognize the effects of these subsequent events in our financial statements as of the balance sheet date; for example, subsequent events affecting the realization of assets such as investment securities may need to be recognized.
- The second type consists of events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date (that is, non-recognized subsequent events). We may be required to disclose the effects of these subsequent events in our SEC filing; for example, if we enter into a significant commitment subsequent to the balance sheet date.

We adopted this new guidance effective June 30, 2009. It requires us to disclose the date for which we have evaluated our subsequent events, which is the date we issue and file with the SEC our financial statements. For this reporting period that is the time of filing on August 12, 2009. At the date of adoption, the new guidance did not have a significant effect on our financial statements.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Transfers of Financial Assets

On June 12, 2009, the FASB issued new accounting guidance on the accounting for transfers of financial assets. The new guidance primarily changes existing guidance as follows:

- Eliminates the scope exception for qualifying special purpose entities thereby requiring a determination as to whether consolidation of such entities is appropriate under consolidation accounting guidance.
- Clarifies that the transferor must consider all arrangements or agreements made contemporaneously with, or in contemplation of, the transfer of financial assets, even if they were not entered into at the time of transfer when determining whether or not the transferor has surrendered control over the transferred financial assets.

This new guidance is applicable only to our transfers of financial assets occurring on or after January 1, 2010. As a result, it has no effect on MPF Loan sales that occur prior to January 1, 2010. Additionally, a determination must be made whether qualifying SPEs, if any, held on or subsequent to January 1, 2010 must be consolidated in accordance with the applicable consolidation accounting guidance. We are still assessing the potential effect the new guidance will have on our operating activities and financial statements.

Variable Interest Entities

On June 12, 2009, the FASB issued new accounting guidance pertaining to consolidating variable interest entities. This new guidance amends existing consolidation accounting principles to require us to perform an analysis to determine whether the enterprise's variable interest or

interests give it a controlling financial interest in a variable interest entity. This analysis identifies the primary beneficiary of a variable interest entity as the enterprise that has both of the following characteristics:

- The power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance.
- The obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity.

This new accounting guidance is effective for us beginning January 1, 2010. Earlier application is prohibited. We are still evaluating the potential implications to our financial statements and operating activities.

FASB Accounting Standards CodificationTM

On July 1, 2009, the FASB issued new accounting guidance pertaining to the accounting standards Codification and the hierarchy of Generally Accepted Accounting Principles. Effective July 1, 2009, the Codification became the single source of authoritative nongovernmental U.S. GAAP. All existing accounting standard documents are superseded. All other accounting literature not included in the Codification will be considered non-authoritative. All guidance contained in the Codification carries an equal level of authority. Any effects of applying the provisions of Codification should be accounted for as a change in accounting principle or correction of an error, as applicable. We do not believe the Codification will have a significant effect on our financials statements.

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Note 4 – Interest Income and Interest Expense

The following table presents interest income and interest expense for the periods indicated:

	Three months ended June 30,		Six months ended June 30,	
	<u>2009</u>	<u>2008</u>	<u>2009</u>	<u>2008</u>
Interest Income -				
Federal Funds sold and securities purchased under agreements to resell	\$ 4	\$ 40	\$ 7	\$ 107
Investment securities -				
Trading	12	10	22	21
Available-for-sale	70	6	94	12
Held-to-maturity	187	155	381	302
Total investment securities	<u>269</u>	<u>171</u>	<u>497</u>	<u>335</u>
Advances	157	278	349	616
MPF Loans held in portfolio	329	422	700	860
Less: Credit enhancement fees paid	(6)	(8)	(12)	(17)
MPF Loans held in portfolio, net	<u>323</u>	<u>414</u>	<u>688</u>	<u>843</u>
Total interest income	<u>753</u>	<u>903</u>	<u>1,541</u>	<u>1,901</u>
Interest Expense -				
Deposits	1	5	1	14
Securities sold under agreements to repurchase	7	12	17	31
Consolidated obligations -				
Discount notes	40	99	82	236
Bonds	532	750	1,110	1,538
Total consolidated obligations	<u>572</u>	<u>849</u>	<u>1,192</u>	<u>1,774</u>
Mandatorily redeemable capital stock	-	-	-	-
Subordinated notes	14	15	28	29
Total interest expense	<u>594</u>	<u>881</u>	<u>1,238</u>	<u>1,848</u>
Net Interest Income before provision for credit losses	<u>159</u>	<u>22</u>	<u>303</u>	<u>53</u>
Provision for credit losses	2	-	5	-
Net interest income	<u>\$ 157</u>	<u>\$ 22</u>	<u>\$ 298</u>	<u>\$ 53</u>

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Note 5 – Investment Securities

For accounting policies concerning our investment securities see Note 7 on page F-12 in our 2008 Form 10-K.

Amortized Cost and Fair Value

The following tables present the amortized cost and fair value of AFS and HTM securities as of the dates indicated.

	Available-for-Sale				Held-to-Maturity					
	As of June 30, 2009	Non-Credit OTTI Recognized in AOCI (Loss)	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Non-Credit OTTI Recognized in AOCI (Loss)	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Non-MBS:										
Government-sponsored enterprises	\$ 287	\$ -	\$ 2	\$ -	\$ 289	\$ 410	\$ -	\$ 21	\$ -	\$ 431
Temporary liquidity guarantee program (FDIC-TLGP)	100	-	*	-	100	-	-	-	-	-
State or local housing agency obligations	-	-	-	-	-	45	-	*	*	45
Small Business Administration / Small Business Investment Companies	778	-	5	(4)	779	256	-	1	-	257
Total non-MBS	1,165	-	7	(4)	1,168	711	-	22	-	733
ABS:										
FFELP student loan ABS	5,083	-	12	-	5,095	-	-	-	-	-
MBS:										
Government-sponsored enterprises residential	4,070	-	63	(21)	4,112	10,262	-	436	-	10,698
Government-guaranteed residential	624	-	3	(1)	626	16	-	1	-	17
MPF Shared Funding	-	-	-	-	-	265	-	-	(12)	253
Private-label residential	167	(83) ¹	121	(2)	94	2,238	(829)	1	(4)	1,406
Private-label home equity	-	-	-	-	-	1,221	(313)	*	(148)	760
Private-label commercial	-	-	-	-	-	84	-	*	*	84
Total MBS	4,861	(83)	78	(24)	4,832	14,086	(1,142)	438	(164)	13,218
Total	11,109	(83)	97	(28)	\$ 11,095	\$ 14,797	(1,142)	\$ 460	(164)	\$ 13,951
Adjustments from amortized cost to carrying value:										
AFS unrealized gains (losses), net	57									(1,142)
Adjustments for non-credit losses	(71)									
Carrying Value on Statements of Condition	\$ 11,095				\$ 11,095			\$ 13,655		

* Less than \$1 million

¹ Net AFS non-credit OTTI charge is \$71 million, consisting of gross losses of \$83 million and subsequent unrealized gains on securities impaired in previous periods of \$12 million.

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As of December 31, 2008	Available-for-Sale				Held-to-Maturity			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Non-MBS:								
Commercial paper	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Government-sponsored enterprises	530	17	-	547	411	21	-	432
State or local housing agency obligations	7	-	-	7	48	-	-	48
Small Business Administration/ Small Business Investment Companies	-	-	-	-	567	3	(1)	569
Total non-MBS	<u>537</u>	<u>17</u>	<u>-</u>	<u>554</u>	<u>1,026</u>	<u>24</u>	<u>(1)</u>	<u>1,049</u>
MBS:								
Government-sponsored enterprises	1,448	36	-	1,484	11,459	306	(17)	11,748
Government-guaranteed	-	-	-	-	17	-	-	17
MPF Shared Funding	-	-	-	-	304	-	(16)	288
Private-label	145	-	(41)	104	3,789	-	(1,163)	2,626
Total MBS	<u>1,593</u>	<u>36</u>	<u>(41)</u>	<u>1,588</u>	<u>15,569</u>	<u>306</u>	<u>(1,196)</u>	<u>14,679</u>
Total	<u>\$ 2,130</u>	<u>\$ 53</u>	<u>\$ (41)</u>	<u>\$ 2,142</u>	<u>\$ 16,595</u>	<u>\$ 330</u>	<u>\$ (1,197)</u>	<u>\$15,728</u>

Realized Other-Than-Temporary Impairment Losses

We adopted new accounting guidance issued by the FASB, as well as guidance from the FHFA, governing the accounting for OTTI effective January 1, 2009 as discussed in **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations**. We perform an assessment of OTTI whenever the fair value of an investment security is less than its amortized cost basis at the balance sheet date. Amortized cost basis includes adjustments made to the cost of a security for accretion, amortization, collection of cash, previous OTTI recognized into earnings (less any cumulative effect adjustments) and fair value hedge accounting adjustments. OTTI is considered to have occurred under the following circumstances:

- If we decide to sell the investment security and its fair value is less than its amortized cost.
- If, based on available evidence, we believe it is more likely than not that we will decide or be required to sell the investment security before the recovery of its amortized cost basis.
- If we do not expect to recover the entire amortized cost basis of the investment security. The difference between the present value of the cash flows expected to be collected and the amortized cost basis represents the amount of credit loss.

Fair Value Write-downs

If OTTI has been incurred and we decide to, or are required to, sell the investment security, we account for

the investment security as if it had been purchased on the measurement date of the OTTI. Specifically, the investment security is written down to fair value resulting in a new amortized cost basis, and any deferred amount in AOCI related to the investment security is written-off. The entire realized loss is recognized in non-interest income (loss). The new amortized cost basis is not changed for subsequent recoveries in fair value. For investments we continue to hold, a new accretible yield is calculated on the impaired security. This is used to calculate the amortization to be recorded into income over the remaining life of the investment security so as to match the amount and timing of future cash flows expected to be collected. This is also re-evaluated quarterly. Subsequent non-OTTI-related increases and decreases (if not an additional OTTI) in the fair value of AFS securities will be included in AOCI.

Credit Loss Only Write-downs

If an OTTI has been incurred, and it is more likely than not that we will not decide to sell or we will not be required to sell the investment security before the recovery of its amortized cost basis, then the OTTI is separated into (a) the amount representing the credit loss and (b) the amount related to all non-credit related factors.

The amount of the total OTTI for a held-to-maturity security that was previously impaired subsequent to initial recognition is determined as the difference between its carrying amount prior to the determination of OTTI and its fair value. The amount of total OTTI for an available-for-sale security that was not previously impaired is determined as the difference between its amortized cost prior to the determination of OTTI and its fair value. The

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amount of total OTTI for an available-for-sale security that was previously impaired is determined as the difference between its carrying amount prior to the determination of OTTI and its fair value. If the fair value of a security is above its carrying value, then no incremental amount is recognized into total OTTI. Credit losses related to previously impaired securities are reclassified out of AOCI into the "Portion of loss recognized in other comprehensive income" in our statements of income.

Amounts recognized in OTTI that relate to the non-credit factors also are included in the "Portion of loss recognized in other comprehensive income". In determining whether a credit loss exists, we use our best estimate of the present value of cash flows expected to be collected from the investment security. We define cash flows expected to be collected as cash flows that we are likely to collect after assessment of all available information. The difference between the present value of the cash flows expected to be collected and the amortized cost basis represents the amount of credit loss.

We measure the credit loss amount related to an investment security's initial occurrence of OTTI using guidance that also applies to the determination of OTTI for impaired loans.

We estimate cash flows expected to be collected taking into consideration the payment structure of the investment security, prepayment speeds, and other relevant components. In regards to payment structure, we use the contractual rate of the security (that is, coupon rate) for fixed-rate securities. For variable-rate securities, we use an implied forward curve rather than the spot interest rate. This is because we believe the implied forward curve provides the best estimate of cash flows expected to be collected. For adjustable-rate securities with initial fixed interest rates, we calculate a security's effective interest rate using a blend of the initial fixed interest rate over the fixed period and the adjustable-rate or rates for periods subsequent to the first fixed period. The initial discount rate for a fixed-, variable-, or adjustable-rate security is consistent with the same rate that was used to project the cash flows expected to be collected on that security. For example, an implied forward curve is used to discount our variable-rate securities.

We account for the OTTI investment security as if the investment security had been purchased on the measurement date of the OTTI at an amortized cost basis equal to the previous amortized cost basis less the OTTI related to credit losses recognized in non-interest income (loss).

The amount of the total OTTI related to other factors also is recognized in AOCI. The new carrying value is not changed for subsequent recoveries in fair value. As of the measurement date, a new accretable yield is calculated on the impaired investment security. This is used to calculate

the amount to be recognized into income over the remaining life of the investment security so as to match the amount and timing of future cash flows expected to be collected. This is also re-evaluated quarterly. Additionally, the OTTI recognized in AOCI for investment securities classified as held-to-maturity is accreted from AOCI to the amortized cost of the investment security over the remaining life of the investment security in a prospective manner on the basis of the amount and timing of future estimated cash flows. That accretion increases the carrying value of the investment security and continues until we sell the investment security, it matures, or there is additional OTTI recognized into earnings.

For OTTI occurrences subsequent to the initial occurrence, the cash flows expected to be collected are discounted using a rate equal to the current yield used to accrete the investment security. Subsequent non-OTTI-related increases and decreases in the fair value of available-for-sale securities will be included in AOCI.

Significant Inputs Used to Calculate OTTI

Beginning with the second quarter of 2009, consistent with the objectives in the FHFA guidance, as discussed in **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations**, the FHLBs formed an OTTI Governance Committee (the "OTTI Committee") with the responsibility for reviewing and approving the key modeling assumptions, inputs and methodologies to be used by the FHLBs to generate cash flow projections used in analyzing credit losses and determining OTTI for private-label MBS. The OTTI Committee charter was approved on June 11, 2009 and provides a formal process by which the other FHLBs can provide input on and approve the assumptions.

In accordance with the FHFA guidance, an FHLB may engage another FHLB to perform the cash flow analysis underlying its OTTI determination. Each FHLB is responsible for making its own determination of impairment, which includes determining the reasonableness of assumptions, inputs, and methodologies used, and performing the required present value calculations using appropriate historical cost bases and yields. FHLBs that hold common private-label MBS are required to consult with one another to ensure that any decision that a commonly held private-label MBS is other-than-temporarily impaired, including the determination of fair value and the credit loss component of the unrealized loss, is consistent among those FHLBs. With respect to such commonly-owned securities, the FHLB of San Francisco performed the cash flow analysis underlying the Bank's other-than-temporary impairment determination.

In order to promote consistency in the application of the assumptions, inputs, and implementation of the OTTI methodology, the FHLBs have established control procedures whereby the FHLBs performing cash flow

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analysis select a sample group of private-label MBS and each perform cash flow analyses on all such test MBS, using the assumptions approved by the OTTI Committee. These FHLBs exchange and discuss the results and make any adjustments necessary to achieve consistency among their respective cash flow models.

For the period ending June 30, 2009, we have completed our OTTI analysis and made our OTTI determination utilizing the key modeling assumptions, inputs, and methodologies approved by the OTTI Committee.

To assess whether the entire amortized cost bases of our private-label MBS will be recovered, we performed a cash flow analysis for each security that was determined to be other-than-temporarily impaired in a previous reporting period as well as those with adverse risk characteristics as of June 30, 2009. The adverse risk characteristics used to select securities for cash flow analysis included: the duration and magnitude of the unrealized loss, credit ratings below investment grade, and criteria related to the credit performance of the underlying collateral, including the ratio of credit enhancement to expected collateral losses and the ratio of seriously delinquent loans to credit enhancement.

For these purposes, expected collateral losses are those that are implied by current delinquencies taking into account a default probability based on the state of delinquency and a loss severity assumption based on

product and vintage; seriously delinquent loans are those that are 60 or more days past due, including loans in foreclosure and real estate owned. In performing the cash flow analysis for each of these securities, we used two models provided by an independent third party. The first model considers borrower characteristics and the particular attributes of the loans underlying the securities in conjunction with assumptions about future changes in home prices and interest rates, to project prepayments, defaults and loss severities. A significant input to the first model is the forecast of future housing price changes for the relevant states and core based statistical areas (CBSA), which are based upon an assessment of the individual housing markets.

Our housing price forecast assumed current-to-trough home price declines ranging from 0 percent to 20 percent over the next 9 to 15 months (resulting in peak-to-trough home price declines of up to 51 percent). Thereafter, home prices are projected to increase 1 percent in the first year, 3 percent in the second year and 4 percent in each subsequent year. The month-by-month projections of future loan performance derived from the first model, which reflect projected prepayments, defaults and loss severities, are then input into a second model that allocates the projected loan level cash flows and losses to the various security classes in the securitization structure in accordance with its prescribed cash flow and loss allocation rules.

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For those securities for which an other-than-temporary impairment was determined to have occurred as of June 30, 2009 (that is, a determination was made that the entire amortized cost bases will not likely be recovered), the following table presents the results based on the inputs in the previous paragraph we used to measure the amount of the credit loss recognized in earnings during the three months ended June 30, 2009:

Classification	Unpaid Principal Balance	Prepayment Rates		Default Rates		Loss Severities		Current Credit Enhancement	
		Weighted Average %	Range %	Weighted Average %	Range %	Weighted Average %	Range %	Weighted Average %	Range %
Prime	\$ 2,231	16.7%	10.0% - 22.2%	35.2%	0.0% - 51.5%	38.8%	0.0% - 43.3%	12.0%	7.7% - 29.3%
Alt-A	187	11.9%	10.2% - 16.1%	65.3%	53.4% - 69.5%	46.8%	43.3% - 49.3%	17.3%	12.6% - 21.5%
Subprime	759	9.1%	6.4% - 22.5%	73.6%	40.1% - 84.1%	66.3%	60.4% - 77.7%	28.1%	0.0% - 45.7%
Total	<u>\$ 3,177</u>								

For the three and six months ending June 30, 2009, we recognized total OTTI, noncredit losses, and net OTTI as shown below. In 2008, under different accounting principles then in effect, we recognized total OTTI of \$30 million and \$63 million for the comparable three and six month periods. These losses were not broken down into credit or non-credit components.

	Balance Sheet					Income Statement		
	Unpaid Principal Balance	Amortized Cost	Gross Unrealized Losses	Gross Unrealized Gains	Fair Value	OTTI Related to Credit Loss	OTTI Related to Non-credit Loss (Recovery)	Total OTTI
For the three months ended June 30, 2009:								
AFS securities	\$ 187	\$ 165	\$ (83)	\$ 12	\$ 94	\$ 8	\$ (14)	\$ (6)
HTM securities ¹	<u>2,990</u>	<u>2,749</u>	<u>(1,140)</u>	<u>28</u>	<u>1,637</u>	<u>116</u>	<u>134</u>	<u>250</u>
Total OTTI impairment	<u>\$ 3,177</u>	<u>\$ 2,914</u>	<u>\$ (1,223)</u>	<u>\$ 40</u>	<u>\$ 1,731</u>	<u>\$ 124</u>	<u>\$ 120</u>	<u>\$ 244</u>
For the six months ended June 30, 2009:								
AFS securities	\$ 187	\$ 165	\$ (83)	\$ 12	\$ 94	\$ 19	\$ 27	\$ 46
HTM securities	<u>3,006</u>	<u>2,762</u>	<u>(1,142)</u>	<u>28</u>	<u>1,648</u>	<u>191</u>	<u>1,049</u>	<u>1,240</u>
Total OTTI impairment	<u>\$ 3,193</u>	<u>\$ 2,927</u>	<u>\$ (1,225)</u>	<u>\$ 40</u>	<u>\$ 1,742</u>	<u>\$ 210</u>	<u>\$ 1,076</u>	<u>\$ 1,286</u>

¹ Only HTM securities that were impaired for the three months ending June 30, 2009 were included in these amounts.

We recognized credit losses into earnings on securities in an unrealized loss position for which we do not expect to recover the entire amortized cost basis. Non-credit losses were recognized in AOCI since we do not intend to sell these securities and we believe it is more likely than not that we will not be required to sell these investments before recovery of their amortized cost basis. We recognized no OTTI charges on our other HTM and AFS MBS in unrealized loss positions because we expect to recover the entire amortized cost basis, we do not intend to sell, and we believe it is more likely than not that we will not be required to sell these securities prior to recovering their amortized cost basis.

The non-credit loss in AOCI on HTM securities will be accreted back into the HTM securities over their remaining life as an increase to the carrying value, since we ultimately expect to collect these amounts. During the three and six months ending June 30, 2009, we recorded accretion of \$72 million and \$83 million.

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The following tables show the roll-forwards of the cumulative amount of credit losses (recognized into earnings) on OTTI investment securities where there was also an additional non-credit portion (recognized into AOCI).

For the three months ended June 30, 2009

	<u>HTM</u>	<u>AFS</u>	<u>Total</u>
Balance April 1, 2009	\$ 125	\$ 14	\$ 139
Additions:			
Credit losses on securities for which OTTI was not previously recognized	12	-	12
Credit losses on securities for which an OTTI charge was previously recognized	<u>104</u>	<u>8</u>	<u>112</u>
Total OTTI recognized three months ended June 30, 2009	<u>116</u>	<u>8</u>	<u>124</u>
Reductions:			
None	-	-	-
Balance June 30, 2009	<u>\$ 241</u>	<u>\$ 22</u>	<u>\$ 263</u>

For the six months ended June 30, 2009

	<u>HTM</u>	<u>AFS</u>	<u>Total</u>
Balance January 1, 2009 ¹	\$ 50	\$ 3	\$ 53
Additions:			
Credit losses on securities for which OTTI was not previously recognized	66	5	71
Credit losses on securities for which an OTTI charge was previously recognized	<u>125</u>	<u>14</u>	<u>139</u>
Total OTTI recognized six months ended June 30, 2009	<u>191</u>	<u>19</u>	<u>210</u>
Reductions:			
None	-	-	-
Balance June 30, 2009	<u>\$ 241</u>	<u>\$ 22</u>	<u>\$ 263</u>

¹ Due to cumulative effect adjustment from the adoption of new accounting standards effective January 1, 2009. See **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations.**

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Unrealized Temporary Losses on our AFS and HTM Portfolios

The first table below breaks out AFS and HTM securities in an unrealized loss position at June 30, 2009 by type of security and by whether or not OTTI charges were recognized. The second table below summarizes only those AFS and HTM securities with unrealized losses as of December 31, 2008.

	Less than 12 Months				12 Months or More				Total	
	Fair Value	Gross Unrealized Losses	Non-Credit OTTI Recognized in AOCI (Loss)	Fair Value	Gross Unrealized Losses	Non-Credit OTTI Recognized in AOCI (Loss)	Fair Value	Gross Unrealized Losses	Non-Credit OTTI Recognized in AOCI (Loss)	
June 30, 2009										
Available-for-Sale Securities										
Non-MBS:										
Government-guaranteed Small Business Administration / Small Business Investment Companies	\$ 1,028	\$ *	\$ -	\$ -	\$ -	\$ -	\$ 1,028	\$ *	\$ -	
MBS:										
Government-sponsored enterprises residential	2,095	(21)	-	-	-	-	2,095	(21)	-	
Government-guaranteed residential	386	(1)	-	94	(2)	(71)	386	(1)	(71)	
Private-label residential	-	-	-	94	(2)	(71)	94	(2)	(71)	
Total	<u>\$ 3,763</u>	<u>\$ (26)</u>	<u>\$ -</u>	<u>\$ 94</u>	<u>\$ (2)</u>	<u>\$ (71)</u>	<u>\$ 3,857</u>	<u>\$ (28)</u>	<u>\$ (71)</u>	
Held-to-Maturity Securities										
Non-MBS:										
Small Business Administration / Small Business Investment Companies	\$ 21	\$ *	\$ -	\$ -	\$ -	\$ -	\$ 21	\$ *	\$ -	
State or local housing agency obligations	2	*	-	1	*	-	3	*	-	
MBS:										
Government-sponsored enterprises residential	2	*	-	2	*	-	4	*	-	
MPF Shared Funding	-	-	-	253	(12)	-	253	(12)	-	
Private-label residential	1	*	-	1,384	(4)	(829)	1,385	(4)	(829)	
Private-label home equity	55	(13)	-	686	(135)	(313)	741	(148)	(313)	
Private-label commercial	-	-	-	9	*	-	9	*	-	
Total	<u>\$ 81</u>	<u>\$ (13)</u>	<u>\$ -</u>	<u>\$ 2,335</u>	<u>\$ (151)</u>	<u>\$ (1,142)</u>	<u>\$ 2,416</u>	<u>\$ (164)</u>	<u>\$ (1,142)</u>	
* Less than \$1 million										

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	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2008						
Available-for-Sale Securities						
MBS:						
Private-label	\$ -	\$ -	\$ 41	\$ (41)	\$ 41	\$ (41)
Total temporarily impaired	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 41</u>	<u>\$ (41)</u>	<u>\$ 41</u>	<u>\$ (41)</u>
Held-to-Maturity Securities						
Non-MBS: Small Business Administration / Small Business Investment Companies	\$ 7	\$ (1)	\$ -	\$ -	\$ 7	\$ (1)
MBS:						
Government-sponsored enterprises	586	(17)	-	-	586	(17)
MPF Shared Funding	-	-	288	(16)	288	(16)
Private-label	1,384	(635)	975	(528)	2,359	(1,163)
Total temporarily impaired	<u>\$ 1,977</u>	<u>\$ (653)</u>	<u>\$ 1,263</u>	<u>\$ (544)</u>	<u>\$ 3,240</u>	<u>\$ (1,197)</u>

Gains and Losses on Trading Securities

The net gains (losses) on trading securities for the periods indicated were as follows:

For the periods ended June 30,	Three months		Six months	
	2009	2008	2009	2008
Net realized gain (loss)	\$ -	\$ -	\$ -	\$ -
Net unrealized gain (loss)	<u>(2)</u>	<u>(15)</u>	<u>(11)</u>	<u>*</u>
Net gain (loss) on trading securities	<u>\$ (2)</u>	<u>\$ (15)</u>	<u>\$ (11)</u>	<u>\$ -</u>

* Less than \$1 million

The following table presents the fair value of trading securities, including MBS:

Fair values as of:	June 30, 2009	December 31, 2008
Non-MBS:		
Government-sponsored enterprises	\$ 1,102	\$ 838
Temporary liquidity guarantee program (FDIC-TLGP)	<u>532</u>	<u>-</u>
Total Non-MBS	<u>1,634</u>	<u>838</u>
MBS:		
Government-sponsored enterprises	21	24
Government-guaranteed	<u>4</u>	<u>4</u>
Total MBS	<u>25</u>	<u>28</u>
Total trading securities	<u>\$ 1,659</u>	<u>\$ 866</u>

Gains and Losses on AFS Securities

In the six months ending June 30, 2009 we had proceeds of \$353 million from the sale of AFS securities. We had no sales from the AFS portfolio during the first six months of 2008. The realized gains and losses from the sales of these securities were as follows:

For the periods ended June 30,	Three months		Six months	
	2009	2008	2009	2008
Realized gain	\$ -	\$ -	\$ 19	\$ -
Realized loss	-	-	-	-
Net realized gain (loss) from sale of AFS securities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 19</u>	<u>\$ -</u>

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Maturity Terms

The following table presents the amortized cost and fair value of AFS and HTM securities by contractual maturity. Expected maturities of some securities, ABS, and MBS may differ from contractual maturities because borrowers of the underlying loans may have the right to prepay such loans.

	<u>Available-for-Sale</u>		<u>Held-to-Maturity</u>	
	<u>Amortized Cost</u>	<u>Fair Value</u>	<u>Amortized Cost</u>	<u>Fair Value</u>
June 30, 2009				
Non-MBS by Year of Maturity -				
Due in one year or less	\$ 82	\$ 84	\$ 190	\$ 190
Due after one year through five years	100	100	421	443
Due after five years through ten years	382	378	55	55
Due after ten years	601	607	45	45
Total non-MBS	<u>1,165</u>	<u>1,169</u>	<u>711</u>	<u>733</u>
ABS:				
FFELP student loans ABS	<u>5,083</u>	<u>5,094</u>	-	-
MBS:				
Government-sponsored enterprises - Residential	4,070	4,112	10,262	10,698
Government-guaranteed - Residential	624	626	16	17
MPF Shared funding	-	-	265	253
Private-label residential	167	94	2,238	1,406
Private-label home equity	-	-	1,221	760
Private-label commercial	-	-	84	84
Total MBS	<u>4,861</u>	<u>4,832</u>	<u>14,086</u>	<u>13,218</u>
Total	11,109	<u>\$ 11,095</u>	14,797	<u>\$ 13,951</u>
Adjustments from amortized cost to carrying value:				
AFS unrealized gains (losses), net		57		
Adjustment for non-credit losses		<u>(71)</u>	<u>(1,142)</u>	
Carrying value on Statements of Condition		<u>\$ 11,095</u>	<u>\$ 13,655</u>	

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Note 6 – Advances

For accounting policies concerning advances, see **Note 8** on page F-18 in our 2008 Form 10-K. At June 30, 2009, we had advances outstanding to members at interest rates ranging from 0.31% to 8.47%.

The following table presents our advances by redemption terms:

As of June 30, 2009	Amount	Weighted Average Interest Rate	Next Maturity or Call Date	Next Maturity or Put Date
Due in one year or less	\$ 9,722	2.76%	\$ 9,748	\$ 14,414
One to two years	4,291	3.45%	4,631	4,371
Two to three years	2,262	3.71%	1,977	2,476
Three to four years	2,043	3.56%	2,065	1,576
Four to five years	1,069	2.46%	1,066	983
More than five years	7,388	2.87%	7,288	2,955
Total par value	26,775	3.03%	\$ 26,775	\$ 26,775
Hedging adjustments	417			
Total advances	\$ 27,192			

We offer advances to members that may be prepaid on call dates without incurring prepayment or termination fees (callable advances). Other advances may only be prepaid by the advance borrower paying a fee (prepayment fee) that makes us financially indifferent to the prepayment of the advance. At June 30, 2009 and December 31, 2008, we had callable advances of \$1.7 billion for both periods.

We also offer puttable advances. With a puttable advance, we have the right to terminate the advance at predetermined exercise dates, which we would typically

exercise when interest rates increase, and the borrower may then apply for a new advance at the prevailing market rate. At June 30, 2009 and December 31, 2008, we had puttable advances outstanding totaling \$7.1 billion and \$8.1 billion.

The following table presents our advances by interest-rate payment terms:

	June 30, 2009	December 31, 2008
Detail of advances by type-		
Fixed-rate	\$ 19,607	\$ 28,192
Variable-rate	7,168	9,338
Total par value of advances	26,775	37,530
Hedging adjustments	417	609
Fair value option adjustments	-	1
Total advances	\$ 27,192	\$ 38,140

As of June 30, 2009 no advance borrower had over 10% of total advances outstanding. At December 31, 2008 we had \$4.4 billion in advances outstanding to Bank of America, N.A., which was 12% of total advances outstanding, with no other advance borrower over 10%. On October 17, 2008, LaSalle Bank, N.A. was merged into Bank of America, N.A. and became ineligible for membership because Bank of America, N.A. has its principal place of business in Charlotte, North Carolina, outside of our membership district.

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Note 7 – MPF Loans

MPF Loans Held in Portfolio

For accounting policies concerning MPF Loans held in portfolio see **Note 9** on page F-19 in our 2008 Form 10-K.

The MPF Program is a secondary mortgage market structure that provides funding to FHLB members that are participating financial institutions (PFIs) through the purchase or funding by an FHLB of MPF Loans. We classify MPF Loans on our statements of condition as held for investment because we have the intent and ability to hold such loans to maturity.

Effective August 1, 2008, we no longer enter into Master Commitments to acquire MPF Loans for investment except for immaterial amounts of MPF Loans that support affordable housing and are guaranteed by the Rural Housing Service of the Department of Agriculture (RHS) or insured by the Department of Housing and Urban Development (HUD).

“MPF Loans” refer to conforming conventional and government fixed-rate mortgage loans secured by one-to-four family residential properties with maturities from five to 30 years or participations in such mortgage loans that are acquired under the MPF Program. In September of 2008, we began offering the MPF Xtra™ product to our PFIs. Under the MPF Xtra product, we purchase MPF Loans from PFIs and concurrently sell them to Fannie Mae as a third-party investor. References to MPF Loans as they relate to the MPF Xtra product exclude mortgage loan participations.

The following table summarizes our MPF Loan information:

	June 30, 2009	December 31, 2008
MPF Loans - single-family		
Medium term (15 years or less):		
Conventional	\$ 8,301	\$ 9,657
Government ¹	208	230
Total medium term	<u>8,509</u>	<u>9,887</u>
Long term (over 15 years):		
Conventional	14,578	17,897
Government ¹	3,543	3,861
Total long term	<u>18,121</u>	<u>21,758</u>
Total par value	26,630	31,645
Agent fees, premium (discount)	116	150
Loan commitment basis adjustment	(13)	(16)
Hedging adjustments	237	311
Receivable from future performance credit enhancement fees	3	2
Allowance for credit loss	(9)	(5)
Total MPF Loans held in portfolio, net	\$ 26,964	\$ 32,087

¹ Government is comprised of FHA- or HUD-insured and VA- or RHS-guaranteed government loans.

MPF Loans held in our portfolio are placed on non-performing (non-accrual) status when it is determined that either (1) the collection of interest or principal is doubtful or (2) interest or principal is past due for 90 days or more, except when the MPF Loan is well-secured and in the process of collection. We do not place MPF Loans over 90 days delinquent on non-performing status when losses are not expected to be incurred as a result of the PFI's assumption of credit risk on MPF Loans by providing credit enhancement protections. We had \$27 million and \$19 million of MPF Loans on non-performing status at June 30, 2009 and December 31, 2008.

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MPF Loans that are on non-performing status, and that are viewed as collateral-dependent loans, are considered impaired. MPF Loans are viewed as collateral-dependent loans when repayment is expected to be provided solely by the sale of the underlying property, and there is no other available and reliable source of repayment. We had impaired MPF Loans of \$18 million and \$12 million at June 30, 2009 and December 31, 2008. An allowance of \$3 million was allocated to these loans at June 30, 2009 and less than \$1 million at December 31, 2008.

The average balance for impaired MPF Loans was \$16 million and \$15 million for the three and six months ended June 30, 2009 compared to \$8 million for the three and six months ended June 30, 2008. Interest income recognized on impaired MPF Loans was less than \$1 million for all periods presented.

When assets have been received in satisfaction of debt, or as a result of actual foreclosures and in-substance foreclosures, MPF Loans are reclassified at fair value as real estate owned in other assets. We had \$40 million and \$35 million in MPF Loans classified as real estate owned in other assets, which had been foreclosed but not yet liquidated at June 30, 2009 and December 31, 2008. For further detail on MPF Loans classified as non-performing, impaired, or real estate owned see **Note 9** on page F-19 in our 2008 Form 10-K.

MPF Xtra Product

MPF Loans sold to us through the MPF Xtra product are classified as held-for-sale, since such MPF Loans are concurrently sold to Fannie Mae as a third-party investor, and will not be held on our balance sheet. We receive a nominal upfront transaction fee which we expect to cover our cost of acting as master servicer for these MPF Loans. This fee is recognized over the life of the MPF Loans as a component of other, net, in non-interest income (loss).

For the six months ended June 30, 2009, we collected \$6 million in fees in connection with the purchase and concurrent sale of \$2.4 billion of MPF Xtra loans. Of the fees collected we recognized earned fee revenue of less than \$1 million for both the three and six month periods, the remainder being deferred and to be recognized over the life of the loans.

During the six months ended June 30, 2009, we were required to repurchase less than \$1 million in MPF Xtra Loans from Fannie Mae, which in turn were repurchased by the PFIs. We incurred no losses on these repurchases.

Note 8 – Allowance for Credit Losses

We have not recorded any allowance for credit losses on our advances. At June 30, 2009 and December 31, 2008, we had rights to collateral with an estimated value greater than the outstanding advances. See **Security Terms** in **Note 8 – Advances** on page F-19 in our 2008 Form 10-K for additional information regarding collateral.

Our allowance for MPF Loan credit losses represents management's estimate of probable losses inherent in our MPF Loan portfolio. MPF Loans sold to Fannie Mae under the MPF Xtra product are not held in our portfolio and therefore are not included in our allowance for credit losses.

The following table presents the changes in the allowance for credit losses on MPF Loans for the periods indicated:

For the periods ended June 30,	Three months		Six months	
	2009	2008	2009	2008
Balance, beginning of period	\$ 8	\$ 2	\$ 5	\$ 2
Chargeoffs	(1)	*	(1)	*
Recoveries	-	-	-	-
Provision for credit losses	2	-	5	-
Balance, end of period	<u>\$ 9</u>	<u>\$ 2</u>	<u>\$ 9</u>	<u>\$ 2</u>

* Less than \$1 million

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Note 9 – Consolidated Obligations

For accounting policies, the description of interest rate payment terms, and other additional information concerning consolidated obligations, see **Note 14** on page F-24 in our 2008 Form 10-K.

The following table summarizes our consolidated obligation discount notes outstanding. Discount notes can have terms ranging from one day to one year in length.

	June 30, 2009	December 31, 2008
Par value outstanding	\$ 40,318	\$ 29,484
Carrying value outstanding	\$ 40,286	\$ 29,466
Weighted average rate at period-end	0.28%	0.64%
Daily average outstanding for the year-to-date period	\$ 37,130	\$ 19,353
Weighted average rate for the year-to-date period	0.44%	2.22%
Highest outstanding at any month-end during the year-to-date period	\$ 43,018	\$ 29,466

The following table presents interest rate payment terms at the time of issuance for the types of consolidated obligation bonds for which we are the primary obligor.

	June 30, 2009	December 31, 2008
Consolidated obligation bonds:		
Fixed-rate non-callable	\$ 35,355	\$ 40,591
Fixed-rate callable	5,610	13,471
Floating-rate	350	975
Step-up	75	50
Inverse floating-rate	50	50
Total par value	41,440	55,137
Bond discounts, net	(36)	(39)
Hedging adjustments	(406)	207
Fair value option adjustments	1	-
Total consolidated obligation bonds	\$ 40,999	\$ 55,305

The following table summarizes consolidated obligation bonds for which we were the primary obligor by redemption terms:

June 30, 2009	Contractual Maturity	Weighted Average Interest Rate	Next Maturity or Call Date
Due in one year or less	\$ 10,579	3.89%	\$ 12,559
One to two years	7,122	4.06%	7,307
Two to three years	5,482	4.60%	5,587
Three to four years	4,490	4.45%	4,516
Four to five years	4,070	5.00%	4,031
More than five years	9,697	5.32%	7,442
Total par value	41,440	4.52%	\$ 41,442
Bond discounts, net	(36)		
Hedging adjustments	(406)		
Fair value option adjustments	1		
Total consolidated obligation bonds	\$ 40,999		

Note 10 – Subordinated Notes

Subordinated notes are unsecured obligations and rank junior in priority of payment to our senior liabilities. Senior liabilities include all of our existing and future liabilities, including deposits, consolidated obligations for which we are the primary obligor, and consolidated obligations of the other FHLBs (for which we are jointly and severally liable). With respect to consolidated obligations for which we are jointly and severally liable, we may, under certain circumstances, (1) have immediate payment obligations and (2) be designated as primary obligor. For further description of our subordinated notes see **Note 15** on page F-26 in our 2008 Form 10-K.

We are permitted to include a percentage of the outstanding principal amount of the subordinated notes (the Designated Amount) in determining compliance with our regulatory capital and minimum regulatory leverage ratio requirements and in calculating our maximum permissible holdings of MBS, and unsecured credit, subject to 20% annual phase-outs beginning in the sixth year following issuance. Currently, 100% of the \$1 billion outstanding subordinated notes are considered the Designated Amount, with the first 20% annual phase-out beginning on June 14, 2011.

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Note 11 – Capital Stock and Mandatorily Redeemable Capital Stock

For accounting policies and other matters concerning capital stock and mandatorily redeemable capital stock, see **Note 18** on page F-28 in our 2008 Form 10-K.

Regulatory capital is defined as the sum of the paid-in value of capital stock and mandatorily redeemable capital stock (together defined as regulatory capital stock) plus retained earnings. No members had concentrations of capital stock greater than or equal to 10% of total capital stock at June 30, 2009 or December 31, 2008.

The regulatory capital ratio required by FHFA regulations for an FHLB that has not implemented a capital plan under the GLB Act is 4.0%. This ratio applies to the Bank when our non-mortgage assets (defined as total assets less advances, acquired member assets, standby letters of credit, intermediary derivative contracts with members, certain MBS, and other investments specified by FHFA regulation) after deducting the amount of deposits and capital, are not greater than 11% of total assets. If the non-mortgage asset ratio is greater than 11%, FHFA regulations require a regulatory capital ratio of 4.76%. See **Minimum Capital Requirements** in **Note 18** on page F-29 in our 2008 Form 10-K for further description of our minimum capital requirements.

The C&D Order we entered into with the Finance Board on October 10, 2007, includes an additional minimum regulatory capital ratio of 4.5%, which currently supersedes the 4.0% regulatory requirement discussed above. In accordance with the C&D Order, we continue to include the Designated Amount of subordinated notes in calculating compliance with this regulatory capital ratio. Our non-mortgage asset ratio on an average monthly basis was above 11% at June 30, 2009, thus we were subject to the 4.76% ratio. At December 31, 2008, our non-mortgage asset ratio was below 11%, thus we were subject to the 4.50% ratio.

The following table summarizes our regulatory capital requirements as a percentage of our total assets:

	Regulatory Capital			
	Requirement in effect		Actual	
	Ratio	Amount	Ratio	Amount
June 30, 2009	4.76%	\$ 4,278	5.16%	\$ 4,638
December 31, 2008	4.50%	\$ 4,146	4.70%	\$ 4,327

Under the C&D Order, we are also required to maintain an aggregate amount of regulatory capital stock plus the Designated Amount of subordinated notes of at least \$3.600 billion. At June 30, 2009 and December 31, 2008, we had an aggregate amount of \$3.801 billion and \$3.787 billion of regulatory capital stock plus the Designated Amount of subordinated notes.

We reclassify capital stock from equity to mandatorily redeemable capital stock (MRCS), a liability on our statements of condition, when a member requests withdrawal from membership or its membership is otherwise terminated, such as when it is acquired by an entity outside of our district. In addition, we reclassify equity to MRCS when a member requests to redeem excess capital stock above their capital stock "floor" in connection with repayment of advances, as permitted under the C&D Order and further described in Note 17 – Regulatory Actions in our 2008 Form 10-K on page F-28. For regulatory purposes, MRCS is considered a part of regulatory capital. The following table shows a reconciliation of the dollar amounts, along with the number of current and former members owning the related capital stock, in MRCS for the periods presented:

	Dollar Amount		Member Count	
	2009	2008	2009	2008
Six months ended June 30,				
MRCS at January 1,	\$ 401	\$ 22	16	12
Membership withdrawals, net	17	13	7	5
Mergers / move - out-of-district	*	152	2	7
FDIC receivership	8	-	2	-
Incremental advance requests ¹	86	-	21	-
Redemptions of MRCS	<u>(86)</u>	<u>(7)</u>	<u>(21)</u>	<u>(5)</u>
MRCS at end of period	<u>\$ 426</u>	<u>\$ 180</u>	<u>27</u>	<u>19</u>

* Less than \$1 million

¹ We redeem excess capital stock above the related member's capital stock floor as permitted under the C&D Order as described in **Note 17-Regulatory Actions** in our 2008 Form 10-K on page F-28.

Under the terms of the C&D Order, as amended, except as discussed in footnote 1 to the table above, any other capital stock repurchases or redemptions, including redemptions upon membership withdrawal or other termination, require approval of the Deputy Director, Division of FHLB Regulation of the FHFA (Deputy Director). We do not believe the denial of stock redemption requests affects the reclassification of mandatorily redeemable capital stock as a liability. Rather, this denial delays the timing of an eventual mandatory redemption.

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Note 12 – Accumulated Other Comprehensive Income (Loss)

The following table summarizes the changes in AOCI for the periods indicated:

	AFS	AFS OTTI Non-Credit	HTM ¹	HTM OTTI Non-Credit	Cash Flow Hedges	Retirement Plans	Total
Balance, December 31, 2007	\$ (13)	\$ -	\$ (138)	\$ -	\$ (98)	\$ (2)	\$ (251)
Net unrealized gain (loss)	(76)	-	-	-	7	1	(68)
Reclassification adjustment for (gain) loss recognized into net income (loss)	-	-	39	-	18	-	57
Total other comprehensive income (loss)	(76)	-	39	-	25	1	(11)
Balance June 30, 2008	\$ (89)	\$ -	\$ (99)	\$ -	\$ (73)	\$ (1)	\$ (262)
Balance December 31, 2008	\$ 12	\$ -	\$ (76)	\$ -	\$ (576)	\$ 1	\$ (639)
January 1, 2009, cumulative effect non-credit impairment adjustment ²	-	(56)	-	(177)	-	-	(233)
Net unrealized gain (loss) non- credit		(41)	-	(1,177)	-	-	(1,218)
Net unrealized gain (loss) subsequent changes	64	12	-	-	239	-	315
Reclassification adjustments from AOCI into income:							
Net interest (income) expense	-	*	9	4	20	-	33
Net impairment (gains) losses	-	14	30	125	-	-	169
Realized net (gain) loss on sale of available-for- sale securities	(19)	-	-	-	-	-	(19)
Derivatives and hedging activities	-	-	-	-	(5)	-	(5)
Compensation and benefits	-	-	-	-	-	*	-
Accretion from OTTI Noncredit to HTM asset	-	-	-	83	-	-	83
Total other comprehensive income (loss)	45	(15)	39	(965)	254	-	(642)
Balance June 30, 2009	\$ 57	\$ (71)	\$ (37)	\$ (1,142)	\$ (322)	\$ 1	\$ (1,514)

* = less than \$1 million

¹ On December 27, 2007 securities with an amortized cost of \$1.602 billion were transferred at fair value from AFS to HTM. The \$138 million unrealized loss on these securities at that time was reported in AOCI and is being amortized using the constant effective interest (i.e., level yield) method over the estimated lives of the securities, based on anticipated prepayments, offset by the interest income accretion related to the discount on the transferred securities. In addition, other-than-temporary impairments on these securities have also been recognized. See **Note 5 – Investments - Held-to-Maturity** for details.

² See **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations**.

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Note 13 – Derivatives and Hedging Activities

The FHFA's regulations, its Financial Management Policy, and our internal asset and liability management policies all establish guidelines for our use of interest rate derivatives. These regulations and policies prohibit the speculative use of financial instruments authorized for hedging purposes. They also limit the amount of counterparty credit risk allowed.

Risk Profile

Market risk is the potential for loss due to market value changes in financial instruments we hold. Interest rate risk is a critical component of market risk. We are exposed to interest rate risk primarily from the effect of interest rate changes on our interest-earning assets and our funding sources which finance these assets. Mortgage-related assets are the predominant sources of interest rate risk in our market risk profile. Those assets include MPF Loans and mortgage-backed securities.

Spread risk is the yield relationship of a financial instrument relative to a reference yield curve, usually LIBOR. Spread risk reflects the supply and demand dynamics for a particular financial instrument. The Option-Adjusted Spread (OAS) is the spread between the yield on the financial instrument and the reference yield curve, less the estimated cost of embedded options. Spread risk may also reflect credit risk. Although we are exposed to spread risk, we do not actively manage spread risk because our interest-earning assets and interest-bearing liabilities are predominantly held to contractual maturity. We invest in GSE obligations, mortgage assets, the taxable portion of state or local housing finance agency securities, and FFELP student loan ABS. The interest rate and prepayment risk associated with these assets are managed through a combination of debt issuance and derivatives. The prepayment options embedded in mortgage assets can result in extensions or contractions in the expected maturities of these investments, primarily depending on changes in interest rates.

The optionality embedded in certain advances can create interest rate risk. When a member prepays an advance, we could suffer lower future income if the principal portion of the prepaid advance were invested in lower-yielding assets that continue to be funded by higher-cost debt. To protect against this risk, we generally charge a prepayment fee that makes us financially indifferent to a member's decision to prepay an advance. When we offer advances (other than short-term advances) that a member may prepay without a prepayment fee, we may finance such advances with callable debt or otherwise hedge this option.

We enter into offsetting delivery commitments under the MPF Xtra product. Accordingly, we are not exposed to market risk with respect to these delivery commitments.

Members may enter into interest rate derivatives directly with us. In these situations, we enter into offsetting interest rate derivatives with non-member counterparties in cases where we are not using the interest rate derivative for our own hedging purposes. This provides smaller members access to the derivatives market.

Hedge Objectives and Strategies

The goal of our interest rate risk management strategy is not to eliminate interest rate risk, but to manage it within appropriate limits. To mitigate the risk of loss, we have established policies and procedures, which include guidelines on the amount of exposure to interest rate changes we are willing to accept. In addition, we monitor the risk to our revenue, net interest margin and average maturity of our interest-earning assets and funding sources.

We measure and manage market exposure through four measurements: duration, convexity, curve, and volatility.

- Duration measures our exposure to parallel interest rate shifts. We do not forecast interest rates, nor take specific duration positions against such forecasts.
- Convexity measures how fast duration changes as a function of interest rate changes. Convexity is largely driven by mortgage cash flows that vary significantly as borrowers respond to rate changes by either prepaying their mortgages or slowing such prepayments.
- Curve quantifies our exposure to non-parallel shifts in the yield curve.
- Volatility describes the degree to which the value of options, explicit or embedded, fluctuates. MPF Loans and mortgage-backed securities include options held by the mortgage borrowers to prepay their loans. As a result, we have effectively sold options by owning MPF Loans and mortgage-backed securities.

We manage duration, convexity, curve, and volatility as part of our hedging activities. We analyze the risk of our mortgage assets on a regular basis and consider the interest rate environment under various rate scenarios. We also perform analyses of the duration and convexity of the portfolio. We hedge the duration and convexity of MPF Loans by using a combination of derivatives placed in either relationships using hedge accounting or in economic hedge relationships. Duration and convexity risks arise principally because of the prepayment option

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embedded in our MPF Loans. As interest rates become more volatile, changes in our duration and convexity profile become more volatile. As a result, our level of economic hedging activity, as discussed below, may increase resulting in an increase in hedging costs.

Our primary risk mitigation tools include funding instruments, swaps, swaptions, caps, and floors. Based on our risk profile, we do not use our funding to match the cash flows of our mortgage assets on a transaction basis. Rather, funding is used to address duration, convexity, curve, and volatility risks at the balance sheet level.

Hedge positions may be executed to reduce exposure or the risk associated with a single transaction or group of transactions. Our hedge positions are evaluated daily and adjusted as deemed necessary.

One strategy we use to manage interest rate risk is to acquire and maintain a portfolio of assets and liabilities which, together with their associated interest rate derivatives, are reasonably matched with respect to the expected maturities or repricings of the assets and liabilities. We may also use interest rate derivatives to adjust the effective maturity, repricing frequency, or option characteristics of financial instruments (such as advances, MPF Loans, MBS, and consolidated obligations) to achieve risk management objectives.

We use either derivative strategies or embedded options in our funding to minimize hedging costs. Swaps are used to manage interest rate exposures. Swaptions, caps and floors are used to manage interest rate and volatility exposures.

An economic hedge is defined as a derivative hedging specific (or a non-specific pool of) underlying assets, liabilities, or derivatives that does not qualify (or was not designated) for hedge accounting, but is an acceptable hedging strategy for risk management purposes. These economic hedging strategies also comply with FHFA regulations that prohibit speculative hedge transactions. An economic hedge may introduce the potential for earnings volatility caused by the changes in fair value on the derivatives that are recorded in income but not offset by recognizing corresponding changes in the fair value of the economically hedged assets, liabilities, or firm commitments.

Accounting for Derivatives – All derivatives are recognized on the statements of condition at fair value and are designated as either (1) a hedge of the fair value of (a) a recognized asset or liability or (b) an unrecognized firm commitment (a fair value hedge); (2) a hedge of (a) a forecasted transaction or (b) the variability of cash flows that are to be received or paid in connection with either a

recognized asset or liability or stream of variable cash flows (a cash flow hedge); or (3) an economic hedge that does not qualify for derivative hedge accounting.

Derivative Hedge Accounting – In order to qualify for hedge accounting, a derivative must be considered highly effective at reducing the risk associated with the exposure being hedged. We prepare formal contemporaneous documentation at the inception and designation of a hedging relationship. Our formal documentation identifies the following:

- Our risk management objectives and strategies for undertaking the hedge.
- The nature of the hedged risk.
- The derivative hedging instrument.
- The hedged item or forecasted transaction.
- The method we will use to retrospectively and prospectively assess the hedging instrument's effectiveness.
- The method we will use to measure the amount of hedge ineffectiveness into earnings.
- Where applicable, relevant details including the date or period when a forecasted transaction is expected to occur.

We formally assess (both at the hedge's inception and at least quarterly) whether the derivatives that are used in hedging transactions have been effective in offsetting changes in the fair value or cash flows of hedged items or forecasted transactions and whether those derivatives may be expected to remain effective in future periods. We use regression analysis to assess the effectiveness of our hedges, with the exception of certain cash flow hedging relationships of anticipated transactions, which utilize dollar value offset.

We assess hedge effectiveness primarily under the long-haul method. However, in certain cases where all conditions are met, we assess hedge effectiveness using the shortcut method. Under the shortcut method we periodically review each hedge relationship to ensure that none of the terms of the interest rate swap and hedged item have changed. Provided that no terms have changed, the entire change in fair value of the interest rate swap is considered to be effective at achieving offsetting changes in fair values or cash flows of the hedged asset or liability. If all the criteria are met, we apply the shortcut method to a qualifying fair value hedge when the relationship is designated on the trade date of both the

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interest rate swap and the hedged item (for example, advances or consolidated obligation bonds are issued), even though the hedged item is not recognized for accounting purposes until the transaction settlement date, provided that the period of time between the trade date and the settlement date of the hedged item is within established conventions for that marketplace.

We record the changes in fair value of the derivative and the hedged item beginning on the trade date. We do not apply the shortcut method unless the hedge is entered into concurrent with either the origination or purchase of an asset being hedged or the issuance of a liability being hedged.

For a qualifying fair value hedge, changes in the fair value of the derivative, along with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk (including changes that reflect losses or gains on firm commitments), are recognized as non-interest income in derivatives and hedging activities. Any ineffective portion of a fair value hedge, which represents the amount by which the change in the fair value of the derivative differs from the change in the fair value of the hedged item, is also recognized as non-interest income in derivatives and hedging activities.

For a qualifying cash flow hedge, changes in the fair value of the derivative, to the extent that the hedge is effective, are recorded in AOCI, until earnings are affected by the variability of cash flows of the hedged transaction. Any ineffective portion of a cash flow hedge is recognized as non-interest income in derivatives and hedging activities.

Amounts recorded in AOCI are reclassified to interest income or expense during the period in which the hedged transaction affects earnings, unless (a) occurrence of the forecasted transaction will *not* occur by the end of the originally specified time period (as documented at the inception of the hedging relationship) or within an additional two-month period of time, in which case the amount in AOCI is immediately reclassified to earnings, or (b) we expect at any time that continued reporting of a net loss in AOCI would lead to recognizing a net loss on the combination of the hedging instrument and hedged transaction (and related asset acquired or liability incurred) in one or more future periods. In such cases a loss is immediately reclassified into derivatives and hedging activities for the amount that is not expected to be recovered.

Discontinuance of Derivative Hedge Accounting – We discontinue derivative hedge accounting prospectively when: (1) we determine that the derivative is no longer effective in offsetting changes in the fair value or cash flows of a hedged item; (2) the derivative and/or the

hedged item expires or is sold, terminated, or exercised; (3) it is no longer probable that the forecasted transaction will occur; or (4) a hedged firm commitment no longer meets the definition of a firm commitment.

In all situations in which hedge accounting is discontinued and the derivative remains outstanding as an economic hedge, we will carry the derivative at its fair value on the statements of condition and will recognize further changes in the fair value of the derivative as non-interest income in derivatives and hedging activities, until the derivative is terminated. We account for discontinued fair value and cash flow hedges as follows:

- For discontinued asset and liability fair value hedges, we begin amortizing the cumulative basis adjustment on the hedged item into net interest income over the remaining life of the hedged item using the level-yield method.
- For cash flow hedges that are discontinued because the forecasted transaction is no longer probable (i.e., the forecasted transaction will not occur in the originally expected period or within an additional two month period of time thereafter), any related gain or loss that was in AOCI is recognized as non-interest income in derivatives and hedging activities.
- For cash flow hedges that are discontinued for reasons other than the forecasted transaction will not occur, we begin reclassifying the AOCI adjustment to net interest income when earnings are affected by the original forecasted transaction.

Economic Hedge Accounting – For economic hedges, changes in fair value of the derivatives are recognized as non-interest income in derivatives and hedging activities. Because these derivatives do not qualify for hedge accounting, there is no fair value adjustment to an asset, liability or firm commitment. Cash flows associated with derivatives are reflected as cash flows from operating activities in the statements of cash flows.

Embedded Derivatives – We may purchase financial instruments in which a derivative instrument is embedded in the financial instrument. Upon executing these transactions, we assess whether the economic characteristics of the embedded derivative are clearly and closely related to the economic characteristics of the remaining component of the financial instrument (i.e., the host contract) and whether a separate, non-embedded instrument with the same terms as the embedded instrument meets the definition of a derivative.

When it is determined that (1) the embedded derivative possesses economic characteristics that are not clearly and closely related to the economic characteristics of the

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host contract and (2) a separate, stand-alone instrument with the same terms qualifies as a derivative instrument, the embedded derivative is separated from the host contract, carried at fair value, and designated as a derivative instrument pursuant to an economic hedge. However, if the entire contract (the host contract and the embedded derivative) were to be measured at fair value, with changes in fair value reported in current earnings (e.g. an investment security classified as "trading"), or if we could not reliably identify and measure the embedded derivative for purposes of separating that derivative from its host contract, the entire contract would be recorded at fair value. We currently do not hold any embedded derivative instrument that requires bifurcation from its host contract.

Purchased Options – Premiums paid to acquire options are included in the initial basis of the derivative and reported in derivative assets on the statements of condition.

Accrued Interest Receivables and Payables – Any differentials between accruals of interest receivables and payables on derivatives designated as fair value or cash flow hedges are recognized as adjustments to the interest income or interest expense of the designated underlying investment securities, advances, consolidated obligations, or other financial instruments. The differentials between accruals of interest receivables and payables on economic hedges are recognized as non-interest income in derivatives and hedging activities.

Firm Commitments

Delivery Commitments are considered derivatives. Accordingly, we record a Delivery Commitment at fair value as a derivative asset or derivative liability, with changes in fair value recognized in derivatives and hedging activities. When the Delivery Commitment settles, the current fair value is included in the carrying amount of the MPF Loans, whenever applicable. In the case of the MPF Loans held for investment, the adjustment is amortized on a level-yield basis over the contractual life of the MPF Loan in interest income. In the case of MPF Loans under the MPF Xtra product, the adjustment to the basis is offset by a corresponding adjustment to the sales price that is associated with the fair value change to the sales Delivery Commitment concurrently entered into with Fannie Mae.

Cash Flow Hedges

Anticipated Discount Notes – Our hedge objective is to mitigate the variability of cash flows associated with the benchmark interest rate, London Interbank Offer Rate (LIBOR), of variable interest streams associated with the

recurring maturity and re-issuance of short-term fixed rate discount notes. The variability in cash flows associated with each new issuance of discount notes results from changes in the benchmark interest rate, LIBOR, over a specified hedge period caused by the recurring maturity and re-issuance of short-term fixed-rate discount notes over that hedge period. Our hedge strategy may involve the use of forward starting swaps to hedge this variability in cash flows due to changes in LIBOR so that a fixed-rate is secured over the life of the hedge relationship. In effect, we are changing what would otherwise be deemed a variable-rate liability into a fixed-rate liability. The total principal amount at issuance of the discount notes (i.e. net proceeds) and the total principal amount of the discount notes on an ongoing basis is equal to or greater than the total notional on the actual swaps used as hedging instruments. We document at hedge origination, and on an ongoing basis, that our forecasted issuances of discount notes are probable. We measure effectiveness each period using the hypothetical derivative method. The purpose of this measurement is to reclassify the amount of hedge ineffectiveness from AOCI to derivatives and hedging activities in the periods where the actual swap has changed in fair value greater than the hypothetical swap's changes in fair value.

We also may use an option to hedge a specified future variable cash stream as a result of rolling over short-term fixed-rate financial instruments such as discount notes. The option will effectively cap the variable cash stream at a predetermined target rate. Hedge effectiveness is assessed monthly using the hypothetical derivative method.

Anticipated CO Bonds – We may enter into an interest rate swap as a hedge of an anticipated issuance of debt to effectively lock in a spread between an interest-earning asset and the cost of funding. All amounts deemed effective are recorded in AOCI, while amounts deemed ineffective are recorded in current earnings. The swap is terminated upon issuance of the instrument, and amounts reported in AOCI are reclassified into earnings over the periods in which earnings are affected by the variability of the cash flows of the debt that was issued. Hedge effectiveness is assessed using the hypothetical derivative method.

Accounting for Failed Forecast of Anticipated Debt Transactions – During 2008, our ability to enter into long-term cash flow hedges was tainted by the non-occurrence of certain anticipated issuances of consolidated obligation bonds. As a result, we do not anticipate entering into such long-term cash flow hedges until we have demonstrated the capability to make reliable forecasts of anticipated long-term debt transactions.

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Variable-Rate Advances – We may use an option to hedge a specified future variable cash flow of variable-rate LIBOR-based advances. The option will effectively cap, or floor, the variable cash flow at a predetermined target rate. Hedge effectiveness is assessed monthly using the hypothetical derivative method that is used to assess and measure the effectiveness of a purchased option used in a cash flow hedge. For effective hedges using options, the option premium is reclassified out of AOCI using the caplet/floorlet method. Specifically, the initial basis of the instrument at the inception of the hedge is allocated to the respective caplets or floorlets comprising the cap or floor. All subsequent changes in fair value of the cap or floor, to the extent deemed effective, are recognized in AOCI. The change in the allocated fair value of each respective caplet or floorlet is reclassified out of AOCI when each of the corresponding hedged forecasted transactions impacts earnings.

Fair Value Hedges

Consolidated Obligation Bonds – We manage the fair value risk of a consolidated obligation by matching the cash inflow on the derivative with the cash outflow on the consolidated obligation. For instance, when a fixed-rate consolidated obligation is issued, we may simultaneously enter into an interest rate swap in which we receive fixed cash flows from a counterparty designed to offset in timing and amount the cash outflows we pay on the consolidated obligation. We also hedge the LIBOR benchmark rate on callable fixed-rate step-up consolidated obligation bonds at specified intervals where we own a call option(s) to terminate the consolidated obligation bond. The hedging instrument is a fixed-rate interest rate swap with a matching step-up feature that converts the callable fixed-rate step-up bond into a floating rate liability and has an offsetting call option(s) to terminate the interest rate swap. Such transactions are treated as fair value hedges. We assess hedge effectiveness primarily under the long-haul method. However, in certain cases where all conditions are met, hedge effectiveness is assessed using the shortcut method. Currently, we principally apply shortcut accounting to certain (1) fixed-rate consolidated obligations (non-callable) and (2) fixed-rate callable consolidated obligations.

Available-for-Sale Securities – We use interest rate swaps to hedge AFS securities to shorten our duration profile in an increasing interest rate environment. Our hedge strategy focuses on hedging the benchmark interest rate of LIBOR by effectively converting fixed-rate securities into floating rate assets to reduce our exposure to rising interest rates. This type of hedge is accounted for as a fair value hedge. We assess hedge effectiveness under the long-haul method. AFS securities are measured at fair value with changes in fair value reported

in AOCI; however, in the case of a fair value hedge, the adjustment of its carrying amount is recognized in earnings rather than in AOCI in order to offset the gain or loss on the hedging instrument. The gain or loss (that is, the change in fair value) on the AFS securities attributable to the hedged risk is the amount that is recognized currently in derivatives and hedging activities in our statement of income. Any gain or loss on these securities that is not attributable to the hedged risk is still recognized into AOCI.

Advances – With issuances of certain puttable advances, we purchase from the member an embedded option that enables us to extinguish the advance. We may hedge a puttable advance by entering into a cancelable interest rate swap where we pay fixed interest payments and receive floating rate interest payments based off of LIBOR. This type of hedge is accounted for as a fair value hedge. We assess hedge effectiveness primarily under the long-haul method. However, in certain cases where all conditions are met, hedge effectiveness is assessed using the shortcut method. Currently, we principally apply shortcut accounting to certain (1) fixed-rate advances (non-puttable) and (2) fixed-rate puttable advances. The swap counterparty can cancel the derivative financial instrument on the same date that we can put the advance back to the member.

MPF Loans – A combination of swaps and options, including futures, is used as a portfolio of derivatives to hedge a portfolio of MPF Loans. The portfolio of MPF Loans consists of one or more pools of similar assets, as designated by factors such as product type and coupon. As the portfolio of loans changes due to liquidations and paydowns, the derivatives portfolio is modified accordingly to hedge the interest rate and prepayment risks effectively. A new hedge relationship between a portfolio of derivatives and a portfolio of MPF Loans is established daily. The relationship is accounted for as a fair value hedge. The long-haul method is used to assess hedge effectiveness.

Economic Hedges

MPF Loans – Options may also be used to hedge the duration and convexity of the MPF Loan portfolio and prepayment risk on MPF Loans, many of which are not identified to specific MPF Loans and, therefore, do not receive fair value or cash flow hedge accounting treatment. These options include interest rate caps, floors, options, or treasury future contracts and swaptions. We may also purchase cancelable swaps to minimize the prepayment risk embedded in the MPF Loans.

Investments – We may manage against prepayment and duration risk by funding investment securities with

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consolidated obligations that have call features, by economically hedging the prepayment risk with caps, floors, or by adjusting the duration of the securities by using derivatives to modify the cash flows of the securities. We issue both callable and non-callable debt to achieve cash flow patterns and liability durations similar to those expected on MBS. We may also use derivatives as an economic hedge to match the expected prepayment characteristics of the MBS.

We may also manage the risk arising from changing market prices and volatility of investment securities classified as trading securities by entering into derivative financial instruments (economic hedges) that offset the changes in fair value of the securities. The market value changes of both the trading securities and the associated derivatives are recognized in non-interest income.

Managing Credit Risk on Derivatives – We are subject to credit risk due to the risk of nonperformance by counterparties to our derivative agreements. The degree of counterparty risk depends on the extent to which master netting arrangements are included in such contracts to mitigate the risk. We manage counterparty credit risk through credit analysis, collateral requirements, and limits on exposure to any individual counterparty. Based on credit analyses and collateral requirements, we do not anticipate any credit losses from our derivative agreements.

The contractual or notional amount of derivatives reflects our involvement in the various classes of financial instruments. The notional amount of derivatives does not measure our credit risk exposure, and our maximum credit exposure is substantially less than the notional amount. We require collateral agreements on derivatives that establish collateral delivery thresholds. Our potential loss due to credit risk as of the balance sheet date is based on the fair value of our derivative assets. This amount assumes that these derivatives would completely fail to perform according to the terms of the contracts and the collateral or other security, if any, for the amount due proved to be of no value to us. In determining maximum credit risk, we consider accrued interest receivables and payables, and the legal right to offset derivative assets and liabilities by counterparty. At June 30, 2009 and December 31, 2008, our maximum credit risk as defined above was \$227 million and \$260 million.

We transact most of our derivatives with major financial institutions and major broker-dealers, of which some, or their affiliates, buy, sell, and distribute consolidated obligations.

We held collateral consisting of securities and cash with a fair value of \$246 million and \$269 million as of June 30, 2009 and December 31, 2008. Additionally, collateral with respect to derivatives with members includes collateral assigned to us, as evidenced by a written security agreement and may be held by the member for our benefit.

Derivatives Exposures to Lehman Brothers Special Financing, Inc.

As of June 30, 2009, we continued to owe a net amount of \$6 million to Lehman Brothers Special Financing Inc. (LBSFI) under an ISDA Master Agreement, as further discussed in “Accounting Issues Related to Lehman Derivative Termination” on page F-42 in our 2008 Form 10-K. It is possible that we may incur additional costs associated with the final settlement procedures with LBSFI, but we do not expect those costs to be material.

Financial Statement Impact and Additional Financial Information

Our net payments on derivative financing activities during the six months ended June 30, 2009 were \$44 million. We perform an evaluation to determine whether an upfront fee received represents a financing activity. Specifically, if an upfront fee received represents more than an insignificant amount, then the initial and subsequent cash flows associated with the derivative are reported on a net basis as a financing activity in our statement of cash flows. We have interpreted the term “insignificant” as denoting an amount that is less than 10% of the present value of an at-the-market derivative’s fully prepaid amount.

Our derivative instruments contain provisions that may require us to post additional collateral with counterparties if there is deterioration in our credit rating. The aggregate fair value of all derivative instruments with credit-risk-related contingent features that are in a liability position on June 30, 2009 is \$840 million for which we have posted collateral of \$775 million in the normal course of business. If the credit-risk-related contingent features underlying these agreements were triggered on June 30, 2009, we would be required to post up to an additional \$59 million of collateral to our counterparties.

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The following table summarizes our derivative instruments as of June 30, 2009.

As of June 30, 2009	Notional Amount	Derivative Assets	Derivative Liabilities
Derivatives in hedge accounting relationships -			
Interest rate swaps	\$ 28,785	\$ 73	\$ (1,368)
Interest rate swaptions	2,855	72	-
Interest rate caps or floors	2,675	255	-
Interest rate futures/TBA	662	-	-
Total	34,977	400	(1,368)
Derivatives not in hedge accounting relationships -			
Interest rate swaps	10,105	140	(130)
Interest rate swaptions	17,702	344	-
Interest rate futures/TBA	950	2	-
Mortgage delivery commitments	1	-	-
Total	28,758	486	(130)
Total before adjustments	\$ 63,735	886	(1,498)
Netting adjustments		(634)	634
Cash collateral and cash collateral related accrued interest		(197)	-
Total adjustments ¹		(831)	634
Derivative assets and liabilities as reported on statements of condition		\$ 55	\$ (864)

¹ Our accounting policy is to offset derivative instruments of the same counterparty under a master netting agreement. Amounts represent the effect of legally enforceable master netting agreements that allow the Bank to settle positive and negative positions and also cash collateral held or placed with the same counterparties.

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The following table represents outstanding notional balances and estimated fair values of derivatives outstanding at December 31, 2008. The notional amount of derivatives outstanding where we acted as an intermediary for the benefit of our members was \$19 million at December 31, 2008.

For the period ending	December 31, 2008	
	Notional	Fair Value
Interest rate swaps:		
Fair value	\$ 33,012	\$ (623)
Cash flow	6,447	(756)
Economic	9,264	(168)
Total	<u>48,723</u>	<u>(1,547)</u>
Interest rate swaptions:		
Fair value	3,930	181
Economic	10,797	272
Total	<u>14,727</u>	<u>453</u>
Interest rate caps/floors:		
Cash flow	2,675	337
Economic	-	-
Total	<u>2,675</u>	<u>337</u>
Interest rate futures/TBAs:		
Fair value	999	2
Economic	450	(1)
Total	<u>1,449</u>	<u>1</u>
Delivery commitments of MPF Loans:		
Economic	-	-
Total	<u>\$ 67,574</u>	<u>(756)</u>
Accrued interest, net at period end		(45)
Cash collateral		(164)
Net derivative balance		<u>\$ (965)</u>
Derivative assets	\$ 102	
Derivative liabilities	(1,067)	
Net derivative balance	<u>\$ (965)</u>	

The following tables present the components of derivatives and hedging activities as presented in the statements of income.

<u>Gain (loss) for period ended June 30, 2009</u>	<u>Three Months</u>	<u>Six Months</u>
Derivatives and hedged items in fair value hedging relationships		
Interest rate swaps	\$ 22	\$ 29
Other	<u>2</u>	<u>(11)</u>
Total net gain (loss) related to fair value hedge ineffectiveness	<u>24</u>	<u>18</u>
Total net gain (loss) related to cash flow hedge ineffectiveness	<u>2</u>	<u>4</u>
Derivatives not designated as hedging instruments under hedge accounting-		
Economic hedges-		
Interest rate swaps	213	462
Interest rate swaptions	(117)	(428)
Interest rate futures/TBA	1	2
Net interest settlements	<u>(1)</u>	<u>(8)</u>
Total gains (losses) on derivatives not in hedge accounting relationships	<u>96</u>	<u>28</u>
Net gains (losses) on derivatives and hedging activities	<u>\$ 122</u>	<u>\$ 50</u>
Gain (loss) for period ended June 30, 2008		
Fair value hedge ineffectiveness	\$ (12)	\$ (32)
Cash flow hedge ineffectiveness	-	-
Cash flow hedge ¹	-	-
Gain (loss) on economic hedges	<u>(8)</u>	<u>(50)</u>
Net gain (loss) on derivatives and hedging activities	<u>\$ (20)</u>	<u>\$ (82)</u>

¹ Related to cash flow hedges on the early extinguishment of debt, including debt transferred to other FHLBs.

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The following table presents, by type of hedged item, the gains (losses) on derivatives and the related hedged items in fair value hedging relationships and the impact of those derivatives on our net interest income.

Three months ended June 30, 2009	Gain (Loss) on Derivative	Gain (Loss) on Hedged Item	Net Fair Value Hedge Ineffectiveness	Effect of Derivatives on Net Interest Income¹
Hedged item type -				
Advances	\$ 110	\$ (107)	\$ 3	\$ (85)
Consolidated obligations - bonds	(442)	464	22	43
MPF Loans held for portfolio	58	(59)	(1)	(18)
Total	\$ (274)	\$ 298	\$ 24	\$ (60)
Six months ended June 30, 2009				
Hedged item type -				
Advances	\$ 188	\$ (186)	\$ 2	\$ (162)
Consolidated obligations - bonds	(622)	654	32	93
MPF Loans held for portfolio	59	(75)	(16)	(36)
Total	\$ (375)	\$ 393	\$ 18	\$ (105)

¹ The net interest on derivatives in fair value hedge relationships is presented in the interest income/expense line item of the respective hedged item.

The following table presents, by type of hedged item, the gains (losses) on derivatives and the related hedged items in cash flow hedging relationships and the impact of those derivatives on our net interest income:

Three months ended June 30, 2009	Effective Portion		Ineffective Portion	
	Gain (Loss) Recognized in AOCI	Location of Gain (Loss) Reclassified From AOCI into Income	Gain (Loss) Reclassified from AOCI into Income	Gain (Loss) Recognized in Derivatives and Hedging Activities
Advances - interest rate floors	\$ (57)	Interest income	\$ (3)	\$ -
Consolidated obligation bonds - interest rate swaps	-	Interest expense	(2)	-
Discount notes - interest rate caps	-	Interest expense	(3)	-
Discount notes - interest rate swaps	210	Interest expense	(1)	3
Total	\$ 153		\$ (9)	\$ 3
Six months ended June 30, 2009				
Advances - interest rate floors	\$ (91)	Interest income	\$ (6)	\$ -
Consolidated obligation bonds - interest rate swaps	-	Interest expense	(4)	-
Discount notes - interest rate caps	-	Interest expense	(8)	-
Discount notes - interest rate swaps	330	Interest expense	(2)	5
Total	\$ 239		\$ (20)	\$ 5

Over the next 12-month period, we expect that \$7 million of deferred cash flow hedging charges recorded in AOCI as of June 30, 2009, will be recognized as a reduction to net interest income. The maximum length of time over which we are hedging our exposure to the variability in future cash flows for forecasted transactions, excluding those forecasted transactions related to the payment of variable interest on existing financial instruments, is 10 years.

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Note 14 – Estimated Fair Value

For accounting policies concerning fair value, see **Note 23** on page F-43 in our 2008 Form 10-K

Fair Value Option

We have elected the fair value option for certain newly acquired financial assets and liabilities. Under fair value accounting guidance, fair value is used for both the initial and subsequent measurement of the designated assets, liabilities, and commitments, with the changes in fair value recognized in net income. Interest income and interest expense carried on financial assets or liabilities carried at fair value is recognized under the level-yield method based solely on the contractual amount of interest due or unpaid. Any transaction fees or costs are no longer amortized and instead are immediately recognized into other non-interest income or other non-interest expense.

Short-term consolidated obligation bonds and advances may not pass prospective or retrospective effectiveness testing under derivative hedge accounting guidance, despite the fact that the interest rate swaps used to hedge such liabilities and assets have matching terms. Accordingly, in cases where we hedge these short-term consolidated obligation bonds and advances, we elect the fair value option in order to better match the change in fair value of the bond or advance with the interest rate swap economically hedging it.

The following table summarizes the activity related to financial assets and liabilities for which we elected the fair value option from December 31, 2008 to June 30, 2009:

	<u>Advances</u>	<u>Consolidated Obligation Bonds</u>
Balance, December 31, 2008	\$ 201	\$ -
New transactions elected for fair value option	-	(2,115)
Maturities and terminations	(200)	-
Net gain (loss) on instruments held at fair value	(1)	(1)
Balance, June 30, 2009	<u>\$ -</u>	<u>\$ (2,116)</u>

The following table presents the income statement effects from changes in fair values for items where we elected the fair value option in 2009. There were no changes in fair value due to changes in credit risk. We did not elect the fair value option for any items in the corresponding 2008 periods.

	<u>Interest income / expense</u>	<u>Net gain (loss) on instruments held at fair value</u>	<u>Total changes in fair value included in current period earnings</u>
Three months ended June 30, 2009			
Consolidated obligation bonds	\$ (1)	\$ (1)	\$ (2)
Six months ended June 30, 2009			
Advances	\$ *	\$ (1)	\$ (1)
Consolidated obligation bonds	(1)	(1)	(2)

* Less than \$1 million

The following table reflects the difference between the aggregate fair value and aggregate remaining contractual principal balance outstanding for items where we selected the fair value option:

	<u>Principal Balance</u>	<u>Fair Value</u>	<u>Fair Value Over (Under) Unpaid Principal Balance</u>
At June 30, 2009			
Consolidated obligation bonds	\$ (2,115)	\$ (2,116)	\$ (1)
At December 31, 2008			
Advances	\$ 200	\$ 201	\$ 1

Fair Value Hierarchy

Outlined below is the application of the fair value hierarchy to our financial assets and liabilities.

Level 1: Quoted Prices in Active Markets for Identical Assets

Our Level 1 financial assets and financial liabilities include certain derivative contracts that are traded in an active exchange market; for example: futures and options on futures.

Level 2: Significant Other Observable Inputs

Our Level 2 category includes certain debt instruments issued by U.S. government-sponsored enterprises, certain TBA contracts (a contract for the purchase or sale of an MBS to be delivered at an agreed-upon future date but does not include a specified pool number and number of pools or precise amount to be delivered),

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certain mortgage-backed debt securities issued by government-sponsored enterprises that trade in liquid over-the-counter markets and certain consolidated obligation bonds and advances carried at fair value under the fair value option.

Level 3: Significant Unobservable Inputs

Our Level 3 category includes certain private-label MBS investments held in our AFS portfolio that are backed by Alt-A mortgage loans and an inverse floating rate consolidated obligation bond along with the derivative asset hedging that bond. Our Level 3 category also includes, on a non-recurring basis, impaired HTM securities, impaired MPF Loans and Real Estate Owned.

Fair Value Methodology

Described below are our fair value measurement methodologies for assets and liabilities measured or disclosed at fair value. Such methodologies were applied to all of the assets and liabilities carried or disclosed at fair value.

Financial Assets

Assets for which fair value approximates carrying value – The estimated fair value of cash and due from banks, Federal Funds sold, securities purchased under agreements to resell, and accrued interest receivable approximates the carrying value due to their short-term nature and negligible credit risk.

Advances – Fair values for advances are determined using the income approach, which converts the expected future cash flows to a single present value. The estimated fair values do not assume prepayment risk, where we receive a fee sufficient to make us financially indifferent to a member's decision to prepay. We use internally constructed curves based on the consolidated obligation curve and a spread, which differs based on the advance size and term.

Investment Securities – Fair values of our investment securities that are actively traded by market participants in the secondary market are determined based on market-based prices provided by a third-party pricing service. Our principal markets for securities portfolios are the secondary institutional markets, with an exit price that is predominantly reflective of bid level pricing in that market. We have evaluated the valuation methodologies used to develop the fair values in order to determine whether such valuations are representative of an exit price in our principal markets.

We use an internal model to value certain investment securities when a quoted market price or third party provided price is unavailable. The internal model uses an income approach, utilizing market based inputs for comparable securities, and we consider such valuations to be level 2. For certain private-label MBS investments, including certain AFS and HTM securities, which are valued on a non-recurring basis, we believe that they are traded in inactive markets.

At June 30, 2009, we used internal assumptions and modeling related to expected cash flows for a portion of our private-label MBS portfolio, which is classified as HTM or AFS on the basis that fair values received from a third-party pricing service represented fair values of distressed sales. The determination was based on the significant bid-ask spread in the markets for these securities and the limited volume of trades relative to historical levels that existed when the market was not distressed (i.e., 2007) as well as other relevant factors such as the intervention of the U.S. Government into the financial markets.

The fair value of our MBS investments with vintages between 2005 and 2007 are based on industry recognized models and discounted cash flow techniques. Models were used for these instruments because there has been a specific review of the projected underlying cash flows, including loss severity, roll-rates and default rates for which we are able to refine our estimate of fair value if an active market existed at the balance sheet date. The modeled values reflect our expectations of future cash flows after accounting for appropriate risk premiums as if an active market existed for these instruments.

MPF Loans held in portfolio – The estimated fair values for MPF Loans are based on modeled prices using independent, market-based inputs. The modeled prices are derived using prices for new MBS issued by GSEs, which are adjusted for differences in coupon, average loan rate, cost of carry, seasoning, and cash flow remittance between MPF Loans and MBS. The referenced MBS are dependent upon the underlying prepayment assumptions priced in the secondary market.

Derivative Assets – Derivative instruments are primarily transacted in the institutional dealer market and priced with observable market assumptions at a mid-market valuation point. We do not provide a credit valuation adjustment based on aggregate exposure by derivative counterparty when measuring the fair value of our derivative assets. This is because the collateral provisions pertaining to our derivatives obviate the need to provide such a credit valuation adjustment. The fair values of our derivatives take into consideration the effects of legally enforceable master netting agreements that allow us to settle positive and negative positions and offset cash collateral with the same counterparty on a net basis. We and each derivative counterparty have bilateral collateral thresholds that take into account both our and our counterparty's credit ratings. As a result of these practices and agreements, we have concluded that the impact of the credit differential between us and our derivative counterparties was sufficiently mitigated to an immaterial level and no further adjustments were deemed necessary to the recorded fair values of derivative assets in the statements of condition as presented.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Financial Liabilities

Liabilities for which fair value approximates carrying value – The estimated fair value of deposits and accrued interest payable approximates the carrying value due to their short-term nature.

Securities Sold Under Agreements to Repurchase – Fair values for securities sold under agreements to repurchase are determined using the income approach, which converts the expected future cash flows to a single present value using market-based inputs. The fair value also takes into consideration any derivative features.

Derivative Liabilities – Derivative instruments are primarily transacted in the institutional dealer market and priced with observable market assumptions at a mid-market valuation point. We do not provide a credit valuation adjustment for our aggregate exposure to our derivative counterparties when measuring the fair value of our derivatives liabilities. This is because the collateral provisions pertaining to our derivatives obviate the need to provide such a credit valuation adjustment. The fair values of our derivatives take into consideration the effects of legally enforceable master netting agreements that allow us to settle positive and negative positions and offset cash collateral with the same counterparty on a net basis. We and each derivative counterparty have bilateral collateral thresholds that take into account both our and our counterparty's credit ratings. As a result of these practices and agreements, we have concluded that the impact of the credit differential between us and our derivative counterparties was sufficiently mitigated to an immaterial level and no further adjustments were deemed necessary to the recorded fair values of derivative liabilities in the statements of condition as presented.

Consolidated Obligations – Fair values of consolidated obligations and discount notes without embedded options are determined based on internal valuation models which use market-based yield curve inputs obtained from the Office of Finance. Fair values of consolidated obligations with embedded options are determined based on internal valuation models with market-based inputs obtained from the

Office of Finance and derivative dealers. Fair value is estimated by calculating the present value of expected cash flows using discount rates that are based on replacement funding rates for liabilities with similar terms. Additionally, we use an internal valuation model to arrive at the fair value of our inverse floating-rate consolidated obligation bond, short-term callable consolidated obligation bonds, and where we elect the fair value option. Their fair value is determined based on the income approach. The income approach uses valuation techniques to convert future amounts to a single present value discounted amount. The measurement is based on the value indicated by current market expectations about those future amounts. In this regard, our internal model discounts anticipated cash flows using an appropriate independent market rate based on the underlying terms of the consolidated obligation bond. Our valuation takes into consideration any credit valuation adjustment. The valuation model is based on an external consolidated obligation curve that reflects trading activities and any potential adjustments for our credit rating.

Mandatorily redeemable capital stock – The fair value of our MRCS is par value adjusted, if appropriate, for any undeclared and/or unpaid dividends that would be owed at the put date, which corresponds to the entire expected redemption amount at the reclassification date. Par rather than market value is used because our MRCS can only be acquired by members (or transferred between members) at par value and redeemed at par value. Capital stock is not traded and no market mechanism exists for the exchange of stock outside the cooperative structure.

Subordinated notes – Fair values are determined based on internal valuation models which use market-based yield curve inputs obtained from a third-party.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

The following tables present financial assets and financial liabilities measured at fair value on a recurring basis:

<u>As of June 30, 2009</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Netting Adj. ¹</u>	<u>Total</u>
Assets -					
Trading securities:					
GSE debt non-MBS	\$ -	\$ 1,102	\$ -	\$ -	\$ 1,102
Other non-MBS debt	-	532	-	-	532
Other U.S. obligations residential MBS	-	4	-	-	4
GSE residential MBS	-	21	-	-	21
Total Trading Securities	<u>-</u>	<u>1,659</u>	<u>-</u>	<u>-</u>	<u>1,659</u>
AFS securities:					
Other U.S. obligations non-MBS	-	779	-	-	779
GSE debt non-MBS	-	289	-	-	289
Other non-MBS debt	-	100	-	-	100
FFELP student loan ABS	-	5,095	-	-	5,095
Other U.S. obligations residential MBS	-	626	-	-	626
GSE residential MBS	-	4,112	-	-	4,112
Private-label residential MBS	-	-	94	-	94
Total AFS Securities	<u>-</u>	<u>11,001</u>	<u>94</u>	<u>-</u>	<u>11,095</u>
Derivative assets	<u>2</u>	<u>856</u>	<u>28</u>	<u>(831)</u>	<u>55</u>
Total assets at fair value	<u>\$ 2</u>	<u>\$ 13,516</u>	<u>\$ 122</u>	<u>\$ (831)</u>	<u>\$12,809</u>
Level 3 as a percent of total assets at fair value			<u>1%</u>		
Liabilities -					
Consolidated obligation bonds	\$ -	\$ 2,116	\$ 75	\$ -	\$ 2,191
Derivative Liabilities	-	1,498	-	(634)	864
Total liabilities at fair value	<u>\$ -</u>	<u>\$ 3,614</u>	<u>\$ 75</u>	<u>\$ (634)</u>	<u>\$ 3,055</u>
Level 3 as a percent of total liabilities at fair value			<u>2%</u>		
As of December 31, 2008					
Assets:					
Trading securities	\$ -	\$ 866	\$ -	\$ -	\$ 866
Advances	-	201	-	-	201
AFS securities	-	2,038	104	-	2,142
Derivative assets	1	220	45	(164)	102
Total assets at fair value	<u>\$ 1</u>	<u>\$ 3,325</u>	<u>\$ 149</u>	<u>\$ (164)</u>	<u>\$ 3,311</u>
Liabilities:					
Consolidated obligation bonds	\$ -	\$ -	\$ 91	\$ -	\$ 91
Derivative Liabilities	-	1,067	-	-	1,067
Total liabilities at fair value	<u>\$ -</u>	<u>\$ 1,067</u>	<u>\$ 91</u>	<u>\$ -</u>	<u>\$ 1,158</u>

¹ Our accounting policy is to offset derivative instruments of the same counterparty under a master netting agreement. Amounts represent the effect of legally enforceable master netting agreements and futures contracts margin accounts that allow us to settle positive and negative positions and also cash collateral held or placed with the same counterparties.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

The following table presents a reconciliation of certain financial assets and financial liabilities that are measured at fair value on the statements of condition using Level 3 inputs for the six months ended June 30, 2009.

	Level 3 Assets/Liabilities		
	AFS Securities Private-label MBS CMO	Derivative Assets	Consolidated Obligation Bonds
Beginning Balance, December 31, 2008	\$ 104	\$ 45	\$ (91)
Gains (losses) realized and unrealized:			
Changes in fair value (included in derivatives & hedging activities on statements of income)	-	(17)	16
Included in AOCI	(10)	-	-
Ending Balance June 30, 2009	<u>\$ 94</u>	<u>\$ 28</u>	<u>\$ (75)</u>
Total gain (loss) in earnings for change in realized gain (loss) for instruments held at period end	<u>\$ -</u>	<u>\$ (17)</u>	<u>\$ 16</u>

Assets Measured at Fair Value on a Non-recurring Basis

Certain held-to-maturity investment securities, MPF Loans, and Real Estate Owned are measured at fair value on a non-recurring basis; that is, they are not measured at fair value on an ongoing basis but are subject to fair value adjustments only in certain circumstances (for example, when there is evidence of other-than-temporary impairment).

The following table presents these financial assets by level within the valuation hierarchy as of June 30, 2009, for which a non-recurring fair value measurement has been recorded.

	Fair Value Measurements as of June 30, 2009 Using			Three months ended June 30, 2009
	Level 1	Level 2	Level 3	Credit (Loss) Reported in Earnings
Assets:				
Impaired HTM securities				
Private-label residential MBS	\$ -	\$ -	\$ 824	\$ (56) ¹
Private-label home equity loan MBS	-	-	308	(60) ²
Impaired MPF Loans ³	-	-	15	(3)
Real Estate Owned ⁴	-	-	45	-
Total non-recurring assets	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,192</u>	<u>\$ (119)</u>

* Less than \$1 million

¹ A total of \$21 million of the \$56 million in credit losses presented do not relate to the private-label residential MBS disclosed as Level 3 as of June 30, 2009. Instead, the \$21 million in credit losses relate to private-label residential MBS that incurred credit losses but did not incur additional declines in fair value.

² A total of \$2 million of the \$60 million in credit losses presented do not relate to the private-label equity loan MBS disclosed as Level 3 as of June 30, 2009. Instead, the \$2 million in credit losses relate to private-label equity loan MBS that incurred credit losses but did not incur additional declines in fair value.

³ In accordance with FASB accounting guidance, a \$3 million decline in fair value was allocated to the allowance for credit losses related to Impaired MPF Loans. Impaired MPF Loans are carried in our statement of condition at amortized cost of \$18 million at June 30, 2009.

⁴ We estimate the fair value of Real Estate Owned using a current broker price opinion when available. If a current broker price opinion is not available, we estimate fair value based on current actual loss severity rates we have incurred on sales of Real Estate Owned excluding estimated selling costs. In accordance with FASB accounting guidance, \$5 million of estimated selling costs were netted out of Real Estate Owned. The net balance carried in our statements of condition at June 30, 2009 was \$40 million.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

The carrying values and estimated fair values of our financial instruments were as follows:

	June 30, 2009		December 31, 2008	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Assets				
Cash and due from banks	\$ 19	\$ 19	\$ 130	\$ 130
Federal Funds sold and securities purchased under agreements to resell	8,790	8,790	1,580	1,580
Trading securities	1,659	1,659	866	866
Available-for-sale securities	11,095	11,095	2,142	2,142
Held-to-maturity securities	13,655	13,951	16,595	15,728
Advances ¹	27,192	27,395	38,140	38,334
MPF Loans held in portfolio, net	26,964	27,512	32,087	32,553
Accrued interest receivable	287	287	367	367
Derivative assets	55	55	102	102
Total Financial Assets	\$ 89,716	\$ 90,763	\$ 92,009	\$ 91,802
Financial Liabilities				
Deposits	\$ 1,186	\$ 1,186	\$ 757	\$ 757
Securities sold under agreements to repurchase	1,200	1,232	1,200	1,243
Consolidated obligations -				
Discount notes	40,286	40,892	29,466	29,480
Bonds ²	40,999	43,627	55,305	58,267
Accrued interest payable	355	355	567	567
Mandatorily redeemable capital stock	426	426	401	401
Derivative liabilities	864	864	1,067	1,067
Subordinated notes	1,000	960	1,000	1,083
Total Financial Liabilities	\$ 86,316	\$ 89,542	\$ 89,763	\$ 92,865

¹ Advances carried at fair value option: \$0 as of June 30, 2009 and \$201 million at December 31, 2008.

² Consolidated obligation bonds carried at fair value option: \$2.116 billion as of June 30, 2009 and \$0 at December 31, 2008.

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Note 15 – Commitments and Contingencies

For further details on commitments and contingencies, see Note 24 on page F-48 in our 2008 Form 10-K.

Consolidated obligations are recorded on a settlement date basis. We record a liability for consolidated obligations on our statements of condition for the proceeds we receive from the issuance of these consolidated obligations. For these issuances, we are designated as the primary obligor. However, each FHLB is jointly and severally obligated for the payment of all consolidated obligations of all of the FHLBs. No liability has been recorded for the joint and several obligations related to other FHLBs' primary obligation on consolidated obligations.

The par value of outstanding consolidated obligations for the FHLBs was \$1.056 trillion and \$1.252 trillion at June 30, 2009 and December 31, 2008. Accordingly, should one or more of the FHLBs be unable to repay the consolidated obligations for which they are the primary obligor, each of the other FHLBs could be called upon to repay all or part of such obligations, as determined or approved by the FHFA.

Our other commitments at the dates shown were as follows:

	<u>June 30, 2009</u>	<u>December 31, 2008</u>
MPF Xtra mortgage purchase commitments ¹	\$ 848	\$ 347
Standby letters of credit	716	857
Unsettled consolidated obligation bonds	290	-
Standby bond purchase agreements	245	168
Unconditional software license renewal fees	9	8
Delivery Commitments for MPF Loans	1	-
Advance commitments	1	1

¹ These are commitments outstanding to purchase MPF Xtra mortgage loans from our PFIs. We have a concurrent commitment to resell these loans to Fannie Mae.

We may be subject to various legal proceedings arising in the normal course of business. After consultation with legal counsel, management is not aware of any such proceedings that might result in our ultimate liability in an amount that would have a material effect on our financial condition or results of operations.

Note 16 – Transactions with Related Parties and Other FHLBs

Related Parties

We are a member-owned cooperative. We define related parties as members that own 10% or more of our capital stock or members whose officers or directors also serve on our Board of Directors. Capital stock ownership is a prerequisite to transacting any member business with us. Members and former members own all of our capital stock.

We conduct advance and MPF Loan business almost exclusively with members. Therefore, in the normal course of business, we extend credit to members whose officers and directors may serve on our Board of Directors. We extend credit to members whose officers or directors may serve as our directors on market terms that are no more favorable to them than the terms of comparable transactions with other members. In addition, we may purchase short-term investments, Federal Funds, and MBS from members (or affiliates of members). All investments are market rate transactions and all MBS are purchased through securities brokers or dealers. Derivative transactions with members and affiliates are executed at market rates.

Members

The table below summarizes balances we had with our members as defined above as related parties (including their affiliates) as reported in the statements of condition as of the dates indicated. Amounts in these tables may change between periods presented, to the extent that our related parties change, based on changes in the composition of our Board membership.

	<u>June 30, 2009</u>	<u>December 31, 2008</u>
Assets-		
Advances	\$ 855	\$ 1,150
Interest receivable - advances	3	4
Liabilities-		
Deposits	\$ 59	\$ 17

Federal Home Loan Bank of Chicago
Notes to Financial Statements - (Unaudited)
(Dollars in millions except per share amounts unless otherwise indicated)

Other FHLBs

The following table summarizes balances we had with other FHLBs as reported in the statements of condition:

	<u>June 30, 2009</u>	<u>December 31, 2008</u>
Liabilities-		
Deposits	\$ 8	\$ 9

Other FHLBs participating in the MPF Program must make deposits with us to support their transactions in the program. These deposits are reported on our statements of condition within interest-bearing deposits, with the respective changes being recorded as financing activities on our statements of cash flows.

The following table summarizes transactions we had with other FHLBs as reported in the statements of income:

	<u>2009</u>	<u>2008</u>
<u>Three months ended June 30,</u>		
Other Income - MPF Program transaction service fees	\$ 1	\$ 2
<u>Six months ended June 30,</u>		
Other Income - MPF Program transaction service fees	\$ 3	\$ 3
Loss on extinguishment of debt transferred to other FHLBs	(5)	-

As the MPF Provider, we record transaction service fees for services provided to other FHLBs in the MPF Program. Transaction service fees are recorded in other, net on our statements of income.

We record a transfer of our consolidated obligations to another FHLB as an extinguishment of debt because we have been released from being the primary obligor. See **Note 14 – Consolidated Obligations** in our 2008 Form 10-K for more information.

The following table summarizes transactions we had with other FHLBs as reported in the statements of cash flows.

	<u>2009</u>	<u>2008</u>
<u>Three months ended June 30,</u>		
Financing activities		
Net change in deposits	\$ 1	\$ (1)

	<u>2009</u>	<u>2008</u>
<u>Six months ended June 30,</u>		
Investing activities		
Purchase of MPF Loan participations from other FHLBs	\$ -	\$ 9

	<u>2009</u>	<u>2008</u>
Financing activities		
Net change in deposits	\$ (1)	\$ (2)
Transfer of consolidated obligation bonds to other FHLBs	(112)	-

MPF Loan participation interests purchased are recorded as investing activities in our statements of cash flows in MPF Loans - purchases (from other FHLBs).

During the second quarter of 2009, we purchased \$2.1 billion of MPF Loans from the FHLB Des Moines and concurrently sold them to Fannie Mae. We received a nominal fee for this transaction to cover our expenses incurred.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

**Item 2. Management's Discussion and Analysis of
Financial Condition and Results of
Operations.**

Forward-Looking Information

Statements contained in this report, including statements describing the objectives, projections, estimates, or future predictions of management, may be "forward-looking statements." These statements may use forward-looking terminology, such as "anticipates," "believes," "expects," "could," "estimates," "may," "should," "will," their negatives, or other variations of these terms. We caution that, by their nature, forward-looking statements involve risks and uncertainties related to our operations and business environment, all of which are difficult to predict and many of which are beyond our control. These risks and uncertainties could cause actual results to differ materially from those expressed or implied in these forward-looking statements and could affect the extent to which a particular objective, projection, estimate, or prediction is realized. As a result, undue reliance should not be placed on such statements.

These forward-looking statements involve risks and uncertainties including, but not limited to, the following: the effect of the requirements of the C&D Order impacting capital stock redemptions and dividend levels; changes to interest rate risk management policies to be implemented in response to the C&D Order; our ability to develop and implement business strategies focused on increasing net income and reducing expenses; general economic and market conditions, including the timing and volume of market activity, inflation/deflation, employment rates, housing prices, the condition of the mortgage and housing markets and the effects on, among other things, mortgage-backed securities; volatility of market prices, rates, and indices, or other factors, such as natural disasters, that could affect the value of our investments or collateral; changes in the value or liquidity of collateral securing advances to our members; changes in the value of and risks associated with our investments in mortgage loans and mortgage-backed securities and the related credit enhancement protections; changes in our ability or intent to hold mortgage-backed securities to maturity; changes in mortgage interest rates and prepayment speeds on mortgage assets; membership changes, including the withdrawal of members due to restrictions on redemption of our capital stock or the loss of large members through mergers and consolidations; changes in the demand by our members for advances; changes in the financial health of our members; competitive forces, including the availability of other sources of funding for our

members; changes to our capital structure from a new capital plan; our ability to attract and retain skilled employees; changes implemented by our regulator and changes in the FHLB Act or applicable regulations as a result of the Housing and Economic Recovery Act of 2008 or otherwise; the impact of new business strategies; our ability to successfully transition to a new business model and implement business process improvements; changes in investor demand for consolidated obligations and/or the terms of interest rate derivatives and similar agreements, including changes in the relative attractiveness of consolidated obligations as compared to other investment opportunities; instability in the credit and debt markets and the effect on future funding costs, sources and availability; political events, including legislative, regulatory, judicial, or other developments that affect us, our members, our counterparties and/or investors in consolidated obligations; the ability of each of the other FHLBs to repay the principal and interest on consolidated obligations for which it is the primary obligor and with respect to which we have joint and several liability; the pace of technological change and our ability to develop and support technology and information systems; our ability to introduce new products and services to meet market demand and to manage successfully the risk associated with new products and services, including new types of collateral used to secure advances; volatility resulting from the effects of, and changes in, various monetary or fiscal policies and regulations, such as those determined by the Federal Reserve Board and the Federal Deposit Insurance Corporation; the impact of new accounting standards and the application of accounting rules, including the impact of regulatory guidance on our application of such standards and rules; the volatility of reported results due to changes in the fair value of certain assets and liabilities and our ability to identify, manage, mitigate, and/or remedy internal control weaknesses and other operational risks.

For a more detailed discussion of the risk factors applicable to us, see **Risk Factors** in this Form 10-Q on page 87 and in our 2008 Form 10-K on page 23. These forward-looking statements are representative only as of the date they are made, and we undertake no obligation to update any forward-looking statement as a result of new information, future events, changed circumstances or any other reason.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

Selected Financial Data

	Three months ended					Six months ended	
	June 30, 2009	March 31, 2009	December 31, 2008	September 30, 2008	June 30, 2008	June 30, 2009	June 30, 2008
Selected statements of income data							
Interest income	\$ 753	\$ 788	\$ 936	\$ 935	\$ 903	\$ 1,541	\$ 1,901
Interest expense	594	644	839	883	881	1,238	1,848
Provision for credit losses	2	3	2	1	-	5	-
Net interest income	157	141	95	51	22	298	53
Non-interest income (loss)	(2)	(151)	(61)	10	(63)	(153)	(141)
Non-interest expense	29	29	34	28	33	58	64
Assessments	23	-	-	-	-	23	-
Net income (loss)	<u>\$ 103</u>	<u>\$ (39)</u>	<u>\$ -</u>	<u>\$ 33</u>	<u>\$ (74)</u>	<u>\$ 64</u>	<u>\$ (152)</u>
Selected ratios and data - annualized							
Net income (loss) to average assets	0.46%	-0.17%	0.00%	0.14%	-0.33%	0.14%	-0.34%
Return on average equity	24.82%	-6.42%	0.00%	4.61%	-10.31%	6.26%	-10.34%
Total average equity to average assets	1.84%	2.67%	2.95%	3.09%	3.16%	2.26%	3.29%
Non-interest expense to average assets	0.13%	0.13%	0.14%	0.12%	0.15%	0.13%	0.14%
Interest spread between yields on interest-earning assets and liabilities	0.58%	0.53%	0.31%	0.09%	-0.05%	0.55%	-0.03%
Net interest margin on interest-earning assets	0.70%	0.64%	0.42%	0.23%	0.10%	0.67%	0.12%

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

As of	June 30, 2009	March 31, 2009	December 31, 2008	September 30, 2008	June 30, 2008
Selected statements of condition data					
Federal Funds sold and securities purchased under agreements to resell	\$ 8,790	\$ 3,010	\$ 1,580	\$ 550	\$ 7,265
Investment securities	26,409	18,062	19,603	20,513	16,599
Advances	27,192	31,197	38,140	35,469	34,679
MPF Loans held in portfolio, net of allowance for credit losses	26,964	29,825	32,087	32,841	33,763
Total assets	89,870	83,750	92,129	91,369	92,827
Total deposits	1,186	1,352	757	1,063	808
Total consolidated obligations, net ¹	81,285	76,162	84,771	83,882	85,923
Subordinated notes	1,000	1,000	1,000	1,000	1,000
Total liabilities	88,172	82,298	89,842	88,478	90,034
Capital stock	2,375	2,355	2,386	2,561	2,548
Retained earnings	837	734	540	540	507
Accumulated other comprehensive income (loss)	(1,514)	(1,637)	(639)	(210)	(262)
Total capital	1,698	1,452	2,287	2,891	2,793
Other selected data					
Regulatory capital and Designated Amount of subordinated notes	\$ 4,638	\$ 4,498	\$ 4,327	\$ 4,279	\$ 4,235
Regulatory capital to assets ratio ²	5.16%	5.37%	4.70%	4.68%	4.56%
All FHLBs consolidated obligations outstanding (par) ³	\$ 1,055,864	\$ 1,135,380	\$ 1,251,542	\$ 1,327,904	\$ 1,255,475
Number of members	814	814	816	819	825
Number of advance borrowers ⁴	571	581	598	591	571
Headcount (full-time)	319	313	313	310	315
Headcount (part-time including summer interns)	21	8	8	6	9
Advances as a percent of total assets	30%	37%	41%	39%	37%
MPF Loans as a percent of total assets	30%	36%	35%	36%	36%

¹ Total consolidated obligations, net, represents the consolidated obligations for which we are the primary obligor.

² The regulatory capital to assets ratio includes the Designated Amount of subordinated notes in regulatory capital.

³ We are jointly and severally liable for the consolidated obligations of the other FHLBs. See **Note 14 – Consolidated Obligations** on page F-24 in the 2008 Form 10-K.

⁴ Advance borrowers are members or former members that have an outstanding advance in the period.

Federal Home Loan Bank of Chicago
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Executive Summary

We recorded net income of \$103 million for the quarter ending June 30, 2009. Net interest income and income from derivative and hedging activities more than offset the net impact of \$124 million of other-than-temporary impairment (OTTI) charges on our private-label MBS portfolio. While the hedging activities produced positive results in the second quarter, such outcomes are highly variable and indicative of the continued complexity of the balance sheet and, therefore, should not be interpreted as a trend. While we are making progress in transitioning our investments away from fixed-rate mortgages, our results may continue to be impacted by volatility in derivative values and hedging expenses for some time to come. Additional highlights from the quarter are as follows:

- Total assets fell 2% from year-end 2008 to \$89.9 billion at June 30, 2009, as the availability of government funding programs and other sources of market liquidity, high levels of customer deposits, and the sluggish economy contributed to our members' reduced borrowing needs. Advances outstanding at the end of the second quarter 2009 were \$27.2 billion, 29% less than at year-end 2008.
- Retained earnings at June 30, 2009 were \$837 million, 55% higher than year-end 2008; \$233 million of this increase resulted from changes in the accounting treatment of OTTI impairments on our private-label MBS portfolio. On January 1, 2009, we recorded a cumulative effect of non-credit impairment adjustments for the prior year of \$233 million in accordance with new accounting guidance on the recognition and presentation of OTTI, as further discussed in **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations**.
- We remain in compliance with all of our regulatory capital requirements.

Summary of Financial Results

Net interest income for the quarter ending June 30, 2009, was \$157 million, compared to \$22 million in the second quarter of the previous year. Interest income for the second quarter of 2009 of \$753 million was 17% lower than interest income of \$903 million in the second quarter of 2008, reflecting the lower rate environment, lower advance levels, and the continuing reduction of our holdings of higher-yielding MPF Loans in portfolio due to prepayments. As we have previously disclosed, we have undertaken an investment strategy focused on agency MBS and other lower-credit risk investments in an effort to reduce the underlying risk profile of the investment portfolio and simplify the hedging activities associated with it.

Interest expense fell 33% from \$881 million in the second quarter of 2008 to \$594 million as we called higher-cost debt and replaced it with shorter-term, lower-cost discount notes.

Non-interest loss of \$2 million resulted primarily from a \$124 million net charge on the other-than-temporary impairment of our private-label MBS investment portfolio, offsetting income of \$122 million from derivative and hedging activities.

The **OTTI** net charge represents anticipated credit losses (those due to projected cash shortfalls on the underlying securities), excluding non-credit losses (primarily the result of current market conditions). We analyze our portfolio of mortgage-backed securities each quarter to assess both credit and non-credit losses. We expect that we will experience additional OTTI charges in future reporting periods, but cannot predict the level of those charges.

Income from **derivatives and hedging activities** for the second quarter of 2009 of \$122 million reflects the continuing volatility in the market and its effect on the concentration of mortgage assets and associated hedges on our balance sheet. Because of the continuing interest rate volatility, we can expect continuing fluctuation in derivatives and hedging income/expense. During the second quarter of 2009, we terminated a portion of fair value hedges of consolidated obligation bonds that resulted in \$155 million of deferred hedging adjustments on the underlying bonds. These costs will be amortized into interest expense over the remaining life of the underlying consolidated obligations as such bonds remain outstanding. As the composition of the balance sheet transitions from one with mortgages making up the majority of assets to one where advances and investments that are less sensitive to interest rate volatility predominate, we expect to continue to see fluctuations in the income and losses from derivatives and hedging. As we make progress in this transition, we expect a reduction in significant fluctuations in the impact of hedging on income in future years.

Advances fell \$10.9 billion (29%) from \$38.1 billion at year-end 2008 to \$27.2 billion at the end of the second quarter of 2009, a reversal of the upward trend in advances over the course of 2008. We believe that this decrease reflects members' reduced borrowing needs resulting from the availability of liquidity through various federal government funding programs, an increase in deposits for many of our members, and the state of the economy. While members across our district have experienced reduced demand, the reduction in advances was concentrated in two large institutions.

We were able to provide unusually high levels of liquidity to members during the height of the credit crisis in 2008,

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illustrating our ability to react quickly to changes in member needs. While remaining a reliable source of liquidity to our members is a crucial role for this Bank, our focus on growing our advances portfolio is to, over time, increase the amount of term financing used by our members. Increasing the advances book in this manner is core to our strategy for transitioning the Bank over the next few years.

Total MPF Loans held in portfolio were \$27.0 billion at June 30, 2009, a reduction of \$5.1 billion (16 %) from year-end 2008 and down \$6.8 billion from the second quarter of 2008. Since the MPF Xtra product was introduced in September 2008, approximately 169 of our PFIs have activated MPF Xtra master commitments and more than 85% of them have delivered loans. The rate environment in the first half of 2009 prompted increases in the volume of loans sold through the MPF Xtra product, surpassing \$2.3 billion to-date for our members and \$0.1 billion for the members of other participating FHLBs. Three other FHLBs began offering the MPF Xtra product to their PFIs during the second quarter of 2009.

Member Credit, Member Collateral, Member Cooperative

Twelve of our members have been resolved by the Federal Deposit Insurance Corporation through the time of filing on August 12, 2009. Our advances were either fully repaid at the time of the resolution or the outstanding obligations were assumed by other financial institutions. We continue to see the effects of the economy stressing some members' earnings and capital positions and expect to see additional resolutions in the coming months.

Rating Change

On July 13, Standard and Poor's upgraded the Bank's counterparty credit rating to AA+ with a stable outlook. S&P cited the Bank's "strong asset quality, solid balance-sheet liquidity, low funding costs, and improving but adequate risk management."

Capital Stock Conversion

We are in the midst of discussions with our regulator regarding a capital stock conversion plan. We believe that stabilizing our capital stock is fundamental to the successful transition of the Bank. We wish to convert as expeditiously as possible so that we can turn our attention to the execution of tactical plans designed to:

- expand our member relationships, including the use of advances, letters of credit, and the MPF Xtra product;
- complete the transition of the balance sheet; and
- appropriately scale our operating expenses.

Financial Outlook

We are in the midst of a transition from a business model that had become increasingly reliant on single-family, fixed-rate mortgages supported by voluntary stock, to a more traditional FHLB model supported by advances to our members. This "Advances" Bank model features the following general concepts:

- *The scale of the Bank will be defined by the size of the advances book, such that the spread on the advances book is expected to cover operating expenses for the Bank, except for those associated with the MPF Program:* We believe that the size of the advances book will, over time, determine the funding available to cover operating expenses.
- *A plan to use the anticipated spread on the investment book to grow retained earnings and to pay an appropriate dividend to members when earnings and risk considerations merit such a payment:* In order to provide for growth in retained earnings and restore at least a nominal dividend once a sustainable level of profitability is restored, we plan to continue to direct our investment decisions toward instruments that have limited credit risk and that we believe are simpler to hedge.
- *The MPF Program is expected to be supported by fees:* We plan to continue to offer off-balance sheet MPF products on a fee-for-service basis. The operating expenses associated with supporting other FHLBs in the program will be offset by fees from the participating banks.

Our goal is to transition the Bank so that it generates consistent earnings, builds retained earnings, restores at least a nominal dividend, and, ultimately, provides enhanced liquidity for members' stock.

We expect that our balance sheet will continue to be impacted by volatility in the financial markets. Further, we have experienced and anticipate further prepayments of our MPF and MBS assets. Although these assets have prepaid, in many cases the funding for these assets remains outstanding. OTTI charges are highly dependent on economic conditions and could increase in future quarters if such conditions deteriorate. In addition, our future results may be constrained by economic scenarios and political decisions outside of our control.

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Results of Operations

	Three months ended June 30,			Six months ended June 30,		
	2009	2008	Change	2009	2008	Change
Interest income	\$ 753	\$ 903	-17%	\$ 1,541	\$ 1,901	-19%
Interest expense	594	881	-33%	1,238	1,848	-33%
Provision for credit losses	2	-	n/m	5	-	n/m
Net interest income	157	22	614%	298	53	462%
Non-interest income (loss)	(2)	(63)	97%	(153)	(141)	-9%
Non-interest expense	29	33	-12%	58	64	-9%
Assessments	23	-	n/m	23	-	n/m
Net income (loss)	<u>\$ 103</u>	<u>\$ (74)</u>	<u>239%</u>	<u>\$ 64</u>	<u>\$ (152)</u>	<u>142%</u>
Net interest margin on interest-earning assets	0.70%	0.10%	0.60%	0.67%	0.12%	0.55%

n/m = not meaningful

Increase (Decrease) in Net Interest Income Due to Changes in Volume/Rates

The following table details the increase or decrease in interest income and expense due to volume or rate variances. In this analysis, the change due to the combined volume/rate variance has been allocated to rate. The calculation is based on a comparison of average balances and rates for the three and six months ended June 30, 2009 versus June 30, 2008.

	For the three months ended June 30, 2009 versus 2008			For the six months ended June 30, 2009 versus 2008		
	Volume	Rate	Net Change	Volume	Rate	Net Change
Increase (decrease) in net interest due to						
Assets						
Federal Funds sold and securities purchased under agreements to resell	\$ 7	\$ (43)	\$ (36)	\$ (2)	\$ (98)	\$ (100)
Total investments	127	(29)	98	217	(55)	162
Advances	(41)	(80)	(121)	(28)	(239)	(267)
MPF Loans held in portfolio	(75)	(16)	(91)	(121)	(34)	(155)
Total interest-earning assets	<u>\$ 18</u>	<u>\$ (168)</u>	<u>\$ (150)</u>	<u>\$ 66</u>	<u>\$ (426)</u>	<u>\$ (360)</u>
Liabilities and Capital						
Interest bearing deposits	\$ 1	\$ (5)	\$ (4)	\$ -	\$ (13)	\$ (13)
Securities sold under agreements to repurchase	-	(5)	(5)	-	(14)	(14)
Consolidated obligation discount notes	133	(192)	(59)	290	(444)	(154)
Consolidated obligation bonds	(274)	56	(218)	(458)	30	(428)
Mandatorily redeemable capital stock	-	-	-	-	-	-
Subordinated notes	-	(1)	(1)	-	(1)	(1)
Total interest-bearing liabilities	<u>\$ (140)</u>	<u>\$ (147)</u>	<u>\$ (287)</u>	<u>\$ (168)</u>	<u>\$ (442)</u>	<u>\$ (610)</u>
Net interest income on interest-earning assets before allowance for credit losses	<u>\$ 158</u>	<u>\$ (21)</u>	<u>\$ 137</u>	<u>\$ 234</u>	<u>\$ 16</u>	<u>\$ 250</u>

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Average Balances/Net Interest Margin/Rates

The following tables detail the components of net interest income.

- Contractual Interest and Yield/Rate are based on average amortized cost balances including premium and discount amortization of \$18 million and \$12 million on MPF Loans held in portfolio during the three months ended June 30, 2009 and 2008, and \$33 million and \$23 million for the corresponding six month periods.
- Total Interest and Effective Yield/Rate includes all other components of interest, including net interest payments or receipts on derivatives, hedge accounting amortization, prepayment fees, and credit enhancement fees. The impact on net interest income related to prior hedging activities is also shown separately as hedge accounting amortization.
- Non-accrual MPF Loans held in portfolio are included in average balances used to determine the yield.
- Average balances and yields are computed using amortized cost balances. They do not include changes in fair value that are reflected as a component of stockholders' equity, nor do they include the effect of OTTI related to non-credit losses.

	Average Balance	Contractual Interest		Total Interest	Effective Yield/ Rate	Hedge Accounting Amortization
		Income/ Expense	Yield/ Rate			
For the three months ended June 30, 2009						
Federal Funds sold and securities purchased under agreements to resell	\$ 8,283	\$ 4	0.19%	\$ 4	0.19%	\$ -
Investments	25,286	269	4.26%	269	4.26%	-
Advances	29,006	221	3.05%	157	2.17%	(15)
MPF Loans held in portfolio	27,677	363	5.25%	323	4.67%	2
Total Interest Income	90,252	857	3.80%	753	3.34%	(13)
Deposits	1,184	1	0.34%	1	0.34%	-
Securities sold under agreements to repurchase	1,200	7	2.33%	7	2.33%	-
Consolidated obligation discount notes	40,346	36	0.36%	40	0.40%	4
Consolidated obligation bonds	41,904	493	4.71%	532	5.08%	32
Mandatorily redeemable capital stock	424	-	0.00%	-	0.00%	-
Subordinated notes	1,000	14	5.60%	14	5.60%	-
Total Interest Expense	86,058	551	2.56%	594	2.76%	36
Net interest margin on interest earning assets	\$ 90,252	\$ 306	1.36%	\$ 159	0.70%	\$ (49)
Interest Spread			1.24%		0.58%	
Average interest-earning assets to interest-bearing liabilities					104.87%	
For the three months ended June 30, 2008						
Federal Funds sold and securities purchased under agreements to resell	\$ 7,033	\$ 40	2.23%	\$ 40	2.23%	\$ -
Investments	14,509	170	4.73%	171	4.73%	-
Advances	34,124	310	3.59%	278	3.22%	1
MPF Loans held in portfolio	33,763	446	5.32%	414	4.90%	-
Total Interest Income	89,429	966	4.32%	903	4.02%	1
Deposits	1,069	5	2.00%	5	2.00%	-
Securities sold under agreements to repurchase	1,201	12	4.03%	12	4.03%	-
Consolidated obligation discount notes	17,084	92	2.14%	99	2.29%	7
Consolidated obligation bonds	65,988	773	4.69%	750	4.55%	6
Mandatorily redeemable capital stock	179	-	0.00%	-	0.00%	-
Subordinated notes	1,000	15	5.68%	15	5.69%	-
Total Interest Expense	86,521	897	4.14%	881	4.07%	13
Net interest margin on interest earning assets	\$ 89,429	\$ 69	0.31%	\$ 22	0.10%	\$ (12)
Interest Spread			0.18%		-0.05%	
Average interest-earning assets to interest-bearing liabilities					103.36%	

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	Average Balance	Contractual Interest		Total Interest	Effective Yield/ Rate	Hedge Accounting Amortization
		Income/ Expense	Yield/ Rate			
For the six months ended June 30, 2009						
Federal Funds sold and securities purchased under agreements to resell	\$ 7,291	\$ 7	0.19%	\$ 7	0.19%	\$ -
Investments	22,357	497	4.45%	497	4.45%	-
Advances	31,546	472	2.99%	349	2.21%	(20)
MPF Loans held in portfolio	29,088	765	5.26%	688	4.73%	3
Total Interest Income	90,282	1,741	3.86%	1,541	3.41%	(17)
Deposits	1,103	1	0.18%	1	0.18%	-
Securities sold under agreements to repurchase	1,200	17	2.83%	17	2.83%	-
Consolidated obligation discount notes	37,130	71	0.38%	82	0.44%	11
Consolidated obligation bonds	45,793	1,072	4.68%	1,110	4.85%	42
Mandatorily redeemable capital stock	416	-	0.00%	-	0.00%	-
Subordinated notes	1,000	28	5.60%	28	5.60%	-
Total Interest Expense	86,642	1,189	2.74%	1,238	2.86%	53
Net interest margin on interest earning assets	\$ 90,282	\$ 552	1.22%	\$ 303	0.67%	\$ (70)
Interest Spread			<u>1.12%</u>		<u>0.55%</u>	
Average interest-earning assets to interest-bearing liabilities					<u>104.20%</u>	
For the six months ended June 30, 2008						
Federal Funds sold and securities purchased under agreements to resell	\$ 7,458	\$ 107	2.83%	\$ 107	2.83%	\$ -
Investments	13,574	334	4.94%	335	4.94%	-
Advances	33,057	644	3.85%	616	3.69%	(2)
MPF Loans held in portfolio	33,980	899	5.32%	843	4.96%	1
Total Interest Income	88,069	1,984	4.51%	1,901	4.30%	(1)
Deposits	1,092	14	2.53%	14	2.53%	-
Securities sold under agreements to repurchase	1,201	31	5.06%	31	5.06%	-
Consolidated obligation discount notes	16,570	223	2.67%	236	2.82%	13
Consolidated obligation bonds	65,192	1,557	4.78%	1,538	4.72%	17
Mandatorily redeemable capital stock	144	-	0.00%	-	0.00%	-
Subordinated notes	1,000	29	5.68%	29	5.69%	-
Total Interest Expense	85,199	1,854	4.35%	1,848	4.33%	30
Net interest margin on interest earning assets	\$ 88,069	\$ 130	0.30%	\$ 53	0.12%	\$ (31)
Interest Spread			<u>0.16%</u>		<u>-0.03%</u>	
Average interest-earning assets to interest-bearing liabilities					<u>103.37%</u>	

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Net Interest Income

Net interest income is the difference between interest income that we receive from advances, MPF Loans, investment securities and other highly liquid short-term investments (such as Federal Funds sold), and our funding costs, which include consolidated obligations, subordinated notes, and other borrowings.

The increase in total net interest income was principally due to the following:

- During the three and six months ended June 30, 2009, we continued to increase our holdings in agency mortgage-backed securities and we invested in FFELP student loan ABS to reduce the negative effect to earnings caused by the prepayment of mortgage assets and maturities of advances during the periods.
- During the three and six months ended June 30, 2009, we continued to replace a portion of our longer-term, higher-rate term debt with shorter-term, lower yielding discount notes. As a result, we were able to take advantage of the lower funding costs on short-term debt prior to the anticipated prepayment of our mortgage assets. For a discussion of how this funding strategy may impact us, see page 29 in the **Risk Factors** section of our 2008 Form 10-K.

The increase in net interest income was partially offset by the following:

- We had a decline in member demand for advances in the three and six months ended June 30, 2009 compared to the same periods in 2008, in addition to a reduction in the yields we earned on our remaining Advance portfolio. We believe that the decrease in demand reflects members' reduced borrowing needs resulting from the availability of liquidity through various federal government funding programs, an increase in deposits for many of our members, and the state of the economy. While members across our district have experienced reduced demand, the reduction in advances was concentrated in two large institutions. We also experienced an increase in advance prepayment activity, and the amount of advance prepayment fees included in interest income was \$11 million and \$14 million for the three and six months ended June 30, 2009, compared to less than \$1 million and \$12 million for the corresponding periods of 2008.
- As of June 30, 2009, MPF Loans held in portfolio, which historically have been higher yielding assets for us, fell more than \$5 billion from December 31, 2008, and were down \$6.8 billion from June 30, 2008 as the low mortgage rate environment increased prepayment

activity during that time. Therefore the interest income earned from MPF Loans was reduced.

- We hedge our duration and convexity profile by using a combination of derivatives placed in hedge accounting relationships. As our duration and convexity profile changed over time as MPF Loan prepayments increased or decreased, certain hedge accounting relationships were de-designated. This has resulted in hedging adjustments of consolidated obligations, MPF Loans and amounts in other comprehensive income being deferred and recognized as negative yield adjustments to the underlying assets or liabilities still outstanding or cash flows being hedged. These yield adjustments continued to negatively impact our net interest income in the first three and six months of 2009. Over the next three 12-month periods, we expect that \$7 million, \$10 million, and \$13 million of deferred cash flow hedging charges recorded in AOCI as of June 30, 2009, will be recognized as a reduction to net interest income.

Non-Interest Income

	Three Months ended June 30,		Six Months ended June 30,	
	2009	2008	2009	2008
Non-interest income (loss) -				
OTTI impairment charges, net	\$ (124)	\$ (30)	\$ (210)	\$ (63)
Trading securities	(2)	(15)	(11)	-
Sale of available-for-sale securities	-	-	19	-
Derivatives and hedging activities	122	(20)	50	(82)
Instruments held at fair value option	(1)	-	(2)	-
Early extinguishment of debt	-	-	(5)	-
Other, net	3	2	6	4
Total non-interest income (loss)	\$ (2)	\$ (63)	\$ (153)	\$ (141)

Other-Than-Temporary Impairment

During the three and six months ended June 30, 2009, we recognized OTTI charges on certain private-label MBS investments collateralized primarily by first-lien mortgages to subprime borrowers. In estimating our expected credit loss with respect to these MBS, we have made certain assumptions regarding the underlying collateral including default rates, loss severities, prepayment rates, and projected delinquency rates which ultimately factor in our estimated future recovery of expected cash flows. See **Note 5 – Investment Securities** to the financial statements for further detail.

Derivatives and Hedging Activities

Non-interest income (loss) also includes net gains or losses from derivatives and hedging activities and net gains or losses on economically hedged trading securities.

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We hedge our duration and convexity profile by using a combination of derivatives placed in fair value, cash flow, or economic hedge relationships as defined under hedge accounting standards. We continually evaluate our hedging policies and practices in an effort to minimize the negative impact on future earnings, while maintaining what we believe is a prudent approach to managing our market risk.

Our results from derivatives and hedging activities, and the change in fair value on our economically hedged trading securities, resulted in gains of \$120 million and \$39 million for the three and six months ended June 30, 2009, as detailed below:

Fair Value Hedges

- Fair value hedges of consolidated obligation bonds resulted in a net gain of \$22 million and \$32 million for the three and six months ended June 30, 2009. The majority of this ineffectiveness resulted from the difference in rate sensitivities between interest rate swaps used as hedges and the consolidated obligation bonds being hedged by those swaps. In addition, we terminated a portion of fair value hedges of consolidated obligation bonds that resulted in \$155 million of deferred hedging adjustments on the underlying bonds. These costs will be amortized into interest expense over the remaining life of the underlying consolidated obligations as such bonds remain outstanding.
- We recorded a loss of \$16 million hedging the duration and convexity of a portion of our MPF Loans during the six months ended June 30, 2009, as the options purchased to offset the embedded prepayment option lost value as the contractual term of the options neared expiration.

Economic Hedges

- Historically, we have used a combination of interest rate derivatives and callable consolidated obligation bonds to economically hedge the duration and convexity risks associated with a portion of our MPF Loan portfolio. Throughout 2008 and early 2009, we called a large portion of our callable debt and relied more on the use of economic hedges with interest rate derivatives to hedge our MPF Loan portfolio. In general, rising interest rates, even in the short-term, will have a positive short-term impact on derivative and hedging activities, and may result in temporary gains being recognized. In general, as rates fall and the likelihood of prepayment of the underlying mortgage portfolio increases, it becomes more expensive to hedge the portfolio. During the three months ended June 30, 2009, compared to the first quarter of 2009, interest rate volatility increased significantly in an upward trending interest rate environment, which positively impacted the value of some of these economic hedges and resulted in a \$93 million and \$27 million gain during the three and six months ended June 30, 2009. As market volatility stabilizes, as it did during the first quarter of 2009, these gains are expected to reverse in subsequent periods.
- A portion of our trading securities are hedged economically with interest rate swaps. Changes in fair value of these swaps are recognized in derivatives and hedging activities and are typically offset by the changes in fair value on the trading securities. During the three and six months ended June 30, 2009, we recognized unrealized losses on trading securities of \$2 million and \$11 million and losses from the interest rate swaps hedging these securities of \$1 million in both periods. The loss on trading securities was mainly due to the widening of spreads between LIBOR and government agency securities in the first quarter of 2009, in addition to a rise in LIBOR offsetting a tightening of those spreads during the second quarter of 2009.

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The following table summarizes the types of hedges and the categories of hedged items that contributed to the gains and losses on derivatives and hedging activities that were recorded as a component of non-interest income (loss):

	Three months ended June 30, 2009				Three months ended June 30, 2008			
	Fair Value	Cash Flow	Economic	Total	Fair Value	Cash Flow	Economic	Total
Hedged Item -								
Advances	\$ 3	\$ -	\$ -	\$ 3	\$ (1)	\$ -	\$ -	\$ (1)
Consolidated obligations	22	3	2	27	(4)	-	-	(4)
Trading securities	-	-	-	-	-	-	14	14
MPF Loans	(1)	-	93	92	(7)	-	(20)	(27)
Delivery commitments on MPF Loans	-	-	*	*	-	-	(2)	(2)
Total derivatives and hedging activities	<u>\$ 24</u>	<u>\$ 3</u>	<u>\$ 95</u>	<u>122</u>	<u>\$ (12)</u>	<u>\$ -</u>	<u>\$ (8)</u>	<u>(20)</u>
Change in fair value on trading securities				(2)				(15)
Total				<u>\$ 120</u>				<u>\$ (35)</u>

	Six months ended June 30, 2009				Six months ended June 30, 2008			
	Fair Value	Cash Flow	Economic	Total	Fair Value	Cash Flow	Economic	Total
Hedged Item -								
Advances	\$ 2	\$ -	\$ -	\$ 2	\$ (1)	\$ -	\$ -	\$ (1)
Consolidated obligations	32	5	1	38	(16)	-	-	(16)
Trading securities	-	-	(1)	(1)	-	-	(6)	(6)
MPF Loans	(16)	-	27	11	(15)	-	(39)	(54)
Delivery commitments on MPF Loans	-	-	*	*	-	-	(5)	(5)
Total derivatives and hedging activities	<u>\$ 18</u>	<u>\$ 5</u>	<u>\$ 27</u>	<u>50</u>	<u>\$ (32)</u>	<u>\$ -</u>	<u>\$ (50)</u>	<u>(82)</u>
Change in fair value on trading securities				(11)				-
Total				<u>\$ 39</u>				<u>\$ (82)</u>

* less than \$1 million

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Early Extinguishment of Debt

During the first quarter of 2009, we extinguished a portion of our term debt in anticipation of the prepayment of our mortgage assets in a lower mortgage rate environment. We recognized a loss of \$5 million on early debt extinguishments during the period, which was offset by a gain of \$6 million on the sale of AFS securities economically hedging the extinguished debt. We did not have any early debt extinguishment during the second quarter of 2009 or during the three and six months ended June 30, 2008.

Non-Interest Expense

For the periods ended June 30,	Three months		Six months	
	2009	2008	2009	2008
Compensation and benefits -				
Wages & benefits	\$ 13	\$ 11	\$ 24	\$ 25
Incentive plans	3	2	6	3
Severance	*	5	*	6
Compensation and benefits	16	18	30	34
Professional fees	3	5	5	7
Amortization and depreciation	4	4	8	9
Finance Board/Finance Agency & Office of Finance expenses	2	1	3	2
Other expense -				
Occupancy costs	1	2	2	3
Office relocation costs	*	1	*	1
Other operating expenses	3	2	10	8
Other expense	4	5	12	12
Total non-interest expense	\$ 29	\$ 33	\$ 58	\$ 64

* less than \$1 million

We continue to make progress on our strategic objective to reduce non-interest expenses, which are down 12% and 9% for the three and six months ended June 30, 2009 from the same periods in 2008. Much of this decrease reflects minimal severance costs to date in 2009 compared to the same period in 2008.

Our decision to move our office to a smaller, more economical space during the third quarter of 2009 is expected to reduce future operating expenses. However, as we continue to improve our systems and operations by investing in automation and process redesign, future costs may temporarily offset expense reductions with a goal of decreasing expenses on a long-term basis.

Assessments

AHP and REFCORP assessments are calculated as a percentage of income before assessments, calculated on an annualized year-to-date basis. Losses in one quarter may be used to offset income in other quarters, but only within the same calendar year. Losses for an entire year can not be carried back or carried forward and used as a credit against other years.

We adopted new OTTI accounting guidance effective January 1, 2009. The initial effect of adoption was to recognize a cumulative effect adjustment to the opening balance of our retained earnings of \$233 million. This adjustment had no impact on our AHP or REFCORP expense or accruals.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

Statements of Condition

All comparisons in the following narrative in this section are based on the below table, comparing June 30, 2009 to December 31, 2008 unless otherwise stated.

As of:	June 30, 2009	December 31, 2008	Change
Assets			
Cash and due from banks	\$ 19	\$ 130	-85%
Federal Funds sold and securities purchased under agreement to resell	8,790	1,580	456%
Investment securities	26,409	19,603	35%
Advances	27,192	38,140	-29%
MPF Loans held in portfolio, net	26,964	32,087	-16%
Other assets	496	589	-16%
Total assets	<u>\$ 89,870</u>	<u>\$ 92,129</u>	<u>-2%</u>
Liabilities and Capital			
Consolidated obligation discount notes	\$ 40,286	\$ 29,466	37%
Consolidated obligation bonds	40,999	55,305	-26%
Other liabilities	5,887	4,071	45%
Subordinated notes	1,000	1,000	-
Total liabilities	<u>88,172</u>	<u>89,842</u>	<u>-2%</u>
Capital stock	2,375	2,386	0%
Retained earnings	837	540	55%
Accumulated other comprehensive income (loss)	(1,514)	(639)	-137%
Total capital	<u>1,698</u>	<u>2,287</u>	<u>-26%</u>
Total liabilities and capital	<u>\$ 89,870</u>	<u>\$ 92,129</u>	<u>-2%</u>
Regulatory capital stock plus Designated Amount of subordinated notes	<u>\$ 3,801</u>	<u>\$ 3,787</u>	<u>0%</u>

Cash and due from banks

We held minimal excess cash directly at the Federal Reserve Bank at June 30, 2009, due in part to more favorable investment alternatives such as the Federal Funds market or other investment security markets.

Federal Funds Sold and Securities Purchased under Agreements to Resell

We have increased our outstanding Federal Funds sold and securities purchased under agreements to resell as advances and mortgage-related assets have paid down; which provided us necessary liquidity to support member advances, purchase replacement assets, and manage our regulatory capital ratios.

Investment Securities

Consistent with our strategy of reinvesting proceeds from the paydown in mortgage related assets, our investment securities balance increased, primarily as we have begun purchasing alternative investments that we believe have lower credit risk and that are easier to hedge, such as FFELP student loan ABS, as approved by the FHFA. At June 30, 2009, we held \$5.1 billion in such ABS.

The following table summarizes our investment securities by issuer with a carrying value exceeding 10% of our total capital:

Issuer as of June 30, 2009	Carrying Value	Fair Market Value
Fannie Mae	\$ 10,185	\$ 10,477
Freddie Mac	6,011	6,175
SLM Student Loan Trust SLMA 2009-1 A	2,208	2,208
SLM Student Loan Trust SLMA 2009-2 A	1,858	1,858
SLM Student Loan Trust SLMA 2009-1 A1	1,029	1,029
Ginnie Mae	646	647
Citibank, NA (TLGP)	401	401
All Others	4,071	3,910
Total Investments	<u>\$ 26,409</u>	<u>\$ 26,705</u>

At June 30, 2009 and December 31, 2008, we did not hold any collateralized debt obligation (CDO) securities.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

Advances

The following table sets forth the outstanding par amount of advances of the largest five advance borrowers:

As of	Five Largest Advance Borrowers			
	June 30, 2009		December 31, 2008	
	Par	%	Par	%
M & I Marshall & Ilsley Bank	\$ 2,601	10%	\$ 2,600	7%
Harris National Association	2,375	9%	2,375	6%
Bank of America ¹	2,251	8%	4,416	12%
State Farm, F.S.B.	1,750	7%	n/a	-
PNC Financial Services Group, Inc. ²	1,343	5%	n/a	-
One Mortgage Partners Corp. ³	n/a	-	2,900	8%
Associated Bank, National Association	n/a	-	2,718	7%
All Other Members	16,455	61%	22,521	60%
Total advances at par	<u>\$ 26,775</u>	<u>100%</u>	<u>\$ 37,530</u>	<u>100%</u>

n/a Was not in the top five list for the date indicated.

¹ Formerly LaSalle Bank, N.A., became ineligible for membership due to an out-of-district merger into Bank of America, N.A. effective October 17, 2008. Its outstanding advances are payable per the original contract terms.

² Formerly MidAmerica Bank, FSB, became ineligible for membership due to an out-of-district merger into National City Bank, effective February 9, 2008. Effective December 31, 2008, National City Corporation merged into PNC Financial Services Group, Inc. Its outstanding advances are payable per the original contract terms.

³ One Mortgage Partners Corp. is a subsidiary of JPMorgan Chase & Co.

Advances fell from year-end 2008 to the end of the second quarter of 2009, a reversal of the upward trend in advances over the course of 2008. We believe that this decrease reflects members' reduced borrowing needs resulting from the availability of liquidity through various

federal government funding programs, an increase in deposits for many of our members, and the state of the economy. While members across our district have experienced reduced demand, the reduction in advances was concentrated in two large institutions.

MPF Loans

Due to economic conditions, we experienced higher rates of prepayments of MPF Loans during the first six months of 2009 compared to historical trends. The decline in market mortgage rates made it economical for a greater number of existing borrowers to refinance their mortgages. If mortgage rates stay at historically low levels, we would expect prepayments to remain at elevated levels. However, if mortgage rates increase, we would expect early prepayments on our MPF Loan portfolio to slow. We can not predict the extent to which future mortgage rates will rise or fall.

In addition, while we no longer enter into master commitments to acquire new MPF Loans for investment on our balance sheet (except for immaterial amounts of MPF Loans to support affordable housing that are guaranteed by the Rural Housing Service (RHS) or insured by the Department of Housing and Urban Development (HUD)), we continue to expand our MPF Xtra program where we buy MPF Loans from our members (and from the members of other FHLBs) and concurrently sell the loans to Fannie Mae. The volume of loans sold for our members and the members of other participating FHLBs MPF Xtra product loans totaling \$1.1 billion and \$2.4 billion for the three and six months ended June 30, 2009. For a description of the MPF Xtra product, see **Credit Risk-MPF Loans** on page 78 of this Form 10-Q.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

The following tables summarize MPF Loans held in portfolio by product and property type:

As of June 30, 2009	Medium Term ¹	Long Term ²	Total
MPF Program type-			
Conventional loans-			
Original MPF	\$ 1,304	\$ 2,802	\$ 4,106
MPF 100	1,302	2,261	3,563
MPF 125	245	531	776
MPF Plus	5,450	8,984	14,434
Government loans	208	3,543	3,751
Total par value of MPF Loans	\$ 8,509	\$ 18,121	26,630
Agent fees, premium (discount)			116
Loan commitment basis adjustment			(13)
SFAS 133 hedging adjustments			237
Receivable from future performance credit enhancement fees			3
Allowance for credit loss			(9)
Total MPF Loans, net			\$ 26,964

As of December 31, 2008	Medium Term ¹	Long Term ²	Total
MPF Program type-			
Conventional loans-			
Original MPF	\$ 1,639	\$ 3,967	\$ 5,606
MPF 100	1,608	3,100	4,708
MPF 125	304	725	1,029
MPF Plus	6,106	10,105	16,211
Government loans	230	3,861	4,091
Total par value of MPF Loans	\$ 9,887	\$ 21,758	31,645
Agent fees, premium (discount)			150
Loan commitment basis adjustment			(16)
SFAS 133 hedging adjustments			311
Receivable from future performance credit enhancement fees			2
Allowance for credit loss			(5)
Total MPF Loans held in portfolio, net			\$ 32,087

¹ Initial contractual maturity of 15 years or less.

² Initial contractual maturity of greater than 15 years.

The following tables summarize information related to our net premium (discount) and hedge accounting cumulative basis adjustments on MPF Loans:

Three months ended June 30,	2009	2008
Net premium amortization expense	\$ 18	\$ 12
Net amortization expense (income) of closed basis adjustments	(2)	-

Six months ended June 30,	2009	2008
Net premium amortization expense	\$ 33	\$ 23
Net amortization expense (income) of closed basis adjustments	(3)	(1)

As of	June 30, 2009	December 31, 2008
Net premium balance at period-end	\$ 116	\$ 150
Cumulative basis adjustments on MPF Loans ¹	227	295
Cumulative basis adjustments closed portion	*	(4)
MPF Loans, par balance	\$ 26,630	\$ 31,645
Premium balance as a percent of MPF Loans	0.44%	0.47%

* Less than \$1 million.

¹ Cumulative basis adjustment on MPF Loans includes hedge accounting adjustments, loan commitment basis adjustments, and anticipated credit enhancement fees.

The change in cumulative basis adjustments on MPF Loans is primarily attributable to changes in fair values under hedge accounting.

Other assets

Other assets declined primarily due to reduced amounts of interest receivable, a result of both a decline in interest-earning assets outstanding and declining interest rates.

Deposits

Although we accept several types of deposits from our customers including demand, overnight, and term deposits, we accept these deposits primarily for the operational convenience of our customers and we do not rely on deposits as a significant source of funding. Our customers temporarily increased their deposits with us at quarter end compared to year end.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

Consolidated Obligation Bonds and Discount Notes

Due to higher long-term funding costs, the market's demand for high quality, short-term investments, and the significant prepayment activity on our mortgage assets, we have not funded a significant amount of our recent financing needs through the issuance of long-term consolidated obligation bonds. Thus, except for relatively minimal amounts, maturing consolidated obligation bonds were replaced by discount note issuances.

The following table shows the percentage breakdown by type of consolidated obligations we issued for the periods shown:

Percent of total issued period ended June 30,	Three months		Six months	
	2009	2008	2009	2008
Consolidated obligation bonds issued	1%	3%	1%	3%
Consolidated discount notes issued	<u>99%</u>	<u>97%</u>	<u>99%</u>	<u>97%</u>
Total consolidated obligation debt issued	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

Our intent is to return to funding a greater portion of our financing needs with longer-term debt as interest rates and market demand for such debt return to more normal or historical levels. Depending on the characteristics of our balance sheet, this debt could have a duration of anywhere from two years to ten years. However, we can not predict when, or to what extent, this will occur.

Other Liabilities

Other liabilities increased, mostly due to \$1.8 billion of investment securities which were purchased but not yet settled as of June 30, 2009. We did not have any unsettled securities at December 31, 2008.

Based on the financial results for the six months ended June 30, 2009, we have accrued additional AHP liability of \$7 million, offset by disbursements of \$6 million. AHP accruals are paid when the amounts are awarded. Amounts currently accrued but not yet awarded will be awarded and paid in the remainder of 2009 or beyond.

We also accrued a liability of \$16 million for REFCORP based on the financial results for the six months ended June 30, 2009. REFCORP assessments are paid in full in the quarter following accrual.

Total Capital

See Capital Resources starting on page 63 for a detailed analysis of the changes in our total capital.

Liquidity, Funding, & Capital Resources

Liquidity Measures

We are required to maintain liquidity in accordance with certain FHFA regulations and guidance, and with policies established by our Board of Directors. See **Liquidity, Funding, & Capital Resources** on page 57 in our 2008 Form 10-K for a detailed description.

We use three different measures of liquidity as follows:

Overnight Liquidity – For the second quarter of 2009, our policy required us to maintain overnight liquid assets at least equal to 3.5% of total assets. As of June 30, 2009, our overnight liquidity was \$9.6 billion, or 10.7% of assets, giving us an excess liquidity of \$6.5 billion.

Deposit Coverage – To support our member deposits, FHFA regulations require us to have an amount equal to the current deposits invested in obligations of the United States government, deposits in eligible banks or trust companies, or advances with maturities not exceeding five years. As of June 30, 2009, we had excess liquidity of \$22.9 billion to support member deposits.

Contingency Liquidity – The cumulative five-business-day liquidity measurement assumes there is a localized credit crisis for all FHLBs where the FHLBs do not have the ability to issue new consolidated obligations or borrow unsecured funds from other sources (e.g., purchasing Federal Funds or customer deposits). Our net liquidity in excess of our total uses and reserves over a cumulative five-business-day period was \$16.0 billion as of June 30, 2009.

In addition to the liquidity measures discussed above, the FHFA provided additional guidance, effective March 6, 2009, requiring all 12 FHLBs to maintain liquidity through short-term investments in an amount at least equal to anticipated cash outflows under two different scenarios. As a result of this new guidance, we are maintaining increased balances in short-term investments. We may fund certain overnight or shorter-term investments and advances with discount notes that have maturities that extend beyond the maturities of the related investments or advances. For a discussion of how this may impact our earnings, see page 24 in the **Risk Factors** section of our 2008 Form 10-K.

Federal Home Loan Bank of Chicago
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Liquidity & Funding

Sources of Funding

During the six months ending June 30, 2009 our operating activities required a net use of cash of \$68 million compared to a use of cash of \$101 million during the first half of 2008. The 2009 net use of cash as compared to 2009 year-to-date net income was primarily due to year to date payments of accrued interest payable of \$212 million offset by the receipt of accrued interest receivable and net noncash adjustments to operating activities of \$81 million. The 2008 net use of cash was less than the 2008 year to date net loss due in part to the losses attributable to non-cash credit-related OTTI charges.

For the six month period ending June 30, 2009, our net cash provided by investing activities was \$2.4 billion. Net cash provided by investing activities primarily relate to a \$10.8 billion decline in outstanding advances and approximately \$5.0 billion in mortgage-related asset pay downs. We believe that the decrease in outstanding assets reflects members' reduced borrowing needs resulting from the availability of liquidity through various federal government funding programs, an increase in deposits for many of our members, and the state of the economy. While members across our district have experienced reduced demand, the reduction in advances was concentrated in two large institutions. We believe the increase in pay downs on mortgage-related assets relate to prepayments by debtors refinancing in the lower interest rate environment experienced during the period. Offsetting the net cash provided from advances and mortgage-related assets were purchases of replacement investments, which primarily consisted of available-for-sale securities totaling \$7.8 billion and trading securities of \$1.1 billion, in addition to more liquid investments such as fed funds and securities purchased under resale agreements.

For the six month period ending June 30, 2009, our net cash used in financing activities was \$2.5 billion. Net cash used in financing activities primarily relate to a \$13.7 billion decline in longer term consolidated obligation bonds offset by \$10.8 billion of funds provided by shorter term discount note issuances. We relied more on discount note issuances given the relatively lower funding costs compared to longer term debt.

For further discussion of our sources of funding, see **Sources of Funding** on page 60 in our 2008 Form 10-K and for details of our consolidated obligations, see **Note 9 – Consolidated Obligations** to the financial statements in this Form 10-Q.

The following table summarizes the consolidated obligations at par value of the FHLBs and those for which we are the primary obligor:

<u>June 30, 2009</u> (par value)	<u>Bonds</u>	<u>Discount</u> <u>Notes</u>	<u>Total</u>
FHLB System	\$ 713,292	\$ 342,572	\$ 1,055,864
FHLB Chicago as primary obligor	41,440	40,318	81,758
As a percent of the FHLB System	6%	12%	8%
<u>December 31, 2008</u> (par value)			
FHLB System	\$ 810,424	\$ 441,118	\$ 1,251,542
FHLB Chicago as primary obligor	55,137	29,484	84,621
As a percent of the FHLB System	7%	7%	7%

Housing and financial markets have been in tremendous turmoil since the middle of 2007, and the U.S. economy is currently in a recession. These economic conditions and the ongoing uncertainty about the depth and duration of the financial crisis and the recession continued to affect our business, as well as that of our members, during the second quarter of 2009.

As the U.S. government continued multiple programs designed to improve the credit markets, conditions appeared to reflect greater strength during the second quarter. While economic data remained mixed during the quarter, short-term funding was both accessible and attractively priced for the FHLBs.

Federal Home Loan Bank of Chicago (Dollars in millions except per share amounts unless otherwise indicated)

During the second quarter of 2009, the Federal Reserve Board (Federal Reserve) continued to support the capital markets through the purchase of GSE term debt, agency MBS, and U.S. Treasury securities. The Federal Reserve purchased approximately \$44 billion in GSE term debt; including \$10.3 billion of FHLB mandated global fixed-rate consolidated bonds during the quarter. By the end of June, Federal Reserve purchases of GSE debt were up to \$97 billion or almost 50% of the \$200 billion allocated to the program. In addition, the Federal Reserve purchased \$162 billion in U.S. Treasury securities during the second quarter. Since inception through June 30, 2009, the Federal Reserve has purchased \$180 billion in U.S. Treasury securities, which brings total purchases to 60% of the \$300 billion committed under the program.

While the FDIC's Temporary Liquidity Guarantee Program (TLGP) continued to provide depository institutions with access to longer-term capital, issuance slowed significantly in the second quarter 2009. On April 1, fees assessed for the TLGP increased and only \$39.5 billion in TLGP-wrapped bonds were priced in the second quarter of 2009 as compared to \$125 billion in the first quarter. This program is set to expire at the end of October 2009 and its expiration may provide an important indication of the health of the debt market for financial institutions.

Consolidated obligation bond funding costs for the FHLBs continued to improve during the second quarter of 2009. During the first quarter of 2009, we called high-cost long-term debt that was eligible to be called, and replaced it with shorter-term, lower cost discount notes. During the second quarter, we further increased our issuance of discount notes over first quarter levels because investor demand for competitively auctioned discount notes increased as market volatility decreased. Also during the second quarter, we began to term-out our debt as FHLB term funding costs continued to improve. We began issuing shorter-term callable consolidated obligation bonds with "step-up" rates that will increase at fixed amounts on predetermined dates. Because the rates on these bonds will "step up" as interest rates increase, demand for these bonds has increased as investors view them as a hedge against potential inflation and any corresponding increase in interest rates.

In January 2009, the FHLB System, through the Office of Finance, implemented a scheduled monthly issuance of global fixed-rate consolidated bonds, which attracted strong investor interest during the second quarter of 2009. As part of this process, management from each FHLB determines and communicates a firm commitment to the Office of Finance for an amount of scheduled global debt to be issued on its behalf. If the FHLBs' orders do not meet the minimum debt issue size, each FHLB receives an allocation of proceeds equal to the larger of the FHLB's commitment or the ratio of the individual FHLB's capital to total capital of all of the FHLBs. If the FHLBs' commitments exceed the minimum debt issue size, then the proceeds are allocated based on actual commitment amount.

During the three and six months ended June 30, 2009, the FHLB System issued a total of \$11.0 billion and \$20.5 billion in fixed-rate bonds with maturities of two and three years under this calendar-date mandated global bond process. Although we were mandatorily allocated \$60 million through this global bond process during the first quarter, we requested and received allocations of \$895 million during the second quarter to take advantage of more favorable term funding costs available through this process.

In addition to the sources of liquidity discussed above, in September 2008, the Treasury established a lending facility designed to provide secured funding on an as needed basis to the housing GSEs, including the FHLBs, as further discussed in **Government Sponsored Enterprise Credit Facility** on page 58 in our 2008 Form 10-K. As of June 30, 2009, we provided the U.S. Treasury with a listing of eligible advance collateral totaling \$19 billion, which would allow maximum borrowings of \$17 billion, however, we have not drawn on this facility and we have no plans to access funding through this facility.

Based upon our excess liquidity position described above under Liquidity Measures and the liquidity available to us under our Lending Agreement with the Treasury, we anticipate remaining in compliance with our liquidity requirements.

Federal Home Loan Bank of Chicago
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Capital Resources

For a description of our current capital rules, see **Current Capital Rules** on page 64 in our 2008 Form 10-K.

The following table reconciles our capital stock reported for regulatory purposes to the amount of capital reported in our statements of condition for the periods presented. Mandatorily Redeemable Capital Stock (MRCS) is included in the calculation of the regulatory capital and leverage ratios but is recorded as a liability in the statements of condition.

	June 30,		December 31,	
	2009		2008	
	\$	%	\$	%
Bank of America, N.A. ¹	\$ 230	8%	\$ 230	8%
One Mortgage Partners Corp. ²	172	6%	172	6%
M&I Marshall & Isley Bank	152	5%	n/a	-
PNC Financial Services Group, Inc. ³	146	5%	146	5%
Harris National Association	140	5%	140	5%
Associated Bank, NA	n/a	-	146	5%
All other members	<u>1,961</u>	<u>71%</u>	<u>1,953</u>	<u>71%</u>
Total regulatory capital stock	<u>2,801</u>	<u>100%</u>	2,787	<u>100%</u>
Less MRCS	<u>(426)</u>		<u>(401)</u>	
Capital stock	<u>2,375</u>		2,386	
Retained earnings	837		540	
Accumulated other comprehensive income (loss)	<u>(1,514)</u>		<u>(639)</u>	
Total capital	<u>\$ 1,698</u>		<u>\$ 2,287</u>	
Regulatory capital stock	<u>\$ 2,801</u>		\$ 2,787	
Designated Amount of subordinated notes	<u>1,000</u>		<u>1,000</u>	
Regulatory capital stock plus Designated Amount of subordinated notes	<u>3,801</u>		3,787	
Retained earnings	<u>837</u>		<u>540</u>	
Regulatory capital plus Designated Amount of subordinated notes	<u>\$ 4,638</u>		<u>\$ 4,327</u>	
Voluntary capital stock	<u>\$ 1,030</u>		<u>\$ 718</u>	

^{n/a} Was not in the top five list for the date indicated.

¹ Formerly LaSalle Bank, N.A., became ineligible for membership due to an out-of-district merger into Bank of America, N.A. effective October 17, 2008. Its capital stock was reclassified to MRCS at that time.

² One Mortgage Partners Corp. is a subsidiary of JPMorgan Chase & Co.

³ Formerly MidAmerica Bank, FSB, became ineligible for membership due to an out-of-district merger into National City Bank, effective February 9, 2008. Its capital stock was reclassified to MRCS at that time. Effective December 31, 2008, National City Corporation merged into PNC Financial Services Group, Inc.

Under the terms of our C&D Order dated October 10, 2007 with the Finance Board, our capital stock repurchases and redemptions, including redemptions upon membership withdrawal or other membership termination, require prior approval of the Deputy Director, except as discussed below. From April 24, 2008 through June 30, 2009, the Deputy Director has denied requests to redeem capital stock totaling \$19 million, in connection with 12 membership withdrawals or other membership terminations. We cannot predict when we will be permitted to resume such capital stock repurchases or redemptions.

On July 24, 2008, the Finance Board amended the C&D Order to allow us to redeem a member's capital stock which becomes excess capital stock above a member's capital stock "floor" (the amount of capital stock a member held as of the close of business at July 23, 2008 plus any required adjustments related to annual membership stock recalculations) in connection with the repayment of advances subject to certain conditions. During the six months ended June 30, 2009, we redeemed \$86 million in excess capital stock as permitted by the amendment to the C&D Order. For further discussion of how a member's capital stock floor is set, see Current Capital Rules on page 64 in our 2008 Form 10-K.

Total capital, as noted in the previous table, decreased from December 31, 2008 to June 30, 2009 primarily due to the adoption of new OTTI accounting guidance effective January 1, 2009. While the new guidance increased retained earnings, this increase was more than offset by the loss in AOCI. See **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations** to the financial statements and **Critical Accounting Policies and Estimates** on page 65 in this Form 10-Q for a detailed description of this change in accounting policy and estimate.

The mandatorily redeemable capital stock balance of \$426 million at June 30, 2009 consists of capital stock for twenty-seven members that have requested withdrawal of membership or otherwise terminated their membership, primarily due to out-of-district mergers.

Federal Home Loan Bank of Chicago (Dollars in millions except per share amounts unless otherwise indicated)

Minimum Regulatory Capital Requirements

For a description of our minimum regulatory leverage and other capital requirements, see **Note 11 – Capital Stock and Mandatorily Redeemable Capital Stock** to the financial statements. As of the date of this filing, we are in compliance with our regulatory leverage and other capital requirements.

GLB Act Requirements

We are required under the Gramm-Leach Bliley Act (GLB Act) to adopt a new capital plan. We continue discussions with the FHFA regarding a capital stock conversion plan and submitted a revised Capital Plan to the Deputy Director on July 16, 2009. We believe that stabilizing our capital stock is fundamental to the successful transition of the Bank and wish to convert as expeditiously as possible, although we cannot predict if the FHFA will approve our revised Capital Plan or when a capital conversion would occur.

We anticipate that our new capital plan will provide for the conversion of our current capital stock to one or more classes of Class B capital stock with a five-year redemption period consistent with the requirements of the GLB Act. We cannot predict how an approved capital plan may impact members who have submitted withdrawal notices and not yet withdrawn from membership or former members that continue to hold capital stock. For a description of our capital requirements under the GLB Act, see **GLB Act Requirements** on page 65 of our 2008 Form 10-K. For a discussion of potential changes to our members' rights under a new capital plan, see page 25 of the **Risk Factors** section of our 2008 Form 10-K.

Retained Earnings & Dividends

Under the terms of the C&D Order, our dividend declarations are subject to the prior written approval of the Deputy Director. Although we currently have in effect a Retained Earnings and Dividend Policy, the policy has been effectively superseded by our regulatory requirements.

In addition to the restrictions under the C&D Order, we may not pay dividends if we fail to satisfy our liquidity requirements under the FHLB Act and FHFA regulations. See Liquidity Measures on page 57 in our 2008 Form 10-K.

Our goal is to transition the Bank to a more traditional FHLB model so that it generates consistent earnings and we are able to restore at least a nominal dividend. In order to provide for growth in retained earnings during this transition, we did not request approval from the Deputy Director to pay a dividend and have retained the full amount of our second quarter net income. We cannot predict when we may resume paying dividends. For a summary of our dividends for the past five quarters, see **Selected Financial Data** on page 46.

As of June 30, 2009, we had retained earnings of \$837 million, which is 55% higher than at year-end 2008. A portion of this increase is due to our early adoption of new OTTI accounting guidance effective January 1, 2009. For a description of this change refer to **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations** to the financial statements and to **Critical Accounting Policies and Estimates** on page 65.

Credit deterioration may continue to negatively impact our MBS portfolio. We believe that future impairments of the MBS portfolio are likely, but cannot predict the impact such impairments may have on our retained earnings and capital position. See page 32 of the **Risk Factors** section of our 2008 Form 10-K.

Accumulated Other Comprehensive Income

The total unrealized loss in AOCI increased by \$875 million from December 31, 2008 to June 30, 2009. The majority of this increase was the result of \$1.2 billion of non-credit losses related to OTTI on our private-label MBS. Also included in the increased unrealized loss was a \$233 million cumulative effect adjustment resulting from the adoption of new OTTI accounting guidance on January 1, 2009. For a description of this change in estimate refer to **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations** to the financial statements and to **Critical Accounting Policies and Estimates** on page 65. Offsetting these charges to AOCI was a \$254 million partial reversal of unrealized hedge accounting losses related to certain cash flow hedges.

Federal Home Loan Bank of Chicago
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Off-Balance Sheet Arrangements

We do not consolidate our investments in variable interest entities, which include MPF Shared Funding securities, investments in mortgage-backed securities (MBS), and investments in Federal Family Education Loan Program (FFELP) student loan asset-backed securities (ABS), as discussed in **Note 2 – Summary of Significant Accounting Policies – Consolidation**. Also refer to **Off-Balance Sheet Arrangements** on page 67 in our 2008 Form 10-K.

Contractual Cash Obligations

For additional information on **Contractual Cash Obligations** see page 68 in our 2008 Form 10-K. Also see **Note 15 – Commitments and Contingencies**. We have not experienced any material changes in contractual cash obligations.

Critical Accounting Policies and Estimates

See **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations** to the financial statements for the impact of recently issued accounting standards on our financial results.

Other-Than-Temporary Impairment (OTTI)

We adopted the new OTTI accounting guidance issued by the FASB on April 9, 2009, retroactive to January 1, 2009, as provided by the FASB. In addition, commencing effective with the first quarter of 2009, the FHFA provided the FHLBs guidance on the process for determining OTTI that would be consistent among all 12 FHLBs. See **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations** for details. The new FASB guidance requires an assessment of OTTI whenever the fair value of an investment security is less than its amortized cost basis at the balance sheet date. Amortized cost basis includes adjustments made to the cost of a security for accretion, amortization, collection of cash, previous OTTI recognized into earnings (less any cumulative effect adjustments) and fair value hedge accounting adjustments. The initial effect of adoption was to recognize a cumulative effect adjustment of \$233 million to the January 1, 2009 opening balance of our retained earnings.

We apply a three step process to determine and account for OTTI for our AFS and HTM investment securities on a quarterly basis. This process is summarized below.

Step 1 – OTTI Assessment

We assess impairment on each individual AFS or HTM investment security. Under Step 1, an AFS or HTM investment security is considered impaired if its fair value is less than its amortized cost. If an AFS or HTM investment security is assessed as impaired, then Step 2 is applied to determine if impairment recognition is appropriate.

Step 2 – OTTI Recognition Determination

Determination of whether losses are other-than-temporary often involves estimating the outcome of future events. Accordingly, judgment is required in determining whether factors exist that indicate an OTTI loss has been incurred at the end of the reporting period. These judgments are based on subjective as well as objective factors, including knowledge and experience about past and current events and assumptions about future events.

We consider OTTI to have been incurred under the following circumstances:

- If we decide to sell the investment security and its fair value is less than its amortized cost.
- If, based on available evidence, we believe it is more likely than not that we will decide or be required to sell the investment security before the recovery of its amortized cost basis.
- If we do not expect to recover the entire amortized cost basis of the investment security. The difference between the present value of the cash flows expected to be collected and the amortized cost basis represents the amount of credit loss.

As of June 30, 2009, we completed our OTTI analysis and made our impairment determination utilizing the risk model and loan performance data source specified in the FHFA guidance as well as the key modeling assumptions, inputs, and methodologies provided by the OTTI Committee.

For our private-label MBS as of June 30, 2009, we analyzed all of the securities with adverse risk characteristics. The adverse risk characteristics used in selecting each of these securities for further analysis included:

- the magnitude of the security's estimated fair value discount as a percentage of the security's carrying value;
- adverse rating agency actions on the security, including negative watch and/or downgrade; and

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- a variety of criteria related to the credit performance of the underlying collateral, including the ratio of credit enhancement to expected losses, the ratio of seriously delinquent loans to credit enhancement, and cumulative losses to date.

For each of the selected securities, we performed a cash flow analysis using models that project prepayments, default rates, and loss severities on the collateral supporting our security, based on underlying loan level borrower and loan characteristics, expected housing price changes, and interest rate assumptions. A significant input to the model is the forecast of housing price changes for the relevant states and metropolitan statistical areas, which are based on an assessment of the relevant housing market. In response to the ongoing deterioration in housing prices, credit market stress, unemployment, and weakness in the U.S. economy in the second quarter of 2009, there was continued deterioration in the credit quality of the collateral. If our analysis does not support a present value of cash flows expected to be collected that is equal to or greater than the amortized cost basis of the private-label MBS, we recognize OTTI.

Step 3 – OTTI Accounting

For a detailed discussion of how we determine fair value write-downs and credit loss only write-downs using our base case (most likely) scenario, see **Note 5 – Investment Securities**.

In addition to evaluating the risk-based selection of our private-label MBS under a base case (or best estimate) scenario, a cash flow analysis was also performed for each of these securities under a more stressful housing price scenario. The more stressful scenario was based on a housing price forecast that was 5 percent lower at the trough than the base case scenario followed by a flatter recovery path. Under the more stressful scenario, current-to-trough home price declines were projected to range from 5 percent to 25 percent over the next 9 to 15 months. Thereafter, home prices were projected to increase 0 percent in the first year, 1 percent in the second year, 2 percent in the third year and 3 percent in each subsequent year.

The following table shows what the impact to net income from credit-related OTTI charges would have been under this adverse scenario. Classifications of MBS as prime, Alt-A, or subprime are made at the time of purchase, and may differ from the current performance characteristics of the instrument.

<u>Actual for the quarter-ended June 30, 2009</u>	<u># of Securities</u>	<u>Unpaid Principal Balance</u>	<u>Credit-Related OTTI</u>
Prime	24	\$ 2,231	\$ (56)
Alt-A	5	187	(8)
Subprime	30	759	(60)
Total private-label MBS	59	\$ 3,177	\$ (124)

<u>Pro-forma for the quarter-ended June 30, 2009 assuming adverse scenario</u>	<u># of Securities</u>	<u>Unpaid Principal Balance</u>	<u>Credit-Related OTTI</u>
Prime	24	\$ 2,231	\$ (124)
Alt-A	5	187	(17)
Subprime	34	866	(107)
Total private-label MBS	63	\$ 3,284	\$ (248)

Fair Value

Also see **Note 14 – Estimated Fair Value** to the financial statements for the amounts of our assets and liabilities classified as Levels 1, 2, or 3.

On April 9, 2009, the FASB released new accounting guidance for determining fair value when the volume and level of activity for an asset or liability has significantly decreased and identifying transactions are not orderly. This new guidance updates previous guidance for estimating fair value measurements when the volume and level of activity for the asset or liability have significantly decreased. It also provides guidance on identifying circumstances that indicate a transaction is not orderly. It emphasizes that despite significant decreases in volume and level of activity and regardless of the valuation technique(s) used for the asset or liability, the fair value measurement remains the same. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions.

We adopted this new guidance effective January 1, 2009. It had no effect on our financial statements at the time of adoption. Specifically, we believe that the guidance further supports our view that current transaction prices should be given little weight when measuring the fair value of our private-label MBS portfolio with vintages between 2005 and 2007. As a result, we continue to use internal pricing models to value our private-label MBS portfolio with vintages between 2005 and 2007. We believe these

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models are more representative of fair values than their values provided by third-party pricing services. Specifically, we believe that the ongoing credit deterioration in the mortgage market, in combination with the large price variability between third-party pricing services across prime, subprime and Alt-A sectors, a widening of bid-ask spreads, low volume and evidence of distressed sales, supports the continued use of our internal models to determine the fair value of our private-label MBS for these vintages. Our internal models use an income approach valuation technique (present value technique) that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs.

Internal models were used for these instruments because there has been a specific review of the projected underlying cash flows, including loss severity, roll-rates and default rates for which we are able to refine our estimate of fair value to reflect a situation whereby an active market existed at the balance sheet date. The internally modeled values reflect our expectations of cash flows expected to be collected after accounting for appropriate non-performance and liquidity risk premiums existing in the current market.

We believe the most relevant inputs to measuring the fair value of these instruments are default rates, loss severity and delinquency trends. Inputs are determined based on relative value analysis, which incorporates comparisons to instruments with similar collateral and risk profiles, including relevant indices such as the ABX. The ABX is an index that tracks the performance of subprime residential mortgage bonds. The methodology utilized to determine our non-performance, prepayment, and liquidity risk assumptions is described below.

Implied Spread used to Value 2005-2007 Subprime and Alt-A Portfolios

The ABX index is comparable in performance by vintage to our subprime portfolio. More specifically, its estimated loss and historical loss experience is similar to that of our subprime portfolio. The ABX index prices are market observable inputs. Our subprime securities are predominately 3-year average life securities which are closer in structure to the Pen AAA ABX indices.

- We derive an implied spread, which is used to calculate our fair values, for both the Pen AAA ABX indices based on vintage with a combination of security-level prepayment curves, default curves and severities.

- The Alt-A sector does not have a trading index as does the ABX market and we identified large discrepancies between pricing vendors on these securities. Because Alt-A securities have deteriorated in quality to more closely behave as subprime securities, we chose to use the same ABX spread level by vintage as we did above for subprime securities for our Alt-A sector securities.

Implied Spread used to Value 2005-2007 Prime Portfolios

There is no traded index (e.g., ABX indices) for prime securities. The majority of securities in our portfolio were originated in 2006. The implied spread used for these securities was based on comparable spreads obtained or observed from dealers and third parties.

The estimated fair value determined by us, our pricing services, and the estimated fair value range we considered for our prime, subprime and Alt-A investment securities that are carried at fair value at June 30, 2009 in our financial statements, either on a nonrecurring or recurring basis, are as follows:

As of June 30, 2009	Estimated Fair Value	Range of Pricing Service Values	
		Min	Max
2005 HTM - Non- Recurring	\$ 4	\$ 3	\$ 3
2006 AFS - Recurring	93	66	75
2006 HTM - Non- Recurring	<u>1,102</u>	<u>1,032</u>	<u>1,148</u>
Total	<u>\$ 1,199</u>	<u>\$ 1,101</u>	<u>\$ 1,226</u>

Use of Pricing Services

We obtain information from a third-party pricing service to value our investment securities and we use an additional third-party pricing service as a validation of our fair values; however, as discussed above, we did not use our pricing service's fair values for a portion of our private-label MBS portfolio at June 30, 2009. In cases where prices were not available from a third-party pricing service, we utilize observable market-inputs to model the fair value. For those securities which we valued using our pricing service, we did not make any adjustments to these estimated fair values.

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Outlined below are the estimated fair values by investment type and fair value hierarchy level:

As of June 30, 2009	Estimated Fair Value	Fair Value Hierarchy Level
Trading	\$ 1,659	2
AFS (Using pricing service)	\$ 5,728	2
AFS (Using pricing service)	2	3
AFS (Modeled)	5,273	2
AFS (Modeled)	92	3
Total AFS	\$ 11,095	

Derivative Instruments – Derivative instruments are primarily transacted in the institutional dealer market and priced with observable market assumptions at a mid-market valuation point. We do not provide a credit valuation adjustment based on aggregate exposure by derivative counterparty when measuring the fair value of our derivatives. The fair values of our derivatives take into consideration the effects of legally enforceable master netting agreements that allow us to settle positive and negative positions and offset cash collateral with the same counterparty on a net basis. We, and each derivative counterparty, have collateral thresholds that take into account both our and our counterparty's credit ratings. As a result of these practices and agreements, we have concluded that the impact of the credit differential between us and our derivative counterparties was sufficiently mitigated to an immaterial level and no adjustment was deemed necessary to the recorded fair values of derivative assets and liabilities in the statements of condition at June 30, 2009 and December 31, 2008.

Controls over Valuation Methodologies

Senior management, independent of our investing and treasury functions, is responsible for our valuation policies. The Asset and Liability Committee approves fair value policies, reviews the appropriateness of current valuation methodologies and policies, and reports significant policy changes to the Risk Management Committee of the Board of Directors. The Audit Committee of the Board of

Directors oversees the controls over these processes including the results of independent model validation where appropriate.

The Market Risk Analysis department, overseen by the Chief Risk Officer, prepares the fair value measurements of our financial instruments independently of the investing and treasury management functions. In addition, the department performs control processes to ensure the fair values generated from pricing models are appropriate. In the event that observable inputs are not available, we use methods that are designed to assure that the valuation approach utilized is appropriate and consistently applied and that the assumptions are reasonable.

Our control processes include reviews of the pricing model's theoretical soundness and appropriateness by personnel with relevant expertise who are independent from the fair value measurement function. For financial instruments where prices or valuations require unobservable inputs, we engage in procedures that include back testing models to subsequent transactions (e.g. termination of a derivative), analysis of actual cash flows to projected cash flows, comparisons with similar observable positions, and comparisons with information received from pricing services. In circumstances where we cannot verify a fair value derived from a valuation model to active market transactions, it is possible that alternative methodologies could produce a materially different estimate of fair value.

Fair Value Measurement Effect on Liquidity and Capital

Fair value measurements of Level 3 financial assets and liabilities may have an effect on our liquidity and capital. Specifically, our estimated fair values for these financial assets and liabilities are highly subjective. Further, we are subject to model risk for certain financial assets and liabilities. Our liquidity and capital could be positively or negatively affected to the extent that the amount that could be realized in an actual sale, transfer or settlement could be more or less than we estimated. This also would apply to the fair value of investment securities deemed other-than-temporarily impaired.

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Risk Management

Operational Risk

See **Risk Management** on page 75 in our 2008 Form 10-K for information regarding operational risk.

Credit Risk

Credit risk is the risk of loss due to default or non-performance of an obligor or counterparty. We are exposed to credit risk principally through:

- issuers/guarantors of investment securities
- unsecured short-term investments
- advances and commitments to make advances
- letters of credit
- MPF Loans
- mortgage insurance providers; and
- derivatives counterparties.

We have established policies and procedures to limit and help monitor our exposures to credit risk.

We extend credit to members on a fully secured basis and are subject to regulatory limits on the amount of credit that we may extend as well as on the types of underlying collateral that we may accept. We are also subject to certain regulatory limits on the amount of unsecured credit that we may have outstanding to any one counterparty or group of affiliated counterparties associated with

purchases of Federal Funds, commercial paper and derivatives activity, which are based in part on our total regulatory capital. We are authorized to determine compliance with the unsecured credit limits based on the sum of our outstanding regulatory capital stock, retained earnings, and the Designated Amount of outstanding subordinated notes for any period that we are subject to the regulatory leverage ratio requirements as further discussed in **Note 11 – Capital Stock and Mandatorily Redeemable Capital Stock** to the financial statements.

Investments

We maintain a portfolio of investments for liquidity purposes and to provide additional earnings. To ensure the availability of funds to meet member credit needs, we maintain a portfolio of short-term liquid assets, principally overnight and short-term Federal Funds sold and securities purchased under agreements to resell, and commercial paper entered into with or issued by highly rated institutions. The longer-term investment securities portfolio includes securities issued by the United States government, United States government agencies, GSEs, FFELP student loan ABS, MPF Shared Funding securities and mortgage-backed securities that are issued by GSEs or that were rated “AAA/Aaa” or “AA/Aa” from S&P, Moody’s, or Fitch at the time of purchase. Securities issued by GSEs are not obligations of, and are not guaranteed by, the United States government.

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The carrying value of our investment securities portfolio by credit rating is shown in the following table.

As of June 30, 2009	Lowest Long Term Rating										Total
	AAA	AA	A	BBB	BB	B	CCC	CC	C	Unrated	
Non-Mortgage Backed Securities:											
Government-sponsored enterprises	\$ 1,801	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,801
Temporary liquidity guarantee program (FDIC - TLGP)	632	-	-	-	-	-	-	-	-	-	632
State or local housing agency obligations	1	44	-	-	-	-	-	-	-	-	45
Small Business Administration / Small Business Investment Companies	1,035	-	-	-	-	-	-	-	-	-	1,035
Total non-MBS	3,469	44	-	-	-	-	-	-	-	-	3,513
Asset Backed Securities:											
FFELP student loan ABS	5,095	-	-	-	-	-	-	-	-	-	5,095
Mortgage Backed Securities:											
Government-sponsored enterprises	14,395	-	-	-	-	-	-	-	-	-	14,395
Government-guaranteed	646	-	-	-	-	-	-	-	-	-	646
Private-label	196	74	201	750	412	102	625	106	23	6	2,495
MPF Shared Funding	255	10	-	-	-	-	-	-	-	-	265
Total MBS	15,492	84	201	750	412	102	625	106	23	6	17,801
Total Investment Securities June 30, 2009	\$ 24,056	\$ 128	\$ 201	\$ 750	\$ 412	\$ 102	\$ 625	\$ 106	\$ 23	\$ 6	\$ 26,409
March 31, 2009	\$ 16,152	\$ 222	\$ 435	\$ 481	\$ 303	\$ 191	\$ 246	\$ 26	\$ -	\$ 6	\$ 18,062
December 31, 2008	\$ 17,553	\$ 200	\$ 865	\$ 641	\$ 219	\$ 59	\$ 48	\$ -	\$ -	\$ 18	\$ 19,603

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The following table shows the credit ratings of our private-label MBS with gross unrealized gains (losses). For a definition of prime, Alt-A, and subprime, see page 77 in our 2008 Form 10-K. These classifications are determined at the time the MBS is purchased. Weighted average collateral delinquency represents the percent of underlying loans that are 60+ days delinquent.

As of June 30, 2009	Amortized Cost	Gross Unrealized Gains (Losses)	Non-Credit OTTI Recognized in AOCI	Weighted Average Collateral Delinquency %
Private-label MBS backed by Prime Loans:				
AAA-rated	\$ 128	\$ (6)	\$ *	1%
AA-rated	45	-	(18)	17%
A-rated	279	4	(115)	21%
BBB	1,058	9	(400)	15%
Below Investment Grade	812	(11)	(296)	14%
Total Prime	2,322	(4)	(829)	14%
Private-label MBS backed by Alt-A Loans:				
AA-rated	1	(1)	-	18%
A-rated	2	(1)	-	23%
Below Investment Grade	164	-	(71)	43%
Total Alt-A	167	(2)	(71)	42%
Private-label MBS backed by Subprime Loans:				
AAA-rated	67	(14)	*	36%
AA-rated	46	(8)	-	37%
A-rated	37	(6)	-	43%
BBB	93	(21)	*	42%
Below Investment Grade	972	(98)	(313)	49%
Unrated	6	(1)	-	0%
Total Subprime	1,221	(148)	(313)	47%
Total Private-label MBS	\$ 3,710	\$ (154)	\$ (1,213)	27%

* Less than \$1 million

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The following table shows the recent credit downgrades within our private-label MBS portfolio subsequent to June 30, 2009 through August 7, 2009. The investment ratings are based on the lowest rating from S&P, Moody's, or Fitch. Prime, Alt-A, and Subprime classifications are determined at the time the MBS is purchased.

<u>Downgraded from AAA:</u>	<u>To AA</u>							
	<u>Carrying Value</u>	<u>Fair Value</u>						
Private-label MBS -								
Prime	\$ 3	\$ 3						
Subprime	3	2						
Total	\$ 6	\$ 5						
<u>Downgraded from AA:</u>	<u>To A</u>		<u>To BBB</u>		<u>To BB</u>			
	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>		
Private-label MBS -								
Prime	\$ -	\$ -	\$ -	\$ -	\$ 28	\$ 28		
Subprime	19	15	1	1	-	-		
Total	\$ 19	\$ 15	\$ 1	\$ 1	\$ 28	\$ 28		
<u>Downgraded from A:</u>	<u>To CCC</u>		<u>To CC</u>					
	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>				
Private-label MBS -								
Prime	\$ 75	\$ 75	\$ 89	\$ 92				
Total	\$ 75	\$ 75	\$ 89	\$ 92				
<u>Downgraded from BBB:</u>	<u>To BB</u>		<u>To B</u>		<u>To CCC</u>		<u>To CC</u>	
	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Carrying Value</u>	<u>Fair Value</u>
Private-label MBS -								
Prime	\$ 67	\$ 69	\$ 64	\$ 67	\$ 297	\$ 286	\$ 158	\$ 173
Subprime	-	-	9	6	1	*	-	-
Total	\$ 67	\$ 69	\$ 73	\$ 73	\$ 298	\$ 286	\$ 158	\$ 173
<u>Total Downgraded</u>	<u>Carrying Value**</u>	<u>Fair Value**</u>						
Private-label MBS -								
Prime	\$ 781	\$ 793						
Subprime	33	24						
Total	\$ 814	\$ 817						

* Less than \$1 million

** Does not include downgrades within below investment grades

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The following table summarizes the par value of our private-label MBS categories by interest rate type. Prime, Alt-A, and Subprime classifications are determined at the time the MBS is purchased.

	June 30, 2009			December 31, 2008		
	Fixed Rate	Variable Rate	Total	Fixed Rate	Variable Rate	Total
Unpaid Principal Balance as of						
Private-label MBS:						
Subprime home equity loans ¹	\$ -	\$ 1,387	\$ 1,387	\$ -	\$ 1,470	\$ 1,470
Private-label Residential MBS (RMBS)-						
Prime	17	2,336	2,353	21	2,509	2,530
Alt-A	-	190	190	-	204	204
Total private-label RMBS	<u>17</u>	<u>2,526</u>	<u>2,543</u>	<u>21</u>	<u>2,713</u>	<u>2,734</u>
Private-label Commercial MBS (CMBS)-						
Prime	74	10	84	82	10	92
Total private-label CMBS	<u>74</u>	<u>10</u>	<u>84</u>	<u>82</u>	<u>10</u>	<u>92</u>
Total unpaid principal balance	<u>\$ 91</u>	<u>\$ 3,923</u>	<u>\$ 4,014</u>	<u>\$ 103</u>	<u>\$ 4,193</u>	<u>\$ 4,296</u>

¹ Primarily first-lien mortgage loans that have lower credit scores, higher debt to income ratios, and higher loan to value ratios.

The following table summarizes our underlying collateral performance and credit enhancement statistics by vintage year of securitization of our private-label MBS. Prime, Alt-A, and Subprime classifications are determined at the time the MBS is purchased.

As of June 30, 2009 Private-label MBS by year of securitization	Weighted Average Market Price (per \$100.00 par)	Original Weighted Average Credit Support %	Weighted Average Credit Support %	Weighted Average Collateral 60+ Days Delinquent
Prime				
2006	\$ 59.18	12%	12%	15%
2005	58.85	14%	14%	23%
2004 and prior	95.92	18%	29%	1%
Prime Total	<u>61.13</u>	<u>12%</u>	<u>13%</u>	<u>14%</u>
Alt-A				
2006	49.62	18%	17%	43%
2004 and prior	50.85	7%	20%	21%
Alt-A Total	<u>49.64</u>	<u>18%</u>	<u>17%</u>	<u>42%</u>
Subprime				
2007	51.24	23%	38%	48%
2006	50.87	23%	33%	48%
2005	81.77	22%	48%	44%
2004 and prior	63.26	42%	59%	19%
Subprime Total	<u>54.83</u>	<u>23%</u>	<u>36%</u>	<u>47%</u>
Total private-label MBS	<u>\$ 58.41</u>	<u>16%</u>	<u>21%</u>	<u>27%</u>

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Other-Than-Temporary Impairment

As of June 30, 2009, 73% of our MBS, with a carrying value of \$12.9 billion and an amortized cost of \$14.1 billion, are classified as held-to-maturity. Of the carrying value, 19% represents private-label MBS. We do not intend to sell these securities and we believe it is not more likely than not that we will be required to sell these securities before its anticipated recovery of each security's remaining amortized cost basis. We actively monitor the credit quality of our MBS to evaluate our exposure to the risk of loss on these investments. For the three and six months ended June 30, 2009, we recognized \$116 million and \$191 million in OTTI charges in earnings related to credit losses on prime and subprime held-to-maturity private-label MBS after we determined that it was likely that we would not recover the entire amortized cost of each of these securities. If delinquency and/or loss rates on mortgages and/or home equity loans continue to

increase, and/or a rapid decline in residential real estate values continues, we could experience further reduced yields or additional losses on these investment securities.

As of June 30, 2009, 27% of our MBS, with a carrying value of \$4.8 billion and an amortized cost of \$4.9 million, are classified as available-for-sale. Of the carrying value, 2% represents private-label MBS. As a result of our OTTI assessment at June 30, 2009, we determined that it was likely that we would not recover the entire amortized cost of these securities. For the three and six months ended June 30, 2009, we recognized \$8 million and \$19 million in OTTI charges in earnings related to credit losses on impairment of available-for-sale private-label MBS classified as Alt-A based upon the nature of the majority of underlying mortgages collateralizing each security at origination.

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The following tables present our private-label MBS by category, vintage year of securitization and the OTTI charges taken on these securities during the six months ended June 30, 2009.

	As of June 30, 2009				Six months ended June 30, 2009		
	Amortized Cost	Gross Unrealized Gains (Losses)	Non-Credit OTTI Recognized in AOCI	Fair Value	Total OTTI Losses	OTTI Related to Non- Credit Losses	OTTI related to Credit Losses
Private-label MBS by year of securitization							
Prime -							
Private-label RMBS							
2006	\$ 2,150	\$ -	\$ (810)	\$ 1,339	\$ (928)	\$ (823)	\$ (105)
2005	43	2	(19)	26	(22)	(20)	(2)
2004 and prior	45	(5)	-	41	(1)	*	(1)
Prime Private-label RMBS Total	<u>2,238</u>	<u>(3)</u>	<u>(829)</u>	<u>1,406</u>	<u>(951)</u>	<u>(843)</u>	<u>(108)</u>
Private-label CMBS							
2004 and prior	84	(1)	-	84	-	-	-
Prime Private-label CMBS Total	<u>84</u>	<u>(1)</u>	<u>-</u>	<u>84</u>	<u>-</u>	<u>-</u>	<u>-</u>
Prime Total	<u>2,322</u>	<u>(4)</u>	<u>(829)</u>	<u>1,490</u>	<u>(951)</u>	<u>(843)</u>	<u>(108)</u>
Alt-A -							
Private-label RMBS							
2006	164	-	(71)	93	(46)	(27)	(19)
2004 and prior	3	(2)	-	1	-	-	-
Alt-A Private-label RMBS Total	<u>167</u>	<u>(2)</u>	<u>(71)</u>	<u>94</u>	<u>(46)</u>	<u>(27)</u>	<u>(19)</u>
Alt-A Total	<u>167</u>	<u>(2)</u>	<u>(71)</u>	<u>94</u>	<u>(46)</u>	<u>(27)</u>	<u>(19)</u>
Subprime							
Home Equity Loans ¹							
2007	9	(4)	-	5	-	-	-
2006	1,020	(111)	(311)	598	(281)	(204)	(77)
2005	157	(23)	(2)	133	(5)	(2)	(3)
2004 and prior	35	(10)	-	25	(3)	*	(3)
Subprime Home Equity Loans Total	<u>1,221</u>	<u>(148)</u>	<u>(313)</u>	<u>761</u>	<u>(289)</u>	<u>(206)</u>	<u>(83)</u>
Subprime Total	<u>1,221</u>	<u>(148)</u>	<u>(313)</u>	<u>761</u>	<u>(289)</u>	<u>(206)</u>	<u>(83)</u>
Total Private-label MBS	<u>\$ 3,710</u>	<u>\$ (154)</u>	<u>\$ (1,213)</u>	<u>\$ 2,345</u>	<u>\$ (1,286)</u>	<u>\$ (1,076)</u>	<u>\$ (210)</u>

* Less than \$1 million

¹ Primarily first-lien mortgage loans that have lower credit score, a higher debt to income ratio, and higher loan to value ratios.

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The following tables summarize OTTI charges recognized during the six months ended June 30, 2009, based on security type and duration of non-credit related and credit related unrealized losses prior to impairment. Prime, Alt-A, and Subprime classifications are determined at the time the MBS is purchased.

For the six months ended June 30, 2009	Non-Credit Portion Recognized in AOCI			Credit Loss Recognized in Net Income		
	Less than 12 months	Greater than 12 months	Total	Less than 12 months	Greater than 12 months	Total
Available-for-sale securities						
Alt-A:						
RMBS	\$ -	\$ (27)	\$ (27)	\$ -	\$ (19)	\$ (19)
Total Alt-A:	-	(27)	(27)	-	(19)	(19)
Total available-for-sale private-label MBS	-	(27)	(27)	-	(19)	(19)
Held-to-maturity securities						
Prime:						
RMBS	-	(843)	(843)	(1)	(107)	(108)
Total Prime	-	(843)	(843)	(1)	(107)	(108)
Subprime:						
Home equity loans ¹	-	(206)	(206)	(6)	(77)	(83)
Total subprime	-	(206)	(206)	(6)	(77)	(83)
Total held-to-maturity private-label MBS	-	(1,049)	(1,049)	(7)	(184)	(191)
Total private-label MBS	\$ -	\$ (1,076)	\$ (1,076)	\$ (7)	\$ (203)	\$ (210)

¹ Primarily first-lien mortgage loans that have lower credit score, a higher debt to income ratio, and higher loan to value ratios.

Unsecured Credit Exposures

For short-term liquidity purposes, we can invest in certificates of deposit, commercial paper, and Federal Funds in order to ensure the availability of funds to meet member credit needs. Because these investments are unsecured, our policy and FHFA regulations restrict these investments to short-term maturities and strong investment grade issuers. Approved issuers are concentrated in the United States and Europe.

The following table shows the carrying value of our unsecured credit exposure by counterparty credit rating (excluding the U.S. government, agencies and instrumentalities) and maturities:

As of June 30, 2009	A-1/ P-1	A-1+/ P-1	A-2/ P-1	Total
Unsecured credit exposure maturities:				
	\$ 2,480	\$ 1,735	\$ 190	\$ 4,405
Overnight	2,285	1,735	190	4,210
2-30 days	195	-	-	195

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Advances

Our advance products provide members with asset-liability management capabilities. We offer advances that can be tailored to help members manage the maturity and prepayment characteristics of mortgage loans by reducing members' interest rate risk associated with holding long-term fixed-rate mortgages. To determine the maximum amount and term of the advances we will lend to a member, we assess the member's creditworthiness and financial condition utilizing financial information available to us, including the quarterly reports members file with their regulators. Credit availability is also determined on the basis of the collateral pledged and we conduct periodic on-site collateral reviews to confirm the quality and quantity of collateral pledged. We require delivery of all securities collateral and may also require delivery of loan collateral under certain conditions (for example, when a member's creditworthiness deteriorates). We refer to both members and former members as borrowers in the following disclosures. For details on our collateral policies see **Advances** starting on page 82 in our 2008 Form 10-K.

The following table describes the range of lending values assigned to the types of collateral we accept for advances.

<u>Type of Collateral</u>	<u>Lending Values Applied to Majority of Collateral</u>
Loans:	
1-4 Family mortgages	60% - 85%
Multi-family mortgages	60% - 70%
Other U.S. Government-guaranteed mortgages	60% - 85%
Community financial institution collateral and other real estate related collateral	25% - 50%
Securities:	
U.S. government / Treasury	97%
U.S. agency (excluding MBS)	97%
U.S. agency MBS	85% - 95%
Non-agency MBS/CMO	50% - 90%

The following table provides an estimate of the total collateral loan value relied upon to secure outstanding credit to borrowers with advance borrowings still outstanding:

<u>As of June 30, 2009</u>	<u>Collateral Loan Value ¹</u>	<u>Advances Outstanding (at Par)</u>
Top 5 advance borrowers	\$ 14,780	\$ 10,320
All other advance borrowers	<u>25,561</u>	<u>16,455</u>
Total	<u>\$ 40,341</u>	<u>\$ 26,775</u>

¹ This collateral secures outstanding advances and other credit obligations as defined in the Member Products and Credit Policy.

Collateral arrangements will vary with borrower credit quality, collateral availability, collateral quality, results of periodic on-site reviews of collateral, and overall borrower credit exposure. On-site collateral verifications are performed on a schedule that varies based upon the Bank's assessment of the credit risk of the borrower, the size of the borrower's advances, the types of collateral pledged, and the amount of collateral coverage. Under the security agreement with our borrowers, we have the right to protect our security position with respect to advances, including requiring the posting of additional collateral, whether or not such additional collateral was required to originate or renew an advance. As a result, we may require the delivery of additional or substitute collateral from any borrower at any time during the life of an advance, including delivery of collateral that would not be eligible to pledge for a new advance.

During the period from January 1, 2009 through the time of filing on August 12, 2009, we had 12 members that were placed into receivership by the FDIC. The total dollar value of credit outstanding at the time of their failure was \$138 million. All outstanding obligations of these members to us were either satisfied or transferred to another financial institution. We did not suffer any credit losses.

Letters of Credit

In addition to providing advances, we also provide standby letters of credit as a product we offer to our members, especially as other third party providers exit this market. As of June 30, 2009, we had \$716 million of standby and confirming letters of credit outstanding to 46 members, compared to \$857 million and 51 members at December 31, 2008. To secure these letters of credit, we require collateral as we do on advances.

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MPF Loans

We refer to conforming conventional and government fixed-rate mortgage loans secured by one-to-four family residential properties with maturities from five to 30 years or participations in such mortgage loans that are acquired under the MPF Program as MPF Loans. References to MPF Loans as they relate to the MPF Xtra product exclude mortgage loan participations. We did not purchase or fund subprime or non-traditional mortgages through the MPF Program.

Under the MPF Xtra product, we purchase MPF Program eligible MPF Loans from participating financial institutions (PFIs) and concurrently sell these MPF Loans to Fannie Mae as a third-party investor. Under the MPF Xtra product, PFIs are not required to provide any credit enhancement (CE Amount) and consequently they are not paid credit enhancement fees (CE Fees) as we do for the other conventional MPF products. In addition, PFIs generally retain the right and responsibility for servicing these loans just as they do for the other MPF products described below. See **Mortgage Standards on page 11 and MPF Servicing** on page 14 in our 2008 Form 10-K.

We have entered into a Mortgage Selling and Servicing Contract with Fannie Mae pursuant to which we concurrently sell conventional MPF Loans acquired from PFIs. In connection with each sale, we make certain customary warranties to Fannie Mae regarding the eligibility of the mortgage loans. If an eligibility requirement or other warranty were breached, Fannie Mae could require us to repurchase the MPF Loan. Such a breach would normally also be a breach of the selling PFI's representations and warranties to us, and we could require the PFI to repurchase that MPF Loan from us. During the six months ended June 30, 2009, we were required to repurchase less than \$1 million in MPF Xtra Loans from Fannie Mae, which in turn were repurchased by the PFIs. We incurred no losses on these repurchases.

Under the Mortgage Selling and Servicing Contract with Fannie Mae, we have agreed to be responsible for the servicing of the MPF Loans by the PFIs. If a PFI were to breach its servicing obligations we have the right to terminate its servicing rights and move the servicing to another qualified PFI and require the breaching PFI to indemnify us for any loss arising from such breach.

Though we will receive a transaction services fee in exchange for the services we provide in connection with the MPF Xtra product, the primary reason for this activity is to provide PFIs with liquidity for their mortgage loan portfolios and to fulfill our housing finance mission.

In the second quarter of 2009, three of the FHLBs participating in the MPF Program (MPF Banks) began to offer the MPF Xtra product to their PFIs thereby facilitating the sale of MPF Loans from their PFIs to us and our concurrent sale to Fannie Mae.

For a PFI that is a member of another MPF Bank to sell and/or service MPF Loans under the MPF Xtra product that MPF Bank is obligated to indemnify us for any loss we pay to Fannie Mae that the PFI is obligated to pay and fails to pay due to insolvency. As of June 30, 2009, 169 PFI's have been approved into the MPF Xtra program.

The following table details MPF Xtra activity in 2009.

For the period ended	June 30, 2009	
	Three Months	Six Months
Loans Funded:		
Amount funded	\$ 1,129	\$ 2,377
Number of loans funded	8,153	16,698
Program Fees:		
Earned	\$ *	\$ *
Unearned ¹	\$ 4	\$ 6

* Less than \$1 million

¹ Unearned program fees are earned ratably over the life of the loans.

Under the MPF Program, we historically purchased MPF Loans for our investment portfolio. Effective August 1, 2008, we no longer enter into new master commitments to acquire MPF Loans for investment except for immaterial amounts of MPF Loans to support affordable housing that are guaranteed by the RHS or insured by HUD.

Setting Credit Enhancement Levels

FHFA regulations require that MPF Loans held in our portfolio be credit enhanced so that our risk of loss is limited to the losses of an investor in an AA rated mortgage-backed security, unless we maintain additional retained earnings in addition to a general allowance for credit losses. In our role as MPF Provider, we analyze the risk characteristics of each conventional MPF Loan (as provided by the PFI) using S&P's LEVELS[®] model in order to determine the required CE Amount for a loan to be acquired and held as an investment by an MPF Bank (MPF Program Methodology). See **Setting Credit Enhancement Levels** on page 85 of our 2008 Form 10-K for a further description.

Except for the MPF Xtra product, the MPF Bank and PFI share the risk of credit losses on conventional MPF products by structuring potential losses on MPF Loans into layers with respect to each master commitment. The MPF products with credit enhancement were designed to allow for periodic resets of the CE Amount as further described in **Setting Credit Enhancement Levels** on page 85 in our 2008 Form 10-K. We had no material changes in reset PFI direct CE Amounts in the first six months of 2009.

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For master commitments with a first loss account (FLA) equal to 100 basis points (all MPF 100, MPF 125 and some MPF Plus master commitments), we only partially rely on our ability to reduce performance based CE Fees when measuring our effective credit protection. As a result, we hold additional retained earnings against the related master commitments in accordance with the AMA regulations which at June 30, 2009 totaled \$71 million.

For the MPF Plus product, the PFI is required to provide a supplemental mortgage insurance (SMI) policy covering the MPF Loans in the master commitment and having a deductible initially equal to the FLA. As of June 30, 2009 and December 31, 2008, the outstanding balance of MPF Loans under MPF Plus master commitments for which the PFI has obtained SMI coverage was \$10.8 billion and \$13.2 billion. The amount of SMI coverage provided against losses was \$135 million at June 30, 2009 and \$225 million at December 31, 2008. The reduction in coverage was due to the resetting of SMI policies as provided in the MPF Plus product structure.

Credit Risk Exposure

Our credit risk on MPF Loans held in our portfolio is the potential for financial loss due to borrower default or depreciation in the value of the real estate collateral securing the MPF Loan, offset by the PFIs' credit enhancement protection amount (CEP Amount). The PFI's CEP Amount consists of the PFI's CE Amount (which may include SMI) and any contingent performance based CE Fees. We also face credit risk of loss on MPF Loans to the extent such losses are not recoverable under the private mortgage insurance (PMI), as well as the PFIs' failure to pay servicer paid losses not covered by FHA or HUD insurance, or VA or RHS guarantees. The portion of MPF Loan balances outstanding exposed to credit losses not recoverable from these sources was approximately \$22.0 billion at June 30, 2009 and \$26.6 billion at December 31, 2008.

Our actual credit exposure is less than these amounts because the borrower's equity, which represents the fair value of underlying property in excess of the outstanding MPF Loan balance, has not been considered. Although

housing prices have declined, a significant decline in the fair value of the underlying property would have to occur before we would be exposed to credit losses on our conventional MPF Loans. This is because our average conventional loan-to-value (LTV) ratio at origination was 68% at both June 30, 2009 and December 31, 2008. For those loans with an LTV ratio over 80%, we require PMI. Please see **Mortgage Guaranty Insurance Provider Concentration** section below for discussion of our credit risk to PMI providers. Our LTV ratio is enhanced by the seasoned nature of our portfolio because principal paydowns lower the LTV ratio. In addition, our credit risk exposure is mitigated for conventional MPF Loans by average FICO® scores at the time of origination that were 737 at June 30, 2009 and 739 at December 31, 2008.

For more information on our credit risk exposure on MPF Loans, see **Credit Risk Exposure** on page 87 in our 2008 Form 10-K.

Concentration Risks

In conjunction with assessing credit risks on the MPF Loan portfolio, we also assess concentration risks that could negatively impact this portfolio. For a description of our concentration risks see page 87 in our 2008 Form 10-K. There were no material changes in our PFI Servicer or Credit Enhancement concentrations since December 31, 2008.

Mortgage Guaranty Insurance Provider Concentration – We are exposed to the risk of non-performance of mortgage insurance (MI) companies. Our policy is to limit our credit exposure to each MI company to 10% of its regulatory capital. Credit exposure is defined as the total of PMI and SMI coverage written by an MI company on MPF Loans held by us that are more than 60 days delinquent. We receive PMI coverage information only at acquisition of MPF Loans and do not receive notification of any subsequent changes in PMI coverage. At June 30, 2009, none of the MI companies were in excess of our limits. For more information on our concentration risk exposure from MI companies, see **Mortgage Guaranty Insurance Provider Concentration** on page 88 in our 2008 Form 10-K.

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The following table details our exposure to MI companies providing insurance coverage:

As of June 30, 2009	Loan Balance with PMI	Loan Balance with SMI	Amount of Coverage			%	Lowest Credit Rating as of August 7, 2009 ¹
			PMI	SMI	Total		
Mortgage Guaranty Insurance Co. (MGIC)	\$ 517	\$ 4,521	\$ 146	\$ 55	\$ 201	36%	BB
Genworth Mortgage Insurance Corp.	218	1,779	63	27	90	16%	BBB
PMI Mortgage Insurance Co.	222	1,511	63	7	70	12%	BB-
United Guaranty Residential Insurance Co.	186	2,366	51	40	91	16%	BBB
All Others	374	630	108	6	114	20%	BB to BBB-
Total MI Coverage	\$ 1,517	\$ 10,807	\$ 431	\$ 135	\$ 566	100%	

¹ All of the above listed MI companies have been placed on negative outlook by at least one Nationally Recognized Statistical Rating Organization (NRSRO).

We perform a quarterly analysis evaluating the financial condition and concentration risk regarding the MI companies. Based on an analysis using the latest available results at June 30, 2009, none of the MI companies passed all of our primary early warning financial tests, which include rating level tests, ratings watch/outlook tests and profitability tests.

If a PMI provider is downgraded, we may request the servicer to obtain replacement PMI coverage with a different provider. However, it is possible that replacement coverage may be unavailable or result in additional cost to us.

As of the time of filing on August 12, 2009, no MI company on the approved MI company list currently has an AA- or better claims paying ability rating from more than one NRSRO, so the current criteria for MI companies to remain on the approved MI company list at this time is acceptability for use in S&P's LEVELS[®] modeling software.

If an SMI provider fails to maintain a credit rating of at least AA- or its equivalent from a NRSRO under the MPF Plus product, the PFI has six months to either replace the SMI policy or provide at its own undertaking an equivalent to the SMI coverage, or it will forfeit its performance based CE fees. Some PFIs have elected to not replace the SMI policies, as a result we have begun withholding performance based CE Fees from these PFIs.

For further discussion of how this may affect us, see **Risk Factors** on page 23 in our 2008 Form 10-K.

Geographic Concentration – We have MPF Loans in all 50 states, Washington, D.C., and Puerto Rico. No single zip code represents more than 1% of MPF Loans on our statements of condition. Our largest concentrations of MPF Loans (of 10% or more) were secured by properties located in Wisconsin (19%) and Illinois (11%). An overall decline in the economy, residential real estate market, or

the occurrence of a natural disaster could adversely affect the value of the mortgaged properties in these states and increase the risk of delinquency, foreclosure, bankruptcy or loss on MPF Loans.

MPF Loan Portfolio Analysis

The following table summarizes our MPF Loan non-accrual status:

As of	June 30, 2009	December, 31 2008
MPF Loans, net	\$ 26,964	\$ 32,087
MPF Loans past due 30-90 days and still accruing interest	655	761
MPF Loans past due 90 days or more and still accruing interest	396	319
Non-accrual MPF Loans, par value	27	19
Impaired MPF Loans ¹	18	12
Loans in foreclosure	131	98
Real estate owned	40	35

¹ MPF Loans that are on non-performing status, and that are viewed as collateral-dependent loans, are considered impaired. MPF Loans are viewed as collateral-dependent loans when repayment is expected to be provided solely by the sale of the underlying property, and there is no other available and reliable source of repayment.

Our interest contractually due on non-accrual loans and our interest received on non-accrual loans was under \$1 million dollars for the three and six months ended June 30, 2009 and 2008. We do not place delinquent MPF Loans on non-performing status when losses are not expected to be incurred as a result of the PFI's assumption of credit risk on MPF Loans by providing credit enhancement protections.

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In the three and six months ended June 30, 2009, we recorded an additional \$2 million and \$5 million provision for MPF Loan credit losses due to recent portfolio and market trends related to rising delinquency rates, increased loss severities, and prepayment speeds. Also included was an increase in estimate of our allocation of losses under the MPF credit risk sharing structure resulting from increased mortgage prepayment rates which negatively impact our ability to offset potential losses through the withholding of PFI credit enhancement fees.

Derivatives

We engage in most of our derivative transactions with large money-center banks and major broker-dealers. Some of these banks and broker-dealers or their affiliates buy, sell, and distribute consolidated obligations. We are subject to credit risk due to the risk of nonperformance by counterparties to our derivative agreements. The degree

of counterparty risk depends on the extent to which master netting arrangements are included in such contracts to mitigate the risk. We manage counterparty credit risk through credit analysis, collateral requirements, and adherence to the requirements set forth in our policies and FHFA regulations. Based on credit analyses and collateral requirements, we do not anticipate any credit losses on our derivative agreements. See **Note 13 – Derivatives and Hedging Activities** to the financial statements for further details.

Derivatives Exposures to Lehman Brothers Special Financing, Inc.

As of June 30, 2009, we owed a net amount of \$6 million to Lehman Brothers Special Financing Inc. (LBSFI) under an ISDA Master Agreement, as further discussed in **Accounting Issues Related to Lehman Derivative Termination** on page F-42 in our 2008 Form 10-K. It is possible that we may incur additional costs associated with the final settlement procedures with LBSFI, but we do not expect those costs to be material.

The maximum amount of exposure to credit loss is the fair value of derivative assets, not the notional amount. The following table summarizes our derivative counterparty credit exposure:

Counterparty Credit Rating as of June 30, 2009	Notional Amount	Exposure at Fair Value ³	Cash Collateral Held	Securities Collateral Held	Total Collateral Held	Net Exposure After Collateral ⁴
AA	\$ 17,941	\$ 139	\$ 162	\$ -	\$ 162	\$ -
A	31,808	88	35	49	84	4
BBB	9	-	-	-	-	-
Affiliates ¹						
AA	5,142	-	-	-	-	-
A	8,832	-	-	-	-	-
Total Counterparties	63,732	227	197	49	246	4
Member Institutions ²	3	-	-	-	-	-
Total derivatives	\$ 63,735	\$ 227	\$ 197	\$ 49	\$ 246	\$ 4

¹ Affiliates are derivative counterparties who are affiliates of our members.

² Member Institutions include: (i) derivatives with members where we are acting as an intermediary, and (ii) delivery commitments for MPF Loans.

³ Exposure at Fair Value excludes cash collateral held.

⁴ Net exposure after collateral is monitored and reported on an individual counterparty basis. Because some counterparties are over-collateralized, net exposure after collateral may not equal the difference between Exposure at Fair Value and Total Collateral Held.

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Credit Ratings

On July 1, 2009, Standard & Poor's Ratings Services announced ratings actions on the FHLBs of Chicago and Seattle. The following is a summary of the actions taken:

The long-term counterparty credit rating for the FHLB of Chicago was upgraded to AA+ with a stable outlook.

The FHLB of Seattle's counterparty credit ratings of AA+/A-1+ were affirmed and it was removed from CreditWatch Negative.

There have been no other changes in our credit ratings subsequent to that which we reported in our first quarter 2009 10-Q. The AAA rating of the FHLBs' consolidated obligations has not been affected by these ratings actions and we do not believe that the actions will have an impact on our cost of or ability to issue debt, or to enter into derivatives agreements.

For further discussion of how ratings changes may impact us in the future in order to fund our business, see **Risk Factors** on page 23 in our 2008 Form 10-K.

Legislative and Regulatory Developments

Changes to Regulation of GSEs

The Housing Act was enacted into law on July 30, 2008 and became effective immediately. The Housing Act established the FHFA as the new federal regulator of the FHLBs, Fannie Mae and Freddie Mac, and addressed other GSE reform issues.

As the FHFA issues regulations to implement the Housing Act, we continue to review the impact and effect of the Housing Act and such regulations on our business and operations. For highlights of significant provisions of the Housing Act that directly affect us, see **Legislative and Regulatory Developments** on page 18 in our 2008 Form 10-K.

Helping Families Save Their Homes Act of 2009

On May 20, 2009, the Helping Families Save Their Home Act of 2009 was enacted to encourage mortgage loan modifications in order to prevent foreclosures and to buttress the federal deposit insurance system. One provision in the act provides a safe harbor from liability for mortgage servicers who modify the terms of a mortgage consistent with certain qualified loan modification plans. Another provision extends through 2013 the temporary increase in federal deposit insurance coverage to \$250,000 for banks, thrifts, and credit unions. The final act did not include a "cramdown" provision that was proposed in an earlier version of the legislation and would have allowed bankruptcy judges to modify the terms of mortgage loans. At this time it is uncertain what effect the provisions regarding loan modifications will have on the value of our mortgage asset portfolio. The extension of federal deposit insurance coverage could decrease demand for our advances.

Proposed Financial Regulatory System Reorganization

On June 17, 2009, President Obama announced a proposal to improve the effectiveness of the federal regulatory structure that would, among other things, cause a restructuring of the current bank regulatory system. One provision of the plan would require the U.S. Treasury Department and the Department of Housing and Urban Development to develop recommendations on the future of the FHLBs, along with Fannie Mae and Freddie Mac, with a goal of developing such recommendations in time for the 2011 U.S. fiscal budget. We are unable to predict what such recommendations may include and therefore can not predict the impact of President Obama's proposal on the Bank.

Final Capital Rule

On January 30, 2009, the FHFA adopted an interim final rule that defines critical capital for the FHLBs, establishes criteria for the capital classifications identified in the Housing Act and sets forth prohibited and mandated actions based on an FHLB's capital classification, as further discussed in **Interim Capital Rule** on page 19 in our 2008 Form 10-K. Effective August 4, 2009, the FHFA adopted the interim final rule as a final regulation with certain clarifying changes. At this time, we do not expect this rule to have a material impact on us.

Proposed Rule for FHLB Membership of Community Development Financial Institutions (CDFIs)

On May 15, 2009, the FHFA published a proposed amendment to its membership regulations to authorize non-federally insured CDFI Fund-certified CDFIs to become members of FHLBs. The newly eligible CDFIs would include community development loan funds, venture capital funds, and state chartered credit unions without federal deposit insurance provided they are certified by the CDFI Fund of the U.S. Treasury Department. The proposed rule sets forth eligibility and related procedural requirements for the newly eligible CDFIs. The comment period ended July 14, 2009.

Proposed Rule on Executive Compensation

On June 5, 2009, the FHFA published a proposed a rule which gives the Director of the FHFA the authority to prohibit and withhold compensation provided by an FHLB to an executive officer that is not reasonable and comparable. The proposed rule also discusses the type of factors the FHFA Director may consider in determining whether executive compensation is reasonable and comparable. In addition to withholding compensation, the FHFA Director would have the authority to approve certain compensation and termination benefits if this rule is adopted as proposed. The comment period ended August 4, 2009.

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Proposed Rule on the Reporting of Fraudulent Financial Instruments and Loans

On June 17, 2009, the FHFA published a proposed rule that would require the FHLBs, Fannie Mae and Freddie Mac to report to the FHFA, upon discovery, that it purchased or sold a fraudulent loan or financial instrument or suspects possible fraud relating to a purchase or sale of any loan or financial instrument. Under the proposed rule, fraud and potential fraud are defined broadly potentially creating significant reporting obligations for us if the rule is implemented as proposed. The comment period ends August 17, 2009.

Proposed Rule Regarding Golden Parachute and Indemnification Payments

On June 29, 2009, the FHFA published a proposed rule setting forth various standards that it will take into consideration when limiting or prohibiting golden parachute and indemnification payments. The provisions of the rule cover payments to our officers and directors. If adopted as proposed, the rule would conform existing FHFA rules on golden parachutes to FDIC rules and further define limitations on golden parachute payments made by Fannie Mae, Freddie Mac or an FHLB that has been assigned less than satisfactory examination ratings. The comment period ended July 29, 2009.

Proposed Rule on Changes to the Board of Directors of the FHLB System Office of Finance

On August 4, 2009, the FHFA proposed a rule that would, among other things, expand the Office of Finance Board of Directors to include all of the FHLB presidents plus an audit committee comprised of three to five independent directors. In addition, the proposed rule would authorize the audit committee to ensure that the FHLBs adopt

consistent accounting policies and procedures as part of the audit committee's oversight of preparation of the FHLB System's combined financial reports. If the FHLBs are not able to agree on such consistent accounting policies and procedures, the proposed rule would permit the audit committee, in consultation with the FHFA, to prescribe them. The comment period ends October 5, 2009. At this time, we cannot predict what impact the final rule may have on us.

FHFA Designation of Size and Composition of the Board of Directors for 2010

On June 22, 2009, the Director of the FHFA determined that a 17-member board of directors will govern the Bank for 2010, comprised of ten member directorships and seven independent directorships. The Director of the FHFA annually determines the size of the board for each FHLB, with the designation of member directorships based on the number of shares of FHLB stock required to be held by members in each state, which for the Bank in 2010 will be six for Illinois and four for Wisconsin. See **Submission of Matters to a Vote of Security Holders** on page 36 in our 2008 Form 10-K for more information on the rules governing the election of our directors.

FHFA Guidance Related to Determining Other-Than-Temporary Impairment

On April 28, 2009 and May 7, 2009, the FHFA provided us with guidance related to our process for determining OTTI with respect to our holdings of private-label MBS. See **Note 3 – Adopted and Recently Issued Accounting Standards & Interpretations** for a description of this guidance.

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**Item 3. Quantitative and Qualitative Disclosures
about Market Risk.**

Market Risk Exposures

Market risk is the risk that the value of our financial assets will decrease due to changes in market risk factors. There are several market risk factors that may impact the value of our financial assets, but interest rate risk, which arises due to the variability of interest rates, is the most critical. Our key interest rate risk exposures include:

- *Yield-curve risk* – We are exposed to movements in the benchmark yield curve used to discount the future cash flows from our assets, liabilities and derivatives.
- *Option risk* – We are exposed to option risk as the value of option positions (explicit and embedded) vary due to changes in the implied volatility of the yield curve as well as the yield curve itself.
- *Basis risk* – We are exposed to basis risk as the yields on different assets, liabilities and derivatives are determined on different benchmark yield curves. This

includes (1) differences between the swap curve and the Office of Finance cost of funds or consolidated obligation curve; (2) changes in individual securities' spreads to the swap curve as a result of changes in supply, demand and credit quality of different securities in the market; and (3) changes in mortgage rates relative to the swap curve.

In an effort to measure our exposure to these risks, we discount the cash flows generated from modeling the terms and conditions of all interest-sensitive assets and liabilities to determine their fair values (or their spread to the swap curve for securities where a third-party price is obtained) in the current interest rate environment. This includes consideration of options both explicit and embedded using a lattice model or Monte Carlo simulation for mortgages and mortgage-backed securities. We estimate yield-curve, option and basis risk exposures by calculating the change in fair value in relation to various parallel changes in interest rates, implied volatility, prepayment speeds, spreads to the swap curve and mortgage rates.

The table below summarizes our sensitivity to various interest rate risk exposures in terms of changes in fair value.

	As of June 30, 2009					As of December 31, 2008				
	Yield Curve Risk	Option Risk		Basis Risk		Yield Curve Risk	Option Risk		Basis Risk	
		Implied Volatility	Prepayment Speeds	LIBOR Spread	Mortgage Spread		Implied Volatility	Prepayment Speeds	LIBOR Spread	Mortgage Spread
Advances	\$ (4)	\$ 6	\$ -	\$ (6)	\$ -	\$ (5)	\$ 5	\$ -	\$ (8)	\$ -
MPF Loans	(7)	(34)	(3)	(9)	4	(5)	(19)	(7)	(7)	4
Mortgage Backed Securities	(6)	(11)	-	(7)	1	(5)	(8)	2	(4)	(1)
Other interest earning assets	(1)	-	-	(4)	-	-	-	-	-	-
Interest-bearing liabilities	14	6	-	14	-	16	7	-	16	-
Derivatives	4	8	-	-	-	(1)	5	-	-	-
Total	\$ -	\$ (25)	\$ (3)	\$ (12)	\$ 5	\$ -	\$ (10)	\$ (5)	\$ (3)	\$ 3

Yield-curve risk – Change in fair value for a one basis point parallel increase in the swap curve.

Option risk (implied volatility) – Change in fair value for a one percent parallel increase in the swaption volatility.

Option risk (prepayment speeds) – Change in fair value for a one percent increase in prepayment speeds.

Basis risk (Spread to LIBOR) – Change in fair value for a one basis point parallel increase in the spread to the swap curve.

Basis risk (Mortgage spread) – Change in fair value for a one basis point increase in mortgage rates.

There were few material changes in our sensitivity to various interest rate risk exposures during the first half of 2009. The only material change was a heightened sensitivity to implied volatility increases in the MPF Loans increasing from a \$19 million loss to a \$34 million loss for a one percent increase in implied swaption volatility.

The sensitivities above are limited in that they do not incorporate other risk exposures that may impact us. These include, but are not limited to, non-parallel shifts in yield curves, implied volatility, prepayment speeds and spreads; and basis risk related to differences between the swap and the consolidated obligation curves.

Our option positions embedded in our mortgage assets and callable debt impact our yield curve risk profile, such that swap curve changes significantly greater than one basis point cannot be linearly interpolated from the table above.

Duration gap, which is expressed in months, is another measure used to express the sensitivity of assets and liabilities to interest rate changes. Duration gap is calculated by aggregating the dollar duration of all assets, liabilities, and derivatives, and dividing that total by the total fair value of assets. A positive duration gap indicates an exposure to rising interest rates, whereas a negative duration gap points to an exposure to falling interest rates. As of June 30, 2009, our duration gap was 0.3 months, compared to -0.3 months as of December 31, 2008.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

As of June 30, 2009 our fair value deficit (relative to book value) was \$1.6 billion, and our market-to-book value ratio was 26%. Our previous year-end fair value deficit was \$3.3 billion, and our market-to-book value ratio was -24%. Favorable movements in implied volatility as well as the accounting effects of investments that were other than temporarily impaired substantially contributed to the improvement in our deficit this quarter.

Interest Rate Risk Management

We manage our exposures to yield curve and volatility changes using swaps, swaptions, caps, floors and callable debt. We do not manage exposure to changes in spreads. We may conduct hedging activity in an effort to reduce exposure to a single transaction or a group of transactions. We evaluate our hedging daily and modify our positions as necessary. See **Note 13 – Derivatives and Hedging Activities** for further information.

Our Asset/Liability Management Committee provides oversight to our interest rate risk management practices and policies. This includes routine reporting to senior Bank management and the Board of Directors, as well as the establishment of an Interest Rate Risk Policy designed to create prudent interest rate risk limits.

On February 20, 2009, we received a non-objection letter from the FHFA related to our proposal to apply temporarily direct dollar limits on changes in fair value under parallel interest rate shocks instead of the duration and convexity limits that were applied in the past. As a result, the Interest Rate Risk Policy in effect as of June 30, 2009, places limits on fair value changes for all measured parallel interest rates scenarios between -200 and +200 basis points. Some scenarios may not be measured when swap rates are less than 2%. The table below shows the fair value changes as of June 30, 2009 with respect to the Interest Rate Risk Policy limits.

The table below shows our market value changes for all measured scenarios as of June 30, 2009 with respect to the Interest Rate Risk Policy limits.

June 30, 2009		
Scenario	Change in Market Value	Change in Market Value must be greater than
-200 bp	\$ *	\$ (185.0)
-100 bp	*	(77.5)
-50 bp	*	(30.0)
-25 bp	(1.6)	(12.5)
+25 bp	(14.1)	(25.0)
+50 bp	(25.7)	(60.0)
+100 bp	(36.6)	(155.0)
+200 bp	(66.1)	(370.0)

* Due to the low interest rate environment at June 30, 2009, these values cannot be calculated.

We continue to work with the FHFA to develop a set of interest rate risk management policies and submitted revised policies to the Deputy Director on July 16, 2009 pursuant to the Consent Cease and Desist order.

The Interest Rate Risk Policy in effect on December 31, 2008 set dollar duration limits to which we were required to manage.

The following table summarizes our duration as of December 31, 2008 in comparison to the Interest Rate Risk Policy limits.

Duration as of December 31, 2008			
Scenario	Actual Duration (whole \$)	Duration Policy Limits	
		Market value of equity is less than \$700 million (in whole \$)	Market value of equity equals or exceeds \$700 million (in years)
- 200 bp	\$ *	\$ -490,000	-7.00 years
- 100 bp	*	-420,000	-6.00 years
Base case	-228,106	±350,000	±5.00 years
+ 100 bp	176,716	+420,000	+6.00 years
+ 200 bp	293,218	+490,000	+7.00 years

* Due to the low interest rate environment, these values cannot be calculated.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

Item 4. Controls and Procedures

Not applicable.

Item 4T. Controls and Procedures

Disclosure Controls and Procedures

Under the supervision and with the participation of management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report (the Evaluation Date). The evaluation of our disclosure controls and procedures by our principal executive officer and principal financial officer included consideration of the restatement described in the "Restatement Note" to the Financial Statements of this Form 10-Q/A, where we restated our Condensed Statement of Cash Flows for the six months ended June 30, 2009. Based on this evaluation and because of the material weakness described below, the principal executive officer and principal financial officer concluded as of the Evaluation Date that the disclosure controls and procedures were not effective to ensure that such that information relating to us that is required to be disclosed in reports filed with the SEC (i) is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms, and (ii) is accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure. Notwithstanding this material weakness, our management has concluded, based on the supplemental procedures performed to prepare the restated Condensed Statement of Cash Flows and reliance on existing controls not impacted by this material weakness, that the financial statements included in this Form 10-Q/A fairly present in all material respects our financial position, results of operations, capital position and cash flows for the periods presented in conformity with generally accepted accounting principles.

Changes in Internal Control Over Financial Reporting

Except for the remediation of the material weakness noted below, there were no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting for the second quarter of 2009. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of annual or interim financial statements will not be prevented or detected on a timely basis.

As of June 30, 2009, we did not maintain effective controls over the preparation and review of our Condensed

Statement of Cash Flows. This control deficiency resulted in an error in our Condensed Statement of Cash Flows as originally reported, which in turn required a restatement of our Condensed Statement of Cash Flows for the six months ended June 30, 2009. Specifically, we did not maintain effective control over the calculation and presentation of cash flows from certain derivative and investment activities which led to the misclassification of cash flows between Operating Activities, Investing Activities, and Financing Activities in the Condensed Statement of Cash Flows for the six months ended June 30, 2009. Accordingly, our management determined that this control deficiency constitutes a material weakness in internal control over financial reporting as of June 30, 2009.

Remediation of Material Weakness

Management has taken steps to remediate the material weakness noted above. Controls over the preparation of the Statement of Cash Flows have been enhanced through the implementation of improved procedural and review controls. Management believes that this material weakness has been fully remediated as of December 31, 2009.

Consolidated Obligations

Our disclosure controls and procedures include controls and procedures for accumulating and communicating information relating to our joint and several liability for the consolidated obligations of other FHLBs. For further information, see **Controls and Procedures** on page 97 of our **2008 Form 10-K**.

Federal Home Loan Bank of Chicago
(Dollars in millions except per share amounts unless otherwise indicated)

PART II

Item 1. Legal Proceedings

We may be subject to various legal proceedings arising in the normal course of business. After consultation with legal counsel, management is not aware of any such proceedings that might result in our ultimate liability in an amount that will have a material effect on our financial condition or results of operations.

Item 1A. Risk Factors

In addition to the information presented below, readers should carefully consider the factors set forth in the **Risk Factors** section on page 23 in our 2008 Form 10-K, which could materially affect our business, financial condition, or future results. The risks described below and in our prior filings are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may also severely affect us.

We are subject to increased credit and liquidity risk exposures related to mortgage loans that back our private-label MBS investments, and any increased delinquency rates and credit losses could adversely affect the yield on or value of these investments.

Prior to February 2007, we invested in private-label MBS, which are backed by subprime, prime and alternative documentation or Alt-A mortgage loans. We held private-label MBS with a carrying value of \$2.495 billion at June 30, 2009 and recorded a total OTTI charge of \$1.286 billion for the first six months of 2009. Although we only invested in AAA rated tranches when purchasing these MBS, a majority of these securities have subsequently been downgraded. See **Credit Risk – Investments** on page 69 for a description of these securities. Delinquencies and losses with respect to residential mortgage loans may continue to increase and residential property values in many states have declined after extended periods during which those values appreciated. If delinquencies and/or default rates on mortgages continue to increase, and/or there is an additional decline in residential real estate values, we could experience reduced yields or additional losses on our private-label MBS.

Market prices for the private-label MBS we hold may continue to decrease due to credit deterioration, market

uncertainty and illiquidity. If these trends continue, we could experience additional other-than-temporary impairment on these investment securities in the future, which could result in significant losses. Furthermore, deterioration in the financial condition of mortgage insurers or other parties that provide credit support for the private-label MBS has adversely affected the value of these securities and may continue.

As described in **Critical Accounting Policies and Estimates** on page 65, other than temporary impairment assessment is a subjective and complex assessment by management. We incurred credit related impairment charges of \$210 million and deferred non-credit related impairment to AOCI of \$1.076 billion for MBS that management determined were other-than-temporarily impaired as of June 30, 2009. If loan credit performance of our private-label MBS deteriorates beyond the forecasted assumptions concerning loan default rates, loss severities, prepayment speeds and delinquencies, we may recognize additional credit losses and reductions to other comprehensive loss. For example, under a scenario with more stressful housing price assumptions that is more fully described under **Critical Accounting Policies and Estimates** on page 65, including house prices that were 5% lower at the trough, our credit-related OTTI charges would have increased by \$124 million for the quarter ending June 30, 2009 from \$124 million to \$248 million. As of June 30, 2009, we held \$837 million of retained earnings.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

Item 3. Defaults upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Federal Home Loan Bank of Chicago

Item 6. Exhibits

- 31.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Principal Executive Officer
- 31.2 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 by the Principal Financial Officer
- 32.1 Certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by the Principal Executive Officer
- 32.2 Certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 by the Principal Financial Officer

Federal Home Loan Bank of Chicago

Glossary of Terms

Advances: Secured loans to members

ABS – Asset-backed-securities

AFS: Available-for-sale securities

Agency MBS: mortgage-backed securities issued by, or comprised of mortgage loans guaranteed by, Fannie Mae or Freddie Mac

Agent Fees: loan origination fees we may pay/receive to/from PFIs for the origination of MPF Loans as our agent

AHP: Affordable Housing Program

Acquired Member Assets (“AMA”): Assets that an FHLB may acquire from or through FHLB System members or housing associates by means of either a purchase or a funding transaction

AOCI: Accumulated Other Comprehensive Income

CE Fee: Credit enhancement fee. PFIs are paid a credit enhancement fee for managing credit risk and in some instances, all or a portion of the CE Fee may be performance based.

CE Amount: A PFI's assumption of credit risk on conventional MPF Loan products that are funded by, or sold to, an MPF Bank by providing credit enhancement either through a direct liability to pay credit losses up to a specified amount or through a contractual obligation to provide SMI. Does not apply to the MPF Xtra product.

CEP Amount: This includes the CE Amount. In addition, the PFI may also contract for a contingent performance based credit enhancement fee whereby such fees are reduced by losses up to a certain amount arising under the master commitment

CFI: Community Financial Institution – Defined as Federal Deposit Insurance Corporation (“FDIC”)-insured institutions with an average of total assets over the prior three years which is less than the level prescribed by the FHFA. The average total assets for calendar year-ends 2006-2008 must be \$1 billion or less (\$625 million for 2005-2007 and \$599 million for 2004-2006).

CMBS: Commercial mortgage backed securities

Conforming mortgage loans: Loans that meet the Fannie Mae's or Freddie Mac's original loan amount limits and underwriting guides. Nonconforming mortgage loans are mortgage loans that do not meet these requirements.

Consolidated Obligations: FHLB debt instruments which are the joint and several liability of all FHLBs; issued by the Office of Finance

Core Based Statistical Areas (CBSA) – Refers collectively to metropolitan and micropolitan statistical areas as defined by the United States Office of Management and Budget. As currently defined, a CBSA must contain at least one urban area of 10,000 or more people.

Delivery Commitment: Mandatory commitment of the PFI to sell or originate eligible mortgage loans

Deputy Director: Deputy Director, Division of FHLB Regulation of the FHFA

Designated Amount: A percentage of the outstanding principal amount of the subordinated notes we are allowed to include in determining compliance with our regulatory capital and minimum regulatory leverage ratio requirements and to calculate our maximum permissible holdings of mortgage-backed securities and unsecured credit

Discount notes: Consolidated obligation discount notes

Fannie Mae: Federal National Mortgage Association

FDIC: Federal Deposit Insurance Corporation

FFELP – Federal Family Education Loan Program

FHA: Federal Housing Administration

FHFA: Federal Housing Finance Agency – The Housing and Economic Recovery Act of 2008 enacted on July 30, 2008 created the Federal Housing Finance Agency which became the new regulator of the FHLBs.

FHLB Act: The Federal Home Loan Bank Act of 1932, as amended

FHLBs: The 12 Federal Home Loan Banks or subset thereof

Federal Home Loan Bank of Chicago

Finance Board: The Federal Housing Finance Board. The Bank was supervised and regulated by the Finance Board, prior to creation of the Federal Housing Finance Agency as regulator of the FHLBs by the Housing Act, effective July 30, 2008.

Fitch: Fitch Ratings, Inc.

FLA: First loss account is a memo account used to track the MPF Bank's exposure to losses until the CE Amount is available to cover losses.

Freddie Mac: Federal Home Loan Mortgage Corporation

GAAP: Generally accepted accounting principles in the United States of America

Ginnie Mae: Government National Mortgage Association

GLB Act: Gramm-Leach-Bliley Act of 1999

GSE: Government sponsored enterprise

Housing Act: Housing and Economic Recovery Act of 2008, enacted July 30, 2008

HUD: Department of Housing and Urban Development

HTM: Held-to-maturity securities

LIBOR: London Interbank Offered Rate

LTV: Loan-to-value ratio

MBS: Mortgage-Backed Security

MI: Mortgage Insurance

Moody's: Moody's Investors Service

MPF®: Mortgage Partnership Finance

MPF Guides: MPF Origination Guide and MPF Servicing Guide

MPF Impaired Loans: An individual loan in which it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement

MPF Loans: Conforming conventional and government fixed-rate mortgage loans secured by one-to-four family residential properties with maturities from five to 30 years or participations in such mortgage loans that are acquired under the MPF Program.

MPF Nonaccrual Loans: Nonperforming mortgage loans in which the collection of principal and interest is determined to be doubtful or when interest or principal is past due for 90 days or more, except when the MPF Loan is well secured and in the process of collection

MPF Provider: The Federal Home Loan Bank of Chicago, in its role of providing programmatic and operational support to the MPF Banks and their PFIs

MPF Shared Funding® program: A program to provide a platform to allow mortgage loans to be sold through the MPF Program system to a third party-sponsored trust and "pooled" into securities.

MPF Xtra™ product: The MPF Program product under which we acquire MPF Loans from PFIs without any CEP Amount and concurrently resell them to Fannie Mae.

NRSRO: Nationally Recognized Statistical Rating Organization

OAS: Option Adjusted Spread

Office of Finance: A joint office of the FHLBs established by the Finance Board to facilitate issuing and servicing of consolidated obligations

OTTI: Other-than-temporary impairment

OTTI Committee – OTTI Governance Committee formed by the FHLBs with the responsibility for reviewing and approving the key modeling assumptions, inputs and methodologies to be used to generate cash flow projections, which are used in analyzing credit losses and determining OTTI for private-label MBS.

PFI: Participating Financial Institution. A PFI is a member (or eligible housing associate) of an MPF Bank that has applied to and been accepted to do business with its MPF Bank under the MPF Program

PFI Agreement: MPF Program Participating Financial Institution Agreement

PMI: Primary mortgage insurance

REFCORP: Resolution Funding Corporation

Federal Home Loan Bank of Chicago

Regulatory Capital: The sum of the paid-in value of capital stock and mandatorily redeemable capital stock (together defined as “regulatory capital stock”) plus retained earnings

Regulatory Capital Ratio: Regulatory capital plus Designated Amount of subordinated notes divided by total period-end assets

RHS: Department of Agriculture Rural Housing Service

RMBS: Residential mortgage backed securities

S&P: Standard and Poor’s Rating Service

SEC: Securities and Exchange Commission

Senior Liabilities: Our existing and future liabilities, such as deposits, consolidated obligations for which we are the

primary obligor, and consolidated obligations of the other FHLBs for which we are jointly and severally liable

SMI: Supplemental Mortgage Insurance

SPE: Special Purpose Entity

System: The Federal Home Loan Bank System consisting of the 12 Federal Home Loan Banks and the Office of Finance

VA: Department of Veteran’s Affairs

Voluntary Capital Stock: Capital stock held by members in excess of their statutory requirement

Voluntary Capital Stock Ratio: Voluntary capital stock divided by regulatory capital

Federal Home Loan Bank of Chicago

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this Amendment No. 1 on Form 10-Q/A to the registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2009 to be signed on its behalf by the undersigned thereunto duly authorized.

Federal Home Loan Bank of Chicago

/s/ Matthew R. Feldman

By: Matthew R. Feldman

Title: President and Chief Executive Officer
(Principal Executive Officer)

Date: February 16, 2010

/s/ Roger D. Lundstrom

By: Roger D. Lundstrom

Title: Executive Vice President, Financial Information and Chief Financial
Officer
(Principal Financial Officer and Principal Accounting Officer)

Date: February 16, 2010

**Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
by the Principal Executive Officer**

I, Matthew R. Feldman, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q/A of the Federal Home Loan Bank of Chicago;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluations; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions);

- a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
- b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 16, 2010

By: /s/ Matthew R. Feldman

Name: Matthew R. Feldman

Title: President and Chief Executive Officer
(Principal Executive Officer)

**Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
by the Principal Financial Officer**

I, Roger D. Lundstrom, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q/A of the Federal Home Loan Bank of Chicago;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluations; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions);

- a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
- b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 16, 2010

By: /s/ Roger D. Lundstrom

Name: Roger D. Lundstrom

Title: Executive Vice President, Financial
Information & Chief Financial Officer
(Principal Financial Officer)

Certification Pursuant to 18 U.S.C. Section 1350,
as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
by the Principal Executive Officer

In connection with the Quarterly Report of the Federal Home Loan Bank of Chicago (the "Bank") on Form 10-Q/A for the period ended June 30, 2009 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Matthew R. Feldman, President and Chief Executive Officer, certify to my knowledge, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350), that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: February 16, 2010

By: /s/ Matthew R. Feldman
Name: Matthew R. Feldman
Title: President and Chief Executive Officer
(Principal Executive Officer)

A signed original of this written statement has been provided to the Bank and will be retained by the Bank and furnished to the Securities and Exchange Commission or its staff upon request.

**Certification Pursuant to 18 U.S.C. Section 1350,
as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
by the Principal Financial Officer**

In connection with the Quarterly Report of the Federal Home Loan Bank of Chicago (the "Bank") on Form 10-Q/A for the period ended June 30, 2009 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Roger D. Lundstrom, Executive Vice President, Financial Information and Chief Financial Officer certify to my knowledge, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350), that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: February 16, 2010

By: /s/ Roger D. Lundstrom
Name: Roger D. Lundstrom
Title: Executive Vice President, Financial
Information and Chief Financial Officer
(Principal Financial Officer)

A signed original of this written statement has been provided to the Bank and will be retained by the Bank and furnished to the Securities and Exchange Commission or its staff upon request.