

# Quarterly Report

FIRST QUARTER 2012



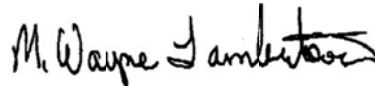
# ***FIRST QUARTER 2012***

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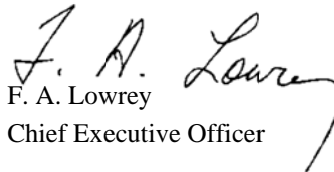
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### **CERTIFICATION**

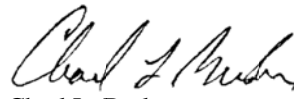
The undersigned certify that we have reviewed the March 31, 2012 quarterly report of AgFirst Farm Credit Bank, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



M. Wayne Lambertson  
Chairman of the Board



F. A. Lowrey  
Chief Executive Officer



Charl L. Butler  
Chief Financial Officer

May 9, 2012

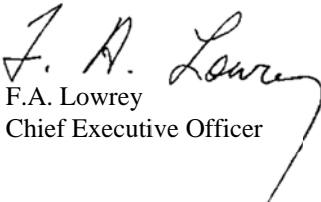
## Report on Internal Control Over Financial Reporting


The Bank's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Bank's Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by, or under the supervision of the Bank's principal executives and principal financial officers, or persons performing similar functions, and effected by its Board of Directors, management and other personnel. This process provides reasonable assurance regarding the reliability of financial reporting information and the preparation of the Financial Statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Bank, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial information in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Bank, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Bank's assets that could have a material effect on its Financial Statements.

The Bank's management has completed an assessment of the effectiveness of internal control over financial reporting as of March 31, 2012. In making the assessment, management used the framework in *Internal Control — Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Bank concluded that as of March 31, 2012, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Bank determined that there were no material weaknesses in the internal control over financial reporting as of March 31, 2012.

  
F.A. Lowrey  
Chief Executive Officer

  
Charl L. Butler  
Chief Financial Officer

May 9, 2012

# Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion reviews the financial condition and results of operations of AgFirst Farm Credit Bank (AgFirst or Bank) as of and for the three month period ended March 31, 2012. These comments should be read in conjunction with the accompanying financial statements, the Notes to the Financial Statements, and the 2011 Annual Report of AgFirst Farm Credit Bank. AgFirst and its related associations (Associations or District Associations) are collectively referred to as the District. The accompanying financial statements were prepared under the oversight of the Audit Committee of the AgFirst Board of Directors.

Key ratios and data reported below, and in the accompanying financial statements, address the financial performance of AgFirst. However, the three months results of operations may not be indicative of an entire year due to the seasonal nature of a portion of AgFirst's business.

## FORWARD-LOOKING INFORMATION

Certain sections of this quarterly report contain forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," "will," or other variations of these terms are intended to identify the forward-looking statements. These statements are based on assumptions and analyses made in light of experience and other historical trends, current conditions, and expected future developments. However, actual results and developments may differ materially from AgFirst's expectations and predictions due to a number of risks and uncertainties, many of which are beyond AgFirst's control. These risks and uncertainties include, but are not limited to:

- political, legal, regulatory, financial markets, and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural infrastructure, international, and farm-related business sectors, as well as in the general economy;
- weather-related, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income of District borrowers;
- changes in United States government support of the agricultural industry and the Farm Credit System (System) as a government-sponsored enterprise (GSE), as well as investor and rating agency reactions to events involving other GSEs and other financial institutions; and
- actions taken by the Federal Reserve System in implementing monetary and fiscal policy, as well as other policies and actions of the Federal government that impact the financial services industry and the debt markets.

## FINANCIAL CONDITION

### Loan Portfolio

AgFirst's loan portfolio consists primarily of direct loans to District Associations (Direct Notes), loan participations/syndications purchased, Correspondent Lending loans (primarily first lien rural residential mortgages), and loans to Other Financing Institutions (OFIs) as shown below:

AgFirst Loan Portfolio (dollars in thousands)	March 31, 2012		December 31, 2011		March 31, 2011	
Direct Notes	\$ 13,471,353	68.99%	\$ 14,094,384	69.94%	\$ 14,201,019	69.62%
Participations/Syndications purchased, net	3,855,860	19.75	3,880,559	19.25	4,153,088	20.36
Correspondent Lending	2,191,632	11.22	2,171,873	10.78	2,035,890	9.98
Loans to OFIs	6,900	0.04	5,250	0.03	8,000	0.04
Total	\$ 19,525,745	100.00%	\$ 20,152,066	100.00%	\$ 20,397,997	100.00%

Total loans outstanding were \$19.5 billion at March 31, 2012, a decrease of \$626.3 million, or 3.11 percent, compared to total loans outstanding at December 31, 2011. Loan volume continues to be impacted by the slow recovery of the general economy, which has affected the Bank's and District Associations' current and prospective customers in a number of ways, including fluctuating demand and prices for certain agricultural products and lower value for real estate and other investment holdings of some borrowers. These conditions have been detrimental to the general sentiment and financial capacity of some of the District's customers. As a result, customers have taken a deliberate approach to expansion plans, in order to preserve their investment and working capital. Each of these factors has contributed to the lower loan demand throughout the District. Future loan demand is very difficult to predict; however, it is expected to remain weak for the remainder of 2012.

### Credit Quality

Credit quality also has been challenged by the slow recovery after a period of prolonged weakness in the economy. Though problem asset levels remained elevated, credit quality has recently stabilized with modest improvement as can be seen in the following table:

AgFirst Total Loan Portfolio Credit Quality as of:			
Classification	March 31, 2012	December 31, 2011	March 31, 2011
Acceptable	87.35%	87.09%	85.55%
OAEM *	9.63%	9.79%	11.20%
Substandard	3.02%	3.12%	3.25%
Doubtful	0.00%	0.00%	0.00%

*\*Other Assets Especially Mentioned*

Certain commodity groups continued to be adversely affected in the current economic cycle. Housing-related industries, such as building products, timber, sawmills, landscape nurseries, and sod operations remained stressed. Also, many customers in the District rely on off-farm income, which has been negatively impacted by the relatively weak general economy. Improvement in these segments is dependent on sustained improvement in such general economic factors as employment levels and housing market activity.

Loan portfolio credit quality has been negatively impacted by lower real estate values in certain geographic areas within the Bank's chartered territory, particularly in Florida. Other areas of the District experienced a less severe reduction, although sales continue to be slow throughout the District. While increasing real estate values are not being observed in the stressed geographic areas, most distressed property sales are occurring at or near appraised values, indicating that reductions in values have slowed. Production farm land has maintained its value better than residential and investment real estate.

The beef and swine industries have experienced a cycle of profitable results. Profitability was primarily achieved through reduction of supply, which led to higher prices. Higher grain and energy costs were offset by higher meat prices for both beef and swine producers.

Many chicken integrators recently experienced losses and cash flow problems due to higher input prices and oversupply, but are currently profitable. Margins for dairy farmers have narrowed, but, in general, remain sufficient to service debt. Volatility of grain prices is a primary concern to the meat and dairy sectors.

Other major segments of the District loan portfolio continued to perform well, including sugar, citrus, cotton, and row crops. High commodity prices for grains were very beneficial to row crop farmers.

Slow economic growth will have an impact on credit quality for some time. Although credit quality is generally stabilizing, it will take time to fully resolve some problem assets due to their dependency on general economic conditions including employment, the housing market, and real estate values.

*Direct Notes*

AgFirst's primary business is to provide funding, operational support, and technology services to District Associations. Each Association, in addition to the Bank, is a federally chartered instrumentality of the United States and is regulated by the Farm Credit Administration (FCA). AgFirst has a revolving line of credit, referred to as a Direct Note, in place with each of the District Associations. Each of the Associations funds its lending and general corporate activities primarily by borrowing under its Direct Note. Lending terms are specified in a separate General Financing Agreement (GFA) between AgFirst and each Association, including the subsidiaries of the Associations. Each GFA contains minimum borrowing base margin, capital, and earnings requirements that must be maintained by the Association.

At March 31, 2012, the total principal amount outstanding under Direct Notes was \$13.471 billion, a decrease of \$623.0 million, or 4.42 percent, compared to December 31, 2011. Borrower payment seasonality and Bank patronage payments were the primary reasons for the decline in Direct Note volume from December to March.

Credit quality statistics for the Direct Note portfolio are shown in the following chart:

Direct Note Credit Quality as of:			
Classification	March 31, 2012	December 31, 2011	March 31, 2011
Acceptable	85.68%	85.65%	84.27%
OAEM *	11.41%	11.38%	13.46%
Substandard	2.91%	2.97%	2.27%
Doubtful	0.00%	0.00%	0.00%

*\*Other Assets Especially Mentioned*

As of March 31, 2012, fourteen of the twenty District Associations' Direct Notes, representing 85.68 percent of the Direct Note portfolio, were classified acceptable. Four of the remaining Direct Notes, representing 11.41 percent of the portfolio, were classified as Other Assets Especially Mentioned (OAEM) and two of the Direct Notes, representing 2.91 percent of the portfolio, were classified as substandard (adverse).

None of the Direct Notes, including those classified as substandard (adverse), are considered impaired. All assets of the various Associations are pledged as collateral for their respective Direct Notes. The risk funds of an Association, including both capital and the allowance for loan losses, protect the interest of the Bank should a Direct Note default. In the opinion of management, all Association Direct Notes are adequately collateralized. Presently, collections of the full amounts due are expected in accordance with the contractual terms of the debt arrangements.

As of March 31, 2012, six Associations were in violation of covenants under the GFA. The Bank allowed these Associations to operate under special credit agreements (SCAs).

At March 31, 2012, FCA had entered into written supervisory agreements with three District Associations with combined assets of approximately \$850.0 million. Those agreements require the District Associations to take corrective actions with respect to certain areas of their operations, including capital, portfolio management, and asset quality. These enforcement actions are not expected to have a significant impact on the Bank's or District's financial condition or results of operations.

*Participations/Syndications*

AgFirst has an active Capital Markets Unit that purchases and sells loan participations and syndications. As of March 31, 2012, the participations/syndications portfolio totaled \$3.856 billion, a decrease of \$24.7 million, or 0.64 percent, from December 31, 2011. As with the Direct Notes, borrower demand is anticipated to remain moderate in 2012.

AgFirst employs a number of management techniques to limit credit risk, including underwriting standards, limits on the amounts of loans purchased from a single originator, and maximum hold positions to a single borrower and commodity. Although the participations/syndications portfolio is comprised of a small number of relatively large loans, it is diversified both geographically and on a commodity basis. Concentration risk throughout the portfolio is mitigated through established maximum hold positions to a single borrower and to a single commodity. Management makes adjustments to credit policy and underwriting standards when appropriate as a part of the ongoing risk management process.

Credit quality statistics for the participations/syndications portfolio are shown in the following chart:

<b>Participations/Syndications Credit Quality as of:</b>			
<b>Classification</b>	<b>March 31, 2012</b>	<b>December 31, 2011</b>	<b>March 31, 2011</b>
Acceptable	85.96%	85.20%	82.98%
OAEM *	8.91%	9.38%	8.87%
Substandard	5.13%	5.42%	8.15%
Doubtful	0.00%	0.00%	0.00%

*\*Other Assets Especially Mentioned*

*Correspondent Lending*

AgFirst also maintains a Correspondent Lending Unit, which consists primarily of first lien residential mortgages. As of March 31, 2012, the correspondent lending portfolio totaled \$2.192 billion. From December 31, 2011 to March 31, 2012, this portfolio increased \$19.8 million, or 0.91 percent.

Essentially all loans in the correspondent lending portfolio are guaranteed by the Federal National Mortgage Association (Fannie Mae) and/or the Federal Agricultural Mortgage Corporation (Farmer Mac), thereby limiting credit risk to AgFirst. The guarantees are in the form of Long-Term Standby Commitments to Purchase, which give AgFirst the right to deliver delinquent loans to the guarantor at par. At March 31, 2012, 99.98 percent of the correspondent lending portfolio was classified as Acceptable and 0.02 percent was classified as OAEM.

*Nonaccrual Loans*

Nonaccrual loans represent all loans for which there is a reasonable doubt as to the collection of principal and/or interest under the contractual terms of the loan. Nonaccrual loans for the Bank at March 31, 2012 were \$72.4 million compared to \$85.2 million at December 31, 2011. Nonaccrual loans decreased \$12.8 million during the first quarter of 2012, due primarily to repayments of \$20.6 million, transfers to other property owned of \$1.5 million, and charge-offs of uncollectible balances of \$981 thousand (composed primarily of charge-offs in the cattle and forestry segments). Offsetting these decreases were \$7.1 million of loan balances transferred to nonaccrual status. The ten largest nonaccrual borrower relationships accounted for 58.45 percent of the total nonaccrual balance. At March 31, 2012, total nonaccrual loans were primarily classified in the forestry (34.32 percent of the total), processing (29.00 percent), other real estate (8.94 percent), and cattle (8.38 percent) segments. Some of these nonaccrual loans are secured by real estate, which has been negatively impacted by the current economic environment as discussed previously. Nonaccrual loans were 0.37 percent of total loans outstanding at March 31, 2012.

### *Troubled Debt Restructurings*

A troubled debt restructuring occurs when a borrower is experiencing financial difficulties and a concession is granted to the borrower that the Bank would not otherwise consider. Concessions are granted to borrowers based on either an assessment of the borrower's ability to return to financial viability or a court order. The concessions can be in the form of a modification of terms, rates, or amounts owed. Acceptance of other assets and/or equity as payment may also be considered a concession. The type of alternative financing granted is chosen in order to minimize the loss incurred by the Bank. Troubled debt restructurings totaled \$61.2 million at March 31, 2012, comprised of \$34.4 million of accruing restructured loans and \$26.8 million of nonaccruing restructured loans. Restructured loans were primarily in the swine (30.97 percent of the total), forestry (24.82 percent), nursery/greenhouse (18.50 percent), processing (13.95 percent), and other real estate (7.66 percent) segments.

### *Other Property Owned*

Other property owned (OPO) consists of assets once pledged as loan collateral that were acquired through foreclosure or deeded to the Bank (or a lender group) in satisfaction of secured loans. OPO may be comprised of real estate, equipment, and equity interests in companies or partnerships. OPO decreased \$3.8 million and totaled \$40.4 million at March 31, 2012. The decrease was due to OPO disposals of \$2.5 million and write-downs of \$3.2 million. Disposals primarily included two land holdings totaling \$2.0 million. Write-downs were comprised primarily of two land holdings totaling \$2.4 million. Offsetting this decrease was property transferred to OPO of \$1.9 million, which was comprised primarily of two land holdings totaling \$1.0 million. The largest OPO holding at March 31, 2012, which was a parcel of land, was \$8.9 million (22.15 percent of the total).

### *Allowance for Loan Losses*

The Bank maintains an allowance for loan losses at a level management considers adequate to provide for probable and estimable credit losses within the loan portfolio as of each reported balance sheet date. The allowance for loan losses was \$28.0 million at March 31, 2012, as compared with \$27.7 million at December 31, 2011. The \$331 thousand increase during the three months ended March 31, 2012 was due primarily to recoveries of \$4.0 million, offset by a reversal of the allowance for loan losses of \$2.7 million and net loan charge-offs of \$981 thousand as their uncollectability became more measurable and apparent during the three month period. Charge-offs were related primarily to the cattle (\$368 thousand) and forestry (\$264 thousand) segments. The allowance at March 31, 2012 included specific reserves of \$9.5 million (33.90 percent of the total) and general reserves of \$18.5 million (66.10 percent). None of the allowance relates to the Direct Note portfolio. The total allowance at March 31, 2012 was comprised primarily of reserves for the processing, primarily chicken (22.78 percent), forestry (20.96 percent), non-farm income (13.13 percent), and nursery/greenhouse (9.91 percent) segments. Declining real estate values impacted charge-offs and reserves in most of these loan segments. See Note 3, *Loans and Allowance for Loan Losses*, in the Notes to the Financial Statements for further information. See *Provision for Loan Losses* section below for details regarding increases to the allowance from provision expense.

### *Liquidity and Funding Sources*

One of AgFirst's primary responsibilities is to maintain sufficient liquidity to fund the lending operations of the District Associations, in addition to its own needs. Along with normal cash flows associated with lending operations, AgFirst has two primary sources of liquidity: the capacity to issue Systemwide Debt Securities through the Federal Farm Credit Banks Funding Corporation; and cash and investments, including its available-for-sale portfolio. The Bank also maintains several lines of credit with commercial banks, as well as securities repurchase agreement facilities.

The U.S. government does not guarantee, directly or indirectly, Systemwide Debt Securities. However, the Farm Credit System, as a GSE, has benefited from broad access to the domestic and global capital markets. This access has provided the System with a dependable source of competitively priced debt which is critical for supporting the System's mission of providing credit to agriculture and rural America. However, concerns regarding the government's borrowing limit and budget imbalances have further highlighted the risks to the System relating to the U.S. fiscal situation. These risks include the implied link between the credit rating of the System and the U.S. Government given the System's status as a GSE.



AgFirst's primary source of liquidity comes from its ability to issue Systemwide Debt Securities, which are the general unsecured joint and several obligations of the System banks. AgFirst continually raises funds to support its mission to provide credit and related services to the rural and agricultural sectors, to repay maturing Systemwide Debt Securities, and to meet other obligations. As a GSE, AgFirst has access to the nation's and world's debt and capital markets. This access has provided AgFirst with a dependable source of competitively priced debt that is critical to support its mission. In August 2011, Standard & Poor's Ratings Services lowered its long-term sovereign credit rating for the U.S. to AA+ from AAA, and affirmed the A-1+ short-term rating. Their outlook on the long-term rating of the U.S. remained negative. Concurrently with such actions, Standard & Poor's Ratings Services lowered the long-term debt rating for the System to AA+ from AAA; however, the A-1+ short-term rating was affirmed, while the outlook on the long-term debt rating of the System remained negative. Also in August 2011, Moody's Investors Service and Fitch Ratings affirmed the Aaa and AAA ratings of the U.S. and affirmed the System's Aaa and AAA long-term debt rating and short-term debt as P-1 and F-1. However, Moody's Investors Service did change the ratings outlook of the U.S. and the System to negative. Similarly, in November 2011, Fitch Ratings, Inc. changed its outlook of the U.S. and the System from "stable" to "negative."

These changes to the System's credit ratings and any future negative changes in the System's credit ratings and/or outlook could increase borrowing costs, limit access to the debt capital markets and trigger additional collateral requirements under derivative contracts and other borrowing arrangements. Any of these changes may also reduce earnings and have a material adverse effect on liquidity, ability to conduct normal business operations, and financial condition and results of operations. However, AgFirst anticipates continued access to funding necessary to support the District's and Bank's needs. At March 31, 2012, AgFirst had \$25.766 billion in total debt outstanding compared to \$27.086 billion at December 31, 2011. Total interest-bearing liabilities decreased primarily due to the decrease in loan volume and liquidity investments as discussed in this report which reduced funding requirements.

At March 31, 2012, AgFirst maintained a \$150.0 million unsecured committed line of credit facility from its primary commercial depository bank. The line of credit is tied to AgFirst's master cash management clearing account. The Bank has securities repurchase agreement facilities with three commercial banks that range in terms from overnight to nine months. Also, AgFirst has overnight Fed Funds lines of credit with two commercial banks.

Cash and cash equivalents, which decreased \$715.0 million from December 31, 2011 to a total of \$586.6 million at March 31, 2012, consist primarily of cash on deposit and money market securities that are short term in nature (from overnight maturities to maturities that range up to 90 days). Money market securities must carry one of the two highest short-term ratings as designated from a Nationally Recognized Statistical Rating Organization (NRSRO). The decrease in cash and cash equivalents was due primarily to the lower amount of cash needed to maintain 15 days of liquidity coverage on maturing debt at March 31, 2012 compared to December 31, 2011.

Investment securities totaled \$7.669 billion, or 27.29 percent of total assets at March 31, 2012, compared to \$7.780 billion, or 26.30 percent, as of December 31, 2011. Investment securities decreased \$111.0 million (1.43 percent), compared to December 31, 2011, as management maintained the investment securities portfolio size generally proportionate with that of the loan portfolio and within regulatory and policy guidelines.

As of March 31, 2012, AgFirst exceeded all applicable regulatory liquidity requirements. FCA regulations require a liquidity policy that establishes a minimum "coverage" level of 90 days. "Coverage" is defined as the number of days that maturing debt could be funded with eligible available-for-sale investments and cash and cash equivalents maintained by the Bank. At March 31, 2012, AgFirst's coverage was 234 days, compared to 205 days at December 31, 2011. At March 31, 2012, the Bank's cash and cash equivalents position provided 19 days coverage and investment securities fully backed by the U.S. government provided an additional 215 days of coverage. Cash provided by the Bank's operating activities, primarily generated from net interest income in excess of operating expenses and maturities in the loan portfolio, is an additional source of liquidity for the Bank that is not reflected in the coverage calculation of 234 days.

Investment securities classified as being available-for-sale totaled \$6.874 billion at March 31, 2012. Available-for-sale investments at March 31, 2012 included \$4.962 billion in Government National Mortgage Association (GNMA) securities backed by the full faith and credit of the U.S. Government, \$1.650 billion in Agency mortgage backed securities, \$233.4 million in non-agency collateralized mortgage obligations (CMOs), and \$28.9 million in asset-backed securities. Since the majority of the portfolio is invested in agency securities, the portfolio is highly liquid and potential credit loss exposure is limited.

AgFirst also maintains a portfolio of investments that are not held for liquidity purposes and are accounted for as a held-to-maturity portfolio. These investments are authorized by FCA Regulations that allow investments in Farmer Mac securities and also in specific investments approved by the FCA as Mission Related Investments. The vast majority of this portfolio is comprised of Mission Related Investments for a program to purchase Rural Housing Mortgage-Backed Securities, which when combined with eligible rural home loans, must not exceed 15.00 percent of total outstanding loans. Investment securities classified as being held-to-maturity totaled \$795.6 million at March 31, 2012.

The FCA considers non-agency asset-backed or mortgage-backed investment securities ineligible if they fall below the top category (AAA/Aaa) credit rating by the NRSROs. The Bank must obtain specific approval from the FCA to continue to hold an ineligible security. For each of these investment securities in the Bank's portfolio at March 31, 2012 rated below AAA/Aaa (total fair value of \$251.7 million and amortized cost of \$302.0 million), the Bank has developed and submitted plans for approval by the FCA that permit the Bank to continue to hold the securities. The FCA has approved, with conditions, the Bank's plans for all but seven investments that have recently become ineligible. The Bank has submitted a plan to hold four of these recently ineligible securities and is in the process of submitting a plan to obtain approval from the FCA to hold the remaining three investments. Management is of the opinion that holding these securities will result in a higher return for the Bank than liquidating them. Based on the Bank's analysis, no other-than-temporary credit related impairment was recognized in 2011 or 2012 on these recently ineligible securities.

For purposes of calculating the risk adjusted assets amount used in the permanent capital, total surplus, and core surplus regulatory ratios, certain Bank ineligible securities are risk weighted between 50 percent and 200 percent instead of 20 percent which is applicable to eligible non-agency securities. These ineligible securities had a fair value of \$110.4 million and amortized cost of \$133.9 million at March 31, 2012. Other ineligible securities must be deducted completely from both capital and risk adjusted assets, based on the extent of their below investment grade rating from NRSROs. These securities had a fair value of \$66.8 million and amortized cost of \$79.5 million at March 31, 2012. The fair value and amortized cost of ineligible non-agency reperformer CMO securities covered by Federal Housing Administration insurance and therefore risk weighted at the standard 20 percent, was \$74.6 million and \$88.5 million, respectively, at March 31, 2012. See the Capital Resources section below for further discussion of the regulatory ratios. In addition, all ineligible investments, except non-agency reperformer CMOs which meet certain conditions, are excluded from liquidity coverage as defined above.

Net unrealized gains related to the available-for-sale securities were \$146.0 million at March 31, 2012, compared to \$132.8 million at December 31, 2011. These net unrealized gains are reflected in Accumulated Other Comprehensive Income (AOCI) in the Financial Statements. The net unrealized gains stem from normal market factors such as the current interest rate environment.

The Bank performs periodic credit reviews, including other-than-temporary impairment analyses, on its entire investment securities portfolio. Additional analysis for each security not rated in the top category by the NRSROs is performed using a cash flow model with key assumptions and performance factors which may include credit default rate, prepayment rate, and loss severity. The objective is to quantify future possible loss of principal or interest due on each identified security. The credit enhancements specific to the individual security are considered as appropriate, and may include monoline credit insurance, subordination, over-collateralization, and excess interest spread. Asset-backed securities covered by insurers are analyzed with insurance and without, to quantify the extent of reliance on their guarantees. Based on the results of all analyses, the Bank recognized other-than-temporary credit related impairment of \$750 thousand on asset-backed securities and non-agency CMOs in its portfolio for the quarter ended March 31, 2012, which was included in Net Other-Than-Temporary Impairment Losses on Investments in the Statements of Income. Credit loss is defined as the shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis. Payment shortfalls, net of insurance recoveries, on asset-backed securities have totaled only \$17.6 million life to date (\$1.2 million in 2012), compared to credit related impairment charges life to date of \$39.5 million (none in 2012). Credit related impairment charges on non-agency CMOs have totaled \$15.6 million life to date (\$750 thousand in 2012). Payment shortfalls on non-agency CMOs totaled \$583 thousand life to date (\$272 thousand in 2012). See Note 2, *Investment Securities*, in the Notes to the Financial Statements for further information.

The Bank considers both a price, or “mark,” provided by a third party pricing service and a value determined using the results of a modeling process for purposes of determining the fair values of securities in the asset-backed and non-agency CMO portfolios, as well as the resulting unrealized gain/loss impact through AOCI. The Bank reviews and periodically discusses with the third party pricing service and valuation experts the assumptions used in their pricing models for the asset-backed and non-agency CMO securities impacted by inactive trading or distressed sales. This process ensures that, when relevant observable inputs are not available, the fair value reported for each security reflects the price expected to be received in an orderly transaction that is not a forced liquidation or distressed sale at the measurement date. The modeling process was factored into the pricing for the asset-backed and non-agency CMO security portfolios.

### *Capital Resources*

Total shareholders’ equity increased \$53.3 million (2.48 percent) from December 31, 2011 to a total of \$2.203 billion at March 31, 2012. This increase is primarily attributed to 2012 unallocated retained earnings from net income of \$123.0 million, increases of \$13.0 million in net unrealized gains during 2012 on investments available-for-sale, and a change in the fair value of derivatives of \$655 thousand. Offsetting the increases were stock and participation certificate net retirements of \$3.2 million and the redemption of preferred stock referenced below.

During the first quarter of 2012, the Bank repurchased, through privately negotiated transactions, and cancelled Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock with a par value of \$110.6 million. The effect of the repurchases on shareholders’ equity was to reduce preferred stock outstanding by \$110.6 million and record \$31.9 million of additional paid-in-capital. Subsequent to quarter-end, the Bank repurchased and cancelled additional shares of Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock with a par value of \$8.0 million. The effect of this transaction was to reduce preferred stock outstanding by \$8.0 million and increase additional paid-in-capital by \$2.2 million.

### *Regulatory Ratios*

AgFirst’s regulatory ratios are shown in the following table:

	<b>Regulatory Minimum</b>	<b>3/31/12</b>	<b>12/31/11</b>	<b>3/31/11</b>
Permanent Capital Ratio	7.00%	21.60%	24.27%	20.78%
Total Surplus Ratio	7.00%	21.57%	24.24%	20.75%
Core Surplus Ratio	3.50%	17.74%	17.08%	13.29%
Net Collateral Ratio*	103.00%	107.06%	106.49%	107.31%

\*The regulatory minimum net collateral ratio was 104.00% previous to the redemption of the Mandatorily Redeemable Cumulative Preferred Stock on December 15, 2011.

FCA sets minimum regulatory capital requirements for System banks and associations. Capital adequacy is evaluated using a number of regulatory ratios. According to the FCA regulations, each institution’s permanent capital ratio is calculated by dividing permanent capital by a risk-adjusted asset base. Risk-adjusted assets refer to the total dollar amount of the institution’s assets adjusted by an appropriate credit conversion factor as defined by regulation. Generally, higher credit conversion factors are applied to assets with more inherent risk.

For all periods presented, AgFirst exceeded minimum regulatory standards for all of the ratios. The Bank’s permanent capital and total surplus ratios decreased at March 31, 2012 as compared to December 31, 2011, primarily as a result of the reduction in preferred stock discussed above.

## RESULTS OF OPERATIONS

Net income for the three months ended March 31, 2012 was \$123.0 million, compared to \$102.9 million for the three months ended March 31, 2011, an increase of \$20.1 million, or 19.53 percent.

### Key results of operations comparisons

	Annualized for the three months ended March 31, 2012	For the year ended December 31, 2011	Annualized for the three months ended March 31, 2011
Return on average assets	1.73%	1.29%	1.40%
Return on average shareholders' equity	22.60%	18.14%	21.29%
Net interest income as a percentage of average earning assets	2.29%	2.08%	2.03%
Net (charge-offs) recoveries to average loans	0.063%	(0.329)%	(0.011)%

### Net Interest Income

Net interest income for the three months ended March 31, 2012 was \$156.2 million compared to \$144.2 million for the same period of 2011, an increase of \$12.0 million or 8.31 percent. The net interest margin was 2.29 percent in the current year three month period, an improvement of 26 basis points over the same period of 2011. Spreads improved for several reasons, but primarily resulted from called debt being replaced by new debt issued at lower interest rates, decreasing funding costs. Over time, as interest rates change and as assets prepay or reprice in a manner more consistent with historical experience, the positive impact on the net interest margin that the Bank has experienced over the last several years from calling debt will likely diminish. Net interest income resulting from the change in balance sheet volume decreased slightly due to lower loan volume as previously discussed.

The following table illustrates the changes in net interest income:

(dollars in thousands)	For the three months ended March 31, 2012 vs. March 31, 2011		
	Increase (decrease) due to changes in:		
	Volume	Rate	Total
Interest Income:			
Loans	\$ (7,615)	\$ (4,651)	\$ (12,266)
Investments & Cash Equivalents	(2,236)	1,895	(341)
Total Interest Income	\$ (9,851)	\$ (2,756)	\$ (12,607)
Interest Expense:			
Interest-Bearing Liabilities	\$ (128)	\$ (24,469)	\$ (24,597)
Changes in Net Interest Income	\$ (9,723)	\$ 21,713	\$ 11,990

### Provision for Loan Losses

AgFirst measures risks inherent in its loan portfolio on an ongoing basis and, as necessary, recognizes provision for loan loss expense so that appropriate reserves for loan losses are maintained. Provision was a net reversal of loan loss expense for the three months ended March 31, 2012 which totaled \$2.7 million and related primarily to borrowers in the forestry segment (81.46 percent of total). For the same period in 2011, provision for loan losses was \$10.9 million. For the three months ended March 31, 2012, provision expense included expense of \$2.3 million and reversals of \$4.9 million related to specific reserves and a reversal of \$127 thousand related to general reserves. Reversals of specific provisions resulted primarily from \$3.2 million in reversals for two borrowers in the forestry segment. See Note 3, *Loans and Allowance for Loan Losses*, in the Notes to the Financial Statements for further information.

*Noninterest Income*

The following table illustrates the changes in noninterest income:

Change in Noninterest Income	For the three months ended March 31,		
	2012	2011	Increase/ (Decrease)
<i>(dollars in thousands)</i>			
Loan fees	\$ 2,364	\$ 2,854	\$ (490)
Gains (losses) from other property owned, net	(3,523)	(5,780)	2,257
Net impairment losses on investments	(750)	(4,458)	3,708
Gains (losses) on sale of rural home loans, net	—	(86)	86
Patronage refunds from other Farm Credit Institutions	46	134	(88)
Other noninterest income	3,034	1,537	1,497
Total noninterest income	\$ 1,171	\$ (5,799)	\$ 6,970

Noninterest income for the three months ended March 31, 2012 increased \$7.0 million (120.19 percent) compared to the corresponding period in 2011. The increases for the three month period were due primarily to reduced losses from other property owned and impairment on investments.

The decrease in loan fees of 17.17 percent for the three month period ended March 31, 2012 was due primarily to a decrease in commitment fees related to participation loans.

Net losses from other property owned for the three months ended March 31, 2012 decreased \$2.3 million primarily due to lower writedowns in 2012 as real estate values began to stabilize. See *Other Property Owned* section above.

Net impairment losses on investments decreased \$3.7 million for the three months ended March 31, 2012 as compared to the same period in 2011. See discussion of 2012 credit related other-than-temporary impairment in the *Liquidity and Funding Sources* section above.

Other noninterest income increased \$1.5 million for the three months ended March 31, 2012 primarily due to a \$942 thousand insurance recovery, \$517 thousand reversal of reserve for unfunded commitments (as commitments are funded, the reserve is included in the allowance for loan losses), and \$251 thousand in relation to performance of investments which fund the non-qualified pension plans.

*Noninterest Expense*

The following table illustrates the changes in noninterest expense:

Change in Noninterest Expense	For the three months ended March 31,		
	2012	2011	Increase/ (Decrease)
<i>(dollars in thousands)</i>			
Salaries and employee benefits	\$ 11,795	\$ 11,068	\$ 727
Occupancy and equipment	3,736	3,452	284
Insurance Fund premiums	1,070	1,364	(294)
Other operating expenses	5,478	4,986	492
Called debt expense	12,745	1,443	11,302
Correspondent lending servicing expense	2,303	2,265	38
Other noninterest expense	—	70	(70)
Total noninterest expense	\$ 37,127	\$ 24,648	\$ 12,479

Noninterest expense for the three months ended March 31, 2012 was \$37.1 million, which reflected an increase of \$12.5 million (50.63 percent) compared to the corresponding period in 2011. The increase for the three month period was due primarily to the increase in called debt expense.

Concession or debt issuance expense is amortized over the life of the underlying debt security. When debt securities are called prior to maturity, any unamortized concession is expensed. Called debt expense increased \$11.3 million (783.23 percent) for the three month period. Call options were exercised on bonds totaling \$8.174 billion for the three months ended March 31, 2012 compared to \$2.546 billion for the same period of 2011. The called debt expense is more than offset by interest expense savings realized as called debt is replaced by new debt issued at a lower rate of interest. Over time, the favorable effect on net interest income is diminished as earning assets reprice downward.

The increase in salaries and employee benefits of 6.57 percent for the three month period ended March 31, 2012 was due primarily to normal salary administration, increased employee benefit costs, and an increase in number of employees at March 31, 2012 compared to March 31, 2011.

Occupancy and equipment expense for the three months ended March 31, 2012 increased 8.23 percent. This increase was due primarily to an increase in software expense for various maintenance agreements and database management.

Farm Credit System Insurance Corporation (FCSIC) premiums decreased minimally for the three month period. The 2012 base annual premium rate is 5 basis points compared to the 2011 base annual premium rate of 6 basis points.

Other operating expenses are comprised of numerous and varied expenses, none of which individually had a significant increase in the three months ended March 31, 2012 compared to the same period in 2011.

Correspondent lending service expense increased 1.68 percent for the three month period ended March 31, 2012. These increases were related primarily to increased agency guarantee fees resulting from higher volume in the correspondent lending portfolio.

Other noninterest expense consists of amortization of mandatorily redeemable preferred stock issuance costs, which fully amortized in May 2011.

## **DISTRICT MERGER ACTIVITY**

Please refer to Note 10, *District Merger Activity*, in the Notes to the Financial Statements for information regarding merger activity in the District.

## **REGULATORY MATTERS**

For the three months ended March 31, 2012, the FCA took no enforcement action against the Bank.

## **RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

Please refer to Note 1, *Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements*, in the Notes to the Financial Statements, and the 2011 Annual Report of AgFirst Farm Credit Bank for recently issued accounting pronouncements.

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**NOTE:** Shareholder investment in a District Association is materially affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 2832, or writing Susanne Caughman, Reporting Manager, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Combined information concerning AgFirst Farm Credit Bank and District Associations can also be obtained at the Bank's website, [www.agfirst.com](http://www.agfirst.com). AgFirst prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no quarterly report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

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# Balance Sheets

<i>(dollars in thousands)</i>	<b>March 31, 2012</b> <i>(unaudited)</i>	<b>December 31, 2011</b> <i>(audited)</i>
<b>Assets</b>		
Cash and cash equivalents	\$ 586,610	\$ 1,301,569
Investment securities:		
Available for sale (amortized cost of \$6,727,712 and \$6,792,584 respectively)	6,873,700	6,925,410
Held to maturity (fair value of \$862,251 and \$928,053 respectively)	795,612	854,862
Total investment securities	7,669,312	7,780,272
Loans	19,525,745	20,152,066
Less: allowance for loan losses	28,045	27,714
Net loans	19,497,700	20,124,352
Accrued interest receivable	79,532	78,906
Investments in other Farm Credit System institutions	65,920	65,964
Premises and equipment, net	13,109	13,706
Other property owned	40,383	44,157
Due from associations	2,974	17,318
Other assets	149,520	151,262
Total assets	\$ 28,105,060	\$ 29,577,506
<b>Liabilities</b>		
Bonds and notes	\$ 25,765,545	\$ 27,086,148
Accrued interest and dividends payable	37,194	42,418
Patronage distribution payable	—	180,726
Other liabilities	99,763	118,944
Total liabilities	25,902,502	27,428,236
Commitments and contingencies (Note 5)		
<b>Shareholders' Equity</b>		
Perpetual preferred stock (Note 8)	289,450	400,000
Capital stock and participation certificates	402,536	405,767
Additional paid-in-capital (Note 8)	31,860	—
Retained earnings		
Allocated	858	858
Unallocated	1,340,155	1,218,648
Accumulated other comprehensive income (loss)	137,699	123,997
Total shareholders' equity	2,202,558	2,149,270
Total liabilities and equity	\$ 28,105,060	\$ 29,577,506

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

# Statements of Income

(unaudited)

<i>(dollars in thousands)</i>	For the three months ended March 31,	
	2012	2011
<b>Interest Income</b>		
Investment securities and other	\$ 48,630	\$ 48,971
Loans	163,827	176,093
Total interest income	212,457	225,064
<b>Interest Expense</b>		
Net interest income	156,238	144,248
Provision for (reversal of allowance for) loan losses	(2,721)	10,896
Net interest income after provision for (reversal of allowance for) loan losses	158,959	133,352
<b>Noninterest Income</b>		
Loan fees	2,364	2,854
Gains (losses) from other property owned, net	(3,523)	(5,780)
Total other-than-temporary impairment losses on investments (Note 2)	(839)	(2,477)
Portion of loss recognized in other comprehensive income (loss) (Note 2)	89	(1,981)
Net other-than-temporary impairment losses on investments	(750)	(4,458)
Gains (losses) on sales of rural home loans, net	—	(86)
Patronage refunds from other Farm Credit institutions	46	134
Other noninterest income	3,034	1,537
Total noninterest income	1,171	(5,799)
<b>Noninterest Expenses</b>		
Salaries and employee benefits	11,795	11,068
Occupancy and equipment	3,736	3,452
Insurance Fund premiums	1,070	1,364
Other operating expenses	5,478	4,986
Called debt expense	12,745	1,443
Correspondent lending servicing expense	2,303	2,265
Other noninterest expense	—	70
Total noninterest expenses	37,127	24,648
Net income	\$ 123,003	\$ 102,905

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



# Statements of Comprehensive Income

(unaudited)

<i>(dollars in thousands)</i>	For the three months ended March 31,	
	2012	2011
<b>Net income</b>	\$ 123,003	\$ 102,905
Other comprehensive income net of tax		
Unrealized gains (losses) on investments available for sale:		
Other-than-temporarily impaired (Note 2)	197	(1,505)
Not other-than-temporarily impaired (Note 2)	12,966	(15,454)
Change in value of firm commitments - when issued securities (Note 7)	655	(1,752)
Employee benefit plans adjustments	(116)	(71)
Other comprehensive income	13,702	(18,782)
Comprehensive income	\$ 136,705	\$ 84,123

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

# Statements of Changes in Shareholders' Equity

(unaudited)

<i>(dollars in thousands)</i>	Perpetual Preferred Stock	Capital Stock and Participation Certificates	Additional Paid-In-Capital	Retained Earnings		Accumulated Other Comprehensive Income	Total Shareholders' Equity
				Allocated	Unallocated		
Balance at December 31, 2010	\$ 400,000	\$ 417,333	\$ —	\$ 871	\$ 1,052,248	\$ 32,329	\$ 1,902,781
Comprehensive income					102,905	(18,782)	84,123
Capital stock/participation certificates issued/(retired), net		(1,917)					(1,917)
Patronage distribution adjustment		(7)			7		—
Balance at March 31, 2011	\$ 400,000	\$ 415,409	\$ —	\$ 871	\$ 1,155,160	\$ 13,547	\$ 1,984,987
<b>Balance at December 31, 2011</b>	<b>\$ 400,000</b>	<b>\$ 405,767</b>	<b>\$ —</b>	<b>\$ 858</b>	<b>\$ 1,218,648</b>	<b>\$ 123,997</b>	<b>\$ 2,149,270</b>
Comprehensive income					<b>123,003</b>	<b>13,702</b>	<b>136,705</b>
Capital stock/participation certificates issued/(retired), net		(3,231)					(3,231)
Redemption of perpetual preferred stock (Note 8)	(110,550)		31,860				(78,690)
Dividends paid on perpetual preferred stock					(1,496)		(1,496)
Balance at March 31, 2012	<b>\$ 289,450</b>	<b>\$ 402,536</b>	<b>\$ 31,860</b>	<b>\$ 858</b>	<b>\$ 1,340,155</b>	<b>\$ 137,699</b>	<b>\$ 2,202,558</b>

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

# Statements of Cash Flows

(unaudited)

<i>(dollars in thousands)</i>	For the three months ended March 31,	
	2012	2011
<b>Cash flows from operating activities:</b>		
Net income	\$ 123,003	\$ 102,905
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation on premises and equipment	1,737	1,715
Premium amortization (discount accretion) on investment securities	2,886	7,418
(Premium amortization) discount accretion on bonds and notes	219	380
Provision for (reversal of allowance for) loan losses	(2,721)	10,896
(Gains) losses on other property owned, net	3,523	5,780
Net impairment losses on investments	750	4,458
(Gains) losses on sales of rural home loans, net	—	86
Net change in loans held for sale	8,736	7,801
Changes in operating assets and liabilities:		
(Increase) decrease in accrued interest receivable	(626)	(1,754)
(Increase) decrease in due from associations	14,344	17,329
(Increase) decrease in other assets	(1,459)	18,265
Increase (decrease) in accrued interest and dividends payable	(5,224)	13,620
Increase (decrease) in other liabilities	(19,297)	(21,232)
Total adjustments	2,868	64,762
Net cash provided by (used in) operating activities	125,871	167,667
<b>Cash flows from investing activities:</b>		
Investment securities purchased	(255,034)	(486,786)
Investment securities sold or matured	375,521	460,303
(Increase) decrease in firm commitments - when issued securities	655	(1,752)
Net (increase) decrease in loans	618,771	494,125
(Increase) decrease in investments in other Farm Credit System institutions	44	52
Purchase of premises and equipment, net	(1,140)	(1,744)
Proceeds from sale of other property owned	2,117	3,333
Net cash provided by (used in) investing activities	740,934	467,531
<b>Cash flows from financing activities:</b>		
Bonds and notes issued	12,336,421	6,458,014
Bonds and notes retired	(13,654,042)	(7,912,762)
Capital stock and participation certificates issued/retired, net	(3,231)	(1,917)
Cash distribution to shareholders	(180,726)	(190,280)
Redemption of perpetual preferred stock (Note 8)	(78,690)	—
Dividends paid on perpetual preferred stock	(1,496)	—
Net cash provided by (used in) financing activities	(1,581,764)	(1,646,945)
Net increase (decrease) in cash and cash equivalents	(714,959)	(1,011,747)
Cash and cash equivalents, beginning of period	1,301,569	1,427,033
Cash and cash equivalents, end of period	\$ 586,610	\$ 415,286
<b>Supplemental schedule of non-cash investing and financing activities:</b>		
Receipt of property in settlement of loans	\$ 1,866	\$ 4,580
Change in unrealized gains (losses) on investments, net	13,163	(16,959)
Change in fair value of derivative instruments (Note 7)	319	(8,493)
Employee benefit plans adjustments	116	71
<b>Non-cash changes related to hedging activities:</b>		
Increase (decrease) in bonds and notes	\$ (3,201)	\$ (11,570)
Decrease (increase) in other assets	3,201	11,570
<b>Supplemental information:</b>		
Interest paid	\$ 61,224	\$ 66,816

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

# Notes to the Financial Statements

*(dollars in thousands, except as noted)*  
*(unaudited)*

## **NOTE 1 — ORGANIZATION, SIGNIFICANT ACCOUNTING POLICIES, AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS**

### **Organization and Significant Accounting Policies**

The accompanying financial statements include the accounts of AgFirst Farm Credit Bank (AgFirst or Bank). AgFirst and its related twenty associations (Associations or District Associations) are collectively referred to as the District. Effective January 1, 2011, Farm Credit of North Florida, ACA, and Farm Credit of Southwest Florida, ACA, merged with and into Farm Credit of South Florida, ACA, which then changed its name to Farm Credit of Florida, ACA, reducing the number of Associations in the District from twenty-two to twenty. A description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations of the Bank as of and for the year ended December 31, 2011 are contained in the 2011 Annual Report to Shareholders. These unaudited first quarter 2012 financial statements should be read in conjunction with the 2011 Annual Report to Shareholders.

The accompanying financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles (GAAP) and prevailing practices within the banking industry. The results for the three months ended March 31, 2012 are not necessarily indicative of the results to be expected for the year ending December 31, 2012.

Certain amounts in the prior period's financial statements may have been reclassified to conform to the current period's financial statement presentation. Such reclassifications had no effect on the prior period net income or total capital as previously reported.

The Bank maintains an allowance for loan losses at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals. A review of individual loans in each respective portfolio is performed periodically to determine the appropriateness of risk ratings and to ensure loss exposure to the Bank has been identified. Certain loan pools acquired from several of the District Associations are analyzed in accordance with the selling Association's allowance methodologies for assigning general and specific allowances. The allowance for loan losses is a valuation account used to reasonably estimate loan losses as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss. The Bank considers factors such as credit risk classifications, collateral values, risk concentrations, weather related conditions, current production and economic conditions, and prior loan loss experience, among others, when determining the allowance for loan losses.

A specific allowance may be established for impaired loans under Financial Accounting Standards Board (FASB) guidance on accounting by creditors for impairment of a loan. Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable market price, or fair value of the collateral if the loan is collateral dependent.

A general allowance may also be established under FASB guidance on accounting for contingencies to reflect estimated probable credit losses incurred in the remainder of the loan portfolio at the financial statement date. The general allowance excludes loans included under the specific allowance discussed above, unless specific characteristics of the loan indicate that it is probable that there would be an incurred loss in a group of loans with those characteristics. The level of the general allowance may be based on management's best estimate of the likelihood of default adjusted for other relevant factors reflecting the current environment.

The credit risk rating methodology is a key component of the Bank's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. The Bank uses a two-dimensional loan rating model based on internally generated combined system risk rating guidance that incorporates a 14-point risk rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan assuming default has occurred or is expected to occur within the next 12 months.

Each of the 14 categories carries a distinct percentage of default probability. The 14-point risk rating scale provides for granularity of the probability of default, especially in the acceptable ratings. There are nine acceptable categories that range from a borrower of the highest quality to a borrower of minimally acceptable quality. The probability of default between 1 and 9 is very narrow and would reflect almost no default to a minimal default percentage. The probability of default grows more rapidly as a loan moves from a "9" to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain.

#### **Recently Issued Accounting Pronouncements:**

In December 2011, the FASB issued Accounting Standards Update (ASU) 2011-11, "Balance Sheet (Topic 220) - Disclosures about Offsetting Assets and Liabilities." The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities. The requirements apply to recognized financial instruments and derivative instruments that are offset in accordance with accounting guidance and for those recognized financial instruments and derivative instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset or not. This guidance is to be applied retrospectively for all comparative periods and is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The adoption of this guidance will not impact the Bank's financial condition or its results of operations, but will result in additional disclosures.

In June 2011, the FASB issued ASU 2011-05, "Comprehensive Income (Topic 220): Presentation of Comprehensive Income." This amendment is intended to increase the prominence of other comprehensive income in financial statements. The current option that permits the presentation of other comprehensive income in the statement of changes in equity has been eliminated. The main provisions of the guidance provides that an entity that reports items of other comprehensive income has the option to present comprehensive income in either one or two consecutive financial statements: (1) A single statement must present the components of net income and total net income, the components of other comprehensive income and total other comprehensive income, and a total for comprehensive income; (2) In a two-statement approach, an entity must present the components of net income and total net income in the first statement. That statement must be immediately followed by a financial statement that presents the components of other comprehensive income, a total for other comprehensive income, and a total for comprehensive income. With either approach, an entity is required to present reclassification adjustments for items reclassified from other comprehensive income to net income in the statement(s). This guidance is to be applied retrospectively. For public entities, it is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance will not impact the Bank's financial condition or results of operations, but will result in changes to the presentation of comprehensive income. In December 2011, the FASB issued guidance (ASU 2011-12; Topic 220) to defer the new requirement to present components of accumulated other comprehensive income reclassified as components of net income on the face of the financial statements. All other requirements in the guidance for comprehensive income are required to be adopted as set forth in the June 2011 guidance. The deferral is effective at the same time the new standard on comprehensive income is adopted.

In May 2011, the FASB issued ASU 2011-04, "Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs." The amendments change the wording used to describe the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments include the following: (1) Application of the highest

and best use and valuation premise is only relevant when measuring the fair value of nonfinancial assets (does not apply to financial assets and liabilities); (2) Aligns the fair value measurement of instruments classified within an entity's shareholders' equity with the guidance for liabilities. As a result, an entity should measure the fair value of its own equity instruments from the perspective of a market participant that holds the instruments as assets; (3) Clarifies that a reporting entity should disclose quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy; (4) An exception to the requirement for measuring fair value when a reporting entity manages its financial instruments on the basis of its net exposure, rather than its gross exposure, to those risks; (5) Clarifies that the application of premiums and discounts in a fair value measurement is related to the unit of account for the asset or liability being measured at fair value. Premiums or discounts related to size as a characteristic of the entity's holding (that is, a blockage factor) instead of as a characteristic of the asset or liability (for example, a control premium), are not permitted. A fair value measurement that is not a Level 1 measurement may include premiums or discounts other than blockage factors when market participants would incorporate the premium or discount into the measurement at the level of the unit of account specified in other guidance; (6) Expansion of the disclosures about fair value measurements. The most significant change will require entities, for their recurring Level 3 fair value measurements, to disclose quantitative information about unobservable inputs used, a description of the valuation processes used by the entity, and a qualitative discussion about the sensitivity of the measurements. New disclosures are required about the use of a nonfinancial asset measured or disclosed at fair value if its use differs from its highest and best use. In addition, entities must report the level in the fair value hierarchy of assets and liabilities not recorded at fair value but where fair value is disclosed. The amendments are to be applied prospectively. The amendments are effective during interim and annual periods beginning after December 15, 2011. Early application is not permitted. The adoption of this guidance will not impact the Bank's financial condition or results of operations, but will result in additional disclosures.

In April 2011, the FASB issued ASU 2011-02, "Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring," which provides for clarification on whether a restructuring constitutes a troubled debt restructuring (TDR). In evaluating whether a restructuring is a TDR, a creditor must separately conclude that both of the following exists: (1) the restructuring constitutes a concession, and (2) the debtor is experiencing financial difficulties. The guidance is effective for nonpublic entities, including the Bank, for annual periods ending on or after December 15, 2012, including interim periods within those annual periods. The guidance should be applied retrospectively to the beginning of the annual period of adoption. The new disclosures about TDR activity required by the guidance on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses," as discussed below, are effective for annual reporting periods ending after December 15, 2011.

In January 2011, the FASB issued ASU 2011-01, "Receivables (Topic 310): Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings." This amendment temporarily delayed the effective date of the disclosures about TDRs required by the guidance previously issued on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses." The effective date of the new disclosures about TDRs coincides with the guidance for determining what constitutes a TDR as described above. The adoption of this guidance had no material impact on the Bank's financial condition and results of operations but resulted in significant additional disclosures.

Other recently issued accounting pronouncements are discussed in the 2011 Annual Report to Shareholders.

**NOTE 2 — INVESTMENT SECURITIES**

**Available-for-sale**

A summary of the amortized cost and fair value of debt securities held as available-for-sale investments follows:

	<b>March 31, 2012</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. GNMA MBS/CMOs	\$ 4,784,006	\$ 180,722	\$ (3,162)	\$ 4,961,566	2.51%
U.S. Govt. Agency MBS	1,630,127	29,158	(9,408)	1,649,877	1.49
Non-Agency CMOs (a)	279,947	153	(46,722)	233,378	0.78
Asset-Backed Securities (a)	33,632	2,241	(6,994)	28,879	0.77
Total	<b>\$ 6,727,712</b>	<b>\$ 212,274</b>	<b>\$ (66,286)</b>	<b>\$ 6,873,700</b>	<b>2.19%</b>

	<b>December 31, 2011</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. GNMA MBS/CMOs	\$ 4,831,529	\$ 174,101	\$ (3,129)	\$ 5,002,501	2.46%
U.S. Govt. Agency MBS	1,634,942	26,459	(10,572)	1,650,829	1.50
Non-Agency CMOs (b)	291,377	248	(49,869)	241,756	0.83
Asset-Backed Securities (b)	34,736	2,239	(6,651)	30,324	0.70
Total	<b>\$ 6,792,584</b>	<b>\$ 203,047</b>	<b>\$ (70,221)</b>	<b>\$ 6,925,410</b>	<b>2.15%</b>

- (a) Gross unrealized losses include non-credit related other-than-temporary impairment recognized in AOCI of \$15.0 million for Non-Agency CMOs and \$5.4 million for Asset-Backed Securities.
- (b) Gross unrealized losses include non-credit related other-than temporary impairment recognized in AOCI of \$15.7 million for Non-Agency CMOs and \$5.0 million for Asset-Backed Securities.

**Held-to-maturity**

A summary of the amortized cost and fair value of debt securities held as held-to-maturity investments follows:

	<b>March 31, 2012</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. Agency MBS	\$ 632,927	\$ 55,487	\$ (185)	\$ 688,229	5.37%
Mission Related Investments	162,685	11,787	(450)	174,022	6.11
Total	<b>\$ 795,612</b>	<b>\$ 67,274</b>	<b>\$ (635)</b>	<b>\$ 862,251</b>	<b>5.52%</b>

	<b>December 31, 2011</b>				
<i>(dollars in thousands)</i>	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Yield</b>
U.S. Govt. Agency MBS	\$ 691,331	\$ 59,389	\$ (188)	\$ 750,532	5.35%
Mission Related Investments	163,531	14,112	(122)	177,521	6.07
Total	<b>\$ 854,862</b>	<b>\$ 73,501</b>	<b>\$ (310)</b>	<b>\$ 928,053</b>	<b>5.49%</b>

A summary of the expected maturity, estimated fair value and amortized cost of investment securities at March 31, 2012 follows:

**Available-for-sale**

<i>(dollars in thousands)</i>	Due in 1 year or less		Due after 1 year through 5 years		Due after 5 years through 10 years		Due after 10 years		Total	
	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
U.S. Govt. GNMA MBS/CMOs	\$ —	— %	\$ —	— %	\$ 3,137	1.73 %	\$ 4,958,429	2.51 %	\$ 4,961,566	2.51 %
U.S. Govt. Agency MBS	—	—	14,404	4.07	17,779	0.80	1,617,694	1.48	1,649,877	1.49
Non-Agency CMOs	—	—	—	—	—	—	233,378	0.78	233,378	0.78
Asset-Backed Securities	—	—	—	—	—	—	28,879	0.77	28,879	0.77
Total fair value	\$ —	— %	\$ 14,404	4.07 %	\$ 20,916	0.93 %	\$ 6,838,380	2.19 %	\$ 6,873,700	2.19 %
Total amortized cost	\$ —		\$ 13,498		\$ 20,756		\$ 6,693,458		\$ 6,727,712	

**Held-to-maturity**

<i>(dollars in thousands)</i>	Due in 1 year or less		Due after 1 year through 5 years		Due after 5 years through 10 years		Due after 10 years		Total	
	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
U.S. Govt. Agency MBS	\$ —	— %	\$ —	— %	\$ 1,256	4.94 %	\$ 631,671	5.37 %	\$ 632,927	5.37 %
Mission Related Investments	2,997	5.20	20,738	6.83	31,380	6.09	107,570	6.01	162,685	6.11
Total amortized cost	\$ 2,997	5.20 %	\$ 20,738	6.83 %	\$ 32,636	6.04 %	\$ 739,241	5.46 %	\$ 795,612	5.52 %
Total fair value	\$ 3,114		\$ 21,880		\$ 35,713		\$ 801,544		\$ 862,251	

Included in the available-for-sale investments are collateralized mortgage obligations (CMOs). Substantially all CMO securities have contractual maturities in excess of ten years. However, expected maturities for CMO securities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

There were no sales of investment securities during the first quarter of 2012 or 2011.

AgFirst's investments include primarily mortgage-backed securities (MBSs) and asset-backed securities (ABSs). These securities are held to maintain a liquidity reserve, manage short-term surplus funds, and manage interest rate risk. These securities must meet the applicable Farm Credit Administration (FCA) regulatory guidelines, which require these securities to be high quality, senior class, and rated in the top category (AAA/Aaa) by Nationally Recognized Statistical Rating Organizations (NRSROs) at the time of purchase. To achieve the ratings, these securities have a guarantee of timely payment of principal and interest, credit enhancements achieved through over-collateralization or other means, and the priority of payments of senior classes over junior classes. All ABSs have credit enhancement features including senior/subordinate structure and/or are backed by a bond insurer.

The FCA considers a MBS or ABS ineligible if it falls below the AAA/Aaa credit rating criteria and requires System institutions to divest of such an investment unless the FCA grants specific approval to continue to hold an ineligible security.

The Bank's MBSs are collateralized by U.S. government or U.S. agency guaranteed residential mortgages and all were rated AAA/Aaa at March 31, 2012. Non-agency CMO securities not rated in the top category by at least one of the NRSROs at March 31, 2012 had a fair value of \$231.7 million. ABSs not rated in the top category by at least one of the NRSROs at March 31, 2012 had a fair value of \$20.1 million. For each of these investment securities in the Bank's portfolio rated below AAA/Aaa, the Bank has developed and submitted plans for approval by the FCA that provide that the securities may be held to maturity. The FCA has approved, with conditions, the Bank's plans for all but seven investments that have recently become ineligible. The Bank has submitted a plan to hold four of these recently ineligible securities and is in the process of submitting a plan to obtain approval from the FCA to hold the remaining three investments.



Held-to-maturity Mission Related Investments consist primarily of Rural America Bonds, which are private placement securities purchased under the Mission Related Program approved by the FCA.

An investment is considered impaired if its fair value is less than its cost. This also applies to those securities other-than-temporarily impaired for which a credit loss has been recognized but noncredit-related losses continue to remain unrealized. The following table shows the fair value and gross unrealized losses for investments that have been in a continuous unrealized loss position aggregated by investment category at March 31, 2012 and December 31, 2011. A continuous unrealized loss position for an investment is measured from the date the impairment was first identified.

<i>(dollars in thousands)</i>	March 31, 2012					
	Less than 12 Months		Greater than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Govt. GNMA MBS/CMOs	\$ 24,453	\$ (137)	\$ 235,725	\$ (3,025)	\$ 260,178	\$ (3,162)
U.S. Govt. Agency MBS	267,992	(1,441)	415,716	(8,152)	683,708	(9,593)
Non-Agency CMOs	–	–	232,831	(46,722)	232,831	(46,722)
Asset-Backed Securities	–	–	22,140	(6,994)	22,140	(6,994)
Mission Related Investments	19,304	(450)	–	–	19,304	(450)
Total	\$ 311,749	\$ (2,028)	\$ 906,412	\$ (64,893)	\$ 1,218,161	\$ (66,921)

<i>(dollars in thousands)</i>	December 31, 2011					
	Less than 12 Months		Greater than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Govt. GNMA MBS/CMOs	\$ 50,348	\$ (29)	\$ 260,965	\$ (3,101)	\$ 311,313	\$ (3,130)
U.S. Govt. Agency MBS	227,889	(1,646)	442,142	(9,114)	670,031	(10,760)
Non-Agency CMOs	–	–	241,092	(49,868)	241,092	(49,868)
Asset-Backed Securities	–	–	27,356	(6,651)	27,356	(6,651)
Mission Related Investments	11,987	(122)	–	–	11,987	(122)
Total	\$ 290,224	\$ (1,797)	\$ 971,555	\$ (68,734)	\$ 1,261,779	\$ (70,531)

FASB guidance for other-than-temporary impairment contemplates numerous factors in determining whether an impairment is other-than-temporary. These factors include: (1) whether or not management intends to sell the security, (2) whether it is more likely than not that management would be required to sell the security before recovering its costs, and (3) whether management expects to recover the security's entire amortized cost basis (even if there is no intention to sell). If the Bank intends to sell the security or it is more likely than not that it would be required to sell the security, the impairment loss equals the full difference between amortized cost and fair value of the security. When the Bank does not intend to sell securities in an unrealized loss position and it is not more likely than not that it would be required to sell the securities, other-than-temporary impairment loss is separated into credit loss and non-credit loss. Credit loss is defined as the shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis.

The Bank performs periodic credit reviews, including other-than-temporary impairment analyses, on its investment securities portfolio. The objective is to quantify future possible loss of principal or interest due on securities in the portfolio. Factors considered in determining whether an impairment is other-than-temporary include among others: (1) the length of time and the extent to which the fair value is less than cost, (2) adverse conditions specifically related to the industry, (3) geographic area and the condition of the underlying collateral, (4) payment structure of the security, (5) ratings by rating agencies, (6) the credit worthiness of bond insurers, and (7) volatility of the fair value changes. Based on the results of all analyses, the Bank has recognized total other-than-temporary impairment during the first three months of 2012 of \$839 thousand in connection with ABS securities and non-agency CMO securities in its portfolio, which is included in Impairment Losses on Investments in the Statements of Income.

Since the Bank does not intend to sell these other-than-temporarily impaired debt securities and is not more likely than not to be required to sell before recovery, the other-than temporary impairment of \$839 thousand is separated into: (1) the estimated amount relating to credit loss (\$750 thousand reflected in Net Income in the Statements of

Income), which is partially offset by (2) the amount relating to all other factors (\$89 thousand gain reflected in the Statements of Comprehensive Income).

The Bank uses the present value of cash flows expected to be collected from the debt security to determine the amount of credit loss. This technique requires assumptions related to the underlying collateral, including default rates, degree and timing of prepayments, and loss severity. Assumptions can vary widely from security to security and are influenced by such factors as loan interest rate, geographical location of the borrower, borrower characteristics, and collateral type.

Significant inputs used in this technique to measure the amount related to the credit loss include, but are not limited to, performance indicators of the underlying assets in the security (including default rates, delinquency rates, and percentage of nonperforming assets), loan-to-collateral value ratios, third-party guarantees, current levels of subordination, vintage, geographic concentration, and credit ratings. The Bank obtains assumptions for the default rate, prepayment rate, and loss severity rate from an independent third party. Default rate assumptions are generally estimated using historical loss and performance information to estimate future defaults. The forecasted cumulative default rates used at March 31, 2012 ranged from 1.46 percent to 42.39 percent for non-agency CMO securities and from 22.72 percent to 82.51 percent for ABS securities. Prepayment rate assumptions are based on forecasted prepayments and resulted in prepayment rates that ranged from 6.98 percent to 20.42 percent for non-agency CMO securities and from 2.73 percent to 6.68 percent for ABS securities at March 31, 2012. At March 31, 2012, the loss severity rates estimated from assumptions ranged from 4.54 percent to 61.15 percent for non-agency CMO securities and from 60.81 percent to 100.00 percent for ABS securities.

For all investments, other than the other-than-temporarily impaired securities discussed above, the Bank has not recognized any other-than-temporary impairment as the unrealized losses resulted from non-credit related factors. The Bank has the ability and intent to hold these investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities. Substantially all of these investments were in U.S. Government agency securities and the Bank expects these securities would not be settled at a price less than their amortized cost. For the three months ended March 31, 2012, net unrealized gains of \$13.0 million were recognized in other comprehensive income for not other-than-temporarily impaired available-for-sale investments.

The following schedules detail the activity related to cumulative credit losses on investments recognized in earnings as of March 31, 2012 and 2011:

<i>(dollars in thousands)</i>	<b>For the Quarter Ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
<b>Beginning balance at January 1</b>	\$ 52,980	\$ 44,791
Additions for the amount related to credit loss for which other-than-temporary impairment was not previously recognized	-	1,463
Additions for the amount related to credit loss for which other-than-temporary impairment was previously recognized	750	2,994
Reductions for increases in expected cash flows	(342)	(352)
<b>Ending balance at March 31</b>	<b>\$ 52,388</b>	<b>\$ 48,896</b>

### NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES

For a complete description of the Bank's accounting for loans (including impaired loans and the allowance for loan losses) and definitions of loan types, see the 2011 Annual Report to Shareholders.

Credit risk arises from the potential inability of an obligor to meet its repayment obligation. The Bank manages credit risk associated with lending activities through an assessment of the credit risk profile of an individual obligor. The Bank sets its own underwriting standards and lending policies that provide direction to loan officers and are approved by the board of directors.

The credit risk management process begins with an analysis of the obligor's credit history, repayment capacity and financial position. Repayment capacity focuses on the obligor's ability to repay the obligation based on cash flows from operations or other sources of income, including non-farm income. Real estate mortgage loans must be secured

by first liens on the real estate collateral. As required by FCA regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures.

The credit risk rating process for loans uses a two-dimensional loan rating structure, incorporating a 14-point risk rating scale (as discussed in Note 1 above) to identify and track a borrower's probability of default and a separate scale addressing loss given default. The loan rating structure calculates estimates of loss through two components, borrower risk and transaction risk. Borrower risk is the risk of loss driven by factors intrinsic to the borrower. The transaction risk or facility risk is related to the structure of a credit (tenor, terms, and collateral).

A summary of loans outstanding at March 31, 2012 and December 31, 2011 follows:

<i>(dollars in thousands)</i>	March 31, 2012	December 31, 2011
Direct notes	\$ 13,471,353	\$ 14,094,384
Real estate mortgage	1,167,230	1,207,221
Production and intermediate-term	1,272,008	1,382,659
Agribusiness		
Loans to cooperatives	258,562	174,552
Processing and marketing	657,183	684,300
Farm-related business	137,028	114,826
Total agribusiness	1,052,773	973,678
Communication	156,618	136,899
Energy	274,065	246,930
Water and waste disposal	28,000	28,000
Rural residential real estate	2,083,774	2,060,025
Loans to other financial institutions (OFIs)	6,900	5,250
Other (including mission-related)	13,024	17,020
Total Loans	\$ 19,525,745	\$ 20,152,066

A substantial portion of the Bank's loan portfolio consists of notes receivable from District Associations (Direct Notes). These notes are used by the Associations to fund their loan portfolios, which collateralize the notes. Therefore the Bank's concentration of credit risk in various agricultural commodities associated with these notes approximates that of the District as a whole. Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities, which would cause them to be similarly impacted by economic or other conditions. A substantial portion of the Associations' lending activities is collateralized, and their exposure to credit loss associated with lending activities is reduced accordingly, which further mitigates credit risk to the Bank.

The Bank may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with FCA regulations. The following tables present participations purchased and sold balances at March 31, 2012 and December 31, 2011:

<i>(dollars in thousands)</i>	March 31, 2012							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 986,016	\$ 26,451	\$ 116,604	\$ 26,791	\$ 17,325	\$ -	\$ 1,119,945	\$ 53,242
Production and intermediate-term	1,251,107	234,305	264,446	188,215	180,624	-	1,696,177	422,520
Agribusiness								
Loans to cooperatives	3,939	61,874	285,630	-	32,108	-	321,677	61,874
Processing and marketing	122,327	256,687	263,220	45,165	590,197	8,352	975,744	310,204
Farm-related business	36,145	38,524	112,568	-	27,795	-	176,508	38,524
Total agribusiness	162,411	357,085	661,418	45,165	650,100	8,352	1,473,929	410,602
Communication	-	45,533	203,066	-	-	-	203,066	45,533
Energy	167	17,438	285,176	-	7,434	-	292,777	17,438
Water and waste disposal	-	-	28,000	-	-	-	28,000	-
Rural residential real estate	263	-	-	-	-	-	263	-
Loans to OFIs	-	-	-	-	6,900	-	6,900	-
Other (including mission-related)	52,330	13,913	-	22,022	-	3,240	52,330	39,175
Total	\$ 2,452,294	\$ 694,725	\$ 1,558,710	\$ 282,193	\$ 862,383	\$ 11,592	\$ 4,873,387	\$ 988,510

December 31, 2011

	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
<i>(dollars in thousands)</i>								
Real estate mortgage	\$ 1,055,560	\$ 41,469	\$ 107,889	\$ 39,820	\$ 17,806	\$ —	\$ 1,181,255	\$ 81,289
Production and intermediate-term	1,470,251	287,117	244,382	245,785	204,505	—	1,919,138	532,902
Agribusiness								
Loans to cooperatives	12,355	29,805	164,560	—	28,717	—	205,632	29,805
Processing and marketing	130,893	266,819	251,802	29,271	618,541	8,750	1,001,236	304,840
Farm-related business	34,077	33,339	93,958	—	21,089	—	149,124	33,339
Total agribusiness	177,325	329,963	510,320	29,271	668,347	8,750	1,355,992	367,984
Communication	—	43,562	181,323	—	—	—	181,323	43,562
Energy	167	16,675	257,196	—	7,510	—	264,873	16,675
Water and waste disposal	—	—	28,000	—	—	—	28,000	—
Rural residential real estate	269	—	—	—	—	—	269	—
Loans to OFIs	—	—	—	—	5,250	—	5,250	—
Other (including mission-related)	57,171	13,913	—	22,022	—	3,240	57,171	39,175
Total	\$ 2,760,743	\$ 732,699	\$ 1,329,110	\$ 336,898	\$ 903,418	\$ 11,990	\$ 4,993,271	\$ 1,081,587

A significant source of liquidity for the Bank is the repayments and maturities of loans. The following table presents the contractual maturity distribution of loans by loan type at March 31, 2012 and indicates that approximately 6.90 percent of loans had maturities of less than one year:

<i>(dollars in thousands)</i>	Due less than 1 year	Due 1 through 5 years	Due after 5 years	Total
Direct notes	\$ 844,574	\$ 3,392,242	\$ 9,234,537	\$ 13,471,353
Real estate mortgage	87,987	411,020	668,223	1,167,230
Production and intermediate-term	328,290	638,631	305,087	1,272,008
Agribusiness				
Loans to cooperatives	20,732	144,495	93,335	258,562
Processing and marketing	58,488	498,215	100,480	657,183
Farm-related business	1,907	105,881	29,240	137,028
Total agribusiness	81,127	748,591	223,055	1,052,773
Communication	—	129,294	27,324	156,618
Energy	4,903	124,378	144,784	274,065
Water and waste disposal	—	—	28,000	28,000
Rural residential real estate	5	1,865	2,081,904	2,083,774
Loans to OFIs	—	6,900	—	6,900
Other (including mission-related)	911	182	11,931	13,024
Total Loans	\$ 1,347,797	\$ 5,453,103	\$ 12,724,845	\$ 19,525,745

The following table shows loans and related accrued interest classified under the FCA Uniform Loan Classification System as a percentage of total loans and related accrued interest receivable by loan type as of March 31, 2012 and December 31, 2011:

	March 31, 2012	December 31, 2011		March 31, 2012	December 31, 2011
<b>Direct notes:</b>			<b>Communication:</b>		
Acceptable	85.68%	85.65%	Acceptable	100.00%	100.00%
OAEM	11.41	11.38	OAEM	-	-
Substandard/doubtful/loss	2.91	2.97	Substandard/doubtful/loss	-	-
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Real estate mortgage:</b>			<b>Energy/water and waste disposal:</b>		
Acceptable	84.91%	84.03%	Acceptable	100.00%	99.25%
OAEM	9.72	9.86	OAEM	-	0.75
Substandard/doubtful/loss	5.37	6.11	Substandard/doubtful/loss	-	-
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Production and intermediate-term:</b>			<b>Rural residential real estate:</b>		
Acceptable	77.10%	78.21%	Acceptable	100.00%	100.00%
OAEM	15.62	15.09	OAEM	-	-
Substandard/doubtful/loss	7.28	6.70	Substandard/doubtful/loss	-	-
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Agribusiness:</b>			<b>Loans to OFIs:</b>		
<b>Loans to cooperatives:</b>			Acceptable	100.00%	100.00%
Acceptable	96.60%	98.40%	OAEM	-	-
OAEM	3.40	1.60	Substandard/doubtful/loss	-	-
Substandard/doubtful/loss	-	-		<u>100.00%</u>	<u>100.00%</u>
	<u>100.00%</u>	<u>100.00%</u>	<b>Other (including mission-related):</b>		
<b>Processing and marketing:</b>			Acceptable	86.61%	87.15%
Acceptable	90.41%	88.78%	OAEM	2.37	1.79
OAEM	3.32	5.05	Substandard/doubtful/loss	11.02	11.06
Substandard/doubtful/loss	6.27	6.17		<u>100.00%</u>	<u>100.00%</u>
	<u>100.00%</u>	<u>100.00%</u>	<b>Total Loans:</b>		
<b>Farm-related business:</b>			Acceptable	87.35%	87.09%
Acceptable	99.54%	99.43%	OAEM	9.63	9.79
OAEM	0.46	0.57	Substandard/doubtful/loss	3.02	3.12
Substandard/doubtful/loss	-	-		<u>100.00%</u>	<u>100.00%</u>
	<u>100.00%</u>	<u>100.00%</u>			
<b>Total agribusiness:</b>					
Acceptable	93.12%	91.76%			
OAEM	2.97	3.90			
Substandard/doubtful/loss	3.91	4.34			
	<u>100.00%</u>	<u>100.00%</u>			

The following tables provide an age analysis of past due loans and related accrued interest as of March 31, 2012 and December 31, 2011:

<i>(dollars in thousands)</i>	March 31, 2012					
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Direct notes	\$ —	\$ —	\$ —	\$ 13,501,358	\$ 13,501,358	\$ —
Real estate mortgage	5,253	26,527	31,780	1,144,706	1,176,486	1,124
Production and intermediate-term Agribusiness	4,339	25,998	30,337	1,249,790	1,280,127	—
Loans to cooperatives	—	—	—	259,800	259,800	—
Processing and marketing	6	4	10	660,428	660,438	—
Farm-related business	—	—	—	137,315	137,315	—
Total agribusiness	6	4	10	1,057,543	1,057,553	—
Communication	—	—	—	156,950	156,950	—
Energy and water/waste disposal	—	—	—	303,896	303,896	—
Rural residential real estate	32,443	4,552	36,995	2,054,194	2,091,189	4,232
Loans to OFIs	—	—	—	6,912	6,912	—
Other (including mission-related)	—	1,456	1,456	11,753	13,209	—
Total	\$ 42,041	\$ 58,537	\$ 100,578	\$ 19,487,102	\$ 19,587,680	\$ 5,356

<i>(dollars in thousands)</i>	December 31, 2011					
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment 90 Days or More Past Due and Accruing Interest
Direct notes	\$ —	\$ —	\$ —	\$ 14,126,861	\$ 14,126,861	\$ —
Real estate mortgage	7,842	32,463	40,305	1,175,866	1,216,171	799
Production and intermediate-term Agribusiness	3,042	28,384	31,426	1,359,086	1,390,512	—
Loans to cooperatives	—	—	—	175,260	175,260	—
Processing and marketing	7	(319)	(312)	687,383	687,071	—
Farm-related business	—	—	—	115,135	115,135	—
Total agribusiness	7	(319)	(312)	977,778	977,466	—
Communication	—	—	—	137,126	137,126	—
Energy and water/waste disposal	—	—	—	276,488	276,488	—
Rural residential real estate	42,505	8,066	50,571	2,015,626	2,066,197	4,553
Lease receivables	—	—	—	—	—	—
Loans to OFIs	—	—	—	5,259	5,259	—
Other (including mission-related)	—	—	—	17,170	17,170	—
Total	\$ 53,396	\$ 68,594	\$ 121,990	\$ 20,091,260	\$ 20,213,250	\$ 5,352

The recorded investment in the receivable is the face amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges, or acquisition costs and may also reflect a previous direct write-down of the investment.

Nonperforming assets (including related accrued interest) and related credit quality statistics at March 31, 2012 and December 31, 2011 are summarized as follows:

<i>(dollars in thousands)</i>	<b>March 31, 2012</b>	<b>December 31, 2011</b>
<b>Nonaccrual loans:</b>		
Real estate mortgage	\$ 34,795	\$ 40,293
Production and intermediate-term Agribusiness	30,539	32,986
Processing and marketing	3,318	4,316
Total agribusiness	3,318	4,316
Rural residential real estate	2,265	5,727
Other (including mission-related)	1,456	1,900
Total nonaccrual loans	<u>\$ 72,373</u>	<u>\$ 85,222</u>
<b>Accruing restructured loans:</b>		
Real estate mortgage	\$ 4,120	\$ 4,134
Production and intermediate-term Agribusiness	11,312	10,017
Processing and marketing	18,938	24,606
Total agribusiness	18,938	24,606
Total accruing restructured loans	<u>\$ 34,370</u>	<u>\$ 38,757</u>
<b>Accruing loans 90 days or more past due:</b>		
Real estate mortgage	\$ 1,124	\$ 799
Production and intermediate-term	-	-
Rural residential real estate	4,232	4,553
Total accruing loans 90 days or more past due	<u>\$ 5,356</u>	<u>\$ 5,352</u>
Total nonperforming loans	\$ 112,099	\$ 129,331
Other property owned	40,383	44,157
Total nonperforming assets	<u>\$ 152,482</u>	<u>\$ 173,488</u>
Nonaccrual loans as a percentage of total loans	0.37%	0.42%
Nonperforming assets as a percentage of total loans and other property owned	0.78%	0.86%
Nonperforming assets as a percentage of capital	<u>6.92%</u>	<u>8.07%</u>

The following table presents information relating to impaired loans (including accrued interest) at March 31, 2012 and December 31, 2011. Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms of the loan.

<i>(dollars in thousands)</i>	<b>March 31, 2012</b>	<b>December 31, 2011</b>
<b>Impaired nonaccrual loans:</b>		
Current as to principal and interest	\$ 13,482	\$ 16,133
Past due	58,891	69,089
Total impaired nonaccrual loans	<u>72,373</u>	<u>85,222</u>
<b>Impaired accrual loans:</b>		
Restructured	34,370	38,757
90 days or more past due	5,356	5,352
Total impaired accrual loans	<u>39,726</u>	<u>44,109</u>
Total impaired loans	<u>\$ 112,099</u>	<u>\$ 129,331</u>

Additional impaired loan information as of March 31, 2012 and December 31, 2011 is summarized as follows:

<i>(dollars in thousands)</i>	March 31, 2012			Three Months Ended March 31, 2012	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
<b>Impaired loans with a related allowance for credit losses:</b>					
Real estate mortgage	\$ 19,565	\$ 21,405	\$ 4,192	\$ 20,023	\$ —
Production and intermediate-term Agribusiness	18,677	24,385	4,155	19,116	45
Processing and marketing	3,314	3,817	1,050	3,392	8
Total agribusiness	3,314	3,817	1,050	3,392	8
Rural residential real estate	—	—	—	—	—
Other (including mission-related)	545	1,879	110	558	—
Total	\$ 42,101	\$ 51,486	\$ 9,507	\$ 43,089	\$ 53
<b>Impaired loans with no related allowance for credit losses:</b>					
Real estate mortgage	\$ 20,474	\$ 40,170	\$ —	\$ 24,112	\$ 75
Production and intermediate-term Agribusiness	23,174	37,909	—	21,263	98
Processing and marketing	18,942	20,079	—	21,037	282
Total agribusiness	18,942	20,079	—	21,037	282
Rural residential real estate	6,497	6,497	—	7,421	122
Other (including mission-related)	911	9,445	—	1,164	—
Total	\$ 69,998	\$ 114,100	\$ —	\$ 74,997	\$ 577
<b>Total impaired loans:</b>					
Real estate mortgage	\$ 40,039	\$ 61,575	\$ 4,192	\$ 44,135	\$ 75
Production and intermediate-term Agribusiness	41,851	62,294	4,155	40,379	143
Processing and marketing	22,256	23,896	1,050	24,429	290
Total agribusiness	22,256	23,896	1,050	24,429	290
Rural residential real estate	6,497	6,497	—	7,421	122
Other (including mission-related)	1,456	11,324	110	1,722	—
Total	\$ 112,099	\$ 165,586	\$ 9,507	\$ 118,086	\$ 630
<b>December 31, 2011</b>					
<i>(dollars in thousands)</i>	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
<b>Impaired loans with a related allowance for credit losses:</b>					
Real estate mortgage	\$ 19,149	\$ 22,763	\$ 3,851	\$ 21,932	\$ —
Production and intermediate-term Agribusiness	19,390	25,027	4,002	15,989	132
Processing and marketing	4,636	4,971	1,050	7,329	6
Total agribusiness	4,636	4,971	1,050	7,329	6
Energy/water and waste disposal	—	—	—	920	—
Rural residential real estate	104	104	36	52	—
Other (including mission-related)	542	1,879	110	932	—
Total	\$ 43,821	\$ 54,744	\$ 9,049	\$ 47,154	\$ 138
<b>Impaired loans with no related allowance for credit losses:</b>					
Real estate mortgage	\$ 26,077	\$ 45,426	\$ —	\$ 56,445	\$ 518
Production and intermediate-term Agribusiness	23,613	43,473	—	46,060	370
Loans to cooperatives	—	—	—	601	—
Processing and marketing	24,286	29,771	—	33,556	1,774
Total agribusiness	24,286	29,771	—	34,157	1,774
Energy/water and waste disposal	—	—	—	248	22
Rural residential real estate	10,176	10,055	—	6,710	161
Other (including mission-related)	1,358	9,641	—	1,390	—
Total	\$ 85,510	\$ 138,366	\$ —	\$ 145,010	\$ 2,845
<b>Total impaired loans:</b>					
Real estate mortgage	\$ 45,226	\$ 68,189	\$ 3,851	\$ 78,377	\$ 518
Production and intermediate-term Agribusiness	43,003	68,500	4,002	62,049	502
Loans to cooperatives	—	—	—	601	—
Processing and marketing	28,922	34,742	1,050	40,885	1,780
Total agribusiness	28,922	34,742	1,050	41,486	1,780
Energy/water and waste disposal	—	—	—	1,168	22
Rural residential real estate	10,280	10,159	36	6,762	161
Other (including mission-related)	1,900	11,520	110	2,322	—
Total	\$ 129,331	\$ 193,110	\$ 9,049	\$ 192,164	\$ 2,983

Unpaid principal balance represents the contractual principal balance of the loan.



There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at March 31, 2012 and December 31, 2011.

A summary of changes in the allowance for loan losses and period end recorded investment in loans at March 31, 2012 and December 31, 2011 follows:

<i>(dollars in thousands)</i>	March 31, 2012									
	Direct Note	Real Estate Mortgage	Production and Intermediate-term	Agribusiness	Communication	Energy and Water/Waste Disposal	Rural Residential Real Estate	Other (including mission related)	Total	
<b>Allowance for credit losses:</b>										
Balance at December 31, 2011	\$ -	\$ 8,882	\$ 12,654	\$ 4,974	\$ 233	\$ 305	\$ 37	\$ 629	\$ 27,714	
Charge-offs	-	(690)	(45)	-	-	-	-	(246)	(981)	
Recoveries	-	2,809	1,224	-	-	-	-	-	4,033	
Provision for loan losses	-	(2,015)	(1,164)	179	37	5	(36)	273	(2,721)	
Balance at March 31, 2012	\$ -	\$ 8,986	\$ 12,669	\$ 5,153	\$ 270	\$ 310	\$ 1	\$ 656	\$ 28,045	
March 31, 2012 allowance ending balance:										
Loans individually evaluated for impairment	\$ -	\$ 4,192	\$ 4,155	\$ 1,050	\$ -	\$ -	\$ -	\$ 110	\$ 9,507	
Loans collectively evaluated for impairment	\$ -	\$ 4,794	\$ 8,514	\$ 4,103	\$ 270	\$ 310	\$ 1	\$ 546	\$ 18,538	
<b>Recorded investment in loans outstanding:</b>										
Ending Balance at March 31, 2012	\$ 13,501,358	\$ 1,176,486	\$ 1,280,127	\$ 1,057,553	\$ 156,950	\$ 303,896	\$ 2,091,189	\$ 20,121	\$ 19,587,680	
March 31, 2012 recorded investment ending balance:										
Loans individually evaluated for impairment	\$ 13,501,358	\$ 141,957	\$ 28,997	\$ 3,318	\$ -	\$ -	\$ 2,090,929	\$ 1,471	\$ 15,768,030	
Loans collectively evaluated for impairment	\$ -	\$ 1,034,529	\$ 1,251,130	\$ 1,054,235	\$ 156,950	\$ 303,896	\$ 260	\$ 18,650	\$ 3,819,650	

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December 31, 2011

<i>(dollars in thousands)</i>	Direct Note	Real Estate Mortgage	Production and Intermediate-term	Agribusiness	Communication	Energy and Water/Waste Disposal	Rural Residential Real Estate	Other (including mission related)	Total
<b>Allowance for credit losses:</b>									
Balance at December 31, 2010	\$ -	\$ 4,836	\$ 5,938	\$ 2,722	\$ 69	\$ 307	\$ -	\$ 1,001	\$ 14,873
Charge-offs	-	(24,572)	(26,023)	(3,847)	-	(3,218)	(36)	(10,083)	(67,779)
Recoveries	-	320	78	-	-	-	-	-	398
Provision for loan losses	-	28,298	32,661	6,099	164	3,216	73	9,711	80,222
Balance at December 31, 2011	\$ -	\$ 8,882	\$ 12,654	\$ 4,974	\$ 233	\$ 305	\$ 37	\$ 629	\$ 27,714

December 31, 2011 allowance ending balance:

Loans individually evaluated for impairment	\$ -	\$ 3,851	\$ 4,002	\$ 1,050	\$ -	\$ -	\$ 36	\$ 110	\$ 9,049
Loans collectively evaluated for impairment	\$ -	\$ 5,031	\$ 8,652	\$ 3,924	\$ 233	\$ 305	\$ 1	\$ 519	\$ 18,665

**Recorded investment in loans outstanding:**

Ending Balance at December 31, 2011	\$ 14,126,861	\$ 1,216,171	\$ 1,390,512	\$ 977,466	\$ 137,126	\$ 276,488	\$ 2,066,197	\$ 22,429	\$ 20,213,250
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December 31, 2011 recorded investment ending balance:

Loans individually evaluated for impairment	\$ 14,126,861	\$ 137,024	\$ 27,206	\$ 4,317	\$ -	\$ -	\$ 2,065,928	\$ 1,517	\$ 16,362,853
Loans collectively evaluated for impairment	\$ -	\$ 1,079,147	\$ 1,363,306	\$ 973,149	\$ 137,126	\$ 276,488	\$ 269	\$ 20,912	\$ 3,850,397

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The following tables present additional information about activity that occurred during the periods presented, related to TDRs. The table does not include purchased credit impaired loans.

**Three months ended March 31, 2012**

	Pre-modification Outstanding Recorded Investment			Total
	Interest Concessions	Principal Concessions	Other Concessions	
<b>Troubled debt restructurings:</b>				
Real estate mortgage	\$ -	\$ 564	\$ -	\$ 564
Total	\$ -	\$ 564	\$ -	\$ 564

**Three months ended March 31, 2012**

	Post-modification Outstanding Recorded Investment			Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Provisions	Charge-offs
<b>Troubled debt restructurings:</b>					
Real estate mortgage	\$ -	\$ 564	\$ -	\$ -	\$ -
Total	\$ -	\$ 564	\$ -	\$ -	\$ -

**Three months ended March 31, 2011**

	Pre-modification Outstanding Recorded Investment			Total
	Interest Concessions	Principal Concessions	Other Concessions	
<b>Troubled debt restructurings:</b>				
Production and intermediate-term	\$ -	\$ 16,373	\$ -	\$ 16,373
Total	\$ -	\$ 16,373	\$ -	\$ 16,373

	Three months ended March 31, 2011				Effects of Modification	
	Post-modification Outstanding Recorded Investment				Provisions	Charge-offs
	Interest Concessions	Principal Concessions	Other Concessions	Total		
<b>Troubled debt restructurings:</b>						
Production and intermediate-term	\$ -	\$ 16,373	\$ -	\$ 16,373	\$ (423)	\$ 423
Total	\$ -	\$ 16,373	\$ -	\$ 16,373	\$ (423)	\$ 423

Interest concessions include interest forgiveness and interest deferment. Principal concessions include principal forgiveness, principal deferment, and maturity extension. Other concessions include additional compensation received which might be in the form of cash or other assets.

The following table presents information regarding TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the first quarter of 2012. Payment default is defined as a payment that was thirty days or more past due.

	Outstanding Recorded Investment at March 31, 2012	
<b>Defaulted troubled debt restructurings:</b>		
Real estate mortgage	\$	562
Production and intermediate-term		12,020
Total	\$	12,582

TDRs outstanding at period end totaled \$61,152, of which \$26,782 were in nonaccrual status.

#### NOTE 4 — FAIR VALUE MEASUREMENT

ASC Topic 820 “Fair Value Measurement” defines fair value, establishes a framework for measuring fair value, and requires fair value disclosures for certain assets and liabilities. For the Bank, these assets and liabilities consist primarily of investments available-for-sale, highly-liquid funds, derivative assets and liabilities, assets held in trust funds, standby letters of credit, impaired loans, other property owned, and collateral liabilities.

This guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability.

The guidance also establishes a fair value hierarchy for disclosure of fair value measurements to maximize the use of observable inputs, that is, inputs that reflect the assumptions market participants would use in pricing an asset or liability based on market data obtained from sources independent of the reporting entity. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument’s categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The three levels of inputs and the classification of the Bank’s assets and liabilities within the fair value hierarchy are as follows:

##### Level 1

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. Level 1 assets and liabilities could include investment securities and derivative contracts that are traded in an active exchange market, in addition to certain U.S. Treasury securities that are highly-liquid and are actively traded in over-the-counter markets.

Level 1 assets consist of assets held in trust funds related to deferred compensation and supplemental retirement plans. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

For cash and cash equivalents, the carrying value is primarily utilized as a reasonable estimate of fair value.

## **Level 2**

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability. Level 2 assets and liabilities could include investment securities that are traded in active, non-exchange markets and derivative contracts that are traded in active, over-the-counter markets.

The fair value of substantially all investment securities is determined from third-party valuation services that estimate current market prices. Inputs and assumptions related to third-party market valuation services are typically observable in the marketplace. Such services incorporate prepayment assumptions and underlying mortgage- or asset-backed collateral information to generate cash flows that are discounted using appropriate benchmark interest rate curves and volatilities. Third-party valuations also incorporate information regarding broker/dealer quotes, available trade information, historical cash flows, credit ratings, and other market information. Such valuations represent an estimated exit price, or price to be received by a seller in active markets to sell the investment securities to a willing participant.

Level 2 assets include investments in U.S. government and agency mortgage-backed securities and U.S. agency debt securities, all of which have unadjusted values from third-party or internal pricing models. The underlying loans for these investment securities are residential mortgages. Also included are federal funds sold, securities purchased under resale agreements, and other highly-liquid funds, all of which are non-exchange-traded instruments. The market value of these federal funds sold and other instruments is generally their face value, plus accrued interest, as these instruments are highly-liquid, readily convertible to cash, and short-term in nature.

The fair value of derivative financial instruments is the estimated amount to be received to sell a derivative asset or paid to transfer a derivative liability in active markets among willing participants at the reporting date. Estimated fair values are determined through internal market valuation models which use an income approach. These models incorporate benchmark interest rate curves (primarily the LIBOR swap curve), potential volatilities of future interest rate movements, and other inputs which are observable directly or indirectly in the marketplace. The Bank compares internally calculated derivative valuations to broker/dealer quotes to substantiate the results.

Collateral liabilities are also considered Level 2. The majority of derivative contracts are supported by bilateral collateral agreements with counterparties requiring the posting of collateral in the event certain dollar thresholds of credit exposure are reached. Face value plus accrued interest approximates the fair value of collateral liabilities.

The carrying value of accrued interest approximates its fair value.

## **Level 3**

Level 3 inputs to the valuation methodology are unobservable and supported by little or no market activity. Level 3 assets and liabilities could include investments and derivative contracts whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, and other instruments for which the determination of fair value requires significant management judgment or estimation. Level 3 assets and liabilities could also include investments and derivative contracts whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

Because no active market exists for the Bank's loans, fair value is estimated by discounting the expected future cash flows using interest rates at which similar loans would currently be made to borrowers with similar credit risk.

For purposes of determining fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool. Fair values of loans in a nonaccrual status are estimated to be the carrying amount of the loan less specific reserves.

Certain loans evaluated for impairment under FASB guidance have fair values based upon the underlying collateral, as the loans were collateral-dependent loans. Since the value of the collateral, less estimated cost to sell, was less than the principal balance of the loan, specific reserves were established for these loans. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy.

The Bank's mortgage-related asset-backed investment portfolio and non-agency CMO investment portfolio are also considered Level 3. The underlying loans for the asset-backed securities are mortgage related. The underlying loans for the non-agency CMO securities are residential mortgages. Based on the currently illiquid marketplace for these investments and the lack of marketplace information available as inputs and assumptions to the valuation process, the Bank classified the mortgage-related asset-backed investment portfolio and non-agency CMO investment portfolio as Level 3 assets. The fair value measurement of these assets involved management's judgment and was based on multiple factors, including information obtained from third-party valuation services using both Level 2 and Level 3 inputs. The significant inputs for the valuation models include yields, probability of default, loss severity, and prepayment rates.

For other investments, fair value is estimated by discounting future annual cash flows using prevailing rates for similar instruments at the measurement date.

Other property owned is classified as a Level 3 asset. The fair value for other property owned is determined by the collateral fair value. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned. Other property owned consists primarily of real and personal property acquired through foreclosure or deed in lieu of foreclosure and is carried as an asset held for sale, which is generally not its highest and best use. These properties are part of the Bank's credit risk mitigation efforts, not its ongoing business. In addition, FCA regulations require that these types of property be disposed of within a reasonable period of time.

Systemwide Debt Securities are not all traded in the secondary market and those that are traded may not have readily available quoted market prices. Therefore, the fair value of the instruments is estimated by calculating the discounted value of the expected future cash flows. The discount rates used are based on the sum of quoted market yields for the Treasury yield curve and an estimated yield-spread relationship between Systemwide Debt Securities and Treasury securities. An appropriate yield-spread is estimated, taking into consideration selling group member (banks and securities dealers) yield indications, observed new GSE debt security pricing, and pricing levels in the related U.S. Dollar (USD) interest rate swap market.

The following tables present the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the periods presented. The Bank had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the reporting period.

<i>(dollars in thousands)</i>	<b>Asset-Backed Investment Securities</b>	<b>Non- Agency CMOs</b>	<b>Standby Letters Of Credit</b>
Balance at January 1, 2012	\$ 30,324	\$ 241,756	\$ 1,787
Total gains or (losses) realized/unrealized:			
Included in earnings	-	(750)	-
Included in other comprehensive income (loss)	(341)	3,052	-
Purchases	-	-	-
Sales	-	-	-
Issuances	-	-	30
Settlements	(1,104)	(10,680)	-
Transfers in and/or out of level 3	-	-	-
Balance at March 31, 2012	<u>\$ 28,879</u>	<u>\$ 233,378</u>	<u>\$ 1,817</u>

<i>(dollars in thousands)</i>	Asset-Backed Investment Securities	Non- Agency CMOs	Standby Letters Of Credit
Balance at January 1, 2011	\$ 34,437	\$ 295,526	\$ 1,263
Total gains or (losses) realized/unrealized:			
Included in earnings	(2,151)	(2,307)	-
Included in other comprehensive income (loss)	(193)	4,719	-
Purchases	-	-	-
Sales	-	-	-
Issuances	-	-	1,110
Settlements	(1,287)	(24,242)	-
Transfers in and/or out of level 3	-	-	-
Balance at March 31, 2011	\$ 30,806	\$ 273,696	\$ 2,373

### Sensitivity to Changes in Significant Unobservable Inputs

For recurring fair value measurements categorized within Level 3 of the fair value hierarchy, the significant unobservable inputs used in the fair value measurement of the residential mortgage-backed securities are prepayment rates, probability of default, and loss severity in the event of default. Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value measurement.

Generally, a change in the assumption used for the probability of default is accompanied by a directionally similar change in the assumption used for the loss severity and a directionally opposite change in the assumption used for prepayment rates.

Management determines the Bank's valuation policies and procedures. Internal valuation processes are calibrated annually by an independent consultant. Fair value measurements are analyzed on a periodic basis. Documentation is obtained for third party information, such as pricing, and periodically evaluated alongside internal information and pricing.

Quoted market prices are generally not available for the instruments presented below. Accordingly, fair values are based on judgments regarding anticipated cash flows, future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

#### Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Valuation Technique(s)	Unobservable Input	Range
Non-Agency CMOs, Asset-Backed Securities	Discounted cash flow	Prepayment forecasts	2.7% – 20.4%
		Probability of default	1.5% – 82.5%
		Loss severity	4.5% – 100%
Firm commitments-when issued securities	Broker/Consensus pricing	Offered quotes	103.101 – 104.209
Mission Related Investments	Discounted cash flow	Probability of default	0% – 16%
		Risk adjusted discount rate	2.00% – 8.25%
Impaired loans and other property owned	Appraisal	Income and expense	*
		Comparable sales	*
		Replacement cost	*
		Comparability adjustments	*

\* Ranges for this type of input are not useful because each collateral property is unique.

**Information about Recurring and Nonrecurring Level 2 Fair Value Measurements**

	<b>Valuation Technique(s)</b>	<b>Input</b>
Investments available for sale	Discounted cash flow	Constant prepayment rate Probability of default Loss severity
	Quoted prices	Price for similar security
Federal funds sold, securities purchased under resale agreements and other	Carrying value	Par/principal and appropriate interest yield
Interest rate swaps	Discounted cash flow	Annualized volatility Counterparty credit risk Own credit risk

**Information about Other Financial Instrument Fair Value Measurements**

	<b>Valuation Technique(s)</b>	<b>Input</b>
Loans	Discounted cash flow	Prepayment forecasts Probability of default Loss severity
Cash and cash equivalents	Carrying value	Par/principal and appropriate interest yield
Other investments	Discounted cash flow	Prepayment rate Probability of default Loss severity
Accrued interest	Carrying value	Coupon interest rates
Assets held in trust funds	Carrying value	Par/principal and appropriate interest yield
Bonds and notes	Discounted cash flow	Benchmark yield curve Derived yield spread Own credit risk
Cash collateral	Carrying value	Par/principal and appropriate interest yield

The following table presents the carrying amounts and fair values of assets and liabilities that are measured at fair value on a recurring and nonrecurring basis, as well as, those financial instruments not measured at fair value, for each of the hierarchy levels at the period ended:

	March 31, 2012					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On comprehensive Income
<b>Recurring Measurements</b>						
<b>Assets:</b>						
Investments available-for-sale:						
U.S. Govt. GNMA MBS/CMOs	\$ 4,961,566	\$ —	\$ 4,961,566	\$ —	\$ 4,961,566	\$ —
U.S. Govt. Agency MBS	1,649,877	—	1,649,877	—	1,649,877	—
Non-Agency CMOs	233,378	—	—	233,378	233,378	—
Commercial MBS	—	—	—	—	—	—
Asset-backed securities	28,879	—	—	28,879	28,879	—
Mission Related Investments	—	—	—	—	—	—
Total investments available-for-sale	6,873,700	—	6,611,443	262,257	6,873,700	—
Commercial paper, bankers' acceptances, CD's & others	—	—	—	—	—	—
Federal funds sold, securities purchased under resale agreements, and other	83,795	—	83,795	—	83,795	—
Interest rate swaps and other financial instruments	49,127	—	49,127	—	49,127	—
Assets held in trust funds	3,597	3,597	—	—	3,597	—
Recurring Assets	\$ 7,010,219	\$ 3,597	\$ 6,744,365	\$ 262,257	\$ 7,010,219	\$ —
<b>Liabilities:</b>						
Interest rate swaps and other financial instruments	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Collateral liabilities	1,359	—	1,359	—	1,359	—
Standby letters of credit	1,817	—	—	1,817	1,817	—
Recurring Liabilities	\$ 3,176	\$ —	\$ 1,359	\$ 1,817	\$ 3,176	\$ —
<b>Nonrecurring Measurements</b>						
<b>Assets:</b>						
Impaired loans	\$ 102,592	\$ —	\$ —	\$ 102,592	\$ 102,592	\$ 2,594
Other property owned	40,383	—	—	43,982	43,982	(3,301)
Nonrecurring Assets	\$ 142,975	\$ —	\$ —	\$ 146,574	\$ 146,574	\$ (707)
<b>Other Financial Instruments</b>						
<b>Assets:</b>						
Cash	\$ 586,610	\$ 586,610	\$ —	\$ —	\$ 586,610	\$ —
Investments held to maturity	795,612	862,251	—	—	862,251	—
Loans	19,395,108	—	—	19,469,605	19,469,605	—
Other investments	—	—	—	—	—	—
Accrued interest receivable	79,532	—	79,532	—	79,532	—
Other Assets	\$ 20,856,862	\$ 1,448,861	\$ 79,532	\$ 19,469,605	\$ 20,997,998	\$ —
<b>Liabilities:</b>						
Systemwide debt securities	\$ 25,765,545	\$ —	\$ —	\$ 25,841,082	\$ 25,841,082	\$ —
Accrued interest payable	37,194	—	37,194	—	37,194	—
Derivative liabilities	—	—	—	—	—	—
Other Liabilities	\$ 25,802,739	\$ —	\$ 37,194	\$ 25,841,082	\$ 25,878,276	\$ —



The following table presents the assets and liabilities that are measured at fair value on a recurring basis for each of the fair value hierarchy levels at the period ended:

<i>(dollars in thousands)</i>	December 31, 2011			
	Level 1	Level 2	Level 3	Total Fair Value
<b>Assets:</b>				
Investments Available-for-sale:				
U.S. Govt. GNMA MBS/CMOs	\$ —	\$ 5,002,501	\$ —	\$ 5,002,501
U.S. Govt. Agency MBS	—	1,650,829	—	1,650,829
Non-Agency CMOs	—	—	241,756	241,756
Commercial MBS	—	—	—	—
Asset-Backed Securities	—	—	30,324	30,324
Mission Related Investments	—	—	—	—
Total Investments Available-for-sale	—	6,653,330	272,080	6,925,410
Commercial paper, Bankers' Acceptances, CD's & Others	—	—	—	—
Federal funds sold, securities purchased under resale agreements, and other	—	83,822	—	83,822
Interest rate swaps and other financial instruments	—	52,647	—	52,647
Assets held in trust funds	3,151	—	—	3,151
Total Assets	\$ 3,151	\$ 6,789,799	\$ 272,080	\$ 7,065,030
<b>Liabilities:</b>				
Interest rate swaps and other financial instruments	\$ —	\$ —	\$ —	\$ —
Collateral liabilities	—	22,139	—	22,139
Standby letters of credit	—	—	1,787	1,787
Total Liabilities	\$ —	\$ 22,139	\$ 1,787	\$ 23,926

Assets and liabilities measured at fair value on a non-recurring basis at period end for each of the fair value hierarchy levels are summarized below:

<i>(dollars in thousands)</i>	December 31, 2011				
	Level 1	Level 2	Level 3	Total Fair Value	Total Gains (Losses)
<b>Assets:</b>					
Impaired loans *	\$ —	\$ —	\$ 34,771	\$ 34,771	\$ (71,913)
Other property owned *	\$ —	\$ —	\$ 48,014	\$ 48,014	\$ (11,402)

\* In accordance with FASB guidance in effect at December 31, 2011, amounts include only those assets remeasured during the reporting period. Total impaired loans at period end were \$120,282 and other property owned was \$48,014.

The following table presents the carrying amounts and fair values of the Bank's financial instruments at December 31, 2011. Carrying amounts include accrued interest if applicable.

<i>(dollars in thousands)</i>	December 31, 2011	
	Carrying Amount	Estimated Fair Value
<b>Financial assets:</b>		
Loans, net of allowance	\$ 20,124,352	\$ 20,406,083
Derivative assets	\$ 52,647	\$ 52,647
Cash & cash equivalents	\$ 1,301,569	\$ 1,301,569
Investment securities	\$ 7,780,272	\$ 7,835,742
Accrued interest receivable	\$ 78,906	\$ 78,906
Assets held in trust funds	\$ 3,151	\$ 3,151
<b>Financial liabilities:</b>		
Bonds and notes	\$ 27,128,566	\$ 27,263,779
Derivative liabilities	\$ —	\$ —

**NOTE 5 — COMMITMENTS AND CONTINGENT LIABILITIES**

Under the Farm Credit Act of 1971, each Farm Credit System (System) bank is primarily liable for its portion of Systemwide bond and discount note obligations. Additionally, the banks are jointly and severally liable for the bonds and notes of the other System banks. The bonds and notes of the System totaled \$186.650 billion at March 31, 2012.

There are no material claims pending against the Bank in which money damages are asserted.

**NOTE 6 — EMPLOYEE BENEFIT PLANS**

The following is a table of retirement and other postretirement benefit expenses for the Bank:

<i>(dollars in thousands)</i>	<b>For the three months ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
Pension	\$ 2,478	\$ 2,431
401k	300	279
Other postretirement benefits	223	295
Total	\$ 3,001	\$ 3,005

The following is a table of retirement and other postretirement benefit contributions for the Bank. Projections are based upon actuarially determined amounts as of the most recent measurement date of December 31, 2011.

<i>(dollars in thousands)</i>	<b>Actual YTD Through 3/31/12</b>	<b>Projected Contributions for Remainder of 2012</b>	<b>Projected Total Contributions 2012</b>
Pensions	\$ 73	\$ 7,121	\$ 7,194
Other postretirement benefits	252	731	983
Total	\$ 325	\$ 7,852	\$ 8,177

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the Bank participates. These amounts may change when a total funding amount and allocation is determined by the respective Plans' Sponsor Committees. Also, market conditions could impact discount rates and return on plan assets which could change contributions necessary before the next plan measurement date of December 31, 2012.

Further details regarding employee benefit plans are contained in the 2011 Annual Report to Shareholders.

**NOTE 7 – DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES**

The Bank's goal is to minimize interest rate sensitivity by managing the repricing characteristics of assets and liabilities so that the net interest margin is not adversely affected by movements in interest rates. The Bank maintains an overall interest rate risk management strategy that may incorporate the use of derivative instruments to lower cost of funding or to reduce interest rate risk. Currently, the primary derivative type used by the Bank is interest rate swaps, which convert fixed interest rate debt to a lower floating interest rate than was achievable from issuing floating rate debt with identical repricing characteristics. They may allow the Bank to lower funding costs, allow it to diversify sources of funding, or alter interest rate exposures arising from mismatches between assets and liabilities. Interest rate swaps enable the Bank to raise long-term borrowings at fixed rates and swap them into floating rates that are lower than those available to the Bank if floating rate borrowings were made directly. Under these arrangements, the Bank agrees with other parties to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating rate index.

The Bank may also purchase interest rate derivatives such as caps, in order to reduce the impact of rising interest rates on its floating-rate debt, and floors, in order to reduce the impact of falling interest rates on its floating-rate assets. In addition, the Bank may also fix a price to be paid in the future which qualifies as a derivative forward contract.

As a result of interest rate fluctuations, interest income and interest expense related to hedged variable-rate assets and liabilities, respectively, will increase or decrease. Another result of interest rate fluctuations is that hedged fixed-rate assets and liabilities will appreciate or depreciate in market value. The effects of any earnings variability or unrealized changes in market value are expected to be substantially offset by the Bank's gains or losses on the derivative instruments that are linked to these hedged assets and liabilities. The Bank considers its strategic use of derivatives to be a prudent method of managing interest rate sensitivity, as it prevents earnings from being exposed to undue risk posed by changes in interest rates.

The primary types of derivative instrument used and the amount of activity for the three months ended March 31, 2012 is summarized in the following table:

<b>Notional Amounts</b> <i>(dollars in millions)</i>	<b>Receive-Fixed</b> <b>Swaps</b>	<b>Forward</b> <b>Contracts</b>
Balance at beginning of period	\$ 535	\$ 66
Additions	-	-
Maturities/amortization	-	(66)
Terminations	-	-
Balance at end of period	<u>\$ 535</u>	<u>\$ -</u>

By using derivative instruments, the Bank exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, the Bank's credit risk will equal the fair value gain in the derivative. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes the Bank, thus creating a repayment risk for the Bank. When the fair value of the derivative contract is negative, the Bank owes the counterparty and, therefore, assumes no repayment risk.

To minimize the risk of credit losses, the Bank deals with counterparties that have an investment grade credit rating from a major rating agency and also monitors the credit standing of and levels of exposure to individual counterparties. The estimated gross credit risk exposure at March 31, 2012 of \$49.1 million was with five counterparties and represented approximately 9.18 percent of the total notional amount of interest rate swaps. The Bank held \$1.4 million of interest-bearing cash collateral and US Treasury securities with a fair value of \$19.5 million, posted by one counterparty related to these swaps. The Bank does not anticipate nonperformance by any of these counterparties. The estimated gross credit risk exposure at December 31, 2011 of \$52.3 million was with five counterparties and represented approximately 9.78 percent of the total notional amount of interest rate swaps. The Bank held \$22.1 million of interest-bearing cash collateral posted by one counterparty related to these swaps. The Bank typically enters into master agreements that contain netting provisions. These provisions allow the Bank to require the net settlement of covered contracts with the same counterparty in the event of default by the counterparty on one or more contracts. A number of swaps are supported by collateral arrangements with counterparties. At period end, the Bank had not posted collateral with respect to any of these arrangements.

The Bank's derivative activities are monitored by its Asset-Liability Management Committee (ALCO) as part of the Committee's oversight of the Bank's asset/liability and treasury functions. The Bank's ALCO is responsible for approving hedging strategies that are developed within parameters established by the Bank's Board of Directors through the Bank's analysis of data derived from financial simulation models and other internal and industry sources. The resulting hedging strategies are then incorporated into the Bank's overall interest rate risk-management strategies.

### **Fair-Value Hedges**

For derivative instruments designated as fair value hedges, the gains or losses on the derivative, as well as the offsetting loss or gain on the hedged item attributable to the hedged risk, are recognized in current earnings. The Bank includes the gain or loss on the hedged items in the same line item (interest expense) as the offsetting loss or gain on the related interest rate swaps. The amount of the loss on interest rate swaps recognized in interest expense for the three months ended March 31, 2012 was \$3.5 million, while the amount of the gain on the Systemwide Debt

Securities was \$3.5 million. The amount of the gain on interest rate swaps recognized in interest expense for the three months ended March 31, 2011 was \$11.1 million, while the amount of the loss on the Systemwide Debt Securities was \$11.1 million. Gains and losses on each derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

### Cash Flow Hedges

From time to time, the Bank may acquire when-issued securities, generally Government National Mortgage Association (GNMA) bonds. The when-issued transactions are contracts to purchase securities that will not be delivered until 30, or more, days in the future. These purchase commitments are considered derivatives (cash flow hedges) in the form of forward contracts. Changes in market value of the contracted securities, between purchase and settlement date, represent the effective portion of the Bank's forward contracts. These amounts are included in Other Comprehensive Income (OCI), and Other Liabilities or Other Assets as appropriate, as firm commitments in the Bank's Balance Sheet for each period end. The Bank had no commitments to purchase GNMA bonds at March 31, 2012. At December 31, 2011, the Bank had committed to purchase \$66.4 million in when-issued GNMA bonds that had a market value of \$66.7 million, a \$319 thousand increase in value.

For derivative instruments that are designated and qualify as a cash flow hedge, such as the Bank's forward contracts, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

### Fair Values of Derivative Instruments

The following tables represent the fair value of derivative instruments at March 31, 2012 and December 31, 2011:

<i>(dollars in thousands)</i>	Balance Sheet Classification – Assets	3/31/12 Fair Value	Balance Sheet Classification – Liabilities	3/31/12 Fair Value
<b>Derivatives designated as hedging instruments:</b>				
Receive-fixed swaps	Other Assets	\$ 49,127	Other Liabilities	\$ –
Forward contracts	Other Assets	–	Other Liabilities	–
Total		\$ 49,127		\$ –

<i>(dollars in thousands)</i>	Balance Sheet Classification – Assets	12/31/11 Fair Value	Balance Sheet Classification – Liabilities	12/31/11 Fair Value
<b>Derivatives designated as hedging instruments:</b>				
Receive-fixed swaps	Other Assets	\$ 52,328	Other Liabilities	\$ –
Forward contracts	Other Assets	319	Other Liabilities	–
Total		\$ 52,647		\$ –

The following table sets forth the amount of net gain (loss) recognized in the Statements of Income for the three months ended March 31, 2012 and 2011.

<i>(dollars in thousands)</i>	Location of Gain or (Loss) Recognized in the Statement of Income	2012 Amount of Gain or (Loss) Recognized in the Statement of Income	2011 Amount of Gain or (Loss) Recognized in the Statement of Income
<b>Derivatives – Fair Value Hedging Relationships:</b>			
Receive-fixed swaps	Noninterest Income	\$ –	\$ –
Total		\$ –	\$ –

The following table sets forth the amount of net gain (loss) recognized in the Statements of Income for the three months ended March 31, 2012 and 2011 and the amount of net gain (loss) recognized in the Balance Sheets for March 31, 2012 and December 31, 2011.

<i>(dollars in thousands)</i>	Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)		Location of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)		Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	
	2012	2011		2012	2011		2012	2011
<b>Derivatives – Cash Flow Hedging Relationships:</b>								
Firm Commitments	\$ 803	\$ (1,868)	Interest Income	\$ 148	\$ (116)	Interest Income	\$ –	\$ –

## NOTE 8 – PERPETUAL PREFERRED STOCK

During the first quarter of 2012, the Bank repurchased, through privately negotiated transactions, and cancelled Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock with a par value of \$110.6 million. The effect of the repurchases on shareholders' equity was to reduce preferred stock outstanding by \$110.6 million and record \$31.9 million of additional paid-in-capital. Subsequent to quarter-end, the Bank repurchased and cancelled additional shares of Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock with a par value of \$8.0 million. The effect of this transaction was to reduce preferred stock outstanding by \$8.0 million and increase additional paid-in-capital by \$2.2 million.

## NOTE 9 - ACCUMULATED OTHER COMPREHENSIVE INCOME

Changes in components of Accumulated Other Comprehensive Income are as follows:

<i>(dollars in thousands)</i>	Unrealized gains (losses) on Investments	Firm Commitments	Employee Benefit Plans	Accumulated Other Comprehensive Income
Balance at December 31, 2010	\$ 43,703	\$ (8,751)	\$ (2,623)	\$ 32,329
Other comprehensive income	(16,959)	(1,752)	(71)	(18,782)
Balance at March 31, 2011	26,744	(10,503)	(2,694)	13,547
Balance at December 31, 2011	132,825	(5,565)	(3,263)	123,997
Other comprehensive income	13,163	655	(116)	13,702
Balance at March 31, 2012	\$ 145,988	\$ (4,910)	\$ (3,379)	\$ 137,699

<i>(dollars in thousands)</i>	For the three months ended March 31,	
	2012	2011
<b>Other Comprehensive Income and Reclassification Amounts:</b>		
Unrealized holding gains (losses) for period	\$ 12,413	\$ (21,417)
Amounts reclassified to (gains) losses in net income		
Amounts reclassified to other-than-temporary impairment in net income	750	4,458
Unrealized gains (losses) on securities, net	13,163	(16,959)
Change in value of cash flow hedges	803	(1,868)
Amounts reclassified to net income	(148)	116
Other	–	–
Change associated with cash flow hedges, net	655	(1,752)
Amounts reclassified to net periodic pension costs	113	77
Net gain (loss) during period	(229)	(148)
Defined benefit post retirement plans, net	\$ (116)	\$ (71)

**NOTE 10 – DISTRICT MERGER ACTIVITY**

In February 2012, the Boards of Directors of Jackson Purchase, ACA and Chattanooga, ACA (collectively referred to as the “Merger Associations”) approved a proposed Plan of Merger (“Merger”). AgFirst Farm Credit Bank has approved the merger and FCA has granted preliminary approval. The Merger will be submitted to shareholders of the Merger Associations for their review and approval. Pending the remaining necessary approvals, including final approval from FCA, the Merger is anticipated to be effective July 1, 2012. The Merger will be accounted for under the acquisition method of accounting guidance.

**NOTE 11 – SUBSEQUENT EVENTS**

The Bank has evaluated subsequent events and has determined that, except as described below, there are none requiring disclosure through May 9, 2012, which is the date the financial statements were issued.

In April 2012, the Bank accrued a \$10.0 million insurance premium refund from the Farm Credit System Insurance Corporation (FCSIC), which insures the System’s debt obligations. This payment is nonrecurring and resulted from the assets of the Farm Credit Insurance Fund exceeding the secure base amount as defined by the Farm Credit Act.