Quarterly Report

Second quarter 2012

AgFirst Farm Credit Bank
and District Associations

Farm Credit
Lending support to rural America™

SECOND QUARTER 2012

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CERTIFICATION

The undersigned certify that we have reviewed the June 30, 2012 quarterly report of AgFirst Farm Credit Bank and District Associations, 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
M. Wayne Lambertson
Chairman of the Board

Leon T. Amerson
Leon T. Amerson
Chief Executive Officer & President

Charl L. Butler
Charl L. Butler
Chief Financial Officer

August 8, 2012

Report on Internal Control Over Financial Reporting

AgFirst Farm Credit Bank (Bank) and each affiliated District Agricultural Credit Association's (District Association) 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 and each District Association's respective Consolidated 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 and each District Association'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 respective Consolidated 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 and each District Association, (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 each District Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Bank and each District Association's assets that could have a material effect on its Consolidated Financial Statements.

The Bank and each District Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of June 30, 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 and each District Association concluded that as of June 30, 2012, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Bank and each District Association determined that there were no material weaknesses in the internal control over financial reporting as of June 30, 2012.

Leon T. Amerson
Chief Executive Officer & President

Charl L. Butler
Chief Financial Officer

August 8, 2012

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

The following discussion reviews the combined financial condition and results of operations of AgFirst Farm Credit Bank (AgFirst or Bank) and the District Agricultural Credit Associations (Associations or District Associations), collectively referred to as the District, as of and for the three and six month periods ended June 30, 2012. These comments should be read in conjunction with the accompanying financial statements, the Notes to the Combined Financial Statements, and the 2011 Annual Report of AgFirst Farm Credit Bank and District Associations. The accompanying combined financial statements were prepared under the oversight of the Audit Committee of the AgFirst Board of Directors.

As of June 30, 2012, the District included twenty Associations, all of which were structured as Agricultural Credit Association (ACA) holding companies, with Federal Land Credit Association (FLCA) and Production Credit Association (PCA) subsidiaries. PCAs originate and service short- and intermediate-term loans; FLCAs originate and service long-term real estate mortgage loans; and ACAs originate both long-term and short- and intermediate-term loans. See Note 12, *District Merger Activity,* in the Notes to the Combined Financial Statements for further information.

Key ratios and data reported below, and in the accompanying financial statements, address the financial performance of the District. However, neither the three months nor the six months results of operations may be indicative of an entire year due to the seasonal nature of a portion of the District'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 the District's expectations and predictions due to a number of risks and uncertainties, many of which are beyond the District'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

The District's aggregate loan portfolio consists primarily of direct loans made by the Associations to eligible borrowers located within their chartered territories. Diversification of the loan volume by type is illustrated in the following table:

Loan Types *(dollars in thousands)*	**June 30, 2012**			**December 31, 2011**			**June 30, 2011**		
Real Estate Mortgage	$	9,748,030	43%	$	9,756,036	43%	$	9,879,533	43%
Production and Intermediate-Term		7,767,612	35		7,924,627	36		8,111,717	36
Rural Residential Real Estate		2,536,007	11		2,470,742	11		2,380,881	10
Agribusiness									
Loans to Cooperatives		244,650	1		256,981	1		336,066	2
Processing and Marketing		1,088,373	5		1,115,490	5		1,240,269	5
Farm-Related Business		384,193	2		348,797	2		322,522	2
Total Agribusiness		1,717,216	8		1,721,268	8		1,898,857	9
Energy		428,219	2		280,700	1		307,341	1
Communication		271,500	1		213,501	1		203,356	1
Water and Waste Disposal		28,021	–		28,022	–		28,022	–
Loans to OFIs		15,650	–		5,250	–		16,000	–
Lease Receivables		5,895	–		2,986	–		8,650	–
Other (including Mission Related)		65,047	–		78,373	–		81,215	–
Total	$	22,583,197	100%	$	22,481,505	100%	$	22,915,572	100%

Total loans outstanding were $22.583 billion at June 30, 2012, an increase of $104.7 million, or 0.45 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 some of the District's customers. As a result, some customers have reduced production and taken a deliberate approach to expansion plans, in order to preserve their investment and working capital. This remains most prevalent in the meat and timber sectors. Improved liquidity positions for grain farmers due to high grain prices have reduced their demand for credit. However, present drought conditions for portions of the District are negatively affecting current year crop production. The resolution of adversely classified loans has impacted loan volume as loans are charged down to their fair value when transitioned to nonaccrual status, liquidated through voluntary or foreclosure sales, or moved to other property owned. Management also targeted decreases for certain low performing portfolio sectors. 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:

Credit Quality as of:			
Classification	**June 30, 2012**	**December 31, 2011**	**June 30, 2011**
Acceptable	89.91%	88.50%	87.51%
OAEM *	4.54%	5.66%	6.04%
Substandard	5.52%	5.77%	6.27%
Doubtful/loss	0.03%	0.07%	0.18%

* *Other Assets Especially Mentioned*

Certain commodity groups continue to be more adversely affected than others 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 weakness in the 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 District'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 values have stabilized. 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 experienced losses and cash flow problems in 2011 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. The future volatility of grain prices remains a primary concern to the meat, dairy, and ethanol sectors. Beef and pork companies continue to project adequate results in 2012. The prospects of the meat complex remain reliant, however, on maintaining strong meat prices to cover higher and volatile feed costs. Feed prices are projected to increase based on significant drought problems in many portions of the corn and soybean production regions. Significant increases in grain prices may challenge the producers in the meat complex in late 2012 and 2013.

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. However, some areas are experiencing high temperatures and drought conditions. These negative crop conditions have led to lower grain production and higher grain prices. Row crop farmers in the drought affected areas could see crop losses; however, crop insurance protection will minimize the resulting financial losses.

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.

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 combined District at June 30, 2012, were $636.8 million compared to $666.7 million at December 31, 2011. Nonaccrual loans decreased $29.9 million during the six month period ended June 30, 2012 due primarily to repayments of $158.7 million, $39.1 million of charge-offs of uncollectible balances, transfers to other property owned of $45.1 million, and reinstatements to accrual status of $11.4 million. Offsetting these decreases were $193.9 million of loan balances transferred to nonaccrual status and advances of $18.1 million. The ten largest nonaccrual borrower relationships accounted for 20.51 percent of the total nonaccrual balance. At June 30, 2012, total nonaccrual loans were primarily in the forestry (23.01 percent of the total), nursery/greenhouse (21.19 percent), other real estate (8.49 percent), cattle (7.03 percent), poultry (7.01 percent), and fruits and vegetables (6.66 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 2.82 percent and 2.97 percent of total loans outstanding at June 30, 2012 and December 31, 2011, respectively.

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 and District Associations 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 and District Associations. Troubled debt restructurings totaled $250.3 million at June 30, 2012, compared to $267.8 million at December 31, 2011. At June 30, 2012, troubled debt restructurings were comprised of $75.8 million of accruing restructured loans and $174.5 million of nonaccruing restructured loans. Restructured loans were primarily in the forestry (27.66 percent of the total), nursery/greenhouse (10.97 percent), poultry (7.92 percent), other real estate (7.52 percent), cattle (6.79 percent), fruits and vegetables (6.56 percent), and processing segments.

Other Property Owned

Other property owned (OPO) consists primarily of assets once pledged as loan collateral that were acquired through foreclosure or deeded to the Bank and District Associations (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 $18.3 million during the first six months of 2012 and totaled $139.9 million at June 30, 2012. For the six months ended June 30, 2012, transfers to OPO were $46.9 million. Offsetting this increase were disposals of $46.1 million and write-downs of OPO of $19.1 million. The largest property write-down of $2.8 million was for a land holding in the forestry segment. At June 30, 2012, the largest OPO holding was an ethanol facility totaling $20.8 million (14.84 percent of the total).

Allowance for Loan Losses

The District 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 $175.1 million at June 30, 2012, as compared with $175.0 million at December 31, 2011. Activity in the allowance for the six months ended June 30, 2012 of $113 thousand included $25.0 million provision expense and recoveries of $14.6 million. Offsetting these increases were loan charge-offs of $39.5 million, as their collectability became more measurable and apparent during the six month period. Charge-offs during the six month period were related primarily to borrowers in the nursery/greenhouse (34.06 percent), forestry (15.27 percent), and cattle (13.38 percent) segments. The allowance at June 30, 2012 included specific reserves of $70.2 million (40.07 percent of the total) and $104.9 million (59.93 percent) of general reserves. The total allowance at June 30, 2012 was comprised primarily of reserves for the forestry (20.31 percent of the total), nursery/greenhouse (15.07 percent), poultry (7.57 percent), cattle (6.13 percent), and fruits/vegetables (6.11 percent) segments. Declining real estate values impacted charge-offs and reserves in many of these loan segments. See Note 3, *Loans and Allowance for Loan Losses*, in the Notes to the Combined 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 and any future negative changes to the System's credit ratings and/or outlook could increase borrowing costs and limit access to the debt capital markets. Any of these changes could 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 June 30, 2012, AgFirst had $26.465 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.

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. During the second quarter of 2012, AgFirst discontinued the $150.0 million unsecured committed line of credit facility from its primary commercial depository bank.

Cash and cash equivalents, which decreased $118.5 million from December 31, 2011 to a total of $1.222 billion at June 30, 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).

Investment securities totaled $7.543 billion, or 23.58 percent of total assets at June 30, 2012, compared to $7.956 billion, or 24.47 percent, as of December 31, 2011. Investment securities decreased $412.1 million (5.18 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 June 30, 2012, AgFirst exceeded all applicable regulatory liquidity requirements. Farm Credit Administration (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 June 30, 2012, AgFirst's coverage was 218 days, compared to 205 days at December 31, 2011. At June 30, 2012, the Bank's cash and cash equivalents position provided 24 days coverage and investment securities fully backed by the U.S. government provided an additional 194 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 218 days.

Investment securities classified as being available-for-sale totaled $6.691 billion at June 30, 2012. Available-for-sale investments at June 30, 2012 included $4.807 billion in Government National Mortgage Association (GNMA) securities backed by the full faith and credit of the U.S. Government, $1.589 billion in Agency mortgage backed securities, $209.3 million in non-agency collateralized mortgage obligations (CMOs), $53.3 million in Mission Related Investments, and $31.9 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.

The District 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 $852.9 million at June 30, 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 District must obtain specific approval from the FCA to continue to hold an ineligible security. For each of these investment securities in the District's portfolio at June 30, 2012 rated below AAA/Aaa (total fair value of $231.6 million and amortized cost of $288.3 million), the District has developed and submitted plans for approval by the FCA that permit the District to continue to hold the securities. The FCA has approved, with conditions, the District's plans for all but seven investments that have recently become ineligible. The District has submitted plans to hold these seven ineligible securities and is awaiting approval from the FCA. Management is of the opinion that holding these securities will result in a higher return for the District than liquidating them. Other-than-temporary credit related impairment of $293 thousand was recognized during the second quarter of 2012 on two of 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 District 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 $104.2 million and amortized cost of $128.4 million at June 30, 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 $57.3 million and amortized cost of $74.8 million at June 30, 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 $70.2 million and $85.1 million, respectively, at June 30, 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 $153.8 million at June 30, 2012, compared to $139.4 million at December 31, 2011. These net unrealized gains are reflected in Accumulated Other Comprehensive Income (AOCI) in the Combined Financial Statements. The net unrealized gains stem from normal market factors such as the current interest rate environment.

The District 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 District recognized other-than-temporary credit related impairment of $3.2 million on asset-backed securities and non-agency CMOs in its portfolio for the six months ended June 30, 2012, which was included in Net Other-Than-Temporary Impairment Losses on Investments in the Combined 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 $18.2 million life to date ($1.7 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 $18.4 million life to date ($3.2 million in 2012). Payment shortfalls on non-agency CMOs totaled $945 thousand life to date ($606 thousand in 2012). See Note 2, *Investment Securities*, in the Notes to the Combined Financial Statements for further information.

Following the market disruptions of 2008, the Bank began considering 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 estimating 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. Over time, the valuations received from the pricing service have converged toward a more reasonable correlation with our understanding of the underlying credit factors and financial metrics of these securities, though the markets remain inactive. Management believes that values supplied by the third party pricing service are currently sufficiently consistent with GAAP and that it is appropriate to return to the methodology used prior to 2009; that being the use of third party pricing alone to reflect the fair values of these portfolios in financial reporting. This methodology change resulted in a decrease of $13.8 million for the total combined fair value of these two portfolios at June 30, 2012.

The Bank reviews and periodically discusses with the third party pricing service 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.

Capital Resources

Total shareholders' equity increased $250.8 million (5.55 percent) from December 31, 2011 to a total of $4.772 billion at June 30, 2012. This increase is primarily attributed to 2012 unallocated retained earnings from net income of $356.8 million, increases of $14.4 million in net unrealized gains during 2012 on investments available-for-sale, and employee benefit plan adjustments of $14.5 million. Offsetting the increases were retained earnings retired of $28.3 million, patronage paid of $6.5 million, preferred stock dividend payments of $11.5 million, net capital stock and participation certificates retired of $5.6 million, and the redemption of preferred stock referenced below.

During the first half 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 $118.6 million. The effect of the repurchases on shareholders' equity was to reduce preferred stock outstanding by $118.6 million and record $34.1 million of additional paid-in-capital.

RESULTS OF OPERATIONS

Net income for the three months ended June 30, 2012 was $195.4 million, compared to $128.6 million for the same period of 2011, an increase of $66.9 million, or 52.00 percent. For the six months ended June 30, 2012, net income was $356.8 million, compared to $264.1 million for the same period of 2011, an increase of $92.7 million, or 35.08 percent.

Key results of operations comparisons

	Annualized for the six months ended June 30, 2012	For the year ended December 31, 2011	Annualized for the six months ended June 30, 2011
Return on average assets	2.26%	1.48%	1.62%
Return on average shareholders' equity	15.38%	10.93%	12.37%
Net interest income as a percentage of average earning assets	3.75%	3.57%	3.52%
Net (charge-offs) recoveries to average loans	(0.22)%	(0.91)%	(0.62)%

Net Interest Income

Net interest income for the three months ended June 30, 2012 was $283.6 million compared to $278.9 million for the same period of 2011, an increase of $4.7 million or 1.68 percent. For the six months ended June 30, 2012, net interest income was $567.1 million, compared to $549.5 million for the same period of 2011, an increase of $17.6 million, or 3.20 percent. The net interest margin was 3.74 percent in the current year three month period, an improvement of 19 basis points over the comparable period of 2011. The net interest margin was 3.75 percent in the current year six month period, an improvement of 23 basis points over the comparable 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, the positive impact on the net interest margin that the District has experienced over the last several years from calling debt will likely diminish.

The following table illustrates the changes in net interest income:

	For the three months ended June 30, 2012 vs. June 30, 2011			For the six months ended June 30, 2012 vs. June 30, 2011		
	Increase (decrease) due to changes in:			Increase (decrease) due to changes in:		
(dollars in thousands)	Volume	Rate	Total	Volume	Rate	Total
Interest Income:						
Loans	$ (6,243)	$ (8,815)	$ (15,058)	$ (14,862)	$ (10,409)	$ (25,271)
Investments & Cash Equivalents	(3,612)	(168)	(3,780)	(6,437)	1,399	(5,038)
Total Interest Income	$ (9,855)	$ (8,983)	$ (18,838)	$ (21,299)	$ (9,010)	$ (30,309)
Interest Expense:						
Interest-Bearing Liabilities	$ (3,989)	$ (19,542)	$ (23,531)	$ (8,089)	$ (39,819)	$ (47,908)
Changes in Net Interest Income	$ (5,866)	$ 10,559	$ 4,693	$ (13,210)	$ 30,809	$ 17,599

Provision for Loan Losses

The District 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. The provision for loan losses was $10.4 million and $25.0 million for the three and six month periods ended June 30, 2012, compared to $55.2 million and $88.9 million for the same periods in 2011. Provision for loan loss expense for the three months ended June 30, 2012 consisted of $14.7 million related to reserves for specific credits and reversals of $4.3 million related to general reserves. Provision expense was related primarily to the nursery/greenhouse ($9.3 million), forestry ($4.5 million), citrus ($2.2 million), grain ($1.7 million), other real estate ($1.6 million), cattle ($1.5 million), and fruits and vegetables segments ($1.4 million), offset by reversals in the processing ($12.8 million) segment. Provision for loan loss expense for the six months ended June 30, 2012 consisted of $30.7 million related to reserves for specific credits and reversals of $5.7 million related to general reserves. Provision expense was related primarily to the nursery/greenhouse ($17.8 million), other real estate ($4.9 million), citrus ($2.8 million), fruits and vegetables ($2.4 million), and cattle ($2.3 million) segments, partially offset by reversals in the processing ($12.6 million) segment. As mentioned previously, declining real estate values were the reason for some of the provision expense recognized by the District. See Note 3, *Loans and Allowance for Loan Losses,* in the Notes to the Combined 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 June 30,**			**For the six months ended June 30,**		
(dollars in thousands)	**2012**	**2011**	**Increase/ (Decrease)**	**2012**	**2011**	**Increase/ (Decrease)**
Loan fees	$ 9,230	$ 9,775	$ (545)	$ 19,546	$ 19,656	$ (110)
Fees for financially related services	1,523	1,934	(411)	3,252	3,179	73
Gains (losses) from other property owned, net	(12,554)	(6,558)	(5,996)	(21,217)	(17,004)	(4,213)
Gains (losses) on investments, net	–	2,973	(2,973)	–	2,973	(2,973)
Net impairment losses on investments	(2,417)	(3,652)	1,235	(3,180)	(8,110)	4,930
Gains (losses) on sale of rural home loans, net	619	602	17	1,209	951	258
Gains from sale of premises and equipment, net	290	466	(176)	447	566	(119)
Patronage refunds from other Farm Credit institutions	43	4	39	454	136	318
Insurance premium refund	33,744	–	33,744	33,744	–	33,744
Other noninterest income	(1,220)	(11)	(1,209)	2,611	2,284	327
Total noninterest income	$ 29,258	$ 5,533	$ 23,725	$ 36,866	$ 4,631	$ 32,235

Noninterest income for the three months and six months ended June 30, 2012 increased $23.7 million and $32.2 million, respectively, compared to the corresponding periods in 2011. The increases for both periods were due primarily to the District's recording $33.7 million of insurance premium refunds during the second quarter of 2012 from the Farm Credit Insurance Corporation (FCSIC), which insures the System's debt obligations. These payments are nonrecurring and resulted from the assets of the FCSIC exceeding the secure base amount as defined by the Farm Credit Act.

The $6.0 million and $4.2 million increases in losses from other property owned for the three and six month periods ended June 30, 2012 compared to the corresponding periods in the prior year resulted from higher losses on OPO and the recognition in the second quarter of 2011 of a previously deferred gain. The $2.3 million gain in 2011 from an ethanol plant sale was recognized in accordance with accounting guidance. The largest losses for the second quarter of 2012 were a $2.0 million loss on a land holding in the forestry segment and a $1.5 million loss on a land holding in the other real estate segment. The six months ended June 30, 2012 included $4.4 million of additional losses on three land holdings in the forestry and other real estate segments. See *Other Property Owned* section above.

Gains on investments of $3.0 million during 2011 were the result of normal investment activities related to managing the composition and overall size of the District's investment portfolio.

Net impairment losses on investments decreased $1.2 million and $4.9 million for the three and six month periods ended June 30, 2012 as compared to the same periods in 2011. See discussion of 2012 credit related other-than-temporary impairment in the *Liquidity and Funding Sources* section above.

For the three months ended June 30, 2012 compared to the same period in 2011, other noninterest income decreased $1.2 million due primarily to an $811 thousand higher provision for unfunded commitments recorded during 2012. Other noninterest income increased $327 thousand for the six months ended June 30, 2012 primarily due to $1.3 million in insurance recoveries.

Noninterest Expense

The following table illustrates the changes in noninterest expense:

Change in Noninterest Expense	**For the three months ended June 30,**			**For the six months ended June 30,**		
(dollars in thousands)	**2012**	**2011**	**Increase/ (Decrease)**	**2012**	**2011**	**Increase/ (Decrease)**
Salaries and employee benefits	$ 63,375	$ 61,984	$ 1,391	$ 129,211	$ 125,505	$ 3,706
Occupancy and equipment	9,126	8,325	801	18,079	16,991	1,088
Insurance Fund premiums	2,768	3,474	(706)	5,515	6,939	(1,424)
Other operating expenses	21,599	19,907	1,692	44,077	40,781	3,296
Called debt expense	7,624	4,416	3,208	20,369	5,859	14,510
Correspondent lending servicing expense	2,253	2,222	31	4,556	4,487	69
Other noninterest expense	–	34	(34)	–	104	(104)
Total noninterest expense	$ 106,745	$ 100,362	$ 6,383	$ 221,807	$ 200,666	$ 21,141

Noninterest expense for the three months and six months ended June 30, 2012 increased $6.4 million and $21.1 million, respectively, compared to the corresponding periods in 2011. The increases for both periods were 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 $3.2 million and $14.5 million for the three month and six month periods, respectively. Call options were exercised on bonds totaling $12.285 billion for the six months ended June 30, 2012 compared to $6.831 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 increases in salaries and employee benefits of $1.4 million and $3.7 million, for the three month and six month periods ended June 30, 2012, respectively, were due primarily to normal salary administration, and increased employee benefit costs.

Occupancy and equipment expense for the three and six month periods ended June 30, 2012 increased $801 thousand and $1.1 million compared to the corresponding periods in the prior year. These increases were due primarily to increases in software expense for various maintenance agreements and database management.

FCSIC premiums decreased minimally for the three and six month periods. 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 for the three and six months ended June 30, 2012 increased $1.7 million and $3.3 million, respectively. A portion of the increases resulted from additional consulting and professional fees required for system enhancements, which increased other operating expenses $943 thousand and $1.1 million for the three and six months ended June 30, 2012, respectively. Also contributing to the increases in other operating expenses for the three and the six months ended June 30, 2012, were travel expenses which increased $151.3 thousand and $326.6 thousand, respectively, related to company cars and employee travel. Increases in public and member relations for the three and the six months periods of $134.8 thousand and $256.8 thousand, respectively, related to annual meetings and annual report expenses. The remainder of the increases in other operating expenses were comprised of numerous and varied expenses, none of which individually had a significant increase in the three or six month periods ended June 30, 2012 compared to the same periods in 2011.

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 12, *District Merger Activity*, in the Notes to the Combined Financial Statements for information regarding merger activity in the District.

REGULATORY MATTERS

Please refer to Note 11, *Regulatory Enforcement Matters*, in the Notes to the Combined Financial Statements for information regarding regulatory matters in the District.

OTHER MATTERS

As previously announced in the 2011 Annual Report of AgFirst Farm Credit Bank and District Associations, F. A. (Andy) Lowrey retired as AgFirst's Chief Executive Officer effective June 30, 2012. The Board of Directors appointed Leon T. (Tim) Amerson, AgFirst's President and Chief Operating Officer, as Chief Executive Officer and President effective July 1, 2012.

Gary L. Alexander resigned from AgFirst's Board of Directors effective July 11, 2012.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

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

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*. 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.

Combined Balance Sheets

(dollars in thousands)	**June 30, 2012**	**December 31, 2011**
	(unaudited)	*(audited)*
Assets		
Cash and cash equivalents	**$ 1,221,624**	$ 1,340,167
Investment securities:		
Available for sale (amortized cost of $6,536,780 and $6,840,738 respectively)	**6,690,575**	6,980,105
Held to maturity (fair value of $923,707 and $1,053,277 respectively)	**852,905**	975,448
Total investment securities	**7,543,480**	7,955,553
Loans	**22,583,197**	22,481,505
Less: allowance for loan losses	**175,089**	174,976
Net loans	**22,408,108**	22,306,529
Loans held for sale	**14,156**	10,201
Other investments	**159,097**	238,552
Accrued interest receivable	**192,153**	197,782
Investments in other Farm Credit System institutions	**12,850**	12,680
Premises and equipment, net	**127,011**	127,445
Other property owned	**139,892**	158,144
Other assets	**166,144**	163,815
Total assets	**$ 31,984,515**	$ 32,510,868
Liabilities		
Bonds and notes	**$ 26,666,400**	$ 27,288,439
Accrued interest and dividends payable	**42,795**	42,570
Dividends and patronage refunds payable	**9,168**	93,665
Pension and other postretirement benefits liability	**379,979**	370,568
Advanced conditional payments	**11,709**	5,553
Other liabilities	**102,446**	188,894
Total liabilities	**27,212,497**	27,989,689
Commitments and contingencies (Note 5)		
Shareholders' Equity		
Perpetual preferred stock (Note 8)	**281,450**	400,000
Protected borrower equity	**3,090**	3,269
Capital stock and participation certificates	**154,007**	159,334
Additional paid-in-capital (Note 8)	**41,973**	7,873
Retained earnings		
Allocated	**1,388,883**	1,415,359
Unallocated	**3,093,714**	2,756,592
Accumulated other comprehensive income (loss)	**(191,099)**	(221,248)
Total shareholders' equity	**4,772,018**	4,521,179
Total liabilities and equity	**$ 31,984,515**	$ 32,510,868

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

Combined Statements of Income

(unaudited)

(dollars in thousands)	For the three months ended June 30, 2012	For the three months ended June 30, 2011	For the six months ended June 30, 2012	For the six months ended June 30, 2011
Interest Income				
Investment securities	**$ 48,770**	$ 51,648	**$ 99,311**	$ 102,612
Loans	**287,006**	302,064	**574,211**	599,482
Other	**1,902**	2,804	**3,936**	5,673
Total interest income	**337,678**	356,516	**677,458**	707,767
Interest Expense	**54,109**	77,640	**110,373**	158,281
Net interest income	**283,569**	278,876	**567,085**	549,486
Provision for loan losses	**10,384**	55,221	**24,974**	88,892
Net interest income after provision for loan losses	**273,185**	223,655	**542,111**	460,594
Noninterest Income				
Loan fees	**9,230**	9,775	**19,546**	19,656
Fees for financially related services	**1,523**	1,934	**3,252**	3,179
Gains (losses) from other property owned, net	**(12,554)**	(6,558)	**(21,217)**	(17,004)
Gains (losses) on investments, net	**—**	2,973	**—**	2,973
Total other-than-temporary impairment losses on investments (Note 2)	**(21,156)**	(402)	**(21,995)**	(2,879)
Portion of loss recognized in other comprehensive income (loss) (Note 2)	**18,739**	(3,250)	**18,815**	(5,231)
Net other-than-temporary impairment losses on investments	**(2,417)**	(3,652)	**(3,180)**	(8,110)
Gains (losses) on sales of rural home loans, net	**619**	602	**1,209**	951
Gains from sale of premises and equipment, net	**290**	466	**447**	566
Patronage refunds from other Farm Credit institutions	**43**	4	**454**	136
Insurance premium refund	**33,744**	—	**33,744**	—
Other noninterest income	**(1,220)**	(11)	**2,611**	2,284
Total noninterest income	**29,258**	5,533	**36,866**	4,631
Noninterest Expenses				
Salaries and employee benefits	**63,375**	61,984	**129,211**	125,505
Occupancy and equipment	**9,126**	8,325	**18,079**	16,991
Insurance Fund premiums	**2,768**	3,474	**5,515**	6,939
Other operating expenses	**21,599**	19,907	**44,077**	40,781
Called debt expense	**7,624**	4,416	**20,369**	5,859
Correspondent lending servicing expense	**2,253**	2,222	**4,556**	4,487
Other noninterest expense	**—**	34	**—**	104
Total noninterest expenses	**106,745**	100,362	**221,807**	200,666
Income before income taxes	**195,698**	128,826	**357,170**	264,559
Provision for income taxes	**279**	261	**416**	459
Net income	**$ 195,419**	$ 128,565	**$ 356,754**	$ 264,100

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

Combined Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the three months ended June 30, 2012	For the three months ended June 30, 2011	For the six months ended June 30, 2012	For the six months ended June 30, 2011
Net income	**$ 195,419**	$ 128,565	**$ 356,754**	$ 264,100
Other comprehensive income net of tax				
Unrealized gains (losses) on investments available for sale:				
Other-than-temporarily impaired (Note 2)	**(18,705)**	3,529	**(18,477)**	2,042
Not other-than-temporarily impaired (Note 2)	**22,422**	61,631	**32,905**	46,258
Change in value of firm commitments - when issued securities (Note 7)	**555**	3,832	**1,210**	2,080
Employee benefit plans adjustments	**7,255**	7,193	**14,511**	14,527
Other comprehensive income (Note 9)	**11,527**	76,185	**30,149**	64,907
Comprehensive income	**$ 206,946**	$ 204,750	**$ 386,903**	$ 329,007

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

Combined Statements of Changes in Shareholders' Equity

(unaudited)

(dollars in thousands)	Perpetual Preferred Stock	Protected Borrower Equity	Capital Stock and Participation Certificates	Additional Paid-in-Capital	Retained Earnings: Allocated	Retained Earnings: Unallocated	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance at December 31, 2010	$ 400,000	$ 3,641	$ 150,031	$ —	$ 1,318,996	$ 2,575,592	$ (291,580)	$ 4,156,680
Comprehensive income						264,100	64,907	329,007
Protected borrower equity retired		(226)						(226)
Capital stock/participation certificates issued (retired), net			2,059					2,059
Dividends declared/paid			235			(383)		(148)
Dividends paid on perpetual preferred stock						(13,706)		(13,706)
Patronage distribution								
Cash						(6,018)		(6,018)
Nonqualified allocated retained earnings					14	(14)		—
Retained earnings retired					(28,991)			(28,991)
Equity issued as result of merger (Note 12)		267	1,936	7,922				10,125
Equity retired as result of merger		(267)	(1,936)			(31,458)		(33,661)
Patronage distribution adjustment			(7)		279	1,414		1,686
Balance at June 30, 2011	$ 400,000	$ 3,415	$ 152,318	$ 7,922	$ 1,290,298	$ 2,789,527	$ (226,673)	$ 4,416,807
Balance at December 31, 2011	$ 400,000	$ 3,269	$ 159,334	$ 7,873	$ 1,415,359	$ 2,756,592	$ (221,248)	$ 4,521,179
Comprehensive income						**356,754**	**30,149**	**386,903**
Protected borrower equity retired		**(179)**						**(179)**
Capital stock/participation certificates issued (retired), net			**(5,558)**					**(5,558)**
Dividends declared/paid			**231**			**(332)**		**(101)**
Dividends paid on perpetual preferred stock						**(11,479)**		**(11,479)**
Redemption of perpetual preferred stock (Note 8)	**(118,550)**			**34,100**				**(84,450)**
Patronage distribution								
Cash						**(6,545)**		**(6,545)**
Retained earnings retired					**(28,425)**	**128**		**(28,297)**
Patronage distribution adjustment					**1,949**	**(1,404)**		**545**
Balance at June 30, 2012	**$ 281,450**	**$ 3,090**	**$ 154,007**	**$ 41,973**	**$ 1,388,883**	**$ 3,093,714**	**$ (191,099)**	**$ 4,772,018**

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

Combined Statements of Cash Flows

(unaudited)

(dollars in thousands)	For the six months ended June 30, 2012	2011
Cash flows from operating activities:		
Net income	**$ 356,754**	$ 264,100
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation on premises and equipment	**8,435**	8,260
Amortization of net deferred loan origination (fees) costs	**(4,535)**	(5,975)
Premium amortization (discount accretion) on investment securities	**1,905**	7,812
(Premium amortization) discount accretion on bonds and notes	**1,537**	(1,172)
Provision for loan losses	**24,974**	88,892
(Gains) losses on other property owned	**21,217**	17,004
(Gains) losses from sale of premises and equipment, net	**(447)**	(566)
Net impairment losses on investments	**3,180**	8,110
(Gains) losses on investments, net	**—**	(2,973)
(Gains) losses on sales of rural home loans, net	**(1,209)**	(951)
Net change in loans held for sale	**13,586**	16,299
Changes in operating assets and liabilities:		
(Increase) decrease in accrued interest receivable	**5,629**	(5,395)
(Increase) decrease in other assets	**(6,798)**	19,597
Increase (decrease) in accrued interest payable	**225**	(4,686)
Increase (decrease) in pension and other postretirement benefits liability	**23,922**	10,472
Increase (decrease) in other liabilities	**(89,628)**	(16,474)
Total adjustments	**1,993**	138,254
Net cash provided by (used in) operating activities	**358,747**	402,354
Cash flows from investing activities:		
Investment securities purchased	**(404,949)**	(766,091)
Proceeds from investment securities sold or matured	**826,819**	872,544
Net (increase) decrease in loans	**(176,174)**	(36,398)
(Increase) decrease in investments in other Farm Credit System institutions	**(170)**	(144)
Purchases of other investments	**(292)**	(2,198)
Proceeds from payments received on other investments	**83,683**	82,542
Purchase of premises and equipment, net	**(8,414)**	(7,469)
Proceeds from sale of premises and equipment, net	**860**	1,099
Proceeds from sale of other property owned	**34,859**	34,006
Net cash provided by (used in) investing activities	**356,222**	177,891
Cash flows from financing activities:		
Bonds and notes issued	**21,599,581**	16,011,227
Bonds and notes retired	**(22,218,688)**	(16,695,026)
Net increase (decrease) in advanced conditional payments	**6,156**	1,373
Protected borrower equity retired	**(179)**	(226)
Capital stock and participation certificates issued/retired, net	**(5,558)**	2,059
Patronage refunds and dividends paid	**(90,598)**	(94,196)
Redemption of perpetual preferred stock (Note 8)	**(84,450)**	—
Dividends paid on perpetual preferred stock	**(11,479)**	(13,706)
Retained earnings retired	**(28,297)**	(28,991)
Net cash provided by (used in) financing activities	**(833,512)**	(817,486)
Net increase (decrease) in cash and cash equivalents	**(118,543)**	(237,241)
Cash and cash equivalents, beginning of period	**1,340,167**	1,463,700
Cash and cash equivalents, end of period	**$ 1,221,624**	$ 1,226,459
Supplemental schedule of non-cash investing and financing activities:		
Financed sales of other property owned	**$ 9,090**	$ 5,014
Receipt of property in settlement of loans	**46,914**	47,173
Change in unrealized gains (losses) on investments, net	**14,428**	48,300
Employee benefit plans adjustments	**14,511**	14,527
Equity issued as result of merger	**—**	10,125
Equity retired as result of merger	**—**	(33,661)
Adjustment of allowance for loan losses related to Association mergers	**—**	(16,097)
Change in fair value of forward contracts (Note 7)	**(386)**	(8,769)
Non-cash changes related to interest rate hedging activities:		
Increase (decrease) in bonds and notes	**$ (4,470)**	$ (10,315)
Decrease (increase) in other assets	**4,470**	10,315
Supplemental information:		
Interest paid	**$ 108,611**	$ 164,120
Taxes paid, net	**388**	432

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

Notes to the Combined 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 combined financial statements include the accounts of AgFirst Farm Credit Bank (AgFirst or Bank) and the District Agricultural Credit Associations (Associations or District Associations), collectively referred to as the District. All significant transactions and balances between AgFirst and the District Associations have been eliminated in combination. A description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations of the District as of and for the year ended December 31, 2011 are contained in the 2011 Annual Report to Shareholders. These unaudited second 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 six months ended June 30, 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 District 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 District has been identified. 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 District 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 District's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. The District 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 District'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 previous option permitting the presentation of other comprehensive income in the statement of changes in equity was 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 applied retrospectively. For public entities, it was effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance did not impact the District's financial condition or results of operations, but resulted in changes to the presentation of comprehensive income. In December 2011, the FASB issued guidance (ASU 2011-12; Topic 220) to defer the 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 were required to be adopted as set forth in the June 2011 guidance. The deferral was 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 changed 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 requires 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 applied prospectively. The amendments are effective for interim and annual periods beginning after December 15, 2011. Early application is not permitted. The adoption of this guidance did not impact the District's financial condition or results of operations, but resulted 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 District, 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 District'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

District investments consist primarily of mortgage-backed securities (MBSs) collateralized by U.S. government or U.S. agency guaranteed residential mortgages. They are held to maintain a liquidity reserve, manage short-term surplus funds, and manage interest rate risk. These securities meet the applicable Farm Credit Administration (FCA) regulatory guidelines related to government agency guaranteed investments.

Included in the available-for-sale investments are non-agency collateralized mortgage obligations (CMOs) and asset backed securities (ABSs). These securities must meet the applicable FCA regulatory guidelines, which require them 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 these ratings, the securities may have a guarantee of timely payment of principal and interest, credit enhancements achieved through over-collateralization or other means, and priority of payments for senior classes over junior classes. All of the non-agency securities owned have credit enhancement features including senior/subordinate structure and/or are backed by a bond insurer.

The FCA considers a non-agency security 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 the ineligible security. Non-agency CMO securities not rated in the top category by at least one of the NRSROs at June 30, 2012 had a fair value of $208.2 million. ABSs not rated in the top category by at least one of the NRSROs at June 30, 2012 had a fair value of $23.5 million. For each of these investment securities in the District's portfolio rated below AAA/Aaa, the District 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 District's plans for all but seven investments that have recently become ineligible. The District has submitted plans to hold these seven ineligible securities and is awaiting approval from the FCA.

Mission Related Investments are generally held to maturity and consist primarily of Rural America Bonds, which are private placement securities purchased under the Mission Related Investment Program approved by the FCA. In its Conditions of Approval for the program, the FCA considers a Rural America Bond ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9. Pursuant to these conditions of approval, the District has submitted and received approval for plans to hold two Rural America Bonds totaling $5.1 million whose credit quality had deteriorated beyond the program limits.

Available-for-sale

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

	June 30, 2012				
(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
U.S. Govt. GNMA MBS/CMOs	$ 4,621,271	$ 188,468	$ (2,631)	$ 4,807,108	2.54%
U.S. Govt. Agency MBS	1,568,433	29,286	(9,211)	1,588,508	1.43
Non-Agency CMOs (a)	266,890	–	(57,104)	209,786	0.64
Asset-Backed Securities (a)	32,475	3,609	(4,181)	31,903	0.63
Mission Related Investments	47,711	5,855	(296)	53,270	5.96
Total	$ 6,536,780	$ 227,218	$ (73,423)	$ 6,690,575	2.22%

	December 31, 2011				
(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
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)	292,075	248	(50,092)	242,231	0.83
Asset-Backed Securities (b)	34,736	2,239	(6,651)	30,324	0.70
Mission Related Investments	47,456	6,909	(145)	54,220	6.14
Total	$ 6,840,738	$ 209,956	$ (70,589)	$ 6,980,105	2.18%

(a) Gross unrealized losses include non-credit related other-than-temporary impairment recognized in AOCI of $38.2 million for Non-Agency CMOs and $2.3 million for Asset-Backed Securities.
(b) Gross unrealized losses include non-credit related other-than temporary impairment recognized in AOCI of $16.0 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:

	June 30, 2012				
(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
U.S. Govt. Agency MBS	$ 572,244	$ 50,085	$ (175)	$ 622,154	5.43%
Asset-Backed Securities	76,193	1,087	(411)	76,869	1.63
Mission Related Investments	204,468	20,588	(372)	224,684	6.05
Total	$ 852,905	$ 71,760	$ (958)	$ 923,707	5.24%

	December 31, 2011				
(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
U.S. Govt. Agency MBS	$ 691,331	$ 59,389	$ (188)	$ 750,532	5.35%
Asset-Backed Securities	74,777	943	(406)	75,314	1.61
Mission Related Investments	209,340	18,472	(381)	227,431	6.01
Total	$ 975,448	$ 78,804	$ (975)	$ 1,053,277	5.21%

There were no sales of investment securities during the first half of 2012. During the first half of 2011, proceeds from sales of investments were $57.3 million and realized gains were $3.0 million.

A summary of the contractual maturity, estimated fair value and amortized cost of investment securities at June 30, 2012 follows:

Available-for-sale

	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	
(dollars in thousands)	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	$ –	– %	$ 90	0.44 %	$ 4,702	1.76 %	$ 4,802,316	2.54 %	$ 4,807,108	2.54 %
U.S. Govt. Agency MBS	–	–	10,172	4.25	15,818	0.89	1,562,518	1.42	1,588,508	1.43
Non-Agency CMOs	–	–	–	–	–	–	209,786	0.64	209,786	0.64
Asset-Backed Securities	–	–	–	–	–	–	31,903	0.63	31,903	0.63
Mission Related Investments	–	–	2,000	5.96	1,142	5.96	50,128	5.96	53,270	5.96
Total fair value	$ –	– %	$ 12,262	4.51 %	$ 21,662	1.30 %	$ 6,656,651	2.21 %	$ 6,690,575	2.22 %
Total amortized cost	$ –		$ 11,885		$ 21,215		$ 6,503,680		$ 6,536,780	

Held-to-maturity

	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	
(dollars in thousands)	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	$ –	– %	$ –	– %	$ 1,189	4.86 %	$ 571,055	5.44 %	$ 572,244	5.43 %
Asset-Backed Securities	1,025	1.90	7,328	0.92	37,188	1.55	30,652	1.88	76,193	1.63
Mission Related Investments	4,998	5.39	30,521	6.50	23,852	6.36	145,097	5.92	204,468	6.05
Total amortized cost	$ 6,023	4.79 %	$ 37,849	5.42 %	$ 62,229	3.46 %	$ 746,804	5.38 %	$ 852,905	5.24 %
Total fair value	$ 6,099		$ 40,016		$ 66,019		$ 811,573		$ 923,707	

Substantially all of these securities have contractual maturities in excess of ten years. However, expected maturities for these types of securities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

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 June 30, 2012 and December 31, 2011. A continuous unrealized loss position for an investment is measured from the date the impairment was first identified.

	June 30, 2012					
	Less than 12 Months		Greater than 12 Months		Total	
(dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Govt. GNMA MBS/CMOs	$ –	$ –	$ 218,128	$ (2,630)	$ 218,128	$ (2,630)
U.S. Govt. Agency MBS	171,405	(1,076)	383,909	(8,310)	555,314	(9,386)
Non-Agency CMOs	227	(1)	209,559	(57,103)	209,786	(57,104)
Asset-Backed Securities	3,492	(37)	34,745	(4,555)	38,237	(4,592)
Mission Related Investments	17,895	(669)	–	–	17,895	(669)
Total	$ 193,019	$ (1,783)	$ 846,341	$ (72,598)	$ 1,039,360	$ (74,381)

	December 31, 2011											
	Less than 12 Months				Greater than 12 Months				Total			
(dollars in thousands)		Fair Value		Unrealized Losses		Fair Value		Unrealized Losses		Fair Value		Unrealized Losses
U.S. Govt. GNMA MBS/CMOs	$	50,349	$	(29)	$	260,966	$	(3,100)	$	311,315	$	(3,129)
U.S. Govt. Agency MBS		227,888		(1,646)		442,141		(9,114)		670,029		(10,760)
Non-Agency CMOs		–		–		241,567		(50,092)		241,567		(50,092)
Asset-Backed Securities		423		(1)		44,651		(7,056)		45,074		(7,057)
Mission Related Investments		38,038		(526)		–		–		38,038		(526)
Total	$	316,698	$	(2,202)	$	989,325	$	(69,362)	$	1,306,023	$	(71,564)

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 District 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 District 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 District 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 District recognized $22.0 million of other-than-temporary impairment during the first six months of 2012 in connection with non-agency ABS and CMO securities in the portfolio, which is included in Impairment Losses on Investments in the Combined Statements of Income.

Since the District 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 $22.0 million is separated into: (1) the estimated amount relating to credit loss ($3.2 million reflected in Net Income in the Combined Statements of Income), which is partially offset by (2) the amount relating to all other factors ($18.8 million gain reflected in the Combined Statements of Comprehensive Income).

The District uses the present value of cash flows expected to be collected from each debt security to determine the amount of credit loss. This technique requires assumptions related to the underlying collateral, including default rates, amount 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 District 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 June 30, 2012 ranged from 1.64 percent to 41.85 percent for non-agency CMO securities and from 13.67 percent to 80.35 percent for ABS securities. Prepayment rate assumptions are based on forecasted prepayments and resulted in prepayment rates that ranged from 7.48 percent to 20.70 percent for non-agency CMO securities and from 3.11 percent to 6.88 percent for ABS securities at June 30, 2012. At June 30, 2012, the loss severity rates estimated from assumptions ranged from 3.90 percent to 77.12 percent for non-agency CMO securities and from 59.46 percent to 100.00 percent for ABS securities.

For investments that are not other-than-temporarily impaired, the District has not recognized any credit losses as the temporary impairments resulted from non-credit related factors. The District 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 District expects these securities would not be settled at a price less than their amortized cost. For the six months ended June 30, 2012, net unrealized gains of $32.9 million were recognized in other comprehensive income for available-for-sale investments that are not other-than-temporarily impaired.

The following schedules detail the activity related to cumulative credit losses on investments recognized in earnings as of June 30, 2012 and 2011:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
(dollars in thousands)	**2012**	**2011**	**2012**	**2011**
Cumulative Losses Beginning of Period	$ 53,718	$ 49,182	$ 53,297	$ 45,077
Additions for the amount related to credit loss for which other-than-temporary impairment was not previously recognized	1,768	–	1,768	1,463
Additions for the amount related to credit loss for which other-than-temporary impairment was previously recognized	648	3,652	1,411	6,646
Reductions for increases in expected cash flows	(191)	(268)	(533)	(620)
Cumulative Losses End of Period	$ 55,943	$ 52,566	$ 55,943	$ 52,566

NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES

For a complete description of the District'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 District manages credit risk associated with lending activities through an assessment of the credit risk profile of an individual obligor. The District 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 follows:

(dollars in thousands)	**June 30, 2012**	**December 31, 2011**
Real estate mortgage	$ 9,748,030	$ 9,756,036
Production and intermediate-term	7,767,612	7,924,627
Agribusiness		
Loans to cooperatives	244,650	256,981
Processing and marketing	1,088,373	1,115,490
Farm-related business	384,193	348,797
Total agribusiness	1,717,216	1,721,268
Communication	271,500	213,501
Energy	428,219	280,700
Water and waste disposal	28,021	28,022
Rural residential real estate	2,536,007	2,470,742
Lease receivables	5,895	2,986
Loans to other financial institutions (OFIs)	15,650	5,250
Other (including mission-related)	65,047	78,373
Total Loans	$ 22,583,197	$ 22,481,505

The District 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 June 30, 2012 and December 31, 2011:

	June 30, 2012					
	Within Farm Credit System		Outside Farm Credit System		Total	
(dollars in thousands)	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 136,580	$ 62,165	$ 108,096	$ 3,646	$ 244,676	$ 65,811
Production and intermediate-term	322,809	205,330	401,423	26,810	724,232	232,140
Agribusiness						
Loans to cooperatives	215,901	–	17,766	–	233,667	–
Processing and marketing	337,027	43,505	623,566	4,035	960,593	47,540
Farm-related business	134,193	8,075	39,170	858	173,363	8,933
Total agribusiness	687,121	51,580	680,502	4,893	1,367,623	56,473
Communication	312,775	–	–	–	312,775	–
Energy	429,453	–	7,434	–	436,887	–
Water and waste disposal	28,000	–	–	–	28,000	–
Rural residential real estate	–	–	52	–	52	–
Lease receivables	1,286	–	–	–	1,286	–
Loans to OFIs	–	–	15,650	–	15,650	–
Other (including mission-related)	–	22,030	6,842	3,241	6,842	25,271
Total	$ 1,918,024	$ 341,105	$ 1,219,999	$ 38,590	$ 3,138,023	$ 379,695

	December 31, 2011					
	Within Farm Credit System		Outside Farm Credit System		Total	
(dollars in thousands)	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 135,657	$ 65,477	$ 111,443	$ 3,792	$ 247,100	$ 69,269
Production and intermediate-term	304,593	333,209	507,782	29,982	812,375	363,191
Agribusiness						
Loans to cooperatives	183,406	–	36,853	–	220,259	–
Processing and marketing	310,301	17,411	660,500	4,135	970,801	21,546
Farm-related business	123,291	7,476	26,798	899	150,089	8,375
Total agribusiness	616,998	24,887	724,151	5,034	1,341,149	29,921
Communication	231,022	–	–	–	231,022	–
Energy	275,443	–	7,510	–	282,953	–
Water and waste disposal	28,000	–	–	–	28,000	–
Rural residential real estate	–	–	53	–	53	–
Lease receivables	1,709	–	–	–	1,709	–
Loans to OFIs	–	–	5,250	–	5,250	–
Other (including mission-related)	–	22,022	9,095	3,240	9,095	25,262
Total	$ 1,593,422	$ 445,595	$ 1,365,284	$ 42,048	$ 2,958,706	$ 487,643

A significant source of liquidity for the District is the repayments and maturities of loans. The following table presents the contractual maturity distribution of loans by loan type at June 30, 2012 and indicates that approximately 17.98 percent of loans had maturities of less than one year:

(dollars in thousands)	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 764,526	$ 2,692,807	$ 6,290,697	$ 9,748,030
Production and intermediate-term	2,619,409	3,118,934	2,029,269	7,767,612
Agribusiness				
Loans to cooperatives	62,286	86,058	96,306	244,650
Processing and marketing	352,386	563,473	172,514	1,088,373
Farm-related business	101,506	202,776	79,911	384,193
Total agribusiness	516,178	852,307	348,731	1,717,216
Communication	84,111	118,520	68,869	271,500
Energy	42,916	174,239	211,064	428,219
Water and waste disposal	21	–	28,000	28,021
Rural residential real estate	29,263	72,572	2,434,172	2,536,007
Lease receivables	2,702	514	2,679	5,895
Loans to OFIs	–	15,650	–	15,650
Other (including mission-related)	2,361	8,879	53,807	65,047
Total Loans	$ 4,061,487	$ 7,054,422	$ 11,467,288	$ 22,583,197

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 June 30, 2012 and December 31, 2011:

	June 30, 2012	December 31, 2011
Real estate mortgage:		
Acceptable	89.26%	88.42%
OAEM	4.70	5.13
Substandard/doubtful/loss	6.04	6.45
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	86.67%	84.82%
OAEM	6.42	8.29
Substandard/doubtful/loss	6.91	6.89
	100.00%	100.00%
Agribusiness:		
Loans to cooperatives:		
Acceptable	95.61%	92.01%
OAEM	3.76	7.39
Substandard/doubtful/loss	0.63	0.60
	100.00%	100.00%
Processing and marketing:		
Acceptable	88.75%	85.52%
OAEM	3.24	6.40
Substandard/doubtful/loss	8.01	8.08
	100.00%	100.00%
Farm-related business:		
Acceptable	94.80%	95.51%
OAEM	2.61	1.80
Substandard/doubtful/loss	2.59	2.69
	100.00%	100.00%
Total Agribusiness:		
Acceptable	91.08%	88.52%
OAEM	3.17	5.61
Substandard/doubtful/loss	5.75	5.87
	100.00%	100.00%

	June 30, 2012	December 31, 2011
Communication:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Energy and water/waste disposal:		
Acceptable	99.51%	98.63%
OAEM	0.49	1.37
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Rural residential real estate:		
Acceptable	98.77%	98.69%
OAEM	0.43	0.47
Substandard/doubtful/loss	0.80	0.84
	100.00%	100.00%
Lease receivables:		
Acceptable	95.13%	89.33%
OAEM	1.22	3.76
Substandard/doubtful/loss	3.65	6.91
	100.00%	100.00%
Loans to OFIs:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Other (including mission-related):		
Acceptable	86.56%	79.66%
OAEM	0.60	1.53
Substandard/doubtful/loss	12.84	18.81
	100.00%	100.00%
Total Loans:		
Acceptable	89.91%	88.50%
OAEM	4.54	5.66
Substandard/doubtful/loss	5.55	5.84
	100.00%	100.00%

The following tables provide an age analysis of past due loans and related accrued interest as of June 30, 2012 and December 31, 2011:

	June 30, 2012					
(dollars in thousands)	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
Real estate mortgage	$ 85,521	$ 166,568	$ 252,089	$ 9,580,991	$ 9,833,080	$ 962
Production and intermediate-term	41,304	157,980	199,284	7,637,458	7,836,742	176
Agribusiness						
Loans to cooperatives	–	1,545	1,545	244,253	245,798	–
Processing and marketing	56	3,789	3,845	1,088,834	1,092,679	–
Farm-related business	825	1,912	2,737	383,192	385,929	–
Total agribusiness	881	7,246	8,127	1,716,279	1,724,406	–
Communication	–	–	–	271,851	271,851	–
Energy and water/waste disposal	–	–	–	458,034	458,034	–
Rural residential real estate	42,699	9,006	51,705	2,494,193	2,545,898	3,383
Lease receivables	–	35	35	5,900	5,935	–
Loans to OFIs	–	–	–	15,675	15,675	–
Other (including mission-related)	1,518	4,242	5,760	60,021	65,781	–
Total	$ 171,923	$ 345,077	$ 517,000	$ 22,240,402	$ 22,757,402	$ 4,521

	December 31, 2011					
(dollars in thousands)	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
Real estate mortgage	$ 141,900	$ 214,314	$ 356,214	$ 9,486,256	$ 9,842,470	$ 1,154
Production and intermediate-term	77,546	180,018	257,564	7,740,979	7,998,543	581
Agribusiness						
Loans to cooperatives	–	1,553	1,553	256,486	258,039	–
Processing and marketing	308	1,621	1,929	1,118,245	1,120,174	–
Farm-related business	804	7,847	8,651	341,940	350,591	–
Total agribusiness	1,112	11,021	12,133	1,716,671	1,728,804	–
Communication	–	–	–	213,810	213,810	–
Energy and water/waste disposal	–	–	–	310,357	310,357	–
Rural residential real estate	52,146	14,358	66,504	2,412,196	2,478,700	4,583
Lease receivables	–	37	37	2,958	2,995	–
Loans to OFIs	–	–	–	5,259	5,259	–
Other (including mission-related)	957	2,383	3,340	75,985	79,325	1,238
Total	$ 273,661	$ 422,131	$ 695,792	$ 21,964,471	$ 22,660,263	$ 7,556

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 June 30, 2012 and December 31, 2011 are summarized as follows:

(dollars in thousands)	June 30, 2012	December 31, 2011
Nonaccrual loans:		
Real estate mortgage	$ 287,373	$ 317,772
Production and intermediate-term	297,627	288,029
Agribusiness		
Loans to cooperatives	1,544	1,551
Processing and marketing	20,415	21,628
Farm-related business	8,096	8,066
Total agribusiness	30,055	31,245
Rural residential real estate	12,470	17,555
Lease receivables	35	207
Other (including mission-related)	9,283	11,901
Total nonaccrual loans	$ 636,843	$ 666,709
Accruing restructured loans:		
Real estate mortgage	$ 43,944	$ 41,793
Production and intermediate-term	29,868	31,523
Agribusiness		
Processing and marketing	–	24,606
Farm-related business	460	48
Total agribusiness	460	24,654
Rural residential real estate	1,573	1,373
Total accruing restructured loans	$ 75,845	$ 99,343
Accruing loans 90 days or more past due:		
Real estate mortgage	$ 962	$ 1,154
Production and intermediate-term	176	581
Rural residential real estate	3,383	4,583
Other (including mission-related)	–	1,238
Total accruing loans 90 days or more past due	$ 4,521	$ 7,556
Total nonperforming loans	$ 717,209	$ 773,608
Other property owned	139,892	158,144
Total nonperforming assets	$ 857,101	$ 931,752
Nonaccrual loans as a percentage of total loans	2.82%	2.97%
Nonperforming assets as a percentage of total loans and other property owned	3.77%	4.12%
Nonperforming assets as a percentage of capital	17.96%	20.61%

The following table presents information relating to impaired loans (including accrued interest) at June 30, 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.

(dollars in thousands)	**June 30, 2012**	**December 31, 2011**
Impaired nonaccrual loans:		
Current as to principal and interest	$ 251,707	$ 197,916
Past due	385,136	468,793
Total impaired nonaccrual loans	636,843	666,709
Impaired accrual loans:		
Restructured	75,845	99,343
90 days or more past due	4,521	7,556
Total impaired accrual loans	80,366	106,899
Total impaired loans	$ 717,209	$ 773,608

Additional impaired loan information as of June 30, 2012 and December 31, 2011 is summarized as follows:

	June 30, 2012			**Quarter Ended June 30, 2012**		**For the Six Months Ended June 30, 2012**	
(dollars in thousands)	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**
Impaired loans with a related allowance for credit losses:							
Real estate mortgage	$ 124,370	$ 157,113	$ 23,885	$ 115,333	$ 907	$ 120,767	$ 1,513
Production and intermediate-term	162,984	194,855	42,201	150,311	1,217	146,454	1,978
Agribusiness							
Loans to cooperatives	–	–	–	–	–	–	–
Processing and marketing	5,028	5,468	1,523	4,953	49	5,805	77
Farm-related business	6,931	8,034	944	6,795	72	6,163	102
Total agribusiness	11,959	13,502	2,467	11,748	121	11,968	179
Rural residential real estate	5,247	7,478	1,323	5,110	33	5,936	72
Lease receivables	–	–	–	–	–	–	–
Other (including mission-related)	3,366	3,262	280	3,316	51	1,667	51
Total	$ 307,926	$ 376,210	$ 70,156	$ 285,818	$ 2,329	$ 286,792	$ 3,793
Impaired loans with no related allowance for credit losses:							
Real estate mortgage	$ 207,909	$ 276,450	$ –	$ 209,328	$ 2,046	$ 212,359	$ 3,211
Production and intermediate-term	164,687	238,422	–	170,212	2,171	176,819	3,209
Agribusiness							
Loans to cooperatives	1,544	1,567	–	1,521	14	1,535	24
Processing and marketing	15,387	29,039	–	19,463	715	27,502	1,085
Farm-related business	1,625	3,305	–	1,594	3	2,737	24
Total agribusiness	18,556	33,911	–	22,578	732	31,774	1,133
Rural residential real estate	12,179	13,918	–	10,208	86	11,278	237
Lease receivables	35	85	–	34	(1)	117	1
Other (including mission-related)	5,917	15,769	–	6,134	21	8,460	76
Total	$ 409,283	$ 578,555	$ –	$ 418,494	$ 5,055	$ 440,807	$ 7,867
Total impaired loans:							
Real estate mortgage	$ 332,279	$ 433,563	$ 23,885	$ 324,661	$ 2,953	$ 333,126	$ 4,724
Production and intermediate-term	327,671	433,277	42,201	320,523	3,388	323,273	5,187
Agribusiness							
Loans to cooperatives	1,544	1,567	–	1,521	14	1,535	24
Processing and marketing	20,415	34,507	1,523	24,416	764	33,307	1,162
Farm-related business	8,556	11,339	944	8,389	75	8,900	126
Total agribusiness	30,515	47,413	2,467	34,326	853	43,742	1,312
Rural residential real estate	17,426	21,396	1,323	15,318	119	17,214	309
Lease receivables	35	85	–	34	(1)	117	1
Other (including mission-related)	9,283	19,031	280	9,450	72	10,127	127
Total	$ 717,209	$ 954,765	$ 70,156	$ 704,312	$ 7,384	$ 727,599	$ 11,660

	December 31, 2011			Year Ended December 31, 2011	
(dollars in thousands)	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ 121,212	$ 143,092	$ 22,652	$ 141,775	$ 2,295
Production and intermediate-term	139,753	186,637	37,916	171,089	2,920
Agribusiness					
Loans to cooperatives	–	–	–	190	–
Processing and marketing	7,723	8,192	1,386	19,970	81
Farm-related business	5,838	7,042	153	6,401	140
Total agribusiness	13,561	15,234	1,539	26,561	221
Energy/water and waste disposal	–	–	–	3,345	–
Rural residential real estate	7,216	9,211	2,073	6,121	162
Lease receivables	37	87	7	103	1
Other (including mission-related)	542	1,879	110	932	–
Total	$ 282,321	$ 356,140	$ 64,297	$ 349,926	$ 5,599
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 239,507	$ 316,615	$ –	$ 262,915	$ 5,317
Production and intermediate-term	180,380	269,949	–	197,867	4,001
Agribusiness					
Loans to cooperatives	1,551	1,580	–	3,115	38
Processing and marketing	38,511	52,708	–	44,022	2,117
Farm-related business	2,276	4,538	–	1,891	55
Total agribusiness	42,338	58,826	–	49,028	2,210
Energy/water and waste disposal	–	–	–	3,344	22
Rural residential real estate	16,295	18,644	–	13,139	301
Lease receivables	170	190	–	226	4
Other (including mission-related)	12,597	22,219	–	6,120	348
Total	$ 491,287	$ 686,443	$ –	$ 532,639	$ 12,203
Total impaired loans:					
Real estate mortgage	$ 360,719	$ 459,707	$ 22,652	$ 404,690	$ 7,612
Production and intermediate-term	320,133	456,586	37,916	368,956	6,921
Agribusiness					
Loans to cooperatives	1,551	1,580	–	3,305	38
Processing and marketing	46,234	60,900	1,386	63,992	2,198
Farm-related business	8,114	11,580	153	8,292	195
Total agribusiness	55,899	74,060	1,539	75,589	2,431
Energy/water and waste disposal	–	–	–	6,689	22
Rural residential real estate	23,511	27,855	2,073	19,260	463
Lease receivables	207	277	7	329	5
Other (including mission-related)	13,139	24,098	110	7,052	348
Total	$ 773,608	$ 1,042,583	$ 64,297	$ 882,565	$ 17,802

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 June 30, 2012 and December 31, 2011.

A summary of changes in the allowance for loan losses and period end recorded investment in loans at June 30, 2012 and December 31, 2011 follows:

(dollars in thousands)	Real Estate Mortgage	Production and Intermediate-term	Agribusiness	Communication	Energy and Water/Waste Disposal	Rural Residential Real Estate	Lease Receivables	Other Loans (including mission related)	Total
Allowance for credit losses:									
Balance at March 31, 2012	$ 65,448	$ 90,942	$ 13,788	$ 550	$ 688	$ 4,093	$ 14	$ 657	$ 176,180
Charge-offs	(12,138)	(6,943)	(181)	–	–	(806)	–	(118)	(20,186)
Recoveries	635	7,998	67	–	–	11	–	–	8,711
Provision for loan losses	11,900	(2,185)	(424)	181	422	285	3	202	10,384
Other	(41)	5	1	–	–	36	–	(1)	–
Balance at June 30, 2012	$ 65,804	$ 89,817	$ 13,251	$ 731	$ 1,110	$ 3,619	$ 17	$ 740	$ 175,089
Balance at December 31, 2011	$ 65,951	$ 89,155	$ 14,050	$ 482	$ 672	$ 4,015	$ 20	$ 631	$ 174,976
Charge-offs	(25,951)	(12,027)	(18)	–	–	(1,137)	–	(365)	(39,498)
Recoveries	4,650	9,856	72	–	–	59	–	–	14,637
Provision for loan losses	22,937	956	(816)	249	438	738	(3)	475	24,974
Other	(1,783)	1,877	(37)	–	–	(56)	–	(1)	–
Balance at June 30, 2012	$ 65,804	$ 89,817	$ 13,251	$ 731	$ 1,110	$ 3,619	$ 17	$ 740	$ 175,089
Balance at March 31, 2011	$ 68,375	$ 83,619	$ 23,973	$ 316	$ 3,699	$ 2,749	$ 100	$ 1,299	$ 184,130
Charge-offs	(12,058)	(20,041)	(19,779)	–	(3,426)	(302)	–	(679)	(56,285)
Recoveries	1,057	372	6	–	–	55	–	–	1,490
Provision for loan losses	12,528	28,059	10,541	70	3,381	777	(22)	(113)	55,221
Adjustment due to merger	(146)	146	–	–	–	–	–	–	–
Other	(38)	(56)	(24)	–	–	38	–	–	(80)
Balance at June 30, 2011	$ 69,718	$ 92,099	$ 14,717	$ 386	$ 3,654	$ 3,317	$ 78	$ 507	$ 184,476
Balance at December 31, 2010	$ 73,636	$ 83,759	$ 19,735	$ 415	$ 599	$ 3,117	$ 67	$ 1,001	$ 182,329
Charge-offs	(18,295)	(29,755)	(20,962)	–	(3,426)	(1,011)	(20)	(679)	(74,148)
Recoveries	1,592	992	32	825	–	59	–	–	3,500
Provision for loan losses	21,668	43,027	17,037	(844)	6,481	1,307	31	185	88,892
Adjustment due to merger	(8,845)	(5,948)	(1,101)	(10)	–	(193)	–	–	(16,097)
Other	(38)	24	(24)	–	–	38	–	–	–
Balance at June 30, 2011	$ 69,718	$ 92,099	$ 14,717	$ 386	$ 3,654	$ 3,317	$ 78	$ 507	$ 184,476
Loans individually evaluated for impairment	$ 23,413	$ 42,002	$ 2,334	$ –	$ –	$ 1,258	$ –	$ 280	$ 69,287
Loans collectively evaluated for impairment	41,919	47,616	10,784	731	1,110	2,296	17	460	104,933
Loans acquired with deteriorated credit quality	472	199	133	–	–	65	–	–	869
Balance at June 30, 2012	$ 65,804	$ 89,817	$ 13,251	$ 731	$ 1,110	$ 3,619	$ 17	$ 740	$ 175,089
Loans individually evaluated for impairment	$ 21,896	$ 37,767	$ 1,458	$ –	$ –	$ 2,012	$ 7	$ 110	$ 63,250
Loans collectively evaluated for impairment	43,300	51,238	12,511	482	672	1,942	13	521	110,679
Loans acquired with deteriorated credit quality	755	150	81	–	–	61	–	–	1,047
Balance at December 31, 2011	$ 65,951	$ 89,155	$ 14,050	$ 482	$ 672	$ 4,015	$ 20	$ 631	$ 174,976
Recorded investment in loans outstanding:									
Loans individually evaluated for impairment	$ 394,039	$ 310,117	$ 32,553	$ –	$ –	$ 2,111,363	$ 217	$ 4,360	$ 2,852,649
Loans collectively evaluated for impairment	9,423,001	7,520,712	1,690,191	271,851	458,034	432,994	5,718	77,096	19,879,597
Loans acquired with deteriorated credit quality	16,040	5,913	1,662	–	–	1,541	–	–	25,156
Ending balance at June 30, 2012	$ 9,833,080	$ 7,836,742	$ 1,724,406	$ 271,851	$ 458,034	$ 2,545,898	$ 5,935	$ 81,456	$ 22,757,402
Loans individually evaluated for impairment	$ 417,257	$ 278,187	$ 39,156	$ –	$ –	$ 2,058,195	$ 207	$ 2,778	$ 2,795,780
Loans collectively evaluated for impairment	9,400,695	7,713,687	1,687,985	213,810	310,357	418,774	2,788	81,806	19,829,902
Loans acquired with deteriorated credit quality	24,518	6,669	1,663	–	–	1,731	–	–	34,581
Ending balance at December 31, 2011	$ 9,842,470	$ 7,998,543	$ 1,728,804	$ 213,810	$ 310,357	$ 2,478,700	$ 2,995	$ 84,584	$ 22,660,263

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 June 30, 2012			
	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
Troubled debt restructurings:				
Real estate mortgage	$ 1,209	$ 15,011	$ 975	$ 17,195
Production and intermediate-term	1,475	16,603	67	18,145
Agribusiness				
Farm related business	694	3,722	321	4,737
Rural residential real estate	4	442	–	446
Total	$ 3,382	$ 35,778	$ 1,363	$ 40,523

	Three months ended June 30, 2012					
	Post-modification Outstanding Recorded Investment				Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Total	Provisions	Charge-offs
Troubled debt restructurings:						
Real estate mortgage	$ 1,209	$ 15,015	$ 945	$ 17,169	$ 391	$ (383)
Production and intermediate-term	679	16,858	68	17,605	403	(3)
Agribusiness						
Farm related business	692	3,722	321	4,735	(268)	–
Rural residential real estate	4	442	–	446	–	–
Total	$ 2,584	$ 36,037	$ 1,334	$ 39,955	$ 526	$ (386)

	Six months ended June 30, 2012			
	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
Troubled debt restructurings:				
Real estate mortgage	$ 5,209	$ 31,192	$ 1,009	$ 37,410
Production and intermediate-term	2,555	28,907	67	31,529
Agribusiness				
Farm related business	694	3,955	321	4,970
Rural residential real estate	4	607	78	689
Total	$ 8,462	$ 64,661	$ 1,475	$ 74,598

	Six months ended June 30, 2012					
	Post-modification Outstanding Recorded Investment				Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Total	Provisions	Charge-offs
Troubled debt restructurings:						
Real estate mortgage	$ 5,202	$ 31,054	$ 964	$ 37,220	$ 703	$ (383)
Production and intermediate-term	1,764	29,214	68	31,046	1,241	(5)
Agribusiness						
Farm related business	692	3,955	321	4,968	(268)	–
Rural residential real estate	4	611	78	693	105	(64)
Total	$ 7,662	$ 64,834	$ 1,431	$ 73,927	$ 1,781	$ (452)

	Three months ended June 30, 2011			
	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
Troubled debt restructurings:				
Real estate mortgage	$ 517	$ 18,600	$ –	$ 19,117
Production and intermediate-term	2,670	66,378	24,474	93,522
Agribusiness				
Processing and marketing	–	1,677	–	1,677
Rural residential real estate	–	1,032	–	1,032
Other/mission related	–	–	1,554	1,554
Total	$ 3,187	$ 87,687	$ 26,028	$ 116,902

	Three months ended June 30, 2011					
	Post-modification Outstanding Recorded Investment				Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Total	Provisions	Charge-offs
Troubled debt restructurings:						
Real estate mortgage	$ 527	$ 21,537	$ –	$ 22,064	$ 1,940	$ (1,859)
Production and intermediate-term	2,670	60,900	25,651	89,221	22,357	(23,760)
Agribusiness						
Processing and marketing	–	1,677	–	1,677	(296)	–
Rural residential real estate	–	1,032	–	1,032	–	–
Other/mission related	–	–	1,554	1,554	–	(679)
Total	$ 3,197	$ 85,146	$ 27,205	$ 115,548	$ 24,001	$ (26,298)

	Six months ended June 30, 2011			
	Pre-modification Outstanding Recorded Investment			
	Interest Concessions	Principal Concessions	Other Concessions	Total
Troubled debt restructurings:				
Real estate mortgage	$ 1,484	$ 29,995	$ 441	$ 31,920
Production and intermediate-term	3,100	99,999	31,309	134,408
Agribusiness				
Processing and marketing	–	1,677	–	1,677
Rural residential real estate	295	1,149	–	1,444
Other/mission related	–	–	1,554	1,554
Total	$ 4,879	$ 132,820	$ 33,304	$ 171,003

	Six months ended June 30, 2011					
	Post-modification Outstanding Recorded Investment				Effects of Modification	
	Interest Concessions	Principal Concessions	Other Concessions	Total	Provisions	Charge-offs
Troubled debt restructurings:						
Real estate mortgage	$ 1,478	$ 32,903	$ 438	$ 34,819	$ 3,053	$ (2,592)
Production and intermediate-term	3,089	94,482	29,207	126,778	23,140	(25,815)
Agribusiness						
Processing and marketing	–	1,677	–	1,677	(296)	–
Rural residential real estate	295	1,132	–	1,427	1	(5)
Other/mission related	–	–	1,554	1,554	–	(679)
Total	$ 4,862	$ 130,194	$ 31,199	$ 166,255	$ 25,898	$ (29,091)

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 outstanding recorded investment for TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the period. Payment default is defined as a payment that was thirty days or more past due.

	Three months ended June 30, 2012	Six months ended June 30, 2012
Defaulted troubled debt restructurings:		
Real estate mortgage	$ 4,663	$ 6,596
Production and intermediate-term	5,090	10,462
Agribusiness		
Farm-related business	–	1
Rural residential real estate	–	25
Total	$ 9,753	$ 17,084

TDRs outstanding at period end totaled $250,330, of which $174,485 were in nonaccrual status.

Purchased Impaired Loans

District entities acquire loans individually and in groups or portfolios. For certain acquired loans that experienced deterioration in credit quality between origination and acquisition, the amount paid for the loan will reflect this fact. At acquisition, each loan is reviewed to determine whether there is evidence of deterioration of credit quality since origination and if it is probable that the holder would be unable to collect all amounts due according to the loan's contractual terms. If both conditions exist, the purchaser determines whether each such loan is to be accounted for individually or whether such loans would be assembled into pools of loans based on common risk characteristics (credit score, loan type, and date of origination, for example). Considerations of value should include expected prepayments, the estimated amount and timing of undiscounted expected principal, interest, and other cash flows (expected at acquisition) for each loan and the subsequently aggregated pool of loans. Any excess of the loan's or pool's scheduled contractual principal and contractual interest payments over all of the cash flows expected at acquisition is an amount that should not be accreted to income (nonaccretable difference). The remaining amount, representing the excess of the loan's cash flows expected to be collected over the amount paid, is accreted into interest income over the remaining life of the loan or pool (accretable yield).

Accounting guidance requires that the purchaser continue to estimate cash flows expected to be collected over the life of the loan or pool. It then evaluates at the balance sheet date whether the present value of its loans, determined using the effective interest rate, has decreased and if so, recognizes a loss. For loans or pools that are not accounted for as debt securities, the present value of any subsequent increase in the loan's or pool's actual cash flows or cash flows expected to be collected is used first to reverse any existing valuation allowance for that loan or pool. For any remaining increases in cash flows expected to be collected, or for loans or pools accounted for as debt securities, a purchaser adjusts the amount of accretable yield recognized on a prospective basis over the loan's or pool's remaining life.

Valuation allowances for all purchased impaired loans reflect only those losses incurred after acquisition, that is, the present value of cash flows expected at acquisition that are not expected to be collected. Valuation allowances are established only subsequent to acquisition of the loans.

As discussed in Note 12, effective January 1, 2011, Farm Credit of North Florida, ACA (NFL), and Farm Credit of Southwest Florida, ACA (SWFL), merged with and into Farm Credit of South Florida, ACA (SFL), which then changed its name to Farm Credit of Florida, ACA (FCFL). The merger was accounted for under the acquisition method of accounting guidance.

In connection with the merger, SFL (now FCFL) purchased impaired loans from NFL and SWFL that are not accounted for as debt securities. The carrying amounts of those loans included in the balance sheet amounts of loans receivable at June 30, 2012, were as follows.

(dollars in thousands)		**June 30, 2012**
Real estate mortgage	$	16,040
Production and intermediate-term		5,913
Agribusiness		
Loans to cooperatives		–
Processing and marketing		–
Farm-related business		1,662
Total agribusiness		1,662
Communication		–
Energy		–
Rural residential real estate		1,541
Total Loans	$	25,156

At June 30, 2012, the allowance for loan losses related to these loans was $869 thousand compared with $1.0 million at December 31, 2011. During the period ended June 30, 2012, provision expense on these loans was $45 thousand compared with $1.1 million for the quarter ended June 30, 2011. There were no reversals of allowance for loan losses during the periods presented for these acquired loans. See above for a summary of changes in the total allowance for loan losses for the period ended June 30, 2012.

There were no loans acquired during 2012 for which it was probable at acquisition that all contractually required payments would not be collected. The total of loans acquired during 2011 for which it was probable at acquisition that all contractually required payments would not be collected are as follows.

(dollars in thousands)		
Real estate mortgage	$	57,735
Production and intermediate-term		18,862
Agribusiness		
Loans to cooperatives		–
Processing and marketing		2,196
Farm-related business		1,734
Total agribusiness		3,930
Communication		–
Energy		–
Rural residential real estate		1,769
Total Loans	$	82,296

Certain of the loans acquired by FCFL in the business combination that are within the scope of purchased impaired loan guidance are accounted for using a cash basis method of income recognition because FCFL cannot reasonably estimate cash flows expected to be collected. Substantially all of the loans acquired were real estate collateral dependent loans. As discussed previously, the real estate market in Florida is extremely unstable, making estimation of the amount and timing of a sale of loan collateral in essentially the same condition as received upon foreclosure indeterminate. As such, FCFL does not have the information necessary to reasonably estimate cash flows expected to be collected to compute its yield. Management determined a nonaccrual classification would be the most appropriate and that no income would be recognized on these loans as is allowed under accounting guidance.

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 District, 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, loans, other property owned, bonds and notes, and collateral liabilities.

Fair value is defined 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 District'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 District 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 District'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 District'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.

Following the market disruptions of 2008, the District began considering 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 estimating the fair values of securities in the asset-backed and most of the non-agency CMO portfolios, as well as, the resulting unrealized gain/loss impact through AOCI. The markets for these types of securities had become inactive and the prices were reflecting distressed and forced sales as evidenced by the volatility. Over time, the valuations received from the pricing service have converged toward a more reasonable correlation with our understanding of the underlying credit factors and financial metrics of these securities, though the markets remain inactive. Management believes that values supplied by the third party pricing service are currently sufficiently consistent with GAAP and that it is appropriate to return to the methodology used prior to 2009; that being the use of third party pricing alone to reflect the fair values of these portfolios in financial reporting. This methodology change resulted in a decrease of $13.8 million for the total combined fair value of these two portfolios at June 30, 2012.

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 District'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. In tandem with the latest guidance on fair value measurement and disclosure, and movement to available for sale classification, $51.9 million of Mission Related Investments were transferred from Level 2 to Level 3 status effective March 31, 2012. The District had no transfers of assets or liabilities into or out of Level 1 during the reporting period.

(dollars in thousands)	**Asset-Backed Investment Securities**	**Non-Agency CMOs**	**Standby Letters of Credit**	**Mission Related Investments**
Balance at January 1, 2012	$ 30,324	$ 241,756	$ 3,073	$ –
Total gains or (losses) realized/unrealized:				
Included in earnings	–	(3,167)	–	–
Included in other comprehensive income (loss)	3,840	(7,262)	–	1,301
Purchases	–	–	–	188
Sales	–	–	–	–
Issuances	–	–	46	–
Settlements	(2,261)	(21,979)	(78)	(103)
Transfers in and/or out of level 3	–	–	–	51,884
Balance at June 30, 2012	$ 31,903	$ 209,348	$ 3,041	$ 53,270

(dollars in thousands)		Asset-Backed Investment Securities		Non-Agency CMOs		Standby Letters Of Credit
Balance at January 1, 2011	$	34,437	$	295,526	$	3,336
Total gains or (losses) realized/unrealized:						
Included in earnings		(2,963)		(4,527)		–
Included in other comprehensive income (loss)		1,353		8,850		–
Purchases		–		–		–
Sales		–		–		–
Issuances		–		–		905
Settlements		(3,375)		(40,520)		(280)
Transfers in and/or out of level 3		–		–		–
Balance at June 30, 2011	$	29,452	$	259,329	$	3,961

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 District'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.

The significant unobservable inputs used to estimate fair value for Level 3 assets and liabilities that are obtained from third party vendors are not included in the table as the specific inputs applied are not provided by the vendor.

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Valuation Technique(s)	Unobservable Input	Range
Firm commitments-when issued securities	Broker/Consensus pricing	Offered quotes	103.542 – 103.933
Mission Related Investments	Discounted cash flow	Probability of default	0% – 16%
		Risk adjusted spread	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

	Valuation Technique(s)	Input
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

	Valuation Technique(s)	Input
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 rates Probability of default Loss severity
Accrued interest	Carrying value	Coupon interest rates
Assets held in trust funds	Quoted prices	Price for identical security
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:

	June 30, 2012					
(dollars in thousands)	**Total Carrying Amount**	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**	**Fair Value Effects On Comprehensive Income**
<u>Recurring Measurements</u>						
Assets:						
Investments available-for-sale:						
U.S. Govt. GNMA MBS/CMOs	$ 4,807,108	$ –	$ 4,807,108	$ –	$ 4,807,108	
U.S. Govt. Agency MBS	1,588,508	–	1,588,508	–	1,588,508	
Non-Agency CMOs	209,786	–	438	209,348	209,786	
Asset-backed securities	31,903	–	–	31,903	31,903	
Mission Related Investments	53,270	–	–	53,270	53,270	
Total investments available-for-sale	6,690,575	–	6,396,054	294,521	6,690,575	
Federal funds sold, securities purchased under resale agreements, and other	149,302	–	149,302	–	149,302	
Interest rate swaps and other derivative instruments	48,587	–	47,858	729	48,587	
Assets held in trust funds	12,524	12,524	–	–	12,524	
Recurring Assets	$ 6,900,988	$ 12,524	$ 6,593,214	$ 295,250	$ 6,900,988	
Liabilities:						
Interest rate swaps and other derivative instruments	$ 23	$ –	$ –	$ 23	$ 23	
Collateral liabilities	1,359	–	1,359	–	1,359	
Standby letters of credit	3,041	–	–	3,041	3,041	
Recurring Liabilities	$ 4,423	$ –	$ 1,359	$ 3,064	$ 4,423	
<u>Nonrecurring Measurements</u>						
Assets:						
Impaired loans	$ 647,053	$ –	$ –	$ 647,053	$ 647,053	$ (30,721)
Other property owned	139,892	–	–	152,261	152,261	(19,472)
Nonrecurring Assets	$ 786,945	$ –	$ –	$ 799,314	$ 799,314	$ (50,193)
<u>Other Financial Instruments</u>						
Assets:						
Cash	$ 1,221,624	$ 1,221,624	$ –	$ –	$ 1,221,624	
Investments held to maturity	852,905		699,023	224,684	923,707	
Loans	21,775,211	–	–	22,090,285	22,090,285	
Other investments	159,097	–	–	164,918	164,918	
Accrued interest receivable	192,153	–	192,153	–	192,153	
Other Assets	$ 24,200,990	$ 1,221,624	$ 891,176	$ 22,479,887	$ 24,592,687	
Liabilities:						
Systemwide debt securities	$ 26,666,400	$ –	$ –	$ 26,784,392	$ 26,784,392	
Accrued interest payable	42,795	–	42,795	–	42,795	
Other Liabilities	$ 26,709,195	$ –	$ 42,795	$ 26,784,392	$ 26,827,187	

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:

	December 31, 2011			
(dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Assets:				
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	–	475	241,756	242,231
Asset-Backed Securities	–	–	30,324	30,324
Mission Related Investments	–	54,220	–	54,220
Total Investments Available-for-sale	–	6,708,025	272,080	6,980,105
Federal funds sold, securities purchased under resale agreements, and other	–	83,822	–	83,822
Interest rate swaps and other derivative instruments	–	52,647	–	52,647
Assets held in trust funds	11,999	–	–	11,999
Total Assets	$ 11,999	$ 6,844,494	$ 272,080	$ 7,128,573
Liabilities:				
Collateral liabilities	$ –	$ 22,139	$ –	$ 22,139
Standby letters of credit	–	–	3,073	3,073
Total Liabilities	$ –	$ 22,139	$ 3,073	$ 25,212

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:

	December 31, 2011				
(dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**	**Total Gains (Losses)**
Assets:					
Impaired loans *	$ –	$ –	$ 221,638	$ 221,638	$ (206,517)
Other property owned *	$ –	$ –	$ 163,531	$ 163,531	$ (36,203)

** In accordance with FASB guidance in effect at December 31, 2011, amounts include only those assets remeasured during the reporting period. The fair value of total impaired loans at period end was $709,311 and the fair value of other property owned was $171,914.*

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

	December 31, 2011	
(dollars in thousands)	**Carrying Amount**	**Estimated Fair Value**
Financial assets:		
Loans, net of allowance	$ 22,306,529	$ 22,607,264
Derivative assets	$ 52,647	$ 52,647
Cash & cash equivalents	$ 1,340,167	$ 1,340,167
Investment securities	$ 7,955,553	$ 8,014,358
Other investments	$ 238,552	$ 246,822
Accrued interest receivable	$ 197,782	$ 197,782
Assets held in trust funds	$ 11,999	$ 11,999
Financial liabilities:		
Bonds and notes	$ 27,331,009	$ 27,464,145

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 $190.678 billion at June 30, 2012.

Legal actions are pending against the District in which claims for money damages are asserted. On the basis of information presently available, management and legal counsel are of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the combined financial position of AgFirst and District Associations.

NOTE 6 — EMPLOYEE BENEFIT PLANS

Following are retirement and other postretirement benefit expenses for the District:

	For the six months ended June 30,	
(dollars in thousands)	**2012**	**2011**
Pension	$ 23,595	$ 23,690
401k	3,369	3,214
Other postretirement benefits	4,098	5,175
Total	$ 31,062	$ 32,079

Following are retirement and other postretirement benefit contributions for the District. Projections are based upon actuarially determined amounts as of the most recent measurement date of December 31, 2011.

(dollars in thousands)	**Actual YTD Through 6/30/12**	**Projected Contributions for Remainder of 2012**	**Projected Total Contributions 2012**
Pensions	$ 324	$ 47,094	$ 47,418
Other postretirement benefits	3,447	3,273	6,720
Total	$ 3,771	$ 50,367	$ 54,138

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the District 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 District'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 District 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 District 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 District 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 District to raise long-term borrowings at fixed rates and swap them into floating rates that are lower than those available to the District if floating rate borrowings were made directly. Under these arrangements, the District 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 District 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 District 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 District's gains or losses on the derivative instruments that are linked to these hedged assets and liabilities. The District 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 six months ended June 30, 2012 is summarized in the following table:

Notional Amounts *(dollars in millions)*	**Receive-Fixed Swaps**	**Forward Contracts**
Balance at beginning of period	$ 535	$ 66
Additions	–	427
Maturities/amortization	–	(66)
Terminations	–	–
Balance at end of period	$ 535	$ 427

By using derivative instruments, the District exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, the District'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 District, thus creating a repayment risk for the District. When the fair value of the derivative contract is negative, the District owes the counterparty and, therefore, assumes no repayment risk.

To minimize the risk of credit losses, the District 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 June 30, 2012 of $47.9 million was with five counterparties and represented approximately 8.95 percent of the total notional amount of interest rate swaps. The District held $1.4 million of interest-bearing cash collateral and U.S. Treasury securities with a fair value of $20.3 million, posted by one counterparty related to these swaps. The District 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 District held $22.1 million of interest-bearing cash collateral posted by one counterparty related to these swaps. The District typically enters into master agreements that contain netting provisions. These provisions allow the District 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 District had not posted collateral with respect to any of these arrangements.

The District's derivative activities which are performed by the Bank, are monitored by its Asset-Liability Management Committee (ALCO) as part of the Committee's oversight of the District'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 District'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 six months ended June 30, 2012 was $4.8 million, while the amount of the gain on the Systemwide Debt Securities was $4.8 million. The amount of the loss on interest rate swaps recognized in interest expense for the six months ended June 30, 2011 was $10.3

million, while the amount of the gain on the Systemwide Debt Securities was $10.3 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 District 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 District'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 District's Combined Balance Sheet for each period end. At June 30, 2012, the District had committed to purchase $426.8 million in when-issued GNMA bonds that had a market value of $427.6 million, a $729 thousand increase in value. At December 31, 2011, the District 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 District'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 June 30, 2012 and December 31, 2011:

(dollars in thousands)	Balance Sheet Classification – Assets	6/30/12 Fair Value	Balance Sheet Classification - Liabilities	6/30/12 Fair Value
Derivatives designated as hedging instruments:				
Receive-fixed swaps	Other Assets	$ 47,858	Other Liabilities	$ –
Forward contracts	Other Assets	729	Other Liabilities	23
Total		$ 48,587		$ 23

(dollars in thousands)	Balance Sheet Classification - Assets	12/31/11 Fair Value	Balance Sheet Classification – Liabilities	12/31/11 Fair Value
Derivatives designated as hedging instruments:				
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 Combined Statements of Income for the six months ended June 30, 2012 and 2011.

(dollars in thousands)	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
Derivatives – Fair Value Hedging Relationships:			
Receive-fixed swaps	Noninterest Income	$ –	$ –
Total		$ –	$ –

The following table sets forth the amount of net gain (loss) recognized in the Combined Statements of Income for the six months ended June 30, 2012 and 2011 and the amount of net gain (loss) recognized in the Combined Balance Sheets for June 30, 2012 and December 31, 2011.

(dollars in thousands)	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**
Derivatives – Cash Flow Hedging Relationships:								
Firm Commitments	$ 1,509	$ 1,810	Interest Income	$ 299	$ (270)	Interest Income	$ –	$ –

NOTE 8 – PERPETUAL PREFERRED STOCK

During the first half 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 $118.6 million. The effect of the repurchases on shareholders' equity was to reduce preferred stock outstanding by $118.6 million and record $34.1 million of additional paid-in-capital.

NOTE 9 - ACCUMULATED OTHER COMPREHENSIVE INCOME

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

(dollars in thousands)	Unrealized gains (losses) on Investments	Firm Commitments	Employee Benefit Plans	Accumulated Other Comprehensive Income
Balance at December 31, 2011	$ 139,367	$ (5,565)	$ (355,050)	$ (221,248)
Other comprehensive income	14,428	1,210	14,511	30,149
Balance at June 30, 2012	153,795	(4,355)	(340,539)	(191,099)
Balance at December 31, 2010	43,337	(8,751)	(326,166)	(291,580)
Other comprehensive income	48,300	2,080	14,527	64,907
Balance at June 30, 2011	$ 91,637	$ (6,671)	$ (311,639)	$ (226,673)

	For the three months ended June 30,		For the six months ended June 30,	
(dollars in thousands)	**2012**	**2011**	**2012**	**2011**
Other Comprehensive Income and Reclassification Amounts:				
Unrealized holding gains (losses) for period	$ 1,299	$ 64,481	$ 11,248	$ 43,163
Amounts reclassified to (gains) losses in net income	–	(2,973)	–	(2,973)
Amounts reclassified to other-than-temporary impairment in net income	2,418	3,652	3,180	8,110
Unrealized gains (losses) on securities, net	3,717	65,160	14,428	48,300
Change in value of cash flow hedges	706	3,678	1,509	1,810
Amounts reclassified to net income	(151)	154	(299)	270
Other	–	–	–	–
Change associated with cash flow hedges, net	555	3,832	1,210	2,080
Prior service cost from plan amendment during period	–	–	–	–
Amounts reclassified to net periodic pension costs	7,255	7,193	14,511	14,527
Net prior service cost	–	–	–	–
Net gain (loss) during period	–	–	–	–
Defined benefit post retirement plans, net	$ 7,255	$ 7,193	$ 14,511	$ 14,527

NOTE 10 — BANK ONLY FINANCIAL DATA

Condensed financial information of AgFirst Farm Credit Bank follows:

Balance Sheet Data

(dollars in thousands)	6/30/12	12/31/11
	(unaudited)	*(audited)*
Cash, cash equivalents and investment securities	$ 8,567,921	$ 9,081,841
Loans	19,985,783	20,152,066
Less: allowance for loan losses	27,981	27,714
Net loans	19,957,802	20,124,352
Other assets	340,483	371,313
Total assets	$ 28,866,206	$ 29,577,506
Bonds and notes	$ 26,464,757	$ 27,086,148
Other liabilities	96,928	342,088
Total liabilities	26,561,685	27,428,236
Perpetual preferred stock	281,450	400,000
Capital stock and participation certificates	398,072	405,767
Additional paid-in-capital	34,100	–
Retained earnings	1,450,062	1,219,506
Accumulated other comprehensive income (loss)	140,837	123,997
Total shareholders' equity	2,304,521	2,149,270
Total liabilities and equity	$ 28,866,206	$ 29,577,506

Statement of Income Data

	For the six months ended June 30,	
(dollars in thousands)	2012	2011
	(unaudited)	*(unaudited)*
Interest income	$ 418,125	$ 451,033
Interest expense	110,068	158,511
Net interest income	308,057	292,522
Provision for loan losses	(2,895)	30,276
Net interest income after provision for loan losses	310,952	262,246
Noninterest expense, net	57,746	54,236
Net income	$ 253,206	$ 208,010

NOTE 11 — REGULATORY ENFORCEMENT MATTERS

At June 30, 2012, FCA had entered into written supervisory agreements with four District Associations with combined assets of approximately $1.847 billion. Those agreements require the four District Associations to take corrective actions with respect to certain areas of their operations, including, as applicable, capital, portfolio management, asset quality, management succession, and board governance. These enforcement actions are not expected to have a significant impact on the Bank's or District's financial condition or results of operations.

NOTE 12 – DISTRICT MERGER ACTIVITY

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, after the FCA granted final approval of the merger on December 20, 2010. Farm Credit of South Florida then changed its name to Farm Credit of Florida, ACA. The merger was accounted for under the acquisition method of accounting.

Prior to the merger, those Associations entered into an agreement with the Bank under which the Bank would provide limited financial assistance to the merged Association in the event of substantial further deterioration in the combined high risk asset portfolio of the merged Association. This agreement relates only to a finite pool of high risk assets of the merged Association existing at the merger date, which had a net total of approximately $144.7 million and $250.0 million at June 30, 2012 and January 1, 2011, respectively. Through this agreement, the merged Association will absorb substantial losses on these high risk assets in advance of the Bank providing financial assistance. This financial "safety net" from the Bank does not include losses that are sustained outside of the high risk asset pool. The agreement provides protection to the Bank, such as limitation on the Association's ability to make patronage distributions and certain other restrictions which are imposed if the merged Association's capital levels fail to meet minimum established levels. Assistance under the agreement, if any, is not expected to have a material impact on the financial condition of the Bank or District.

As the accounting acquirer, South Florida accounted for the transaction by using its historical information and accounting policies and adding the identifiable assets and liabilities of North Florida and Southwest Florida as of the acquisition date of January 1, 2011 at their respective fair values.

As cooperative organizations, Farm Credit associations operate for the mutual benefit of their borrowers and other customers, and not for the benefit of equity investors. As such, their capital stock provides no significant interest in corporate earnings or growth. Specifically, due to restrictions in applicable regulations and the bylaws, the associations can issue stock only at its par value of $5 per share, the stock is not tradable, and the stock can be retired only for the lesser of par value or book value. In these and other respects, the shares of North Florida and Southwest Florida stock that were converted in the merger and the shares of Farm Credit of Florida's stock to which they were converted had identical rights and attributes. For this reason, the conversion of North Florida and Southwest Florida stock pursuant to the merger occurred at a one-for-one exchange ratio (i.e., each North Florida and Southwest Florida share was converted into one share of Florida's stock with an equal par value).

Management believes that because the stock in each Association is fixed in value (although subject to impairment), the Association's stock issued pursuant to the merger provides no basis for estimating the fair value of the consideration transferred pursuant to the merger. In the absence of a purchase price determination, the Association identified and estimated the acquisition date fair value of North Florida and Southwest Florida's equity interests instead of the fair value of South Florida's equity interests transferred as consideration. The fair value of the assets acquired, including specific intangible assets and liabilities assumed from North Florida and Southwest Florida, was measured based on various estimates using assumptions that the Association's management believes are reasonable utilizing information currently available. Use of different estimates and judgments could yield materially different results. This evaluation produced a fair value of identifiable assets acquired and liabilities assumed that was substantially equal to the fair value of the member interests transferred in the merger. As a result, management recorded no goodwill.

The following table reflects the identifiable assets acquired and liabilities assumed from North Florida and Southwest Florida, the acquisition adjustment and the merged entity balances at January 1, 2011:

Consolidation of Assets Acquired and Liabilities Assumed at January 1, 2011

	SW Florida	North Florida	Acquisition Adjustment	Acquisition Values	South Florida	Florida
Assets						
Cash	$ –	$ 13	$ –	$ 13	$ 2,790	$ 2,803
Investment securities:						
Held to maturity	40,097	–	(544)	39,553	1,987	41,540
Loans	231,555	404,425	(34,755)	601,225	559,912	1,161,137
Less: allowance for loan losses	(4,483)	(11,614)	16,097	–	(10,679)	(10,679)
Net loans	227,072	392,811	(18,658)	601,225	549,233	1,150,458
Other investments	–	10,211	428	10,639	–	10,639
Accrued interest receivable	1,405	1,871	–	3,276	2,086	5,362
Investments in other Farm Credit institutions	6,495	9,486	–	15,981	8,716	24,697
Premises and equipment, net	867	2,575	–	3,442	5,348	8,790
Other property owned	2,173	6,310	–	8,483	4,516	12,999
Due from AgFirst Farm Credit Bank	2,337	4,038	–	6,375	4,484	10,859
Other assets	4,924	3,887	–	8,811	4,658	13,469
Total assets	$ 285,370	$ 431,202	$ (18,774)	$ 697,798	$ 583,818	$ 1,281,616
Liabilities						
Notes payable to AgFirst Farm Credit Bank	$ 240,578	$ 366,559	$ 4,691	$ 611,828	$ 454,284	$ 1,066,112
Accrued interest payable	482	823	–	1,305	1,006	2,311
Patronage refund payable	15	40	–	55	671	726
Advanced conditional payments	–	407	–	407	3,710	4,117
Other liabilities	3,312	4,345	–	7,657	5,119	12,776
Total liabilities	244,387	372,174	4,691	621,252	464,790	1,086,042
Commitments and contingencies						
Members' Equity						
Protected borrower stock	228	40	(1)	267	2,463	2,730
Capital stock and participation certificates	525	1,411	–	1,936	635	2,571
Additional paid-in-capital	–	–	7,994	7,994	(121)	7,873
Retained earnings						
Allocated	25,592	40,872	–	66,464	30,879	97,343
Unallocated	14,753	16,705	(31,458)	–	85,057	85,057
Accumulated other comprehensive income (loss)	(115)	–	–	(115)	115	–
Total members' equity	40,983	59,028	(23,465)	76,546	119,028	195,574
Total liabilities and members' equity	$ 285,370	$ 431,202	$ (18,774)	$ 697,798	$ 583,818	$ 1,281,616

Disclosures related to acquired impaired loans are contained in Note 3, Loans and Allowance for Loan Losses.

The acquisition method of accounting requires the financial statement presentation of combined balances as of the date of the merger, but of only the acquirer for previous periods.

Effective July 1, 2012, Chattanooga, ACA, merged with and into Jackson Purchase, ACA, after the Farm Credit Administration granted final approval of the merger on June 26, 2012. Jackson Purchase, ACA, then changed its name to River Valley AgCredit, ACA. The merger was accounted for under the acquisition method of accounting.

NOTE 13 — SUBSEQUENT EVENTS

The District has evaluated subsequent events and has determined that, except as described in Note 12 above, there are none requiring disclosure through August 8, 2012, which is the date the financial statements were issued.