

# SECOND QUARTER 2019

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## CERTIFICATION

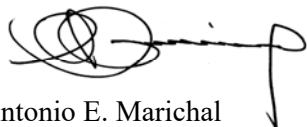
The undersigned certify that we have reviewed the June 30, 2019 quarterly report of Puerto Rico Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



Víctor M. Ayala Benítez  
Chairman of Board of Directors



Ricardo L. Fernández  
Chief Executive Officer



Antonio E. Marichal  
Member of Board of Directors  
Chairman of the Audit Committee

August 8, 2019


# Report on Internal Control Over Financial Reporting

The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's 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 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 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 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 Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Association's assets that could have a material effect on its Consolidated Financial Statements.

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of June 30, 2019. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association's management concluded that as of June 30, 2019, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association's management determined that there were no material weaknesses in the internal control over financial reporting as of June 30, 2019.



Ricardo L. Fernández  
Chief Executive Officer

August 8, 2019

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

*(dollars in thousands)*

The following commentary reviews the consolidated financial condition and results of operations of Puerto Rico Farm Credit, ACA (Association) for the period ended June 30, 2019. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements, and the 2018 annual report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

## **LOAN PORTFOLIO**

The Association provides funds to farmers, rural homeowners, and farm-related businesses for financing short and intermediate-term loans and long-term real estate mortgage loans. The Association also maintains a portfolio of purchased loans, originated by other Farm Credit System entities and non-system entities. The Association's predominant chartered territory (CT) agricultural commodities were dairy, fruits (including plantains and coffee) and rural housing which totaled approximately \$70,933 or 48.19 percent of the gross principal balance, net of sold loans, at June 30, 2019.

The outstanding loan volume of the Association at June 30, 2019 was \$146,200 a decrease of \$2,889 or 1.94 percent as compared to \$149,089 at December 31, 2018. Loans originated within the Association's chartered territory were lower by approximately \$4,069 and participation loans purchased increased by approximately \$1,180. The loan volume decrease was a result of paydowns in chartered territory loans. Increases in interest rates have led to lower demand for credit and for additional paydowns to take place as well.

Net loans outstanding at June 30, 2019 totaled \$144,584 as compared to \$147,403 at December 31, 2018. Net loans made up 94.76 percent of total assets at June 30, 2019, as compared to 93.80 percent at December 31, 2018.

Non-accrual loans totaled \$6,672 or 4.56 percent of total loans at June 30, 2019, compared to \$1,929 or 1.29 percent of total loans at December 31, 2018. Nonaccrual loans increased during the six months of 2019 primarily due to a \$4,741 CT loan transferred from accrual to nonaccrual status.

The overall delinquency rate for the accruing loan portfolio decreased during the second quarter 2019. Management expects that high risk loans may increase slightly by the end of the year if another natural event were to hit Puerto Rico. Otherwise, it does not expect any increase in delinquency or high risk loans.

The allowance for loan losses decreased \$70 to \$1,616 at June 30, 2019 from \$1,686 at December 31, 2018. The decrease was primarily due to a decrease in the general reserve for CT collateral risk, among other decreases on various CT and PL accruing industries, partially offset by an increase in the CT specific reserves and increases in the general reserves for CT dairy and CT processing industries. Management will continue to monitor certain risks, such as collateral risk and other factors that may increase the risk of the portfolio, such as climate conditions, government fiscal policy and overall economic conditions on the island. The total allowance for loan losses to outstanding loan volume decreased to 1.11 percent at June 30, 2019 from 1.13 percent at December 31, 2018.

During the first six months of 2019, a charge-off of \$76 was recognized on a CT nonaccrual loan. Also, a recovery of \$5 was recognized on a CT nonaccrual loan that liquidated. The Association is actively marketing acquired properties and may incur additional accounting losses or gains as sales are completed.

The economic output of the island decreased again in 2018 as disaster relief funds did not arrive as expected. The unofficial GDP reduction is estimated at 4.7% for fiscal year 2018. It is expected to decrease again in fiscal 2019 for the same reasons. The economy was expected to improve slightly in 2020 but recent events that led to the resignation of the Governor will most likely have a negative impact on the economy by delaying federal funds and lowering investment on the island. The long-term challenge continues to be implementing a sustainable economic model that promotes investment and is free of political biases.

The fiscal oversight board, established in 2016 under the PROMESA Act, is in charge of correcting the government finances while allowing the repayment of government debt exceeding \$70 billion. The fiscal oversight board has been less effective than originally expected as the Act is unclear on certain matters and legal disputes have limited the board's effectiveness to comply with the requirements of the Act. Management actively monitors corrective measures taken by the government

or imposed by the fiscal oversight board that could significantly impact economic activity and/or agricultural production in the island, that could in turn, negatively impact the business of the Association.

The Association has sufficient capital to withstand considerable deterioration in credit quality as a result of continuing adverse economic conditions or other natural disasters of large magnitude.

Through all this, the agricultural sector's outlook is stable and should remain as such over the next year as local food production is only 10% of food consumed in Puerto Rico. This should allow farmers to continue managing their operations profitably and maintain the credit quality of the Association's portfolio.

The local dairy industry continues to struggle in 2019 as supply is exceeding demand and farmers are receiving lower prices. The Association continues to monitor events within the industry and their potential impact on the performance of the dairy portfolio. The Association lends almost 30% of total loans to this industry and has implemented risk management practices to reduce overall risk.

Other agricultural sectors do not represent significant risk for the association. Management monitors all sectors and does not anticipate any adverse impact to the portfolio in 2019.

As mentioned before, the Association continues to identify opportunities that allow it to fulfill its public mission. The Board of Directors and management remain cautious of the Association's ability to quickly grow the portfolio under the prevailing economic environment. Management will focus on establishing strategic alliances that promote agricultural production growth and targeted marketing to viable farmers in sectors demonstrating the ability to grow and remain competitive in a changing marketplace.

## RESULTS OF OPERATIONS

### For the three months ended June 30, 2019

The Association recorded net income for the three months ended June 30, 2019 of \$500 as compared to \$449 for the same period in 2018. This \$51 increase in net income is primarily attributed to an increase in noninterest income.

Net interest income was \$1,278 for the three months ended June 30, 2019 compared to \$1,263 for the same period in 2018, representing an increase of \$15 or 1.19 percent attributed to the increases in the Prime Rate.

Provision for loan losses was \$45 for the three months ended June 30, 2019 compared to a reversal of allowance for loan losses of \$28 for the same period in 2018. During the second quarter 2019, the provision for loan losses was mainly due to an increase in general reserve for the CT dairy industry.

Noninterest income for the three months ended June 30, 2019 totaled \$325 compared to \$263 for the same period of 2018, resulting in an increase of \$62 or 23.57 percent. This increase was mainly due to an increase in gains on other transactions as a result of a reversal of the reserve for unfunded commitments.

Noninterest expense was \$1,059 for the three months ended June 30, 2019 as compared to \$1,105 for the same period in 2018, resulting in a decrease of \$46 or 4.16 percent. This decrease was primarily due to a decrease of \$102 in other operating expenses partially offset by an increase of \$61 in salaries and employee benefits.

### For the six months ended June 30, 2019

Net income for the six months ended June 30, 2019 totaled \$1,177 compared to \$1,326 for the same period in 2018, a decrease of \$149 or 11.24 percent. The decrease was mainly due to a decrease in insurance fund refunds from the Farm Credit System Corporation (FCSIC).

Net interest income increased \$243 or 10.09 percent to \$2,652 for the six months ended June 30, 2019, from \$2,409 for the same period in 2018. The increase is attributed to an increase in interest income compared to prior year.

Provision for loan losses increased \$44 for the six months ended June 30, 2019 compared to the same period in 2018. In 2018, an improvement in collateral risk within the loan portfolio allowed the Association to recognize a larger reversal of allowance for loan losses compared to the same period in 2019.

Noninterest income for the six months ended June 30, 2019 totaled \$589 as compared to \$916 for the same period in 2018, a decrease of \$327 or 35.70 percent. The decrease was mainly due to a \$316 decrease in insurance fund refunds from the Farm Credit System Insurance Corporation (FCSIC).

In 2019 and 2018, the Association recorded \$23 and \$339, respectively, of insurance premium refunds from the Farm Credit System Insurance Corporation (FCSIC), which insures the System's debt obligations. The amount is reflected in noninterest income on the Consolidated Statements of Comprehensive Income. These payments are nonrecurring and resulted from the assets of the Farm Credit Insurance Fund exceeding the secure base amount as defined by the Farm Credit Act.

Noninterest expense was \$2,064 for the six months ended June 30, 2019 as compared to \$2,042 for the same period in 2018, an increase of \$22 or 1.08 percent. The increase was primarily related to an increase in salaries and employee benefits of \$136 partially offset by a decrease of \$98 in other operating expenses.

Although the Association is subject to federal income tax, the Association does not expect to incur a federal tax liability in

2019 due to the taxable loss carryforward. A benefit of \$1 for income taxes has been recognized in 2019.

## LIQUIDITY AND FUNDING SOURCES

### Liquidity

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses, and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. Sufficient liquid funds have been available to meet all financial obligations.

### Funding Sources

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate notes. The variable rate notes are utilized by the Association to fund variable rate loan advances and operating fund requirements. The fixed rate notes are used specifically to fund fixed rate loan advances made by the Association.

The total notes payable to the Bank at June 30, 2019 was \$95,265 as compared to \$97,533 at December 31, 2018. The decrease of \$2,268 or 2.33 percent is primarily due to a decrease in loan volume outstanding during the period. The Association had no lines of credit outstanding with third parties as of June 30, 2019.

### Funds Management

The Bank and the Association manage assets and liabilities to provide a broad range of loan products and funding options, which are designed to allow the Association to be competitive

in all interest rate environments. The primary objective of the asset/liability management process is to provide stable earnings, while maintaining adequate capital levels by managing exposure to credit and interest rate risks.

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to either the Prime Rate or the 90-day London Interbank Offered Rate (LIBOR). Fixed rate loans are priced based on the current cost of Farm Credit System debt of similar terms to maturity. The Association does not offer or include adjustable rate mortgages (ARMS) in its portfolio of loan products.

The majority of the interest rate risk in the Association balance sheet is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control interest rate risk associated with the loan portfolio.

## CAPITAL RESOURCES

Total members' equity at June 30, 2019 increased by \$1,168 or 2.14 percent to \$55,733 from December 31, 2018 total of \$54,565. The increase was primarily attributable to year-to-date net income.

Total capital stock and participation certificates were \$444 at June 30, 2019 compared to \$453 at December 31, 2018. The decrease of \$9 was the result of retirement of capital stock on loans liquidated in the normal course of business.

Unallocated retained earnings were \$55,289 at June 30, 2019 for an increase of \$1,177 or 2.18 percent from December 31, 2018 when unallocated retained earnings totaled \$54,112. The increase was due to 2019 year-to-date net income.

### Key financial condition ratios were as follows:

	<u>6/30/19</u>	<u>12/31/18</u>
Total Members' Equity to Asset	36.53%	34.72%

## Regulatory Capital Ratios

The Association's regulatory capital ratios are shown in the following table:

	<b>Regulatory Minimum, Including Buffer*</b>	<b>6/30/19</b>	<b>12/31/18</b>	<b>6/30/18</b>
Permanent Capital Ratio	7.00%	39.32%	40.13%	37.60%
Common Equity Tier 1 (CET1) Capital Ratio	7.00%	38.88%	39.65%	37.20%
Tier 1 Capital Ratio	8.50%	38.88%	39.65%	37.20%
Total Regulatory Capital Ratio	10.50%	40.13%	40.90%	38.32%
Tier 1 Leverage Ratio	5.00%	35.34%	35.58%	33.53%
Unallocated Retained Earnings (URE) and URE Equivalents Leverage Ratio	1.50%	36.03%	36.28%	34.20%

\*Includes fully phased-in capital conservation buffers which will be effective January 1, 2020.

The FCA sets minimum regulatory capital adequacy requirements for System banks and associations. The requirements are based on regulatory ratios as defined by the FCA and include common equity tier 1 (CET1), tier 1, total capital, permanent capital, tier 1 leverage, and unallocated retained earnings (URE) and URE equivalents leverage ratios.

The permanent capital, CET1, tier 1, and total capital ratios are calculated by dividing the three-month average daily balance of the capital numerator, as defined by the FCA, by a risk-adjusted asset base. Unlike these ratios, the tier 1 leverage and URE and URE equivalents leverage ratios do not incorporate any risk-adjusted weighting of assets. Risk-adjusted assets refer to the total dollar amount of the institution's assets adjusted by an appropriate credit conversion factor as defined by regulation. Generally, higher credit conversion factors are applied to assets with more inherent risk. The tier 1 leverage and URE and URE equivalents leverage ratios are calculated by dividing the three-month average daily balance of the capital numerator, as defined by the FCA, by the three-month average daily balance of total assets adjusted for regulatory deductions.

If the capital ratios fall below the minimum regulatory requirements, including the buffer amounts, capital distributions (equity redemptions, dividends, and patronage) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval. For all periods presented, the Association

exceeded minimum regulatory standards for all capital ratios. There are no trends, commitments, contingencies, or events that are likely to affect the Association's ability to meet regulatory minimum capital standards and capital adequacy requirements

## REGULATORY MATTERS

On April 3, 2019, the Farm Credit Administration issued a proposed rule that would clarify the factors that System institutions should consider when categorizing high-risk loans and placing them in nonaccrual status. The rule would also revise the criteria by which loans are reinstated to accrual status, and would revise the application of the criteria to certain loans in nonaccrual status to distinguish between the types of risk that cause loans to be placed in nonaccrual status. The public comment period ended on June 3, 2019.

## OTHER MATTERS

The Association continues its service agreement with Farm Credit of Florida, ACA for a fee. These services include, but do not fully cover and are not limited to, accounting, reporting, risk management, human resources and, loan on-boarding and servicing. Both parties are in compliance with the terms of the agreement and expect to continue working under the agreement in 2019.

## RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1, *Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements*, in the Notes to the Financial Statements, and the 2018 Annual Report to Shareholders for recently issued accounting pronouncements. Additional information is provided in the following table.

The following Accounting Standards Update (ASU) was issued by the Financial Accounting Standards Board (FASB) but has not yet been adopted:

Summary of Guidance	Adoption and Potential Financial Statement Impact
<i>ASU 2016-13 – Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments</i>	
<ul style="list-style-type: none"> <li>Replaces multiple existing impairment standards by establishing a single framework for financial assets to reflect management's estimate of current expected credit losses (CECL) over the complete remaining life of the financial assets.</li> <li>Changes the present incurred loss impairment guidance for loans to an expected loss model.</li> <li>The Update also modifies the other-than-temporary impairment model for debt securities to require an allowance for credit impairment instead of a direct write-down, which allows for reversal of credit impairments in future periods based on improvements in credit.</li> <li>Eliminates existing guidance for purchased credit impaired (PCI) loans, and requires recognition of an allowance for expected credit losses on these financial assets.</li> <li>Requires a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption.</li> <li>Effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early application will be permitted for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018.</li> </ul>	<ul style="list-style-type: none"> <li>Implementation efforts have begun by establishing a cross-discipline governance structure. The implementation includes identification of key interpretive issues, scoping of financial instruments, and assessing existing credit loss forecasting models and processes against the new guidance.</li> <li>The new guidance is expected to result in an increase in allowance for credit losses due to several factors, including: <ol style="list-style-type: none"> <li>The allowance related to loans and commitments will most likely increase to cover credit losses over the full remaining expected life of the portfolio, and will consider expected future changes in macroeconomic conditions,</li> <li>An allowance will be established for estimated credit losses on any debt securities,</li> <li>The nonaccretable difference on any PCI loans will be recognized as an allowance, offset by an increase in the carrying value of the related loans.</li> </ol> </li> <li>The extent of the increase is under evaluation, but will depend upon the nature and characteristics of the financial instrument portfolios, and the macroeconomic conditions and forecasts at the adoption date.</li> <li>The guidance is expected to be adopted in first quarter 2021.</li> </ul>

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**NOTE:** Shareholder investment in the 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. 2764, or writing Matthew Miller, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at its website, [www.agfirst.com](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-981-3323, or writing Alice Rivera, Puerto Rico Farm Credit, ACA, PO Box 363649, San Juan, PR 00936-3649, or accessing the website, [www.prfarmcredit.com](http://www.prfarmcredit.com). The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

# Puerto Rico Farm Credit, ACA

## Consolidated Balance Sheets

<i>(dollars in thousands)</i>	June 30, 2019 <i>(unaudited)</i>	December 31, 2018 <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 159	\$ 662
Loans	146,200	149,089
Allowance for loan losses	(1,616)	(1,686)
Net loans	144,584	147,403
Accrued interest receivable	634	652
Equity investments in other Farm Credit institutions	1,617	1,623
Premises and equipment, net	1,130	1,007
Other property owned	3,857	3,894
Accounts receivable	411	1,732
Other assets	193	165
Total assets	<b>\$ 152,585</b>	<b>\$ 157,138</b>
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 95,265	\$ 97,533
Accrued interest payable	287	270
Patronage refunds payable	1	3,001
Accounts payable	291	956
Other liabilities	1,008	813
Total liabilities	<b>96,852</b>	<b>102,573</b>
Commitments and contingencies (Note 7)		
<b>Members' Equity</b>		
Capital stock and participation certificates	444	453
Unallocated retained earnings	55,289	54,112
Total members' equity	<b>55,733</b>	<b>54,565</b>
Total liabilities and members' equity	<b>\$ 152,585</b>	<b>\$ 157,138</b>

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



**Puerto Rico Farm Credit, ACA**  
**Consolidated Statements of**  
**Comprehensive Income**

*(unaudited)*

<i>(dollars in thousands)</i>	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2019	2018	2019	2018
<b>Interest Income</b>				
Loans	\$ 2,131	\$ 2,041	\$ 4,363	\$ 3,923
<b>Interest Expense</b>				
Notes payable to AgFirst Farm Credit Bank	853	778	1,711	1,514
Net interest income	1,278	1,263	2,652	2,409
Provision for (reversal of allowance for) loan losses	45	(28)	1	(43)
Net interest income after provision for (reversal of allowance for) loan losses	1,233	1,291	2,651	2,452
<b>Noninterest Income</b>				
Loan fees	19	37	50	52
Patronage refunds from other Farm Credit institutions	199	219	404	451
Gains (losses) on sales of premises and equipment, net	29	—	29	—
Gains (losses) on other transactions	78	7	83	74
Insurance Fund refunds	—	—	23	339
Total noninterest income	325	263	589	916
<b>Noninterest Expense</b>				
Salaries and employee benefits	518	457	976	840
Occupancy and equipment	47	44	105	81
Insurance Fund premiums	16	19	33	39
(Gains) losses on other property owned, net	4	9	7	41
Other operating expenses	474	576	943	1,041
Total noninterest expense	1,059	1,105	2,064	2,042
Income before income taxes	499	449	1,176	1,326
Provision (benefit) for income taxes	(1)	—	(1)	—
Net income	500	449	1,177	1,326
Other comprehensive income	—	—	—	—
Comprehensive income	\$ 500	\$ 449	\$ 1,177	\$ 1,326

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

**Puerto Rico Farm Credit, ACA**  
**Consolidated Statements of Changes in**  
**Members' Equity**

*(unaudited)*

<i>(dollars in thousands)</i>	<b>Capital Stock and Participation Certificates</b>	<b>Unallocated Retained Earnings</b>	<b>Total Members' Equity</b>
Balance at December 31, 2017	\$ 485	\$ 53,803	\$ 54,288
Comprehensive income		1,326	1,326
Capital stock/participation certificates issued/(retired), net	(27)		(27)
Balance at June 30, 2018	\$ 458	\$ 55,129	\$ 55,587
<b>Balance at December 31, 2018</b>	<b>\$ 453</b>	<b>\$ 54,112</b>	<b>\$ 54,565</b>
<b>Comprehensive income</b>		<b>1,177</b>	<b>1,177</b>
<b>Capital stock/participation certificates issued/(retired), net</b>	<b>(9)</b>		<b>(9)</b>
<b>Balance at June 30, 2019</b>	<b>\$ 444</b>	<b>\$ 55,289</b>	<b>\$ 55,733</b>

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

# Notes to the Consolidated Financial Statements

*(dollars in thousands, except as noted)*

*(unaudited)*

## **Note 1 — Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements**

### ***Organization***

The accompanying financial statements include the accounts of Puerto Rico Farm Credit, ACA and its Production Credit Association (PCA) and Federal Land Credit Association (FLCA) subsidiaries (collectively, Association). A description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations for the Association as of and for the year ended December 31, 2018, are contained in the 2018 Annual Report to Shareholders. These unaudited interim consolidated financial statements should be read in conjunction with the latest Annual Report to Shareholders.

### ***Basis of Presentation***

In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary for a fair statement of results for the periods presented. These adjustments are of a normal recurring nature, unless otherwise disclosed.

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

The results of any interim period are not necessarily indicative of those to be expected for a full year.

### ***Significant Accounting Policies***

The Association's accounting and reporting policies conform with U.S. generally accepted accounting principles (GAAP) and practices in the financial services industry. To prepare the financial statements in conformity with GAAP, management must make estimates based on assumptions about future economic and market conditions (for example, unemployment, market liquidity, real estate prices, etc.) that affect the reported amounts of assets and liabilities at the date of the financial statements, income and expenses during the reporting period, and the related disclosures. Although these estimates contemplate current conditions and expectations of change in the future, it is reasonably possible that actual conditions may be different than anticipated, which could materially affect results of operations and financial condition.

Management has made significant estimates in several areas, including loans and allowance for loan losses (Note 2, *Loans and Allowance for Loan Losses*), investment securities and other-than-temporary impairment (Note 3, *Investments*), and

financial instruments (Note 5, *Fair Value Measurement*). Actual results could differ from those estimates.

For further details of significant accounting policies, see Note 2, *Summary of Significant Accounting Policies*, from the latest Annual Report.

### ***Accounting Standards Updates (ASUs) Issued During the Period***

The following ASUs were issued by the Financial Accounting Standards Board (FASB) since the most recent year end:

- In May 2019, the FASB issued ASU 2019-05 Financial Instruments—Credit Losses (Topic 326): Targeted Transition Relief. The amendments in this Update provide entities with an option to irrevocably elect the fair value option applied on an instrument-by-instrument basis for certain financial assets upon the adoption of Topic 326. The fair value option election does not apply to held-to-maturity debt securities. For entities that have not yet adopted the amendments in ASU 2016-13, the effective date and transition methodology for the amendments in this Update are the same as in that Update. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.
- In April 2019, the FASB issued ASU 2019-04 Codification Improvements to Topic 326 Financial Instruments—Credit Losses, Topic 815 Derivatives and Hedging, and Topic 825 Financial Instruments. The amendments in this Update clarify, correct, and improve various aspects of the guidance in the following Updates related to financial instruments: ASU 2016-01 Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Liabilities, ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, and ASU 2017-12 Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. The items addressed generally are not expected to have a significant effect on current accounting practice or to create a significant administrative cost for most entities. For entities that have not yet adopted the amendments in ASU 2016-13, the effective dates and transition requirements for the amendments related to this Update are the same as the effective dates and transition requirements in ASU 2016-13. The transition adjustment includes adjustments made as a result of an entity developing or amending its accounting policy upon adoption of the amendments in this Update for determining when accrued interest receivables are deemed

uncollectible and written off. For entities that have adopted the amendments in ASU 2017-12 as of the issuance date of this Update, the effective date is as of the beginning of the first annual period beginning after the issuance date of this Update. For those entities, early adoption is permitted, including adoption on any date on or after the issuance of this Update. The amendments in this Update related to ASU 2016-01 are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted in any interim period following the issuance of this Update as long as the entity has adopted all of the amendments in ASU 2016-01. The amendments in this Update should be applied on a modified-retrospective transition basis by means of a cumulative-effect adjustment to the opening retained earnings balance in the statement of financial position as of the date an entity adopted all of the amendments in ASU 2016-01. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

- In March 2019, the FASB issued ASU 2019-01 Leases (Topic 842): Codification Improvements. The Update addresses potential implementation issues that could arise as organizations implement Topic 842. The amendments in the Update include the following items brought to the Board's attention through interactions with stakeholders: 1. Determining the fair value of the underlying asset by lessors that are not manufacturers or dealers; 2. Presentation on the statement of cash flows—sales-type and direct financing leases; 3. Transition disclosures related to Topic 250, Accounting Changes and Error Corrections. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

#### ***ASUs Pending Effective Date***

For a detailed description of the ASUs below, see the latest Annual Report.

Potential effects of ASUs issued in previous periods:

- In August 2018, the FASB issued ASU 2018-15 Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract. The amendments align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by the amendments in this Update. The guidance is effective for public business entities for fiscal years beginning after December 15,

2019, and interim periods within those fiscal years. Early adoption is permitted, including adoption in any interim period, for all entities. The amendments should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

- In August 2018, the FASB issued ASU 2018-13 Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement. The amendments are part of the FASB's disclosure framework project. The project's objective and primary focus are to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by GAAP that is most important to users of each entity's financial statements. The amendments remove, modify or add certain disclosures contained in the financial statement footnotes related to fair value. Additionally, the guidance is intended to promote the appropriate exercise of discretion by entities when considering fair value measurement disclosures and to clarify that materiality is an appropriate consideration of entities and their auditors when evaluating disclosure requirements. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Certain amendments should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. Early adoption is permitted upon issuance. Entities are permitted to early adopt any removed or modified disclosures upon issuance of this Update and delay adoption of the additional disclosures until their effective date. The removed disclosures were adopted effective with the 2018 Annual Report. Evaluation of any possible effects the additional and modified disclosures guidance may have on the statements of financial condition and results of operations is in progress.
- In June 2016, the FASB issued ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. This Update, and subsequent clarifying guidance issued, is intended to improve financial reporting by requiring timelier recording of credit losses on financial instruments. It requires an organization to measure all expected credit losses for financial assets held at the reporting date. Financial institutions and other organizations will use forward-looking information to estimate their credit losses. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public companies that are not SEC filers, it will take effect for fiscal years beginning after December 15, 2020, and

interim periods within those fiscal years. Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 31, 2018. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

#### ***Accounting Standards Effective During the Period***

There were no changes in the accounting principles applied from the latest Annual Report, other than any discussed below.

No recently adopted accounting guidance issued by the FASB had a significant effect on the current period reporting. See the most recent Annual Report for a detailed description of each of the standards below:

- In February 2018, the FASB issued ASU 2018-02 Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The guidance allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. The amendments eliminate the stranded tax effects resulting from the Tax Cuts and Jobs Act and are intended to improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The Update also requires certain disclosures about stranded tax effects. The guidance was effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Adoption of this guidance had no impact on the statements of financial condition and results of operations.
- In March 2017, the FASB issued ASU 2017-08 Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities. The guidance relates to certain callable debt securities and shortens the amortization period for any premium to the earliest call date. The Update was effective for interim and annual periods beginning after December 15, 2018 for public business entities. Adoption of this guidance had no impact on the statements of financial condition and results of operations.
- In February 2016, the FASB issued ASU 2016-02 Leases (Topic 842). This Update, and subsequent clarifying guidance issued, requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Leases will be classified as either finance leases or operating leases. This distinction will be relevant for the pattern of expense recognition in the income statement. Lessor

accounting activities are largely unchanged from existing lease accounting. The Update also eliminates leveraged lease accounting but allows existing leveraged leases to continue their current accounting until maturity, termination or modification. The amendments were effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, for public business entities.

#### **Transition Information**

- The guidance was adopted using the optional modified retrospective method and practical expedients for transition. Under this transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption.
- The package of practical expedients was elected, which allowed existing leases to be largely accounted for consistent with current guidance, except for the incremental balance sheet recognition for lessees.
- There will not be a material change to the timing of future expense recognition.
- The adoption of this guidance had no impact on the Association.
- Given the limited changes to lessor accounting, there were no material changes to recognition or measurement.

#### **Note 2 — Loans and Allowance for Loan Losses**

The Association 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 Association has been identified. See Note 3, *Loans and Allowance for Loan Losses*, from the latest Annual Report for further discussion.

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

A summary of loans outstanding at period end follows:

	June 30, 2019	December 31, 2018
Real estate mortgage	\$ 63,554	\$ 63,434
Production and intermediate-term	36,392	37,355
Loans to cooperatives	1,096	903
Processing and marketing	22,714	21,920
Farm-related business	243	254
Communication	9,023	11,369
Power and water/waste disposal	1,451	1,450
Rural residential real estate	10,014	10,692
International	1,713	1,712
<b>Total loans</b>	<b>\$ 146,200</b>	<b>\$ 149,089</b>

A substantial portion of the Association's lending activities is collateralized, and exposure to credit loss associated with lending activities is reduced accordingly.

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with Farm Credit Administration (FCA) regulations. The following tables present the principal balance of participation loans at periods ended:

	June 30, 2019							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 6,821	\$ 1,161	\$ —	\$ —	\$ 303	\$ —	\$ 7,124	\$ 1,161
Production and intermediate term	6,558	2,081	—	—	2,381	—	8,939	2,081
Loans to cooperatives	1,101	—	—	—	—	—	1,101	—
Processing and marketing	13,924	8,817	—	—	—	—	13,924	8,817
Farm-related business	—	—	—	—	233	—	233	—
Communication	9,049	—	—	—	—	—	9,049	—
Power and water/waste disposal	1,454	—	—	—	—	—	1,454	—
International	1,714	—	—	—	—	—	1,714	—
<b>Total</b>	<b>\$ 40,621</b>	<b>\$ 12,059</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 2,917</b>	<b>\$ —</b>	<b>\$ 43,538</b>	<b>\$ 12,059</b>

	December 31, 2018							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	\$ 3,939	\$ 1,257	\$ —	\$ —	\$ 342	\$ —	\$ 4,281	\$ 1,257
Production and intermediate term	6,190	2,255	—	—	2,557	—	8,747	2,255
Loans to cooperatives	908	—	—	—	—	—	908	—
Processing and marketing	13,264	7,096	—	—	316	—	13,580	7,096
Farm-related business	—	—	—	—	243	—	243	—
Communication	11,405	—	—	—	—	—	11,405	—
Power and water/waste disposal	1,454	—	—	—	—	—	1,454	—
International	1,714	—	—	—	—	—	1,714	—
<b>Total</b>	<b>\$ 38,874</b>	<b>\$ 10,608</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 3,458</b>	<b>\$ —</b>	<b>\$ 42,332</b>	<b>\$ 10,608</b>

A significant source of liquidity for the Association is the repayments of loans. The following table presents the contractual maturity distribution of loans by loan type at the latest period end:

	June 30, 2019			
	Due Less Than 1 Year	Due 1 Through 5 Years	Due After 5 Years	Total
Real estate mortgage	\$ 8,351	\$ 32,408	\$ 22,795	\$ 63,554
Production and intermediate-term	4,927	28,461	3,004	36,392
Loans to cooperatives	53	1,043	—	1,096
Processing and marketing	1,802	10,341	10,571	22,714
Farm-related business	—	—	243	243
Communication	—	6,324	2,699	9,023
Power and water/waste disposal	—	—	1,451	1,451
Rural residential real estate	4	676	9,334	10,014
International	—	1,373	340	1,713
<b>Total loans</b>	<b>\$ 15,137</b>	<b>\$ 80,626</b>	<b>\$ 50,437</b>	<b>\$ 146,200</b>
Percentage	10.35%	55.15%	34.50%	100.00%

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

The following table shows the recorded investment of loans, classified under the FCA Uniform Loan Classification System, as a percentage of the recorded investment of total loans by loan type as of:

	June 30, 2019	December 31, 2018		June 30, 2019	December 31, 2018
<b>Real estate mortgage:</b>			<b>Communication:</b>		
Acceptable	97.37%	95.62%	Acceptable	100.00%	81.83%
OAEM	0.28	1.85	OAEM	–	18.17
Substandard/doubtful/loss	2.35	2.53	Substandard/doubtful/loss	–	–
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Production and intermediate-term:</b>			<b>Power and water/waste disposal:</b>		
Acceptable	85.34%	88.12%	Acceptable	100.00%	100.00%
OAEM	4.19	1.16	OAEM	–	–
Substandard/doubtful/loss	10.47	10.72	Substandard/doubtful/loss	–	–
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Loans to cooperatives:</b>			<b>Rural residential real estate:</b>		
Acceptable	100.00%	100.00%	Acceptable	93.07%	92.87%
OAEM	–	–	OAEM	1.06	3.50
Substandard/doubtful/loss	–	–	Substandard/doubtful/loss	5.87	3.63
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Processing and marketing:</b>			<b>International:</b>		
Acceptable	100.00%	100.00%	Acceptable	100.00%	100.00%
OAEM	–	–	OAEM	–	–
Substandard/doubtful/loss	–	–	Substandard/doubtful/loss	–	–
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>
<b>Farm-related business:</b>			<b>Total loans:</b>		
Acceptable	100.00%	100.00%	Acceptable	94.73%	93.27%
OAEM	–	–	OAEM	1.24	2.71
Substandard/doubtful/loss	–	–	Substandard/doubtful/loss	4.03	4.02
	<u>100.00%</u>	<u>100.00%</u>		<u>100.00%</u>	<u>100.00%</u>

The following tables provide an aging analysis of the recorded investment of past due loans as of:

	June 30, 2019				
	30 Through	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans
	89 Days Past Due				
Real estate mortgage	\$ 218	\$ 1,249	\$ 1,467	\$ 62,424	\$ 63,891
Production and intermediate-term	36	19	55	36,501	36,556
Loans to cooperatives	–	–	–	1,097	1,097
Processing and marketing	–	–	–	22,793	22,793
Farm-related business	–	–	–	243	243
Communication	–	–	–	9,027	9,027
Power and water/waste disposal	–	–	–	1,452	1,452
Rural residential real estate	537	46	583	9,477	10,060
International	–	–	–	1,715	1,715
Total	\$ 791	\$ 1,314	\$ 2,105	\$ 144,729	\$ 146,834

	December 31, 2018				
	30 Through	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans
	89 Days Past Due				
Real estate mortgage	\$ 396	\$ 1,305	\$ 1,701	\$ 62,054	\$ 63,755
Production and intermediate-term	465	64	529	37,031	37,560
Loans to cooperatives	–	–	–	904	904
Processing and marketing	–	–	–	21,996	21,996
Farm-related business	–	–	–	254	254
Communication	–	–	–	11,371	11,371
Power and water/waste disposal	–	–	–	1,452	1,452
Rural residential real estate	485	46	531	10,202	10,733
International	–	–	–	1,716	1,716
Total	\$ 1,346	\$ 1,415	\$ 2,761	\$ 146,980	\$ 149,741

Nonperforming assets (including related accrued interest receivable as applicable) and related credit quality statistics at period end were as follows:

	June 30, 2019	December 31, 2018
<b>Nonaccrual loans:</b>		
Real estate mortgage	\$ 1,754	\$ 1,740
Production and intermediate-term	4,801	64
Rural residential real estate	117	125
Total	<u>\$ 6,672</u>	<u>\$ 1,929</u>
<b>Accruing restructured loans:</b>		
Real estate mortgage	\$ 1,343	\$ 2,411
Production and intermediate-term	2,486	6,480
Rural residential real estate	113	115
Total	<u>\$ 3,942</u>	<u>\$ 9,006</u>
<b>Accruing loans 90 days or more past due:</b>		
Total	<u>\$ —</u>	<u>\$ —</u>
Total nonperforming loans	\$ 10,614	\$ 10,935
Other property owned	3,857	3,894
Total nonperforming assets	<u>\$ 14,471</u>	<u>\$ 14,829</u>
Non-accrual loans as a percentage of total loans	4.56%	1.29%
Nonperforming assets as a percentage of total loans and other property owned	9.64%	9.69%
Nonperforming assets as a percentage of capital	<u>25.96%</u>	<u>27.18%</u>

The following table presents information related to the recorded investment of impaired loans at period end. 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.

	June 30, 2019	December 31, 2018
<b>Impaired nonaccrual loans:</b>		
Current as to principal and interest	\$ 5,303	\$ 452
Past due	1,369	1,477
Total	<u>\$ 6,672</u>	<u>\$ 1,929</u>
<b>Impaired accrual loans:</b>		
Restructured	\$ 3,942	\$ 9,006
90 days or more past due	—	—
Total	<u>\$ 3,942</u>	<u>\$ 9,006</u>
Total impaired loans	<u>\$ 10,614</u>	<u>\$ 10,935</u>
Additional commitments to lend	<u>\$ —</u>	<u>\$ 750</u>

The following tables present additional impaired loan information at period end. Unpaid principal balance represents the contractual principal balance of the loan.

	June 30, 2019			Three Months Ended June 30, 2019		Six Months Ended June 30, 2019	
	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
<b>Impaired loans:</b>							
<b>With a related allowance for credit losses:</b>							
Real estate mortgage	\$ 712	\$ 706	\$ 52	\$ 644	\$ 11	\$ 701	\$ 23
Production and intermediate-term	—	—	—	—	—	—	—
Rural residential real estate	—	—	—	—	—	—	—
Total	<u>\$ 712</u>	<u>\$ 706</u>	<u>\$ 52</u>	<u>\$ 644</u>	<u>\$ 11</u>	<u>\$ 701</u>	<u>\$ 23</u>
<b>With no related allowance for credit losses:</b>							
Real estate mortgage	\$ 2,385	\$ 2,783	\$ —	\$ 2,159	\$ 37	\$ 2,346	\$ 75
Production and intermediate-term	7,287	7,696	—	6,593	113	7,168	231
Rural residential real estate	230	273	—	207	3	225	7
Total	<u>\$ 9,902</u>	<u>\$ 10,752</u>	<u>\$ —</u>	<u>\$ 8,959</u>	<u>\$ 153</u>	<u>\$ 9,739</u>	<u>\$ 313</u>
<b>Total impaired loans:</b>							
Real estate mortgage	\$ 3,097	\$ 3,489	\$ 52	\$ 2,803	\$ 48	\$ 3,047	\$ 98
Production and intermediate-term	7,287	7,696	—	6,593	113	7,168	231
Rural residential real estate	230	273	—	207	3	225	7
Total	<u>\$ 10,614</u>	<u>\$ 11,458</u>	<u>\$ 52</u>	<u>\$ 9,603</u>	<u>\$ 164</u>	<u>\$ 10,440</u>	<u>\$ 336</u>



Impaired loans:	December 31, 2018			Year Ended December 31, 2018	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
<b>With a related allowance for credit losses:</b>					
Real estate mortgage	\$ 712	\$ 706	\$ 6	\$ 888	\$ 38
Production and intermediate-term	—	—	—	—	—
Rural residential real estate	—	—	—	—	—
Total	\$ 712	\$ 706	\$ 6	\$ 888	\$ 38
<b>With no related allowance for credit losses:</b>					
Real estate mortgage	\$ 3,439	\$ 3,745	\$ —	\$ 4,287	\$ 182
Production and intermediate-term	6,544	6,876	—	8,157	347
Rural residential real estate	240	281	—	299	13
Total	\$ 10,223	\$ 10,902	\$ —	\$ 12,743	\$ 542
<b>Total impaired loans:</b>					
Real estate mortgage	\$ 4,151	\$ 4,451	\$ 6	\$ 5,175	\$ 220
Production and intermediate-term	6,544	6,876	—	8,157	347
Rural residential real estate	240	281	—	299	13
Total	\$ 10,935	\$ 11,608	\$ 6	\$ 13,631	\$ 580

A summary of changes in the allowance for loan losses and recorded investment in loans for each reporting period follows:

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Communication	Power and Water/Waste Disposal	Rural Residential Real Estate	International	Total
<b>Activity related to the allowance for credit losses:</b>								
Balance at March 31, 2019	\$ 287	\$ 984	\$ 86	\$ 16	\$ 4	\$ 193	\$ 1	\$ 1,571
Charge-offs	—	—	—	—	—	—	—	—
Recoveries	—	—	—	—	—	—	—	—
Provision for loan losses	33	27	1	—	—	(16)	—	45
Balance at June 30, 2019	\$ 320	\$ 1,011	\$ 87	\$ 16	\$ 4	\$ 177	\$ 1	\$ 1,616
Balance at December 31, 2018	\$ 269	\$ 1,095	\$ 76	\$ 44	\$ 4	\$ 197	\$ 1	\$ 1,686
Charge-offs	(76)	—	—	—	—	—	—	(76)
Recoveries	5	—	—	—	—	—	—	5
Provision for loan losses	122	(84)	11	(28)	—	(20)	—	1
Balance at June 30, 2019	\$ 320	\$ 1,011	\$ 87	\$ 16	\$ 4	\$ 177	\$ 1	\$ 1,616
Balance at March 31, 2018	\$ 316	\$ 950	\$ 74	\$ 47	\$ 16	\$ 138	\$ 1	\$ 1,542
Charge-offs	—	—	—	—	—	—	—	—
Recoveries	1	—	—	—	—	—	—	1
Provision for loan losses	(23)	(32)	(5)	(1)	(1)	34	—	(28)
Balance at June 30, 2018	\$ 294	\$ 918	\$ 69	\$ 46	\$ 15	\$ 172	\$ 1	\$ 1,515
Balance at December 31, 2017	\$ 271	\$ 991	\$ 92	\$ 49	\$ 6	\$ 152	\$ 2	\$ 1,563
Charge-offs	(1)	—	—	—	—	(8)	—	(9)
Recoveries	4	—	—	—	—	—	—	4
Provision for loan losses	20	(73)	(23)	(3)	9	28	(1)	(43)
Balance at June 30, 2018	\$ 294	\$ 918	\$ 69	\$ 46	\$ 15	\$ 172	\$ 1	\$ 1,515
<b>Allowance on loans evaluated for impairment:</b>								
Individually	\$ 52	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 52
Collectively	268	1,011	87	16	4	177	1	1,564
Balance at June 30, 2019	\$ 320	\$ 1,011	\$ 87	\$ 16	\$ 4	\$ 177	\$ 1	\$ 1,616
Individually	\$ 6	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 6
Collectively	263	1,095	76	44	4	197	1	1,680
Balance at December 31, 2018	\$ 269	\$ 1,095	\$ 76	\$ 44	\$ 4	\$ 197	\$ 1	\$ 1,686
<b>Recorded investment in loans evaluated for impairment:</b>								
Individually	\$ 2,945	\$ 7,238	\$ —	\$ —	\$ —	\$ 159	\$ —	\$ 10,342
Collectively	60,946	29,318	24,133	9,027	1,452	9,901	1,715	136,492
Balance at June 30, 2019	\$ 63,891	\$ 36,556	\$ 24,133	\$ 9,027	\$ 1,452	\$ 10,060	\$ 1,715	\$ 146,834
Individually	\$ 3,914	\$ 6,480	\$ —	\$ —	\$ —	\$ 161	\$ —	\$ 10,555
Collectively	59,841	31,080	23,154	11,371	1,452	10,572	1,716	139,186
Balance at December 31, 2018	\$ 63,755	\$ 37,560	\$ 23,154	\$ 11,371	\$ 1,452	\$ 10,733	\$ 1,716	\$ 149,741

\*Includes the loan types: Loans to cooperatives, Processing and marketing, and Farm-related business.

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 pre-modification and post-modification outstanding recorded investment and the effects of the modifications that occurred during the periods presented. There were no new TDRs that occurred during three or six months ended June 30, 2019 or the three months ended June 30, 2018.

Outstanding Recorded Investment	Six Months Ended June 30, 2018				Charge-offs
	Interest Concessions	Principal Concessions	Other Concessions	Total	
<b>Pre-modification:</b>					
Real estate mortgage	\$ —	\$ 260	\$ —	\$ 260	
Total	\$ —	\$ 260	\$ —	\$ 260	
<b>Post-modification:</b>					
Real estate mortgage	\$ —	\$ 266	\$ —	\$ 266	\$ —
Total	\$ —	\$ 266	\$ —	\$ 266	\$ —

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

There were no TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the periods presented. Payment default is defined as a payment that was thirty days or more past due.

The following table provides information at period end on outstanding loans restructured in troubled debt restructurings. These loans are included as impaired loans in the impaired loan table:

	Total TDRs		Nonaccrual TDRs	
	June 30, 2019	December 31, 2018	June 30, 2019	December 31, 2018
Real estate mortgage	\$ 1,734	\$ 2,812	\$ 391	\$ 401
Production and intermediate-term	7,238	6,480	4,752	—
Rural residential real estate	159	161	46	46
Total loans	\$ 9,131	\$ 9,453	\$ 5,189	\$ 447
Additional commitments to lend	\$ —	\$ 750		

The following table presents information as of period end:

	June 30, 2019
Carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession	\$ —
Recorded investment of consumer mortgage loans secured by residential real estate for which formal foreclosure proceedings are in process	\$ —

### Note 3 — Investments

#### Equity Investments in Other Farm Credit System Institutions

Equity investments in other Farm Credit System institutions are generally nonmarketable investments consisting of stock and participation certificates, allocated surplus, and reciprocal investments in other institutions regulated by the FCA. These investments are carried at cost and evaluated for impairment based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value.

Associations are required to maintain ownership in AgFirst (AgFirst or the Bank) in the form of Class B or Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association owned 0.55 percent of the issued stock of the Bank as of June 30, 2019 net of any reciprocal investment. As of

that date, the Bank's assets totaled \$33.8 billion and shareholders' equity totaled \$2.5 billion. The Bank's earnings were \$131 million for the first six months of 2019. In addition, the Association held \$134 in investments related to other Farm Credit institutions.

### Note 4 — Debt

#### Notes Payable to AgFirst Farm Credit Bank

The Association's indebtedness to the Bank represents borrowings by the Association to fund its earning assets. This indebtedness is collateralized by a pledge of substantially all of the Association's assets. The contractual terms of the revolving line of credit are contained in the General Financing Agreement (GFA). The GFA also defines Association performance criteria for borrowing from the Bank, which

includes borrowing base margin, earnings and capital covenants, among others.

### Note 5 — Fair Value Measurement

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.

Accounting guidance establishes a 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 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 hierarchy tiers is based upon the lowest level of input that is significant to the fair value measurement.

The classifications within the fair value hierarchy are as follows:

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2 inputs 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 3 inputs are unobservable and supported by little or no market activity. Valuation is determined using pricing models, discounted cash flow methodologies, or similar techniques, and could include significant management judgment or estimation. Level 3 assets and liabilities also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

For a complete discussion of the inputs and other assumptions considered in assigning various assets and liabilities to the fair value hierarchy levels, see the latest Annual Report to Shareholders.

There were no Level 3 assets or liabilities measured at fair value on a recurring basis for the periods presented. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the periods presented.

Fair values are estimated at each period end date for assets and liabilities measured at fair value on a recurring basis. Other Financial Instruments are not measured at fair value in the statement of financial position, but their fair values are estimated as of each period end date. The following tables summarize the carrying amounts of these assets and liabilities at period end, and their related fair values.

	June 30, 2019				
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
<b>Recurring Measurements</b>					
<b>Assets:</b>					
Recurring Assets	\$ —	\$ —	\$ —	\$ —	\$ —
<b>Liabilities:</b>					
Recurring Liabilities	\$ —	\$ —	\$ —	\$ —	\$ —
<b>Nonrecurring Measurements</b>					
<b>Assets:</b>					
Impaired loans	\$ 660	\$ —	\$ —	\$ 660	\$ 660
Other property owned	3,857	—	—	4,261	4,261
Nonrecurring Assets	\$ 4,517	\$ —	\$ —	\$ 4,921	\$ 4,921
<b>Other Financial Instruments</b>					
<b>Assets:</b>					
Cash	\$ 159	\$ 159	\$ —	\$ —	\$ 159
Loans	143,924	—	—	144,559	144,559
Other Financial Assets	\$ 144,083	\$ 159	\$ —	\$ 144,559	\$ 144,718
<b>Liabilities:</b>					
Notes payable to AgFirst Farm Credit Bank	\$ 95,265	\$ —	\$ —	\$ 96,038	\$ 96,038
Other Financial Liabilities	\$ 95,265	\$ —	\$ —	\$ 96,038	\$ 96,038

December 31, 2018

	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
<b>Recurring Measurements</b>					
<b>Assets:</b>					
Recurring Assets	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Liabilities:</b>					
Recurring Liabilities	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Nonrecurring Measurements</b>					
<b>Assets:</b>					
Impaired loans	\$ 706	\$ -	\$ -	\$ 706	\$ 706
Other property owned	3,894	-	-	4,300	4,300
Nonrecurring Assets	\$ 4,600	\$ -	\$ -	\$ 5,006	\$ 5,006
<b>Other Financial Instruments</b>					
<b>Assets:</b>					
Cash	\$ 662	\$ 662	\$ -	\$ -	\$ 662
Loans	146,697	-	-	146,301	146,301
Other Financial Assets	\$ 147,359	\$ 662	\$ -	\$ 146,301	\$ 146,963
<b>Liabilities:</b>					
Notes payable to AgFirst Farm Credit Bank	\$ 97,533	\$ -	\$ -	\$ 98,206	\$ 98,206
Other Financial Liabilities	\$ 97,533	\$ -	\$ -	\$ 98,206	\$ 98,206

**SENSITIVITY TO CHANGES IN SIGNIFICANT UNOBSERVABLE INPUTS**

Discounted cash flow or similar modeling techniques are generally used to determine the recurring fair value measurements for Level 3 assets and liabilities. Use of these techniques requires determination of relevant inputs and assumptions, some of which represent significant unobservable inputs as indicated in the tables that follow. Accordingly, changes in these unobservable inputs may have a significant impact on fair value.

Certain of these unobservable inputs will (in isolation) have a directionally consistent impact on the fair value of the instrument for a given change in that input. Alternatively, the fair value of the instrument may move in an opposite direction for a given change in another input. Where multiple inputs are used within the valuation technique of an asset or liability, a change in one input in a certain direction may be offset by an opposite change in another input having a potentially muted impact to the overall fair value of that particular instrument. Additionally, a change in one unobservable input may result in a change to another unobservable input (that is, changes in

certain inputs are interrelated with one another), which may counteract or magnify the fair value impact.

**Inputs to Valuation Techniques**

Management determines the Association's valuation policies and procedures. The Bank performs the majority of the Association's valuations, and its valuation processes are calibrated annually by an independent consultant. The fair value measurements are analyzed on a quarterly basis. For other valuations, documentation is obtained for third party information, such as pricing, and periodically evaluated alongside internal information and pricing that is available.

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

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

	Fair Value	Valuation Technique(s)	Unobservable Input	Range
Impaired loans and other property owned	\$ 4,921	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 Other Financial Instrument Fair Value Measurements**

	Valuation Technique(s)	Input
Cash	Carrying value	Par/principal and appropriate interest yield
Loans	Discounted cash flow	Prepayment forecasts Probability of default Loss severity
Notes payable to AgFirst Farm Credit Bank	Discounted cash flow	Prepayment forecasts Probability of default Loss severity

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## Note 6 — Employee Benefit Plans

The following is a table of retirement expenses for the Association:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Pension	\$ 72	\$ 97	\$ 145	\$ 209
401(k)	29	24	55	43
Total	\$ 101	\$ 121	\$ 200	\$ 252

The following is a table of retirement contributions for the Association:

	Actual YTD Through 6/30/19	Projected Contributions For Remainder of 2019	Projected Total Contributions 2019
Pension	\$ —	\$ 290	\$ 290

Contributions in the above table include an allocated estimate of funding for the multi-employer pension plan in which the Association participates. The projected amount may change when a total funding amount and allocation is determined by the pension plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change the contribution necessary before the next plan measurement date of December 31, 2019.

Further details regarding employee benefit plans are contained in the 2018 Annual Report to Shareholders.

## Note 7 — Commitments and Contingent Liabilities

From time to time, legal actions are pending against the Association in which claims for money damages are asserted. On at least a quarterly basis, the Association assesses its liabilities and contingencies in connection with outstanding legal proceedings utilizing the latest information available. While the outcome of legal proceedings is inherently uncertain, on the basis of information presently available, management, after consultation with legal counsel, is of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the Association. Because it is not probable that the Association will incur a loss or the loss is not estimable, no liability has been recorded for any claims that may be pending.

## Note 8 — Subsequent Events

The Association evaluated subsequent events and determined there were none requiring disclosure through August 8, 2019, which was the date the financial statements were issued.