AgSouth Farm Credit, ACA

THIRD QUARTER 2019

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CERTIFICATION

The undersigned certify that we have reviewed the September 30, 2019 quarterly report of AgSouth 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.

Pat Calhoun
Chief Executive Officer

Bo Fennell
Chief Financial Officer

James C. Carter, Jr.
Chairman of the Board

November 8, 2019

AgSouth Farm Credit, ACA

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 affected 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 September 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 September 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 September 30, 2019.

Pat Calhoun
Chief Executive Officer

Bo Fennell
Chief Financial Officer

November 8, 2019

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

(dollars in thousands)

The following commentary reviews the financial condition and results of operations of AgSouth Farm Credit, ACA (Association) for the period ended September 30, 2019. This information should be read in conjunction with the accompanying financial statements, notes to the financial statements, and the 2018 Annual Report of AgSouth Farm Credit, ACA. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

FORWARD LOOKING INFORMATION

This quarterly report contains 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 our expectations and predictions due to a number of risks and uncertainties, many of which are beyond our control. These risks and uncertainties include, but are not limited to:

- political, legal, regulatory and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international, and farm-related business sectors;
- weather-related, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry; and
- actions taken by the Federal Reserve System in implementing monetary policy.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association’s loan portfolio is diversified over a wide range of agricultural commodities produced in our region, including timber, poultry (broilers, turkeys and eggs), sod, nursery and horticulture, cotton, feed grains, soybeans and hay, beef cattle, horses, peanuts, blueberries, fruits, and nuts. Loans to producers of these commodities total $1,569,268 or 86 percent of the Association’s portfolio. Farm size varies, and many of the Association’s customers have diversified farming operations. These factors, along with the numerous opportunities for non-farm income in the area, reduce to some degree the level of income dependency on any given commodity.

AGRICULTURE OVERVIEW

AgSouth’s service area experienced very hot and predominantly dry growing conditions during the third quarter of 2019 with little impact from tropical weather disturbances. September brought Hurricane Dorian which veered away from a direct hit to both South Carolina and Georgia with very little impact.

The National Agricultural Statistics Service (NASS) crop progress and condition report for September 30, 2019 reported the following: South Carolina topsoil moisture as being 15 percent adequate with Georgia being 8 percent adequate for the week ending September 29, 2019. The report indicated the crop condition of peanuts in South Carolina as 63 percent good to excellent and 32 percent fair with 24 percent of the crop harvested to date. For Georgia, 57 percent were rated good to excellent and 28 percent fair with 28 percent of the crop harvested to date. Peanut production in Georgia is expected to be up slightly from 2018 production at 2.9 billion pounds. In South Carolina, peanut production is expected to be down 20 percent from 2018 production at 223 million pounds.

Cotton harvest in South Carolina was reported to be 12 percent complete at the end of the third quarter 2019 and rated the condition of the cotton crop to be 63 percent good to excellent with 29 percent fair. In Georgia, 54 percent of the cotton crop is rated good to excellent and 31 percent fair with 18 percent of the crop harvested to date.

The 2019 soybean harvest is just in the early stages, but NASS is rating the crop as 52 percent good to excellent, 36 percent fair and 12 percent poor to very poor in South Carolina. In Georgia, the soybean crop is rated 33 percent good to excellent, 40 percent fair and 27 percent poor to very poor. Soybean production is expected to be down 36 percent from 2018 at 3.47 million bushels in Georgia and up 4 percent from 2018 at

11.6 million bushels in South Carolina. Pasture quality for both Georgia and South Carolina decreased during the third quarter with 82 percent of the acreage rated very poor to fair and 17 percent rated good for the week ending September 29, 2019.

Corn harvest was 95% complete in both Georgia and South Carolina as of September 22, 2019. The South Carolina state yield forecast for grain production is projected at 40.4 million bushels, up 3 percent from 2018. In Georgia, corn for grain production is forecast at 55.6 million bushels, up 11 percent from 2018 in Georgia.

Weather conditions for the 2019 blueberry harvest allowed farmers in Southeast Georgia to produce their best crop since 2016. The 2019 yields are still being calculated, but expectations are that they will exceed the past two years. Some late freezes impacted yields in 2017 and 2018.

Tobacco production for 2019 is forecast to be down 24 percent and 23 percent, respectively for Georgia and South Carolina from 2018.

US winter wheat production totaled 1.96 billion bushels in 2019, up 4 percent from the revised 2018 total of 1.89 billion bushels. South Carolina production for 2019 was 2.16 million bushels which is down 38 percent from 2018. Winter wheat planted acreage, at 70,000 acres, was down 10,000 acres from 2018. For Georgia, wheat production is down 27 percent from 2018, the lowest production since 1972, and wheat planted acreage, at 150,000 acres, is down 50,000 acres from 2018. Wheat markets in South Carolina and Georgia have continued to shrink with the growth of peanuts competing for acres and time during normal wheat harvest season.

According to the most recent NASS Broiler Hatchery News Release in 2019, domestic broiler growers placed 183 million chicks for meat production as of September 28, 2019, which is up 5 percent from the comparable week a year earlier. South Carolina chick placements were 4.57 million, which was down 4 percent from the same week in 2018. Georgia hatcheries placed 28.33 million chicks, which is up 3 percent from the same week in 2018. Cumulative placements for the United States were up 2 percent from the same period a year earlier. Poultry remains our highest portfolio concentration paid from agricultural income.

Stumpage prices for most product types across the South declined in the third quarter of 2019 as compared to the same quarter in 2018. Pine sawtimber, chip-n-saw and pulpwood, as well as, hardwood pulpwood were all down for the quarter. Hardwood sawtimber was up over third quarter 2018. These seasonal price movements follow typical historical trends. Southern pine lumber prices improved slightly in the third quarter of 2019 as did prices for Oriented Strand Board (OSB); however, southern pine plywood prices were down.

According to the US Census, US housing starts for month end August 2019 totaled 852,000 units, down 2 percent from the same period in 2018. Total starts in the South were up 4 percent for the same period in 2018.

The NASS published a Southern Region Land Values and Cash Rents Report on August 7, 2019. The US farm real estate average value per acre was $3,160 in 2019, up $60 per acre from 2018 values. NASS reported US farm land average cash rent for all cropland (irrigated, non-irrigated and pasture) was $138 per acre in 2018 and increased to $140 per acre in 2019. South Carolina farm land average cash rent per acre for all cropland was $48.50 in 2018 and dropped to $47.00 in 2019. South Carolina farm real estate average value per acre was $3,310 in 2018 and increased to $3,400 in 2019. Georgia farm land average cash rent per acre for all cropland was $116 in 2018 and rose to $126 in 2019. Georgia farm real estate average value per acre was $3,510 in 2018 and decreased to $3,470 in 2019.

The Conference Board Leading Economic Index (LEI) was 112.1 in August 2019 which was no change compared to July 2019, following a 0.4 percent increase in July 2019. The Conference Board stated, "The US LEI remained unchanged in August, following a large increase in July. Housing permits and the Leading Credit Index offset the weakness in the index from the manufacturing sector and the interest rate spread. The recent trends in the LEI are consistent with a slow but still expanding economy, which has been primarily driven by strong consumer spending and robust job growth."

The Conference Board US Consumer Confidence Index dropped from 134.2 in August 2019 to 125.1 in September 2019. The Conference Board stated "Consumers were less positive in their assessment of current conditions and their expectations regarding the short-term outlook also weakened. The escalation in trade and tariff tensions in late August appears to have rattled consumers. However, this pattern of uncertainty and volatility has persisted for much of the year and it appears confidence is plateauing. While confidence could continue hovering around current levels for months to come, at some point this continued uncertainty will begin to diminish consumers' confidence in the expansion."

Unemployment in South Carolina is at 3.2 percent as of August 2019. This is a drop from 3.5 percent in June 2019 and 3.4 percent in July 2019. Unemployment in Georgia, while higher than in South Carolina, has been slowly decreasing during 2019 from 3.9 percent in March 2019 to 3.6 percent at August 2019 month end. The US unemployment rate dropped to 3.5 percent in September 2019 after remaining at 3.7 percent for June, July and August 2019. With the strength and growth shown by the US economy, the Federal Reserve reduced interest rates (25 basis points) for the second time this year on September 18, 2019.

The Federal Reserve lowered interest rates by 25 basis points on July 31, 2019 and again on September 18, 2019. The

Federal Reserve lowers interest rates as it tries to guard the United States economy against trade-related uncertainty and slowing global growth. The trade issues with China continue to have a negative impact on all agricultural commodity prices. The USDA has tried to offset some of this with the Market Facilitation Program payments. Many farmers within our service territory will be eligible for Wildfire and Hurricane Indemnity Program (WHIP) payments based on their counties being declared disaster areas due to hurricane damage to crops in 2018.

ASSOCIATION BALANCE SHEET

The gross loan volume of the Association as of September 30, 2019 was $1,824,809, an increase of $31,357 or 1.75 percent compared to $1,793,452 at December 31, 2018. Net loans outstanding at September 30, 2019 were $1,808,477 as compared to $1,778,008 at December 31, 2018. Net loans accounted for 95.11 percent of total assets at September 30, 2019, as compared to 94.33 percent of total assets at December 31, 2018.

The increase in gross loan volume during the reporting period is attributed to the funding of operating lines of credit and term loans during the busiest time of the growing season. Advances on most operating lines are now funded and anticipated additional growth by the sales team is being realized. Competition for good quality loans remains strong from some commercial banks, but the Association has remained competitive in a difficult rate environment.

The Association typically structures loans to meet the needs of the borrower. Many term loans are made for ten years or less allowing the borrower to build equity faster and thus reducing the risk in the loan portfolio.

At December 31, 2018 the Association held Investments in debt securities totaling $5,280. These investments are Rural America Bonds made under the authority for Mission Related Investments granted by the Farm Credit Administration (FCA). At September 30, 2019 Investments in debt securities totaled $5,080, a decrease of $200 from December 31, 2018. The 3.79 percent decrease is from expected payments made year to date in 2019.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality is at an acceptable level and credit administration remains satisfactory. Nonaccrual loans increased from $12,093 at December 31, 2018 to $15,824 at September 30, 2019. The balance of nonaccrual loans is decreased by liquidations, loans returning to accrual status, or transfer of assets to other property owned offset by transfers to nonaccrual status. Association staff is working diligently to work out all nonaccrual debt situations.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at September 30, 2019 was $16,332 compared to $15,444 at December 31, 2018 and was considered by management to be adequate to cover possible losses. The increase in the allowance account is in conjunction with comparative loan volume during the first quarter of 2019 and represents similar risk characteristics to the portfolio as a whole. The reserve set aside for unfunded commitments is $668 which is an increase of $111 compared to the total at December 31, 2018 of $557. The reserve for unfunded commitments is included in Other liabilities. The Asset/Liability Committee (ALCO) of the Association, which is comprised of members of executive management and staff assigned to special assets management, met in September 2019 to review the allowance account. The ALCO determined that the composition between the allowance for loan losses on the outstanding portfolio and the reserve required for unfunded commitments needed to be adjusted and an additional general reserve was required. The ALCO considered the general economic conditions, the potential for deterioration in the existing portfolio, the loan growth in the portfolio, and the amount of outstanding loan commitments in determining the level of allowance.

As of the end of the third quarter of 2019, the Association had originated $140,479 in loans for the secondary market. Originations for the same period 2018 were $117,817. The 19.23 percent increase is due to increased volume as the market continues to remain strong for both refinancing and new home purchases given the declining rate environment. As of September 30, 2019 the Association held $2,836 in qualifying Loans held for sale. At December 31, 2018 loans held for sale totaled $359.

Accrued interest receivable increased $736 or 3.82 percent from $19,251 as of December 31, 2018 to $19,987 as of September 30, 2019. The increase is directly tied to the increase in average loans outstanding for the current period and an increase in average loan participations sold compared to December 31, 2018.

Equity investments in other Farm Credit institutions decreased from $24,151 at December 31, 2018 to $24,011 at September 30, 2019. The slight decrease of $140, or less than one percent, is the result of a slightly lower balance of investment in other Farm Credit institutions, which varies based on participations sold on a patronage basis.

Premises and equipment net increased $417 from $20,894 at December 31, 2018 to $21,311 at September 30, 2019. The primary reason for the increase of 2.00 percent is the result of the purchase of land in Baxley, GA for a new branch office.

Other property owned increased to $4,729 at September 30, 2019 from $4,627 at December 31, 2018. The increase of $102 or 2.20 percent in Other property owned is the result of transfers to Other property owned exceeding sales and write-downs of existing Other property owned during the reporting period. The Association is actively marketing all properties for sale. For

Accounts receivable decreased $15,014 from $25,162 at December 31, 2018 to $10,148 at September 30, 2019. The decrease is the result of the patronage distribution receivable at December 31, 2018 from AgFirst and other Farm Credit institutions, which totaled $12,487 in regular distribution and $11,805 in a special distribution. As of September 30, 2019 this line item included two quarters of patronage accrual from AgFirst and other Farm Credit institutions totaling $9,541.

Other assets increased from $2,104 at December 31, 2018 to $2,208 at September 30, 2019. The majority of other assets is made up of prepaid retirement expense which totaled $1,302 as of September 30, 2019 compared to $1,336 as of December 31, 2018.

On the liability side of the balance sheet, Notes payable to AgFirst Farm Credit Bank increased from $1,461,549 at December 31, 2018 to $1,480,413 at September 30, 2019. The $18,864 or 1.29 percent increase is tied to the increase in loans outstanding.

Accrued interest payable decreased $56, or 1.35 percent, from $4,136 at December 31, 2018 to $4,080 at September 30, 2019. The decrease is tied to the increase in the notes outstanding balance and a decrease in the weighted average interest rate on the notes payable balance outstanding.

Patronage refunds payable decreased $10,022 from $10,361 at December 31, 2018 to $339 at September 30, 2019. The decrease is the result of the cash portion of the 2018 Patronage distribution on the Association's records at December 31, 2018 moving from Patronage refund payable to Other liabilities. This amount totaled $10,133 at December 31, 2018. At September 30, 2019 no patronage distribution for 2019 has been declared.

Accounts payable decreased $138 from $1,700 at December 31, 2018 to $1,562 at September 30, 2019. The 8.12 percent decrease is due to the payable established to pay the insurance premiums on loans to the Farm Credit System Insurance Corporation (FCSIC). At December 31, 2018 the payable related to the FCSIC totaled $1,172, and at September 30, 2019 the payable was $891.

Other liabilities decreased $3,740 from $17,124 at December 31, 2018 to $13,384 at September 30, 2019. The 21.84 percent decrease is due to a payable established for the revolvement of the 2013 Allocated Surplus distribution and the cash portion of the 2018 Patronage distribution. These liabilities have decreased as checks have been presented for payment at the commercial bank.

Capital stock and participation certificates increased from $9,567 at December 31, 2018 to $9,942 at September 30, 2019. The increase of $375 or 3.92 percent is due to new borrowers purchasing stock during the reporting period in excess of liquidations of stock when loans pay out.

Allocated surplus decreased from $126,003 at December 31, 2018 to $105,777 at September 30, 2019. This is a decrease of $20,226 or 16.05 percent. The reduction is from the decision made by the Board of Directors to revolve the 2013 series of Allocated Surplus in February 2019. This revolvement totaled $20,434. The checks and notices for this revolvement were generated and mailed in March 2019.

Unallocated surplus increased $31,521 or 12.38 percent from the December 31, 2018 balance of $254,648. The balance of $286,169 at September 30, 2019 includes the retention of a portion of 2018 fiscal year end earnings and earnings year to date in 2019.

RESULTS OF OPERATIONS

For the three months ended September 30, 2019

Net income for the three months ended September 30, 2019 totaled $11,566 as compared to $11,385 for the same period in 2018. This is an increase of $181 or 1.59 percent. The following commentary explains the variance.

At September 30, 2019 interest income increased $937 from $27,354 at September 30, 2018 to $28,291. This increase of 3.43 percent is primarily due to the increased average loan volume and in the weighted average loan yield between the two reporting periods. Nonaccrual income, which is included in interest income, was $40 for the three months ended September 30, 2019 as compared to $169 for the same period in 2018.

For the three months ended September 30, 2019 interest income on investments totaled $86 compared to $90 for the three months ended September 30, 2018. Investment income declined $4 or 4.44 percent due to the lower outstanding balance of investments between the two reporting periods.

Interest expense for the three months ended September 30, 2019 increased $725 from $11,873 at September 30, 2018 to $12,598 at September 30, 2019. The variance is 6.11 percent and is tied to the weighted average direct note rate between the two reporting periods.

Net interest income before the provision for loan loss increased $212 for the three months ended September 30, 2019 as compared to the same period in 2018 due primarily to the increased earnings on a higher balance of average earning assets.

Net interest income after the provision for loan losses increased $615 during the quarter ending September 30, 2019 compared to September 30, 2018. A net provision for loan losses of $326 was made in the quarter ending September 30, 2019. The provision entry represents an adjustment between the general provision and the unfunded commitments provision which is booked to Other liabilities.

Noninterest income increased $420 over the same period last year. The commentary that follows will detail the aggregate difference.

Loan fees increased $40, or 4.29 percent, due to an increase in SMM underwriting fees and late fees earned during the quarter compared to the same period in 2018.

Fees for financially related services decreased $193 from $489 at September 30, 2018 to $296 at September 30, 2019. The decrease of 39.47 percent is due to the decrease in crop insurance premiums earned during the reporting period.

Patronage refunds from other Farm Credit institutions increased $199 from $3,330 at September 30, 2018 to $3,529 at September 30, 2019. The increase of 5.98 percent is related to an increase in loans sold to AgFirst and other Farm Credit Institutions. See *Note 2* for more information.

Gains on the sale of rural home loans increased $243 from $431 at September 30, 2018 compared to $674 at September 30, 2019. An increase in originations between the two reporting periods resulted in the increased gains.

Gains on the sale of premises and equipment for the period ending September 30, 2019 totaled $130 compared to $10 for the period ending September 30, 2018. The increase of $120 is directly related to the sale of multiple fleet vehicles during the period.

Losses on other transactions totaled $205 at September 30, 2019 compared to $207 at September 30, 2018. The difference is $2 or less than one percent.

Other noninterest income was $50 during the three months ended September 30, 2019 compared to $37 for the three months ending September 30, 2018. This line item captures the volume premium paid by AgFirst for secondary market loans sold to AgFirst.

Noninterest expense for the three months ended September 30, 2019 totaled $9,658 and increased $854 or 9.70 percent when compared to $8,804 for the same period of 2018. Salaries and employee benefits expense are the largest portion of noninterest expense and totaled $7,102 for the three months ended September 30, 2019. Salaries and employee benefits increased $778 between the two reporting periods. The majority of the 12.30 percent increase is related to incentive expense, which is accrued monthly in 2019 compared to semi-annually in 2018.

Occupancy and equipment expense at September 30, 2019 was $506 compared to $530 for the same period in 2018. This is a decrease of $24 or 4.53 percent. The decrease is tied to furniture purchases made in 2018 for the Statesboro Operations Center not being warranted in 2019 and a decrease in maintenance and repairs.

The Insurance Fund premiums at September 30, 2018 were $300 and at September 30, 2019 were $303. The $3 or 1.00 percent increase is due to the higher accruing loan volume in 2019.

In the three months ending September 30, 2019 the Association experienced losses on the sale of Other property owned in the amount of $104. During the same period of 2018, the Association booked losses on the sale of Other property owned of $15. The losses and expenses incurred in 2019 included write-downs on some of the properties at sale or when a new appraisal was received justifying the write-down.

Other operating expenses increased $8 from $1,635 at September 30, 2018 compared to $1,643 at September 30, 2019. The increase of less than one percent is primarily attributed to an increase in training and other expenses between the reporting periods. Other operating expenses also include purchased services, advertising and communications and all other expenses necessary to run the business.

For the nine months ended September 30, 2019

Net income for the nine months ended September 30, 2019, totaled $31,891 as compared to $31,502 for the same period in 2018. This is an increase of $389 or 1.23 percent. The following narrative will explain the variance.

At September 30, 2019 interest income increased $4,962 to $82,975 compared to $78,013 for the same period in 2018. The increase was due to the amount of interest income earned on loans and this represents an increase of 6.36 percent. The increase is tied to the increase in accruing loan volume between the reporting periods and an increase in the overall weighted average interest rate earned. Nonaccrual income, which is included in interest income, was $334 for the nine months ended September 30, 2019 as compared to $670 for the same period in 2018. The decrease of $336 is the result of a decrease in the recognition of interest income when nonaccrual loans pay off or pay down.

For the nine months ending September 30, 2018 interest income on investments totaled $270 compared to $257 for the same period ended September 30, 2019. Investment income declined $13 or 4.81 percent due to the lower outstanding balance of investments between the two reporting periods.

Interest expense increased $3,846 or 11.68 percent from $32,915 at September 30, 2018 to $36,761 for the nine months ended September 30, 2019. The increase is attributable to the higher direct note balance between the reporting periods and a higher weighted average direct note rate.

Net interest income before the provision for loan loss increased $1,116 or 2.47 percent for the nine months ended September 30, 2019 as compared to the same period in 2018 primarily due to the increase in loan volume. Net interest income after the provision for loan losses increased $52 for the period ending September 30, 2019 primarily due to the increase in the provision.

The Provision for loan losses amount in the 2018 reporting period totaled $167 and there were provision entries totaling $1,231 in the 2019 reporting period. In September 2019, the Association's ALCO made the decision that the allowance account required an increase to the general reserve and a decrease to the allowance for unfunded commitments which resides within Other Liabilities. These decisions were made after analyzing the risk in the current portfolio. The ALCO analysis included reviewing historical trends, loan size, loan performance and credit quality reports.

Noninterest income for the nine months ended September 30, 2019 increased $224 compared to the same period of 2018. Loan fees increased $164 or 6.24 percent. In the first nine months of 2019, late fees on loans increased $156 to $289 compared to $133 for 2018. Fees earned on loans sold in the secondary market for the first nine months of 2019 were $1,738 or 4.49 percent higher than the same period in 2018. The volume of loans sold increased as well. Loan fees on portfolio activity increased slightly between the two reporting periods.

Fees for financially related services decreased $195 from $1,010 at September 30, 2018 compared to $815 at September 30, 2019. The 19.31 percent decrease in fees for financially related services is the result of a decrease in fee income earned on the sale of multi-peril crop insurance.

The patronage refunds from other Farm Credit institutions increased $50 from $9,828 at September 30, 2018 to $9,878 at September 30, 2019. The increase of less than one percent is due to an increase in the average balance of loans sold to AgFirst and other Farm Credit institutions which resulted in a higher patronage refund amount accrued.

Gains on the sale of rural home loans increased $507 from $1,347 at September 30, 2018 to $1,854 at September 30, 2019. Gains increased due to the increase in loan volume compared to the prior period.

Gains on the sale of premises and equipment increased $31 from $139 for the period ending September 30, 2018 to $170 at September 30, 2019. The gains were recorded when Association automobiles were replaced in 2019.

Losses on other transactions totaled $1 for the nine months ended September 30, 2019 compared to a loss of $309 for the same period in 2018. The loss recorded in the 2019 reporting period is primarily related to the allowance entry for unfunded commitments.

Insurance Fund refunds totaled $366 at September 30, 2019 compared to $989 during the nine months ended September 30, 2018. The decrease of $623 or 62.99 percent is tied to the lower refund amount given to the AgFirst District by the Farm Credit System Insurance Corporation compared to last year.

Other noninterest income decreased $18 from $144 at September 30, 2018 compared to $126 at September 30, 2019. The variance of 12.50 percent is due to volume premiums paid by AgFirst for secondary market activity. In 2018, the Association earned $143 in volume premiums and for the period ending September 30, 2019 the Association has earned $120 in volume premiums.

Noninterest expense for the nine months ended September 30, 2019, decreased $113 compared to the same period of 2018 from $29,207 to $29,094. Salaries and employee benefits expense increased $158 between the two reporting periods. The less than one percent increase in salaries and employee benefits is tied to the increase in the expense for incentive and a decrease in pension funding in 2019. The Association accrues for the 2019 incentive payment based upon plan results which are included in salary and benefit expense. The Association evaluated 2019 performance measures for incentive purposes and determined that some employees could earn incentive in 2019. Based upon this information, the Association will continue to accrue for incentive. The expense associated with the incentive accrual balance as of September 30, 2019 is $2,358. Association results will be re-evaluated prior to the end of the fourth quarter 2019 to determine the most accurate accrual for the 2019 incentive plan.

Occupancy and equipment expense at September 30, 2019 was $1,698 compared to $1,868 for the same period in 2018. The decrease is tied to furniture purchases made in 2018 for the Statesboro Operations Center not being warranted in 2019.

The Insurance Fund premium increased from $869 at September 30, 2018 to $891 at September 30, 2019. The increase of $22 or 2.53 percent is due to the higher accruing loan volume in 2019.

Losses on the sale or write-down of other property owned totaled $195 for the nine months ending September 30, 2019. When compared to the same period in 2018, losses on other property owned totaled $20. The losses or write-downs were required after new contracts, sale closings, and/or new appraisals were obtained and the book value needed to more accurately reflect the current market value.

Other operating expenses decreased $298 from $5,402 at September 30, 2018 compared to $5,104 at September 30, 2019. The decrease is primarily due to a decrease in phone services, nonproperty insurance, and purchased services.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (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 Bank advances the funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at September 30, 2019 was $1,480,413 as compared to $1,461,549 at December 31, 2018. The $18,864 increase, or 1.29 percent, is directly tied to an increase in loan volume.

CAPITAL RESOURCES

Total members' equity at December 31, 2018 totaled $389,992. At September 30, 2019 total members' equity had increased by $11,670 to $401,662. The increase in total members' equity is due to the increase in Unallocated retained earnings offset by a decrease in Allocated retained earnings between the two reporting periods. At December 31, 2018 Allocated retained earnings totaled $126,003 compared to $105,777 at September 30, 2019. The decrease is due to the revolvement of the 2013 series of allocated surplus in the first quarter of 2019. At December 31, 2018, Unallocated retained earnings totaled $254,648 and increased to $286,169. The increase in Unallocated retained earnings is due to the decision to retain a portion of the 2018 earnings for capital purposes and year to date 2019 earnings.

Total Capital stock and participation certificates were $9,942 on September 30, 2019 compared to $9,567 on December 31, 2018. The increase is attributed to the purchase of new stock and participation certificates for new borrowing entities offset by the retirement of stock and participation certificates on loans liquidated in the normal course of business.

The Association's capital ratios are calculated in accordance with FCA regulations, as follows:

- The CET1 ratio is the sum of statutory minimum purchased borrower stock, other required borrower stock held for a minimum of 7 years, allocated equities held for a minimum of 7 years or not subject to revolvement, unallocated retained earnings, paid-in capital, less certain regulatory required deductions including the amount of investments in other System institutions, divided by average risk-adjusted assets.
- The tier 1 capital ratio is CET1 capital plus non-cumulative perpetual preferred stock, divided by average risk-adjusted assets.
- The total capital ratio is tier 1 capital plus other required borrower stock held for a minimum of 5 years, subordinated debt and limited-life preferred stock greater than 5 years to maturity at issuance subject to certain limitations, allowance for loan losses and reserve for unfunded commitments under certain limitations less certain investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
- The permanent capital ratio is all at-risk borrower stock, any allocated excess stock, unallocated retained earnings, paid-in capital, subordinated debt and preferred stock subject to certain limitations, less certain investments in other System institutions, divided by PCR risk-adjusted assets.
- The tier 1 leverage ratio is tier 1 capital, divided by average assets less regulatory deductions to tier 1 capital.
- The UREE leverage ratio is unallocated retained earnings, paid-in capital, and allocated surplus not subject to revolvement less certain regulatory required deductions including the amount of allocated investments in other System institutions divided by average assets less regulatory deductions to tier 1 capital.
- 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.

The following sets forth the regulatory capital ratios, which were effective January 1, 2017:

Ratio	Minimum Requirement	Capital Conservation Buffer*	Minimum Requirement with Capital Conservation Buffer	Capital Ratios as of September 30, 2019
Risk-adjusted ratios:				
CET1 Capital	4.5%	1.875%	6.375%	14.77%
Tier 1 Capital	6.0%	1.875%	7.875%	14.77%
Total Capital	8.0%	1.875%	9.875%	21.69%
Permanent Capital Ratio	7.0%	0.0%	7.000%	20.93%
Non-risk-adjusted:				
Tier 1 Leverage Ratio	4.0%	1.0%	5.0%	14.03%
UREE Leverage Ratio	1.5%	0.0%	1.5%	13.89%

**The capital conservation buffers have a 3 year phase-in period and will become fully effective January 1, 2020. Risk-adjusted ratio minimums will increase 0.625% each year until fully phased in. There is no phase-in period for the tier 1 leverage ratio.*

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.

On September 18, 2019, the Farm Credit Administration issued a proposed rule to amend its investment regulations to allow System associations to purchase and hold the portion of certain loans that non-System lenders originate and sell in the secondary market, and that the USDA unconditionally guarantees or insures as to timely payment of principal and interest. The rule would authorize associations to buy investments to augment the liquidity of rural credit markets, reduce the capital burden on community banks and other non-System lenders who choose to sell their USDA guaranteed portions of loans, and to enhance the ability of associations to manage risk. The public comment period ends on November 18, 2019.

On September 23, 2019, the Farm Credit Administration issued a proposed rule that would ensure the System's capital requirements, including certain regulatory disclosures, reflect the current expected credit losses methodology, which revises the accounting for credit losses under U.S. generally accepted accounting principles. The proposed rule identifies which credit loss allowances under CECL are eligible for inclusion in a System institution's regulatory capital. Credit loss allowances related to loans, lessor's net investments in leases, and held-to-maturity debt securities would be included in a System institution's Tier 2 capital up to 1.25% of the System institution's total risk weighted assets. Credit loss allowances for available-for-sale debt securities and purchased credit impaired assets would not be eligible for inclusion in a System institution's Tier 2 capital. In addition, the proposed regulation does not include a transition phase-in period for the CECL day 1 cumulative effect adjustment to retained earnings on a System institution's regulatory capital ratios. The public comment period ends on November 22, 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
ASU 2016-13 – Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	
• 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. • Changes the present incurred loss impairment guidance for loans to an expected loss model. • 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. • Eliminates existing guidance for purchased credit impaired (PCI) loans, and requires recognition of an allowance for expected credit losses on these financial assets. • Requires a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption. • 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.	• 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. • The new guidance is expected to result in an increase in allowance for credit losses due to several factors, including: 1. 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, 2. An allowance will be established for estimated credit losses on any debt securities, 3. 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. • 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. • The guidance is expected to be adopted in first quarter 2021.

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 their website, ***www.agfirst.com***. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-633-9091, ext. 2674, writing Bo Fennell, CFO, AgSouth Farm Credit, ACA, P.O. Box 718, Statesboro, GA 30459, or accessing the Association's website ***www.agsouthfc.com***. The Association prepares an electronic version of the Annual Report which is available on the Association's web site within 75 days after the end of the fiscal year and distributes the Annual report to Shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the 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 institution.

Reports of suspected or actual wrongdoings involving the Association, its employees and/or Directors, can be made anonymously and confidentially through the Association's Whistleblower Hotline (SpeakUp) at 1-844-850-6496 or *www.convercent.com/report*.

AgSouth Farm Credit, ACA

Consolidated Balance Sheets

(dollars in thousands)	September 30, 2019 *(unaudited)*	December 31, 2018 *(audited)*
Assets		
Cash	**$ 2,653**	$ 5,026
Investments in debt securities:		
Held to maturity (fair value of $5,420 and $5,419, respectively)	**5,080**	5,280
Loans	**1,824,809**	1,793,452
Allowance for loan losses	**(16,332)**	(15,444)
Net loans	**1,808,477**	1,778,008
Loans held for sale	**2,836**	359
Accrued interest receivable	**19,987**	19,251
Equity investments in other Farm Credit institutions	**24,011**	24,151
Premises and equipment, net	**21,311**	20,894
Other property owned	**4,729**	4,627
Accounts receivable	**10,148**	25,162
Other assets	**2,208**	2,104
Total assets	**$ 1,901,440**	$ 1,884,862
Liabilities		
Notes payable to AgFirst Farm Credit Bank	**$ 1,480,413**	$ 1,461,549
Accrued interest payable	**4,080**	4,136
Patronage refunds payable	**339**	10,361
Accounts payable	**1,562**	1,700
Other liabilities	**13,384**	17,124
Total liabilities	**1,499,778**	1,494,870
Commitments and contingencies (Note 8)		
Members' Equity		
Capital stock and participation certificates	**9,942**	9,567
Retained earnings		
Allocated	**105,777**	126,003
Unallocated	**286,169**	254,648
Accumulated other comprehensive income (loss)	**(226)**	(226)
Total members' equity	**401,662**	389,992
Total liabilities and members' equity	**$ 1,901,440**	$ 1,884,862

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

AgSouth Farm Credit, ACA

Consolidated Statements of Income

(unaudited)

(dollars in thousands)	For the Three Months Ended September 30, 2019	For the Three Months Ended September 30, 2018	For the Nine Months Ended September 30, 2019	For the Nine Months Ended September 30, 2018
Interest Income				
Loans	**$ 28,205**	$ 27,264	**$ 82,718**	$ 77,743
Investments	**86**	90	**257**	270
Total interest income	**28,291**	27,354	**82,975**	78,013
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	**12,598**	11,788	**36,761**	32,706
Other	**—**	85	**—**	209
Total interest expense	**12,598**	11,873	**36,761**	32,915
Net interest income	**15,693**	15,481	**46,214**	45,098
Provision for loan losses	**326**	729	**1,231**	167
Net interest income after provision for loan losses	**15,367**	14,752	**44,983**	44,931
Noninterest Income				
Loan fees	**973**	933	**2,794**	2,630
Fees for financially related services	**296**	489	**815**	1,010
Patronage refunds from other Farm Credit institutions	**3,529**	3,330	**9,878**	9,828
Gains (losses) on sales of rural home loans, net	**674**	431	**1,854**	1,347
Gains (losses) on sales of premises and equipment, net	**130**	10	**170**	139
Gains (losses) on other transactions	**205**	207	**(1)**	(309)
Insurance Fund refunds	**—**	—	**366**	989
Other noninterest income	**50**	37	**126**	144
Total noninterest income	**5,857**	5,437	**16,002**	15,778
Noninterest Expense				
Salaries and employee benefits	**7,102**	6,324	**21,206**	21,048
Occupancy and equipment	**506**	530	**1,698**	1,868
Insurance Fund premiums	**303**	300	**891**	869
(Gains) losses on other property owned, net	**104**	15	**195**	20
Other operating expenses	**1,643**	1,635	**5,104**	5,402
Total noninterest expense	**9,658**	8,804	**29,094**	29,207
Net income	**$ 11,566**	$ 11,385	**$ 31,891**	$ 31,502

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

AgSouth Farm Credit, ACA

Consolidated Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the Three Months Ended September 30, 2019	2018	For the Nine Months Ended September 30, 2019	2018
Net income	**$ 11,566**	$ 11,385	**$ 31,891**	$ 31,502
Other comprehensive income net of tax				
Employee benefit plans adjustments	—	2	—	5
Comprehensive income	**$ 11,566**	$ 11,387	**$ 31,891**	$ 31,507

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

AgSouth Farm Credit, ACA

Consolidated Statements of Changes in Members’ Equity

(unaudited)

(dollars in thousands)	Capital Stock and Participation Certificates	Retained Earnings: Allocated	Retained Earnings: Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2017	$ 9,097	$ 121,876	$ 234,892	$ (374)	$ 365,491
Comprehensive income			31,502	5	31,507
Capital stock/participation certificates issued/(retired), net	369				369
Retained earnings retired		(19,476)			(19,476)
Patronage distribution adjustment		(14)	20		6
Balance at September 30, 2018	$ 9,466	$ 102,386	$ 266,414	$ (369)	$ 377,897
Balance at December 31, 2018	**$ 9,567**	**$ 126,003**	**$ 254,648**	**$ (226)**	**$ 389,992**
Cumulative effect of change in accounting principle			**8**		**8**
Comprehensive income			**31,891**		**31,891**
Capital stock/participation certificates issued/(retired), net	**375**				**375**
Retained earnings retired		**(20,490)**			**(20,490)**
Patronage distribution adjustment		**264**	**(378)**		**(114)**
Balance at September 30, 2019	**$ 9,942**	**$ 105,777**	**$ 286,169**	**$ (226)**	**$ 401,662**

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

AgSouth Farm Credit, ACA

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 AgSouth Farm Credit, ACA and its Production Credit Association (PCA) and Federal Land Credit Association (FLCA) subsidiaries (collectively, the 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 6, *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.

  <u>Transition Information</u>

  - 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.
  - Upon adoption, a cumulative-effect adjustment to equity of approximately $8 was recorded. In addition, a Right of Use Asset in the amount of $218 and Lease Liability in the amount of $210 were recognized.
  - 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:

	September 30, 2019	December 31, 2018
Real estate mortgage	$ 1,357,967	$ 1,336,239
Production and intermediate-term	348,899	348,156
Processing and marketing	22,054	21,505
Farm-related business	24,679	23,992
Rural residential real estate	70,788	63,124
Other (including Mission Related)	422	436
Total loans	$ 1,824,809	$ 1,793,452

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:

	September 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	$ 5,699	$ 138,815	$ 414	$ 9,126	$ –	$ –	$ 6,113	$ 147,941
Production and intermediate-term	287	84,521	611	–	3,831	–	4,729	84,521
Processing and marketing	–	97,208	305	26,233	–	–	305	123,441
Farm-related business	3,387	12,693	–	–	–	–	3,387	12,693
Total	$ 9,373	$ 333,237	$ 1,330	$ 35,359	$ 3,831	$ –	$ 14,534	$ 368,596

	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	$ 3,268	$ 162,669	$ 434	$ 9,551	$ –	$ –	$ 3,702	$ 172,220
Production and intermediate-term	–	53,384	618	–	4,175	–	4,793	53,384
Processing and marketing	–	20,254	293	18,039	–	–	293	38,293
Farm-related business	3,358	11,362	–	–	–	–	3,358	11,362
Total	$ 6,626	$ 247,669	$ 1,345	$ 27,590	$ 4,175	$ –	$ 12,146	$ 275,259

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:

	September 30, 2019			
	Due Less Than 1 Year	Due 1 Through 5 Years	Due After 5 Years	Total
Real estate mortgage	$ 37,846	$ 205,577	$ 1,114,544	$ 1,357,967
Production and intermediate-term	187,269	123,490	38,140	348,899
Processing and marketing	2,601	8,182	11,271	22,054
Farm-related business	5,204	12,034	7,441	24,679
Rural residential real estate	7,127	2,009	61,652	70,788
Other (including Mission Related)	–	–	422	422
Total loans	$ 240,047	$ 351,292	$ 1,233,470	$ 1,824,809
Percentage	13.16%	19.25%	67.59%	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:

	September 30, 2019	December 31, 2018
Real estate mortgage:		
Acceptable	97.41%	97.46%
OAEM	1.80	1.90
Substandard/doubtful/loss	0.79	0.64
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	94.60%	96.76%
OAEM	3.60	2.48
Substandard/doubtful/loss	1.80	0.76
	100.00%	100.00%
Processing and marketing:		
Acceptable	89.46%	94.32%
OAEM	–	–
Substandard/doubtful/loss	10.54	5.68
	100.00%	100.00%
Farm-related business:		
Acceptable	86.83%	94.11%
OAEM	9.15	4.59
Substandard/doubtful/loss	4.02	1.30
	100.00%	100.00%

	September 30, 2019	December 31, 2018
Rural residential real estate:		
Acceptable	98.49%	98.34%
OAEM	0.79	0.98
Substandard/doubtful/loss	0.72	0.68
	100.00%	100.00%
Other (including Mission Related):		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Total loans:		
Acceptable	96.67%	97.27%
OAEM	2.19	2.00
Substandard/doubtful/loss	1.14	0.73
	100.00%	100.00%

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

	September 30, 2019				
	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
Real estate mortgage	$ 4,727	$ 3,301	$ 8,028	$ 1,362,414	$ 1,370,442
Production and intermediate-term	1,667	3,271	4,938	350,724	355,662
Processing and marketing	397	666	1,063	21,240	22,303
Farm-related business	1,139	161	1,300	23,537	24,837
Rural residential real estate	646	53	699	70,401	71,100
Other (including Mission Related)	–	–	–	424	424
Total	8,576	7,452	16,028	1,828,740	1,844,768

	December 31, 2018				
	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
Real estate mortgage	$ 6,254	$ 2,483	$ 8,737	$ 1,339,698	$ 1,348,435
Production and intermediate-term	2,687	1,693	4,380	350,162	354,542
Processing and marketing	281	666	947	20,809	21,756
Farm-related business	152	194	346	23,808	24,154
Rural residential real estate	400	80	480	62,869	63,349
Other (including Mission Related)	–	–	–	437	437
Total	$ 9,774	$ 5,116	$ 14,890	$ 1,797,783	$ 1,812,673

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

	September 30, 2019	December 31, 2018
Nonaccrual loans:		
Real estate mortgage	$ 8,933	$ 6,798
Production and intermediate-term	5,591	4,008
Processing and marketing	666	667
Farm-related business	415	313
Rural residential real estate	219	307
Total	$ 15,824	$ 12,093
Accruing restructured loans:		
Real estate mortgage	$ 4,514	$ 6,579
Production and intermediate-term	401	273
Rural residential real estate	173	136
Total	$ 5,088	$ 6,988
Accruing loans 90 days or more past due:		
Total	$ –	$ –
Total nonperforming loans	$ 20,912	$ 19,081
Other property owned	4,729	4,627
Total nonperforming assets	$ 25,641	$ 23,708
Nonaccrual loans as a percentage of total loans	0.87%	0.67%
Nonperforming assets as a percentage of total loans and other property owned	1.40%	1.32%
Nonperforming assets as a percentage of capital	6.38%	6.08%

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.

	September 30, 2019	December 31, 2018
Impaired nonaccrual loans:		
Current as to principal and interest	$ 7,196	$ 4,810
Past due	8,628	7,283
Total	$ 15,824	$ 12,093
Impaired accrual loans:		
Restructured	$ 5,088	$ 6,988
90 days or more past due	–	–
Total	$ 5,088	$ 6,988
Total impaired loans	$ 20,912	$ 19,081
Additional commitments to lend	$ –	$ –

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

	September 30, 2019			Three Months Ended September 30, 2019		Nine Months Ended September 30, 2019	
Impaired loans:	**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**
With a related allowance for credit losses:							
Real estate mortgage	$ 640	$ 634	$ 58	$ 581	$ 4	$ 589	$ 20
Production and intermediate-term	1,414	1,719	453	1,283	9	1,300	43
Processing and marketing	–	–	–	–	–	–	–
Farm-related business	71	71	19	65	1	65	2
Rural residential real estate	–	–	–	–	–	–	–
Total	$ 2,125	$ 2,424	$ 530	$ 1,929	$ 14	$ 1,954	$ 65
With no related allowance for credit losses:							
Real estate mortgage	$ 12,807	$ 15,069	$ –	$ 11,626	$ 83	$ 11,775	$ 393
Production and intermediate-term	4,578	6,186	–	4,157	30	4,209	142
Processing and marketing	666	652	–	605	4	613	21
Farm-related business	344	452	–	311	2	316	11
Rural residential real estate	392	454	–	356	2	361	12
Total	$ 18,787	$ 22,813	$ –	$ 17,055	$ 121	$ 17,274	$ 579
Total impaired loans:							
Real estate mortgage	$ 13,447	$ 15,703	$ 58	$ 12,207	$ 87	$ 12,364	$ 413
Production and intermediate-term	5,992	7,905	453	5,440	39	5,509	185
Processing and marketing	666	652	–	605	4	613	21
Farm-related business	415	523	19	376	3	381	13
Rural residential real estate	392	454	–	356	2	361	12
Total	$ 20,912	$ 25,237	$ 530	$ 18,984	$ 135	$ 19,228	$ 644

Impaired loans:	December 31, 2018 Recorded Investment	Unpaid Principal Balance	Related Allowance	Year Ended December 31, 2018 Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 255	$ 255	$ 54	$ 264	$ 17
Production and intermediate-term	332	488	32	343	21
Processing and marketing	–	–	–	–	–
Farm-related business	–	–	–	–	–
Rural residential real estate	–	–	–	–	–
Total	$ 587	$ 743	$ 86	$ 607	$ 38
With no related allowance for credit losses:					
Real estate mortgage	$ 13,122	$ 15,145	$ –	$ 13,571	$ 857
Production and intermediate-term	3,949	5,469	–	4,085	259
Processing and marketing	667	652	–	689	43
Farm-related business	313	397	–	324	20
Rural residential real estate	443	505	–	459	29
Total	$ 18,494	$ 22,168	$ –	$ 19,128	$ 1,208
Total impaired loans:					
Real estate mortgage	$ 13,377	$ 15,400	$ 54	$ 13,835	$ 874
Production and intermediate-term	4,281	5,957	32	4,428	280
Processing and marketing	667	652	–	689	43
Farm-related business	313	397	–	324	20
Rural residential real estate	443	505	–	459	29
Total	$ 19,081	$ 22,911	$ 86	$ 19,735	$ 1,246

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*	Rural Residential Real Estate	Other (including Mission Related)	Total
Activity related to the allowance for credit losses:						
Balance at June 30, 2019	$ 11,954	$ 2,999	$ 393	$ 599	$ 4	$ 15,949
Charge-offs	(64)	(124)	–	–	–	(188)
Recoveries	57	188	–	–	–	245
Provision for loan losses	(133)	420	25	14	–	326
Balance at September 30, 2019	$ 11,814	$ 3,483	$ 418	$ 613	$ 4	$ 16,332
Balance at December 31, 2018	$ 11,485	$ 3,032	$ 385	$ 538	$ 4	$ 15,444
Charge-offs	(201)	(731)	–	–	–	(932)
Recoveries	170	211	2	206	–	589
Provision for loan losses	360	971	31	(131)	–	1,231
Balance at September 30, 2019	$ 11,814	$ 3,483	$ 418	$ 613	$ 4	$ 16,332
Balance at June 30, 2018	$ 10,655	$ 2,867	$ 276	$ 479	$ 4	$ 14,281
Charge-offs	(43)	(121)	–	(1)	–	(165)
Recoveries	29	37	1	25	–	92
Provision for loan losses	440	197	95	(3)	–	729
Balance at September 30, 2018	$ 11,081	$ 2,980	$ 372	$ 500	$ 4	$ 14,937
Balance at December 31, 2017	$ 11,214	$ 2,797	$ 280	$ 520	$ 4	$ 14,815
Charge-offs	(112)	(296)	–	(90)	–	(498)
Recoveries	246	169	3	35	–	453
Provision for loan losses	(267)	310	89	35	–	167
Balance at September 30, 2018	$ 11,081	$ 2,980	$ 372	$ 500	$ 4	$ 14,937
Allowance on loans evaluated for impairment:						
Individually	$ 58	$ 453	$ 19	$ –	$ –	$ 530
Collectively	11,756	3,030	399	613	4	15,802
Balance at September 30, 2019	$ 11,814	$ 3,483	$ 418	$ 613	$ 4	$ 16,332
Individually	$ 54	$ 32	$ –	$ –	$ –	$ 86
Collectively	11,431	3,000	385	538	4	15,358
Balance at December 31, 2018	$ 11,485	$ 3,032	$ 385	$ 538	$ 4	$ 15,444
Recorded investment in loans evaluated for impairment:						
Individually	$ 13,576	$ 5,991	$ 1,081	$ 392	$ –	$ 21,040
Collectively	1,356,866	349,671	46,059	70,708	424	1,823,728
Balance at September 30, 2019	$ 1,370,442	$ 355,662	$ 47,140	$ 71,100	$ 424	$ 1,844,768
Individually	$ 13,598	$ 4,285	$ 980	$ 445	$ –	$ 19,308
Collectively	1,334,837	350,257	44,930	62,904	437	1,793,365
Balance at December 31, 2018	$ 1,348,435	$ 354,542	$ 45,910	$ 63,349	$ 437	$ 1,812,673

**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.

	Three Months Ended September 30, 2019				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ 320	$ 789	$ –	$ 1,109	
Production and intermediate-term	–	91	–	91	
Total	$ 320	$ 880	$ –	$ 1,200	
Post-modification:					
Real estate mortgage	$ 314	$ 820	$ –	$ 1,134	$ –
Production and intermediate-term	–	94	–	94	–
Total	$ 314	$ 914	$ –	$ 1,228	$ –

	Nine Months Ended September 30, 2019				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ 333	$ 1,710	$ –	$ 2,043	
Production and intermediate-term	171	239	–	410	
Total	$ 504	$ 1,949	$ –	$ 2,453	
Post-modification:					
Real estate mortgage	$ 327	$ 1,743	$ –	$ 2,070	$ –
Production and intermediate-term	164	276	–	440	(39)
Total	$ 491	$ 2,019	$ –	$ 2,510	$ (39)

	Three Months Ended September 30, 2018				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ –	$ 456	$ –	$ 456	
Total	$ –	$ 456	$ –	$ 456	
Post-modification:					
Real estate mortgage	$ –	$ 416	$ –	$ 416	$ –
Total	$ –	$ 416	$ –	$ 416	$ –

	Nine Months Ended September 30, 2018				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ 203	$ 490	$ –	$ 693	
Production and intermediate-term	275	22	–	297	
Total	$ 478	$ 512	$ –	$ 990	
Post-modification:					
Real estate mortgage	$ 208	$ 449	$ –	$ 657	$ –
Production and intermediate-term	287	28	–	315	–
Total	$ 495	$ 477	$ –	$ 972	$ –

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.

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 September 30,		Nine Months Ended September 30,	
	2019	**2018**	**2019**	**2018**
Real estate mortgage	$ –	$ 114	$ –	$ 229
Production and intermediate-term	20	185	20	740
Total	$ 20	$ 299	$ 20	$ 969

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

	Total TDRs		Nonaccrual TDRs	
	September 30, 2019	December 31, 2018	September 30, 2019	December 31, 2018
Real estate mortgage	$ 8,553	$ 10,633	$ 4,039	$ 4,054
Production and intermediate-term	1,472	1,545	1,071	1,272
Farm-related business	3	3	3	3
Rural residential real estate	173	171	–	35
Total loans	$ 10,201	$ 12,352	$ 5,113	$ 5,364
Additional commitments to lend	$ –	$ –		

The following table presents information as of period end:

	September 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

Investments in Debt Securities

The Association's investments consist primarily of Rural America Bonds (RABs), which are private placement securities purchased under the Mission Related Investment (MRI) program approved by the FCA. In its Conditions of Approval for the program, the FCA generally considers a RAB ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9 and requires System institutions to provide notification to FCA when a security becomes ineligible. Any other bonds purchased under the MRI program, approved on a case-by-case basis by FCA, may have different eligibility requirements. At September 30, 2019 the Association held no RABs whose credit quality had deteriorated beyond the program limits.

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

	September 30, 2019				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 5,080	$ 340	$ –	$ 5,420	6.53%

	December 31, 2018				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 5,280	$ 139	$ –	$ 5,419	6.41%

A summary of the contractual maturity, amortized cost and estimated fair value of investment securities held-to-maturity follows:

	September 30, 2019		
	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	$ –	$ –	–%
After one year through five years	–	–	–
After five years through ten years	906	960	5.50
After ten years	4,174	4,460	6.75
Total	$ 5,080	$ 5,420	6.53%

Some of these investments have contractual maturities in excess of ten years. However, expected maturities for these types of securities can 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. A continuous unrealized loss position for an investment is measured from the date the impairment was first identified. The Association had no investments that were in a continuous unrealized loss position for the periods presented.

The recording of an impairment is predicated on: (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 Association 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 Association 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 Association 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.

The Association 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 to estimate the amount of 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 Association may obtain assumptions for the default rate, prepayment rate, and loss severity rate from an independent third party, or generate the assumptions internally.

The Association has not recognized any credit losses as any impairments were deemed temporary and resulted from non-credit related factors. The Association has the ability and intent to hold these temporarily impaired 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, especially after considering credit enhancements.

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 7.27 percent of the issued stock of the Bank as of September 30, 2019 net of any reciprocal investment. As of that date, the Bank's assets totaled $34.6 billion and shareholders' equity totaled $2.5 billion. The Bank's earnings were $192 million for the first nine months of 2019. In addition, the Association held investments of $4,281 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 — Members' Equity

Accumulated Other Comprehensive Income (AOCI)

Changes in Accumulated Other Comprehensive Income by Component *(a)*

	Three Months Ended September 30, 2019	Three Months Ended September 30, 2018	Nine Months Ended September 30, 2019	Nine Months Ended September 30, 2018
Employee Benefit Plans:				
Balance at beginning of period	$ (226)	$ (371)	$ (226)	$ (374)
Other comprehensive income before reclassifications	–	–	–	–
Amounts reclassified from AOCI	–	2	–	5
Net current period other comprehensive income	–	2	–	5
Balance at end of period	$ (226)	$ (369)	$ (226)	$ (369)

	Reclassifications Out of Accumulated Other Comprehensive Income *(b)*				
	Three Months Ended September 30,		Nine Months Ended September 30,		
	2019	**2018**	**2019**	**2018**	**Income Statement Line Item**
Defined Benefit Pension Plans:					
Periodic pension costs	$ –	$ (2)	$ –	$ (5)	See Note 7.
Net amounts reclassified	$ –	$ (2)	$ –	$ (5)	

(a) Amounts in parentheses indicate debits to AOCI.
(b) Amounts in parentheses indicate debits to profit/loss.

Note 6 — 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.

	September 30, 2019				
	Total Carrying Amount	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Recurring Measurements					
Assets:					
Assets held in trust funds	$ 1,931	$ 1,931	$ –	$ –	$ 1,931
Recurring Assets	$ 1,931	$ 1,931	$ –	$ –	$ 1,931
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 1,595	$ –	$ –	$ 1,595	$ 1,595
Other property owned	4,729	–	–	5,258	5,258
Nonrecurring Assets	$ 6,324	$ –	$ –	$ 6,853	$ 6,853
Other Financial Instruments					
Assets:					
Cash	$ 2,653	$ 2,653	$ –	$ –	$ 2,653
Investment securities, held-to-maturity	5,080	–	–	5,420	5,420
Loans	1,809,718	–	–	1,824,468	1,824,468
Other Financial Assets	$ 1,817,451	$ 2,653	$ –	$ 1,829,888	$ 1,832,541
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 1,480,413	$ –	$ –	$ 1,482,407	$ 1,482,407
Other Financial Liabilities	$ 1,480,413	$ –	$ –	$ 1,482,407	$ 1,482,407

	December 31, 2018									
	Total Carrying Amount		Level 1		Level 2		Level 3		Total Fair Value	
Recurring Measurements										
Assets:										
Assets held in trust funds	$	2,006	$	2,006	$	–	$	–	$	2,006
Recurring Assets	$	2,006	$	2,006	$	–	$	–	$	2,006
Liabilities:										
Recurring Liabilities	$	–	$	–	$	–	$	–	$	–
Nonrecurring Measurements										
Assets:										
Impaired loans	$	501	$	–	$	–	$	501	$	501
Other property owned		4,627		–		–		5,103		5,103
Nonrecurring Assets	$	5,128	$	–	$	–	$	5,604	$	5,604
Other Financial Instruments										
Assets:										
Cash	$	5,026	$	5,026	$	–	$	–	$	5,026
Investment securities, held-to-maturity		5,280		–		–		5,419		5,419
Loans		1,777,866		–		–		1,763,220		1,763,220
Other Financial Assets	$	1,788,172	$	5,026	$	–	$	1,768,639	$	1,773,665
Liabilities:										
Notes payable to AgFirst Farm Credit Bank	$	1,461,549	$	–	$	–	$	1,439,810	$	1,439,810
Other Financial Liabilities	$	1,461,549	$	–	$	–	$	1,439,810	$	1,439,810

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.

Investment Securities

The fair values of predominantly all Level 3 investment securities have consistent inputs, valuation techniques and correlation to changes in underlying inputs. The models used to determine fair value for these instruments use certain significant unobservable inputs within a discounted cash flow or market comparable pricing valuation technique. Such inputs generally include discount rate components including risk premiums, prepayment estimates, default estimates and loss severities.

These Level 3 assets would decrease (increase) in value based upon an increase (decrease) in discount rates, defaults, or loss severities. Conversely, the fair value of these assets would generally increase (decrease) in value if the prepayment input were to increase (decrease).

Generally, a change in the assumption used for defaults is accompanied by a directionally similar change in the risk premium component of the discount rate (specifically, the portion related to credit risk) and a directionally opposite change in the assumption used for prepayments. Unobservable inputs for loss severities do not normally increase or decrease based on movements in the other significant unobservable inputs for these Level 3 assets.

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	$ 6,853	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
Investment securities, held-to-maturity	Discounted cash flow	Prepayment rates Risk-adjusted discount rate
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

Note 7 — Employee Benefit Plans

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2019	2018	2019	2018
Pension	$ 939	$ 1,313	$ 2,661	$ 3,939
401(k)	295	238	894	755
Other postretirement benefits	222	186	683	652
Total	$ 1,456	$ 1,737	$ 4,238	$ 5,346

The following is a table of retirement and other postretirement benefit contributions for the Association:

	Actual YTD Through 9/30/19	Projected Contributions For Remainder of 2019	Projected Total Contributions 2019
Pension	$ 121	$ 3,493	$ 3,614
Other postretirement benefits	683	227	910
Total	$ 804	$ 3,720	$ 4,524

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the Association participates. These amounts may change when a total funding amount and allocation is determined by the respective Plan's Sponsor Committee. 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, 2019.

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

Note 8 — Commitments and Contingent Liabilities

From time to time, legal actions are pending against the Association in which claims for monetary 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.

Note 9 — Subsequent Events

The Association evaluated subsequent events and determined that, except as described below, there were none requiring disclosure through November 8, 2019, which was the date the financial statements were issued.

On October 21, 2019, AgFirst's Board of Directors indicated an intention to declare, in December 2019, a special patronage distribution. The Association will receive between approximately $6,156 and $6,977 which will be recorded as patronage refunds from other Farm Credit institutions.