

ANNUAL 2 0 0 8 REPORT

FINANCING RURAL AMERICA



FARM CREDIT OF SOUTHWEST FLORIDA, ACA

2008 ANNUAL REPORT

Contents

Message from the President 2-3

Report of Management 4

Report on Internal Control Over Financial Reporting 5

Consolidated Five-Year Summary of Selected Financial Data 6

Management’s Discussion & Analysis of Financial Condition & Results of Operations 7-19

Disclosure Required by Farm Credit Administration Regulations 20-23

Report of the Audit Committee 24

Report of Independent Auditors 25

Consolidated Financial Statements 26-29

Notes to the Consolidated Financial Statements 30-41

Management

Jimmy V. Knight President & Chief Executive Officer

Bryan L. Byrd Executive Vice President and Chief Operating Officer

Ronnie D. Crawford Chief Lending Officer

William F. Federer Chief Relationship Officer

Daniel B. Irby Chief Financial Officer

Board of Directors

Walter S. Farr Chairman

John R. Alexander Vice Chairman

Howard P. “Rowdy” Bateman Director

John Roy Gough Director

Jerry M. Newlin Director

Lisa Sherman Director

John F. Smoak, Jr. Director

E. E. “Bucky” Waldron Director

J. Mark Wheeler Director

Message from the President

The past year has been one of the most challenging years in our Association's history. The U.S. housing bubble began to burst in late 2007, and our area was one of the hardest-hit in the nation. At one point in 2008, Ft. Myers led all major U.S. metropolitan areas in the number of foreclosures. As home sales and home values continued their steep decline in 2008, land prices began to fall. Today, land values are 40 percent or more below the previous year's level.

The ailing real estate market created a wrenching tear in southwest Florida's economy. Unemployment in our territory has risen dramatically. As the economy spiraled downward in the third and fourth quarters and the financial markets collapsed, many of the businesses we finance—especially those associated with the real estate market—developed cash-flow problems. When they were not able to meet their obligations, we saw our credit quality decline.

In late 2008, our staff devoted hours and hours to reviewing each and every loan in our portfolio to determine its viability. As problems were identified, we took the proactive and fiscally responsible step of increasing the Association's reserves to account for potential losses. By year end, we had made provisions for loan losses totaling \$4.2 million. Naturally, this reduced our current-year earnings by a like amount. Without those provisions, our 2008 net income would have been nearer normal levels, around \$6.3 million.

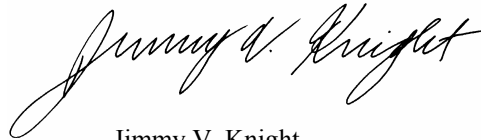
We know we haven't seen the bottom of the economic downturn yet, but we think we have identified the potential problems in our portfolio. We are working with distressed borrowers to keep their loans and their businesses in good standing.

Farm Credit of Southwest Florida came into this economic downturn with a solid capital position. Even though we had to set aside funds for potential losses in 2008, we are still financially strong. To help keep us strong, we will pay a smaller-than-normal portion of our 2008 patronage distribution in cash, and we will not revolve the 2003 series of allocated surplus in April, as we had planned. In addition, we have extended our surplus revolvment cycles from five years to seven years for the time being.

The Board and I want to assure you that we are still providing credit to the agricultural community that we serve. Unlike many lenders, we have not "turned off the spigot." Our goal—moreover, our mission—is to be a reliable and stable source of credit in good times and bad, and we are meeting our mission every day. We are financing creditworthy farmers, ranchers, agribusinesses and rural homeowners, and we will continue to do so, as we have the last 92 years.

Even as we struggled with credit problems in 2008, we took steps to improve the efficiency of the Association's operations. To reduce costs, we turned to our primary service provider, AgFirst Farm Credit Bank, and asked them to provide additional services for us, including accounting, reporting and information management. While Association management retains the responsibility and accountability for all of these areas, we are able to take advantage of the economies of scale that AgFirst offers. The new arrangement has saved us time and money and, in some cases, resulted in higher quality services than we could normally afford. More importantly, it has allowed us to devote more resources to serving our borrowers, our #1 priority.

As we look forward to 2009, we know there will be new challenges to conquer. It will take time for the economy to return to normalcy. In the meantime, be assured that your Association is here to serve you and to help you through these difficult times. As in 1916, the year the Farm Credit System was authorized by Congress, our mission in 2009 is to improve “the income and well-being of American farmers and ranchers by furnishing sound, adequate, and constructive credit to them”...in good times and in bad.



Jimmy V. Knight
President and Chief Executive Officer

February 27, 2009

Report of Management

The accompanying Consolidated Financial Statements and related financial information appearing throughout this annual report have been prepared by management of Farm Credit of Southwest Florida, ACA (Association) in accordance with generally accepted accounting principles appropriate in the circumstances. Amounts which must be based on estimates represent the best estimates and judgments of management. Management is responsible for the integrity, objectivity, consistency, and fair presentation of the Consolidated Financial Statements and financial information contained in this report.


Management maintains and depends upon an internal accounting control system designed to provide reasonable assurance that transactions are properly authorized and recorded, that the financial records are reliable as the basis for the preparation of all financial statements, and that the assets of the Association are safeguarded. The design and implementation of all systems of internal control are based on judgments required to evaluate the costs of controls in relation to the expected benefits and to determine the appropriate balance between these costs and benefits. The Association maintains an internal audit program to monitor compliance with the systems of internal accounting control. Audits of the accounting records, accounting systems and internal controls are performed and internal audit reports, including appropriate recommendations for improvement, are submitted to the Board of Directors.

The Consolidated Financial Statements have been examined by independent public auditors, whose report appears elsewhere in this annual report. The Association is also subject to examination by the Farm Credit Administration.

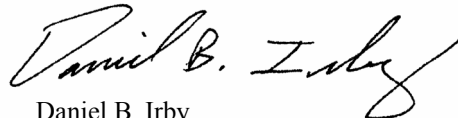
The Consolidated Financial Statements, in the opinion of management, fairly present the financial condition of the Association. The undersigned certify that we have reviewed the 2008 annual report of Farm Credit of Southwest Florida, ACA, that the report has been prepared under the oversight of the Audit 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.



Walter S. Farr
Chairman of the Board



Jimmy V. Knight
Chief Executive Officer



Daniel B. Irby
Chief Financial Officer

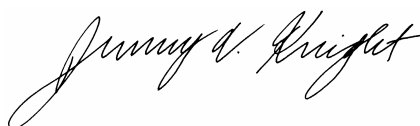
February 27, 2009

Report on Internal Control Over Financial Reporting

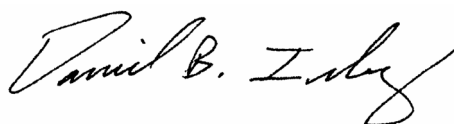
The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's Consolidated Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by, or under the supervision of the Association's principal executives and principal financial officers, or persons performing similar functions, and effected by its Board of Directors, management and other personnel, to provide 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 and 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 December 31, 2008. In making the assessment, management used the framework in *Internal Control — Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association concluded that as of December 31, 2008, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of December 31, 2008.



Jimmy V. Knight
Chief Executive Officer



Daniel B. Irby
Chief Financial Officer

February 27, 2009

Consolidated Five - Year Summary of Selected Financial Data

<i>(dollars in thousands)</i>	2008	2007	December 31, 2006	2005	2004
Balance Sheet Data					
Cash	\$ —	\$ 64	\$ —	\$ 466	\$ 1,051
Investment securities	38,517	36,958	32,202	—	—
Loans	198,532	258,245	219,599	276,618	257,156
Less: allowance for loan losses	4,293	232	187	183	337
Net loans	194,239	258,013	219,412	276,435	256,819
Investments in other Farm Credit institutions	17,174	11,166	12,209	4,638	4,419
Other property owned, net	178	—	—	—	—
Other assets	13,159	13,704	12,050	9,160	8,953
Total assets	\$ 263,267	\$ 319,905	\$ 275,873	\$ 290,699	\$ 271,242
Notes payable to AgFirst Farm Credit Bank*	\$ 211,647	\$ 260,052	\$ 217,032	\$ 233,259	\$ 215,910
Accrued interest payable and other liabilities with maturities of less than one year	4,282	8,284	7,082	5,674	5,192
Total liabilities	215,929	268,336	224,114	238,933	221,102
Protected borrower stock	329	356	508	622	936
Capital stock and participation certificates	553	581	601	656	666
Retained earnings					
Allocated	22,637	26,030	25,779	25,257	25,445
Unallocated	23,984	24,827	24,871	25,231	23,093
Accumulated other comprehensive income (loss)	(165)	(225)	—	—	—
Total members' equity	47,338	51,569	51,759	51,766	50,140
Total liabilities and members' equity	\$ 263,267	\$ 319,905	\$ 275,873	\$ 290,699	\$ 271,242
Statement of Income Data					
Net interest income	\$ 4,395	\$ 6,316	\$ 7,616	\$ 6,402	\$ 6,204
Provision for (reversal of allowance for) loan losses	4,183	26	(10)	(123)	(6,611)
Noninterest income (expense), net	1,904	2,952	595	622	(198)
Net income	\$ 2,116	\$ 9,242	\$ 8,221	\$ 7,147	\$ 12,617
Key Financial Ratios					
Rate of return on average:					
Total assets	0.85%	3.25%	2.79%	2.67%	4.87%
Total members' equity	4.34%	18.13%	16.11%	14.28%	31.13%
Net interest income as a percentage of					
average earning assets	2.03%	2.43%	2.71%	2.49%	2.42%
Net (chargeoffs) recoveries to average loans	(0.07)%	0.01%	0.01%	(0.01)%	(0.02)%
Total members' equity to total assets	17.98%	16.12%	18.76%	17.81%	18.49%
Debt to members' equity (:1)	4.56	5.20	4.33	4.62	4.41
Allowance for loan losses to loans	2.16%	0.09%	0.09%	0.07%	0.13%
Permanent capital ratio	12.05%	15.19%	17.08%	18.07%	17.53%
Total surplus ratio	11.83%	15.13%	16.85%	17.81%	18.39%
Core surplus ratio	10.59%	10.67%	14.27%	12.63%	14.47%
Net Income Distribution					
Estimated patronage refunds:					
Cash	\$ 700	\$ 2,996	\$ 2,512	\$ 1,721	\$ 1,894
Qualified allocated retained earnings	—	261	—	—	—
Nonqualified allocated retained earnings	1,300	6,049	4,665	3,196	3,518

* General financing agreement is renewable on three-year cycles. The next renewal date is December 31, 2009.

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

(dollars in thousands, except as noted)

GENERAL OVERVIEW

The following commentary summarizes the financial condition and results of operations of Farm Credit of Southwest Florida, ACA, (Association) for the year ended December 31, 2008 with comparisons to the years ended December 31, 2007 and December 31, 2006. This information should be read in conjunction with the Consolidated Financial Statements, Notes to the Consolidated Financial Statements and other sections in this Annual Report. The 2008 Annual Report to shareholders was prepared under the oversight of the Audit Committee of the Board of Directors. For a list of the Audit Committee members, refer to the "Report of the Audit Committee" reflected in this Annual Report. Information in any part of this Annual Report may be incorporated by reference in answer or partial answer to any other item of the Annual Report.

The Association is an institution of the Farm Credit System (System), which was created by Congress in 1916 and has served agricultural producers for over 90 years. The System's mission is to maintain and improve the income and well being of American farmers, ranchers, and producers or harvesters of aquatic products and farm-related businesses. The System is the largest agricultural lending organization in the United States. The System is regulated by the Farm Credit Administration, (FCA), which is an independent safety and soundness regulator.

The Association is a cooperative, which is owned by the members (also referred to throughout this Annual Report as stockholders or shareholders) served. The territory of the Association extends across a diverse agricultural region of 10 counties in Southwest Florida and has offices in Arcadia, Wauchula, and Lake Suzy, Florida. Refer to Note 1, "Organization and Operations," of the Notes to the Consolidated Financial Statements for counties in the Association's territory. The Association provides credit to farmers, ranchers, rural residents, and agribusinesses. The Association's success begins with our extensive agricultural experience and knowledge of the market.

The Association obtains funding from AgFirst Farm Credit Bank (AgFirst or Bank). The Association is materially affected and shareholder investment in the Association could be affected by the financial condition and results of operations of the Bank. Copies of the Bank's Annual and Quarterly Reports are on the AgFirst website, www.agfirst.com, or may be obtained at no charge by calling 1-800-845-1745, extension 378, or writing Stephen Gilbert, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202.

Copies of the Association's Annual and Quarterly reports are also available upon request free of charge on the Association's website, www.farmcreditswfl.com, or by calling 1-800-307-5677, extension 141, or writing Jeremy Christian, Controller, 330 N. Brevard Ave. Arcadia Florida 34266. The Association

prepares an electronic version of the Annual Report, which is available on the website, within 75 days after the end of the fiscal year and distributes the Annual Reports 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 needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

FORWARD LOOKING INFORMATION

This annual information statement 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.

AGRICULTURAL OUTLOOK

The February 2009 United States Department of Agriculture (USDA) forecast estimates that 2009 farmers' net cash income, which is a measure of the cash income after payment of business expenses, will decrease to \$77.3 billion, down \$16.1 billion from 2008 and up \$5.5 billion from its 10-year average. Contributing to this decrease in farmers' net cash income are decreases in cash receipts for crops and livestock of \$18.7 billion and \$10.9 billion, respectively, and a decrease in direct government payments of \$1.0 billion, offset in part by a decrease in cash expenses of \$14.1 billion and an increase in farm-related income of \$400 million.

In general, 2008 has been an excellent year for U.S. crop producers, particularly for feed crops, oilseeds and food grains. The high level of farmers' net cash income is primarily the result of high commodity prices during the first half of the year. These higher prices were principally due to strong demand from foreign buyers and the domestic biofuels industry. Corn producers were the primary beneficiaries of the increased demand that has been putting pressure on prices. Other crop prices, in general, increased due to increased acreage to plant corn, decreasing the acreage available for other crops, and to consumers seeking lower cost alternatives to corn. Inadequate rainfall in competitor countries and increased international consumption, from growth in population and rising incomes, reduced world supplies of corn and soybeans, which has translated into rising demand for farm commodities. In addition, the U.S. dollar has depreciated against major foreign currencies in recent years resulting in greater demand for U.S. agricultural exports. However, during the latter half of 2008, many of these factors shifted. A dramatic downturn in the global economy decreased international consumption. Oil prices dropped dampening the demand for ethanol. Crop production outlook improved in certain regions of the world. Further, the dollar strengthened in the latter half of 2008. The combination of these events resulted in a dramatic drop in commodity prices in late 2008 to levels more in line with commodity prices at December 31, 2007. The following table sets forth the commodity prices per bushel for certain crops and by hundredweight for beef cattle from December 31, 2005 to December 31, 2008:

Commodity	12/31/08	12/31/07	12/31/06	12/31/05
Corn	\$4.10	\$3.76	\$3.01	\$1.92
Soybeans	\$9.24	\$10.00	\$6.18	\$5.77
Wheat	\$5.97	\$7.74	\$4.52	\$3.54
Beef Cattle	\$79.80	\$88.90	\$83.10	\$93.30

Elevated crop prices, particularly in early 2008, and the resulting volatility from a dramatic drop in crop prices in the latter half of 2008 had both positive and negative impacts on the Association, as a lender to the agricultural and rural sectors. Elevated commodity prices and increased prices and demand for farm inputs generally result in an increase in average agribusiness loans outstanding. While higher commodity prices have positively impacted grain farmers through the first nine months of 2008, a continuation of recent declines in grain prices could have an unfavorable impact in the near future. The volatility of these prices has resulted in higher risk profiles for Association borrowers, particularly borrowers who purchased at elevated crop prices for future production purposes.

The USDA's February 2009 income outlook shows a great deal of variation depending on farm size, geographic location, and commodity specialties. While the Association utilized the USDA analysis to provide a general understanding of the U.S. agricultural economic outlook, this outlook does not take into account all aspects of the Association's business.

The USDA classifies all farms into three primary categories: commercial farms, intermediate farms and rural residential farms. Commercial farms represent about 11 percent of U.S. farms by number and represent 75 percent of total U.S. farm production. Intermediate farms, defined as ones in which the primary occupation is farming and gross sales are below \$250,000, represent 26 percent of U.S. farms by number and

account for 16 percent of total production. The remaining 63 percent of U.S. farms are classified as rural residential farms where the primary occupation is not farming and the farms produce less than \$250,000 in products and only account for 9 percent of total production.

In addition to farmers' net cash income, off-farm income is an important source of income for the repayment of farm debt obligations and is less subject to cycles in agriculture. The USDA measures farm household income, which is defined as earnings from farming activities plus off-farm income. Nearly 100 percent of farm household income for operators of rural residential farms and more than 80 percent of farm household income for intermediate farms is generated from off-farm sources. Further, USDA data suggests that approximately 25 percent of farm household income for commercial farms is generated from off-farm income. The USDA forecasts 2009 farm household income to decrease 15 percent for commercial farms and 19 percent for intermediate farms.

According to the USDA February 2009 forecast, farm business balance sheets continued to strengthen in the last few years, as measured by debt relative to assets and equity levels. Farm debt to farm assets is forecasted to decline from 10.0 percent for 2008 to 9.1 percent for 2009. Farmers' equity (farm business assets less farm business debt) is expected to continue to rise by 0.9 percent in 2009, after increasing 6.9 percent in 2008.

One measure of the financial health of the agricultural sector used by the USDA is the assessment of farmers' utilization of their capacity to repay debt (actual debt as a percentage of maximum debt that can be supported by farmers' current income). Higher capacity utilization rates indicate tighter cash flow positions and, consequently, higher exposure to financial risk. These estimates do not take into account, however, off-farm income sources. Since 1970, debt repayment capacity utilization has ranged from a low of 35.8 percent in 1973 to 104.1 percent in 1981, and has remained relatively stable since 1987, averaging about 50.0 percent. The USDA suggests an increase in the use of repayment capacity from 43.0 percent in 2008 to 50.0 percent in 2009.

As estimated by the USDA, the Farm Credit System's market share of farm business debt, defined as debt incurred by those involved in on-farm agricultural production, had grown to 36.7 percent at December 31, 2007, as compared with 28.3 percent at December 31, 2000. Farm business debt is forecasted to grow only 0.9 percent in 2009. The USDA's forecast of slow moderation in debt growth is due to decreases in agricultural production costs and to high levels of earnings during the past two years that may enable certain producers to self finance crop production.

In general, agriculture has experienced a sustained period of favorable economic conditions, due to stronger commodity prices, higher land values, and, to a lesser extent, government support programs. To date, the Association's financial results have been positively impacted as a result of these conditions. Production agriculture, however, remains a cyclical business that is heavily influenced by commodity prices. In an environment of less favorable economic conditions in agriculture and without sufficient government support programs, the Association's financial performance and credit

quality measures would likely be negatively impacted. Conditions in the general and agricultural economy have become more volatile with the recent instability in the global financial markets and recent declines in commodity prices. Any negative impact from these less favorable conditions should be lessened by geographic and commodity diversification and the influence of off-farm income sources supporting agricultural-related debt. However, agricultural borrowers who are more reliant on off-farm income sources may be more adversely impacted by a weakened general economy.

CRITICAL ACCOUNTING POLICIES

The financial statements are reported in conformity with accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because management must make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2, "Summary of Significant Accounting Policies," of the Notes to the Consolidated Financial Statements. The following is a summary of certain critical policies.

- *Allowance for loan losses* — The allowance for loan losses is management's best estimate of the amount of probable losses existing in and inherent in our loan portfolio. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through allowance reversals and loan charge-offs. The allowance for loan losses is determined based on a periodic evaluation of the loan portfolio, which generally considers relevant historical charge-off experience adjusted for relevant factors. These factors include types of loans, credit quality, specific industry conditions, general economic and political conditions, and changes in the character, composition, and performance of the portfolio, among other factors.

Significant individual loans are evaluated based on the borrower's overall financial condition, resources, and payment record, the prospects for support from any financially responsible guarantor, and, if appropriate, the estimated net realizable value of any collateral. The allowance for loan losses attributable to these loans is established by a process that estimates the probable loss inherent in the loans, taking into account various historical and projected factors, internal risk ratings, regulatory oversight, and geographic, industry and other factors.

Changes in the factors considered by management in the evaluation of losses in the loan portfolios could result in a change in the allowance for loan losses and could have a direct impact on the provision for loan losses and the results of operations.

- *Valuation methodologies* — Management applies various valuation methodologies to assets and liabilities that often involve a significant degree of judgment, particularly when liquid markets do not exist for the particular items being valued. Quoted market prices are referred to when estimating

fair values for certain assets for which an observable liquid market exists, such as most investment securities. Management utilizes significant estimates and assumptions to value items for which an observable liquid market does not exist. Examples of these items include impaired loans, pension and other postretirement benefit obligations, and certain other financial instruments. These valuations require the use of various assumptions, including, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing and liquidation values. The use of different assumptions could produce significantly different results, which could have material positive or negative effects on the Association's results of operations.

- *Pensions* — The Bank and its related Associations participate in defined benefit retirement plans. These plans are noncontributory and benefits are based on salary and years of service. In addition, the Bank and its related Associations also participate in defined contribution retirement savings plans. Pension expense for all plans is recorded as part of salaries and employee benefits. Pension expense for the defined benefit retirement plans is determined by actuarial valuations based on certain assumptions, including expected long-term rate of return on plan assets and discount rate. The expected return on plan assets for the year is calculated based on the composition of assets at the beginning of the year and the expected long-term rate of return on that portfolio of assets. The discount rate is used to determine the present value of our future benefit obligations. The discount rate for 2008 was selected by reference to analysis and yield curves of the plans' actuary and industry norms.

REGIONAL ECONOMIC CONDITIONS

The Florida economy is among the weakest in the U.S., stymied by the national downturn and excessive exposure to an abysmal housing market. The Florida economy is anchored by procyclical industries such as construction, professional/business services, and tourism and, as such, it is being more profoundly affected by a broad-based contraction in the national economy. In conjunction with record food and energy prices, the downturn in Florida's cyclical industries has pushed the state's consumer confidence to a new all-time low.

Housing

The housing correction has accelerated in recent months, with price declines above 50% of their peak amount in some areas. Prices are falling most in suburban areas, which experienced the greatest overbuilding and are subject to longer commutes that are falling out of favor due to the rise in gasoline prices. House prices are falling because an excess supply and will continue to drop until excess inventory is absorbed. Intense price declines have put an increasing number of homeowners in negative equity positions and income disruptions are prompting them to default on their mortgages.

Credit Crunch

The problems with credit are weighing on Florida through three primary channels: (1) reduced credit availability is causing job loss in impaired financial sub-industries that had strong ties to the housing boom. (2) creditors are tightening the reins on

homebuilders, and many of the cash-strapped developers are being foreclosed upon and forced into bankruptcy. (3) creditors are extending much less credit and at terms that are more expensive. The new credit environment, underpinned by a sharp decrease in creditors' appetite for risk, will force more firms into bankruptcy, restrain construction, and cause continued layoffs in finance.

Summary

The credit weakness and fractured housing market will continue to weigh on the Florida economy, which will hemorrhage jobs throughout the next year. In the long term, the state's strong demographic and economic fundamentals will allow Florida to expand well in excess of the national growth rate.

Citrus

The 2007-08 Florida citrus crop showed some recovery from the hurricane affected seasons of 2004-05, 2005-06, and 2006-07. With an estimated crop of 170 million boxes of oranges produced, this crop was larger than the three previous seasons. As a point of comparison, however, the 2003-04 seasons produced the near-record orange crop of 242 million boxes. Although bearing tree numbers continue to decline, yields in 2007-08 were up, with boxes per tree at the highest level since the 2003-04 crop.

Grapefruit production remained nearly constant at 26.6 million boxes. This level of production, however, is still substantially below pre-hurricane production levels. The presence of citrus canker has had more profound consequences for grapefruit producers making it unlikely that the grapefruit industry will ever fully recover from the hurricanes of 2004 and 2005 and the results of the canker eradication program.

Long-Run Outlook

Typically, when major weather events strike Florida, the stage is set for a period of higher prices. These higher prices stimulate a replanting process and as new trees mature, prices begin to recede. In this cycle, however, three factors may disrupt this process. First is the impact of citrus canker and greening on citrus nursery trees. Citrus canker resulted in nearly two thirds of the nursery stock being destroyed and many nurseries were forced to close. New tree nurseries are now in production, although the supply of new trees is somewhat limited resulting in high prices for nursery trees. These high prices will likely stimulate new investment in tree nurseries, and create more supply of new trees for replanting.

The rapid increase in energy costs has dramatically increased the cost of production. Muraro, in his annual caretaking survey, indicates that increased input costs, especially fertilizer, have pushed the annual cost of tree maintenance to over \$1200 per acre, an increase of 50 percent compared to five years ago.

Another factor is citrus greening. This is a highly destructive disease whose impact is still limited, but continues to spread in the state. It is not known if citrus greening can be controlled and therefore, many growers are uncertain regarding future production prospects. This uncertainty has a negative effect on the willingness of growers to make investments in new plantings.

Given these observations, if citrus demand remains stable, it is likely that the industry is in a period of higher prices across all citrus products but soft demand from continued economic woes could depress prices as consumers seek less expensive juice products.

Limited planting of new trees means that fruit production is likely trending downward over the next several seasons. In addition, as greening begins to affect production in both Brazil and Florida, it represents another negative factor on future fruit production. With production in Florida and Brazil flat to down, processed orange prices will rise over time. The long-run outlook for grapefruit is better than it has been for several seasons. There are signs that the demand for grapefruit juice is beginning to expand. Florida remains the main supplier of fresh grapefruit to the world market. The primary negative factor facing grapefruit is disease, both citrus greening and citrus canker. The end of the rural land boom in Florida means that selling citrus groves for development has abated. Labor costs will continue to be an issue of some concern.

Cattle

Florida has mostly cow-calf operators, which is a ranch where cows are raised and bred mainly to produce calves destined for the beef market. The cows produce a calf crop each year, and the operation keeps some heifer calves from each crop for breeding herd replacements. The rest are sold between the ages of 6 to 12 months along with non-productive cows and bulls. Such calves are often sold to western producers who raise them as feeder cattle.

Beef Supply Situation

U.S. cattle farmers are not increasing the inventory of cattle and calves. The expected increases in the inventory of cattle and calves have been negated by lower calf market prices, substantially higher production costs (feed, fertilizer, fuel, labor, land rents, etc.), poor pasture, and range conditions affecting many cow-calf states as well as large levels of competing meats. In addition, the uncertainties associated with beef export trade, food safety, country of origin labeling, domestic and foreign consumer demand, alternative uses of land (pasture acreage moving into grain production and/or conservation programs and other non-farm uses such as recreation and rural non-farm development), and numerous other issues have likely also caused many cattle farmers to reduce their cattle inventory. Thus, the current cattle cycle will likely continue to liquidate cattle numbers until profitability can be achieved.

In the mid-year July 1, 2008 Cattle Report, cattle farmers told USDA they had fewer beef cows that had calved (-0.60 percent) than a year ago and beef cow replacements were down -2.1 percent from a year ago. A decrease in beef cow replacements and beef cows that have calved during 2008 suggests that herd expansion has halted for the reasons mentioned above.

A smaller inventory of cattle and calves and smaller calf crop during 2008 will likely limit the growth in beef production during 2009. USDA projects U.S. beef production during 2009 to be about 26.55 billion pounds. The level of beef production will be influenced by the level of feeder and live cattle imports (from Canada and Mexico).

Beef Demand and Trade

Beef demand during the first two quarters of 2008 weakened compared with a year ago (retail all fresh domestic beef demand index). Beef demand has felt some challenges the last two years due to less interest in protein diets and tightening consumer grocery budgets due to the higher cost of living. Beef demand is expected to further weaken during 2009 as consumers continue to experience rising prices for most goods and services. If consumer disposable income does not rise proportionally, shopping habits and choices will shift as prices rise forcing consumers to substitute and/or reduce the bundle of goods and services they consume. The weakening U.S. economy during 2009 is expected to result in a decrease in domestic beef demand. Additionally, world beef demand may also decrease due to weak economies.

Sugar

The U.S. sweetener market is the largest and most diverse in the world. The United States is the largest consumer of sweeteners, including high fructose corn syrup, and is one of the largest global sugar importers. The United States ranks among the top sugar producers, and is one of the few countries with significant production of both sugarbeets and sugarcane. Since the mid-1990s, sugarcane has accounted for about 45 percent of the total sugar produced domestically, and sugar beets for about 55 percent of production. U.S. sugar production expanded significantly from the early 1980s to the 2000s. The production increases are due to a substantial investment in new processing equipment, the adoption of new technologies, the use of improved crop varieties, and acreage expansion because of higher prices for sugar relative to alternative crops.

The USDA's production estimates and projections are based primarily on information provided by beet sugar processors and cane sugar millers. FY 2009 sugar production is forecast at 7.454 million short tons, raw value (STRV) which is a decrease of about 10% from 2008. Beet sugar is forecast at 4.0 million STRV for 2009 which is 84% of FY 2008 level. Farmers of sugar beets have reduced plantings recently and converted to grains due to higher returns for corn, wheat, and soybeans. Cane sugar is forecast at 3.454 million STRV or roughly the same as FY 2008.

Prices are forecast to be higher than prior year with the contraction of supply. The third-quarter 2008 raw sugar futures price has averaged 23.47 cents/lb, which is well above the last year's 21.98 cents/lb. Prices should remain relatively stable for 2009 as current year's inventories are low compared to historical average and USDA has recently endorsed continuation of the sugar tariff quota, which will benefit domestic producers.

Floriculture/Nursery

Floriculture (the Green Industry) includes annual and perennial flowering plants, cut flowers, and cut cultivated greens and foliage plants. Nursery crops include woody ornamental trees and shrubs, sod and unfinished plant products. Greenhouse and nursery crops constitute a third of the total farm cash receipts from horticulture crops, which include vegetables, fruits, and tree nuts.

The Green Industry has become a major sector within U.S. agriculture, is of key importance to farmers, rural communities, and consumers, and has been a bright sector of U.S. agriculture recently, but continued larger imports of produce, processed

fruits & vegetables, cut flowers and nursery stock raise competitive pressure on domestic producers. With increased growth projections, production and marketing of landscape crops have provided an alternative for some farmers who have produced traditional agricultural crops, e.g., corn, soybeans, and vegetables. Producers of all sizes are focusing on marketing and carefully looking at innovative branding campaigns to boost their sales. Smaller growers are looking for niches and value added products. Many of them are retailing directly to consumers. Much opportunity still exists but producers must either provide innovative and distinct products or seek to be a low cost producer.

The Green Industry in the United States represents \$148 billion in economic impacts and almost 2 million jobs nationally. Nursery and floral production represented one of the fast growing sectors in agriculture in the last decade; however, slowing growth in demand and tighter margins point to a maturing market. Also, with demand tied in large part to the housing market, a slow down is in order.

In 2007 and 2008, higher petroleum prices led to greater price inflation in the food and agriculture sector as costs rose for fertilizer, storage, processing, and transport. This trend for higher production costs coupled with weak real estate market will flag demand in 2009 despite the abundant availability of quality nursery and floral. As a result, product prices and net income for U.S. producers will decline or remain flat.

Florida is a leading producer in the nursery & landscaping industry ranked second only to California in the United States. In the end, the level of growth expected in Southwest Florida over the next decade will help to foster growth for area producers; however, short-term conditions will prove difficult and some firms are likely to fail.

Dairy

Market conditions are changing rapidly as three major forces are converging: (1) the milk supply in the U.S. is tightening to one percent growth due to reduced producer margins. Feed costs are still high by historical levels, and alfalfa hay remains a major cost. Add to this lower milk prices and dairy farmers are realizing declining revenues and increased expenses thus reducing profitability and resulting in fewer milking cows. (2) demand for U.S. exports is declining. Exports of nonfat dry milk and butter may decline further in 2009. Therefore, even though the milk supply is declining, demand is falling even faster. (3) macro economic conditions are resulting in a stronger dollar, weaker commodity prices, higher inflation, higher unemployment, and reduced income levels. All of these factors are contributing to a reduction in domestic use. Combined, these trends should result in weaker dairy market prices in 2009.

For 2009 the futures prices for corn and soybean meal are declining but expected to remain above long-term averages and the price of premium quality hay remains high. As market prices soften, milk producer's profit margins will be squeezed. The consumption of cheese, particularly American cheese, seems less impacted by the state of the economy than other commodities. Consumers may trade down in terms of their eating behavior, but will still consume cheese.

Vegetable / Melon

Vegetables are grown in Florida on approximately 300,000 acres, for a total annual value of \$1.2 billion. While the major vegetable commodities are tomato, bell pepper, strawberry, potato, green bean, and watermelon, over 40 vegetable crops are produced in the state. The main challenges the industry is currently facing are global competition, labor, and water issues. Field production in Mexico and Central American countries and greenhouse production in Canada and European countries now also target the winter market historically open for Florida produce. In this context, vegetable growers constantly strive to improve their cultural practices in order to remain competitive and maintain profitability. As a response to these needs, several statewide research/extension programs focus on vegetable variety development and evaluation, update of fertilization, irrigation, weed, and pest control recommendations, and assessment of the environmental impact of vegetable production on ground water quality. Among these programs, work on water and nutrient management includes irrigation scheduling methods, field-testing of possible best management practices, and the development of controlled-release fertilizer programs for vegetable production.

Prices for fresh vegetables averaged 6% above the prior year through the first 9 months of 2008. Given the reduced acreage planted and average weather this fall, supplies are expected to be lower and retail prices slightly higher. Demand for fresh vegetables should remain stable and continue to grow. Diet concerns and new technologies that improve the quality and variety of vegetables available to consumers will continue to increase demand. Globalization of markets through trade agreements will increase the level of competition. The 2009 season is likely to see a highly volatile market with some producers doing well and others suffering from low returns depending on weather & production in various regions of the county.

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 through numerous product types.

Business Segments	2008		December 31, 2007		2006	
	<i>(dollars in thousands)</i>					
Commercial Lending	\$ 45,973	23.16%	\$ 105,109	40.70%	\$ 91,359	41.60%
Capital Markets Lending	132,312	66.64	130,333	50.47	113,068	51.49
Rural America Bonds	10,567	5.32	7,037	2.72	3,457	1.57
Country Mortgages and Retail Lending	9,680	4.88	15,766	6.11	11,715	5.34
Total Association	<u>\$ 198,532</u>	<u>100.00%</u>	<u>\$ 258,245</u>	<u>100.00%</u>	<u>\$ 219,599</u>	<u>100.00%</u>

The gross loan volume of the Association as of December 31, 2008, was \$198,532, a decrease of \$59,713 or 23.12 percent as compared to \$258,245 at December 31, 2007, and a decrease of \$21,067 or 9.59 percent as compared to \$219,599 at December 31, 2006. Net loans outstanding (gross loans net of the allowance for loan losses) on December 31, 2008, were \$194,239 as compared to \$258,013 at December 31, 2007 and \$219,412 at December 31, 2006. Net loans accounted for 73.78 percent of total assets on December 31, 2008 as compared to 80.65 percent of total assets at December 31, 2007 and 79.53 percent of total assets at December 31, 2006. The Association's decrease in gross loan volume during 2008 is largely attributed to the sale of

loan assets through the AgFirst Capitalization Participation Pool (CPP) and the general weakening of the economy.

The Association's total servicing loan volume was \$1.264 billion at December 31, 2008 as compared to \$1.248 billion for December 31, 2007. Total servicing loan volume is equal to the Association's loan volume outstanding plus loans sold and available commitments. The total servicing loan volume represents the total amount of loans that are serviced by the Association.

The diversification of the Association loan volume by type for each of the past three years is shown below.

Loan Type	2008		December 31, 2007		2006	
	<i>(dollars in thousands)</i>					
Real estate mortgage	\$ 99,315	50.03%	\$ 143,035	53.92%	\$ 121,681	55.41%
Production and intermediate-term	44,001	22.16	75,021	30.51	67,278	30.64
Processing and marketing	36,771	18.52	24,632	9.54	18,011	8.20
Farm-related business	12,020	6.05	12,044	4.66	8,515	3.88
Rural home	1,863	0.94	1,686	0.65	1,863	0.85
Energy	1,800	0.91	1,827	0.71	2,251	1.03
Loans to cooperatives	1,642	0.83	-	-	-	-
Communication	1,120	0.56	-	-	-	-
Total	<u>\$ 198,532</u>	<u>100.00%</u>	<u>\$ 258,245</u>	<u>100.00%</u>	<u>\$ 219,599</u>	<u>100.00%</u>

While we make loans and provide financially related services to qualified borrowers in the agricultural and rural sectors and to certain related entities, our loan portfolio is diversified.

The geographic distribution of the loans by state for the past three years is as follows:

State	December 31,		
	2008	2007	2006
Florida	61.45%	75.90%	75.75%
Georgia	6.77	2.82	5.43
South Carolina	5.71	5.60	7.16
Minnesota	3.55	1.78	1.87
California	2.94	2.25	1.66
North Carolina	2.56	1.68	1.70
New York	2.19	1.82	2.42
Virginia	1.36	1.15	0.90
Texas	1.32	1.49	-
Ohio	0.36	0.87	0.79
Washington	-	-	1.63
Other	11.79	4.62	0.69
	<u>100.00%</u>	<u>100.00%</u>	<u>100.00%</u>

Commodity and industry categories are based upon the Standard Industrial Classification system published by the federal government. The system is used to assign commodity or industry categories based upon the largest agricultural commodity of the customer.

The major commodities in the Association loan portfolio are shown below. The predominant commodities are Citrus, Non-Farm, and Horticulture, which constitute over 47 percent of the entire portfolio. The Non-Farm commodities are primarily Rural America Bonds approved under the Farm Credit Administration Bond Pilot Program (see *Mission-Related Investments* section below) and lessors of agriculture property.

Commodity Type	2008		December 31, 2007		2006	
			<i>(dollars in thousands)</i>			
Citrus	\$ 52,628	27%	\$ 84,075	33%	\$ 79,064	36%
Other	26,822	14	32,154	13	34,290	16
Non-Farm	22,893	12	9,510	4	5,895	3
Horticulture	16,793	8	41,894	16	31,443	14
Farm Services	14,219	7	11,572	4	7,728	4
Cattle	12,912	6	18,522	7	15,715	7
Timber	12,195	6	13,494	5	19,799	9
Saw & Paper Mill	10,387	5	5,224	2	9,152	4
Fuel Manufacturing	7,787	4	3,779	1	-	-
Vegetables and Melons	7,460	4	6,786	3	3,105	1
Other Field Crops	5,573	3	5,219	2	-	-
Dairy Farms	4,621	2	8,820	3	6,769	3
Sugar Cane	4,242	2	5,096	2	4,969	2
Financial Institutions	-	-	-	-	1,671	1
General Farm	-	-	6,620	3	-	-
Misc. Business/ Credit Institutions	-	-	5,480	2	-	-
Total	\$ 198,532	100%	\$ 258,245	100%	\$ 219,599	100%

Repayment ability is closely related to the commodities produced by our borrowers, and increasingly, the off-farm income of borrowers. The Association's loan portfolio contains a concentration of Citrus and Horticultural producers. Although a large percentage of the loan portfolio is concentrated in these enterprises, many of these operations are diversified within their enterprise and/or with crop production that reduces overall risk exposure. Even though the concentration of large loans has increased over the past several years, the agricultural enterprise mix of these loans is diversified and similar to that of the overall portfolio. The risk in the portfolio associated with commodity concentration and large loans is reduced by the range of diversity of enterprises in the Association's territory.

For the past few years, the Association has experienced a shift in loan assets. The long-term volume trend has been downward while the short and intermediate-term loan volume trend is upward. The short-term portfolio, which is heavily influenced by operating-type loans, normally reaches a peak balance in August and rapidly declines in the fall months as commodities are marketed and proceeds are applied to repay operating loans.

During 2008, the Association increased activity in the buying of loan participations while decreasing activity in the selling of loan participations within the System. This provides a means for the Association to spread credit concentration risk and realize non-patronage sourced interest and fee income, which is intended to strengthen our capital position.

Loan Participations	2008	2007	2006
	<i>(dollars in thousands)</i>		
Participations Purchased			
– FCS Institutions	\$ 418,051	\$ 404,621	\$ 347,705
Participations Purchased			
– Non-FCS Institutions	-	-	-
Participations Sold	(737,483)	(745,989)	(572,114)
Total	\$(319,432)	\$(341,368)	\$(224,409)

The Association did not have any loans sold with recourse, retained subordinated participation interests in loans sold, or interests in pools of subordinated participation interests for the year ended December 31, 2008.

The Association sells qualified long-term mortgage loans into the secondary market. For the year ended December 31, 2008, the Association originated loans for resale totaling \$34, which was sold into the secondary market. The Association also participates in the Farmer Mac Long Term Stand-By program. Farmer Mac was established by Congress to provide liquidity to agricultural lenders. At December 31, 2008, the Association had loans amounting to \$4,609 which were 100 percent guaranteed by Farmer Mac.

MISSION-RELATED INVESTMENTS

During 2005, the FCA initiated an investment program to stimulate economic growth and development in rural areas. The FCA outlined a program to allow System institutions to hold such investments, subject to approval by the FCA on a case-by-case basis. FCA approved a Rural America Bonds pilot program under the mission-related investments umbrella, as described below.

In October 2005, the FCA authorized AgFirst and the Associations to make investments in Rural America Bonds under a three-year pilot period. Rural America Bonds may include debt obligations issued by public and private enterprises, corporations, cooperatives, other financing institutions, or rural lenders where the proceeds would be used to support agriculture, agribusiness, rural housing, or economic development, infrastructure, or community development and revitalization projects in rural areas. Examples include investments that fund value-added food and fiber processors and marketers, agribusinesses, commercial enterprises that create and maintain employment opportunities in rural areas, community services, such as schools, hospitals, and government facilities, and other activities that sustain or revitalize rural communities and their economies. The objective of this pilot program is to help meet the growing and diverse financing needs of agricultural enterprises, agribusinesses, and rural communities by providing a flexible flow of money to rural areas through bond financing. These bonds may be classified as Loans or Investments on the Consolidated Balance Sheets depending on the nature of the investment. As of December 31, 2008 and December 31, 2007, the Association had \$13,956 and \$8,052, respectively, in Rural America Bonds, and they are classified as Loans or Investments on the Consolidated Balance Sheets.

INVESTMENT SECURITIES

As permitted under FCA regulations, the Association is authorized to hold eligible investments for the purposes of reducing interest rate risk and managing surplus short-term funds. The Bank is responsible for approving the investment policies of the Association. The Bank annually reviews the investment portfolio of every Association that it funds. The Association's investments, which are classified as being held-to-maturity, consist of asset-backed securities (ABS). The ABSs amounted to \$35,128 at December 31, 2008 and \$35,598 at December 31, 2007. These ABSs are rated AAA, as their principal, which amounted to \$32,886 at December 31, 2008, is guaranteed by the full faith and credit of the United States government.

In view of the recent economic conditions and volatility related to these types of securities, the Association is actively monitoring the creditworthiness of these securities. These securities are supported by various forms of credit enhancements including insurance guarantees from AAA rated insurers, over-collateralization and favorable priority of payments. Based on our evaluations, we believe these securities do not pose a significant risk of loss given the credit enhancements and relatively short weighted average lives. However, in the event a security is downgraded, we may be required by our regulator to dispose of the security.

CREDIT RISK MANAGEMENT

Credit risk arises from the potential inability of an obligor to meet its repayment obligation. As part of the process to evaluate the success of a loan, the Association continues to review the credit quality of the loan portfolio on an ongoing basis. With the approval of the Association Board of Directors, the Association establishes underwriting standards and lending policies that provide direction to loan officers. Underwriting standards include, among other things, an evaluation of:

- Character – borrower integrity and credit history
- Capacity – repayment capacity of the borrower based on cash flows from operations or other sources of income
- Collateral – protection for the lender in the event of default and a potential secondary source of repayment
- Capital – ability of the operation to survive unanticipated risks
- Conditions – intended use of the loan funds

The credit risk management process begins with an analysis of the borrower’s credit history, repayment capacity, and financial position. Repayment capacity focuses on the borrower’s ability to repay the loan based upon cash flows from operations or other sources of income, including non-farm income. Real estate loans must be collateralized by first liens on the real estate (collateral). As required by FCA regulations, each institution that makes loans on a collateralized basis must have collateral evaluation policies and procedures. Real estate mortgage loans may be made only in amounts up to 85 percent of the original appraised value of the property taken as collateral or up to 97 percent of the appraised value if guaranteed by a state, federal, or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Appraisals are required for loans of more than \$250,000. In addition, each loan is assigned a credit risk rating based upon the underwriting standards. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses, and risks in a particular relationship.

We review the credit quality of the loan portfolio on an ongoing basis as part of our risk management practices. Each loan is classified according to the Uniform Classification System, which is used by all Farm Credit System institutions. Below are the classification definitions.

- Acceptable – Assets are expected to be fully collectible and represent the highest quality.
- Other Assets Especially Mentioned (OAEM) – Assets are currently collectible but exhibit some potential weakness.

- Substandard – Assets exhibit some serious weakness in repayment capacity, equity, and/or collateral pledged on the loan.
- Doubtful – Assets exhibit similar weaknesses to substandard assets. However, doubtful assets have additional weaknesses in existing facts, conditions and values that make collection in full highly questionable.
- Loss – Assets are considered uncollectible.

The following table presents selected statistics related to the credit quality of loans including accrued interest at December 31.

Credit Quality	2008	2007	2006
Acceptable & OAEM	89.11%	99.61%	99.87%
Substandard	10.47	0.39	0.13
Doubtful	0.42	–	–
Loss	–	–	–
Total	100.00%	100.00%	100.00%

Nonperforming Assets

The Association’s loan portfolio is divided into performing and high-risk categories. A Special Assets Management Department is responsible for servicing loans classified as high-risk. The high-risk assets, including accrued interest, are detailed below:

High-risk Assets	December 31,		
	2008	2007	2006
	<i>(dollars in thousands)</i>		
Nonaccrual loans	\$14,437	\$ 995	\$ –
Restructured loans	–	–	–
Accruing loans 90 days past due	–	–	613
Total high-risk loans	14,437	995	613
Other property owned	178	–	–
Total high-risk assets	\$14,615	\$ 995	\$ 613
Ratios			
Nonaccrual loans to total loans	7.27%	0.39%	–%
High-risk assets to total assets	5.55%	0.31%	0.22%

Nonaccrual loans represent all loans where there is a reasonable doubt as to the collection of principal and/or future interest accruals, under the contractual terms of the loan. In substance, nonaccrual loans reflect loans where the accrual of interest has been suspended. Nonaccrual loans increased \$13,442 in 2008. This increase resulted primarily from loans of 4 borrower relationships that had deteriorated in repayment capacity.

Loan restructuring is available to financially distressed borrowers. Restructuring of loans occurs when the Association grants a concession to a borrower based on either a court order or good faith in a borrower’s ability to return to financial viability. The concessions can be in the form of a modification of terms or rates, a compromise of amounts owed, or deed in lieu of foreclosure. Other receipts of assets and/or equity to pay the loan in full or in part are also considered restructured loans. The type of alternative financing structure chosen is based on minimizing the loss incurred by both the Association and the borrower.

Allowance for Loan Losses

The allowance for loan losses at each period end was considered by Association management to be adequate to absorb probable losses existing in and inherent to its loan portfolio. The increase in the allowance for loan losses in 2008 was primarily due to the borrower relationships placed in nonaccrual status as discussed above.

The following table presents the activity in the allowance for loan losses for the most recent three years:

	Year Ended December 31,		
	2008	2007	2006
Balance at beginning of year	\$ 232	\$ 187	\$ 183
Charge-offs:			
Production and intermediate term	(25)	-	-
Real estate mortgage	(94)	-	-
Rural residential real estate	(19)	-	-
Total charge-offs	(138)	-	-
Recoveries:			
Real estate mortgage	16	17	14
Production and intermediate term	-	2	-
Total recoveries	16	19	14
Net (charge-offs) recoveries	(122)	19	14
Provision for (reversal of allowance for) loan losses	4,183	26	(10)
Balance at end of year	<u>\$ 4,293</u>	<u>\$ 232</u>	<u>\$ 187</u>
Ratio of net (charge-offs) recoveries during the period to average loans outstanding during the period	<u>(0.067)%</u>	<u>0.01%</u>	<u>0.01%</u>

The allowance for loan losses by loan type for the most recent three years is as follows:

Allowance for Loan Losses by Type	December 31,		
	2008	2007	2006
	<i>(dollars in thousands)</i>		
Real estate mortgage	\$ 2,958	\$ 197	\$ 170
Production and intermediate-term	327	20	16
Agribusiness	972	15	-
Rural residential real estate	36	-	1
Total allowance for loan losses	<u>\$ 4,293</u>	<u>\$ 232</u>	<u>\$ 187</u>

The allowance for loan losses as a percentage of loans outstanding and as a percentage of certain other credit quality indicators is shown below:

Allowance for Loan Losses as a Percentage of:	December 31,		
	2008	2007	2006
Total loans	2.16%	0.09%	0.09%
Nonperforming loans	29.74%	23.30%	30.51%
Nonaccrual loans	29.74%	23.30%	-%

Please refer to Note 4, "Loans and Allowance for Loan Losses," of the Notes to the Consolidated Financial Statements, for further information concerning the allowance for loan losses.

RESULTS OF OPERATIONS

Net Interest Income

Net interest income was \$4.4 million, \$6.3 million and \$7.6 million in 2008, 2007 and 2006, respectively. Net interest income is the difference between interest income and interest expense. Net interest income is a principal source of earnings for the Association and is impacted by volume, yields on assets and cost of debt. Net interest income decreased by \$1.9 million or 30.41 percent in 2008 compared to 2007. The primary reason for the decrease in net interest income is attributed to loan volume as the Association sold an additional \$90 million in 2008 to the AgFirst Capitalization Participation Pool. The sold loans generate income in the form of patronage.

The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following table:

Change in Net Interest Income:

	Volume*	Nonaccrual		Total
		Rate	Income	
	<i>(dollars in thousands)</i>			
12/31/08 - 12/31/07				
Interest income	\$ (3,358)	\$ (4,291)	\$ (86)	\$ (7,735)
Interest expense	(1,966)	(3,848)	-	(5,814)
Change in net interest income	<u>\$ (1,392)</u>	<u>\$ (443)</u>	<u>\$ (86)</u>	<u>\$ (1,921)</u>
12/31/07 - 12/31/06				
Interest income	\$ (1,661)	\$ (14)	\$ 86	\$ (1,589)
Interest expense	(674)	385	-	(289)
Change in net interest income	<u>\$ (987)</u>	<u>\$ (399)</u>	<u>\$ 86</u>	<u>\$ (1,300)</u>

* Volume variances can be the result of increased/decreased loan volume or from changes in the percentage composition of assets and liabilities between periods.

Noninterest Income

Noninterest income for each of the three years ended December 31 is shown in the following table:

Noninterest Income	For the Year Ended			Percentage	
	December 31,			Increase/(Decrease)	
	2008	2007	2006	2008/ 2007	2007/ 2006
	<i>(dollars in thousands)</i>				
Loan fees	\$ 702	\$ 612	\$ 680	14.71%	(10.00)%
Fees for financially related services	112	-	-	-	-
Patronage refund from other					
Farm Credit Institutions	7,008	8,434	5,663	(16.91)	48.93
Other noninterest income	4	249	192	(98.39)	29.69
Total noninterest income	<u>\$ 7,826</u>	<u>\$ 9,295</u>	<u>\$ 6,535</u>	<u>(15.80)%</u>	<u>42.23%</u>

The decrease of \$1,426, or 16.91 percent, in patronage refunds is attributed to affiliated Farm Credit Associations reducing patronage distributions paid on loans purchased from the Association. This reduction in patronage refund is a result of having to capitalize prior year loan growth and increased non-accrual volume within the System. The ACA receives patronage from Farm Credit Cooperative entities who pay patronage on loans purchased from the Association.

Noninterest Expense

Noninterest expense for each of the three years ended December 31 is shown in the following table:

Noninterest Expense	For the Year Ended			Percentage	
	December 31,			Increase/(Decrease)	
	2008	2007	2006	2008/ 2007	2007/ 2006
<i>(dollars in thousands)</i>					
Salaries and employee benefits	\$ 3,660	\$ 3,930	\$ 3,651	(6.87)%	7.64%
Occupancy and equipment	398	418	392	(4.78)	6.63
Insurance Fund premiums	268	340	373	(21.18)	(8.85)
Other operating expenses	1,595	1,731	1,460	(7.86)	18.56
Total noninterest expense	\$ 5,921	\$ 6,419	\$ 5,876	(7.76)%	9.24%

Noninterest expense decreased \$498 or 7.76 percent for the year ended December 31, 2008, as compared to the same period of 2007 and increased \$45 or 0.77 percent compared to December 31, 2006.

Salaries and employee benefits decreased in 2008, as compared with 2007, primarily due to decreased costs associated with merit and incentive compensation.

Insurance Fund premiums decreased 21.18 percent for the twelve months ended December 31, 2008, compared to the same period of 2007. This decrease was due to lower insured loan volume for the first half of 2008 and the change in methodology (base) in the second half of 2008 to insured debt outstanding for assessing the insurance premiums as a result of the 2008 Farm Bill. Please refer to the "Regulatory Matters" section of this management's discussion and analysis for details concerning the 2008 Farm Bill.

Income Taxes

The Association recorded a provision for income taxes of \$1 for the year ended December 31, 2008, as compared to a benefit of \$76 for 2007 and a provision of \$64 for 2006. Refer to Note 2, "Summary of Significant Accounting Policies, Income Taxes," of the Notes to the Consolidated Financial Statements, for more information concerning Association income taxes.

Key Results of Operations Comparisons

Key results of operations comparisons for each of the twelve months ended December 31 are shown in the following table:

Key Results of Operations Comparisons	For the 12 Months Ended		
	12/31/08	12/31/07	12/31/06
Return on average assets	0.85%	3.25%	2.79%
Return on average members' equity	4.34%	18.13%	16.11%
Net interest income as a percentage of average earning assets	2.03%	2.43%	2.71%
Net (charge-offs) recoveries to average loans	(0.067)%	0.01%	0.01%

A key factor in the growth of net income for future years will be continued improvement in net interest and noninterest income. Our goal is to generate earnings sufficient to fund operations, adequately capitalize the Association, and achieve an adequate rate of return for our members. To meet this goal, the general economy and to a certain extent the agricultural economy along with the real estate market must rebound and show improvement and the Association must meet certain objectives. These objectives are to attract and maintain high quality loan volume

priced at competitive rates and to manage credit risk in our entire portfolio, while efficiently meeting the credit needs of our members.

LIQUIDITY AND FUNDING SOURCES

Liquidity and Funding

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement (GFA). The GFA 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, creating notes payable (or direct loans) to the Bank. The Bank manages interest rate risk through direct loan pricing and asset/liability management. The notes payable are segmented into variable rate and fixed rate components. 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. Association capital levels effectively create a borrowing margin between the amount of loans outstanding and the amount of notes payable outstanding. This margin is commonly referred to as "Loanable Funds."

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. The liquidity policy of the Association is to manage cash balances to maximize debt reduction and to increase loan volume. As borrower payments are received, they are applied to the Association's note payable to the Bank. The Association's participation in the Farmer Mac, investments, and other secondary market programs provides additional liquidity. Sufficient liquid funds have been available to meet all financial obligations. There are no known trends likely to result in a liquidity deficiency for the Association.

Total notes payable to the Bank at December 31, 2008, was \$211,647 as compared to \$260,052 at December 31, 2007 and \$217,032 at December 31, 2006. The decrease of 18.61 percent compared to December 31, 2007 was primarily attributable to the decreased loan growth of the Association from the sale of loan assets through the CPP and the general weakening of the economy. The average volume of outstanding notes payable to the Bank was \$194,645, \$226,965 and \$238,372 for the years ended December 31, 2008, 2007, and 2006 respectively. Refer to Note 7, "Notes Payable to AgFirst Farm Credit Bank," of the Notes to the Consolidated Financial Statements, for weighted average interest rates and maturities, and additional information concerning the Association's notes payable.

The Association had no lines of credit from third party financial institutions as of December 31, 2008.

Funds Management

The Bank and the Association manage assets and liabilities to provide a broad range of loan products and funding options, which are designed to allow the Association to be competitive in all interest rate environments. The primary objective of the

asset/liability management process is to provide stable and rising earnings, while maintaining adequate capital levels by managing exposure to credit and interest rate risks.

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed, adjustable and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to market indices such as the Prime Rate or the 90-day London Interbank Offered Rate (LIBOR). Adjustable rate mortgages are indexed to U.S. Treasury Rates. Fixed rate loans are priced based on the current cost of System debt of similar terms to maturity.

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

Relationship with the Bank

The Association's statutory obligation to borrow only from the Bank and the Bank's ability to access capital of the Association is discussed in Note 5, "Investment in AgFirst Farm Credit Bank" and Note 7, "Notes Payable to AgFirst Farm Credit Bank" of the Notes to the Consolidated Financial Statements included in this Annual Report.

The Bank's role in mitigating the Association's exposure to interest rate risk is described in the "Liquidity and Funding Sources" section of this Management's Discussion and Analysis and in Note 7, "Notes Payable to AgFirst Farm Credit Bank" included in this Annual Report.

CAPITAL RESOURCES

Capital serves to support asset growth and provide protection against unexpected credit and interest rate risk and operating losses. Capital is also needed for future growth and investment in new products and services.

The Association Board of Directors (Board) establishes, adopts, and maintains a formal written capital adequacy plan to ensure that adequate capital is maintained for continued financial viability, to provide for growth necessary to meet the needs of members/borrowers, and to ensure that all stockholders are treated equitably. There were no material changes to the capital plan for 2008 that would affect minimum stock purchases or would have an effect on the Association's ability to retire stock and distribute earnings. The Board has elected to extend the revolvment cycle for retiring allocated surplus stock to 7 years from 5 years.

Total members' equity at December 31, 2008, decreased 8.20 percent to \$47,338 from the December 31, 2007 total of \$51,569. At December 31, 2007, total members' equity decreased 0.37 percent from the December 31, 2006 total of \$51,759. The decrease for both years was primarily attributed to the Association's Board adopting a shorter revolvment cycle and thereby distributing additional allocated surplus back to members.

Total capital stock and participation certificates were \$882 on December 31, 2008, compared to \$937 on December 31, 2007 and \$1,109 on December 31, 2006. The decrease was attributed to the protected stock and participation certificates in loans liquidated in the normal course of business, retirement of excess stock through revolvment and new loans being capitalized at lower levels.

FCA sets minimum regulatory capital requirements for System banks and associations. Capital adequacy is evaluated using a number of regulatory ratios. According to the FCA regulations, each institution's permanent capital ratio is calculated by dividing permanent capital by a risk-adjusted asset base. Risk adjusted assets mean the total dollar amount of the institution's assets adjusted by an appropriate credit conversion factor as defined by regulation. For all periods represented, the Association exceeded minimum regulatory standards for all the ratios.

The Association's capital ratios as of December 31 and the FCA minimum requirements follow:

	2008	2007	2006	Regulatory Minimum
Permanent capital ratio	12.05%	15.19%	17.08%	7.00%
Total surplus ratio	11.83%	15.13%	16.85%	7.00%
Core surplus ratio	10.59%	10.67%	14.27%	3.50%

The decrease in the Association's permanent capital, total surplus, and core surplus for December 31, 2008 was attributed to reduced earnings as a result of increased provisions for loan losses related to declining credit quality. The decrease for December 31, 2007 was attributed to increased loan volume within the Association. There are no trends, commitments, contingencies, or events that are likely to affect the Association's ability to meet regulatory minimum capital standards and capital adequacy requirements.

See Note 8, "Members' Equity," of the Consolidated Financial Statements, for further information concerning capital resources.

PATRONAGE PROGRAM

Prior to the beginning of any fiscal year, the Association's Board of Directors, by adoption of a resolution, may establish a Patronage Allocation Program to distribute its available consolidated net earnings. This resolution provides for the application of net earnings in the manner described in the Association's Bylaws. This includes the setting aside of funds to increase surplus to meet minimum capital adequacy standards established by FCA Regulations, to increase surplus to meet Association capital adequacy standards to a level necessary to support competitive pricing at targeted earnings levels, and for reasonable reserves for necessary purposes of the Association. After excluding net earnings attributable to (a) the portion of loans participated to another institution, and (b) participation loans purchased, remaining consolidated net earnings are eligible for allocation to borrowers. Refer to Note 8, "Members' Equity," of the Notes to the Consolidated Financial Statements, for more information concerning the patronage distributions. The Association declared patronage distributions of \$2,000 in 2008, \$8,500 in 2007, and \$8,000 in 2006.

YOUNG, BEGINNING AND SMALL (YBS) FARMERS AND RANCHERS PROGRAM

The Association's mission is to provide financial services to agriculture and the rural community, which includes providing

credit to young*, beginning** and small*** farmers. Because of the unique needs of these individuals, and their importance to the future growth of the Association, the Association has established annual marketing goals to increase our market share of loans to YBS farmers. Specific marketing plans have been developed to target these groups, and resources have been designated to help ensure YBS borrowers have access to a stable source of credit. As a result of a depressed Florida economy and a tightening credit market, only one sixth of the 2008 specific marketing goals established were met.

The following table outlines the loan volume and number of YBS loans in the loan portfolio for the Association.

	As of December 31, 2008	
	Number of Loans	Amount of Loans
Young	77	\$9,586
Beginning	219	32,419
Small	293	19,368

Note: For purposes of the above table, a loan could be classified in more than one category, depending upon the characteristics of the underlying borrower.

The 2002 USDA (2002 is the latest USDA Ag census data available; next census will be available in February 2009) Ag census data has been used as a benchmark to measure penetration of the Association’s marketing efforts. The census data indicated that within the Association’s chartered territory (counties) 26.27 percent were Young, 12.33 percent were Beginning, and 4.94 percent were Small. Comparatively, as of December 31, 2008, the Association’s YBS portfolio contained 30.20 percent Young, 10.70 percent Beginning, and 5.05 percent Small farmers of the ACA’s census data demographic.

The Association focuses on education and financial support in helping YBS farmers finance their operations. Educational programs include seminars, speaking opportunities and training sessions, which are conducted throughout the year. These educational opportunities are both in-house, in the form of events held by the Association, and external, in which case, the Association provides a speaker or provides educational materials. The Association website, www.farmcreditswfl.com, includes an entire section of information and resources for YBS visitors to the site. Educational programs also include those activities in which the Association participates in local events as a sponsor (such as 4-H and FFA fairs) or as an exhibitor (such as industry or trade shows).

The focus on financial support addresses the specific credit programs and partnerships that the Association has developed to help small farmers, young farmers, and farmers just starting out. It comprises programs such as those offered by the Farm Service Agency (FSA), which includes guaranteed and direct loans to qualifying borrowers. The Association is a “preferred lender,” the highest status designated by FSA.

The Association is also a Guaranteed Participating Lender for the Small Business Administration (SBA), which offers lending programs specifically for small borrowers. Additionally, the Association offers flexible financing options in-house for qualifying borrowers.

A senior executive oversees the YBS program and coordinates the efforts of other staff members. The Association includes

YBS goals in the annual strategic plan, and reports on those goals and achievements to the Board of Directors on a quarterly basis.

The Association is committed to the future success of young, beginning and small farmers.

* **Young farmers** are defined as those farmers, ranchers, producers or harvesters of aquatic products who are age 35 or younger as of the date the loan is originally made.

** **Beginning farmers** are defined as those farmers, ranchers, producers or harvesters of aquatic products who have 10 years or less farming or ranching experience as of the date the loan is originally made.

*** **Small farmers** are defined as those farmers, ranchers, producers or harvesters of aquatic products who normally generate less than \$250 in annual gross sales of agricultural or aquatic products at the date the loan is originally made.

REGULATORY MATTERS

For the twelve months ended December 31, 2008, the FCA took no enforcement action against the Association.

On June 16, 2008, FCA published a proposed rule in the Federal Register that would authorize Banks, Associations, or service corporations to invest in rural communities, i.e., communities that have fewer than 50,000 residents and are outside of an urbanized area, under certain conditions. The proposed rule would authorize two types of rural community investments: (1) investment in debt securities that would involve projects or programs that benefit the public in rural communities, and (2) equity investment in venture capital funds, which funds create economic opportunities and jobs in rural communities by providing capital to small or start-up businesses. Under the proposed rule, these investments would be limited to 150 percent of the institution’s total surplus. The comment period closed August 15, 2008.

Federal Legislation

In June, 2008, Congress passed the 2008 Farm Bill. This 2008 Farm Bill governs farm commodity, conservation, and other USDA programs for five years, from 2008 through 2012. The 2008 Farm Bill includes significant federal financial support for wheat, feed grains, cotton, rice, oilseeds, and dairy. It also contains new, expanded assistance for certain specialty crops. Overall, the 2008 Farm Bill maintains the government payments to farmers that had been in place under the previous farm bill. It also amended the Farm Credit Act to allow the Insurance Corporation to assess insurance premiums based on each Bank’s prorata share of adjusted outstanding insured debt (rather than loans), aligning premiums with the risk that is being insured. Premiums of up to 20 basis points could be charged against insured debt adjusted for loans and investments guaranteed by U.S. or state governments, and up to an additional 10 basis points could be charged for any nonaccrual loan volume or investments that are other-than-temporarily impaired. Previously, premiums of up to 15 basis points could be charged on accruing loans and up to 25 basis points for nonaccrual loans.

Using the new authorities contained in the 2008 Farm Bill, in June 2008, the Insurance Corporation sets premiums at 15 basis points on adjusted insured debt outstanding for the third quarter

of 2008 and 18 basis points on adjusted insured debt outstanding for the fourth quarter of 2008. In addition, for the second half of 2008, there was a 10 basis point premium on the average principal outstanding for nonaccrual loans and on the average amount of any other-than-temporarily impaired investments. The Insurance Corporation has provided guidance to System institutions that the premium rates will be increased to 20 basis points in 2009.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 158, "*Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*" (SFAS No. 158). SFAS No. 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in that funded status in the year in which the changes occur through other comprehensive income. SFAS No. 158 further requires the determination of the fair value of plan assets at year-end and recognition of actuarial gains and losses, prior service costs or credits, and transition assets and obligations as a component of other comprehensive income. In addition, SFAS No. 158 requires that the funded status of a plan be measured as of the date of the year-end financial statements, effective for fiscal years ending after December 15, 2008. Prior to 2008, the District used a measurement date of September 30th. In 2008, the District used a measurement date of December 31st as required. See Note 10, "Employee Benefit Plans", of the Consolidated Financial Statements, for the impact of SFAS No. 158 on the current period.

In September 2006, the FASB also issued Statement of Financial Accounting Standards No. 157, "*Fair Value Measurements*" (SFAS No. 157). SFAS No. 157 defines fair

value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. As a result, there is now a common definition of fair value to be used throughout generally accepted accounting principles. The FASB believes that the new standard will make the measurement of fair value more consistent and comparable and improve disclosures about those measures. SFAS No. 157 clarifies that the term fair value is intended to mean a market-based measure, not an entity-specific measure. In measuring fair value for a financial statement item, SFAS No. 157 sets forth a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The highest priority is given to quoted prices in active markets and the lowest priority to unobservable inputs. Additional disclosure requirements are required for the lowest priority level. The Association adopted SFAS No. 157 effective January 1, 2008, on a prospective basis. See Note 13, "Fair Value Measurement," of the Consolidated Financial Statements, for disclosures required by SFAS No. 157.

In December 2007, the FASB issued Statements of Financial Accounting Standards No. 141R, "*Business Combinations*" (SFAS No. 141R). SFAS No. 141R requires business combinations to be accounted for under the acquisition method of accounting (previously called the purchase method). The acquisition method requires (a) identifying the acquirer, (b) determining the acquisition date, (c) recognizing and measuring the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, at their acquisition date fair values, and (d) recognizing and measuring goodwill or a gain from a bargain purchase. SFAS No. 141R will be applied to business combinations on or after January 1, 2009. The Association is still evaluating the provisions of SFAS No. 141R, but believes that its adoption will significantly impact its accounting for combinations/acquisitions that may occur in 2009 and beyond.

Disclosure Required by Farm Credit Administration Regulations

Description of Business

Descriptions of the territory served, persons eligible to borrow, types of lending activities engaged in, financial services offered and related Farm Credit organizations are incorporated herein by reference to Note 1 of the Consolidated Financial Statements, "Organization and Operations," included in this Annual Report to shareholders.

The description of significant developments that had or could have a material impact on earnings or interest rates to borrowers, acquisitions or dispositions of material assets, material changes in the manner of conducting the business, seasonal characteristics, and concentrations of assets, if any, is incorporated in "Management's Discussion & Analysis of Financial Condition & Results of Operations" included in this Annual Report.

Description of Property

The following table sets forth certain information regarding the properties of the reporting entity, all of which are located in Florida:

<u>Location</u>	<u>Description</u>	<u>Form of Ownership</u>
330 N. Brevard Avenue Arcadia	Administrative Offices	Owned
1311 Highway 17 N. Wauchula	Branch	Owned
340 N. Brevard Avenue Arcadia	Operations	Owned
12415 SW Sheri Avenue, Suite A Lake Suzy	Country Mortgages	Leased

The Lake Suzy office is on a 3-year renewable contract lease term through April 2012.

Legal Proceedings

Information, if any, to be disclosed in this section is incorporated herein by reference to Note 12 of the Consolidated Financial Statements, "Commitments and Contingencies," included in this Annual Report.

Description of Capital Structure

Information to be disclosed in this section is incorporated herein by reference to Note 8 of the Consolidated Financial Statements, "Members' Equity," included in this Annual Report.

Description of Liabilities

The description of liabilities and contingent liabilities to be disclosed in this section is incorporated herein by reference to Notes 2, 7 and 12 of the Consolidated Financial Statements included in this Annual Report.

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

"Management's Discussion & Analysis of Financial Condition & Results of Operations," which appears in this Annual Report and is to be disclosed in this section, is incorporated herein by reference.

Senior Officers

The following represents certain information regarding the senior officers of the Association and their business experience for the past five years:

<u>Senior Officer</u>	<u>Position, Prior Experience, and Other Business Interests</u>
-----------------------	---

Jimmy V. Knight	President & Chief Executive Officer since January 1997.
Bryan L. Byrd	Executive Vice President & Chief Operating Officer since July 2002.
Daniel B. Irby	Senior Vice President & Chief Financial Officer since May 2005. His previous experience was a tax and financial accountant, providing consulting services to clients of CPA firms.
Ronnie D. Crawford	Senior Vice President & Chief Lending Officer since October 2006. He has been with the ACA for 22 years and has held various positions including Branch Manager, Internal Reviewer, Litigation Specialist, Credit Administrator, and Risk Policy Manager until promoted to Chief Lending Officer in October 2006.
William F. Federer	Senior Vice President & Chief Relationship Officer since 2007. He has been with the ACA for 10 years and has held various positions including Sr. Agricultural - Commercial Loan Officer, and Lending Coach.

The total amount of compensation earned by the CEO and the highest paid officers as a group during the years ended December 31, 2008, 2007 and 2006, is as follows:

Name of Individual or Number in Group	Year	Annual		Deferred Comp.	Perq./ Other*	Total
		Salary	Bonus			
Jimmy V. Knight	2008	\$305,012	-	-	\$20,257	\$325,269
Jimmy V. Knight	2007	\$265,010	\$ 85,982	-	\$18,050	\$369,042
Jimmy V. Knight	2006	\$247,792	\$100,155	\$20,984	\$ 6,371	\$375,301
5	2008	\$588,904	-	-	\$31,792	\$620,696
5	2007	\$558,770	\$180,111	-	\$25,566	\$764,447
5	2006	\$471,309	\$190,581	-	\$10,411	\$671,301

* Primarily comprised of company contributions to 401(k) plan (see Note 10 of the Consolidated Financial Statements, "Employee Benefit Plans," included in this Annual Report), group life insurance premiums, and Association-provided automobile.

In addition to a base salary, senior officers may earn additional compensation through the Employee Profit Sharing Plan (EPS) approved by the Board of Directors and adopted beginning in fiscal year 2007. All employees are covered under the EPS Plan which is designed to motivate employees to exceed the business plan goals during the fiscal year. These goals typically include net income and credit quality. In addition, some senior officers may earn additional compensation through the Loan Officers Sales Performance Plan.

Loan Officers are compensated for loans made that exceed specific Business Plan goals approved by the Board of Directors. Both plan years run from November 1 to October 31 and distribution for both plans is made in the last quarter of the year.

Additionally, all employees are reimbursed for all direct travel expenses incurred when traveling on Association business. A copy of the travel policy is available to shareholders upon written request.

Disclosure of information on the total compensation paid during 2008 to any senior officer, or to any other individual included in the aggregate, is available to shareholders upon request.

NONQUALIFIED PLANS

Defined Benefit-Type

The Association sponsors a non-qualified defined benefit supplemental executive retirement plan. The purpose of the non-qualified plan is to provide benefits that supplement the qualified defined benefit plan in which the Association’s employees participate. For eligible key employees, compensation in excess of the 401(a)(17) limit and benefits in excess of the 415(b) limit in the qualified defined benefit plan will be made up through the non-qualified plan. As a non-qualified plan, assets have been allocated and separately invested for this plan, but are not isolated from the general creditors of the Association.

Defined Contribution-Type

The Association sponsors a non-qualified supplemental deferred compensation plan. The purpose of the non-qualified plan is to provide supplemental deferred compensation options to eligible key employees. As a non-qualified plan, assets have been allocated and separately invested for this plan, but are not isolated from the general creditors of the Association.

Directors

The following chart details the year the director began serving on the board, the current term of expiration, total cash compensation paid for days served at Board Meetings and incidentals:

DIRECTOR	ORIGINAL YEAR OF ELECTION OR APPOINTMENT	CURRENT TERM EXPIRATION	TOTAL COMP. PAID DURING 2008
Walter S. Farr, <i>Chairman</i>	1991	2010	\$11,200
John R. Alexander, <i>Vice Chairman</i>	1992	2009	9,400
Howard P. Bateman	2004	2010	9,800
John Roy Gough	1992	2009	9,000
Jerry M. Newlin	2007	2011	7,350
John F. Smoak, Jr.	1981	2009	9,600
J. Mark Wheeler	1999	2011	9,800
E.E. "Bucky" Waldron, <i>Outside Director</i>	2002	2011	9,800
Lisa Sherman, <i>Outside Director</i>	2008	2011	400
William G. Welles III, <i>Retired Chairman</i>	1975	Retired April 2008	4,000
			<u>\$80,350</u>

Note: In 2008, Lisa Sherman was appointed to the Board in December of the fourth quarter and received honoraria compensation for one Board meeting.

The following represents certain information regarding the directors of the Association and their principal occupation and employment for the past five years:

Walter S. Farr, Chairman, is a retired Certified Public Accountant who has interests in citrus and beef cattle. He serves as a Trustee and Officer of the Matred Carlton Olliff Foundation, a charitable organization.

John R. Alexander, Vice Chairman, is the Chairman of the Board of Alico Inc., which is a land management corporation traded on NASDAQ under the symbol ALCO.

Howard P. "Rowdy" Bateman, manages a citrus and cattle operation for Bright Hour Ranch in Desoto County. He has personal interests in a family cattle operation, as well as his own personal cattle operation. Mr. Bateman currently serves on the Peace River Valley Citrus Growers Association Board, and serves as a member of the Florida Cattleman’s Foundation.

John Roy Gough is an agri-chemical salesman also involved in citrus and cattle ranching.

Jerry M. Newlin, is Vice President of citrus production and harvesting for Orange-Co LP. He serves as a member of Florida Citrus Production Managers Association and is a Board member of Florida Citrus Production Research Advisory Council (Research Box Tax).

John F. Smoak, Jr. is self-employed through Smoak Groves, Inc., a privately owned agri-business corporation.

J. Mark Wheeler, is chief financial officer of Wheeler Farms, inc., which grows citrus in Brevard, Desoto, Glades and Polk Counties in Florida. He serves on the Boards of AgFirst Farm Credit Bank, Florida Citrus Mutual, an industry trade association, and Wheeler Brothers, Inc., a family-held citrus contract harvesting corporation. Mr. Wheeler is president of Hardee Livestock Market, Inc., a beef cattle operation, and Boston Mining Company, a citrus, real estate and cash investment organization.

E.E. "Bucky" Waldron, Outside Director, is an attorney in a private civil practice in Desoto County.

Lisa Sherman, Outside Director, is a Certified Public Accountant who has an interest in beef cattle.

Subject to approval by the board, the Association may allow directors honoraria of \$400 for attendance at meetings, committee meetings, or special assignments and \$1,250 per quarter for incidental services. Chairman of the Board receives \$1,500 per quarter for incidental services, \$500 for attendance of meetings or special assignments. Directors who serve as Chairman of committees are compensated \$500 for attendance of these meetings. Total compensation paid to directors as a group was \$107,300. No director received more than \$5,000 in non-cash compensation during the year.

The following chart details the number of meetings, other activities, current committee assignments, and additional compensation paid for other activities for each director:

Name of Director	Days Served		Committee Assignments	Comp. Paid for other Activities
	Regular Board Meetings	Other Official Activities		
Walter S. Farr, <i>Chairman</i>	12	16	Audit, Primary Representative of the AgFirst Nominating Committee	\$7,100
John R. Alexander, <i>Vice Chairman</i>	11	8	Chairman-Compensation, Alternate Representative of the AgFirst Nominating Committee	2,700
Howard P. Bateman	12	10	Audit, Political Communication Advocate (CAP) District Advisory Committee (DAC)	4,000
John Roy Gough	10	2	Compensation	800
Jerry M. Newlin	9	5	Compensation	2,000
John F. Smoak, Jr.	12	4	Compensation	1,600
J. Mark Wheeler	12	15	Chairman-Audit, AgFirst Farm Credit Council, AgFirst Employee Benefit Committee	4,950
E.E. "Bucky" Waldron	13	10	Audit	3,800
Lisa Sherman	1	0	Audit	0
William G. Welles III, <i>Retired Chairman</i>	2	0	Retired Chairman	0
				\$ 26,950

Directors are reimbursed on an actual cost basis for all expenses incurred in the performance of official duties. Such expenses may include transportation, lodging, meals, tips, tolls, parking of cars, laundry, registration fees, and other expenses associated with travel on official business. A copy of the policy is available to shareholders of the Association upon request.

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was \$59,051 for 2008, \$47,768 for 2007, and \$28,890 for 2006.

Transactions with Senior Officers and Directors

The reporting entity’s policies on loans to and transactions with its officers and directors, to be disclosed in this section are incorporated herein by reference to Note 11 of the Consolidated Financial Statements, “*Related Party Transactions*,” included in this Annual Report.

Transactions Other Than Loans

There have been no transactions that occurred at any time during the year ended December 31, 2008, between the Association and senior officers or directors, their immediate family members or any organizations with which they are affiliated, which require reporting per FCA regulations. There were no transactions with any senior officer or director related to the purchase or retirement of preferred stock of the Association, for the year ended December 31, 2008.

Involvement in Certain Legal Proceedings

There were no matters which came to the attention of management or the board of directors regarding involvement of current directors or senior officers in specified legal proceedings which should be disclosed in this section. No directors or senior officers have been involved in any legal proceedings during the last five years which require reporting per FCA regulations.

Relationship with Independent Auditor

There were no changes in or material disagreements with our independent auditor on any matter of accounting principles or financial statement disclosure during this period.

Aggregate fees incurred by the Association for services rendered by its independent auditor for the year ended December 31, 2008 were as follows:

	<u>2008</u>
Independent Auditor	
PricewaterhouseCoopers LLP	
Audit services	\$ 52,162
Nonaudit services	-
Total	<u>\$ 52,162</u>

Audit fees were for the annual audit of the Consolidated Financial Statements. There were no nonaudit services provided by the Association’s independent auditor during 2008.

Consolidated Financial Statements

The Consolidated Financial Statements, together with the report thereon of PricewaterhouseCoopers LLP dated February 27, 2009 and the Report of Management, which appear in this Annual Report to shareholders are incorporated herein by reference.

Copies of the Association’s Annual and Quarterly Reports are available upon request, free of charge, by calling 863-494-0500, or writing Farm Credit of Southwest Florida, ACA, Attention: **Jeremy Christian, Controller**, 330 N. Brevard Avenue, Arcadia, Florida 34266. The Reports can also be obtained by going to the Association’s web site at www.farmcreditswfl.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 Reports 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.

Borrower Information Regulations

Since 1972, Farm Credit Administration (FCA) regulations have required that borrower information be held in strict confidence by Farm Credit System (FCS) institutions, their directors, officers and employees. These regulations provide Farm Credit institutions clear guidelines for protecting their borrowers’ nonpublic personal information.

On November 10, 1999, the FCA Board adopted a policy that requires FCS institutions to formally inform new borrowers at loan closing of the FCA regulations on releasing borrower information and to address this information in the Annual Report. The implementation of these measures ensures that new and existing borrowers are aware of the privacy protections afforded them through FCA regulations and Farm Credit System institution efforts.

Credit and Services to Young, Beginning, and Small Farmers and Ranchers and Producers or Harvesters of Aquatic Products

Information to be disclosed in this section is incorporated herein by reference to the similarly named section in the Management’s Discussion & Analysis of Financial Condition & Results of operations section included in this Annual Report to the shareholders.

Shareholder Investment

Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank (Bank or AgFirst). Copies of the Bank's Annual and Quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 378, or writing Stephen Gilbert, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained by going to AgFirst's web site at www.agfirst.com. The Bank prepares an electronic version of the Annual Report, which is available on the Bank's website, within 75 days after the end of the fiscal year and distributes the Annual Reports to shareholders within 90 days after the end of the fiscal year. The Bank prepares an electronic version of the Quarterly Report, which is available on the Bank's website, within 40 days after the end of each fiscal quarter, except that no report needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Bank.

Report of the Audit Committee

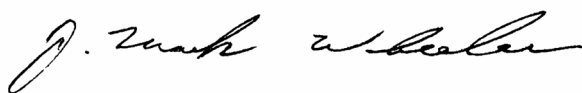
The Audit Committee of the Board of Directors (Committee) is comprised of the directors named below. None of the directors who serve on the Committee is an employee of Farm Credit of Southwest Florida, ACA (Association) and in the opinion of the Board of Directors; each is free of any relationship with the Association or management that would interfere with the director's independent judgment on the Committee.

The Committee has adopted a written charter that has been approved by the Board of Directors. The Committee has reviewed and discussed the Association's audited financial statements with management, which has primary responsibility for the financial statements.

PricewaterhouseCoopers LLP (PwC), the Association's independent auditor for 2008, is responsible for expressing an opinion on the conformity of the Association's audited financial statements with accounting principles generally accepted in the United States of America. The Committee has discussed with PwC the matters that are required to be discussed by Statement on Auditing Standards No. 114 (*The Auditor's Communication With Those Charged With Governance*). PwC has provided to the Committee the written disclosures and the letter required by Independence Standards Board Standard No. 1 (*Independence Discussions with Audit Committees*), and the Committee has discussed with PwC that firm's independence.

The Committee has also concluded that PwC's provision of non-audit services, if any, to the Association is compatible with PwC's independence.

Based on the considerations referred to above, the Committee recommended to the Board of Directors that the audited financial statements be included in the Association's Annual Report for 2008. The foregoing report is provided by the following independent directors, who constitute the Committee:



J. Mark Wheeler
Chairman of the Audit Committee

Members of Audit Committee

Howard P. Bateman
Walter S. Farr
Lisa Sherman
E.E. (Bucky) Waldron

February 27, 2009

Report of Independent Auditors



PricewaterhouseCoopers LLP
10 Tenth Street, Suite 1400
Atlanta, GA 30309
Telephone (678) 419 1000

Report of Independent Auditors

To the Board of Directors and Members
of Farm Credit of Southwest Florida, ACA

In our opinion, the accompanying Consolidated Balance Sheets and the related Consolidated Statements of Income, of Changes in Members' Equity and of Cash Flows present fairly, in all material respects, the financial position of Farm Credit of Southwest Florida, ACA (the Association) and its subsidiaries at December 31, 2008, 2007 and 2006, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

February 27, 2009

Consolidated Balance Sheets

<i>(dollars in thousands)</i>	December 31, 2008	December 31, 2007	December 31, 2006
Assets			
Cash	\$ —	\$ 64	\$ —
Investment securities:			
Held to maturity (fair value of \$37,221 \$36,599 and \$31,977 respectively)	38,517	36,958	32,202
Total investment securities	38,517	36,958	32,202
Loans	198,532	258,245	219,599
Less: allowance for loan losses	4,293	232	187
Net loans	194,239	258,013	219,412
Accrued interest receivable	1,715	2,617	3,191
Investments in other Farm Credit institutions	17,174	11,166	12,209
Premises and equipment, net	1,070	1,072	984
Other property owned, net	178	—	—
Due from AgFirst Farm Credit Bank	5,521	5,247	3,641
Other assets	4,853	4,768	4,234
Total assets	\$ 263,267	\$ 319,905	\$ 275,873
Liabilities			
Notes payable to AgFirst Farm Credit Bank	\$ 211,647	\$ 260,052	\$ 217,032
Accrued interest payable	731	1,274	1,117
Patronage refund payable	737	2,646	2,516
Other liabilities	2,814	4,364	3,449
Total liabilities	215,929	268,336	224,114
Commitments and contingencies			
Members' Equity			
Protected borrower stock	329	356	508
Capital stock and participation certificates	553	581	601
Retained earnings			
Allocated	22,637	26,030	25,779
Unallocated	23,984	24,827	24,871
Accumulated other comprehensive income (loss)	(165)	(225)	—
Total members' equity	47,338	51,569	51,759
Total liabilities and members' equity	\$ 263,267	\$ 319,905	\$ 275,873

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

Consolidated Statements of Income

<i>(dollars in thousands)</i>	For the year ended December 31,		
	2008	2007	2006
Interest Income			
Investment securities	\$ 1,512	\$ 1,770	\$ 959
Loans	10,872	18,349	20,749
Total interest income	12,384	20,119	21,708
Interest Expense			
Notes payable to AgFirst Farm Credit Bank	7,989	13,803	14,092
Net interest income	4,395	6,316	7,616
Provision for (reversal of allowance for) loan losses	4,183	26	(10)
Net interest income after provision for (reversal of allowance for) loan losses	212	6,290	7,626
Noninterest Income			
Loan fees	702	612	680
Fees for financially related services	112	—	—
Patronage refund from other Farm Credit institutions	7,008	8,434	5,663
Gains (losses) on other property owned, net	4	6	6
Other noninterest income	—	243	186
Total noninterest income	7,826	9,295	6,535
Noninterest Expense			
Salaries and employee benefits	3,660	3,930	3,651
Occupancy and equipment	398	418	392
Insurance Fund premiums	268	340	373
Other operating expenses	1,595	1,731	1,460
Total noninterest expense	5,921	6,419	5,876
Income before income taxes	2,117	9,166	8,285
Provision (benefit) for income taxes	1	(76)	64
Net income	\$ 2,116	\$ 9,242	\$ 8,221

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

Consolidated Statements of Changes in Members' Equity

<i>(dollars in thousands)</i>	Protected Borrower Stock	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2005	\$ 622	\$ 656	\$25,257	\$ 25,231	\$ —	\$ 51,766
Net income				8,221		8,221
Protected borrower stock retired	(114)					(114)
Capital stock/participation certificates issued/(retired), net		(55)				(55)
Patronage distribution						
Cash				(2,512)		(2,512)
Nonqualified allocated retained earnings			4,665	(4,665)		—
Retained earnings retired			(4,995)			(4,995)
Patronage distribution adjustment			852	(1,404)		(552)
Balance at December 31, 2006	508	601	25,779	24,871	—	51,759
Net income				9,242		9,242
Protected borrower stock retired	(152)					(152)
Capital stock/participation certificates issued/(retired), net		(20)				(20)
Patronage distribution						
Cash				(2,996)		(2,996)
Qualified allocated retained earnings			261	(261)		—
Nonqualified allocated retained earnings			6,049	(6,049)		—
Retained earnings retired			(5,300)			(5,300)
Patronage distribution adjustment			(759)	20		(739)
Adjustment to initially apply FAS No. 158 (Note 10)					(225)	(225)
Balance at December 31, 2007	356	581	26,030	24,827	(225)	51,569
Net income				2,116		2,116
Protected borrower stock retired	(27)					(27)
Capital stock/participation certificates issued/(retired), net		(28)				(28)
Patronage distribution						
Cash				(700)		(700)
Nonqualified allocated retained earnings			1,300	(1,300)		—
Retained earnings retired			(5,513)			(5,513)
Patronage distribution adjustment			820	(939)		(119)
Employee benefit plan adjustments (Note 10)				(20)	60	40
Balance at December 31, 2008	\$ 329	\$ 553	\$22,637	\$ 23,984	\$ (165)	\$ 47,338

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

Consolidated Statements of Cash Flows

<i>(dollars in thousands)</i>	For the year ended December 31,		
	2008	2007	2006
Cash flows from operating activities:			
Net income	\$ 2,116	\$ 9,242	\$ 8,221
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	166	173	160
Amortization of net deferred loan origination (fees) costs	(490)	(283)	(495)
Amortization of premiums on purchased loans			
Premium amortization/discount accretion on investments	607	—	—
Provision for (reversal of allowance for) loan losses	4,183	26	(10)
(Gains) losses on other property owned, net	(4)	(6)	(6)
(Increase) decrease in accrued interest receivable	902	574	(1,697)
(Increase) decrease in due from AgFirst Farm Credit Bank	(274)	(1,606)	(462)
(Increase) decrease in other assets	(85)	(534)	(685)
Increase (decrease) in accrued interest payable	(543)	157	79
Increase (decrease) in other liabilities	(1,506)	696	543
Total adjustments	2,956	(803)	(2,573)
Net cash provided by (used in) operating activities	5,072	8,439	5,648
Cash flows from investing activities:			
Purchases of investment securities, held to maturity	(11,602)	(13,795)	(35,411)
Proceeds from maturities of or principal payments received on investment securities, held to maturity	9,436	9,039	3,209
Net (increase) decrease in loans	59,903	(38,344)	57,528
(Increase) decrease in investment in other Farm Credit institutions	(6,008)	1,043	(7,571)
Purchases of premises and equipment	(164)	(261)	(206)
Net cash provided by (used in) investing activities	51,565	(42,318)	17,549
Cash flows from financing activities:			
Advances on (repayment of) notes payable to AgFirst Farm Credit Bank, net	(48,405)	43,020	(16,227)
Protected borrower stock retired	(27)	(152)	(114)
Capital stock and participation certificates issued/(retired), net	(28)	(20)	(55)
Patronage refunds and dividends paid	(2,728)	(3,605)	(2,272)
Retained earnings retired	(5,513)	(5,300)	(4,995)
Net cash provided by (used in) financing activities	(56,701)	33,943	(23,663)
Net increase (decrease) in cash	(64)	64	(466)
Cash, beginning of period	64	—	466
Cash, end of period	\$ —	\$ 64	\$ —
Supplemental schedule of non-cash activities:			
Loans transferred to other property owned	\$ 178	\$ —	\$ —
Cash dividends or patronage distributions declared or payable	700	2,996	2,512
Increase in liability resulting from adoption of FAS 158 (Note 10)	—	225	—
Employee benefit plan adjustments (Note 10)	(40)	—	—
Supplemental information:			
Interest paid	\$ 8,532	\$ 13,646	\$ 14,013
Taxes (refunded) paid, net	36	(35)	(12)

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)

Note 1 — Organization and Operations

A. **Organization:** Farm Credit of Southwest Florida, ACA (Association) is a member-owned cooperative which provides credit and credit-related services to or for the benefit of eligible borrowers/shareholders for qualified purposes in the counties of Charlotte, Collier, DeSoto, Glades, Hardee, Hendry, Highlands, Lee, Manatee, and Sarasota in the state of Florida.

The Association is a lending institution of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations, which was established by Acts of Congress to meet the credit needs of American agriculture and is subject to the provisions of the Farm Credit Act of 1971, as amended (Farm Credit Act). The most recent significant amendment to the Farm Credit Act was the Agricultural Credit Act of 1987. At December 31, 2008, the System was comprised of four Farm Credit Banks, one Agricultural Credit Bank and ninety associations.

AgFirst Farm Credit Bank (Bank) and its related associations are collectively referred to as the "District." The Bank provides funding to associations within the District and is responsible for supervising certain activities of the Association, as well as the other associations operating within the District. The District consists of the Bank and twenty-two Agricultural Credit Associations (ACAs), all of which are structured as ACA parent-companies, which have two wholly owned subsidiaries, a Federal Land Credit Association (FLCA) and a Production Credit Association (PCA). FLCAs are tax-exempt while ACAs and PCAs are taxable.

ACA parent-companies provide financing and related services through its FLCA and PCA subsidiaries. The FLCA makes collateralized long-term agricultural real estate and rural home mortgage loans. The ACA makes short- and intermediate-term loans for agricultural production or operating purposes.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the System banks and associations. The FCA examines the activities of the associations and certain actions by the associations are subject to the prior approval of the FCA and the supervising bank.

The Farm Credit Act established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is required to be used (1) to ensure the timely payment of principal and interest on Systemwide debt obligations (Insured debt), (2) to ensure the retirement of protected borrower capital at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for discretionary uses by the Insurance Corporation to provide assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System bank has been required to pay premiums, which may be passed on to the Association, into the Insurance Fund, based on its annual average loan principal outstanding until the monies in the Insurance Fund reach the

"secure base amount." The secure base amount is defined in the Farm Credit Act as 2.0 percent of the aggregate insured obligations (Systemwide debt obligations) or such other percentage of the aggregate obligations as the Insurance Corporation in its sole discretion determines to be actuarially sound. When the amount in the Insurance Fund exceeds the secure base amount, the Insurance Corporation is required to reduce premiums, but it still must ensure that reduced premiums are sufficient to maintain the level of the Insurance Fund at the secure base amount. In June 2008, with the passage of the Food, Conservation, and Energy Act of 2008 (Farm Bill), the basis for assessing premiums was changed, beginning with the second half of 2008, to reflect each association's pro rata share of outstanding insured debt. The Farm Bill imposes premiums of up to 20 basis points on adjusted insured debt obligations, with the Insurance Corporation Board having the ability to reduce the amount, and a risk surcharge of 10 basis points on nonaccrual loans and other-than-temporarily impaired investments. Premiums for the third and fourth quarters of 2008 were 15 and 18 basis points, respectively.

B. **Operations:** The Farm Credit Act sets forth the types of authorized lending activity, persons eligible to borrow, and financial services which can be offered by the Association. The Association is authorized to provide, either directly or in participation with other lenders, credit, credit commitments and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents, and farm-related businesses.

The Association may sell to any System borrowing member, on an optional basis, credit or term life insurance appropriate to protect the loan commitment in the event of death of the debtor(s). The sale of other insurance necessary to protect a member's farm or aquatic unit is permitted, but limited to hail and multi-peril crop insurance, and insurance necessary to protect the facilities and equipment of aquatic borrowers.

Note 2 — Summary of Significant Accounting Policies

The accounting and reporting policies of the Association conform with accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. Significant estimates are discussed in these footnotes, as applicable. Actual results may differ from these estimates.

Certain amounts in prior years' financial statements may have been reclassified to conform to the current year's presentation. Such reclassifications had no effect on net income or total members' equity of prior years. The Consolidated Financial Statements include the accounts of the FLCA and the PCA. All significant inter-company transactions have been eliminated in consolidation.

- A. **Cash:** Cash, as included in the statements of cash flows, represents cash on hand and on deposit at banks.
- B. **Investment Securities:** The Association, as permitted under the FCA regulations, holds investments for purposes of maintaining a liquidity reserve, managing short-term surplus funds and managing interest rate risk. The Association's investments are classified as held-to-maturity and accordingly have been reported at amortized cost. Purchase premiums and discounts are amortized or accreted ratably over the term of the respective security which approximates effective interest method.

The Association may also hold additional investments in accordance with mission-related investment and other investment programs, approved by the Farm Credit Administration. These programs allow the Association to make investments that further the System's mission to serve rural America. Mortgage-backed securities issued by Farmer Mac are considered other investments. Mission-related investments for which the Association has the intent and ability to hold to maturity are classified as held-to-maturity and carried at cost, adjusted for the amortization of premiums and accretion of discounts. Farmer Mac investments are classified either as held-to-maturity or available-for-sale depending on the institution's ability and intent to hold the investment to maturity. The ACA does not hold any Farmer Mac Investment Securities.

The Association reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered impairment, is temporary or other-than-temporary. In the event of other-than-temporary impairment, the cost basis of the investment would be written down to its fair value, and the realized impairment loss would be included in earnings in the period of impairment.

- C. **Loans and Allowance for Loan Losses:** Long-term real estate mortgage loans generally have original maturities ranging from 5 to 40 years. Substantially all short- and intermediate-term loans for agricultural production or operating purposes have maturities of 10 years or less. Loans are carried at their principal amount outstanding adjusted for charge-offs and deferred loan fees or costs.

Loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately collateralized and in the process of collection) or circumstances indicate that collection of principal and/or interest is in doubt. When a loan is placed in nonaccrual status, accrued interest deemed uncollectible is reversed (if accrued in the current year) or charged against the allowance for loan losses (if accrued in the prior year).

When loans are in nonaccrual status, the interest portion of payments received in cash is recognized as interest income if collection of the recorded investment in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it. Otherwise, loan payments are applied against the recorded investment in the loan. Nonaccrual loans may be returned to accrual status when principal and interest are current, prior charge-offs have been recovered, the ability of the borrower to fulfill the contractual repayment terms is fully expected and the loan is not classified "doubtful" or "loss."

Loans are charged-off, wholly or partially, as appropriate, at the time they are determined to be uncollectible.

In cases where a borrower experiences financial difficulties and the Association makes certain monetary concessions to the borrower through modifications to the contractual terms of the

loan, the loan is classified as a restructured loan. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

Loan origination fees and direct loan origination costs are deferred as part of the carrying amount of the loan and the net fee or cost is amortized over the life of the related loan as an adjustment to interest income using the effective interest method.

The allowance for loan losses is a valuation account used to reasonably estimate loan and lease losses existing as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss.

The allowance for loan losses is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition and prior loan loss experience. It is based on estimates, appraisals and evaluations of loans which, by their nature, contain elements of uncertainty and imprecision. The possibility exists that changes in the economy and its impact on borrower repayment capacity will cause these estimates, appraisals and evaluations to change.

The level of allowance for loan losses is generally based on recent charge-off experience adjusted for relevant environmental factors. The Association considers the following factors when adjusting the historical charge-offs experience:

- Changes in credit risk classifications,
- Changes in collateral values,
- Changes in risk concentrations,
- Changes in weather related conditions, and
- Changes in economic conditions.

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms of the loan. Impaired loans include nonaccrual loans, restructured loans, and loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is formally restructured or until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full.

A specific allowance may be established for impaired loans under Statement of Financial Accounting Standards No. 114. Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as practically expedient, at the loan's observable market price or fair value of the collateral if the loan is collateral dependent.

The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through allowance for loan losses reversals and loan charge-offs.

- D. **Investment in AgFirst Farm Credit Bank and Other Farm Credit Institutions:** The Association is required to maintain ownership in the Bank in the form of Class C stock. Accounting for this investment is on the cost plus allocated equities basis.

Patronage refunds from the Bank are accrued as earned. The receivable for such patronage refunds is classified as due from AgFirst Farm Credit Bank.

- E. **Other Property Owned:** Other property owned, consisting of real and personal property acquired through a collection action, is recorded upon acquisition at fair value less estimated selling costs. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income, expenses, and carrying value adjustments related to other property owned are included in gains (losses) on other property owned, net.
- F. **Premises and Equipment:** Premises and equipment are carried at cost less accumulated depreciation. Land is carried at cost. Depreciation is provided on the straight-line method over the estimated useful lives of the assets. Gains and losses on dispositions are reflected in current earnings. Maintenance and repairs are charged to expense and improvements are capitalized.
- G. **Advanced Conditional Payments:** The Association is authorized under the Farm Credit Act to accept advance payments from borrowers. To the extent the borrower's access to such advance payments is restricted, the advanced conditional payments are netted against the borrower's related loan balance. Amounts in excess of the related loan balance and amounts to which the borrower has unrestricted access are presented as interest-bearing liabilities in the accompanying Consolidated Balance Sheets. Advanced conditional payments are not insured. Interest is generally paid by the Association on such accounts.
- H. **Employee Benefit Plans:** Substantially all employees of the Association may participate in the AgFirst Farm Credit Retirement Plan (Plan), which is a defined benefit plan and is considered a multi-employer plan. The Plan is noncontributory and includes eligible District employees. The "Projected Unit Credit" actuarial method is used for financial reporting purposes. The cost of the Plan is allocated based on a percentage of each institution's salary expense to the total salary expense for all Plan participants.

Substantially all employees of the Association may also be eligible to participate in a defined contribution Districtwide 401(k) plan, which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Association contributes \$.50 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. For employees hired on or after January 1, 2003, the Association contributes \$1.00 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as adjusted by the Internal Revenue Service. 401(k) plan costs are expensed as funded.

The Association may provide certain health care and life insurance benefits to eligible retired employees. Substantially all employees may become eligible for these benefits if they reach early retirement age while working for the Association.

- I. **Income Taxes:** The Association is generally subject to Federal and certain other income taxes. As previously described, the ACA holding company has two wholly-owned subsidiaries, a PCA and a FLCA. The FLCA subsidiary is exempt from federal and state income taxes as provided in the Farm Credit Act. The ACA holding company and the PCA subsidiary are subject to federal, state and certain other income taxes.

The Association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage refunds. The Association distributes patronage on the basis of book income.

The Association accounts for income taxes under the asset and liability method, recognizing deferred tax assets and liabilities for the expected future tax consequences of the temporary differences between the carrying amounts and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled.

The Association records a valuation allowance at the balance sheet dates against that portion of the Association's deferred tax assets that, based on management's best estimates of future events and circumstances, more likely than not (a likelihood of more than 50 percent) will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of our expected patronage program, which reduces taxable earnings.

- J. **Patronage Refund from AgFirst and Other Financial Institutions:** The Association records patronage refunds from the Bank and certain District Associations on an accrual basis.
- K. **Fair Value Measurement:** Effective January 1, 2008, the Association adopted Statement of Financial Accounting Standards No. 157, "Fair Value Measurement." (SFAS No. 157). This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS No. 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability. SFAS No. 157 establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. It describes three levels of inputs that may be used to measure fair value:

Level 1 — Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 — Observable inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly. Level 2 inputs include the following: (a) quoted prices for similar assets or liabilities in active markets; (b) quoted prices for identical or similar assets or liabilities in markets that are not active so that they are traded less frequently than exchange-traded instruments, the prices are not current or principal market information is not released publicly; (c) inputs other than quoted prices that are observable such as interest rates and yield curves, prepayment speeds, credit risks and default rates and (d) inputs derived principally from or corroborated by observable market data by correlation or other means.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. These unobservable inputs reflect the reporting entity's own assumptions about assumptions that market participants would use in pricing the asset or liability. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

See Note 13 for disclosures required by SFAS No. 157.

- L. **Recently Issued Accounting Pronouncements:** In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS No. 158). SFAS No. 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in that funded status in the year in which the changes occur through other comprehensive income. SFAS No. 158 further requires the determination of the fair value of plan assets at year-end and recognition of actuarial gains and losses, prior service costs or credits, and transition assets and obligations as a component of other comprehensive income. In addition, SFAS No. 158 requires that the funded status of a plan be measured as of the date of the year-end financial statements, effective for fiscal years ending after December 15, 2008. Prior to 2008, the District used a measurement date of September 30th. In 2008, the District used a measurement date of December 31st as required. See Note 10 for the impact of SFAS No. 158 on the current period.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141R, "Business Combinations" (SFAS No. 141R). SFAS No. 141R requires business combinations to be accounted for under the acquisition method of accounting (previously called the purchase method). The acquisition method requires (a) identifying the acquirer, (b) determining the acquisition date, (c) recognizing and measuring the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, at their acquisition date fair values, and (d) recognizing and measuring goodwill or a gain from a bargain purchase. SFAS No. 141R will be applied to business combinations on or after January 1, 2009. The Association is still evaluating the provisions of SFAS No. 141R, but believes that its adoption will significantly impact its accounting for combinations/acquisitions that may occur in 2009 and beyond.

Note 3 — Investment Securities

A summary of the amortized cost and fair value of investment securities held-to-maturity at December 31, 2008, 2007 and 2006 follows:

	December 31, 2008				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Asset backed securities	\$ 35,128	\$ -	\$ (1,017)	\$ 34,111	2.55%
Other	\$ 3,389	\$ 44	\$ (323)	\$ 3,110	6.37%

	December 31, 2007				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Asset backed securities	\$ 35,958	\$ 3	\$ (378)	\$ 35,583	5.47%
Other	\$ 1,000	\$ 16	\$ -	\$ 1,016	7.75%

	December 31, 2006				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
Asset backed securities	\$ 32,202	\$ 10	\$ (235)	\$ 31,977	5.83%

The Association's investments consist primarily of asset-backed securities (ABSs). These ABSs are rated AAA, as they are guaranteed by the full faith and credit of the United States government. Unrealized losses at December 31, 2008 are primarily due to reduced liquidity in the securities markets stemming from general adversity in the financial markets and are not credit related.

The following table shows the fair value and gross unrealized losses for investments in a loss position by the length of time the securities have been in a continuous unrealized loss position at December 31, 2008. The continuous loss position is based on the date the impairment occurred. The Association performs periodic credit reviews, including other-than-temporary impairment analysis, on its investment securities portfolio. The objective is to quantify any future possible loss of principal or interest due on each security identified for additional analysis. Based on the results of all analyses, the Association has not recognized any other-than-temporary impairment in connection with these investments. The unrealized losses on these investments resulted primarily from reduced liquidity in the securities markets stemming from general adversity in the financial markets. The Association has the ability and intent to hold these investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities, especially after considering credit enhancements. All securities continue to perform. Substantially all of these investments were in U. S. government securities and the Association expects that these securities would not be settled at a price less than their amortized cost.

	Less than 12 Months		Greater than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Asset-backed securities	\$ 12,602	\$ (262)	\$ 21,510	\$ (754)
Other	\$ 1,934	\$ (323)	\$ -	\$ -

A summary of the expected maturity, amortized cost and estimated fair value of investment securities at December 31, 2008 follows:

	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	\$ -	\$ -	- %
After one year through five years	1,671	1,617	1.62
After five years through ten years	24,902	24,202	2.75
After ten years	11,944	11,402	3.35
Total	\$ 38,517	\$ 37,221	2.89%

Note 4 — Loans and Allowance for Loan Losses

A summary of loans follows:

	December 31,		
	2008	2007	2006
Real estate mortgage	\$ 99,142	\$ 139,256	\$ 121,681
Production and intermediate term	44,271	78,800	67,278
Loans to cooperatives	1,678	-	18,011
Processing and marketing	36,378	24,632	8,515
Farm related business	12,222	12,044	-
Communication	1,144	-	2,251
Energy	1,840	1,827	-
Water and waste disposal	-	-	1,863
Rural residential real estate	1,857	1,686	-
Total loans	\$ 198,532	\$ 258,245	\$ 219,599

A substantial portion of the Association's lending activities is collateralized and the Association's exposure to credit loss associated with lending activities is reduced accordingly. An estimate of the Association's credit risk exposure is considered in the determination of the allowance for loan losses.

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Long-term real estate loans are collateralized by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in the loan to value ratios in excess of the regulatory maximum.

The following table presents information relating to impaired loans as defined in Note 2.

	December 31,		
	2008	2007	2006
Impaired nonaccrual loans:			
Current as to principal and interest	\$ 8,686	\$ -	\$ -
Past due	5,751	995	-
Total impaired nonaccrual loans	14,437	995	-
Impaired accrual loans:			
Restructured accrual loans	-	-	-
Accrual loans 90 days or more past due	-	-	613
Total impaired accrual loans	-	-	613
Total impaired loans	\$ 14,437	\$ 995	\$ 613

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at December 31, 2008.

Interest income is recognized and cash payments are applied on nonaccrual impaired loans as described in Note 2. The following table presents interest income recognized on impaired loans.

	Year Ended December 31,		
	2008	2007	2006
Interest income recognized on impaired nonaccrual loans	\$ 36	\$ 86	\$ -
Interest income on impaired accrual loans	-	4	4
Interest income recognized on impaired loans	\$ 36	\$ 90	\$ 4

The following table presents information concerning impaired loans as of December 31,

	2008	2007	2006
Impaired loans with related allowance	\$ 11,329	\$ 914	\$ -
Impaired loans with no related allowance	3,108	81	613
Total impaired loans	\$ 14,437	\$ 995	\$ 613
Allowance on impaired loans	\$ 3,659	\$ 163	\$ -

The following table summarizes impaired loan information for the year ended December 31,

	2008	2007	2006
Average impaired loans	\$ 6,534	\$ 1,495	\$ 43

The following table summarizes interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans:

	Year Ended December 31,		
	2008	2007	2006
Interest income which would have been recognized under the original loan terms	\$ 511	\$ 151	\$ 2
Less: interest income recognized	-	86	-
Foregone interest income	\$ 511	\$ 65	\$ 2

The changes in the allowance for loan losses are as follows:

	Year Ended December 31,		
	2008	2007	2006
Balance at beginning of year	\$ 232	\$ 187	\$ 183
Charge-offs:			
Production and intermediate term	(25)	—	—
Real estate mortgage	(94)	—	—
Rural residential real estate	(19)	—	—
Total charge-offs	(138)	—	—
Recoveries:			
Real estate mortgage	16	17	14
Production and intermediate term	—	2	—
Total recoveries	16	19	14
Net (charge-offs) recoveries	(122)	19	14
Provision for (reversal of allowance for) loan losses	4,183	26	(10)
Balance at end of year	\$ 4,293	\$ 232	\$ 187
Ratio of net (charge-offs) recoveries during the period to average loans outstanding during the period	(0.067)%	0.01%	0.01%

In addition, the following is a breakdown of the allowance for loan losses for the end of the last three fiscal years:

	December 31, 2008		December 31, 2007	
	Amount	%	Amount	%
Real estate mortgage	\$ 2,958	69%	\$ 197	85%
Production and intermediate term	327	7	20	9
Agribusiness	972	23	15	6
Rural residential real estate	36	1	—	—
Total	\$ 4,293	100%	\$ 232	100%

	December 31, 2006	
	Amount	%
Real estate mortgage	\$ 170	91%
Production and intermediate term	16	9
Agribusiness	—	—
Rural residential real estate	1	—
Total	\$ 187	100%

To mitigate the risk of loan losses, the Association may enter into long-term standby “commitment to purchase” agreements with the Federal Agricultural Mortgage Corporation (Farmer Mac). The agreements, which are effectively credit guarantees that will remain in place until the loans are paid in full, give the Association the right to sell the loans identified in the agreements to Farmer Mac in the event of default (typically four months past due), subject to certain conditions. The balance of loans under long-term standby commitments was \$4,609, \$6,695 and \$8,163 at December 31, 2008, 2007 and 2006, respectively. Fees paid to Farmer Mac for such commitments totaled \$28, \$39 and \$62 for the years ended December 31, 2008, 2007 and 2006, respectively. These amounts are classified as noninterest expense.

Note 5 — Investment in AgFirst Farm Credit Bank

The Association is required to maintain ownership in the Bank of Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements.

Note 6 — Premises and Equipment

Premises and equipment consists of the following:

	December 31,		
	2008	2007	2006
Land	\$ 167	\$ 164	\$ 163
Buildings and improvements	1,054	1,027	910
Furniture and equipment	870	877	809
	2,091	2,068	1,882
Less: accumulated depreciation	1,021	996	898
Total	\$ 1,070	\$ 1,072	\$ 984

Note 7 — Notes Payable to AgFirst Farm Credit Bank

The Association’s indebtedness to the Bank represents borrowings by the Association to fund its loan portfolio. This indebtedness is collateralized by a pledge of substantially all of the Association’s assets and the terms of the revolving lines of credit are governed by a general financing agreement. Interest rates on both variable and fixed rate notes payable are generally established loan-by-loan based on the Bank’s marginal cost of funds, capital position, operating costs and return objectives. The interest rate is periodically adjusted by the Bank based upon agreement between the Bank and the Association. The weighted average interest rates on the variable rate notes were 3.34 percent for LIBOR-based loans, 2.30 percent for Prime-based loans, and the weighted average remaining maturities were 2.2 years and 3.5 years, respectively, at December 31, 2008. The weighted average interest rate on the fixed rate and adjustable rate mortgage (ARM) notes payable which are match funded by the Bank was 3.67 percent and the weighted average remaining maturity was 5.3 years at December 31, 2008. The weighted average interest rate on all interest-bearing notes payable was 3.21 percent and the weighted average remaining maturity was 4.4 years at December 31, 2008.

Variable rate and fixed rate notes payable represent approximately 51.31 percent and 48.69 percent, respectively, of total notes payable at December 31, 2008.

Under the Farm Credit Act, the Association is obligated to borrow only from the Bank, unless the Bank approves borrowing from other funding sources. The Bank, consistent with FCA regulations, has established limitations on the Association’s ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2008, the Association’s notes payable were within the specified limitations.

Note 8 — Members’ Equity

A description of the Association’s capitalization requirements, protection mechanisms, regulatory capitalization requirements and restrictions, and equities are provided below.

A. Protected Borrower Stock

Protection of certain borrower stock is provided under the Farm Credit Act, which requires the Association, when retiring protected borrower stock, to retire such stock at par or stated value regardless of its book value. Protected borrower stock includes capital stock and participation certificates, which were outstanding as of January 6, 1988, or were issued or allocated prior to October 6, 1988. If an Association is unable to retire protected borrower stock at par value or stated value, amounts required to retire this equity would be obtained from the Insurance Fund.

B. Capital Stock and Participation Certificates

In accordance with the Farm Credit Act and the Association’s capitalization bylaws, each borrower is required to invest in Class C common stock for agricultural loans, or participation certificates in the case of rural home and farm related business loans, as a condition of borrowing. The initial borrower investment, through either purchase or transfer, must be in an amount equal to the lesser of \$1 thousand or two percent of the loan. The Board of Directors may increase the amount of investment if necessary to meet the Association’s capital needs. Loans designated for sale or sold into the Secondary Market on or after April 16, 1996 will have no voting stock or participation certificate purchase requirement if sold within 180 days following the date of designation.

The borrower acquires ownership of the capital stock or participation certificates at the time the loan is made, but usually does not make a cash investment. The aggregate par value is generally added to the principal amount of the related loan obligation. The Association retains a first lien on the stock or participation certificates owned by borrowers. Retirement of such equities will generally be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock or participation certificates.

C. Regulatory Capitalization Requirements and Restrictions

The FCA’s capital adequacy regulations require the Association to achieve permanent capital of 7.00 percent of risk-adjusted assets and off-balance-sheet commitments. Failure to meet the 7.00 percent capital requirement can initiate certain mandatory and possibly additional discretionary actions by the FCA that, if undertaken, could have a direct material effect on the Association’s financial statements. The Association is prohibited from reducing permanent capital by retiring stock or making certain other distributions to shareholders unless prescribed capital standards are met. The FCA regulations also require that additional minimum standards for capital be achieved. These standards require all System institutions to achieve and maintain ratios as defined by FCA regulations. These required ratios are total surplus as a percentage of risk-adjusted assets of 7.00 percent and of core surplus as a percentage of risk-adjusted assets of 3.50 percent. The Association’s permanent capital, total surplus and core surplus ratios at December 31, 2008 were 12.05 percent, 11.83 percent and 10.59 percent, respectively.

An FCA regulation empowers it to direct a transfer of funds or equities by one or more System institutions to another System institution under specified circumstances. The Association has not been called upon to initiate any transfers and is not aware of any proposed action under this regulation.

D. Description of Equities

The Association is authorized to issue or have outstanding Classes A and D Preferred Stock, Classes A, B and C Common Stock, Classes B and C Participation Certificates and such other classes of equity as may be provided for in amendments to the bylaws in such amounts as may be necessary to conduct the Association’s business. All stock and participation certificates have a par or face value of five dollars (\$5.00) per share.

The Association had the following shares outstanding at December 31, 2008:

Class	Protected	Shares Outstanding	
		Number	Aggregate Par Value
B Common/Nonvoting	Yes	65,200	\$ 326
C Common/Voting	No	101,800	509
B Participation Certificates/Nonvoting	Yes	600	3
C Participation Certificates/Nonvoting	No	8,800	44
Total Capital Stock and Participation Certificates		176,400	\$ 882

Protected common stock and participation certificates are retired at par or face value in the normal course of business. At-risk common stock and participation certificates are retired at the sole discretion of the Board at book value not to exceed par or face amounts, provided the minimum capital adequacy standards established by the Board are met.

Retained Earnings

The Association maintains an unallocated retained earnings account and an allocated retained earnings account. The minimum aggregate amount of these two accounts is determined by the Board. At the end of any fiscal year, if the retained earnings accounts otherwise would be less than the minimum amount determined by the Board as necessary to maintain adequate capital reserves to meet the commitments of the Association, the Association shall apply earnings for the year to the unallocated retained earnings account in such amounts as may be determined necessary by the Board. Unallocated retained earnings are maintained for each borrower to permit liquidation on a patronage basis.

The Association maintains an allocated retained earnings account consisting of earnings held and allocated to borrowers on a patronage basis. In the event of a net loss for any fiscal year, such allocated retained earnings account will be subject to full impairment in the order specified in the bylaws beginning with the most recent allocation.

The Association has a first lien and security interest on all retained earnings account allocations owned by any borrowers, and all distributions thereof, as additional collateral for their indebtedness to the Association. When the debt of a borrower is in default or is in the process of final liquidation by payment or otherwise, the Association, upon approval of the Board, may order any and all retained earnings account allocations owned by such borrower to be applied on the indebtedness.

Allocated equities shall be retired solely at the discretion of the Board; provided, however, that minimum capital standards established by the FCA and the Board are met.

At December 31, 2008, allocated members’ equity consisted of no qualified and \$22,637 of nonqualified distributions. Nonqualified distributions are tax deductible only when redeemed.

Dividends

The Association may declare noncumulative dividends on its capital stock and participation certificates provided the dividend rate does not exceed 20 percent of the par value of the respective capital stock and participation certificates. Such dividends may be paid solely on Classes A and D Preferred Stock or on all classes of stock and participation certificates.

The rate of dividends paid on Class A Preferred Stock for any fiscal year may not be less than the rate of dividend paid on Class A, B or C Common Stock or participation certificates for such year. The rate of dividends on Class A, B and C Common Stock and participation certificates shall be at the same rate per share.

Dividends may not be declared if, after recording the liability, the Association would not meet its capital adequacy standards. No dividends were declared by the Association for any of the periods included in these Consolidated Financial Statements.

Patronage Distributions

Prior to the beginning of any fiscal year, the Board, by adoption of a resolution, may obligate the Association to distribute to borrowers on a patronage basis all or any portion of available net earnings for such fiscal year or for that and subsequent fiscal years. Patronage distributions are based on the proportion of the borrower's interest to the amount of interest earned by the Association on its total loans unless another proportionate patronage basis is approved by the Board.

If the Association meets its capital adequacy standards after making the patronage distributions, the patronage distributions may be in cash, authorized stock of the Association, allocations of earnings retained in an allocated members' equity account, or any one or more of such forms of distribution. Patronage distributions of the Association's earnings may be paid on either a qualified or nonqualified basis, or a combination of both, as determined by the Board. A minimum of 20 percent of the total qualified patronage distribution to any borrower for any fiscal year shall always be paid in cash.

Transfer

Classes A and D Preferred, Classes A, B and C Common Stocks, and Classes B and C Participation Certificates may be transferred to persons or entities eligible to purchase or hold such equities.

Impairment

Any net losses recorded by the Association shall first be applied against unallocated members' equity. To the extent that such losses would exceed unallocated members' equity, such losses would be applied consistent with the Association's bylaws and distributed pro rata to each share and/or unit outstanding in the class, in the following order:

1. Allocated Surplus evidenced by nonqualified written notices of allocation.
2. Allocated Surplus evidenced by qualified written notices of allocation
3. Classes A, B and C Common Stock, Classes B and C Participation Certificates
4. Classes A and D Preferred Stock

Liquidation

In the event of liquidation or dissolution of the Association, any assets of the Association remaining after payment or retirement of all liabilities shall be distributed to the holders of the outstanding stock and participation certificates in the following order:

1. Classes A and D Preferred Stock
2. Classes A and B and C Common Stock and Class B and C Participation Certificates
3. Holders of allocated surplus evidenced by qualified written notices of allocation.
4. Holders of allocated surplus evidenced by non-qualified written notices of allocation.

5. All unallocated surplus issued after April 23, 1998 shall be distributed to Patrons of the Association from the period beginning April 23, 1998.
6. Any remaining assets of the Association after such distributions shall be distributed ratably to the holders of all classes of stock and participation certificates.

E. Accumulated Other Comprehensive Income (Loss)

The Association reports accumulated other comprehensive income (loss) (AOCI) in its Consolidated Statements of Changes in Members' Equity. The Association recognized AOCI of \$60 and \$(225) in 2008 and 2007, respectively, due to SFAS No. 158 (see Note 10 for further information).

Note 9 — Income Taxes

The provision (benefit) for income taxes follows:

	Year Ended December 31,		
	2008	2007	2006
Current:			
Federal	\$ 1	\$ (68)	\$ 46
State	—	1	18
	<u>1</u>	<u>(67)</u>	<u>64</u>
Deferred:			
Federal	—	(9)	—
State	—	—	—
	<u>—</u>	<u>(9)</u>	<u>—</u>
Total provision (benefit) for income taxes	<u>\$ 1</u>	<u>\$ (76)</u>	<u>\$ 64</u>

The provision (benefit) for income tax differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to pretax income as follows:

	December 31,		
	2008	2007	2006
Federal tax at statutory rate	\$ 720	\$ 3,116	\$ 2,817
State tax, net	—	7	12
Patronage distributions	(238)	(1,107)	(854)
Tax-exempt FLCA earnings	(461)	(2,118)	(2,029)
Change in deferred tax asset valuation allowance	(75)	75	—
Bank equity redemption	95	98	—
Other	(40)	(147)	118
Provision (benefit) for income taxes	<u>\$ 1</u>	<u>\$ (76)</u>	<u>\$ 64</u>

Deferred tax assets and liabilities are comprised of the following at:

	December 31,		
	2008	2007	2006
Deferred income tax assets:			
Allowance for loan losses	\$ 133	\$ 86	\$ 27
Loan origination fees	27	44	-
Annual leave	94	80	15
Nonaccrual loan interest	7	3	1
Postretirement health benefits	536	522	123
Deferred incentive	71	90	-
Other	38	-	38
Gross deferred tax assets	906	825	204
Less: valuation allowance	-	(75)	-
Gross deferred tax assets, net of valuation allowance	906	750	204
Deferred income tax liabilities:			
Loan origination fees	-	-	(10)
Defined pension benefits	(906)	(742)	(201)
Depreciation	-	(8)	(2)
Other	-	-	-
Gross deferred tax liability	(906)	(750)	(213)
Net deferred tax asset (liability)	\$ -	\$ -	\$ (9)

At December 31, 2008, deferred income taxes have not been provided by the Association on approximately \$1.3 million of patronage refunds received from the Bank prior to January 1, 1993. Such refunds, distributed in the form of stock, are subject to tax only upon conversion to cash. The tax liability related to future conversions is not expected to be material.

The Association recorded a valuation allowance of \$0, \$75 and \$0 during 2008, 2007 and 2006, respectively. The Association will continue to evaluate the realizability of these deferred tax assets and adjust the valuation allowance accordingly.

There were no uncertain tax positions identified related to the current year and the Association has no unrecognized tax benefits at December 31, 2008 for which liabilities have been established. The Association recognizes interest and penalties, if any, related to unrecognized tax benefits as a component of income tax expense. The tax years that remain open for federal and major state income tax jurisdictions are 2005 and forward.

Note 10 — Employee Benefit Plans

The employees of the Association may participate in a Districtwide defined benefit retirement plan. This plan is noncontributory and covers substantially all Association employees. Benefits are based on salary and years of service. As a participant in the District's defined benefit plan, the Association funded \$650 for 2008, and \$0 for 2007 and 2006, through its note payable to the Bank. Plan expenses included in salaries and employee benefits were \$295 for 2008, \$321 for 2007, and \$380 for 2006.

The District sponsors a plan providing certain benefits (primarily health care) to its retirees. Certain Association charges related to this plan are an allocation of District charges based on the Association's proportional share of the plan liability. Postretirement benefits other than pensions (primarily health care benefits) included in salaries and employee benefits were \$75 for 2008, \$74 for 2007, and \$78 for 2006.

Under SFAS No. 158, accounting for the standard follows the plan sponsor, which is at the District entity level for the Districtwide benefit plans in which the Association participates. Therefore, there is no impact to the Association's financial statements due to SFAS No. 158 for the two defined benefit plans discussed above. Additional financial information for the District sponsored plans, including the impact of SFAS No. 158, may be found in Notes to the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations' 2008 Annual Report.

In addition, supplemental retirement benefits are provided to certain key employees under a supplemental defined benefit executive plan. Assets have been allocated and separately invested for this plan but are not isolated from the general creditors of the Association.

The supplemental defined benefit executive plan is unfunded and had a projected benefit obligation of \$265 and a net under-funded status of \$265 at December 31, 2008. Net periodic pension cost for the period was \$80. The assumptions used to determine the projected benefit obligation included a discount rate of 6.30 percent.

SFAS No. 158 requires the recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. The balance sheet recognition provisions of SFAS No. 158 were adopted at December 31, 2007 by the Association for the single employer supplemental nonqualified plan, resulting in an adjustment of \$225 to accumulated other comprehensive income (AOCI).

SFAS No. 158 also requires that employers measure the benefit obligation and plan assets as of the fiscal year end for fiscal years ending after December 15, 2008. In fiscal 2007 and earlier, a September 30 measurement date was used for pension and other postretirement benefit plans. SFAS No. 158 provides two approaches for an employer to transition to a fiscal year end measurement date. The approach applied by the Association allows for the use of the measurements determined for the prior year end. Under this alternative, pension and other postretirement benefit expense measured for the three-month period October 1, 2007 to December 31, 2007 (determined using the September 30, 2007 measurement date) is reflected as an adjustment to beginning 2008 unallocated retained earnings. As a result, the Association decreased unallocated retained earnings by \$20.

SFAS No. 158 further requires the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of AOCI. These amounts are subsequently recognized as components of net periodic benefit costs over time. For 2008, \$60 has been recognized as a net credit to AOCI to reflect these elements.

The Association participates in a defined contribution Districtwide 401(k) plan, which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Association will contribute \$.50 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. For employees hired on or after January 1, 2003, the Association will contribute \$1.00 for each \$1.00 of the maximum employee contribution of 6 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as adjusted by the Internal Revenue Service. Employer contributions to this plan were \$86, \$94, and \$86 for the years ended December 31, 2008, 2007 and 2006, respectively.

Note 11 — Related Party Transactions

In the ordinary course of business, the Association enters into loan transactions with officers and directors of the Association, their immediate families and other organizations with which such persons may be associated. Such loans are subject to special approval requirements contained in the FCA regulations and are made on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated borrowers.

Total loans to such persons at December 31, 2008 amounted to \$1,753. During 2008, \$1,383 of new loans were made and repayments totaled \$2,208. In the opinion of management, none of these loans outstanding at December 31, 2008 involved more than a normal risk of collectibility.

Note 12 — Commitments and Contingencies

The Association has various commitments outstanding and contingent liabilities.

The Association may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers and to manage their exposure to interest-rate risk. These financial instruments include commitments to extend credit and/or commercial letters of credit. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commercial letters of credit are agreements to pay a beneficiary under conditions specified in the letter of credit. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. At December 31, 2008, \$43,679 of commitments to extend credit and \$1,343 of commercial letters of credit was outstanding.

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the Consolidated Balance Sheets until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and management applies the same credit policies to these commitments. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower.

The Association also participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. At December 31, 2008, the Association had outstanding \$3,468 of standby letters of credit, with expiration dates ranging from December 31, 2008 to April 2, 2012. The maximum potential amount of future payments the Association may be required to make under these existing guarantees is \$3,468.

A guarantor is required to recognize at the inception of a guarantee, a liability for the fair value of the guarantee commitment. The Association has determined the fair value of the guarantee commitment based upon the fees to be earned over the life of the guarantee. The fair value is updated periodically to reflect changes in individual guarantee amounts and the remaining life to maturity of the individual guarantees

in the Association's inventory. At December 31, 2008, the Association's inventory of standby letters of credit had a fair value of \$64 and was included in other liabilities.

During 2006, the Association agreed to become one of several investors in a USDA approved Rural Business Investments Company (RBIC). At December 31, 2008 there was an outstanding commitment of \$131 to make additional equity purchases.

Note 13 — Fair Value Measurement

As described in Note 2, the Association adopted SFAS No. 157 effective January 1, 2008 which expanded the Association's fair value disclosure for certain assets and liabilities measured at fair value on a recurring and non-recurring basis. These assets and liabilities primarily consist of assets held in trust funds, standby letters of credit, and impaired loans.

SFAS No. 157 establishes a fair value hierarchy for disclosure of fair value measurements to maximize the use of observable inputs, that is, inputs that reflect the assumptions market participants would use in pricing an asset or liability based on market data obtained from sources independent of the reporting entity. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The three levels of inputs and the classification of the Association's financial instruments within the fair value hierarchy are as follows:

Level 1

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. The Association's Level 1 assets at December 31, 2008 consist of assets held in trust funds related to deferred compensation and supplemental retirement plans. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

Level 2

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability. The Association has no Level 2 assets or liabilities measured at fair value on a recurring basis at December 31, 2008.

Level 3

Level 3 inputs to the valuation methodology 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. Level 3 assets at December 31, 2008 include impaired loans which represent the fair value of certain loans that were evaluated for impairment under SFAS No. 114. The fair value was based upon the underlying collateral since these were collateral-dependent loans. The fair value measurement process uses independent appraisals and other market-based information,

but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy. When the value of the collateral, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established. Level 3 liabilities at December 31, 2008 include standby letters of credit whose market value is internally calculated based on information that is not observable either directly or indirectly in the marketplace.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents the assets and liabilities that are measured at fair value on a recurring basis at December 31, 2008 for each of the fair value hierarchy levels:

	December 31, 2008			
	Level 1	Level 2	Level 3	Total Fair Value
Assets:				
Assets held in trust funds	\$ 263	\$ -	\$ -	\$ 263
Total Assets	\$ 263	\$ -	\$ -	\$ 263
Liabilities:				
Standby letters Of credit	\$ -	\$ -	\$ 64	\$ 64
Total Liabilities	\$ -	\$ -	\$ 64	\$ 64

The following table presents the changes in Level 3 assets and liabilities measured at fair value on a recurring basis:

	Standby Letters Of Credit
Balance at January 1, 2008	\$ 115
Total gains or (losses) realized/unrealized:	
Included in earnings	-
Included in other comprehensive loss	-
Purchases, sales, issuances And settlements, net	(51)
Transfers in and/or out of level 3	-
Balance at December 31, 2008	\$ 64

Assets and Liabilities Measured at Fair Value on a Non-recurring Basis

Assets and liabilities measured at fair value on a non-recurring basis at December 31, 2008 for each of the fair value hierarchy values are summarized below:

	December 31, 2008				Total Gains (Losses)
	Level 1	Level 2	Level 3	Total Fair Value	
Assets:					
Impaired Loans	\$ -	\$ -	\$ 7,670	\$ 7,670	\$ (3,659)

Note 14 — Disclosures About Fair Value of Financial Instruments

The following table presents the carrying amounts and fair values of the Association's financial instruments at December 31, 2008, 2007 and 2006.

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

The estimated fair values of the Association's financial instruments are as follows:

	December 31, 2008		December 31, 2007	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash	\$ -	\$ -	\$ 64	\$ 64
Loans, net of allowance	\$ 194,239	\$ 196,194	\$ 258,013	\$ 260,831
Investment securities	\$ 38,517	\$ 37,221	\$ 36,958	\$ 36,599
Assets held in trust funds	\$ 263	\$ 263	\$ 284	\$ 284
Financial liabilities:				
Notes payable to AgFirst Farm Credit Bank	\$ 211,647	\$ 213,786	\$ 260,052	\$ 263,010
December 31, 2006				
Financial assets:				
Cash	\$ -	\$ -		
Loans, net of allowance	\$ 219,412	\$ 221,511		
Investment securities	\$ 32,202	\$ 31,977		
Assets held in trust funds	\$ 21	\$ 21		
Financial liabilities:				
Notes payable to AgFirst Farm Credit Bank	\$ 217,032	\$ 218,426		

A description of the methods and assumptions used to estimate the fair value of each class of the Association's financial instruments for which it is practicable to estimate that value follows:

- A. **Cash:** The carrying value is a reasonable estimate of fair value.
- B. **Loans:** Because no active market exists for the Association's loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans would be made to borrowers with similar credit risk. As the discount rates are based on the Bank's loan rates, as well as management estimates, management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale.

For purposes of determining fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

Fair value of loans in a nonaccrual status is estimated to be the carrying amount less specific reserves.

The carrying value of accrued interest approximates its fair value.

C. **Investment Securities:** Fair value is based upon quoted market price.

D. **Investment in AgFirst Farm Credit Bank and Other Farm Credit Institutions:** Estimating the fair value of the Association's investment in the Bank and Other Farm Credit Institutions is not practicable because the stock is not traded. As described in Note 5, the net investment is a requirement of borrowing from the Bank and is carried at cost plus allocated equities in the accompanying Consolidated Balance Sheets. The Association owns 3.58 percent of the issued stock of the Bank as of December 31, 2008 net of any reciprocal investment. As of that date, the Bank's assets totaled \$29.9 billion and shareholders' equity totaled \$1.2 million. The Bank's earnings were \$217 million during 2008.

In addition, the Association has an investment of \$3,577 related to other Farm Credit institutions.

E. **Notes Payable to AgFirst Farm Credit Bank:** The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

F. **Commitments to Extend Credit and Standby Letters of Credit:** The estimated market value of off-balance-sheet commitments is minimal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics and since the related credit risk is not significant.

G. **Assets Held in Trust Funds:** See Note 13 for discussion of estimation of fair value for this instrument.

Note 15 — Quarterly Financial Information (Unaudited)

Quarterly results of operations for the years ended December 31, 2008, 2007 and 2006 follow:

	2008				
	First	Second	Third	Fourth	Total
Net interest income	\$ 1,523	\$ 858	\$ 910	\$ 1,104	\$ 4,395
Provision for (reversal of allowance for) loan losses	883	1,166	653	1,481	4,183
Noninterest income (expense), net	911	(150)	1,021	122	1,904
Net income (loss)	\$ 1,551	\$ (458)	\$ 1,278	\$ (255)	\$ 2,116

	2007				
	First	Second	Third	Fourth	Total
Net interest income	\$ 1,584	\$ 1,486	\$ 1,569	\$ 1,677	\$ 6,316
Provision for (reversal of allowance for) loan losses	(36)	(17)	(83)	162	26
Noninterest income (expense), net	187	639	707	1,419	2,952
Net income (loss)	\$ 1,807	\$ 2,142	\$ 2,359	\$ 2,934	\$ 9,242

	2006				
	First	Second	Third	Fourth	Total
Net interest income	\$ 1,970	\$ 1,794	\$ 1,953	\$ 1,899	\$ 7,616
Provision for (reversal of allowance for) loan losses	67	7	(64)	(20)	(10)
Noninterest income (expense), net	(276)	77	320	474	595
Net income (loss)	\$ 1,627	\$ 1,864	\$ 2,337	\$ 2,393	\$ 8,221

(This page intentionally left blank)

(This page intentionally left blank)

(This page intentionally left blank)