



PROUD MEMBER OF THE FARM CREDIT SYSTEM

## Quarterly Report To Stockholders

For the Quarter Ended September 30, 2020

## REPORT OF MANAGEMENT

The undersigned certify that this quarterly report has been reviewed and prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of his knowledge and belief.

*Ben R. Novosad*

Ben R. Novosad,  
Chief Executive Officer

*John Malazzo*

John Malazzo,  
Chairman, Board of Directors

*Don VandeVanter*

Don VandeVanter,  
Chief Financial Officer

November 5, 2020

# *Third Quarter 2020 Financial Report*

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**MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS  
(Dollars in thousands)**

The following commentary reviews the financial performance of Capital Farm Credit, ACA, referred to as the association, for the quarter ended September 30, 2020. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2019 Annual Report to Stockholders. The association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial institutions established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder. The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries, Capital Farm Credit, PCA and Capital Farm Credit, FLCA. The consolidated financial statements were prepared under the oversight of the association's audit committee.

The association continues to operate with several employees working remotely in the Coronavirus Disease (COVID-19) pandemic environment. The association has a limited number of employees at certain locations and administrative offices. However, a little more than 50 percent of its staff are working from the office, which is a slight increase from the second quarter. The association's Pandemic Response Team (PRT), which is responsible for ensuring the safety of our employees and our members, continues to meet weekly to discuss guidelines for employees based on local/state/federal recommendations. The PRT sends frequent communications to all employees regarding expectations for employees who may be working at an office location. The association continues to serve its members without much interruption.

The state's economy deteriorated in the second quarter of 2020, with unemployment rates skyrocketing to 13.5 percent in April and job losses plummeting 8.4 percent as of August 2020. Most of the damage was seen in the leisure and hospitality and oil and gas industries, but all sectors were affected negatively with the COVID containment measures. There has been a rebound during the third quarter, especially in the services and manufacturing sectors. State unemployment improved to 6.8 percent in August. The Federal Reserve Bank of Dallas predicts a 4.8 percent annual decline in employment for Texas in 2020.

The association successfully implemented a payment deferral program for its customers affected by COVID-19. As of September 30, 2020, there were 708 loans with volume of \$400,325 that sought relief under the deferral program. This program was not focused on any specific commodity but offered to all members who had not been delinquent more than 30 days at any time in the previous 12 months. The association also became a certified Small Business Administration (SBA) lender, implementing the Payroll Protection Program (PPP) of the Coronavirus Aid Relief and Economic Security (CARES) Act, offering loans to existing customers with 100 percent guarantees by the SBA under certain parameters. So far during 2020, the association made 99 loans for \$6,194 under the PPP. As of September 30, 2020, none of the PPP loans have yet been forgiven.

Continued demand for real estate loans remained strong in the third quarter of 2020. This is being driven by a low interest rate environment and the desire for many members who want to relocate from cities to rural areas. However, demand for production volume is significantly lower in 2020 compared to the previous year. This is a result of weak agricultural commodity prices as well as very dry conditions. A lot of the cotton crop has failed, and producers will be dependent on crop insurance and government support this year. In addition, the oil and gas industry has significantly reduced production with the reduced demand during the pandemic. Many wells have been taken offline. Many producers and landowners with royalty interest will continue to be negatively impacted until demand picks up. Livestock producers and dairy farmers have also been negatively impacted with reductions in commodity prices and issues in the supply chain. Nevertheless, the Association's credit quality remains relatively stable, as producers have been supported by the government's fiscal stimulus.

**Patronage Refunds by Association**

In September 2020, the board of directors approved a resolution to retire \$55,000 in nonqualified allocated equities which will be paid to the recipients in November 2020. The retirement was a distribution of 57 percent of the earnings allocated in 2012.

The board of directors approved a \$176,537 patronage distribution for 2019. Of that amount \$88,550 of this distribution was paid in cash in March 2020 and \$87,987 was distributed in the form of nonqualified allocated equity, which means the owners of these distributions will not pay federal income taxes until the equities are retired. It is the board's intention with these allocations to assign ownership of the earnings of the association, allowing the stockholders to benefit more fully from the earnings of the association and to create a method to make future equity distributions in the form of cash. While there is not a planned retirement of these allocated equities, the board of directors makes annual evaluations of the association's capital position to determine potential cash retirements of these equities.

In September 2019 the board of directors approved a resolution to retire \$38,206 in nonqualified allocated equities which were paid to the recipients in November 2019. The retirement was a distribution of all remaining allocated equities from 2011. In September 2018

the board of directors approved a resolution to retire \$50,000 in nonqualified allocated equities which were paid to the recipients in November 2018. The retirement was a distribution of 56 percent of the earnings allocated in 2011.

### Loan Portfolio

Total loans outstanding at September 30, 2020, including nonperforming loans, were \$8,379,785 compared to \$7,822,838 at December 31, 2019, reflecting an increase of \$556,947, or approximately 7.1 percent, with notable increases in the real estate mortgage, farm-related business and communication sectors. This rate of growth is a result of an attractive rate environment and significant increase in demand for rural properties.

The association's portfolio quality remains strong. Despite a slight decrease in high risk assets, overall credit quality has remained relatively consistent with 96.3 percent acceptable at September 30, 2020 and 96.5 percent at December 31, 2019. Substandard loans decreased from 2.0 percent at December 31, 2019 to 1.6 percent at September 30, 2020 offset by an increase in other assets especially mentioned from 1.5 percent at December 31, 2019 to 2.1 percent at September 30, 2020. The association recorded \$1,595 in recoveries and \$1,615 in charge-offs for the nine months ended September 30, 2020, and \$934 in recoveries and \$3,991 in charge-offs for the same period in 2019. The association's allowance for loan losses was 0.4 percent of total loans outstanding as of September 30, 2020, and December 31, 2019.

### Risk Exposure

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned. The association's high-risk assets decreased by 0.5 percent in the first nine months of 2020. The decrease has been in loans 90 days past due and still accruing interest, formally restructured loans and other property owned offset by an increase in nonaccrual loans. The following table summarizes the association's components and trends of high-risk assets:

	<u>September 30, 2020</u>	<u>%</u>	<u>December 31, 2019</u>	<u>%</u>
Nonaccrual loans	\$ 66,236	86.4	\$ 61,535	79.8
Loans 90 days past due and still accruing interest	793	1.0	3,840	5.0
Formally restructured loans	9,296	12.1	10,861	14.1
Other property owned, net	361	0.5	859	1.1
Total	<u>\$ 76,686</u>	<u>100.0</u>	<u>\$ 77,095</u>	<u>100.0</u>

Nonaccrual loans increased \$4,701 during the nine months ended September 30, 2020, with increases primarily in the production and intermediate term and real estate mortgage industries with an offset in the energy and farm-related business industries. Nonaccrual loans were 0.8 percent of total loans outstanding at September 30, 2020 and at December 31, 2019.

Loans that are 90 or more days past due and still accruing interest decreased \$3,047 in the nine months ended September 30, 2020 primarily in the real estate mortgage industry. These loans have a documented plan that details how and when the amount owed will be paid.

Formally restructured accrual loans decreased \$1,565 during the first nine months of 2020. Most of these restructurings have been to extend the repayment terms for customers who were significantly affected by lower commodity prices. The association is cooperating with distressed borrowers to help them work through temporary repayment problems.

Other property owned decreased \$498 during the nine months ended September 30, 2020. The association is actively working with real estate professionals to ensure properties are accurately valued on the association's books and that proactive marketing activities are in place.

Management also continues to routinely evaluate and monitor counterparty and collateral risks in an effort to avoid concentrations that could result in excess exposure to a single counterparty or type of collateral. The loan portfolio management practices that are in place have been designed to ensure loans and industries with actual or potential problems are promptly identified, monitored and addressed in a manner that allows the lending staff to work with problem customers and industries through periods of adversity.

### Results of Operations

The association had net income of \$155,931 and \$52,065 for the nine and three months ended September 30, 2020, respectively, as compared to net income of \$133,845 and \$47,994 for the same periods in 2019, reflecting an increase of \$22,086 and \$4,071 or 16.5 and 8.5 percent, respectively. The increase in net income was primarily the result of a reduction of \$2,034 in provision for loan losses,

a reduction of \$14,837 in interest expense on the direct note and an increase in noninterest income of \$10,618 for the nine month period ended September 30, 2020.

Net interest income was \$183,453 and \$62,505 for the nine and three months ended September 30, 2020, respectively, compared to \$175,201 and \$58,912 for the same periods in 2019. Interest income for the nine and three months ended September 30, 2020, decreased by \$6,645 and \$5,654 or 2.1 and 5.2 percent from the same periods of 2019, because of the decline in interest rates of almost 0.52 percent, despite the increase in loan volume of \$556,947. Interest expense for the nine and three months ended September 30, 2020, decreased by \$14,897 and \$9,247 or 10.3 and 18.6 percent from the same periods of 2019 due to lower interest rates.

The effects of changes in average volume and interest rates on net interest income in the nine months ended September 30, 2020, as compared with the corresponding period of the prior year, are presented in the following tables:

	For the nine months ended September 30, 2020		For the nine months ended September 30, 2019	
	Average Balance	Interest	Average Balance	Interest
Accrual loans and investments	\$ 7,997,900	\$313,136	\$ 7,472,335	\$ 319,781
Interest-bearing liabilities	6,843,155	129,683	6,376,611	144,580
Impact of capital	\$ 1,154,745		\$ 1,095,724	
Net interest income		<u>\$183,453</u>		<u>\$ 175,201</u>
Net interest income as a percentage of average earning assets		3.06%		3.13%
		<u>Average Yield</u>		<u>Average Yield</u>
Yield on loans		5.23%		5.72%
Cost of interest-bearing Liabilities		2.53%		3.03%
Net interest spread		<u>2.70%</u>		<u>2.69%</u>

	2020 vs. 2019		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest income	\$ 22,512	\$ (29,157)	\$ (6,645)
Interest expense	10,588	(25,485)	(14,897)
Net interest income	<u>\$ 11,924</u>	<u>\$ (3,672)</u>	<u>\$ 8,252</u>

The association's noninterest income for the nine and three months ended September 30, 2020 increased by \$10,618 and \$4,615 or 26.1 and 37.8 percent, respectively, from the same periods in 2019. The increase for the nine month period is primarily due to an increased patronage from the Bank of \$5,160, or 17.3 percent and an increase in loan fees of \$5,681, or 165.3 percent, offset by a decrease in gains on sales of premises and equipment of \$1,020 or 71.6 percent. The increase in loan fees was driven by the significant drop in interest rates during the year as many members converted higher interest rates to lower rates and paid conversion fees for that benefit. The increase in noninterest income for the three month period was a result of an increase of \$2,320 or 22.7 percent in patronage from the Bank, an increase of \$1,978 or 134.0 percent in loan fees and an increase of \$519 or 266.2 percent in other noninterest income.

Noninterest expenses for the nine and three months ended September 30, 2020, decreased by \$1,174 and \$866 or 1.6 and 3.7 percent, respectively, from the same periods of 2019. Costs related to travel, training and public and member relations have been directly impacted by the pandemic, as many events have been cancelled for the protection of the participants. For the nine months ended September 30, 2020, these decreases were offset by increases in salaries and employee benefits driven by an increase in the number of employees and salary adjustments. For the three months ended September 30, 2020, the decreases were offset by increases in insurance fund premiums as a result of increased rates and by increases in occupancy and equipment, as a result of new or renewed leases during the quarter.

The association's return on average assets for the nine months ended September 30, 2020, was 2.5 percent compared to 2.3 percent for the same period in 2019. The association's return on average equity for the nine months ended September 30, 2020, was 15.6 percent, compared to 13.5 percent for the same period in 2019.

**Liquidity and Funding Sources**

The association secures the majority of its lendable funds from the Bank, which obtains its funds through the issuance of System-wide obligations. The following schedule summarizes the association's borrowings.

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
Note payable to the bank	\$7,115,101	\$6,604,398
Accrued interest on note payable	13,081	16,157
Total	<u>\$7,128,182</u>	<u>\$6,620,555</u>

The association operates under a general financing agreement (GFA) with the Bank. The current GFA is effective through September 30, 2023. The outstanding balance of \$7,115,101 as of September 30, 2020, is recorded as a liability on the association's balance sheet. The note carried a weighted average interest rate of 2.21 percent at September 30, 2020. The indebtedness is collateralized by a pledge of substantially all of the association's assets to the Bank and is governed by the GFA. The increase in note payable to the Bank since December 31, 2019 is due to the association's increase in loan volume and the distribution of the 2019 patronage refund. The decrease in accrued interest on the note payable, despite the increase in the note payable, is the result of the decrease in interest from 2.73 percent at December 31, 2019 to 2.21 percent at September 30, 2020. The maximum amount the association may borrow from the Bank as of September 30, 2020, was \$8,206,522 as defined by the GFA.

The liquidity policy of the association is to manage cash balances to maximize debt reduction, and to increase accrual loan volume. This policy will continue to be pursued during 2020. As borrower payments are received, they are applied to the association's note payable with the Bank.

**Capital Resources and Regulatory Matters**

The association's capital position increased by \$101,523 at September 30, 2020, compared to December 31, 2019 primarily as a result of net earnings for the period, offset by the Board of Directors' declaration to retire \$55,000 in allocated equities. Farm Credit Administration regulations require the association to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and unallocated retained earnings and equivalents (UREE) ratios. The permanent capital ratio remains in effect, with some modifications to align with the new regulations. As of September 30, 2020, the association exceeded all regulatory capital requirements. For more information, see Note 5-“Members Equity” in the accompanying financial statements.

**Significant Recent Accounting Pronouncements**

Refer to Note 1 – “Organization and Significant Accounting Policies” in this quarterly report for disclosures of recent accounting pronouncements which may impact the association's consolidated financial position and results of operations and for critical accounting policies.

**Relationship with the Farm Credit Bank of Texas**

The association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the 2019 Annual Report of Capital Farm Credit more fully describe the association's relationship with the Bank.

The annual and quarterly stockholder reports of the Bank are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, Corporate Communications, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9204. The annual and quarterly stockholder reports for the Bank are also available on its website at [www.farmcreditbank.com](http://www.farmcreditbank.com).

The association's annual and quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Capital Farm Credit, ACA, P.O. Box 488, Hondo, Texas 78861 or calling (830) 426-4589. Copies of the association's quarterly and annual stockholder reports are also available on its Website at [www.capitalfarmcredit.com](http://www.capitalfarmcredit.com) or can be requested by e-mailing [Javier.Lemus@capitalfarmcredit.com](mailto:Javier.Lemus@capitalfarmcredit.com).

**CAPITAL FARM CREDIT, ACA**  
**CONSOLIDATED BALANCE SHEETS**  
(Dollars in thousands)

	<b>September 30, 2020</b>	December 31, 2019
	<b>(Unaudited)</b>	<b>(Audited)</b>
<b><u>ASSETS</u></b>		
Cash	\$ 2	\$ 2
Loans	8,379,785	7,822,838
Less: Allowance for losses	(35,914)	(30,798)
Net Loans	8,343,871	7,792,040
Accrued interest receivable - loans	70,466	71,378
Investment - held-to-maturity	2,666	3,418
Accrued interest receivable - investments	36	51
Investment in and receivable from the Bank:		
Capital stock	133,542	135,011
Receivable	39,581	19,474
Investment in Rural Business Investment Company (RBIC)	12,003	12,631
Investments in other Farm Credit Institutions	10,976	9,858
Other property owned, net	361	859
Premises and equipment, net	15,448	15,403
Right of use asset - leases	10,581	10,671
Other assets	15,854	15,182
 Total assets	 \$ 8,655,387	 \$ 8,085,978
<b><u>LIABILITIES</u></b>		
Note payable to the Bank	\$ 7,115,101	\$ 6,604,398
Advanced conditional payments	12,689	6,502
Accrued interest payable	13,081	16,157
Lease liabilities	10,754	10,814
Drafts outstanding	185	2,110
Patronage distributions payable	55,006	88,555
Unfunded post retirement medical obligations	26,699	26,300
Reserve for unfunded commitments	547	665
Other liabilities	35,644	46,319
 Total liabilities	 7,269,706	 6,801,820
<b><u>MEMBERS' EQUITY</u></b>		
Capital stock and participation certificates	26,582	25,980
Non-qualified allocated retained earnings	619,877	674,877
Unallocated retained earnings	742,155	586,224
Accumulated other comprehensive loss	(2,933)	(2,923)
 Total members' equity	 1,385,681	 1,284,158
 Total liabilities and members' equity	 \$ 8,655,387	 \$ 8,085,978

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

**CAPITAL FARM CREDIT, ACA**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(dollars in thousands)  
**(UNAUDITED)**

	For the three months ended September 30, 2020	For the three months ended September 30, 2019	For the nine months ended September 30, 2020	For the nine months ended September 30, 2019
<b><u>Interest Income</u></b>				
Loans	\$ 102,956	\$ 108,589	\$ 313,016	\$ 319,605
Investments	34	55	120	176
Total interest income	<u>102,990</u>	<u>108,644</u>	<u>313,136</u>	<u>319,781</u>
<b><u>Interest Expense</u></b>				
Note Payable to the Bank	40,484	49,708	129,669	144,506
Advance conditional payments	1	24	14	74
Total interest expense	<u>40,485</u>	<u>49,732</u>	<u>129,683</u>	<u>144,580</u>
Net interest income	<u>62,505</u>	<u>58,912</u>	<u>183,453</u>	<u>175,201</u>
<b><u>Provision for Loan Losses</u></b>				
Provision for (reversal of) loan losses	4,455	(549)	5,018	7,052
Net interest income after provision for losses	<u>58,050</u>	<u>59,461</u>	<u>178,435</u>	<u>168,149</u>
<b><u>Noninterest Income</u></b>				
Patronage income from the Bank	12,540	10,220	34,912	29,752
Loan fees	3,454	1,476	9,118	3,437
Financially related services income	412	450	1,196	1,181
Gain on sale of premises and equipment, net	62	57	404	1,424
Gain on other property owned, net	33	202	63	117
Other noninterest income (loss)	324	(195)	5,531	4,695
Total noninterest income	<u>16,825</u>	<u>12,210</u>	<u>51,224</u>	<u>40,606</u>
<b><u>Noninterest Expense</u></b>				
Salaries and employee benefits	15,671	15,877	50,834	49,255
Insurance Fund premium	1,801	1,369	4,315	4,011
Occupancy and equipment	1,344	1,171	4,114	3,855
Advertising	934	988	2,740	2,900
Travel	655	1,034	2,039	3,190
Public and member relations	365	630	1,838	2,562
Purchased services	440	590	1,789	2,047
Supervisory and exam expense	424	496	1,442	1,488
Data processing	390	497	1,165	1,206
Business Insurance Expense	15	15	1,008	1,038
Communications	253	260	760	768
Director's expense	190	220	598	756
Training	64	253	270	663
Other noninterest expenses	264	276	816	1,163
Total noninterest expenses	<u>22,810</u>	<u>23,676</u>	<u>73,728</u>	<u>74,902</u>
Income before income tax	<u>52,065</u>	<u>47,995</u>	<u>155,931</u>	<u>133,853</u>
Provision for income tax	0	1	-	8
Net income	<u>\$ 52,065</u>	<u>\$ 47,994</u>	<u>\$ 155,931</u>	<u>\$ 133,845</u>
Other comprehensive (loss):				
Change in postretirement benefit plans	(3)	(46)	(10)	(137)
Income tax expense related items of other comprehensive income	-	-	-	-
Other comprehensive (loss), net of tax	<u>(3)</u>	<u>(46)</u>	<u>(10)</u>	<u>(137)</u>
<b>COMPREHENSIVE INCOME</b>	<u>\$ 52,062</u>	<u>\$ 47,948</u>	<u>\$ 155,921</u>	<u>\$ 133,708</u>

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

**CAPITAL FARM CREDIT, ACA**  
**CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY**  
(Dollars in thousands)  
(UNAUDITED)

	<b>Capital Stock/ Participation Certificates</b>	<b>Retained Earnings</b>		<b>Accumulated Other Comprehensive Income (Loss)</b>	<b>Total Members' Equity</b>
		<b>Non-qualified Allocated</b>	<b>Unallocated</b>		
Balance at December 31, 2018	\$ 25,804	\$ 624,839	\$ 581,674	\$ (79)	\$ 1,232,238
Net income	-	-	133,845	-	133,845
Other comprehensive loss	-	-	-	(137)	(137)
Capital stock/participation certificates issued	2,803	-	-	-	2,803
Capital stock/participation certificates/ allocated equities retired	(2,658)	(38,202)	-	-	(40,860)
Change in patronage declared and paid	-	252	78	-	330
Balance at September 30, 2019	25,949	586,889	715,597	(216)	1,328,219
Net income	-	-	47,160	-	47,160
Other comprehensive loss	-	-	-	(2,707)	(2,707)
Capital stock/participation certificates issued	953	-	-	-	953
Capital stock/participation certificates/ allocated equities retired	(922)	(4)	-	-	(926)
Patronage distributions declared:	-	-	-	-	-
Cash	-	-	(88,550)	-	(88,550)
Nonqualified allocations	-	87,987	(87,987)	-	-
Change in patronage declared and paid	-	5	4	-	9
Balance at December 31, 2019	25,980	674,877	586,224	(2,923)	1,284,158
Net income	-	-	155,931	-	155,931
Other comprehensive loss	-	-	-	(10)	(10)
Capital stock/participation certificates issued	4,071	-	-	-	4,071
Capital stock/participation certificates/ allocated equities retired	(3,469)	(55,000)	-	-	(58,469)
<b>Balance at September 30, 2020</b>	<b>\$ 26,582</b>	<b>\$ 619,877</b>	<b>\$ 742,155</b>	<b>\$ (2,933)</b>	<b>\$ 1,385,681</b>

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

**CAPITAL FARM CREDIT, ACA**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(Dollars in thousands)**  
**(UNAUDITED)**

**NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:**

Capital Farm Credit, ACA including its wholly owned subsidiaries, Capital Farm Credit, PCA and Capital Farm Credit, FLCA, (collectively called the “association”), is a member-owned cooperative which provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes in 192 counties in the state of Texas. The association is a lending institution of the Farm Credit System (System) which was established by acts of Congress and is subject to the provisions of the Farm Credit Act of 1971, as amended (Act), to meet the needs of American agriculture.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2019 as contained in the 2019 Annual Report to Stockholders.

In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles (GAAP), except for the inclusion of a statement of cash flows. GAAP require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the association has elected not to include a statement of cash flows in these consolidated financial statements. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2020. Descriptions of the significant accounting policies are included in the 2019 Annual Report to Stockholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the banking industry. Certain amounts in the prior period’s financial statements have been reclassified to conform to current financial statement presentation.

In March 2020, the Financial Accounting Standards Board (FASB) issued guidance entitled “Facilitation of the Effects of Reference Rate Reform on Financial Reporting.” The guidance provides optional expedients and exceptions for applying GAAP to contracts, hedging relationships and other transactions affected by reference rate reform. The guidance simplifies the accounting evaluation of contract modifications that replace a reference rate affected by reference rate reform and contemporaneous modifications of other contracts related to the replacement of the reference rate. With respect to hedge accounting, the guidance allows amendment of formal designation and documentation of hedging relationships in certain circumstances as a result of reference rate reform and provides additional expedients for different types of hedges, if certain criteria are met. The optional amendments are effective as of March 12, 2020, through December 31, 2022. The institution is evaluating the impact of adoption on the institution’s financial condition and its results of operations.

In December 2019, the FASB issued guidance entitled “Simplifying the Accounting for Income Taxes.” This guidance eliminates certain intra period tax allocations, foreign deferred tax recognition and interim period tax calculations. In addition, the guidance simplifies disclosure regarding capital and franchise taxes, the allocation of goodwill in business combinations, subsidiary financial statements and other disclosures. The new guidance is intended to eliminate and/or simplify certain aspects of income tax accounting that are complex or that require significant judgment in application or presentation. The guidance becomes effective for fiscal years beginning after December 15, 2021. Early adoption of the guidance is permitted and the institution adopted this guidance on January 1, 2020. The adoption of this guidance did not materially impact the institution’s financial condition or results of operations.

In August 2018, FASB issued guidance entitled “Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Cost.” The guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by this guidance. This guidance became effective for interim and annual periods beginning after December 15, 2019. The guidance also requires an entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. It further specifies where to present expense and payments in the financial statements. The guidance is to be applied on a retrospective or prospective

basis to all implementation costs incurred after the date of adoption. The adoption of this guidance did not materially impact the Association’s financial condition or its results of operations.

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Defined Benefit Plans.” The guidance modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance becomes effective for fiscal years ending after December 15, 2020. Early adoption is permitted. The guidance is to be applied on a retrospective basis for all periods. The adoption of this guidance will not impact the Association’s financial condition or its results of operations, but will impact the employee benefit plan disclosures.

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement.” The guidance modifies the requirements on fair value measurements by removing, modifying or adding to the disclosures. This guidance became effective for interim and annual periods beginning after December 15, 2019. Early adoption was permitted and an entity was permitted to early adopt any removal or modified disclosures and delay adoption of the additional disclosures until their effective date. The Association early adopted the removal and modified disclosures during the fourth quarter of 2018. The adoption of this guidance did not impact the Association’s financial condition or its results of operations but did impact the fair value measurements disclosures.

In June 2016, the FASB issued guidance entitled “Measurement of Credit Losses on Financial Instruments.” The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange Commission filers this guidance was to become effective for interim and annual periods beginning after December 15, 2020, with early application permitted. In November 2019, the FASB issued an update that amends the mandatory effective date for this guidance for certain institutions. The change resulted from a change in the effective date philosophy that extends and simplifies the adoption by staggering the dates between large public entities and other entities. As a result of the change, the new credit loss standard, for those institutions qualifying for the delay, becomes effective for interim and annual reporting periods beginning after December 15, 2022, with early adoption permitted. The Association qualifies for the delay in the adoption date. The Association continues to evaluate the impact of adoption on the Association’s financial condition and its results of operations.

## NOTE 2 — INVESTMENTS:

### Investments Held-to-Maturity

The association’s held-to-maturity investment consists of Farmer Mac guaranteed agricultural mortgage-backed securities (AMBS). A summary of the amortized cost and fair value of investment securities held-to-maturity is as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield	Weighted Average Life (Years)
<b>September 30, 2020</b>						
Agricultural mortgage-backed securities	\$ 2,666	\$ 71		\$ 2,737	4.72%	3.10
<b>December 31, 2019</b>						
Agricultural mortgage-backed securities	\$ 3,418	\$ 45	\$ -	\$ 3,463	5.57%	2.82

The Farmer Mac AMBS were received in exchange for mortgage loans which were previously covered under the long-term standby commitments to purchase agreement with Farmer Mac. No gain or loss was recognized in the financial statements upon completion of the exchange transactions. Terms of the agreement call for a guarantee fee of 20-50 basis points to be paid to Farmer Mac, and for the association to receive a 30-basis-point fee for servicing the underlying loans.

The association has not experienced any impairments of these securities. Farmer Mac guarantees the underlying mortgages, and the association has the ability and intent to hold these securities to maturity or pay-off and it is unlikely the association would be required to sell these securities. These AMBS have contractual weighted average maturities of 3.10 years as of September 30, 2020; however, expected maturities differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

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

A summary of loans follows:

Industry	September 30 2020	%	December 31 2019	%
Real estate mortgage	\$ 6,440,876	77.0	\$ 5,970,318	76.4
Production and intermediate term	924,793	11.0	938,685	12.0
Farm-related business	740,947	8.8	659,056	8.4
Rural residential real estate	104,137	1.2	101,540	1.3
Energy	50,218	0.6	64,481	0.8
Communication	87,166	1.0	56,378	0.7
Lease receivables	15,451	0.2	16,558	0.2
Mission-related investments	6,154	0.1	6,022	0.1
Water and waste disposal	10,043	0.1	9,800	0.1
Total	\$ 8,379,785	100.0	\$ 7,822,838	100.0

At September 30, 2020, the association held four transactions, which are reported as loans on the consolidated balance sheet totaling \$5,869 and with \$0 in remaining commitments extended under the Rural America Bond Program approved by the FCA. The program is designed to meet the growing and changing needs of agricultural enterprises, agribusinesses and rural communities by providing investment in rural areas.

The association is authorized under the Farm Credit Act to accept “advance conditional payments” (ACPs) from borrowers. To the extent the borrower’s access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against loans as presented on the balance sheet. The association held \$90,724 and \$62,977 in funds which were netted against the loan balance at September 30, 2020 and December 31, 2019, respectively. Unrestricted advance conditional payments are included in liabilities. ACPs are not insured, and interest is generally paid by the association on such balances. Balances of ACPs were \$12,689 and \$6,502 on the balance sheet at September 30, 2020, and December 31, 2019, respectively.

The association purchases or sells participation interests in loans with other parties in order to diversify risk, manage loan volume and comply with FCA regulations. The following table presents information regarding the balances of participations purchased and sold as of September 30, 2020:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
	Real estate mortgage	145,788	757,154	7,763	-	\$ 153,551
Production and Intermediate-term	239,015	613,070	-	-	239,015	613,070
Farm-related business	572,358	150,167	3,739	-	576,097	150,167
Communication	87,166	-	-	-	87,166	-
Energy	50,218	-	-	-	50,218	-
Lease receivables	15,451	-	-	-	15,451	-
Water and waste disposal	9,959	-	-	-	9,959	-
Mission-related investments	1,953	-	3,916	-	5,869	-
Total	\$ 1,121,908	\$ 1,520,391	\$ 15,418	\$ -	\$ 1,137,326	\$ 1,520,391

Nonperforming assets (including related accrued interest) and related credit quality statistics are as follows:

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
<b>Nonaccrual loans:</b>		
Real estate mortgage	\$ 37,849	\$ 32,198
Production and intermediate-term	21,411	20,827
Farm-related business	4,026	5,316
Rural residential real estate	348	108
Energy	2,602	3,086
Total nonaccrual loans	<u>\$ 66,236</u>	<u>\$ 61,535</u>
<b>Accruing restructured loans:</b>		
Real estate mortgage	\$ 4,675	\$ 4,798
Production and intermediate-term	2,813	2,224
Energy	-	1,944
Mission-related investments	2,003	2,041
Total accruing restructured loans	<u>\$ 9,491</u>	<u>\$ 11,007</u>
<b>Accruing loans 90 days or more past due:</b>		
Real estate mortgage	\$ 194	\$ 3,224
Production and intermediate-term	607	670
Total accruing loans 90 days or more past due	<u>\$ 801</u>	<u>\$ 3,894</u>
Total nonperforming loans	<u>\$ 76,528</u>	<u>\$ 76,436</u>
Other property owned	361	859
Total nonperforming assets	<u>\$ 76,889</u>	<u>\$ 77,295</u>

One credit quality indicator utilized by the association is the FCA Uniform Loan Classification System that categorizes loans into five categories. The categories are defined as follows:

- 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 factors, conditions and values that make collection in full highly questionable, and
- Loss – assets are considered uncollectible.

The following table shows loans and related accrued interest as a percentage of total loans and related accrued interest receivable by loan type as of:

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
<b>Real estate mortgage</b>		
Acceptable	97.3%	97.5%
OAEM	1.5%	0.9%
Substandard/doubtful	1.2%	1.6%
	<u>100.0%</u>	<u>100.0%</u>
<b>Production and intermediate-term</b>		
Acceptable	90.3%	91.8%
OAEM	6.0%	3.2%
Substandard/doubtful	3.7%	5.0%
	<u>100.0%</u>	<u>100.0%</u>
<b>Farm-related business</b>		
Acceptable	94.3%	93.6%
OAEM	3.4%	5.1%
Substandard/doubtful	2.3%	1.3%
	<u>100.0%</u>	<u>100.0%</u>
<b>Rural residential real estate</b>		
Acceptable	98.4%	98.3%
OAEM	1.1%	1.3%
Substandard/doubtful	0.5%	0.4%
	<u>100.0%</u>	<u>100.0%</u>
<b>Energy</b>		
Acceptable	94.8%	92.2%
OAEM	-	-
Substandard/doubtful	5.2%	7.8%
	<u>100.0%</u>	<u>100.0%</u>
<b>Communication</b>		
Acceptable	100.0%	100.0%
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
<b>Mission-related investments</b>		
Acceptable	100.0%	100.0%
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
<b>Lease receivables</b>		
Acceptable	92.1%	100.0%
OAEM	7.9%	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
<b>Water and waste disposal</b>		
Acceptable	100.0%	100.0%
OAEM	-	-
Substandard/doubtful	-	-
	<u>100.0%</u>	<u>100.0%</u>
<b>Total Loans</b>		
Acceptable	96.3%	96.5%
OAEM	2.1%	1.5%
Substandard/doubtful	1.6%	2.0%
	<u>100.0%</u>	<u>100.0%</u>

The following table provides an age analysis of past due loans (including accrued interest) as of:

September 30, 2020	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or less than 30 Days Past Due	Total Loans	Loans > 90 Days and Accruing
Real estate mortgage	\$ 43,285	\$ 10,130	\$ 53,415	\$ 6,446,865	\$ 6,500,280	\$ 194
Production and intermediate-term	10,355	4,406	14,761	918,155	932,916	607
Farm-related business	2,495	913	3,408	739,737	743,145	-
Rural residential real estate	1,570	152	1,722	102,782	104,504	-
Energy	-	-	-	50,312	50,312	-
Communication	69	-	69	87,105	87,174	-
Mission-related investments	-	-	-	6,286	6,286	-
Lease receivables	-	-	-	15,590	15,590	-
Water and waste disposal	-	-	-	10,044	10,044	-
Total	\$ 57,774	\$ 15,601	\$ 73,375	\$ 8,376,876	\$ 8,450,251	\$ 801
December 31, 2019	30-89 Days Past Due	90 Days or More	Total Past Due	Not Past Due or less than 30	Total Loans	Loans > 90 Days and Accruing
Real estate mortgage	\$ 52,469	\$ 16,315	\$ 68,784	\$ 5,956,359	\$ 6,025,143	\$ 3,224
Production and intermediate-	10,402	10,972	21,374	930,226	951,600	670
Farm-related business	2,090	-	2,090	659,947	662,037	-
Rural residential real estate	1,196	30	1,226	100,697	101,923	-
Energy	-	-	-	64,623	64,623	-
Communication	-	-	-	56,381	56,381	-
Mission-related investments	-	-	-	6,076	6,076	-
Lease receivables	-	-	-	16,607	16,607	-
Water and waste disposal	-	-	-	9,826	9,826	-
Total	\$ 66,157	\$ 27,317	\$ 93,474	\$ 7,800,742	\$ 7,894,216	\$ 3,894

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

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the association for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Troubled debt restructurings are undertaken in order to improve the likelihood of recovery on the loan and may include, but are not limited to, forgiveness of principal or interest, interest rate reductions that are lower than the current market rate for new debt with similar risk, or significant term or payment extensions.

As of September 30, 2020, the total recorded investment of troubled debt restructured loans was \$20,058, including \$10,762 classified as nonaccrual and \$9,296 classified as accrual, with specific allowance for loan losses of \$1,515. Commitments to lend funds to borrowers whose loan terms have been modified in a troubled debt restructuring were \$200 and \$80 as of September 30, 2020 and at December 31, 2019, respectively.

The following tables present additional information regarding troubled debt restructurings, which includes both accrual and nonaccrual loans with troubled debt restructuring designation, that occurred during the nine months and three months ended September 30, 2020. The premodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end prior to the restructuring. The postmodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end the restructuring occurred. Loans formally restructured prior to January 1, 2019, were \$17,545.

Troubled Debt Restructuring Activity

	2020		2019	
	Pre-TDR Designation	Post-TDR Designation	Pre-TDR Designation	Post-TDR Designation
	Balance	Balance	Balance	Balance
Nine months ended September 30:				
Real estate mortgage	2,207	2,186	506	1,417
Production and intermediate-term	2,389	1,647	885	888
Total	<u>\$ 4,596</u>	<u>\$ 3,833</u>	<u>\$ 1,391</u>	<u>\$ 2,305</u>

	2020		2019	
	Pre-TDR Designation	Post-TDR Designation	Pre-TDR Designation	Post-TDR Designation
	Balance	Balance	Balance	Balance
Three months ended September 30:				
Real estate mortgage	1,941	1,920	132	145
Production and intermediate-term	737	537	112	114
Total	<u>\$ 2,678</u>	<u>\$ 2,457</u>	<u>\$ 244</u>	<u>\$ 259</u>

In restructurings where principal is forgiven, the amount of the forgiveness is immediately charged off. In restructurings where accrued interest is forgiven, the interest is reversed (if current year interest) or charged off (if prior year interest). Charge-offs recorded at the modification date were \$872 for the nine months ended September 30, 2020.

The predominant form of concession granted for troubled debt restructuring includes extension of terms. Other types of modifications include principal or accrued interest reductions, interest rate decreases and delayed payments, among others. At times, these terms might be offset with incremental payments, collateral or new borrower guarantees, in which case the association assesses all of the modified terms to determine if the overall modification qualifies as a troubled debt restructuring.

The association did not have loans that met the accounting criteria as a troubled debt restructuring and that occurred within the previous 12 months and for which there was a subsequent payment default during the period. A payment default is defined as a payment that is 30 days past due after the date the loan was restructured.

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

	Loans Modified as TDRs		TDRs in Nonaccrual Status*	
	September 30, 2020	December 31, 2019	September 30, 2020	December 31, 2019
Real estate mortgage	\$ 8,850	\$ 7,379	\$ 4,230	\$ 2,581
Production and intermediate-term	7,319	6,220	4,595	3,997
Mission related investments	1,953	2,042	-	-
Energy	1,936	1,944	1,937	-
Total	<u>\$ 20,058</u>	<u>\$ 17,585</u>	<u>\$ 10,762</u>	<u>\$ 6,578</u>

\*represents the portion of loans modified as TDRs that are in nonaccrual status

Additional impaired loan information is as follows:

	At September 30, 2020			At December 31, 2019		
	Loan Balance	Unpaid Principal Balance	Related Specific Allowance	Loan Balance	Unpaid Principal Balance	Related Specific Allowance
<b>Impaired loans with a related allowance for loan losses:</b>						
Real estate mortgage	\$ 69	\$ 69	\$ 23	\$ 771	\$ 934	\$ 37
Production and intermediate-term	8,281	9,920	2,217	6,870	9,301	892
Farm-related business	1,959	2,348	368	1,602	2,583	368
Rural residential real estate	34	57	6	-	-	-
Energy	2,589	2,589	1,572	3,086	3,086	167
Mission-related investments	1,946	1,946	44	134	134	42
Total	<u>\$ 14,878</u>	<u>\$ 16,929</u>	<u>\$ 4,230</u>	<u>\$ 12,463</u>	<u>\$ 16,038</u>	<u>\$ 1,506</u>
<b>Impaired loans with no related allowance for loan losses:</b>						
Real estate mortgage	\$ 42,593	\$ 43,741	\$ -	\$ 39,340	\$ 40,691	\$ -
Production and intermediate-term	16,452	23,765	-	16,790	24,123	-
Farm-related business	2,067	4,303	-	3,714	5,977	-
Rural residential real estate	314	390	-	108	279	-
Energy	13	13	-	1,934	-	-
Mission-related investments	7	7	-	1,887	1,887	-
Total	<u>\$ 61,446</u>	<u>\$ 72,219</u>	<u>\$ -</u>	<u>\$ 63,773</u>	<u>\$ 72,957</u>	<u>\$ -</u>
<b>Total impaired loans:</b>						
Real estate mortgage	\$ 42,662	\$ 43,810	\$ 23	\$ 40,111	\$ 41,625	\$ 37
Production and intermediate-term	24,733	33,685	2,217	23,660	33,424	892
Farm-related business	4,026	6,651	368	5,316	8,560	368
Rural residential real estate	348	447	6	108	279	-
Energy	2,602	2,602	1,572	5,020	3,086	167
Mission-related investments	1,953	1,953	44	2,021	2,021	42
Total	<u>\$ 76,324</u>	<u>\$ 89,148</u>	<u>\$ 4,230</u>	<u>\$ 76,236</u>	<u>\$ 88,995</u>	<u>\$ 1,506</u>

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

	For the Three Months Ended				For the Nine Months Ended			
	September 30, 2020		September 30, 2019		September 30, 2020		September 30, 2019	
	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
<b>Impaired loans with a related allowance for loan losses:</b>								
Real estate mortgage	\$ 68	\$ -	\$ 1,765	\$ -	\$ 142	\$ -	\$ 1,289	\$ 4
Production and intermediate-term	8,767	15	10,988	12	7,814	62	8,338	155
Farm-related business	1,852	-	2,600	35	1,724	-	2,620	143
Rural residential real estate	34	-	-	-	27	-	10	-
Energy	2,158	4	3,223	-	1,729	4	3,284	-
Mission-related investments	1,946	30	134	3	1,557	92	135	8
Total	<u>\$ 14,825</u>	<u>\$ 49</u>	<u>\$ 18,710</u>	<u>\$ 50</u>	<u>\$ 12,993</u>	<u>\$ 158</u>	<u>\$ 15,676</u>	<u>\$ 310</u>
<b>Impaired loans with no related allowance for loan losses:</b>								
Real estate mortgage	\$ 45,648	\$ 302	\$ 37,641	\$ 145	\$ 43,061	\$ 851	\$ 36,437	\$ 613
Production and intermediate-term	18,269	145	20,062	102	18,941	437	15,840	458
Farm-related business	1,791	11	3,884	3	3,583	64	3,844	3
Rural residential real estate	301	5	216	-	219	11	291	-
Energy	13	-	92	2	651	-	71	2
Mission-related investments	8	-	1,888	29	426	-	1,914	88
Lease receivables	-	-	30	-	-	-	10	-
Total	<u>\$ 66,030</u>	<u>\$ 463</u>	<u>\$ 63,813</u>	<u>\$ 281</u>	<u>\$ 66,881</u>	<u>\$ 1,363</u>	<u>\$ 58,407</u>	<u>\$ 1,164</u>
<b>Total impaired loans:</b>								
Real estate mortgage	\$ 45,716	\$ 302	\$ 39,406	\$ 145	\$ 43,203	\$ 851	\$ 37,726	\$ 617
Production and intermediate-term	27,036	160	31,050	114	26,755	499	24,178	613
Farm-related business	3,643	11	6,484	38	5,307	64	6,464	146
Rural residential real estate	335	5	216	-	246	11	301	-
Energy	2,171	4	3,315	2	2,380	4	3,355	2
Mission-related investments	1,954	30	2,022	32	1,983	92	2,049	96
Lease receivables	-	-	30	-	-	-	10	-
Total	<u>\$ 80,855</u>	<u>\$ 512</u>	<u>\$ 82,523</u>	<u>\$ 331</u>	<u>\$ 79,874</u>	<u>\$ 1,521</u>	<u>\$ 74,083</u>	<u>\$ 1,474</u>

A summary of changes in the allowance for loan losses and the ending balance including accrued interest of loans

	Real Estate Mortgage	Production and Intermediate Term	Farm related business	Rural Residential Real Estate	Energy and Water/Waste Disposal	Communication	Mission Related Investments	Lease Receivable	Total
<b>Allowance for credit losses:</b>									
Balance at									
June 30, 2020	\$ 12,863	\$ 11,314	\$ 5,644	\$ 105	\$ 1,568	\$ 99	\$ 43	\$ 108	\$ 31,744
Charge-offs	-	(919)	-	-	-	-	-	-	(919)
Recoveries	-	589	16	2	-	-	-	-	607
(Reversal) provision for loan losses	2,776	1,819	(287)	10	84	56	1	(4)	4,455
Transfer from reserve on unfunded commitments	(25)	40	11	-	2	(1)	-	-	27
Balance at September 30, 2020	<u>\$ 15,614</u>	<u>\$ 12,843</u>	<u>\$ 5,384</u>	<u>\$ 117</u>	<u>\$ 1,654</u>	<u>\$ 154</u>	<u>\$ 44</u>	<u>\$ 104</u>	<u>\$ 35,914</u>
Balance at									
December 31, 2019	13,664	12,989	3,314	109	519	77	42	84	\$ 30,798
Charge-offs	(22)	(1,439)	-	(25)	(129)	-	-	-	(1,615)
Recoveries	415	1,132	32	16	-	-	-	-	1,595
(Reversal) provision for loan losses	1,588	(2)	2,053	17	1,263	77	2	20	5,018
Transfer from reserve on unfunded commitments	(31)	163	(15)	-	1	-	-	-	118
Balance at September 30, 2020	<u>\$ 15,614</u>	<u>\$ 12,843</u>	<u>\$ 5,384</u>	<u>\$ 117</u>	<u>\$ 1,654</u>	<u>\$ 154</u>	<u>\$ 44</u>	<u>\$ 104</u>	<u>\$ 35,914</u>
Allowance for loan losses:									
Ending Balance at September 30, 2020									
Individually evaluated for impairment	\$ 23	\$ 2,217	\$ 368	\$ 6	\$ 1,572	\$ -	\$ 44	\$ -	\$ 4,230
Collectively evaluated for impairment	\$ 15,591	\$ 10,626	\$ 5,016	\$ 111	\$ 82	\$ 154	\$ -	\$ 104	\$ 31,684
Balance at									
June 30, 2019	\$ 11,397	\$ 15,296	\$ 3,177	\$ 105	\$ 1,519	\$ 87	\$ 42	\$ 90	\$ 31,713
Charge-offs	(4)	(2,035)	-	-	-	-	-	-	(2,039)
Recoveries	167	185	1	8	-	-	-	-	361
Provision (reversal) for loan losses	239	(561)	(253)	1	31	6	-	(12)	(549)
Transfer from reserve on unfunded commitments	(2)	53	(15)	-	-	-	-	-	36
Balance at September 30, 2019	<u>\$ 11,797</u>	<u>\$ 12,938</u>	<u>\$ 2,910</u>	<u>\$ 114</u>	<u>\$ 1,550</u>	<u>\$ 93</u>	<u>\$ 42</u>	<u>\$ 78</u>	<u>\$ 29,522</u>
Balance at									
December 31, 2018	\$ 8,517	\$ 11,915	\$ 3,439	\$ 98	\$ 1,331	\$ 86	\$ 41	\$ 68	\$ 25,495
Charge-offs	(23)	(3,957)	-	(11)	-	-	-	-	(3,991)
Recoveries	541	361	9	23	-	-	-	-	934
Provision (reversal) for loan losses	2,765	4,559	(512)	4	218	7	1	10	7,052
Transfer from reserve on unfunded commitments	(3)	60	(26)	-	1	-	-	-	32
Balance at September 30, 2019	<u>\$ 11,797</u>	<u>\$ 12,938</u>	<u>\$ 2,910</u>	<u>\$ 114</u>	<u>\$ 1,550</u>	<u>\$ 93</u>	<u>\$ 42</u>	<u>\$ 78</u>	<u>\$ 29,522</u>
Allowance for loan losses:									
Ending Balance at September 30, 2019									
individually evaluated for impairment	\$ 62	\$ 1,355	\$ 368	\$ -	\$ 1,046	\$ -	\$ 42	\$ -	\$ 2,873
collectively evaluated for impairment	\$ 11,735	\$ 11,583	\$ 2,542	\$ 114	\$ 504	\$ 93	\$ -	\$ 78	\$ 26,649

**Recorded Investments****in Loans Outstanding:**

Ending Balance at

September 30, 2020

\$	6,502,458	\$	930,737	\$	743,145	\$	104,505	\$	60,356	\$	87,174	\$	6,286	\$	15,590	\$	8,450,251
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Individually evaluated for impairment

\$	42,717	\$	24,831	\$	4,026	\$	348	\$	2,602	\$	-	\$	2,004	\$	-	\$	76,528
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Collectively evaluated for impairment

\$	6,459,741	\$	905,906	\$	739,119	\$	104,157	\$	57,754	\$	87,174	\$	4,282	\$	15,590	\$	8,373,723
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Ending Balance at

December 31, 2019

\$	6,025,143	\$	951,600	\$	662,037	\$	101,923	\$	74,449	\$	56,381	\$	6,076	\$	16,607	\$	7,894,216
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Individually evaluated for impairment

\$	40,111	\$	23,660	\$	5,316	\$	108	\$	5,020	\$	-	\$	2,021	\$	-	\$	76,236
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Collectively evaluated for impairment

\$	5,985,032	\$	927,940	\$	656,721	\$	101,815	\$	69,429	\$	56,381	\$	4,055	\$	16,607	\$	7,817,980
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**NOTE 4 —LEASES:**

The association evaluates arrangements at inception to determine if it meets the criteria for a lease. Leases with an initial term of 12 months or less are not recorded on the balance sheet with lease expense recognized on a straight-line basis over the lease term. Operating leases with terms greater than 12 months are included in right of use asset-leases (ROU) and lease liabilities on the balance sheet.

ROU assets represent the association's right to use an underlying asset for the lease term and lease liabilities represent the association's obligation to make lease payments arising from the lease. Operating ROU assets and liabilities are recognized based on the present value of the lease payments over the lease term. As the rate implicit in the lease is generally not readily determinable for the association's operating leases, the discount rates used to determine the present value of the association's lease liability are based on the association's incremental borrowing rate at the lease commencement date and commensurate with the remaining lease term. The incremental borrowing rate for a lease is the association's cost of funds from the Bank over a similar term at an amount equal to the lease payments in a similar economic environment. The association's lease terms may include options to extend or terminate the lease when it is reasonably certain that the association will exercise that option. Lease expense for lease payments is recognized on a straight-line basis over the lease term and is included in "Occupancy and equipment" in the income statement.

The components of lease expense were as follows:

Classification	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2020	September 30, 2019	September 30, 2020	September 30, 2019
Operating lease expense	\$ 599	\$ 580	\$ 1,775	\$ 1,543
Short-term lease expense	16	38	36	186
Total lease expense	<u>\$ 615</u>	<u>\$ 618</u>	<u>\$ 1,811</u>	<u>\$ 1,729</u>

Other information related to leases was as follows:

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2020	September 30, 2019	September 30, 2020	September 30, 2019
Cash paid for amounts included in the measurement of lease liabilities:				
Operating cash flows from operating leases	\$ 596	\$ 605	\$ 1,771	\$ 1,714
Right-of-use assets obtained in exchange for new lease obligations:				
Operating leases	525	51	1,547	1,143

Lease term and discount rate are as follows:

	September 30, 2020	December 31, 2019
Weighted average remaining lease term in years		
Operating leases	4.6	5.0
Weighted average discount rate		
Operating leases	2.2	3.3

Future minimum lease payments under non-cancellable leases as of September 30, 2020 were as follows:

	Operating Leases
2020 (excluding the nine months ended 9/30/2020)	\$ 609
2021	2,296
2022	2,149
2023	1,899
2024	1,592
Thereafter	2,849
Total lease payments	<u>11,394</u>
Less: interest	-
Total	<u>\$ 11,394</u>

#### NOTE 5 — MEMBERS EQUITY:

The association's board of directors has established a Capital Adequacy Plan (Plan) that includes the capital targets that are necessary to achieve the institution's capital adequacy goals as well as the minimum permanent capital standards. The Plan monitors projected patronage, equity retirements and other actions that may decrease the association's permanent capital. In addition to factors that must be considered in meeting the minimum standards, the board of directors also monitors the following factors: capability of management; quality of operating policies, procedures and internal controls; quality and quantity of earnings; asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan and lease portfolios; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the association's goals and objectives with the board.

#### Regulatory Capital Ratios

	<u>Regulatory Minimums</u>	<u>Conservation Buffers</u>	<u>Total</u>	<u>As of September 30, 2020</u>	<u>As of December 31, 2019</u>
Risk-adjusted:					
Common equity tier 1 ratio	4.5%	2.5%	7.0%	14.4%	14.6%
Tier 1 capital ratio	6.0%	2.5%	8.5%	14.4%	14.6%
Total capital ratio	8.0%	2.5%	10.5%	14.8%	15.0%
Permanent capital ratio	7.0%	0.0%	7.0%	14.5%	14.7%
Non-risk-adjusted:					
Tier 1 leverage ratio	4.0%	1.0%	5.0%	15.0%	15.2%
UREE leverage ratio	1.5%	0.0%	1.5%	8.2%	8.9%

The details for the amounts used in the calculation of the regulatory capital ratios as of September 30, 2020:

90 Day Average Balances (dollars in thousands)	<b>Common equity tier 1 ratio</b>	<b>Tier 1 capital ratio</b>	<b>Total capital ratio</b>	<b>Permanent capital ratio</b>
Numerator:				
Unallocated retained earnings	\$ 695,953	\$ 695,953	\$ 695,953	\$ 695,953
Common Cooperative Equities:				
Statutory minimum purchased borrower stock	26,402	26,402	26,402	26,402
Allocated equities held $\geq 7$ years	674,266	674,266	674,266	674,266
Nonqualified allocated equities not subject to retirement	-	-	-	-
Allowance for loan losses and reserve for credit losses subject to certain limitations	-	-	32,711	
Regulatory Adjustments and Deductions:				
Amount of allocated investments in other System institutions	(134,138)	(134,138)	(134,138)	(134,138)
Other regulatory required deductions	(2,016)	(2,016)	(2,016)	(2,016)
	<u>1,260,467</u>	<u>1,260,467</u>	<u>1,293,178</u>	<u>1,260,467</u>
Denominator:				
Risk-adjusted assets excluding allowance	8,736,959	8,736,959	8,736,959	8,736,959
Regulatory Adjustments and Deductions:				
Regulatory deductions included in total capital		-	-	-
Allowance for loan losses	-	-	-	(32,138)
	<u>8,736,959</u>	<u>8,736,959</u>	<u>8,736,959</u>	<u>8,704,821</u>

90 Day Average Balances (dollars in thousands)	<b>Tier 1 leverage ratio</b>	<b>UREE leverage ratio</b>
Numerator:		
Unallocated retained earnings	\$ 695,953	\$ 695,953
Common Cooperative Equities:		
Statutory minimum purchased borrower stock	26,402	-
Allocated equities held $\geq 7$ years	674,266	
Regulatory Adjustments and Deductions:		
Amount of allocated investments in other System institutions	(134,138)	(9,894)
Other regulatory required deductions	(2,016)	(2,016)
	<u>1,260,467</u>	<u>684,043</u>
Denominator:		
Total Assets	8,558,352	8,558,352
Regulatory Adjustments and Deductions:		
Regulatory deductions included in tier 1 capital	(182,335)	(182,335)
	<u>8,376,017</u>	<u>8,376,017</u>

The association's accumulated other comprehensive income (loss) relates entirely to its nonpension other postretirement benefits. Amortization of prior service (credits) cost and of actuarial (gain) loss are reflected in "Salaries and employee benefits" in the Consolidated Statement of Comprehensive Income. The following table summarizes the changes in accumulated other comprehensive income (loss) for the nine months ended September 30:

	<b>2020</b>	<b>2019</b>
Accumulated other comprehensive (loss) at January 1	\$ (2,923)	\$ (79)
Amortization of prior service (credit) included in salaries and employee benefits	(138)	(137)
Amortization of actuarial loss included in salaries and employee benefits	128	-
Other comprehensive (loss), net of tax	(10)	(137)
Accumulated other comprehensive (loss) at September 30	<u>\$ (2,933)</u>	<u>\$ (216)</u>

## NOTE 6 — INCOME TAXES:

The association conducts its business activities through two wholly-owned subsidiaries. Long-term mortgage lending activities are conducted through a wholly-owned FLCA subsidiary which is exempt from federal and state income tax. Short- and intermediate-term lending activities are conducted through a wholly-owned PCA subsidiary. The PCA subsidiary and the ACA holding company are subject to income tax. The association operates 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 dividends in the form of cash, stock or allocated retained earnings. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage dividends. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized.

## NOTE 7 — FAIR VALUE MEASUREMENTS:

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 15 to the 2019 Annual Report to Stockholders for a more complete description.

Assets and liabilities measured at fair value on a recurring basis, which are measured at fair value at the end of each reporting period on the association's consolidated balance sheet, are summarized below. The association did not have any liabilities measured at fair value on a recurring basis.

<b>September 30, 2020</b>	<b>Fair Value Measurement Using</b>			<b>Total Fair Value</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Assets:				
Assets held in nonqualified benefit trusts	\$ 9,113	\$ -	\$ -	\$ 9,113
Total assets	\$ 9,113	\$ -	\$ -	\$ 9,113
<b>December 31, 2019</b>	<b>Fair Value Measurement Using</b>			<b>Total Fair Value</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Assets:				
Assets held in nonqualified benefit trusts	\$ 8,293	\$ -	\$ -	\$ 8,293
Total assets	\$ 8,293	\$ -	\$ -	\$ 8,293

Assets and liabilities measured at fair value on a nonrecurring basis, which are fair value measurements that are triggered by particular circumstances such as impaired assets, for each of the fair value hierarchy levels are summarized below. The association did not have any liabilities measured at fair value on a nonrecurring basis.

<b>September 30, 2020</b>	<b>Fair Value Measurement Using</b>			<b>Total Fair Value</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Assets:				
Loans	\$ -	\$ -	\$ 10,648	\$ 10,648
Other property owned	-	-	405	405
<b>December 31, 2019</b>	<b>Fair Value Measurement Using</b>			<b>Total Fair Value</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Assets:				
Loans	\$ -	\$ -	\$ 10,957	\$ 10,957
Other property owned	-	-	942	942

Loans represents the fair value of certain loans that were evaluated for impairment under the authoritative guidance "Accounting by Creditors for Impairment of a Loan." The fair value was based upon the underlying collateral since these were collateral-dependent loans for which real estate is the collateral. With regard to nonrecurring measurements for impaired loans and other property owned, it is not practicable to provide specific information on inputs, as each collateral property is unique. System institutions utilize

appraisals to value these loans and other property owned and take into account unobservable inputs, such as income and expense, comparable sales, replacement cost and comparability adjustments.

## **Valuation Techniques**

As more fully discussed in Note 15 to the 2019 Annual Report to Stockholders, authoritative guidance 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. The following represents a brief summary of the valuation techniques used for the association's assets and liabilities. For a more complete description, see Notes to the 2019 Annual Report to Stockholders.

### *Investments*

Include mortgage-backed securities issued by the Federal Agricultural Mortgage Corporation (Farmer Mac). Fair values are estimated using discounted cash flows considering market interest rates, estimated prepayment rates, probabilities of default and loss severities. Inputs depend significantly on management judgements and experience with the securities. These fair value measurements are classified as level 3 investments.

### *Assets Held in Nonqualified Benefits Trusts*

Assets held in trust funds related to deferred compensation and supplemental retirement plans are classified within Level 1. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

### *Standby Letters of Credit*

The fair value of letters of credit approximate the fees currently charged for similar agreements or the estimated cost to terminate or otherwise settle similar obligations.

### *Loans Evaluated for Impairment*

For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon the underlying collateral since the loans are collateral-dependent loans for which real estate is the collateral. 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, a majority of these loans have fair value measurements that fall within Level 3 of the fair value hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established. The fair value of these loans would fall under Level 2 of the hierarchy if the process uses independent appraisals and other market-based information.

### *Other Property Owned*

Other property owned is generally classified as Level 3 of the fair value hierarchy. The process for measuring the fair value of the other property owned involves the use of independent appraisals and other market-based information. Costs to sell represent transaction costs and are not included as a component of the asset's fair value. As a result, these fair value measurements fall within Level 3 of the hierarchy.

### *Cash*

For cash, the carrying amount is a reasonable estimate of fair value.

### *Loans*

Fair value is estimated by discounting the expected future cash flows using the associations' current interest rates at which similar loans would be made to borrowers with similar credit risk. The discount rates are based on the associations' current loan origination rates as well as management's estimates of credit risk. Management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale and could be less.

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

The fair value of loans in nonaccrual status that are current as to principal and interest is estimated as described above, with appropriately higher interest rates which reflect the uncertainty of continued cash flows. For collateral-dependent impaired loans, it is assumed that collection will result only from the disposition of the underlying collateral.

*Commitments to Extend Credit*

The fair value of commitments is estimated using the fees currently charged for similar agreements, taking into account the remaining terms of the agreements and the creditworthiness of the counterparties. For fixed-rate loan commitments, estimated fair value also considers the difference between current levels of interest rates and the committed rates.

**NOTE 8 — EMPLOYEE BENEFIT PLANS:**

The following table summarizes the components of net periodic benefit costs of nonpension other postretirement employee benefits for the three and nine months ended September 30:

	For the three months ended		For the nine months ended	
	September 30		September 30	
	Other Benefits		Other Benefits	
	2020	2019	2020	2019
Service Cost	\$ 92	\$ 86	\$ 278	\$ 257
Interest Cost	224	269	671	804
Expected return on plan assets	-	-	-	-
Amortization of prior service (credits)	(46)	(46)	(138)	(137)
Amortization of net actuarial loss	43	-	128	-
Net periodic benefit cost	<u>\$ 313</u>	<u>\$ 309</u>	<u>\$ 939</u>	<u>\$ 924</u>

The association’s liability for the unfunded accumulated obligation for these benefits at September 30, 2020, was \$26,699 and is included in “Unfunded post-retirement medical obligations” in the balance sheet.

The structure of the district’s defined benefit pension plan is characterized as multiemployer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (bank and associations). The association recognizes its amortized annual contributions to the plan as an expense. Contributions due and unpaid are recognized as a liability. For the DB plan, the association recognized costs of \$1,376 and \$1,760 for the nine months ended September 30, 2020 and 2019. The association previously disclosed in its financial statements for the year ended December 31, 2019, that it expected to contribute \$813 to the district’s defined benefit pension plan in 2020. As of September 30, 2020, \$717 of contributions have been made. The association presently anticipates contributing an additional \$96 to fund the defined benefit pension plan in 2020 for a total of \$813.

The association’s contributions to the DC Plan are expensed as incurred. For the nine months ended September 30, 2020 and 2019, the association recognized pension costs of \$2,185 and \$2,019, respectively.

Employees are also eligible to participate in the Farm Credit Benefits Alliance 401(k) Plan. Contributions to the 401(k) plan are expensed as incurred. For the nine months ended September 30, 2020 and 2019, the association contributed \$1,719 and \$1,656, respectively.

The association also participates in a defined contribution nonqualified supplemental 401(k) plan. The total expenses of the nonqualified plan included in the association’s employee benefit costs were \$705 and \$554 for the nine months ended September 30, 2020 and 2019, respectively.

**NOTE 9 — COMMITMENTS AND CONTINGENT LIABILITIES:**

The association is involved in various legal proceedings in the normal course of business. In the opinion of legal counsel and management, there are no legal proceedings at this time that are likely to materially affect the association.

**NOTE 10 — SUBSEQUENT EVENTS:**

The association has evaluated subsequent events through November 5, 2020, which is the date the financial statements were issued and there are no other significant events requiring disclosure as of this date.