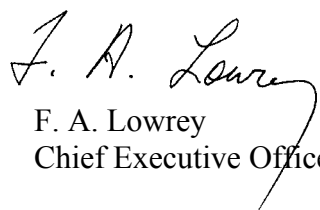



THIRD QUARTER 2003

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F. A. Lowrey
Chief Executive Officer


Paul Lemoine
Chairman of the Board

October 29, 2003

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

(dollars in thousands, except as noted)

The following discussion reviews the combined financial condition and results of operations of AgFirst Farm Credit Bank (AgFirst) and the District Agricultural Credit Associations (ACAs or District Associations), collectively referred to as the District, for the three months and nine months ended September 30, 2003. These comments should be read in conjunction with the accompanying financial statements and the 2002 Annual Report of AgFirst Farm Credit Bank and District Associations.

As of January 1, 2003, the District consisted of AgFirst, its subsidiary (the Farm Credit Finance Corporation of Puerto Rico) and twenty-four Agricultural Credit Associations.

FINANCIAL OVERVIEW

- Net income for the three months ended September 30, 2003 was \$78,849, a decrease of \$3,128 or 3.82 percent, compared to the three months ended September 30, 2002. Net income for the nine months ended September 30, 2003 was \$244,203 an increase of \$7,876 or 3.33 percent, compared to the same period ended September 30, 2002. The three-month decrease was primarily attributed to the \$9,672 increase in noninterest expense, and a \$1,840 increase in provision for income taxes. These increases were offset by a decrease of \$5,437 in provision for loan losses, an increase of \$2,339 in net interest income, and an increase of \$608 in noninterest income. The year-to-date increase in net income was primarily attributed to the \$29,880 increase in net interest income, an \$8,185 increase in noninterest income and a decrease of \$5,180 in provision for loan losses. These increases were offset by an increase of \$36,081 in noninterest expense.
- Total assets at September 30, 2003 increased \$1,429,496, or 8.70 percent compared to December 31, 2002. This increase was primarily attributed to increased loan and investment volume.
- Bonds and notes outstanding at September 30, 2003 increased \$1,262,802, or 9.33 percent, in order to fund the additional loan and investment volume.

Key ratios and data reported below, and in the accompanying financial statements, address the financial performance of the District in more detail. The nine months' results of operations are not indicative of an entire year due to the seasonal nature of a portion of the District's assets.

FINANCIAL CONDITION

Loan Portfolio

Gross loan volume at September 30, 2003 was \$14,158,481, an increase of \$335,392 or 2.43 percent as compared to December 31, 2002, and an increase of \$599,913 or 4.42 percent compared to September 30, 2002. The moderate increase in loans outstanding is the result of a significant increase in Association loans, offset by a decrease in AgFirst's net participations and secondary mortgage market loans outstanding.

Loan volume classified as Acceptable (which includes Other Assets Especially Mentioned) as of September 30, 2003 remained relatively consistent compared to December 31, 2002 and September 30, 2002. Other Assets Especially Mentioned loan assets are considered fully collectible but have potential weaknesses. Nonaccrual loan assets for the combined District at September 30, 2003 were .85 percent of total loans outstanding as compared to .82 percent at December 31, 2002 and .88 percent at September 30, 2002.

The allowance for loan losses at September 30, 2003 of \$316,494, or 2.24 percent of gross loan volume, is considered by management to be adequate to absorb potential losses on existing loans. Refer to Note 2, "Allowance for Loan Losses," in the notes to the combined financial statements of this report for further information.

Associations report that Hurricane Isabel's damage was not significant except in some very localized areas. Throughout the District, crop reports are generally positive, with most crops producing better-than-average yields and favorable harvesting conditions.

LIQUIDITY AND FUNDING SOURCES

As of September 30, 2003, AgFirst and all District Associations exceeded all regulatory liquidity requirements. Cash, cash equivalents and investment securities totaled \$3,661,082 or 20.50 percent of total assets at September 30, 2003, compared to \$2,597,575 or 15.81 percent as of December 31, 2002. At September 30, 2003, the Bank had 162 days of coverage as defined by the System's common liquidity policy.

Interest-bearing liabilities, consisting of bonds and notes, increased by \$1,262,802, or 9.33 percent, compared to bonds and notes outstanding at December 31, 2002. Interest-bearing liabilities increased primarily due to the increase in loan and investment volume previously mentioned.

Effective July 1, 2003, AgFirst adopted SFAS No. 150, “*Accounting for Certain Financial Instruments with Similar Characteristics of Both Liabilities and Equity*,” which requires that its Series 1 Preferred Stock (mandatorily redeemable) be classified as a liability rather than as a component of equity, and that the related dividends incurred subsequent to June 30, 2003 be classified as a component of interest expense.

Capital Resources

Total District shareholders’ equity increased \$149,007 from December 31, 2002 to September 30, 2003. The increase was primarily the result of \$244,203 in net income and stock issuances of \$12,408, which was partially offset by retirements of surplus of \$75,164 and stock of \$13,720, patronage distributions of \$8,599, accrued/paid dividends of \$9,690, and a decrease in accumulated other comprehensive loss of \$1,275.

On October 14, 2003, AgFirst issued \$150,000 of Class A Perpetual Non-Cumulative Preferred Stock, Series 2. Dividends on the stock are non-cumulative and will be payable semi-annually in arrears on the fifteenth day of June and December in each year, commencing December 15, 2003, at an annual rate equal to 7.30 percent of the par value of \$1 thousand per share. In the event dividends are not declared on the Series 2 Preferred Stock for payment on any dividend Payment Date, then such dividends shall not cumulate and shall cease to accrue and be payable.

Key financial condition comparisons:

| | 9/30/03 | 12/31/02 |
|---|---------|----------|
| Shareholders’ Equity to Assets | 13.61% | 13.88% |
| Total Liabilities to Shareholders’ Equity | 6.26:1 | 6.10:1 |
| Allowance for Loan Losses to Loans | 2.24% | 2.25% |

RESULTS OF OPERATIONS

Net Interest Income

Net interest income for the three months ended September 30, 2003 was \$142,074, an increase of \$2,339 or 1.67 percent compared to the three months ended September 30, 2002. Net interest income for the nine months ended September 30, 2003 was \$434,515, an increase of \$29,880 or 7.38 percent compared to the same period ended September 30, 2002. The increase is primarily attributed to the increase in loans and investments, offset somewhat by the reclassification of preferred stock dividends as interest expense and a lessening of the impact derived from debt called during prior periods (discussed below).

As noted above, interest expense for the three- and nine-month periods ended September 30, 2003 includes \$4,721 of dividend expense related to preferred stock, which was characterized as “true dividends” in prior periods. This “reclassification” had a negative impact on spread and net interest margin.

AgFirst executed call options (trend began in 2001) on a significant volume of fixed-rate debt through July 2003, replacing the called debt with lower-cost, fixed-rate debt. Loan prepayment activity somewhat offset a portion of the benefit achieved by calling debt, but the efficiency of calling large blocks of debt resulted in significant improvement in net interest margin. Profitability is expected to return to lower, more typical levels in a stable-to-rising rate environment as asset prepayments “catch up” to called debt levels, or as the assets and underlying funding mature or reprice in the normal course of business.

Provision for Loan Losses

The provision for loan losses for the third quarter of 2003 was \$(280), as compared to \$5,155 for the same period of the prior year. The provision for loan losses for the nine months ended September 30, 2003 was \$8,804, as compared to \$13,982 for the same period of the prior year. The provision reversal recorded during the three months ended September 30, 2003 was primarily the result of three Associations recording minimal reversals of provision based on the determination that reduced credit risk within their individual portfolios warranted a reduction in their allowance for loan losses.

Noninterest Income

Noninterest income for the three months ended September 30, 2003 was \$12,197, an increase of \$608 compared to the three months ended September 30, 2002. Noninterest income for the nine months ended September 30, 2003 was \$41,333, an increase of \$8,185 as compared to the nine months ended September 30, 2002. The three-month increase was primarily attributed to an increase in loan fees, financially related services, and other miscellaneous income. These increases were offset by a decrease in realized gains on investments. The year-to-date increase was due primarily to increases of \$5,726 in fees related to secondary mortgage market and participation loan activity, a \$2,696 net positive variance in net realized losses on investments (a \$2,467 loss in 2002 compared to recoveries of \$229 recorded in 2003), \$881 in financially related services, and \$1,319 in miscellaneous income, which is in part related to \$900 in dividend income from other Farm Credit Institutions. These increases were offset by a decrease of \$2,437 in income related to District Association federal tax settlement refunds received in the first nine months of 2002.

Noninterest Expense

Noninterest expense for the three and nine months ended September 30, 2003 was \$75,686 and \$222,883, respectively, an increase of \$9,672 and \$36,081, respectively, as compared to the corresponding periods in 2002. The three-month increase was primarily attributed to the increases of salaries and employee benefits related to SFAS No. 87, “Employers’ Accounting for Pension,” (FAS 87) of \$2,454, SFAS No. 106, “Employers’ Accounting for Postretirement Benefits Other than Pensions,” (FAS 106) of \$1,347, and salaries and other employee benefits (excluding FAS 87 & FAS 106) of \$2,733. In addition, there was \$4,667 in losses on the sale of rural home loans compared to none realized in 2002, and \$986 in unrealized net losses on secondary mortgage market (SMM) activity that did not occur in 2002. Also, the Farm Credit System Insurance Corporation (FCSIC) had a \$3,048 increase in premiums. These increases were offset by decreases of \$3,205 in called debt expense and \$1,817 in Intra-system financial assistance (FAC) expense. The decrease in called debt expense is the result of increasing interest rates, resulting in a sharp decrease in “in the money” call options. The decrease in FAC expense relates to the retirement of a bond in July 2003.

The nine-month increase was due in part to the increases of \$7,607 in FAS 87 expense and \$3,972 in FAS 106 expense, \$6,063 in salaries and other employee benefits (excluding FAS 87 and FAS 106), \$3,048 in called debt expense and \$9,100 in FCSIC premiums. In addition, during 2003, realized gains related to the sale of rural home loans decreased \$4,358 from 2002, mortgage servicing rights were written down by \$3,000 to reflect current market value and \$986 was recorded in net unrealized losses related to SMM activity. These increases were offset by the \$2,102 decrease in purchased services related to District-wide projects. Purchased service fees incurred in the current nine-month period have primarily been related to projects such as the implementation of PeopleSoft Financial Suite, which are deferred until completion of the first implementation phase.

Provision for Income Taxes

The provision (benefit) for income taxes for the three and nine months ended September 30, 2003 was \$17 and \$(41), respectively. This represents a decrease in tax benefit of \$1,840 for the quarter and a decrease in provision of \$712 for year-to-date compared to the same periods in 2002. The variance for the quarter would be primarily attributed to the majority of IRS tax settlement refunds received during 2002 as compared to 2003.

Key results of operations comparisons:

| | Annualized for the nine months ended 9/30/03 | For the year ended 12/31/02 |
|--|---|--|
| Return on Average Assets | 1.94% | 2.04% |
| Return on Average Shareholders’ Equity | 13.46% | 13.28% |
| Net Interest Income as a Percentage of Average Earning Assets | 3.45% | 3.63% |
| Chargeoffs, Net of (Recoveries), to Average Loans | .03% | .12% |

Combined Balance Sheets

| <i>(dollars in thousands)</i> | September 30, 2003 <i>(unaudited)</i> | December 31, 2002 |
|--|---|----------------------|
| Assets | | |
| Cash and cash equivalents | \$ 550,600 | \$ 444,457 |
| Investment securities | 3,110,482 | 2,153,118 |
| Loans | 14,158,481 | 13,823,089 |
| Less: allowance for loan losses | 316,494 | 311,180 |
| Net loans | 13,841,987 | 13,511,909 |
| Accrued interest receivable | 158,626 | 131,638 |
| Investments in other Farm Credit System institutions | 18,667 | 18,736 |
| Premises and equipment, net | 83,868 | 77,361 |
| Other property owned | 3,092 | 4,828 |
| Other assets | 89,175 | 84,954 |
| Total assets | <u>\$ 17,856,497</u> | <u>\$ 16,427,001</u> |
| Liabilities | | |
| Bonds and notes | \$ 14,801,338 | \$ 13,538,536 |
| Mandatorily redeemable preferred stock* | 225,000 | — |
| Accrued interest payable | 52,807 | 43,733 |
| Dividends and patronage refunds payable | 11,026 | 64,180 |
| Postretirement benefits other than pensions | 76,425 | 67,193 |
| Pension liability | 61,871 | 61,822 |
| Other liabilities | 198,467 | 145,142 |
| Total liabilities | <u>15,426,934</u> | <u>13,920,606</u> |
| Commitments and contingencies | | |
| Mandatorily redeemable preferred stock* | <u>—</u> | <u>225,839</u> |
| Shareholders' Equity | | |
| Protected borrower equity | 12,724 | 15,486 |
| Capital stock and participation certificates | 126,033 | 124,541 |
| Retained earnings | | |
| Allocated | 688,485 | 756,525 |
| Unallocated | 1,711,701 | 1,494,659 |
| Accumulated other comprehensive loss | (109,380) | (110,655) |
| Total shareholders' equity | <u>2,429,563</u> | <u>2,280,556</u> |
| Total liabilities and equity | <u>\$ 17,856,497</u> | <u>\$ 16,427,001</u> |

* Beginning July 1, 2003, term preferred stock is required to be reported prospectively as a liability in accordance with Statement of Financial Accounting Standards No. 150.

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

Combined Statements of Income

(unaudited)

| <i>(dollars in thousands)</i> | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|---|-----------|--|------------|
| | 2003 | 2002 | 2003 | 2002 |
| Interest Income | | | | |
| Investment securities | \$ 12,615 | \$ 15,029 | \$ 44,064 | \$ 48,054 |
| Loans | 200,350 | 211,493 | 601,718 | 631,261 |
| Total interest income | 212,965 | 226,522 | 645,782 | 679,315 |
| Interest Expense | 70,891 | 86,787 | 211,267 | 274,680 |
| Net interest income | 142,074 | 139,735 | 434,515 | 404,635 |
| Provision for loan losses | (281) | 5,156 | 8,803 | 13,983 |
| Net interest income after provision for loan losses | 142,355 | 134,579 | 425,712 | 390,652 |
| Noninterest Income | | | | |
| Loan fees | 9,238 | 8,529 | 30,829 | 25,103 |
| Fees for financially related services | 1,484 | 1,211 | 3,632 | 2,751 |
| Interest related to IRS refunds | — | 189 | 67 | 2,504 |
| Realized gains (losses) on investments, net | 29 | 320 | 229 | (2,467) |
| Miscellaneous | 1,446 | 1,340 | 6,576 | 5,257 |
| Total noninterest income | 12,197 | 11,589 | 41,333 | 33,148 |
| Noninterest Expenses | | | | |
| Salaries and employee benefits | 42,128 | 35,594 | 125,585 | 107,943 |
| Occupancy and equipment | 5,845 | 5,873 | 17,217 | 16,767 |
| Insurance Fund premium | 4,077 | 1,029 | 12,120 | 3,020 |
| Other operating expenses | 14,415 | 14,981 | 40,493 | 42,595 |
| Intra-System financial assistance expenses | 2,036 | 3,853 | 11,342 | 11,450 |
| Called debt expense | 1,154 | 4,359 | 11,318 | 8,270 |
| Impairment of servicing assets | — | — | 3,000 | — |
| Loss (gain) on sale of rural home loans | 4,667 | — | (243) | (4,601) |
| Unrealized loss on SMM activity, net | 986 | — | 986 | — |
| Miscellaneous | 378 | 325 | 1,065 | 1,358 |
| Total noninterest expenses | 75,686 | 66,014 | 222,883 | 186,802 |
| Income before income taxes | 78,866 | 80,154 | 244,162 | 236,998 |
| Provision (benefit) for income taxes | 17 | (1,823) | (41) | 671 |
| Net income | \$ 78,849 | \$ 81,977 | \$ 244,203 | \$ 236,327 |

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

Combined Statements of Changes in Preferred Stock and Shareholders' Equity

(unaudited)

| | Preferred Stock | Protected Borrower Equity | Capital Stock and Participation Certificates | Retained Earnings | | Accumulated Other Comprehensive Income | Total Preferred Stock and Shareholders' Equity |
|--|-----------------|---------------------------|--|-------------------|--------------|--|--|
| | | | | Allocated | Unallocated | | |
| <i>(dollars in thousands)</i> | | | | | | | |
| Balance at December 31, 2001 | \$225,839 | \$ 19,261 | \$ 127,271 | \$ 733,378 | \$ 1,393,592 | \$ 7,041 | \$ 2,506,382 |
| Comprehensive income | | | | | | | |
| Net income | | | | | 236,327 | | 236,327 |
| Unrealized gains (losses) on investments available for sale | | | | | | 10,180 | 10,180 |
| Change in fair value of derivative instruments | | | | | | (14,309) | (14,309) |
| Total comprehensive income | | | | | | | 232,198 |
| Protected borrower equity retired | | (3,230) | | | | | (3,230) |
| Capital stock/participation certificates issued/retired, net | | | (2,820) | | | | (2,820) |
| Dividends declared/paid | | | 68 | | (149) | | (81) |
| Preferred stock dividends accrued | 14,164 | | | | (14,164) | | — |
| Preferred stock dividends paid | (9,443) | | | | | | (9,443) |
| Patronage distribution | | | | | | | |
| Cash | | | | | (7,995) | | (7,995) |
| Nonqualified allocated retained earnings | | | | | | | — |
| Retained earnings retired | | | | (69,430) | | | (69,430) |
| Patronage distribution adjustment | | | | 2,660 | (1,754) | | 906 |
| Balance at September 30, 2002 | \$230,560 | \$ 16,031 | \$ 124,519 | \$ 666,608 | \$ 1,605,857 | \$ 2,912 | \$ 2,646,487 |
| Balance at December 31, 2002 | \$225,839 | \$ 15,486 | \$ 124,541 | \$ 756,525 | \$ 1,494,659 | \$(110,655) | \$ 2,506,395 |
| Comprehensive income | | | | | | | |
| Net income | | | | | 244,203 | | 244,203 |
| Unrealized gains (losses) on investments available for sale | | | | | | 1,940 | 1,940 |
| Change in fair value of derivative instruments | | | | | | (693) | (693) |
| Pension liability | | | | | | 28 | 28 |
| Total comprehensive income | | | | | | | 245,478 |
| Protected borrower equity retired | | (2,762) | | | | | (2,762) |
| Capital stock/participation certificates issued/retired, net | | | 1,450 | | | | 1,450 |
| Dividends declared/paid | | | 42 | | (289) | | (247) |
| Reclass of preferred stock to liabilities | (225,839) | | | | | | (225,839) |
| Preferred stock dividends accrued | 9,443 | | | | (9,443) | | — |
| Preferred stock dividends paid | (9,443) | | | | | | (9,443) |
| Patronage distribution | | | | | | | |
| Cash | | | | | (8,599) | | (8,599) |
| Allocated retained earnings | | | | 2,466 | (2,466) | | — |
| Retained earnings retired | | | | (75,164) | | | (75,164) |
| Patronage distribution adjustment | | | | 4,658 | (6,364) | | (1,706) |
| Balance at September 30, 2003 | \$ — | \$ 12,724 | \$ 126,033 | \$ 688,485 | \$ 1,711,701 | \$(109,380) | \$ 2,429,563 |

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

Combined Statements of Cash Flows

(unaudited)

| | For the nine months ended September 30, | |
|---|--|--------------|
| (dollars in thousands) | 2003 | 2002 |
| Cash flows from operating activities: | | |
| Net income | \$ 244,203 | \$ 236,327 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation on premises and equipment | 9,487 | 8,915 |
| Provision for loan losses | 8,803 | 13,983 |
| (Gains) losses on other property owned, net | 291 | (283) |
| Realized (gains) losses on investments, net | (229) | 2,467 |
| Realized (gains) losses on mortgage loans held for sale | (243) | (4,601) |
| Proceeds from sale of mortgage loans held for sale | 756,231 | 433,016 |
| Purchase of mortgage loans held for sale (net of principal repayment) | (863,098) | (568,164) |
| Changes in operating assets and liabilities: | | |
| (Increase) decrease in accrued interest receivable | (26,988) | (29,040) |
| (Increase) decrease in investments in other Farm Credit System institutions | 69 | (811) |
| (Increase) decrease in other assets | (4,221) | 12,410 |
| Increase (decrease) in accrued interest and preferred stock dividend payable | 8,235 | (12,330) |
| Increase (decrease) in other liabilities | 62,179 | (38,744) |
| Total adjustments | (49,484) | (183,182) |
| Net cash provided by (used in) operating activities | 194,719 | 53,145 |
| Cash flows from investing activities: | | |
| Investment securities purchased | (3,735,308) | (1,617,922) |
| Investment securities sold or matured | 2,780,113 | 1,758,263 |
| Net (increase) decrease in loans | (235,672) | (558,393) |
| Purchase of premises and equipment, net | (15,994) | (10,693) |
| Proceeds from sale of other property owned | 5,801 | 2,731 |
| Net cash provided by (used in) investing activities | (1,201,060) | (426,014) |
| Cash flows from financing activities: | | |
| Bonds and notes issued | 42,432,489 | 36,355,365 |
| Bonds and notes retired | (41,170,380) | (35,823,529) |
| Protected borrower equity retired | (2,762) | (3,230) |
| Capital stock and participation certificates issued/retired, net | 1,450 | (2,820) |
| Patronage refunds and dividends paid | (63,706) | (67,414) |
| Dividends paid on preferred stock | (9,443) | (9,443) |
| Retained earnings retired | (75,164) | (69,430) |
| Net cash provided by (used in) financing activities | 1,112,484 | 379,499 |
| Net increase (decrease) in cash and cash equivalents | 106,143 | 6,630 |
| Cash and cash equivalents, beginning of period | 444,457 | 339,541 |
| Cash and cash equivalents, end of period | \$ 550,600 | \$ 346,171 |
| Supplemental schedule of non-cash investing and financing activities: | | |
| Financed sales of other property owned | \$ 612 | \$ 999 |
| Loans transferred to other property owned | 4,513 | 3,556 |
| Patronage refund and dividends payable | 8,846 | 17,519 |
| Non-cash changes related to hedging activities: | | |
| Decrease (increase) in loans | \$ 1,781 | \$ (1,824) |
| Increase (decrease) in bonds and notes | 2,459 | (9,320) |
| Decrease (increase) in other assets | 3,108 | 10,129 |
| Increase (decrease) in other liabilities | (553) | 1,350 |
| Supplemental information: | | |
| Interest paid | \$ 202,193 | \$ 287,010 |
| Taxes paid, net | 2,787 | (5,772) |

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

Notes to the Combined Financial Statements

(dollars in thousands, except as noted)
(unaudited)

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

The accompanying combined financial statements include the accounts of AgFirst Farm Credit Bank (AgFirst) and the accounts of the District Agricultural Credit Associations (ACAs or District Associations), collectively referred to as the District, and reflect the investments in and allocated earnings of the service organizations in which AgFirst has a partial ownership interest. All significant transactions and balances among AgFirst and the District Associations have been eliminated in combination.

The significant accounting policies followed and the financial condition and results of operations of the combined Bank as of and for the year ended December 31, 2002, are contained in the 2002 Annual Report to Stockholders. These unaudited third quarter 2003 financial statements should be read in conjunction with the 2002 Annual Report to Stockholders.

In May 2003, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity* (SFAS No. 150 or the Statement). The Statement requires that certain instruments having characteristics of both liabilities and equity be classified as liabilities effective July 1, 2003. The Statement is to be implemented by reporting the cumulative effect of a change in accounting principle for financial instruments created before the issue date of the Statement and still existing at the beginning of the interim period of adoption. Restatement is not permitted.

Prior to the implementation of SFAS No. 150, the mandatorily redeemable preferred stock issued by AgFirst in May 2001 in the amount of \$225 million (225,000 shares) was classified as mezzanine equity (between the liability section and the equity section of the financial statement of position) and was considered to be a component of capital for certain regulatory ratios. The dividends accrued and paid on the preferred stock were charged directly to unallocated surplus. Effective July 1, 2003, the preferred stock was reclassified as a liability and dividends are recorded in interest expense prospectively. However, it will continue to be treated as a component of capital in the Bank's regulatory ratios.

The accompanying financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with accounting principles generally accepted in the United States of America (GAAP). The results for the nine months ended September 30, 2003 are not necessarily indicative of the results to be expected for the year ending December 31, 2003.

The District maintains allowances for loan losses in accordance with GAAP. The loan portfolios are reviewed quarterly to determine the adequacy of the allowances for losses. As of September 30, 2003, the allowances for losses are adequate in management's opinion to provide for possible losses on existing loans.

NOTE 2 — ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses follows:

| | |
|--|-------------------|
| Balance at 12-31-01 | \$ 301,615 |
| Provision for loan losses | 13,983 |
| Loans (charged off), net of recoveries | <u>(14,906)</u> |
| Balance at 9-30-02 | <u>\$ 300,692</u> |
| | |
| Balance at 12-31-02 | \$ 311,180 |
| Provision for loan losses | 8,803 |
| Loans (charged off), net of recoveries | <u>(3,489)</u> |
| Balance at 9-30-03 | <u>\$ 316,494</u> |

NOTE 3 — COMMITMENTS AND CONTINGENT LIABILITIES

Under the Farm Credit Act of 1971, each System bank is primarily liable for its portion of Systemwide bond and discount note obligations. Additionally, the banks are contingently liable for the Systemwide obligations of the System banks. The total consolidated Systemwide debt securities of the System were \$93.1 billion at September 30, 2003.

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

NOTE 4 — PREFERRED STOCK

On October 14, 2003, AgFirst issued \$150,000 of Class A Perpetual Non-Cumulative Preferred Stock, Series 2. Dividends on the stock are non-cumulative and will be payable semi-annually in arrears on the fifteenth day of June and December in each year, commencing December 15, 2003, at an annual rate equal to 7.30 percent of the par value of \$1 thousand per share. In the event dividends are not declared on the Series 2 Preferred Stock for payment on any dividend Payment Date, then such dividends shall not cumulate and shall cease to accrue and be payable.

NOTE 5 — BANK ONLY FINANCIAL DATA

Condensed financial information of AgFirst follows:

Balance Sheet Data

| | 9/30/03 | 12/31/02 (Audited) |
|--|----------------------|-----------------------|
| Cash and investment securities | \$ 3,644,715 | \$ 2,512,937 |
| Loans | 12,278,679 | 12,008,041 |
| Less: allowance for loan losses | 33,951 | 31,155 |
| Net loans | 12,244,728 | 11,976,886 |
| Other assets | 211,224 | 211,367 |
| Total assets | <u>\$ 16,100,667</u> | <u>\$ 14,701,190</u> |
| Bonds and notes | \$ 14,801,338 | \$ 13,538,536 |
| Mandatorily redeemable preferred stock * | 225,000 | — |
| Other liabilities | 190,792 | 179,970 |
| Total liabilities | <u>15,217,130</u> | <u>13,718,506</u> |
| Mandatorily redeemable preferred stock * | <u>—</u> | <u>225,839</u> |
| Capital stock and participation certificates | 249,083 | 249,444 |
| Retained earnings | 653,473 | 527,673 |
| Accumulated other comprehensive loss | (19,025) | (20,272) |
| Total shareholders' equity | <u>883,537</u> | <u>756,845</u> |
| Total liabilities and equity | <u>\$ 16,100,667</u> | <u>\$ 14,701,190</u> |

* Beginning July 1, 2003, term preferred stock is required to be reported prospectively as a liability in accordance with Statement of Financial Accounting Standards No. 150.

Statement of Income Data

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|--|---|------------------|--|-------------------|
| | 2003 | 2002 | 2003 | 2002 |
| Interest income | \$ 127,043 | \$ 151,556 | \$ 399,253 | \$ 463,643 |
| Interest expense | 70,875 | 86,781 | 211,202 | 274,656 |
| Net interest income | 56,168 | 64,775 | 188,051 | 188,987 |
| Provision for loan losses | <u>—</u> | <u>—</u> | <u>2,500</u> | <u>2,000</u> |
| Net interest income after provision for loan losses | 56,168 | 64,775 | 185,551 | 186,987 |
| Noninterest income (expense), net | <u>(17,658)</u> | <u>(15,989)</u> | <u>(50,302)</u> | <u>(43,598)</u> |
| Net income | <u>\$ 38,510</u> | <u>\$ 48,786</u> | <u>\$ 135,249</u> | <u>\$ 143,389</u> |