SECOND QUARTER 2001

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F. A. Lowrey

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Chief Executive Officer

F. Merrel Lust

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Chairman of the Board

July 25, 2001

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 *Ag***First** *Farm Credit Bank* (*Ag***First**) and the District Agricultural Credit Associations (ACAs or District Associations), collectively referred to as the District, for the three months and six months ended June 30, 2001. These comments should be read in conjunction with the accompanying financial statements and the 2000 Annual Report of *Ag***First** *Farm Credit Bank* and District Associations.

- Net income for the three months and six months ended June 30, 2001 was $79,111 and $142,172, respectively, an increase of $23,102 or 41.2 percent and $31,674 or 28.7 percent, compared to the same periods in 2000. The three month increase was primarily due to a $9,233 increase in net interest income, a $7,624 increase in noninterest income and a $7,872 decrease in provision for income taxes, which were partially offset by an increase in allowance for loan losses of $2,544. The year-to-date increase in net income was primarily attributed to an increase of $15,029 in net interest income, an increase of $13,160 in noninterest income, and a decrease of $9,699 in provision for income taxes, which were partially offset by an increase in provision for loan losses of $4,497 and an increase in noninterest expense of $1,717. Reference *Results of Operations* for additional details.

- Total assets at June 30, 2001 increased 5.86 percent compared to December 31, 2000. The $878,056 increase in loan volume and accrued interest was partially offset by a $118,321 decrease in investments and cash and cash equivalents. Other assets increased $37,204 from December 31, 2000 to June 30, 2001, which is primarily attributed to a $20,057 increase in accounts receivable related to District Association IRS settlement refunds and related interest, an increase of $9,405 for adjustments related to SFAS No. 133, "*Accounting for Derivative Instruments and Hedging Activities,*" an $8,472 increase in prepaid retirement, and an increase of $2,674 in deferred expenses related to the issuance of preferred stock.

- Total liabilities increased $508,841 or 4.5 percent as compared to December 31, 2000. Bonds and notes outstanding at June 30, 2001 increased $564,208 in order to fund the above noted additional loan volume. Additionally, *Ag***First** issued $225 million of mandatorily redeemable preferred stock, which also contributed to the funding of the additional loan volume (Refer to Note 4 for additional information). Other liabilities increased $22,126 from December 31, 2000, which was primarily attributed to a $41,308 increase in the short term funds held and an increase of $4,137 for adjustments related to SFAS No. 133, "*Accounting for Derivatives Instruments and Hedging Activities,*" which were partially offset by a $17,458 reduction in the controlled disbursement account (related to timing differences within loan activity) and a $7,784 reduction in payables from surplus retirement.

- Credit quality remained relatively consistent during the second quarter of 2001 compared to December 31, 2000 and June 30, 2000. Nonaccrual loan assets at June 30, 2001 were .58 percent of total loans outstanding as compared to .60 percent at December 31, 2000 and .87 percent at June 30, 2000.

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

DISTRICT OPERATIONS

As of January 1, 2001, the District consisted of *Ag***First**, its subsidiary (the Farm Credit Finance Corporation of Puerto Rico) and twenty-four District Associations. During the course of 2000, several District Associations consolidated and effective January 1, 2001, the one Production Credit Association (PCA) reorganized as an ACA. Consolidation/merger activity for 2000 and 2001 included:

- Tar Heel Farm Credit, ACA and East Carolina Farm Credit, ACA to form East Carolina Farm Credit, ACA – effective July 1, 2000
- Keystone Farm Credit, ACA, Delaware Farm Credit, ACA, Central Maryland Farm Credit, ACA, Marva Farm Credit, ACA, and Chesapeake Farm Credit, ACA to form MidAtlantic Farm Credit, ACA – effective July 1, 2000
- Edisto Farm Credit, ACA and Palmetto Farm Credit, ACA to form Palmetto Farm Credit, ACA – effective July 1, 2000
- West Virginia Farm Credit, ACA, Roanoke Farm Credit, ACA, Southwest Virginia Farm Credit, ACA, and Blue Ridge Farm Credit, ACA to form Farm Credit of the Virginias, ACA – effective January 1, 2001

FINANCIAL CONDITION

Loan Portfolio

Gross loan volume at June 30, 2001 was $11,964,106, a 7.83 percent increase over the December 31, 2000 amount of $11,095,176 and a 15.2 percent increase over the June 30, 2000 amount of $10,386,063. Loan asset growth continues to be consistent with the trend that began in the last quarter of 2000 as District Associations benefited from tightened conditions in the commercial bank market as well as a continuation of broader activity by both *Ag***First** and District Associations in participation loans originated by other Farm Credit institutions.

The allowance for loan losses at June 30, 2001 of $290,957 is 2.43 percent of gross loan volume and is considered by management to be adequate to absorb potential losses on existing loans information. Refer to Note 2, *"Allowance for Loan Losses"* in the notes to the combined financial statements of this report for further information.

Liquidity and Funding Sources

As of June 30, 2001, *Ag***First** and all District Associations exceeded all regulatory liquidity requirements. Cash and investment securities totaled $2,207,969, or 15.42 percent of total assets. Interest-bearing liabilities, consisting of bonds and notes, increased by $564,208, or 5.12 percent, compared to bonds and notes outstanding at December 31, 2000. Interest-bearing liabilities were increased in order to fund a portion of the increase in loan volume with the issuance of the preferred stock also contributing to the funding of the additional loan volume.

Capital Resources

Total shareholders' equity, excluding preferred stock, increased $58,274 from December 31, 2000 to June 30, 2001. This net increase was primarily the result of a $142,172 increase in retained earnings from net income, which was partially offset by retirements of surplus of $70,031 and stock retirements of $8,517.

Key financial condition comparisons:

	6/30/01	12/31/00
Shareholders' Equity* to Assets	15.50%	15.98%
Shareholders' Equity and Preferred Stock to Assets	17.08%	N/A
Allowance for Loan Losses to Loans	2.43%	2.57%

** Excludes preferred stock. (See Note 4.)*

RESULTS OF OPERATIONS

Net interest income for the three months and six months ended June 30, 2001 was $117,468 and $230,598, respectively, compared to $108,235 and $215,569 for the same periods of 2000. The increases in net interest income for both periods were primarily the result of higher average volume in earning assets.

Noninterest income for the three and six months ended June 30, 2001 was $13,616 and $24,836, respectively, an increase of $7,624 and $13,160 as compared to the same periods in 2000. The three month increase was primarily attributed to a $3,420 increase in loan fees, prepayment fee penalties, and financially related fees, and a $3,761 increase in other income related to interest on District ACA federal tax settlement refunds. The year-to-date increase was primarily attributed to a $4,807 increase in loan fees, prepayment fee penalties and fees for financially related services, $2,731 related to realized gains on sales of investments, and a $4,715 increase in other income related to interest on District ACA federal tax settlement refunds.

Noninterest expense for the three and six months ended June 30, 2001 was $52,102 and $109,275, respectively, a decrease of $917 and an increase of $1,717, respectively, as compared to the same periods in 2000. The three-month decrease was primarily attributed to a decrease of $3,583 in salaries and employee benefits that would be related to recent District Association merger and consolidation activity, which was partially offset by an increase of $1,774 in miscellaneous expenses related primarily to the write-off of unamortized expenses on called debt and an increase of $1,129 in other operating expenses. The year-to-date increase was primarily attributed to an increase of $3,246 in miscellaneous expenses related to called debt and an increase of $2,359 in other operating expenses, which were partially offset by a decrease of $3,761 in salaries and employee benefits attributed to recent District Association merger and consolidation activity.

The benefit for income taxes for the three months and six months ended June 30, 2001 was $(3,900) and $(2,576) respectively, decreases of $(7,872) and $(9,699), respectively, as compared to the same periods in 2000. The decreases in provision for income taxes for the periods were primarily attributed to the Associations' reorganization to form ACA Holding Company structures, which includes decreases in federal tax effective rates related to the formation of tax-exempt FLCAs and the recording of approximately $15 million in IRS settlement refunds year-to-date, both of which were offset by deferred tax assets adjustments of approximately $9 million.

Key results of operations comparisons:

	Annualized for the six months ended 6/30/01	For the year ended 12/31/00
Return on Average Assets	2.09%	1.85%
Return on Average Shareholders' Equity*	13.08%	11.05%
Net Interest Income as a Percentage of Average Earning Assets	3.41%	3.50%
Chargeoffs, Net of (Recoveries), to Average Loans	0.01%.	0.02%

** Excludes preferred stock. (See Note 4.)*

IRS TAX SETTLEMENT

District Agricultural Credit Associations have filed refund claims with the Internal Revenue Service asserting that earnings from their long-term mortgage lending activities are exempt from taxation. Settlement negotiations are in process to resolve this issue, which have resulted in refunds (or will in the future) of a portion of taxes previously paid.

The terms of the settlement agreements stipulate that income generated by ACAs will be taxable in future periods. However, ACAs may reorganize, with the approval of their stockholders and FCA, to operate their long-term mortgage lending activities through a newly created FLCA subsidiary. As of July 1, 2001, sixteen District Associations have reorganized as parent-subsidiary structures. As part of the settlement agreement, the IRS has confirmed that FLCAs formed in this manner are tax-exempt. Effective tax rates for ACAs should be reduced in future years as the reorganizations occur. For the six months ended June 30, 2001, $15,278 was recognized as ACA federal tax refund amounts and $4,715 was recognized as interest related to the federal tax refunds.

Combined Balance Sheets

(dollars in thousands)	June 30, 2001	December 31, 2000
	(unaudited)	
Assets		
Cash and cash equivalents	$ 274,812	$ 326,204
Investment securities	1,933,157	2,000,086
Loans	11,964,106	11,095,176
Less: allowance for loan losses	290,957	284,867
Net loans	11,673,149	10,810,309
Accrued interest receivable	188,254	179,128
Investments in other Farm Credit System institutions	18,401	18,275
Premises and equipment, net	72,916	68,555
Other property owned	3,987	6,369
Other assets	150,699	113,495
Total assets	$ 14,315,375	$ 13,522,421
Liabilities		
Bonds and notes	$ 11,578,765	$ 11,014,557
Accrued interest payable	95,190	120,708
Dividends and patronage refunds payable	6,875	58,850
Other liabilities	189,219	167,093
Total liabilities	11,870,049	11,361,208
Commitments and contingencies		
Preferred Stock (Note 4)	225,839	—
Shareholders' Equity		
Protected borrower equity	20,394	23,634
At-risk equity:		
Capital stock and participation certificates	127,579	132,856
Retained earnings		
Allocated	635,941	704,010
Unallocated	1,432,931	1,302,163
Accumulated other comprehensive income (loss)	2,642	(1,450)
Total shareholders' equity	2,219,487	2,161,213
Total liabilities and equity	$ 14,315,375	$ 13,522,421

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

Combined Statements of Income

(unaudited)

(dollars in thousands)	For the three months ended June 30, 2001	For the three months ended June 30, 2000	For the six months ended June 30, 2001	For the six months ended June 30, 2000
Interest Income				
Investment securities and other	$ 28,269	$ 35,973	$ 63,142	$ 71,253
Loans	239,492	227,558	483,878	444,604
Total interest income	267,761	263,531	547,020	515,857
Interest Expense	150,293	155,296	316,422	300,288
Net interest income	117,468	108,235	230,598	215,569
Provision for loan losses	3,771	1,227	6,563	2,066
Net interest income after provision for loan losses	113,697	107,008	224,035	213,503
Noninterest Income				
Loan fees	6,517	3,097	11,770	6,963
Fees for financially related services	1,139	1,048	2,052	1,942
Gains (losses) from other property owned, net	777	61	801	44
Realized gains (losses) on investments, net	89	—	2,731	—
Miscellaneous	5,094	1,786	7,482	2,727
Total noninterest income	13,616	5,992	24,836	11,676
Noninterest Expenses				
Salaries and employee benefits	29,398	32,981	64,495	68,256
Occupancy and equipment	4,826	4,792	9,980	9,553
Other operating expenses	12,556	11,427	24,520	22,161
Intra-System financial assistance expenses	3,484	3,755	6,904	7,458
Miscellaneous	1,838	64	3,376	130
Total noninterest expenses	52,102	53,019	109,275	107,558
Income before income taxes	75,211	59,981	139,596	117,621
Provision (benefit) for income taxes	(3,900)	3,972	(2,576)	7,123
Net income	$ 79,111	$ 56,009	$ 142,172	$ 110,498

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

Combined Statements of Changes in Shareholders' Equity

(unaudited)

(dollars in thousands)	Preferred Stock	Protected Borrower Equity	At-Risk Equity: Capital Stock and Participation Certificates	At-Risk Equity: Retained Earnings: Allocated	At-Risk Equity: Retained Earnings: Unallocated	At-Risk Equity: Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance at December 31, 1999	$ —	$ 28,297	$ 152,639	$ 659,297	$ 1,249,773	$ (11,034)	$ 2,078,972
Comprehensive income							
Net income					110,498		110,498
Unrealized gains (losses) on investments available for sale, net of reclassification adjustments						546	546
Total comprehensive income							111,044
Protected borrower equity retired		(3,818)					(3,818)
At-risk equity:							
Capital stock/participation certificates issued/retired, net			(22,705)				(22,705)
Dividends declared/paid			183		(438)		(255)
Patronage distribution							
Cash					(3,891)		(3,891)
Allocated retained earnings				4,330	(4,330)		—
Retained earnings retired				(55,874)			(55,874)
Patronage distribution adjustment				(741)	944		203
Balance at June 30, 2000	$ —	$ 24,479	$ 130,117	$ 607,012	$ 1,352,556	$ (10,488)	$ 2,103,676
Balance at December 31, 2000	$ —	$ 23,634	$ 132,856	$ 704,010	$ 1,302,163	$ (1,450)	$ 2,161,213
Comprehensive income							
Cumulative effect of a change in accounting for derivatives						(1,037)	(1,037)
Net income					142,172		142,172
Unrealized gains (losses) on investments available for sale and derivative instruments						5,129	5,129
Total comprehensive income							146,264
Preferred stock issued	225,000						225,000
Protected borrower equity retired		(3,240)					(3,240)
At-risk equity:							
Capital stock/participation certificates issued/retired, net			(5,465)				(5,465)
Dividends declared/paid	839		188		(2,711)		(1,684)
Patronage distribution							
Cash					(6,002)		(6,002)
Retained earnings retired				(70,031)			(70,031)
Patronage distribution adjustment				1,962	(2,691)		(729)
Balance at June 30, 2001	$225,839	$ 20,394	$ 127,579	$ 635,941	$ 1,432,931	$ 2,642	$ 2,445,326

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

Combined Statements of Cash Flows

(unaudited)

(dollars in thousands)	For the six months ended June 30, 2001	2000
Cash flows from operating activities:		
Net income	$ 142,172	$ 110,498
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation on premises and equipment	5,189	5,384
Provision for loan losses	6,563	2,066
(Gains) losses on other property owned, net	(801)	(44)
Realized (gains) losses on investments, net	(2,731)	—
Changes in operating assets and liabilities:		
(Increase) decrease in accrued interest receivable	(9,126)	(30,513)
(Increase) decrease in investments in other Farm Credit System institutions	(126)	(44)
(Increase) decrease in other assets	(37,204)	790
Increase (decrease) in accrued interest payable	(25,518)	3,571
Increase (decrease) in other liabilities	22,151	4,241
Total adjustments	(41,603)	(14,549)
Net cash provided by (used in) operating activities	100,569	95,949
Cash flows from investing activities:		
Investment securities purchased	(842,129)	(1,398,805)
Investment securities sold or matured	919,189	1,459,113
Net (increase) decrease in loans	(870,934)	(222,554)
Purchase of premises and equipment, net	(9,550)	(8,247)
Proceeds from sale of other property owned	4,689	2,572
Net cash provided by (used in) investing activities	(798,735)	(167,921)
Cash flows from financing activities:		
Bonds and notes issued	21,109,469	11,893,011
Bonds and notes retired	(20,548,569)	(11,814,167)
Preferred stock issued	225,000	—
Protected borrower equity retired	(3,240)	(3,818)
At-risk equity:		
Capital stock and participation certificates issued/retired, net	(5,465)	(22,705)
Patronage refunds and dividends paid	(58,921)	(49,111)
Dividends paid on preferred stock	(1,469)	—
Retained earnings retired	(70,031)	(55,874)
Net cash provided by (used in) financing activities	646,774	(52,664)
Net increase (decrease) in cash and cash equivalents	(51,392)	(124,636)
Cash and cash equivalents, beginning of period	326,204	391,515
Cash and cash equivalents, end of period	$ 274,812	$ 266,879
Supplemental schedule of non-cash investing and financing activities:		
Financed sales of other property owned	$ 467	$ 334
Loans transferred to other property owned	1,998	1,222
Patronage refund and dividends payable	7,686	4,146
Accrued dividends on preferred stock	839	—
Change in unrealized gains (losses) on investments and derivative instruments, net	5,129	546
Supplemental information:		
Interest paid	$ 341,940	$ 296,717
Taxes paid, net	3,267	7,957

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 *Ag***First** *Farm Credit Bank* (*Ag***First**) 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 *Ag***First** has a partial ownership interest. All significant transactions and balances among *Ag***First** 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, 2000, are contained in the 2000 Annual Report to Stockholders. These unaudited second quarter 2001 financial statements should be read in conjunction with the 2000 Annual Report to Stockholders.

SFAS No. 133, *"Accounting for Derivative Instruments and Hedging Activities,"* as amended, requires derivatives to be reported on the balance sheet as assets and liabilities, measured at fair value. Changes in the values of those derivatives are accounted for as gains or losses or as a component of other comprehensive income depending on the use of the derivative and whether it qualifies for hedge accounting. *Ag***First** adopted the Statement, as amended, on January 1, 2001.

On January 1, 2001, *Ag***First** recorded a net cumulative effect-type adjustment of $(112) in earnings and recorded a cumulative effect-type adjustment of $(1,037) in accumulated other comprehensive income at adoption of SFAS No. 133. Other effects on the balance sheet were insignificant.

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 (GAAP). The results for the six months ended June 30, 2001 are not necessarily indicative of the results to be expected for the year ending December 31, 2001.

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 June 30, 2001, 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 12-31-99	$ 278,953
Provision for loan losses	2,066
Loans (charged off), net of recoveries	(276)
Balance at 6-30-00	$ 280,743
Balance at 12-31-00	$ 284,867
Provision for loan losses	6,563
Loans (charged off), net of recoveries	(473)
Balance at 6-30-01	$ 290,957

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.

Actions are pending against *Ag***First** 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 *Ag***First** and District Associations.

NOTE 4 — PREFERRED STOCK

On May 17, 2001, *Ag***First** issued $225 million of Class A Cumulative Preferred Stock, which represents 225,000 shares at $1 thousand per share par value and is mandatorily redeemable on December 15, 2016. Dividends on this preferred stock are payable on June 15th and December 15th of each year beginning June 15, 2001 through December 2011 at the rate of 8.393 percent per annum of the par value of $1 thousand per share. Thereafter, dividends will be paid in arrears on the fifteenth day of each March, June, September and December of each year, commencing March 15, 2012. Beginning March 15, 2012, the rate will change to a variable rate. On or after the dividend payment date in December 2011, the preferred stock will be redeemable in whole or in part at the option of *Ag***First** on any dividend payment date at its par value plus accrued and unpaid dividends.

NOTE 5 — BANK ONLY FINANCIAL DATA

Condensed financial information of *Ag***First** follows:

Balance Sheet Data

	6/30/01	12/31/00 *(Audited)*
Cash and investment securities	$ 2,175,748	$ 2,241,674
Loans	10,319,346	9,496,503
Less: allowance for loan losses	22,416	21,416
Net loans	10,296,930	9,475,087
Other assets	205,907	197,338
Total assets	$ 12,678,585	$ 11,914,099
Bonds and notes	$ 11,578,765	$ 11,014,557
Other liabilities	126,437	211,768
Total liabilities	11,705,202	11,226,325
Preferred Stock (Note 4)	225,839	—
Capital stock and participation certificates	302,326	301,189
Retained earnings	442,576	388,035
Accumulated other comprehensive income (loss)	2,642	(1,450)
Total shareholders' equity	747,544	687,774
Total liabilities and equity	$ 12,678,585	$ 11,914,099

Statement of Income Data

	For the three months ended June 30, 2001	For the three months ended June 30, 2000	For the six months ended June 30, 2001	For the six months ended June 30, 2000
Interest income	$191,074	$187,598	$392,213	$365,779
Interest expense	150,081	155,158	316,159	299,999
Net interest income	40,993	32,440	76,054	65,780
Provision for loan losses	—	—	1,000	—
Net interest income after provision for loan losses	40,993	32,440	75,054	65,780
Noninterest income (expense), net	(9,661)	(9,823)	(18,205)	(19,538)
Net income	$ 31,332	$ 22,617	$ 56,849	$ 46,242