Delivering Value

2011 Annual Report

AgFirst
Farm Credit Bank

Our Mission

To provide services and funding that enable our Associations to serve their markets in a competitive and efficient manner.

THE AGFIRST FARM CREDIT DISTRICT

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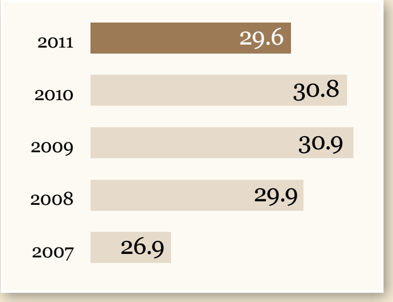
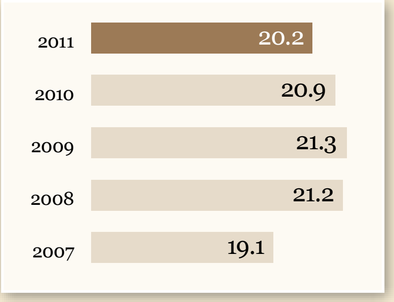
of Selected Consolidated Financial Data

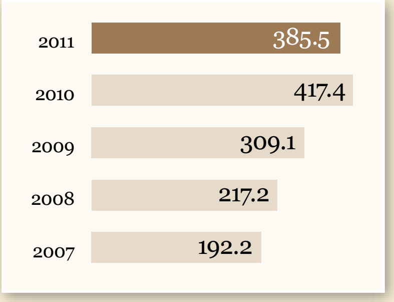
Total Assets
$ in billions



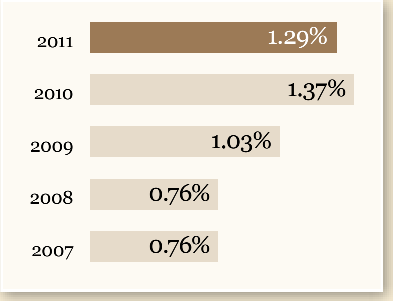
Loans
$ in billions



Net Income
$ in millions



Return on Assets



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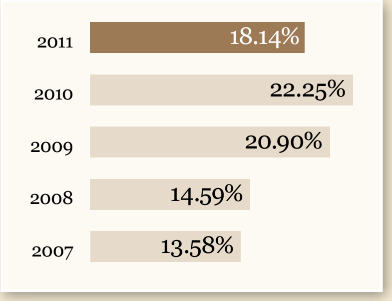
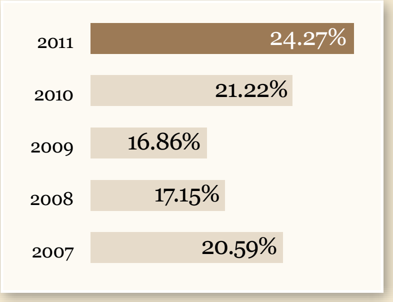
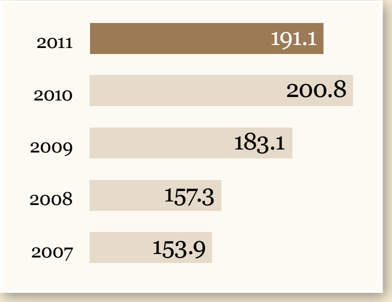


Permanent Capital Ratio



Cash Distribution
$ in millions



Five-Year Summary of Selected Consolidated Financial Data

(dollars in thousands)	As of or for the year ended December 31, 2011	2010	2009	2008	2007
Consolidated Balance Sheet Data					
Cash and cash equivalents	$ 1,301,569	$ 1,427,033	$ 938,884	$ 277,003	$ 558,770
Investment securities	7,780,272	8,076,678	8,226,209	7,993,157	6,908,797
Loans	20,152,066	20,905,165	21,327,319	21,239,330	19,114,517
Less: allowance for loan losses	27,714	14,873	32,292	44,565	2,816
Net loans	20,124,352	20,890,292	21,295,027	21,194,765	19,111,701
Other property owned	44,157	39,719	25,909	540	—
Other assets	327,156	347,844	381,515	445,586	347,353
Total assets	$ 29,577,506	$ 30,781,566	$ 30,867,544	$ 29,911,051	$ 26,926,621
Obligations with maturities of one year or less	$ 12,095,042	$ 12,557,028	$ 14,306,748	$ 14,037,745	$ 11,353,878
Obligations with maturities greater than one year	15,333,194	16,096,757	14,755,466	14,407,214	13,890,262
Mandatorily redeemable preferred stock	—	225,000	225,000	225,000	225,000
Total liabilities	27,428,236	28,878,785	29,287,214	28,669,959	25,469,140
Perpetual preferred stock	400,000	400,000	400,000	400,000	400,000
Capital stock and participation certificates	405,767	417,333	438,707	434,929	364,759
Retained earnings					
Allocated	858	871	965	805	705
Unallocated	1,218,648	1,052,248	863,862	762,550	730,724
Accumulated other comprehensive income (loss)	123,997	32,329	(123,204)	(357,192)	(38,707)
Total shareholders' equity	2,149,270	1,902,781	1,580,330	1,241,092	1,457,481
Total liabilities and shareholders' equity	$ 29,577,506	$ 30,781,566	$ 30,867,544	$ 29,911,051	$ 26,926,621
Consolidated Statement of Income Data					
Net interest income	$ 594,777	$ 571,246	$ 489,661	$ 366,521	$ 260,878
Provision for (reversal of allowance for) loan losses	80,222	40,002	46,648	43,342	2,481
Noninterest income (expense), net	(129,097)	(113,849)	(133,870)	(106,012)	(66,188)
Net income	$ 385,458	$ 417,395	$ 309,143	$ 217,167	$ 192,209
Consolidated Key Financial Ratios					
Rate of return on average:					
Total assets	1.29%	1.37%	1.03%	0.76%	0.76%
Total shareholders' equity	18.14%	22.25%	20.90%	14.59%	13.58%
Net interest income as a percentage of average earning assets	2.08%	1.96%	1.66%	1.29%	1.04%
Net (chargeoffs) recoveries to average loans	(0.329)%	(0.276)%	(0.278)%	(0.008)%	(0.001)%
Total shareholders' equity to total assets	7.27%	6.18%	5.12%	4.15%	5.41%
Debt to shareholders' equity (:1)	12.76	15.18	18.53	23.10	17.47
Allowance for loan losses to loans	0.14%	0.07%	0.15%	0.21%	0.01%
Permanent capital ratio	24.27%	21.22%	16.86%	17.15%	20.59%
Total surplus ratio	24.24%	21.19%	16.83%	17.11%	20.54%
Core surplus ratio	17.08%	13.79%	9.85%	10.43%	13.04%
Collateral ratio	106.49%	106.44%	105.66%	105.56%	106.02%
Net Income Distribution					
Cash distributions	$ 191,060	$ 200,772	$ 183,116	$ 157,278	$ 153,894
Perpetual preferred stock dividend	27,413	27,413	27,413	27,413	19,501

Message

FROM THE CHAIRMAN OF THE BOARD AND THE CHIEF EXECUTIVE OFFICER

M. Wayne Lambertson
Chairman of the Board

F. A. Lowrey
Chief Executive Officer

"Backed by the financial and operational resources of the Bank, each of our District Associations has been able to fully serve its markets and individual members regardless of local economic conditions."

The weak general economy and distressed land values continue to challenge the Bank and many Associations in the AgFirst District. These factors have adversely affected credit quality. Loan demand throughout the District is expected to remain low for some period of time.

During this period of adversity, the Bank's business model and the strengths of the District's cooperative structure have been well tested and proven. The positioning of the Bank's balance sheet and the ability it affords to improve our funding costs in the lower interest environment have greatly benefitted our financial performance. Backed by the financial and operational resources of the Bank, each of our District Associations has been able to fully serve its markets and individual members regardless of local economic conditions.

Maintaining a strong balance sheet, both in terms of capital and earning assets, is an integral part of the Bank's business model. Earnings generated by the Bank's loan and investments portfolios, enhanced by very favorable funding costs, enabled the Bank to return $191 million in cash patronage to our Association owners and other financial partners in 2011, including special distributions of $40 million, out of net income that totaled $385 million. Over the last few years, we have been able to significantly strengthen our capital base through earnings retention. This allowed the Bank to retire, through calls and repurchases, more than $315 million of preferred stock in late 2011 and the first two months of 2012. This will enhance the Bank's value to our common shareholders in the future. At the same time, we have maintained the capacity to issue additional preferred stock if and when growth in the Bank and District Association loan portfolios should require it. That flexibility is a key goal of the Bank's capital plan.

Another key element of the Bank's business model is providing operational support and technology infrastructure for our District Associations. The continuing enhancement and reliability of those service and infrastructure elements are critical to the Bank's mission and the ongoing success of our District Associations.

For six weeks during August and September, the Bank's headquarters in Columbia were virtually uninhabitable. Early in the morning on Saturday, August 13th, a city water main break flooded the lowest floor of the building, where the primary electrical, heat and air conditioning equipment are housed. The District's computer operations are located one floor above the flooded area. Our computer equipment was not damaged by the water, but electrical power to the building was completely disrupted and repairs required the custom manufacture and installation of replacement electrical equipment. Although the vast majority of our Bank staff was housed in temporary office space or worked from home for the six weeks it took to make the permanent repairs, our data systems were down for only 16 hours on that Saturday. Our Associations were fully operational when they opened for business the Monday following the flood.

We are very proud of the response of our employees during this event, and thankful for the support of our Association customers and owners. Although our recovery efforts were extremely effective, we learned a great deal from the experience and are dedicating additional resources to our business continuity and disaster recovery capabilities.

We are also working steadily to enhance our loan accounting and servicing systems and our credit risk management processes. This is a multi-year effort to rebuild completely the way we manage and analyze loan information. The end result will be better operating efficiency for our Associations, improved service and products for their customers and better tools to manage credit risk at the Bank, our Associations and the District level.

Finally, we continue to focus on our staff and plan for the future. Last month, we announced that Tim Amerson will be the next Chief Executive Officer of AgFirst, effective July 1, 2012. It is very rewarding to promote an individual who has worked for the Bank for the past 25 years into this position. During his time at AgFirst, Tim has contributed significantly to the Bank's success and he is the right person to lead us as we move forward.

The past year was very challenging. We responded with stable earnings, a stronger capital structure and more reliable technology infrastructure. We have a bank staff in place that is very capable and dedicated to customer service. However, our most valuable strengths remain the close relationships we have developed across our District and our unique ability within the Farm Credit System to work together for our mutual success.

M. Wayne Lambertson

M. Wayne Lambertson
Chairman of the Board

F. A. Lowrey

F. A. Lowrey
Chief Executive Officer

March 13, 2012

AgFirst Profile

and Business Model

AgFirst is a member of the Farm Credit System, the largest agricultural lending organization in the United States. As one of the four Banks in the Farm Credit System, we provide funding and services to 20 affiliated Agricultural Credit Associations in 15 eastern states and Puerto Rico. Our Associations, in turn, provide financing to 80,000 farmers, ranchers, rural homeowners, and agribusinesses.

“AgFirst exists to serve and provide value to its affiliated Associations and their borrowers.”

Our primary business is providing funding to our affiliated Associations. We also provide operational and technology support and manage credit portfolio, interest-rate, and other risks on a District-wide basis.

AgFirst exists to serve and provide value to its affiliated Associations and their borrowers. We refer to the way we go about providing services and adding value as the “AgFirst Business Model.” The foundation of our model is the strong relationships we have with our Association boards and management teams.

We strive to operate the Bank in a profitable and highly efficient manner so that we can deliver competitive funding and services to our Associations. Our model provides our Associations with the operational infrastructure of a major financial institution. This enables our Associations, both large and small, to meet the needs of their customers in an effective manner.

An integral part of our business model is the way we manage our balance sheet and operate other lines of business, in addition to funding and directly supporting our Associations. These lines of business allow us to generate earnings streams which help offset our operating costs and ultimately lower the Associations’ costs of borrowing.

Benefits of Association Ownership and Investment in AgFirst

AgFirst is a federated cooperative; that is, we are a cooperative owned by other cooperatives, our 20 affiliated Associations. The Associations are, in turn, owned by their borrowers, who are primarily farmers.

Our Associations benefit from their ownership of AgFirst in two important ways. By delivering funding and services to all 20 Associations, AgFirst achieves economies of scale that could not be realized by the Associations individually. In addition, AgFirst shares its profits with its Associations through patronage refunds, which reduce the Associations’ cost of borrowing and, ultimately, their borrowers’ cost of borrowing.

Another AgFirst objective is to capitalize the Bank primarily through retained earnings, supplemented as necessary with preferred stock, rather than direct Association stockholder investments. We have gradually reduced the Association investment requirement in recent years, from 5.25 percent of direct notes outstanding in 1993 to 1.75 percent in 2006, where it remains today. The earnings provided by our other lines of business help AgFirst meet this objective.

Appropriately leveraging our Associations’ capital investment in the Bank is an important component of our business model. Our business model helps to ensure strong returns on that capital as a result of the income from our secondary business lines. Further, our direct note pricing gives credit to Associations for their investment in the Bank.

Funding

Like all Banks in the Farm Credit System, AgFirst obtains its funds primarily through the sale of notes and bonds to the investing public. Because the System has the capacity to issue large volumes of highly rated securities across a broad range of maturities and pricing structures, the Associations we serve enjoy a dependable and competitively priced source of funding.

AgFirst absorbs most of the interest-rate risk associated with the various loan products offered by our affiliated Associations, including both variable and adjustable interest rate products tied to various indices and fixed-rate products. This gives Associations the flexibility to offer a full array of loan and other financial products to their members. AgFirst uses callable debt, interest-rate swaps, and other funding techniques to maintain a conservative risk profile.

Other Lines of Business

Our primary focus is being a wholesale lender and a first-class service provider for our affiliated Associations. However, we offset our operating expenses through additional earnings streams. These other lines of business ultimately provide direct value to the Bank’s stockholders.

AgFirst’s Capital Markets portfolio began as a means to accommodate Association over-lines on large credits. It still provides that benefit to Associations. However, its purpose has expanded over time. It now provides both the Bank and Associations with a resource to buy and sell loan assets that can be used to manage capital utilization and credit portfolio risk issues such as commodity concentration.

AgFirst’s Capital Markets Unit manages this portfolio and provides Associations with expertise in large-loan lending and servicing. This partnership gives Associations an important tool for serving their individual markets and facilitates their access to a wider market.

The Capital Markets portfolio generates significant levels of income that benefit the Bank’s stockholders. Earnings from the Capital Markets portfolio are used to pay patronage or servicing fees on Capital Markets loans. The portfolio’s excess net income is available

> "The foundation of our model is the strong relationships we have with our Association boards and management teams."

for general patronage to the Bank's stockholders, to reduce the costs of the Bank's operations, and to provide an additional means for the Bank to build capital for the benefit of stockholders.

The geographic size and diversity of our District, coupled with our combined financial strength, give us both the flexibility and the capacity to serve our customers and to manage our risks. As a financial intermediary, we utilize our Capital Markets portfolio to help individual Associations diversify their loan portfolios and fully serve their largest customers. We emphasize to Association management teams our commitment to purchase quality loans they originate that may exceed the size they can safely hold or which pose excessive concentration risk. This enables Associations to transfer portfolio risks to AgFirst, where they can be managed effectively across the District. Our Associations can then concentrate on the specific needs of their creditworthy members with confidence, knowing that the Bank will be a reliable partner.

The Bank's Correspondent Lending Unit (CLU) buys individual rural home mortgages from originators. Most of its volume is originated by Associations within our District, but the CLU also purchases loans from other Farm Credit Associations and other originators throughout the United States. The CLU benefits Associations by enabling them to serve a competitive market and providing them the option to sell low-margin loans, while generating fee income. The Bank is able to create economies of scale from larger volume to keep its operating costs low and generate a profit on the portfolio. This is a non-patronage line of business, with the net earnings directly benefiting the Bank's stockholders.

AgFirst's investment portfolio is primarily a liquidity management tool, but it also generates net income for the Bank. In managing its investment portfolio, AgFirst concentrates on investments with low credit and price risk. Despite the market difficulties experienced since 2008, the level of credit risk has been limited by maintaining a high percentage of the portfolio in U.S. Government- or U.S. Agency-guaranteed investments. As with the other portfolios, the net earnings from investments flow into capital and directly benefit the Bank's stockholders.

These additional lines of business are critical to the AgFirst business model. They provide an expanded line of products and services to Associations and generate additional earnings that offset the Bank's operating costs, flow into capital, and are used to pay patronage to Associations, all of which ultimately benefit Associations by reducing their costs of borrowing and Bank capital investment requirements.

Services

AgFirst primarily uses a "bundled" approach in providing core services to its affiliated Associations. Core services are available to all affiliates, with the cost shared by them through the direct note pricing. This approach enables AgFirst to serve large and small Associations and provide the same standard of care to all Associations, regardless of size. In addition to these bundled services, AgFirst offers additional—or "expanded"—services, usually at the Bank's incremental cost, to the Associations that wish to use them. These expanded services help create further efficiencies in their operations.

Core Services

- Loan Origination, Aggregation, and Customer Relationship Management Systems
- Loan Accounting Systems
- Financial Reporting and Accounting Systems
- Marketing
- Compliance Support
- Human Resource Consulting

Expanded Services

- Accounts Payable/Fixed Assets
- Participation Loan Accounting
- High-Risk Assets Accounting
- Payroll
- Technology Infrastructure Management

Keeping Connected

We are proud of the close relationships we maintain with our affiliated Associations. We assign a Relationship Manager (RM) to each Association. The RM serves as an account manager and liaison between the Bank and Association. The RM is responsible for servicing the Association's direct note with the Bank, assessing the Association's risk-bearing capacity, and facilitating communications between the Association and all functions within the Bank. In addition, RMs are available to assist Associations to market and structure large, complex loans upon request.

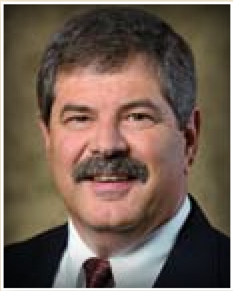
Association CEOs and AgFirst senior staff meet as a group on a regular basis to discuss topics of common concern. At those meetings, CEOs often pass along ideas and suggestions to AgFirst management and their fellow CEOs, and AgFirst provides updates on Bank and System issues, as well as technology and other projects that impact Association operations.

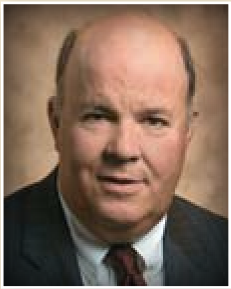
In the AgFirst business model, the Bank and Associations remain independent of one another, but work together to achieve their respective goals and objectives and plan for future needs.

Board of Directors


M. Wayne Lambertson
Chairman


Robert H. Spiers, Jr.
Vice Chairman


Gary L. Alexander


Jack W. Bentley, Jr.


James C. Carter, Jr.


Bonnie V. Hancock


Dale R. Hershey


Paul M. House


Thomas W. Kelly


Lyle Ray King


John S. Langford


S. Alan Marsh


James L. May


Bobby E. McCollum, Jr.


James M. Norsworthy III


Katherine A. Pace


Jimmy D. Poston


Walter L. Schmidlen, Jr.


William H. Voss


J. Mark Wheeler

Report of Management

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

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

AgFirst has a Code of Ethics for its Chief Executive Officer, Senior Financial Officers, and other Senior Officers who are involved with preparation and distribution of financial statements and maintenance of the records supporting the financial statements. A copy of the AgFirst Code of Ethics may be viewed on the Bank's website at www.agfirst.com.

The Consolidated Financial Statements have been examined by independent certified public accountants, whose report appears elsewhere in this Annual Report. The Bank is also subject to examination by the Farm Credit Administration.

The Consolidated Financial Statements, in the opinion of management, fairly present the financial condition of the Bank. The undersigned certify that we have reviewed the 2011 Annual Report of AgFirst Farm Credit Bank, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.

M. Wayne Lambertson

M. Wayne Lambertson
Chairman of the Board

F. A. Lowrey

F. A. Lowrey
Chief Executive Officer

Charl L Butler

Charl L. Butler
Senior Vice President and Chief Financial Officer

March 13, 2012

Report on Internal Control

over Financial Reporting

The Bank's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Bank's Consolidated Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by or under the supervision of the Bank's principal executives and principal financial officers, or persons performing similar functions, and effected by its Board of Directors, management and other personnel. This process provides reasonable assurance regarding the reliability of financial reporting information and the preparation of the Consolidated Financial Statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Bank, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial information in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Bank, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Bank's assets that could have a material effect on its Consolidated Financial Statements.

The Bank's management has completed an assessment of the effectiveness of internal control over financial reporting as of December 31, 2011. In making the assessment, management used the framework in *Internal Control — Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Bank's management concluded that as of December 31, 2011, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Bank's management determined that there were no material weaknesses in the internal control over financial reporting as of December 31, 2011.

F. A. Lowrey

F.A. Lowrey
Chief Executive Officer

Charl L Butler

Charl L. Butler
Senior Vice President and Chief Financial Officer

March 13, 2012

Management's Discussion & Analysis

of Financial Condition & Results of Operations

(as of December 31, 2011)

AgFirst Farm Credit Bank (the Bank or AgFirst) is one of the banks of the Farm Credit System (the System), a nationwide system of cooperatively owned banks and associations. The System was established by Acts of Congress and is subject to the provisions of the Farm Credit Act of 1971, as amended (the Farm Credit Act).

As of December 31, 2011, the nation was served by four Farm Credit Banks (FCBs) and one Agricultural Credit Bank (ACB). With the merger of CoBank, ACB and U.S. AgBank, FCB effective January 1, 2012, the nation is currently served by three FCBs and one ACB, each of which has specific lending authorities within its chartered territory. The ACB also has certain additional specific nationwide lending authorities. AgFirst is chartered to serve the states of Pennsylvania, Delaware, Maryland, Virginia, West Virginia, North Carolina, South Carolina, Georgia, Florida, Alabama, Mississippi, the Commonwealth of Puerto Rico and portions of the states of Ohio, Tennessee, Kentucky and Louisiana.

Each FCB and the ACB serves one or more of either Production Credit Associations (PCAs) that originate and service short- and intermediate-term loans, Federal Land Credit Associations (FLCAs) that originate and service long-term real estate mortgage loans, and/or Agricultural Credit Associations (ACAs) that originate both long-term and short-term and intermediate-term loans. PCAs, FLCAs and ACAs are collectively referred to as associations. AgFirst and its related associations (Associations or District Associations) are collectively referred to as the District (District). The Associations are structured as cooperatives in which each Association is owned by its borrowers. AgFirst also operates as a cooperative. The District Associations own all of AgFirst's voting stock. As of December 31, 2011, the District consisted of the Bank and twenty District Associations. All twenty were structured as ACA holding companies, with FLCA and PCA subsidiaries. See Note 21, *District Merger Activity*, in the Notes to the Consolidated Financial Statements for a discussion of recent merger activity.

The following commentary reviews the Consolidated Financial Statements of condition and results of operations of AgFirst as of and for the years ended December 31, 2011, 2010, and 2009. This information should be read in conjunction with the accompanying Consolidated Financial Statements, the Notes to the Consolidated Financial Statements and other sections of this Annual Report. The Consolidated Financial Statements were prepared under the oversight of the Audit Committee of the Bank's Board of Directors. For a list of the Audit Committee members, refer to the "Report of the Audit Committee" included in this Annual Report. See Note 1, *Organization and Operations*, in the Notes to the Consolidated Financial Statements for a discussion of the operations of AgFirst.

FORWARD-LOOKING INFORMATION

Certain sections of this Annual Report contain forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," "will," or other variations of these terms are intended to identify the forward-looking statements. These statements are based on assumptions and analyses made in light of experience and other historical trends, current conditions, and expected future developments. However, actual results and developments may differ materially from AgFirst's expectations and predictions due to a number of risks and uncertainties, many of which are beyond AgFirst's control. These risks and uncertainties include, but are not limited to:

- political, legal, regulatory, financial markets, and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural infrastructure, international, and farm-related business sectors, as well as in the general economy;
- weather-related, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income of District borrowers;
- changes in United States government support of the agricultural industry and the System as a government-sponsored enterprise (GSE), as well as investor and rating agency reactions to events involving other GSEs and other financial institutions; and
- actions taken by the Federal Reserve System in implementing monetary and fiscal policy, as well as other policies and actions of the Federal government that impact the financial services industry and the debt markets.

AGRICULTURAL OUTLOOK

The following United States Department of Agriculture (USDA) analysis provides a general understanding of the U.S. agricultural economic outlook. However, this outlook does not take into account all aspects of AgFirst's business. References to the USDA information in this section refer to the entire U.S. agricultural market and are not limited to AgFirst.

The February 2012 USDA forecast estimates 2011 farmers' net cash income, which is a measure of the cash income after payment of business expenses, increased to $108.7 billion, up $16.4 billion from 2010 and up $28.4 billion from its 10-year average of $80.3 billion. The improvement in 2011 farmers' net cash income was due primarily to increases in crop receipts of $24.0 billion and livestock receipts of $24.6 billion, partially offset by a $34.7 billion increase in cash expenses.

The February 2012 USDA forecast for the farm economy, as a whole, projects 2012 farmers' net cash income to decrease to $96.3 billion, a $12.4 billion decrease from 2011, but $16.0 billion above the 10-year average. The forecasted decrease in farmers' net cash income for 2012 is primarily due to an expected increase in cash expenses of $11.3 billion, while crop and livestock receipts remain near the 2011 levels.

For 2012, the USDA expects crop receipts to increase slightly, as increases in corn and most other feed grains offset declines in wheat, hay, vegetables/melons, and fruits/tree nuts. The drought in parts of the U.S. in 2011 is expected to depress sales of many crops through its negative impact on production. Livestock receipts are expected to decline marginally in 2012. While receipts for cattle are anticipated to increase as demand for beef in the Asian markets remains strong, dairy receipts are expected to decrease as milk prices are forecasted to be lower.

The following table sets forth the commodity prices per bushel for certain crops and by hundredweight for beef cattle from December 31, 2008 to December 31, 2011:

Commodity	**12/31/11**	**12/31/10**	**12/31/09**	**12/31/08**
Corn	$5.86	$4.82	$3.60	$4.11
Soybeans	$11.50	$11.60	$9.80	$9.24
Wheat	$7.19	$6.45	$4.87	$5.95
Beef Cattle	$120.00	$98.10	$78.50	$79.70

The USDA's income outlook varies depending on farm size, geographic location, and commodity specialties. The USDA classifies all farms into three primary categories: commercial farms, intermediate farms and rural residential farms. Commercial farms, large scale farms with gross sales greater than $250 thousand, represent about 12 percent of U.S. farms by number but represent over 80 percent of total U.S. farm production. Commercial farms are expected to have a 17 percent increase in average net cash income in 2011. Intermediate farms, defined as ones in which the primary occupation is farming and gross sales are between $10 thousand and $250 thousand, represent 28 percent of U.S. farms by number and account for 18 percent of total production. Intermediate farms are expected to have a 14 percent increase in average net cash income in 2011. The remaining 60 percent of U.S. farms are classified as rural residential farms where the primary occupation is not farming and the farms produce less than $10 thousand in sales. Rural residential farms only account for 2 percent of total production.

In addition to farmers' net cash income, off-farm income is an important source of funds for the repayment of farm debt obligations and is less subject to cycles in agriculture. However, off-farm income can be directly affected by conditions in the general economy. The USDA measures farm household income, which is defined as earnings from farming activities plus off-farm income. Nearly 100 percent of farm household income for operators of rural residential farms and approximately 90 percent of farm household income for intermediate farms is generated from off-farm sources. Further, USDA data suggests that approximately 24 percent of farm household income for commercial farms is generated from off-farm income.

According to the USDA's February 2012 forecast, farm sector asset values and farm debt are forecasted to rise modestly in 2012. Farm sector asset values are expected to rise 5.6 percent from $2.34 trillion for 2011 to $2.47 trillion in 2012 primarily due to an increase in the value of farm real estate. The values of machinery/equipment, purchased inputs and financial assets are expected to rise modestly in 2012, while the value of livestock and poultry inventories is expected to decline slightly. The main factors driving higher farmland values are the continued strength of commodity prices, low interest rates, expectations of continued favorable net returns and growth in agricultural exports. Farmers' equity (farm business assets minus debt) is expected to rise 5.7 percent from $2.10 trillion in 2011 to $2.22 trillion in 2012.

One measure of the financial health of the agricultural sector used by the USDA is the assessment of farmers' utilization of their capacity to repay debt (actual debt as a percentage of maximum debt that can be supported by farmers' current income). Higher capacity utilization rates indicate tighter cash flow positions and, consequently, higher exposure to financial risk. Lower rates indicate healthier cash flow and financial positions. These estimates do not take into account, however, off-farm income sources. Since 1970, debt repayment capacity utilization has ranged from a low of 37 percent in 1973 to a high of 110 percent in 1981, and has remained relatively stable since 1987, averaging about 50 percent. The forecast for 2012 predicts farmers' utilization to increase from 40 percent in 2011 to approximately 47 percent for 2012.

As estimated by the USDA in February 2012, the Farm Credit System's market share of farm business debt, defined as debt incurred by those involved in on-farm agricultural production, grew to 41.4 percent at December 31, 2010 (latest available data), as compared with 40.1 percent at December 31, 2009. Overall, farm business debt is forecasted to increase in 2012 to $254.1 billion from $244.8 billion in 2011.

In general, agriculture has experienced a sustained period of favorable economic conditions due to stronger commodity prices, higher farm land values, and, to a lesser extent, government support programs. To date, AgFirst's financial results have remained favorable as a result of the favorable agricultural economic conditions. Production agriculture, however, remains a cyclical business that is heavily influenced by commodity prices. In an environment of less favorable economic conditions in agriculture and without sufficient government support programs, AgFirst's financial performance and credit quality measures would likely be negatively impacted. Conditions in the general and agricultural economies remain volatile given the state of the global economy. Certain agriculture sectors, as described more fully in this *Management's Discussion and Analysis*, experienced significant financial stress during 2011 and could continue to experience financial stress in 2012. Any negative impact from these less favorable conditions should be lessened by geographic and commodity diversification and the influence of off-farm income sources supporting agricultural-related debt. However, agricultural borrowers who are more reliant on off-farm income sources may be more adversely impacted by a weakened general economy.

SIGNIFICANT ACCOUNTING POLICIES

The financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. Consideration of AgFirst's significant accounting policies is critical to the understanding of the Bank's results of operations and financial position because some accounting policies require complex or subjective judgments and estimates that may affect the value of certain assets or liabilities as well as the recognition of certain income and expense items. In many instances, management has to make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2, *Summary of Significant Accounting Policies*, of the Notes to the Consolidated Financial Statements. The following is a summary of certain critical accounting policies:

- *Allowance for loan losses* — The allowance for loan losses is management's best estimate of the amount of probable losses existing in and inherent in the Bank's loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals.

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

  In addition to the allowance for loan losses attributable to specific loans, the Bank may also establish a general allowance for loan losses based on management's assessment of risk inherent in the loans in the Bank's portfolio that were not specifically evaluated. In establishing general reserves, factors affecting certain commodity types or industries may be taken into consideration, as well as other factors previously discussed. Certain loan pools purchased from various Associations are analyzed in accordance with the selling Associations' allowance methodologies for assigning general and specific allowances. Allowances are established on these pools based on that analysis after Bank management's determination that the methodologies employed are appropriate.

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

  The overall adequacy of the allowance for loan losses is validated further through periodic evaluations of the loan portfolio, which generally consider historical charge-off experiences adjusted for relevant factors. These factors include types of loans, credit quality, specific industry conditions, collateral value, general economic and political conditions, and changes in the character, composition, and performance of the portfolio, among other factors.

- *Valuation methodologies* — Management applies various valuation methodologies to assets and liabilities that often involve a significant degree of judgment, particularly when active markets do not exist for the particular items being valued. Quoted market prices are referred to when estimating fair values for certain assets for which an observable active market exists. Management utilizes third party valuation services to obtain fair value prices for the majority of the Bank's investment securities. Management also utilizes significant estimates and assumptions to value items for which an observable active market does not exist. Examples of these items include: impaired loans, other property owned, pension and other postretirement benefit obligations, certain derivatives, certain investment securities and other financial instruments. These valuations require the use of various assumptions, including, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing, and liquidation values. The use of different assumptions could produce significantly different asset or liability values, which could have material positive or negative effects on the Bank's results of operations.

- *Pensions* — The Bank and its related Associations participate in defined benefit retirement plans. These plans are noncontributory and benefits are based on salary and years of service. The Bank and its related Associations also participate in defined contribution retirement savings plans. Pension expense for all plans is recorded as part of salaries and employee benefits. Pension expense for the defined benefit retirement plans is determined by actuarial valuations based on certain assumptions, including the expected long-term rate of return on plan assets and a discount rate. The expected return on plan assets for the year is calculated based on the composition of assets at the beginning of the year and the expected long-term rate of return on that portfolio of assets. The discount rate is used to determine the present value of future benefit obligations. The discount rate for 2011 was selected by reference to analysis and yield curves developed by the plans' actuary and industry norms. The yield curve selected follows the accounting guidance that the basis for discount rates should be higher-quality zero-coupon bonds with durations that match the expected cash flows of the plans that underlie the obligation.

LOAN PORTFOLIO

AgFirst's loan portfolio consists primarily of direct loans to District Associations (Direct Notes), loan participations/syndications purchased, Correspondent Lending loans (primarily first lien rural residential mortgages), and loans to Other Financing Institutions (OFIs) as shown below at December 31:

AgFirst Loan Portfolio

(dollars in thousands)	2011		2010		2009	
Direct Notes	$ 14,094,384	69.94%	$ 14,778,448	70.69%	$ 14,890,793	69.82%
Participations/Syndications Purchased, net	3,880,559	19.25	4,163,794	19.92	4,758,466	22.31
Correspondent Lending	2,171,873	10.78	1,957,923	9.37	1,671,060	7.84
Loans to OFIs	5,250	0.03	5,000	0.02	7,000	0.03
Total	$ 20,152,066	100.00%	$ 20,905,165	100.00%	$ 21,327,319	100.00%

The diversification of AgFirst's loan volume by type for each of the past three years at December 31 is shown below:

(dollars in thousands)	2011		2010		2009	
Direct Notes	$ 14,094,384	69.94 %	$ 14,778,448	70.69 %	$ 14,890,794	69.82 %
Rural Residential Real Estate	2,060,025	10.22	1,831,928	8.76	1,548,829	7.26
Production and Intermediate-Term	1,382,659	6.86	1,486,639	7.11	1,708,861	8.01
Real Estate Mortgage	1,207,221	5.99	1,401,285	6.70	1,686,948	7.91
Agribusiness						
Loans to Cooperatives	174,552	0.87	162,167	0.78	181,336	0.85
Processing and Marketing	684,300	3.40	712,171	3.41	773,263	3.63
Farm-Related Business	114,826	0.57	61,801	0.30	59,173	0.28
Total Agribusiness	973,678	4.84	936,139	4.49	1,013,772	4.76
Energy	246,930	1.22	296,213	1.42	304,517	1.43
Communication	136,899	0.68	113,021	0.54	104,208	0.49
Water and Waste Disposal Loans	28,000	0.14	28,000	0.13	28,000	0.13
Lease Receivables	–	–	6,331	0.03	9,121	0.04
Loans to OFIs	5,250	0.03	5,000	0.02	7,000	0.03
Other (including Mission Related)	17,020	0.08	22,161	0.11	25,269	0.12
Total	$ 20,152,066	100.00 %	$ 20,905,165	100.00 %	$ 21,327,319	100.00 %

Total loans outstanding were $20.152 billion at December 31, 2011, a decrease of $753.1 million, or 3.60 percent, compared to total loans outstanding at December 31, 2010. Loans outstanding at the end of 2010 had decreased $422.2 million, or 1.98 percent, compared to December 31, 2009. Relatively modest loan demand, a trend that began in late 2008, reflects the weakness in the general economy.

Since 2008, the weakened economy impacted the Bank's and District Associations' current and prospective customers in a number of ways, including fluctuating demand and prices for certain agricultural products and lower value for real estate and other investment holdings of some borrowers. These conditions have been detrimental to the general sentiment and financial capacity of many of the District's customers. As a result, many customers have reduced production, delayed expansion plans, and generally taken actions to preserve their investment and working capital. Each of these factors has contributed to the lower loan demand throughout the District. Future loan demand is very difficult to predict. However, it is expected to remain weak in 2012.

Certain commodity groups continued to be more adversely affected than others in the current economic cycle. Housing-related industries, such as building products, timber, sawmills, landscape nurseries, and sod operations remained stressed. Also, many customers in the District rely on off-farm income, which has been negatively impacted by the weakness in the general economy. Improvement in these segments is dependent on such general economic factors as employment levels and housing market activity.

Loan portfolio credit quality has been negatively impacted by lower real estate values in certain geographic areas within the Bank's chartered territory, particularly in Florida. Other areas of the District experienced a less severe reduction in real estate values although sales continue to be slow throughout the District.

The beef and swine industries experienced a cycle of profitable results in 2011. Profitability was primarily achieved through reduction of supply, which led to higher prices. Higher grain and energy costs were offset by higher meat prices for both beef and swine producers in 2011.

Many chicken integrators experienced losses and cash flow problems in 2011 due to higher input prices and oversupply. Margins for dairy farmers have narrowed, but, in general, remain sufficient to service debt. Margins remained tight for ethanol producers due to increased input costs, especially high corn prices. The future volatility of grain prices remains a primary concern to the meat, dairy, and ethanol sectors.

Other major segments of the District loan portfolio continued to perform well, including sugar, citrus, cotton, and row crops. High commodity prices for grains were very beneficial to row crop farmers. However, the future volatility of grain prices remains a primary concern to many of the Bank's sectors. While adverse weather conditions impacted row crop yields in certain locations of the District, in general, these borrowers were protected by crop insurance. Production farm land values and sales have held up better than residential and investment real estate.

Each loan in the Bank's portfolio is classified according to a Uniform Classification System, which is used by all System institutions. Below are the classification definitions.

- *Acceptable* – Assets are expected to be fully collectible and represent the highest quality.
- *Other Assets Especially Mentioned (OAEM)* – Assets are currently collectible but exhibit some potential weakness.
- *Substandard* – Assets exhibit some serious weakness in repayment capacity, equity, and/or collateral pledged on the loan.
- *Doubtful* – Assets exhibit similar weaknesses to substandard assets. However, doubtful assets have additional weaknesses in existing facts, conditions and values that make collection in full highly questionable.
- *Loss* – Assets are considered uncollectible.

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

AgFirst Total Loans Credit Quality	2011	2010	2009
Acceptable	87.09%	85.21%	86.60%
OAEM	9.79	10.00	9.48
Adverse*	3.12	4.79	3.92
Total	100.00%	100.00%	100.00%

* *Adverse loans include substandard, doubtful, and loss loans.*

The credit conditions discussed above affect the credit quality of the Bank's participation/syndication loan portfolio directly. They also affect the credit quality of loan portfolios and earnings performance of the individual District Associations, which in turn is reflected in the quality of the Bank's Direct Notes. Continued weakness in the general economy and certain agricultural sectors will have an impact on credit quality for some time. Although credit quality is stabilizing, it will take time to fully resolve some problem assets due to their dependency on general economic conditions, including employment, the housing market, and real estate values.

Direct Notes

AgFirst's primary business is to provide funding, operational support, and technology services to District Associations. Each Association, in addition to the Bank, is a federally chartered instrumentality of the United States and is regulated by the Farm Credit Administration (FCA). AgFirst has a revolving line of credit, referred to as a Direct Note, in place with each of the District Associations. Each of the Associations funds its lending and general corporate activities primarily by borrowing under its Direct Note. Lending terms are specified in a separate General Financing Agreement (GFA) between AgFirst and each Association, including the subsidiaries of the Associations. Each GFA contains minimum borrowing base margin, capital, and earnings requirements that must be maintained by the Association. Refer to Note 1, *Organization and Operations*, in the Notes to the Consolidated Financial Statements for further discussion.

At December 31, 2011, total Direct Note volume outstanding was $14.094 billion, a decrease of $684.1 million, or 4.63 percent, compared to December 31, 2010. Direct Note volume of $14.778 billion at December 31, 2010, decreased $112.3 million, or 0.75 percent, compared to December 31, 2009. Weak customer loan demand at the Associations and a generally more conservative credit approach were the primary reasons for the decline in growth. Also, in some cases, business development resources have been redirected to problem asset management.

For 2011, 2010, and 2009, respectively, earnings for the combined Associations totaled $277.9 million, $330.1 million, and $238.1 million, producing an average return on assets of 1.54 percent, 1.83 percent, and 1.31 percent, and an average return on equity of 8.85 percent, 10.99 percent, and 8.44 percent.

AgFirst provides each Association with core operating systems and support, including a loan origination system, loan accounting and servicing systems, general ledger and related financial accounting systems, and a human resources/payroll system. With AgFirst providing such systems and other services, the Associations are able to achieve operating efficiencies ordinarily afforded only to much larger organizations. In addition, having common systems supported by AgFirst provides an opportunity to automate the AgFirst/Association lending process. One of the most significant advantages of this is a match-funding mechanism that automatically creates Direct Note advances that match the repricing and maturity characteristics of each underlying Association loan. The Association's interest rate risk and operational risks are significantly reduced by employing these systems.

Ultimately, the Associations' ability to repay their Direct Note obligations is significantly dependent upon the repayment of loans made to their borrowers. Accordingly, AgFirst's direct and indirect credit exposure depends upon the creditworthiness of both the Associations that are direct borrowers and the underlying borrowers of the Associations whose loans, as well as the other assets of the Associations, secure their Direct Notes.

AgFirst continually monitors the risk-bearing capacity of each Association through a variety of mechanisms, including testing of the reliability of the Association's risk ratings assigned to each of their loans, periodic meetings with the Association's management and board, regular formalized risk assessments, and prior-approval of loan transactions that exceed the Association's delegated lending authority as determined by AgFirst.

All Associations are subject to an annual audit by independent certified public accountants and periodic examination by FCA. Each Association is required by regulatory mandate to perform continuous internal credit, appraisal, and audit reviews. Litigation in which Associations are involved is typically loan related and poses no material threat to their viability.

The following table presents selected statistics related to the credit quality of the Direct Note portfolio including accrued interest at December 31:

AgFirst Direct Note Credit Quality	2011	2010	2009
Acceptable	85.65%	83.96%	86.13%
OAEM	11.38	11.28	11.26
Adverse*	2.97	4.76	2.61
Total	100.00%	100.00%	100.00%

* *Adverse loans include substandard, doubtful, and loss loans.*

As of December 31, 2011, fourteen of the twenty District Associations' Direct Notes, representing 85.65 percent of the Direct Note portfolio, were classified acceptable. Four of the remaining Direct Notes, representing 11.38 percent of the portfolio, were classified as Other Assets Especially Mentioned (OAEM) and two of the Direct Notes, representing 2.97 percent of the portfolio, were classified as substandard (adverse).

Subsequent to year-end, one Association's Direct Note was moved from acceptable to OAEM and another Association's Direct Note was moved from OAEM to acceptable. If these changes were reflected in the table above, the result would be to increase OAEM and decrease acceptable by 4.57 percent.

None of the Direct Notes, including those classified as substandard (adverse), are considered impaired. All assets of the various Associations are pledged as collateral for their respective Direct Notes. The risk funds of an Association, including both capital and the allowance for loan losses, protect the interest of the Bank should a Direct Note default. In the opinion of management, all Association Direct Notes are adequately collateralized. Presently, collections of the full amounts due are expected in accordance with the contractual terms of the debt arrangements.

As of December 31, 2011, seven Associations were in violation of covenants under the GFA. The Bank approved waivers of the defaults and allowed these Associations to operate under special credit agreements (SCAs) pursuant to their respective GFAs.

At December 31, 2011, FCA had entered into written supervisory agreements with three District Associations with combined assets of approximately $900.0 million. Those agreements require the three District Associations to take corrective actions with respect to certain areas of their operations, including capital, portfolio management, and asset quality. These enforcement actions are not expected to have a significant impact on the Bank's or District's financial condition or results of operations.

Associations employ a number of risk management techniques to limit credit exposures. Each Association has adopted underwriting standards, individual borrower exposure limits, commodity exposure limits, and other risk management techniques. AgFirst and the Associations actively purchase and sell loan participations to achieve diversified portfolios. Some Associations utilize guarantees from U.S. government agencies/departments, including the Farm Service Agency, the Small Business Administration, and the Federal Agricultural Mortgage Corporation (Farmer Mac), to further limit credit exposures. At December 31, 2011, Associations collectively had $1.840 billion under such government or GSE guarantee programs, compared to $1.618 billion, and $1.459 billion, at December 31, 2010 and 2009, respectively.

At year-end, the combined Associations' loans including accrued interest were classified as follows:

District Associations Credit Quality	2011	2010	2009
Acceptable	87.80%	86.40%	86.99%
OAEM	5.50	6.54	6.20
Adverse*	6.70	7.06	6.81
Total	100.00%	100.00%	100.00%

** Adverse loans include substandard, doubtful, and loss loans.*

Delinquencies (loans 90 days or more past due) were 2.12 percent of the combined Association total loan assets at year-end 2011 compared to 2.29 percent and 1.71 percent at year-end 2010 and 2009, respectively.

Nonperforming assets for the combined Associations represented 4.54 percent of total loan assets or $758.3 million, compared to 4.63 percent or $796.1 million for 2010, and 3.57 percent or $606.6 million for 2009. Nonperforming assets consist of nonaccrual loans, accruing restructured loans, accruing loans 90 days or more past due and other property owned.

Association net loan charge-offs of $139.7 million, $93.6 million and $77.9 million were recognized in 2011, 2010, and 2009, respectively. As a percentage of total average loans, net charge-offs for the combined Associations were 0.83 percent for 2011 compared to 0.56 percent and 0.46 percent in 2010 and 2009, respectively. Each Association maintains an allowance for loan losses determined by its management based upon its unique circumstances.

The following table illustrates the risk bearing capacity of the Associations at December 31, 2011:

Association	Regulatory Permanent Capital Ratio	Regulatory Core Surplus Ratio	Regulatory Total Surplus Ratio	Allowance/ Loans
AgCarolina Financial	18.46%	14.98%	14.98%	1.50%
AgChoice	16.56%	13.79%	15.73%	0.62%
Ag Credit	18.93%	14.72%	17.00%	0.87%
AgGeorgia	14.98%	12.20%	14.61%	1.24%
AgSouth	15.98%	11.14%	15.51%	0.66%
ArborOne	18.07%	15.70%	17.60%	1.28%
Cape Fear	20.26%	19.87%	19.87%	0.95%
Carolina	17.47%	13.82%	16.80%	0.43%
Central Florida	18.84%	15.72%	18.16%	2.97%
Central Kentucky	14.05%	12.30%	12.63%	1.18%
Chattanooga	16.12%	10.42%	14.05%	1.15%
Colonial	20.04%	19.32%	19.32%	1.01%
Farm Credit of Florida	16.33%	15.62%	15.62%	1.29%
Farm Credit of the Virginias	15.08%	13.85%	13.85%	0.53%
First South	15.28%	13.10%	14.14%	0.55%
Jackson Purchase	17.40%	15.36%	16.51%	0.98%
MidAtlantic	16.57%	16.00%	16.19%	0.51%
Northwest Florida	17.80%	16.79%	17.53%	2.00%
Puerto Rico	18.61%	18.22%	18.22%	1.99%
Southwest Georgia	20.64%	17.03%	20.28%	1.51%

The minimum regulatory capital ratios for System banks and associations are 7.00 percent for the permanent capital ratio, 3.5 percent for the core surplus ratio, and 7.00 percent for the total surplus ratio.

Affiliated Associations serve primarily all or a portion of fifteen states and Puerto Rico. The District's large footprint results in geographic diversity, which is a natural credit risk-reducing factor for AgFirst. The following table illustrates the geographic distribution of the Associations' loan volume outstanding by state for the past three years at December 31:

	District Associations		
State	2011	2010	2009
North Carolina	16%	15%	15%
Georgia	13	13	13
Virginia	11	11	11
Florida	10	12	13
Pennsylvania	10	10	10
Ohio	8	7	6
Maryland	7	7	7
South Carolina	6	6	6
Alabama	4	3	3
Kentucky	3	3	3
Mississippi	2	2	2
Delaware	2	2	2
West Virginia	2	2	2
Louisiana	1	1	1
Tennessee	1	1	1
Puerto Rico	1	1	1
Other	3	4	4
Total	100%	100%	100%

Only five states have loan volume representing 10.00 percent or more of the total. Commodity diversification, guarantees, and borrowers with significant reliance on non-farm income further mitigate the geographic concentration risk in these states.

The diversity of commodity types and income sources supporting Association loan repayment further mitigates credit risk to AgFirst. The Associations' credit portfolios are comprised of a number of segments having varying, and in some cases complementary, agricultural characteristics. Commodity and industry categories are based on the Standard Industrial Classification system published by the federal government. This system is used to assign commodity or industry categories based on the largest agricultural commodity of the customer. The following table illustrates the aggregate credit portfolio of the Associations by major commodity segments at December 31:

District Associations

	Percent of Portfolio		
Commodity Group	**2011**	**2010**	**2009**
Forestry	15%	16%	16%
Poultry	14	13	13
Fruits/Vegetables	10	10	10
Cattle	8	8	8
Grain	7	6	7
Other Real Estate	6	7	7
Dairy	5	6	6
Corn	5	4	2
Nursery/Greenhouse	4	4	4
Processing	3	3	4
Rural Home	3	3	3
Tobacco	3	3	3
Swine	3	3	3
Cotton	3	3	2
Citrus	1	1	1
Other	10	10	11
Total	100%	100%	100%

Diversification is further enhanced by a prevalence of non-farm income among the borrowers, as demonstrated by the following table as of December 31 of each year, which segregates part-time farm loans into a unique segment. Part-time farming is defined as farming not being the primary business or vocation of the applicant with agricultural operations representing less than 50 percent of their total business income.

District Associations

	Percent of Portfolio		
Commodity Group	**2011**	**2010**	**2009**
Part-time Farmers	37%	38%	39%
Poultry	12	11	11
Forestry	5	6	6
Dairy	5	5	6
Fruits/Vegetables	5	5	5
Grain	5	4	5
Corn	4	4	2
Nursery/Greenhouse	3	4	4
Swine	3	3	3
Cattle	3	3	2
Cotton	3	2	2
Processing	3	3	3
Rural Home	2	2	2
Tobacco	2	2	2
Other Real Estate	2	2	2
Citrus	1	1	1
Other	5	5	5
Total	100%	100%	100%

As illustrated in the above chart, Associations had concentrations of *full-time farmers* of 5.00 percent or greater in only five commodities: poultry, forestry, dairy, fruits/vegetables, and grain. All five commodities have a large geographic dispersion with production over the entire AgFirst footprint. Also, many poultry, forestry, dairy, fruit/vegetables, and grain producers have significant secondary income from off-farm employment by a family member.

Concentrations within the Associations are further limited through the number of farm units producing poultry or dairy products. Poultry concentration is further dispersed as production is segregated among chicken, turkey, and egg production. Dairy herds range in size from less than one hundred cows to approximately ten thousand. Lower cost of production and reduction of supply have proved beneficial to poultry and dairy producers in 2011.

Forestry is divided principally into hardwood and softwood production and value-added processing. The timber from hardwood production is further processed into furniture, flooring, and high-grade paper and is generally located at the more northern latitudes and higher elevations. Softwood timber production is typically located in the coastal plains of the AgFirst footprint and is used for building materials for the housing market and pulp to make paper and hygiene products. Forestry production operations at the Associations range in size from less than fifty acres to thousands of acres, with value-added processing being conducted at sawmills, planer mills, and paper mills.

The fruits/vegetables portion of the aggregate Association portfolio is made up of a diverse group of many different fruits and vegetables grown throughout the AgFirst District footprint. The volume is spread broadly over the base of Associations.

As mentioned previously, loans exceeding an Association's delegated lending authority must be pre-approved by AgFirst. As a result, larger agribusiness loans are typically analyzed by AgFirst's commercial lending staff as well as the Association's own lending staff prior to an Association committing to such loans.

Exposure to losses is reduced further through collateralization and other credit enhancements, including federal government guarantees. Typically, multiple loans to the same borrower are cross-collateralized and cross-defaulted. By law, all long-term loans must be secured by a first lien on real estate with an initial loan to appraised value not exceeding 85.00 percent. As of December 31, 2011, such loans represent over 50.00 percent of the District Association loans.

Participations/Syndications

AgFirst has an active Capital Markets Unit that purchases and sells loan participations and syndications. The Capital Markets Loan Officers and Association Relationship Managers work with the Associations to originate loans within the District's territory, provide commercial loan expertise to augment the Associations' staff, as needed, and provide an outlet for loans that exceed Associations' various hold limits. Additionally, the Capital Markets Unit actively pursues the purchase of participations and syndications originated outside of the District's territory by other System institutions, commercial banks, and other lenders. These loans may be held as earning assets of AgFirst or sub-participated to the Associations. The Capital Markets Unit also sells participations outside of the District to manage AgFirst's and the District Associations' loan concentrations and hold positions.

AgFirst's participation volume outstanding decreased by 6.80 percent from year-end 2010 to 2011 and decreased by 12.50 percent from year-end 2009 to 2010. As with the Direct Notes, borrower demand in this portfolio is anticipated to remain moderate in 2011.

The following table shows total participations/syndications portfolio credit exposures as of December 31, 2011, 2010, and 2009. Participation purchased and sold balances include charge-offs, premiums, discounts, and deferred fees and costs.

	AgFirst Participations		
(dollars in thousands)	**2011**	**2010**	**2009**
Participations Purchased	$ 4,965,411	$ 5,392,636	$ 6,183,774
Less: Participations Sold	1,084,852	1,228,842	1,425,308
Net Outstanding	3,880,559	4,163,794	4,758,466
Available Unused Commitments	2,374,573	2,078,821	2,093,193
Letters of Credit and Guarantees	129,344	203,434	239,620
Total Exposure	$ 6,384,476	$ 6,446,049	$ 7,091,279

Like the Associations, AgFirst employs a number of management techniques to limit credit risk, including underwriting standards, limits on the amounts of loans purchased from a single originator, and maximum hold positions to a single borrower and commodity. Although the participations/syndications portfolio is comprised of a small number of relatively large loans, it is diversified both geographically and on a commodity basis. Concentration risk throughout the portfolio is mitigated through established maximum hold positions to a single borrower and to a single commodity. Management makes adjustments to credit policy and underwriting standards when appropriate as a part of the ongoing risk management process.

The following table illustrates AgFirst's participation/syndication portfolio by geographic distribution at December 31:

	AgFirst Participations					
(dollars in thousands)	**2011**		**2010**		**2009**	
Florida	$ 538,467	14%	$ 699,891	17%	$ 974,827	20%
North Carolina	452,335	12	465,068	11	566,539	12
Georgia	371,158	10	384,696	9	421,634	9
Virginia	201,524	5	208,033	5	218,663	5
Pennsylvania	177,685	5	243,316	6	305,646	6
South Carolina	163,888	4	115,054	3	174,489	4
Ohio	135,861	4	132,194	3	120,728	2
California	134,192	3	162,449	4	194,977	4
Alabama	132,471	3	140,027	3	150,946	3
Mississippi	129,842	3	171,812	4	143,477	3
Minnesota	119,590	3	97,376	2	78,399	2
Missouri	113,362	3	99,729	2	86,239	2
Texas	107,990	3	150,567	4	180,344	4
New York	93,855	2	87,736	2	84,503	2
Louisiana	79,757	2	86,858	2	86,381	2
Illinois	79,300	2	43,054	1	30,177	1
Kentucky	78,490	2	82,094	2	102,806	2
Oregon	77,550	2	89,862	2	94,356	2
Colorado	74,575	2	58,596	1	78,431	2
Tennessee	63,050	2	83,436	2	89,435	2
Connecticut	62,725	2	59,661	1	61,217	1
Delaware	57,328	1	70,444	2	89,106	2
Washington	56,167	1	61,054	2	82,337	2
Arkansas	51,948	1	47,470	1	50,161	1
North Dakota	38,446	1	31,237	1	31,638	1
Massachusetts	37,036	1	29,395	1	21,964	0
Iowa	35,689	1	38,914	1	42,168	1
New Jersey	33,236	1	34,402	1	34,158	1
Nebraska	29,490	1	34,773	1	12,577	0
Puerto Rico	28,042	1	28,102	1	29,748	0
Oklahoma	19,492	1	16,204	0	20,131	0
Other	106,018	2	110,290	3	100,264	2
	$ 3,880,559	100%	$ 4,163,794	100%	$ 4,758,466	100%

The largest major commodity concentrations are in the food and kindred products, agribusiness, and forestry groups. Food and kindred products, the largest commodity as of December 31, 2011, consist of meat, dairy, grain mill and other miscellaneous food products. The following shows the various major commodity groups in the portfolio and their percentage of the portfolio's outstanding volume at December 31:

AgFirst Participations	**Percent of Portfolio**		
Commodity Group	**2011**	**2010**	**2009**
Food and Kindred Products	16%	13%	13%
Agribusiness	13	14	12
Forestry	13	14	15
Electric Utilities	7	7	6
Poultry & Eggs	5	5	5
Cattle	5	5	5
Lumber/Paper	4	5	5
Citrus	4	5	6
Horticulture	4	4	5
Swine	4	3	5
Telephone Utilities	4	3	2
Sugar Cane/Sugar Beets	2	2	2
Other	19	20	19
Total	100%	100%	100%

Weakness continued in the housing related segments of the portfolio which include: lumber and building products companies, timber producers, landscape and sod nurseries, and borrowers with significant real estate debt. Increases in housing starts and a sustained recovery in the general economy are needed to improve the financial capacity of these borrowers.

Continued weakness in the general economy and resulting higher rate of unemployment could further compromise the credit quality of the District's borrowers who rely on non-farm income. Many borrowers who have historically had stable income from non-farm sources such as stock portfolios and capital gains income from traded assets have seen reductions in these income sources.

Other major segments of the District loan portfolio continued to perform well, including the sugar, orange juice, and row crop segments.

The following table represents the Participation/Syndication credit quality as of December 31:

Participation/Syndication **Credit Quality**	**2011**	**2010**	**2009**
Acceptable	85.20%	82.81%	83.44%
OAEM	9.38	10.07	7.18
Adverse	5.42	7.12	9.38
Total	100.00%	100.00%	100.00%

* *Adverse loans include substandard, doubtful, and loss loans.*

Correspondent Lending

AgFirst also maintains the Correspondent Lending Unit (Correspondent Lending), which consists primarily of first lien residential mortgages. Essentially all loans purchased by Correspondent Lending are guaranteed by the Financial National Mortgage Association (Fannie Mae) and/or the Federal Agricultural Mortgage Corporation (Farmer Mac), thereby limiting credit risk to AgFirst. The guarantees are in the form of Long-Term Standby Commitments to Purchase, which give AgFirst the right to deliver delinquent loans to the guarantor at par.

The table below illustrates the Correspondent Lending outstanding balance of loans at December 31:

	AgFirst Correspondent Lending					
(dollars in millions)	2011		2010		2009	
Rural Home Loans – Guaranteed	$ 2,003	92.23%	$ 1,765	90.16%	$ 1,479	88.49%
Part-time Farm Loans – Guaranteed	109	5.03	122	6.24	131	7.87
Agricultural Loans – Guaranteed	2	0.07	2	0.08	2	0.12
Non-guaranteed Loans	58	2.67	69	3.52	59	3.52
Total	$ 2,172	100.00%	$ 1,958	100.00%	$ 1,671	100.00%

Rural home loans are underwritten to conform to Fannie Mae underwriting standards and are guaranteed by Fannie Mae. Part-time farm loans conform to Farmer Mac underwriting standards and are guaranteed by Farmer Mac. During 2011, AgFirst purchased $480.4 million of rural home loans.

AgFirst owned $2.003 billion in rural home loans at December 31, 2011. These loans are the most significant portion of the Correspondent Lending portfolio due to the Associations' active participation in Fannie Mae home loan programs.

AgFirst owned $109.3 million in part-time farm loans at December 31, 2011. Part-time farm loans represent first lien mortgages on homes with property characteristics (such as acreage or agricultural improvements) that may not conform to Fannie Mae standards. These loans are guaranteed by Farmer Mac. The guarantee program for these loans was discontinued by Farmer Mac in 2010, which will result in lower part-time farm loan balances as these loans are repaid.

AgFirst owned $1.6 million of agricultural loans that are guaranteed by Farmer Mac at December 31, 2011. This segment is small, due primarily to the Associations' propensity to hold agricultural loans in-portfolio. A number of Associations obtain Farmer Mac guarantees for qualifying segments of their agricultural portfolios, thereby eliminating their need to sell those loans to AgFirst.

The $57.9 million of non-guaranteed loans at December 31, 2011 generally consists of loans that are being held for eventual delivery to, or guarantee by, Fannie Mae or Farmer Mac. Such loans are secured by first-lien mortgages and were considered high quality assets at time of purchase.

The majority of loans owned and/or serviced by AgFirst are sub-serviced through agreements with third parties. The total volume owned as of December 31, 2011 was $2.172 billion. The total volume serviced but not owned as of December 31, 2011 was $60.0 million.

MISSION RELATED INVESTMENTS

The FCA initiated a program in 2005 to allow System institutions to make and hold investments that stimulate economic growth and development in rural areas. The investments are subject to approval by the FCA on a case-by-case basis. FCA approved the Rural Housing Mortgage-Backed Securities pilot program and the Rural America Bonds pilot program as described below.

Rural Housing Mortgage-Backed Securities

Rural Housing Mortgage-Backed Securities (RHMS) must be fully guaranteed by a government agency or GSE. The rural housing loans backing the RHMS must be conforming first-lien residential mortgage loans originated by non-System lenders in "rural areas" as defined by the Farm Security and Rural Investment Act of 2002, or eligible rural housing loans originated by System lenders under FCA Regulations. Investment securities at December 31, 2011 included $683.1 million in RHMS classified as held-to-maturity, compared to $902.6 million at December 31, 2010 and $1.237 billion at December 31, 2009. In November 2009, the FCA approved a continuation of the RHMS program for another three years.

Rural America Bonds

In October 2005, the FCA approved the Rural America Bonds investment program for a three-year pilot period and in October 2008 approved a continuation of the program for an as yet undetermined time period. In recognition of the economic interdependence between agricultural and rural communities, AgFirst and the Associations seek to safely and soundly invest in debt obligations that support farmers, ranchers, agribusinesses, and their rural communities and businesses. In doing so, AgFirst and the Associations hope to increase the well-being and prosperity of American farmers, ranchers, and rural residents. As of December 31, 2011, the District had $319.0 million in the Rural America Bond program, compared to $309.6 million at December 31, 2010. The Bank had $171.5 million invested in the program as of December 31, 2011, an increase of $20.7 million from December 31, 2010. Of the $171.5 million, the Bank had $153.6 million reflected in investment securities and $17.9 million reflected as loans on the Consolidated Balance Sheet at December 31, 2011. In order to purchase additional investments under this program, the Bank must maintain a minimum net collateral ratio of 105.00 percent and a minimum total surplus ratio of 9.00 percent.

FARMER MAC

At December 31, 2011, AgFirst owned $840 thousand of class B voting restricted common stock, $391 thousand of class C non-voting unrestricted stock, $8.3 million of Farmer Mac MBS investment securities and had $110.9 million of loans guaranteed by Farmer Mac. District Associations had $354.2 million of loans guaranteed by Farmer Mac at December 31, 2011.

RISK MANAGEMENT

The organizational structure of AgFirst facilitates communication of operational and risk management issues throughout all layers of management and across all functional areas. AgFirst's President and Chief Operating Officer, who also acts as the Chief Risk Officer and reports directly to the Chief Executive Officer of the Bank, is responsible for:

- Providing overall leadership, vision, and direction for enterprise risk management;
- Establishing an integrated risk management framework for all aspects of risk across the organization;
- Ensuring development of risk management policies, including the quantification of management's risk appetite through specific risk limits;
- Implementing a set of risk metrics and reports, including key risk exposures and early warning indicators;
- Reviewing and approving recommendations for the allocation of economic capital to business activities based on risk, and optimizing the Bank's risk portfolio through business activities and risk transfer strategies;
- Improving the Bank's risk management readiness through coordination of communication and training programs, risk-based performance measurement and incentives, and other change management programs;
- Assigning responsibility for development of analytical systems and data management capabilities to support the risk management program; and
- Reporting periodically to the Board of Directors on actions taken to strengthen the Bank's system of internal controls.

Overview

The Bank is in the business of making agricultural and other loans that requires accepting certain risks in exchange for compensation for the risks undertaken. Proper management of the risks inherent in AgFirst's business is essential for current and long-term financial performance. The objectives of risk management are to identify and assess risks, and to properly and effectively mitigate, measure, price, monitor, and report risks in the Bank's business activities.

Types of risks to which the Bank has exposure include:

- *structural risk* — risk inherent in the business and related to the System structures comprised of interdependent networks of cooperative lending institutions,
- *credit risk* — risk of loss arising from an obligor's failure to meet the terms of its contract or failure to perform as agreed,
- *interest rate risk* — risk that changes in interest rates may adversely affect the Bank's operating results and financial condition,
- *liquidity risk* — risk of loss arising from the inability to meet obligations when they come due,
- *operational and reputational risk* — risk of loss resulting from inadequate or failed internal processes or systems, errors by employees or external events, and
- *political risk* — risk of loss of support for the System and agriculture by federal and state governments.

Structural Risk Management

Structural risk results from the fact that AgFirst, along with its related Associations, is part of the System, which is comprised of banks and associations that are cooperatively owned, directly or indirectly, by their borrowers. Because System institutions are financially and operationally interdependent, this structure at times requires action by consensus or contractual agreement. The Federal Farm Credit Banks Funding Corporation (Funding Corporation) provides for the issuance, marketing, and processing of Systemwide Debt Securities using a network of investment dealers and dealer banks. The System banks fund association loans with Systemwide debt. Refer to Note 8, *Bonds and Notes*, in the Notes to the Consolidated Financial Statements for further discussion. The banks are jointly and severally liable for the repayment of Systemwide Debt Securities, exposing each bank to the risk of default of the others. Although capital at the association level reduces the banks' credit exposures with respect to their related associations, that capital may not be available to support the payment of principal and interest on Systemwide Debt Securities.

In order to mitigate this risk, the System utilizes two integrated contractual agreements executed by and among the banks— the Amended and Restated Contractual Interbank Performance Agreement (CIPA) and the Second Amended and Restated Market Access Agreement (MAA). Under provisions of the CIPA, a score is calculated that measures the financial condition and performance of each district using various ratios that take into account each district's and bank's capital, asset quality, earnings, interest-rate risk, and liquidity. Based on these measures, the CIPA establishes an agreed-upon standard of financial condition and performance that each district must achieve and maintain. The CIPA also establishes monetary penalties if the performance standard is not met. These penalties will occur at the same point at which a bank would be required to provide additional monitoring information under the MAA.

The MAA establishes criteria and procedures for the banks that provide operational oversight and control over a bank's access to System funding if the creditworthiness of the bank declines below certain agreed-upon levels. The MAA provides for the identification and resolution of individual bank financial problems in a timely manner and discharges the Funding Corporation's statutory responsibility for determining conditions for each bank's participation in each issuance of Systemwide Debt Securities.

Credit Risk Management

Credit risk arises from the potential inability of an obligor to meet its repayment obligation and exists in outstanding loans, letters of credit, unfunded loan commitments, the investment portfolio and derivative counterparty credit exposures. The Bank manages credit risk associated with lending activities through an assessment of the credit risk profile of an individual obligor. The Bank sets underwriting standards and lending policies consistent with FCA regulations which provide direction to loan officers and are approved by the board of directors.

The credit risk management process begins with an analysis of the obligor's credit history, repayment capacity and financial position. Repayment capacity focuses on the obligor's ability to repay the obligation based on cash flows from operations or other sources of income, including non-farm income. Real estate mortgage loans must be secured by first liens on the real estate collateral. As required by FCA regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures.

The credit risk rating process for loans uses a two-dimensional loan rating structure, incorporating a 14-point risk rating scale to identify and track a borrower's probability of default and a separate scale addressing loss given default. The loan rating structure calculates estimates of loss through two components, borrower risk and transaction risk. Borrower risk is the risk of loss driven by factors intrinsic to the borrower. The transaction risk or facility risk is related to the structure of a credit (tenor, terms, and collateral).

Through their participation in loans or interests in loans to/from other institutions within the System and outside the System, the Bank and District Associations limit their exposure to both borrower and commodity concentrations. This also allows the Bank and District Associations to manage growth and capital and to improve geographic diversification. Concentration risk is reviewed and measured by industry, product, geography and customer limits.

Although neither the Bank nor any other System institution receives any direct government support, credit quality is indirectly enhanced by government support in the form of program payments to borrowers, which improve their ability to honor their commitments. However, due to the geographic location of the District and the resulting types of agriculture, government programs account for a relatively small percentage of net farm income in the territory served by the District Associations.

AgFirst's loan portfolio is divided into performing and high-risk categories. Although high risk assets remain elevated compared to historical levels, as a result of its credit risk management process, the Bank's high-risk assets continue to be a small percentage of the total loan volume and total assets. The high-risk assets, including accrued interest, at December 31 are detailed in the following table:

(dollars in thousands)	**2011**	**2010**	**2009**
AgFirst High-risk Assets			
Nonaccrual loans	$ 85,222	$ 115,720	$ 217,307
Restructured loans	38,757	45,303	–
Accruing loans 90 days past due	5,352	6,575	10,211
Total high-risk loans	129,331	167,598	227,518
Other property owned	44,157	39,719	25,909
Total high-risk assets	$ 173,488	$ 207,317	$ 253,427
Ratios			
Nonaccrual loans to total loans	0.42%	0.55%	1.02%
High-risk assets to total assets	0.59%	0.67%	0.82%

Nonaccrual Loans

Nonaccrual loans represent all loans for which there is a reasonable doubt as to the collection of principal and/or interest under the contractual terms of the loan. Nonaccrual loans for the Bank at December 31, 2011 were $85.2 million compared to $115.7 million at December 31, 2010. Nonaccrual loans decreased $30.5 million during 2011 due primarily to repayments of $79.9 million and charge-offs of uncollectible balances of $67.9 million (composed primarily of charge-offs in the forestry and processing segments). Other decreases to nonaccrual loans consisted of transfers to other property owned of $36.5 million and reinstatements to accrual status of $5.9 million. Offsetting these decreases were $157.7 million of loan balances transferred to nonaccrual status during 2011. The ten largest nonaccrual borrower relationships accounted for 61.51 percent of the total nonaccrual balance. At December 31, 2011, total nonaccrual loans were primarily classified in the forestry (31.16 percent of the total), processing (27.69 percent), cattle (12.44 percent), and other real estate (6.94 percent) segments. Some of these nonaccrual loans are secured by real estate, which has been negatively impacted by the current economic environment as discussed previously. Nonaccrual loans were 0.42 percent of total loans outstanding at December 31, 2011.

Troubled Debt Restructuring

A troubled debt restructuring occurs when a borrower is experiencing financial difficulties and a concession is granted to the borrower that the Bank would not otherwise consider. Concessions are granted to borrowers based on either an assessment of the borrower's ability to return to financial viability or a court order. The concessions can be in the form of a modification of terms, rates, or amounts owed. Acceptance of other assets and/or equity as payment may also be considered a concession. The type of alternative financing granted is chosen in order to minimize the loss incurred by the Bank. Troubled debt restructurings totaled $69.8 million at December 31, 2011, comprised of $38.8 million of accruing restructured loans and $31.0 million of nonaccruing restructured loans. Restructured loans were primarily in the swine (35.24 percent of the total), forestry (19.14 percent), nursery/greenhouse (14.34 percent), processing (14.05 percent), and cattle (10.44 percent) segments.

Other Property Owned

Other property owned (OPO) consists of assets once pledged as loan collateral that were acquired through foreclosure or deeded to the Bank (or a lender group) in satisfaction of secured loans. OPO may be comprised of real estate, equipment, and equity interests in companies or partnerships. OPO increased $4.4 million and totaled $44.2 million at December 31, 2011. The increase was due to property received in settlement of loans of $36.3 million, which was comprised primarily of two land holdings of $21.1 million and an ethanol plant totaling an additional $5.8 million. Offsetting this increase were OPO disposals of $17.9 million and OPO write-downs of $14.0 million. Disposals primarily included three land holdings totaling $10.7 million and a vineyard and winery holding of $2.4 million. Write-downs were comprised primarily of three land holdings totaling $8.4 million. The largest OPO holding at December 31, 2011, which was a parcel of land, was $11.3 million (25.69 percent of the total).

Interest Rate Risk Management

The objective of interest rate risk management is to generate an adequate level of net interest income in any interest rate environment. AgFirst uses a variety of analytical techniques to manage the complexities associated with offering numerous loan options. Interest rate sensitivity gap analysis is used to monitor the repricing characteristics of AgFirst's interest-earning assets and interest-bearing liabilities. Simulation analysis is used to determine the potential change in net interest income and in the market value of equity under various possible future market interest rate environments.

AgFirst and the District Associations adhere to a philosophy that loans should be priced competitively in the market and that loan rates and spreads should be contractually established at loan closing such that a borrower is not subject to rate changes at the discretion of management or boards of directors. Therefore, District Association variable rate and adjustable rate loans are generally indexed to market rates, and fixed rate loans are priced based on market rates. Loan products offered by the Associations include prime-indexed variable rate loans, LIBOR-indexed variable rate loans, one-, three- and five-year Treasury-indexed adjustable rate loans, and fixed rate loans. Variable rate and adjustable rate loans are offered with or without caps. Terms are available for up to 30 years. A variety of repayment options are offered, with the ability to pay on a monthly, quarterly, semi-annual or annual frequency. In addition, customized repayment schedules may be negotiated to fit a borrower's unique circumstances.

The following tables represent AgFirst's projected change in net interest income and market value of equity for various rate movements as of December 31, 2011:

Net Interest Income
(dollars in thousands)

Scenarios	Net Interest Income	% Change
+4.0% Shock	$453,199	(10.51)%
+2.0% Shock	$505,033	(0.27)%
Base line	$506,424	– %
-50% of 3M Tbill **	$506,877	0.09 %

Market Value of Equity
(dollars in thousands)

Scenarios	Assets	Liabilities*	Equity*	% Change
Book Value	$29,577,506	$27,828,236	$1,749,270	– %
+4.0% Shock	$27,784,721	$26,261,383	$1,523,338	(23.56) %
+2.0% Shock	$29,031,730	$27,165,183	$1,866,547	(6.34) %
Base line	$30,106,156	$28,113,184	$1,992,972	– %
-50% of 3M Tbill **	$30,110,631	$28,117,222	$1,993,409	0.02 %

* *For interest rate risk management, the $400.0 million in perpetual preferred stock is included in liabilities rather than equity.*

** *When the three-month Treasury bill interest rate is less than 4 percent, both the minus 200 and minus 400 basis point shocks are replaced with a downward shock equal to one-half of the three-month Treasury bill rate.*

The following table sets forth the repricing characteristics of interest-earning assets and interest-bearing liabilities outstanding at December 31, 2011. The amount of assets and liabilities shown in the table, which reprice or mature during a particular period, were determined in accordance with the earlier of term-to-repricing or contractual maturity, anticipated prepayments, and, in the case of liabilities, the exercise of call options.

	Repricing/Maturity Gap Analysis				
(dollars in thousands)	**0 to 6 months**	**6 months to 1 Year**	**1 to 5 Years**	**Over 5 Years**	**Total**
Floating Rate Loans					
Adjustable/Indexed Loans	$ 4,097,975	$ 24,901	$ 65,870	$ 16,947	$ 4,205,693
Fixed Rate Loans					
Fixed Rate Loans	63,677	35,430	135,598	42,636	277,341
Fixed Rate Prepayable	5,305,299	3,096,487	6,618,596	563,428	15,583,810
Nonaccrual Loans					
Nonaccrual Loans	–	–	–	85,222	85,222
Total Loans	**9,466,951**	**3,156,818**	**6,820,064**	**708,233**	**20,152,066**
Total Investments *	**3,209,763**	**1,034,547**	**2,509,919**	**1,109,865**	**7,864,094**
TOTAL INTEREST EARNING ASSETS	**$ 12,676,714**	**$ 4,191,365**	**$ 9,329,983**	**$ 1,818,098**	**$ 28,016,160**
Interest-Bearing Liabilities					
Systemwide bonds and notes	$ 14,041,936	$ 8,571,804	$ 4,137,908	$ 334,500	$ 27,086,148
Interest rate swaps	535,000	(175,000)	(310,000)	(50,000)	–
TOTAL INTEREST-BEARING LIABILITIES	**$ 14,576,936**	**$ 8,396,804**	**$ 3,827,908**	**$ 284,500**	**$ 27,086,148**
Interest Rate Sensitivity Gap	**$ (1,900,222)**	**$ (4,205,439)**	**$ 5,502,075**	**$ 1,533,598**	
Sensitivity Gap as % of Total Earning Assets	(6.78)%	(15.01)%	19.64%	5.47%	
Cumulative Gap	$ (1,900,222)	$ (6,105,661)	$ (603,586)	$ 930,012	
Cumulative Gap as a % of Total Earning Assets	(6.78)%	(21.79)%	(2.15)%	3.32%	
Rate Sensitive Assets/Rate Sensitive Liabilities	0.87	0.50	2.44	6.39	

** includes cash equivalents*

At December 31, 2011, the Repricing/Maturity Gap showed the Bank with a cumulative liability sensitive position out to one year as repricing/maturing debt exceeded assets that mature or reprice during that time period. Liability sensitivity implies an increase in net interest income in falling interest rate scenarios and lower net interest income in rising interest rate scenarios. However, the Repricing/Maturity Gap Analysis is a "point in time" view and is representative of the interest rate environment at December 31, 2011. The Repricing/Maturity Gap Analysis must be used with other analysis methods as the maturity and repricing attributes of balance sheet accounts react differently in changing interest rate environments. During a period of rising interest rates, call options on fixed rate debt are not exercised and the debt terms extend to reflect the longer original maturity dates. Prepayment optionality on fixed rate assets also slows as the economic incentive for borrowers to refinance decreases and extends the asset's term. To supplement the Repricing Maturity Gap Analysis the Bank utilizes financial simulation modeling. The results of simulation analyses on the Bank balance sheet reflect a neutral sensitivity position with a liability sensitive position in scenarios with higher interest rates. In a falling interest rate scenario, the balance sheet maturity/repricing position is relatively neutral. However, it should be noted that the low level of interest rates limits the falling interest rate scenario to a minimal change for the down interest rate shock.

At December 31, 2011, AgFirst had outstanding interest rate swaps with notional amounts totaling $535 million. All of these derivative transactions were executed to create synthetic floating-rate debt to achieve a lower cost of funding. AgFirst also had forward contracts to create a fixed purchase price with notional amounts totaling $66.4 million at December 31, 2011 (see further discussion below). The Bank may also use derivatives for asset/liability management purposes to reduce interest rate risk.

As of December 31, 2011, the Bank had committed to purchase $66.4 million of GNMA securities all settling by February, 2012. These commitments are considered (cash flow hedging) derivatives in the form of forward contracts. The market value of these securities had increased $319 thousand between the time the Bank had committed to purchase the securities and year-end. This amount, which represents the effective portion of the Bank's forward contracts, is included as a credit in Other Comprehensive Income (OCI) and as a debit in Other Assets as firm commitments in the Bank's Consolidated Balance Sheet at December 31, 2011.

AgFirst policy prohibits the use of derivatives for speculative purposes. See Note 17, *Derivative Financial Instruments and Hedging Activities*, in the Notes to the Consolidated Financial Statements for additional information. The following table shows the activity in derivatives during the year ended December 31, 2011:

Notional amounts *(dollars in millions)*	**Receive Fixed**	**Forward Contracts**
Balance at December 31, 2010	$ 1,135	$ 445
Additions	–	330
Maturities/amortizations	(600)	(709)
Terminations	–	–
Balance at December 31, 2011	$ 535	$ 66

Liquidity Risk Management

One of AgFirst's primary responsibilities is to maintain sufficient liquidity to fund the lending operations of the District Associations, in addition to its own needs. Along with normal cash flows associated with lending operations, AgFirst has two primary sources of liquidity: the capacity to issue Systemwide Debt Securities through the Federal Farm Credit Banks Funding Corporation; and cash and investments, including its available-for-sale portfolio. The Bank also maintains several lines of credit with commercial banks, as well as securities repurchase agreement facilities.

Investments and Cash and Cash Equivalents

Investment securities and cash and cash equivalents outstanding as of December 31, 2011 for AgFirst totaled $9.082 billion compared to $9.504 billion and $9.165 billion at December 31, 2010 and 2009, respectively.

AgFirst's investment portfolio and cash and cash equivalents consisted of the following security types as of December 31:

AgFirst Investment Securities and Cash and Cash Equivalents

(dollars in thousands)	**2011**		**2010**		**2009**	
Investment Securities						
Available for Sale						
Agency CMOs	$ 5,002,501	64.30%	$ 5,221,510	64.65%	$ 4,197,055	51.01%
Agency ARMs	1,650,829	21.22	1,561,784	19.33	2,337,499	28.42
Non-Agency CMOs	241,756	3.10	206,633	2.56	256,006	3.11
Asset-Backed Securities	30,324	0.39	34,437	0.43	47,465	0.58
Total Available for Sale	$ 6,925,410	89.01%	$ 7,024,364	86.97%	$ 6,838,025	83.12%
Held to Maturity						
Rural Housing MBS	$ 683,070	8.78%	$ 902,557	11.17%	$ 1,237,233	15.04%
MBS Guaranteed by Farmer Mac	8,261	0.11	11,091	0.14	12,818	0.16
Mission Related Investments	163,531	2.10	138,666	1.72	138,133	1.68
Total Held to Maturity	854,862	10.99	1,052,314	13.03	1,388,184	16.88
Total Investment Securities	$ 7,780,272	100.00%	$ 8,076,678	100.00%	$ 8,226,209	100.00%
Cash and Cash Equivalents						
Cash	$ 1,217,747	93.56%	$ 1,366,289	95.74%	$ 705,993	75.20%
Fed Funds	–	–	–	–	–	–
Master Notes	–	–	52,000	3.65	86,690	9.23
Repos	83,822	6.44	8,744	0.61	146,201	15.57
Total Cash and Cash Equivalents	$ 1,301,569	100.00%	$ 1,427,033	100.00%	$ 938,884	100.00%
Total Investment Securities and Cash and Cash Equivalents	$ 9,081,841		$ 9,503,711		$ 9,165,093	

Cash and cash equivalents, which decreased $125.5 million from December 31, 2010 to a total of $1.302 billion at December 31, 2011, consist primarily of cash on deposit, but also includes money market securities that are short term in nature (from overnight maturities to maturities that range up to 90 days). Money market securities must carry one of the two highest short-term ratings from a rating agency. The decrease in cash and cash equivalents was due primarily to the lower amount of cash needed to maintain 15 days of liquidity coverage on maturing debt at December 31, 2011 compared to December 31, 2010. FCA regulations provide that a System bank may hold certain eligible available-for-sale investments in an amount not to exceed 35.00 percent of its total loans outstanding. These investments serve to provide liquidity to the Bank's operations, to manage short-term funds, and to manage interest rate risk. AgFirst maintains an investment portfolio for these purposes comprised primarily of short-duration, high-quality investments. At year-end 2011, the Bank's eligible available-for-sale investments were 34.37 percent of the total loans outstanding.

Investment securities totaled $7.780 billion, or 26.30 percent of total assets at December 31, 2011, compared to $8.077 billion, or 26.24 percent, as of December 31, 2010. Investment securities decreased $296.4 million, 3.67 percent, compared to December 31, 2010 as management maintained the investment securities portfolio size generally proportionate with that of the loan portfolio and within regulatory and policy guidelines.

As of December 31, 2011, AgFirst exceeded all applicable regulatory liquidity requirements. FCA regulations require a liquidity policy that establishes a minimum "coverage" level of 90 days. "Coverage" is defined as the number of days that maturing debt could be funded with eligible available-for-sale investments and cash and cash equivalents maintained by the Bank.

At December 31, 2011, AgFirst's coverage was 205 days compared to 208 days at December 31, 2010. At December 31, 2011, the Bank's cash and cash equivalents position provided 25 days of the total 205 days of liquidity coverage. Investment securities fully backed by the U.S. government provided an additional 180 days of liquidity. Cash provided by the Bank's operating activities, primarily generated from net interest income in excess of operating expenses and maturities in the loan portfolio, is an additional source of liquidity for the Bank that is not reflected in the coverage calculation of 205 days.

Investment securities classified as being available-for-sale totaled $6.925 billion at December 31, 2011. Available-for-sale investments included $5.003 billion in Agency Collateralized Mortgage Obligations (CMOs), $1.651 billion in Agency Adjustable Rate Mortgages, $241.8 million in non-agency CMOs, and $30.3 million in asset-backed securities. Since the majority of the portfolio is invested in agency securities, the portfolio is highly liquid and potential credit loss exposure is limited.

AgFirst also maintains a portfolio of investments that are not held for liquidity purposes and are accounted for as a held-to-maturity portfolio. These investments are authorized by FCA Regulations that allow investments in Farmer Mac securities and also in specific investments approved by the FCA as Mission Related Investments. The vast majority of this portfolio is comprised of Mission Related Investments for a program to purchase RHMS, which when combined with eligible rural home loans, must not exceed 15.00 percent of total outstanding loans (see *Mission Related Investments* section above). Investment securities classified as being held-to-maturity totaled $854.9 million at December 31, 2011.

The FCA considers non-agency asset-backed or mortgage-backed investment securities ineligible if they fall below the top category (AAA/Aaa) credit rating by the Nationally Recognized Statistical Rating Organizations (NRSROs). The Bank must obtain specific approval from the FCA to continue to hold an ineligible security. For each of these investment securities in the Bank's portfolio at December 31, 2011 rated below AAA/Aaa (total fair value of $261.3 million and amortized cost of $314.2 million), the Bank has developed and submitted plans for approval by the FCA that permit the Bank to continue to hold the securities. The FCA has approved, with conditions, the Bank's plans for all but seven investments that have recently become ineligible. The Bank has submitted a plan to hold four of these recently ineligible securities and is in the process of submitting a plan to obtain approval from the FCA to hold the remaining three investments. Management is of the opinion that holding these securities will result in a higher return for the Bank than liquidating them. Based on the Bank's analysis, no other-than-temporary credit related impairment was recognized in 2011 on these recently ineligible securities.

For purposes of calculating the risk adjusted assets amount used in the permanent capital, total surplus, and core surplus regulatory ratios, certain Bank ineligible securities are risk weighted between 50 percent and 200 percent instead of 20 percent which is applicable to eligible non-agency securities. These ineligible securities had a fair value of $115.0 million and amortized cost of $139.3 million at December 31, 2011. Other ineligible securities must be deducted completely from both capital and risk adjusted assets, based on the extent of their below investment grade rating from NRSROs. These securities had a fair value of $70.2 million and amortized cost of $83.8 million at December 31, 2011. The fair value and amortized cost of ineligible non-agency reperformer CMO securities covered by Federal Housing Administration insurance and therefore risk weighted at the standard 20 percent, was $76.1 million and $91.0 million, respectively, at December 31, 2011. See the *Capital Resources* section below for further discussion of the regulatory ratios. In addition, all ineligible investments, except non-agency reperformer CMOs which meet certain conditions, are excluded from liquidity coverage as defined above.

Net unrealized gains related to the available-for-sale securities were $132.8 million at December 31, 2011, compared to $43.7 million at December 31, 2010. These net unrealized gains are reflected in Accumulated Other Comprehensive Income (AOCI) in the Financial Statements. The net unrealized gains stem from normal market factors such as the current interest rate environment.

The Bank performs periodic credit reviews, including other-than-temporary impairment analyses, on its entire investment securities portfolio. Additional analysis for each security not rated in the top category by the NRSROs is performed using a cash flow model with key assumptions and performance factors which may include credit default rate, prepayment rate, and loss severity. The objective is to quantify future possible loss of principal or interest due on each identified security. The credit enhancements specific to the individual security are considered as appropriate, and may include monoline credit insurance, subordination, over-collateralization, and excess interest spread. Asset-backed securities covered by insurers are analyzed with insurance and without, to quantify the extent of reliance on their guarantees. Based on the results of all analyses, the Bank recognized other-than-temporary credit related impairment of $9.3 million on asset-backed securities and non-agency CMOs in its portfolio for the year ended December 31, 2011, which was included in Net Other-Than-Temporary Impairment Losses on Investments in the Consolidated Statements of Income. Credit loss is defined as the shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis. Payment shortfalls, net of insurance recoveries, on asset-backed securities have totaled only $16.4 million life to date ($5.9 million in 2011), compared to credit related impairment charges life to date of $39.5 million ($3.6 million in 2011). Credit related impairment charges on non-agency CMOs have totaled $14.8 million life to date ($5.7 million in 2011). Payment shortfalls on non-agency CMOs totaled $311 thousand for 2011 and life to date. See Note 3, *Investment Securities,* in the Notes to the Consolidated Financial Statements for further information.

The Bank considers both a price, or “mark,” provided by a third party pricing service and a value determined using the results of a modeling process for purposes of determining the fair values of securities in the asset-backed and non-agency CMO portfolios, as well as the resulting unrealized gain/loss impact through AOCI. The Bank reviews and periodically discusses with the third party pricing service and valuation experts the assumptions used in their pricing models for the asset-backed and non-agency CMO securities impacted by inactive trading or distressed sales. This process ensures that, when relevant observable inputs are not available, the fair value reported for each security reflects the price expected to be received in an orderly transaction that is not a forced liquidation or distressed sale at the measurement date. The modeling process was factored into the pricing for the asset-backed and non-agency CMO security portfolios.

Systemwide Debt Securities

The U.S. government does not guarantee, directly or indirectly, Systemwide Debt Securities. However, the Farm Credit System, as a GSE, has benefited from broad access to the domestic and global capital markets. This access has provided the System with a dependable source of competitively priced debt which is critical for supporting the System’s mission of providing credit to agriculture and rural America. However, recent concerns regarding the government’s borrowing limit and budget imbalances have further highlighted the risks to the System relating to the U.S. fiscal situation. These risks include the implied link between the credit rating of the System and the U.S. Government given the System’s status as a GSE.

AgFirst’s primary source of liquidity comes from its ability to issue Systemwide Debt Securities, which are the general unsecured joint and several obligations of the System banks. AgFirst continually raises funds to support its mission to provide credit and related services to the rural and agricultural sectors, to repay maturing Systemwide Debt Securities, and to meet other obligations. As a GSE, AgFirst has access to the nation’s and world’s debt and capital markets. This access has provided AgFirst with a dependable source of competitively priced debt that is critical to support its mission. In August 2011, Standard & Poor’s Ratings Services lowered its long-term sovereign credit rating for the U.S. to AA+ from AAA, and affirmed the A-1+ short-term rating. Their outlook on the long-term rating of the U.S. remained negative. Concurrently with such actions, Standard & Poor’s Ratings Services lowered the long-term debt rating for the System to AA+ from AAA; however, the A-1+ short-term rating was affirmed, while the outlook on the long-term debt rating of the System remained negative. Also in August 2011, Moody’s Investors Service and Fitch Ratings affirmed the Aaa and AAA ratings of the U.S. and affirmed the System’s Aaa and AAA long-term debt rating and short-term debt as P-1 and F-1. However, Moody’s Investors Service did change the ratings outlook of the U.S. and the System to negative. Similarly, in November 2011, Fitch Ratings, Inc. changed its outlook of the U.S. and the System from “stable” to “negative.”

These changes to the System’s credit ratings and any future negative changes in the System’s credit ratings and/or outlook could increase borrowing costs, limit access to the debt capital markets and trigger additional collateral requirements under derivative contracts and other borrowing arrangements. Any of these changes may also reduce earnings and have a material adverse effect on liquidity, ability to conduct normal business operations, and financial condition and results of operations. Despite these ratings changes and some continuing adversity in the financial debt markets, as a result of the System’s financial performance, credit quality and standing in the capital markets, AgFirst anticipates continued access to funding necessary to support the District’s and Bank’s needs. AgFirst’s year-to-date average balance of Systemwide Debt Securities at December 31, 2011, was $27.371 billion. At December 31, 2011, AgFirst had $27.086 billion in total System debt outstanding compared to $28.326 billion at December 31, 2010 and $28.694 billion at December 31, 2009.

AgFirst’s participation in outstanding Systemwide Debt Securities as of December 31, 2011 is shown in the following table:

	Bonds		Discount Notes		Total	
Maturities	**Amortized Cost**	**Weighted Average Interest Rate**	**Amortized Cost**	**Weighted Average Interest Rate**	**Amortized Cost**	**Weighted Average Interest Rate**
			(dollars in thousands)			
2012	$ 8,594,066	0.42%	$ 3,158,888	0.14%	$ 11,752,954	0.34%
2013	5,823,057	0.58	–	–	5,823,057	0.58
2014	2,848,961	0.89	–	–	2,848,961	0.89
2015	1,761,741	1.43	–	–	1,761,741	1.43
2016	1,235,979	2.01	–	–	1,235,979	2.01
2017 and after	3,663,456	2.68	–	–	3,663,456	2.68
Total	$ 23,927,260	1.02%	$ 3,158,888	0.14%	$ 27,086,148	0.92%

In the preceding table, weighted average interest rates include the effect of related derivative financial instruments.

Refer to Note 8, *Bonds and Notes*, in the Notes to the Consolidated Financial Statements, for additional information related to debt.

Lines of Credit

AgFirst maintains a $150.0 million unsecured committed line of credit facility from its primary commercial depository bank. The line of credit is tied to AgFirst's master cash management clearing account. The Bank has securities repurchase agreement facilities with three commercial banks that range in terms from overnight to nine months. Also, AgFirst has overnight Fed Funds lines of credit with two commercial banks.

Operational and Reputational Risk Management

Operational risk is the risk of loss resulting from inadequate or failed processes or systems, human factors or external events, including the execution of unauthorized transactions by employees, errors relating to transaction processing and technology, breaches of the internal control system and the risk of fraud by employees or persons outside the System. AgFirst's and the Associations' boards of directors are required, by regulation, to adopt internal control policies that provide adequate direction to their respective institutions in establishing effective controls over and accountability for operations, programs, and resources. The policies must include, at a minimum, the following items:

- direction to management that assigns responsibility for the internal control function to an officer of the institution,
- adoption of internal audit and control procedures,
- direction for the operation of a program to review and assess an institution's assets,
- adoption of loan, loan-related assets and appraisal review standards, including standards for scope of review selection and standards for work papers and supporting documentation,
- adoption of asset quality classification standards,
- adoption of standards for assessing credit administration, including the appraisal of collateral, and
- adoption of standards for the training required to initiate a program.

In addition, AgFirst has implemented a Risk Management Policy to ensure that business exposures to risk are identified, measured and controlled, using the most effective and efficient methods to eliminate, reduce, or transfer such exposures. AgFirst's risk management structure was designed to ensure that an effective enterprise-wide risk management program is in place. Exposure to operational risk is typically identified with the assistance of senior management and internal audit plans developed with higher risk areas receiving more review.

Political Risk Management

System institutions are instrumentalities of the federal government and are intended to further governmental policy concerning the extension of credit to or for the benefit of agricultural and rural America. The System and its borrowers may be significantly affected by federal legislation that impacts the System directly, such as changes to the Farm Credit Act, or indirectly, such as agricultural appropriations bills. However, government programs account for a relatively small percentage of net farm income in the territory served by the District Associations. Political risk to the System is the risk of loss of support for the System or agriculture by the U.S. government.

The District addresses political risk by actively supporting the Farm Credit Council, which is a full-service, federal trade association representing the System before Congress, the Executive Branch, and others. The Council provides the mechanism for "grassroots'' involvement in the development of System positions and policies with respect to federal legislation and government actions that impact the System. Additionally, the District takes an active role in representing the individual interests of System institutions and their borrowers before Congress. In addition to the Farm Credit Council, each district has its own Council, which is a member of the Farm Credit Council. The district Councils represent the interests of their members on a local and state level, as well as on a federal level.

ALLOWANCE FOR LOAN LOSSES

The Bank maintains an allowance for loan losses at a level management considers adequate to provide for probable and estimable credit losses within the loan portfolio as of each reported balance sheet date. The Bank increases the allowance by recording a provision for loan losses in the income statement. Loan losses are recorded against and serve to decrease the allowance when management determines that any portion of a loan is uncollectible. Any subsequent recoveries are added to the allowance. Impaired and certain other significant loans were reviewed individually to determine that appropriate reserves were in place at year end. All other participation loans were analyzed collectively and general reserves were established based on that collective analysis including the risk rating and potential for loss given default of the underlying loans.

The allowance for loan losses was $27.7 million at December 31, 2011, as compared with $14.9 million and $32.3 million at December 31, 2010 and 2009, respectively. The increase during 2011 of $12.8 million was due primarily to the provision expense of $80.2 million, offset by loan charge-offs of $67.8 million. Charge-offs were related primarily to the forestry (27.27 percent of the total) and processing (22.54 percent) segments. The allowance at December 31, 2011 included specific reserves of $9.0 million (32.65 percent of the total) primarily related to credits for participation borrower relationships within the forestry and processing industries and $18.7 million of general reserves (67.35 percent) attributed to participation loans. The total allowance at December 31, 2011 was comprised primarily of reserves for processing (22.16 percent), forestry (20.74 percent), and non-farm income (14.03 percent) segments. Declining real estate values impacted charge-offs and reserves in several of these loan segments. See Note 4, *Loans and Allowance for Loan Losses*, in the Notes to the Consolidated Financial Statements for further information. See *Provision for Loan Losses* section below for details regarding increases to the allowance from provision expense.

The following table presents the activity in the allowance for loan losses for the most recent three years at December 31:

AgFirst Allowance for Loan Losses Activity:

(dollars in thousands)	**2011**	**2010**	**2009**
Balance at beginning of year	$ 14,873	$ 32,292	$ 44,565
Charge-offs:			
Real Estate Mortgage	(24,572)	(42,430)	(25,904)
Production and Intermediate-Term	(26,023)	(8,590)	(645)
Agribusiness	(3,847)	(7,379)	(32,203)
Energy	(3,218)	–	–
Rural Residential Real Estate	(36)	–	(328)
Other (including Mission Related)	(10,083)	–	–
Total charge-offs	(67,779)	(58,399)	(59,080)
Recoveries:			
Real Estate Mortgage	320	799	34
Production and Intermediate-Term	78	19	–
Agribusiness	–	160	125
Other (including Mission Related)	–	–	–
Total recoveries	398	978	159
Net (charge-offs) recoveries	(67,381)	(57,421)	(58,921)
Provision for (reversal of allowance for) loan losses	80,222	40,002	46,648
Balance at end of year	$ 27,714	$ 14,873	$ 32,292
Ratio of net (charge-offs) recoveries during the period to average loans outstanding during the period	(0.329)%	(0.276)%	(0.278)%

The allowance for loan losses by loan type for the most recent three years at December 31 is presented in the following table:

AgFirst Allowance for Loan Losses by Loan Type *(dollars in thousands)*	**2011**	**2010**	**2009**
Real Estate Mortgage	$ 8,882	$ 4,836	$ 11,583
Production and Intermediate-Term	12,654	5,938	11,606
Agribusiness	4,974	2,722	8,286
Communication	233	69	72
Energy	283	307	274
Rural Residential Real Estate	37	–	12
Water and Waste Disposal	22	–	–
Other (including Mission Related)	629	1,001	459
Total	$ 27,714	$ 14,873	$ 32,292

The allowance for loan losses as a percentage of loans outstanding and as a percentage of certain other credit quality indicators at December 31 is shown below:

	2011	**2010**	**2009**
Allowance for loan losses to loans	0.14%	0.07%	0.15%
Allowance for loan losses to nonaccrual loans	32.52%	12.85%	14.92%
Allowance for loan losses to participation loans and Correspondent Lending loans	0.46%	0.24%	0.50%

Despite negative credit quality trends, the financial positions of the Bank and District Associations' borrowers have generally remained strong as farmers' net cash income has been at favorable levels. This has been due, in part, to increases in commodity prices and direct federal government payments. With borrowers' generally strong financial positions and the continued management emphasis on underwriting standards, the credit quality of the Bank loan portfolio has remained sound despite the trends. However, as discussed previously, uncertainty in the general economic environment has increased the potential for additional prospective risks in the loan portfolio. See Note 4, *Loans and Allowance for Loan Losses*, in the Notes to the Consolidated Financial Statements and the *Significant Accounting Policies* section above for further information concerning the allowance for loan losses.

RESULTS OF OPERATIONS

Net Income

AgFirst net income totaled $385.5 million for the year ended December 31, 2011, a decrease of $31.9 million from 2010. AgFirst net income totaled $417.4 million for the year ended December 31, 2010, an increase of $108.3 million over 2009. Major components of the changes in net income for the referenced periods are outlined in the following table and discussion:

Changes in Net Income *(dollars in thousands)*	**Year Ended December 31,** **2011**	**2010**
Net income (for prior year)	$ 417,395	$ 309,143
Increase (decrease) due to:		
Total interest income	(65,409)	(78,043)
Total interest expense	88,940	159,628
Net interest income	23,531	81,585
Provision for loan losses	(40,220)	6,646
Noninterest income	(19,762)	11,188
Noninterest expense	4,514	8,833
Total increase (decrease) in net income	(31,937)	108,252
Net income	$ 385,458	$ 417,395

Key Results of Operations Comparisons

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

Key Results of Operations Comparisons	**For the Year Ended** **12/31/11**	**12/31/10**	**12/31/09**
Return on average assets	1.29%	1.37%	1.03%
Return on average shareholders' equity	18.14%	22.25%	20.90%
Net interest income as a percentage of average earning assets	2.08%	1.96%	1.66%
Net (charge-offs) recoveries to average loans	(0.329)%	(0.276)%	(0.278)%

Interest Income

Total interest income for the year ended December 31, 2011 was $888.1 million, a decrease of $65.4 million, as compared to the same period of 2010. Total interest income for 2010 was $953.5 million, a decrease of $78.0 million, as compared to the same period of 2009. The decrease in both years was primarily the result of lower earning asset yields due to the declining market interest rate environment. Also, the volume of interest earning assets decreased in 2011, with a decrease in average earning assets of $583.9 million. The average yield on interest earning assets decreased 16 basis points in 2011.

The following table illustrates the impact of volume and yield changes on interest income:

Net Change in Interest Income *(dollars in thousands)*	**Year Ended December 31,** **2011-2010**	**2010-2009**
Current year increase (decrease) in average earning assets	$ (583,890)	$ (372,780)
Prior year average yield	3.27%	3.49%
Interest income variance attributed to change in volume	(19,086)	(13,017)
Current year average earning assets	28,586,241	29,170,131
Current year increase (decrease) in average yield	(0.16)%	(0.22)%
Interest income variance attributed to change in yield	(46,323)	(65,026)
Net change in interest income	$ (65,409)	$ (78,043)

Interest Expense

Total interest expense for the year ended December 31, 2011 was $293.3 million, a decrease of $88.9 million, as compared to the same period of 2010. Total interest expense for the year ended December 31, 2010 was $382.3 million, a decrease of $159.6 million, as compared to the same period of 2009. The decrease in both years was primarily attributed to the decrease in average rates paid on System debt obligations.

The following table illustrates the impact of volume and rate changes on interest expense:

Net Change in Interest Expense *(dollars in thousands)*	**Year Ended December 31,** **2011-2010**	**2010-2009**
Current year increase (decrease) in average interest-bearing liabilities	$ (841,617)	$ 141,815
Prior year average rate	1.34%	1.91%
Interest expense variance attributed to change in volume	(11,309)	2,715
Current year average interest-bearing liabilities	27,607,491	28,449,108
Current year increase (decrease) in average rate	(0.28)%	(0.57)%
Interest expense variance attributed to change in rate	(77,631)	(162,343)
Net change in interest expense	$ (88,940)	$ (159,628)

Net Interest Income

Net interest income increased from 2010 to 2011 and from 2009 to 2010, as illustrated by the following table:

AgFirst Analysis of Net Interest Income
Year Ended December 31,
(dollars in thousands)

	2011			**2010**			**2009**		
	Avg. Balance	**Interest**	**Avg. Yield**	**Avg. Balance**	**Interest**	**Avg. Yield**	**Avg. Balance**	**Interest**	**Avg. Yield**
Loans	$ 20,504,629	$ 691,762	3.37%	$ 20,817,231	$ 760,681	3.65%	$ 21,198,295	$ 830,778	3.92%
Cash & investments	8,081,612	196,349	2.43%	8,352,900	192,839	2.31%	8,344,616	200,785	2.41%
Total earning assets	$ 28,586,241	$ 888,111	3.11%	$ 29,170,131	$ 953,520	3.27%	$ 29,542,911	$ 1,031,563	3.49%
Interest-bearing liabilities	$ 27,607,491	$ (293,334)	1.06%	$ 28,449,108	$ (382,274)	1.34%	$ 28,307,293	$ (541,902)	1.91%
Spread			2.05%			1.93%			1.58%
Impact of capital	$ 978,750		0.03%	$ 721,023		0.03%	$ 1,235,618		0.08%
Net Interest Income (NII) & NII to average earning assets		$ 594,777	2.08%		$ 571,246	1.96%		$ 489,661	1.66%

Net interest income for the year ended December 31, 2011 was $594.8 million compared to $571.2 million for the same period of 2010, an increase of $23.5 million or 4.12 percent. The net interest margin was 2.08 percent and 1.96 percent in the current year and previous year, respectively, an improvement of 12 basis points. The increase in the net interest margins was primarily attributable to the ability to refinance outstanding debt at favorable interest rates in the current low interest rate environment. During 2011, 2010, and 2009, the Bank called debt totaling $21.490 billion, $28.087 billion, and $25.838 billion, respectively, and was able to lower cost of funds relative to assets, which did not repay or reprice as quickly. Over time, as interest rates change and as assets prepay or reprice in a manner more consistent with historical experience, the positive impact on the net interest margin that the Bank has experienced over the last several years from calling debt will likely diminish. Loan pricing compared to the underlying cost of funds also improved during the 2011 period, reflecting increased liquidity and credit risk premiums in the lending markets. Change in net interest income due to the decrease in balance sheet volume was minimal as a result of decreased loan demand previously discussed.

Provision for Loan Losses

AgFirst measures risks inherent in its portfolio on an ongoing basis and as necessary, recognizes provision for loan loss expense so that appropriate reserves for loan losses are maintained. The $80.2 million in provision for loan loss expense for the year ended December 31, 2011 consisted of $71.9 million related to reserves for specific credits and $8.3 million related to general reserves. Provision expense for 2011 consisted primarily of specific reserve increases for three participation borrower relationships totaling $30.4 million. Provision expense for 2011 primarily related to borrowers in the forestry (28.21 percent of the total) and processing (25.33 percent) segments.

As mentioned previously, declining real estate values were, in part, the reason for some of the provision expense recognized by the Bank. See Note 4, *Loans and Allowance for Loan Losses*, in the Notes to the Consolidated Financial Statements for further information.

Noninterest Income

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

Noninterest Income	**For the Year Ended December 31,**			**Increase (Decrease)**	
(dollars in thousands)	**2011**	**2010**	**2009**	**2011/ 2010**	**2010/ 2009**
Loan fees	$ 12,267	$ 16,309	$ 13,312	$ (4,042)	$ 2,997
Gains (losses) from other property owned, net	(12,192)	(5,392)	(2,824)	(6,800)	(2,568)
Gains (losses) on investments, net	3,048	1,568	9,918	1,480	(8,350)
Net impairment losses on investments	(9,253)	(11,912)	(26,168)	2,659	14,256
Gains (losses) on derivatives, net	–	–	469	–	(469)
Gains (losses) on sales of rural home loans, net	(262)	(112)	1	(150)	(113)
Patronage refunds from other Farm Credit Institutions	2,632	2,928	5,327	(296)	(2,399)
Insurance premium refund	–	10,440	–	(10,440)	10,440
Other noninterest income	2,587	4,760	7,366	(2,173)	(2,606)
Total noninterest income	$ (1,173)	$ 18,589	$ 7,401	$ (19,762)	$ 11,188

The decrease in loan fees in 2011 and the increase in loan fees in 2010 were due primarily to a $3.1 million prepayment penalty for a significant loan that paid off in 2010.

The increase in net losses from other property owned during 2011 primarily resulted from write-downs of three land holdings. See discussion of 2011 expense in the *Other Property Owned* section above.

Gains on investments during 2011 and 2010 were the result of normal investment activities related to managing the composition and overall size of the Bank's portfolio. Gains on investments during 2009 were from sales to achieve certain portfolio limits and liquidity parameters.

The net impairment losses on investments in 2011 and 2010 were due to the recognition of credit related other-than-temporary impairment on certain asset-backed and non-agency CMO securities in the Bank's investment portfolio. See further discussion in the *Investments and Cash and Cash Equivalents* section above.

Patronage refunds from other Farm Credit institutions decreased $296 thousand in 2011 and $2.4 million in 2010. These decreases resulted primarily from the amount of dividends received from Farmer Mac senior cumulative perpetual preferred stock that was purchased at the end of third quarter 2008 and redeemed in full by Farmer Mac in January 2010. Also, for 2009, there was an increase in patronage received from another System bank to which, during 2008, the Bank sold a total of $200 million participation interest in its direct note receivable from a District Association.

The Bank recorded $10.4 million of insurance premium refunds during the first quarter of 2010 from the Farm Credit System Insurance Corporation (FCSIC), which insures the System's debt obligations. These payments are nonrecurring and resulted from the assets of the Farm Credit Insurance Fund exceeding the secure base amount as defined by the Farm Credit Act.

Other noninterest income was $2.6 million for the year ended December 31, 2011, or a $2.2 million decrease compared to December 31, 2010, primarily due to a $2.0 million loss reserve for unfunded commitments recorded in 2011. The $2.6 million decrease in 2010 compared to 2009 was due primarily to a captive insurance allocated loss based on claims experience recorded in 2010, compared to a gain recorded in 2009 as well as a gain recorded in 2009 from the Bank's termination of the captive mortgage insurance program and income from outside sources for services to Associations and other Farm Credit System entities.

Noninterest Expense

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

Noninterest Expense	**For the Year Ended December 31,**			**Increase/(Decrease)**	
(dollars in thousands)	**2011**	**2010**	**2009**	**2011/ 2010**	**2010/ 2009**
Salaries and employee benefits	$ 46,881	$ 43,105	$ 40,960	$ 3,776	$ 2,145
Occupancy and equipment	14,360	15,675	14,720	(1,315)	955
Insurance Fund premiums	5,360	5,147	20,605	213	(15,458)
Other operating expense	24,920	21,401	21,873	3,519	(472)
Called debt expense	27,450	38,420	36,531	(10,970)	1,889
Correspondent lending servicing expense	8,847	8,413	6,303	434	2,110
Other noninterest expenses	106	277	279	(171)	(2)
Total noninterest expenses	$ 127,924	$ 132,438	$ 141,271	$ (4,514)	$ (8,833)

Salaries and employee benefits increased over the three year period of 2009 through 2011 as a result of normal salary administration and increased benefit costs as well as an increase in the number of employees during 2011.

The $213 thousand increase in 2011 and $15.5 million decrease in 2010 in the Insurance Fund premiums resulted primarily from a change in the premium rate. The annual premium rate was 20 basis points for 2009. The Insurance Fund Board decreased the premium to 5 basis points for 2010, and increased the premium to 6 basis points for 2011. The premium rate for 2012 is 5 basis points.

Other operating expense increased $3.5 million in 2011, or 16.44 percent, compared to 2010. A portion of the increase resulted from an additional $1.3 million in consulting services expense required for certain system enhancements. The remainder of the increase in other operating expenses was comprised of numerous and varied expenses, none of which individually had a significant increase in the twelve months ended December 31, 2011, compared to the same period in 2010.

Concession or debt issuance expense is amortized over the life of the underlying debt security. When debt securities are called prior to maturity, any unamortized concession is expensed. Called debt expense decreased $11.0 million and increased $1.9 million for the years ended December 31, 2011 and 2010, respectively. Call options were exercised on bonds totaling $21.490 billion in 2011 and $28.087 billion in 2010. The called debt expense is more than offset by interest expense savings realized as called debt is replaced by new debt issued at a lower rate of interest. Over time, the favorable effect on net interest income is diminished as earning assets reprice downward.

The increases in correspondent lending servicing expense for 2011 and 2010 are due primarily to increased agency guarantee fees resulting from higher volume in the correspondent lending portfolio.

Other noninterest expense primarily consists of amortization of mandatorily redeemable preferred stock issuance costs which fully amortized in May, 2011.

CAPITAL

Capital serves to support future asset growth, investment in new products and services, and to provide protection against credit, interest rate, and other risks, and operating losses. A sound capital position is critical to provide protection to investors in Systemwide Debt Securities and to ensure long-term financial success.

The AgFirst Capitalization Plan (the "Plan") approved by the Bank's board of directors establishes guidelines to ensure that adequate capital is maintained for continued financial viability, to provide for growth necessary to meet the needs of members/borrowers, and to ensure that all stockholders are treated equitably. The Bank's capital objectives are considered adequate to support inherent risk. There were no material changes to the Plan for 2011 that have an effect on the Bank's ability to retire stock and distribute earnings.

Total shareholders' equity at December 31, 2011 was $2.149 billion, compared to $1.903 billion and $1.580 billion at December 31, 2010 and 2009, respectively. The increase in 2011 of $246.5 million was primarily related to the increase in retained earnings from net income of $385.5 million and $89.1 million in net unrealized gains during 2011 on investments available-for-sale, a component of AOCI. These increases were offset by patronage declared of $191.1 million, preferred stock dividends paid of $27.4 million, and the net retirement of $12.2 million in capital stock and participation certificates. The total AOCI balance at December 31, 2011 was a positive $124.0 million compared to a positive $32.3 million at December 31, 2010. The increase in total shareholders' equity of $322.5 million during 2010 was primarily related to net income of $417.4 million and $164.8 million in net unrealized gains for investments available-for-sale, offset by $200.8 million of patronage declared and preferred stock dividends paid of $27.4 million.

Capital stock and participation certificates totaled $405.8 million at December 31, 2011, compared to $417.3 million at December 31, 2010, a decrease of $11.6 million. This decrease was due primarily to stock redemption related to participation loans purchased from Associations. The Associations are required to maintain ownership in the Bank in the form of Class B and Class C stock. The Associations' minimum stock requirement is 1.75 percent of Association Direct Note balances. A stock equalization computation is made annually and the decrease in the Direct Note balances mentioned in the *Direct Note* section above explains the fluctuations in Association owned capital stock.

On December 15, 2011, AgFirst redeemed $225.0 million of Mandatorily Redeemable Cumulative Preferred Stock which was issued on May 17, 2001, at a par value of $1 thousand per share. The stock was redeemed at par value together with accrued and unpaid dividends. On October 14, 2003, AgFirst issued $150.0 million of Perpetual Non-Cumulative Preferred Stock at a par value of $1 thousand per share. On June 8, 2007, AgFirst issued $250.0 million of Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock, Series 1. See Note 9, *Mandatorily Redeemable Preferred Stock*, Note 10, *Shareholders' Equity*, and Note 22, *Subsequent Events,* in the Notes to the Consolidated Financial Statements for further information concerning the preferred stock issuances.

Regulatory Ratios

The Bank's regulatory ratios at December 31 are shown in the following table:

	Regulatory Minimum	AgFirst Ratio as of 12/31/11	12/31/10	12/31/09
Permanent Capital Ratio	7.00%	24.27%	21.22%	16.86%
Total Surplus Ratio	7.00%	24.24%	21.19%	16.83%
Core Surplus Ratio	3.50%	17.08%	13.79%	9.85%
Net Collateral Ratio*	103.00%	106.49%	106.44%	105.66%

*The regulatory minimum net collateral ratio was 104.00% previous to the redemption of the Mandatorily Redeemable Cumulative Preferred Stock on December 15, 2011.

FCA sets minimum regulatory capital requirements for System banks and associations. Capital adequacy is evaluated using a number of regulatory ratios. According to the FCA regulations, each institution's permanent capital ratio is calculated by dividing permanent capital by a risk-adjusted asset base. Risk-adjusted assets refer to the total dollar amount of the institution's assets adjusted by an appropriate credit conversion factor as defined by regulation. Generally, higher credit conversion factors are applied to assets with more inherent risk.

The FCA notified AgFirst that the June 2007 issuance of $250.0 million of Perpetual Non-Cumulative Subordinated Preferred Stock (as discussed above) could be included in core surplus only up to an amount not to exceed 25.00 percent of total core surplus, inclusive of the preferred stock component. At December 31, 2011, the full amount of this preferred stock issuance could be included in core surplus.

Subsequent to the redemption of the $225.0 million of Mandatorily Redeemable Cumulative Preferred Stock on December 15, 2011 (as discussed above), the FCA further notified AgFirst that the October 2003 issuance of $150.0 million of Perpetual Non-Cumulative Preferred Stock (as discussed above) could also be included in core surplus up to an amount not to exceed 25.00 percent of total core surplus, inclusive of the preferred stock component. Prior to December 15, 2011, the $150.0 million Perpetual Non-Cumulative Preferred Stock was not included in core surplus.

For all periods presented, AgFirst exceeded minimum regulatory standards for all of the ratios. Regulatory ratios for each District Association at December 31 are presented in the *Direct Notes* section above. All Associations met all of the regulatory minimum capital requirements at December 31, 2011.

Unlike the permanent capital, total surplus and core surplus ratios, the net collateral ratio does not incorporate any risk-adjusted weighting of assets. The collateral ratio is calculated by dividing the Bank's collateral, as defined by FCA regulations, by total liabilities. The permanent capital, total surplus, and core ratios are calculated using three-month average daily balances for both capital and assets. The temporary net gains in AOCI, as discussed above, do not affect the reported capital ratios because the effect of AOCI is excluded entirely from the risk-based capital ratios. The Bank's permanent capital, total surplus, and core surplus ratios increased at December 31, 2011 as compared to December 31, 2010, primarily as a result of the increase in capital exceeding the growth in assets on both a total and risk adjusted basis. The increase in these ratios at December 31, 2010 compared to December 31, 2009, was also the result in part of FCA's approval of a change in capital treatment of certain ineligible securities. Beginning in the second quarter of 2010, more favorable capital treatment was permitted for the risk weighting of the senior-most positions of asset-backed securities and non-agency CMOs, as well as guaranteed amounts of non-agency reperformer CMOs. For purposes of the net collateral ratio, all ineligible investments are stated at lower of cost or market, except that guaranteed amounts of non-agency reperformer CMOs are used if higher than the lower of cost or market. The core surplus ratio increased 29 basis points as of December 31, 2011 as a result of AgFirst including a portion of the $150.0 million preferred stock (subject to FCA's limitations, as discussed above) effective with the December 15, 2011 redemption of the Mandatorily Redeemable Preferred Stock. The December 31, 2011 net collateral ratio was negatively impacted by 82 basis points due to not replacing the Mandatorily Redeemable Cumulative Preferred Stock.

Refer to Note 10, *Shareholders' Equity*, in the Notes to the Consolidated Financial Statements for additional information regarding regulatory capitalization requirements and restrictions.

ECONOMIC CAPITAL

As discussed previously (see *Risk Management* section above), risk is an inherent part of the Bank's business activities. The Bank's capital management framework is intended to ensure there is sufficient capital to support the underlying risks of our business activities, exceed all regulatory capital requirements, and achieve certain capital adequacy objectives. The Bank has implemented an economic capital measurement process, including appropriate methodologies and assumptions, to quantify the capital requirements related to our primary areas of risk. The Bank periodically quantifies the economic capital requirements, based on the credit risk, interest rate risk, operational risk, and market risk inherent in its operations. For a further discussion of these risks, see the *Risk Management* section above. Due to the evolving nature of the economic capital concept, the Bank anticipates these methodologies and assumptions will continue to be refined.

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

AgFirst is committed to providing sound and dependable credit to young, beginning, and small (YBS) farmers and ranchers. Because of the unique needs of these individuals, and their importance to the future growth of the Associations, the Associations have established annual marketing goals to increase market shares of loans to YBS farmers. Specific marketing plans have been developed to target these groups, and resources have been designated to help ensure YBS borrowers' access to a stable source of credit. AgFirst and the District Associations recognize that YBS farmers are vitally important to the future of agriculture and are committed to continue offering programs to help educate, assist, and provide quality financial services to YBS farmers.

The FCA regulatory definitions for YBS farmers and ranchers are as follows:

Young Farmer – A farmer, rancher, or producer or harvester of aquatic products who was age 35 or younger as of the date the loan was originally made.

Beginning Farmer – A farmer, rancher, or producer or harvester of aquatic products who had 10 years or less farming or ranching experience as of the date the loan was originally made.

Small Farmer – A farmer, rancher, or producer or harvester of aquatic products who normally generated less than $250 thousand in annual gross sales of agricultural or aquatic products at the date the loan was originally made.

It is important to note that due to the regulatory definitions a farmer/rancher may be included in multiple categories as they would be included in each category in which the definition was met.

The following table summarizes information regarding the combined District's loans outstanding to Young and Beginning Farmers and Ranchers as of December 31, 2011:

Young, and Beginning Farmers and Ranchers
Number/Volume of Loans Outstanding
(dollars in thousands)

Category	Number of Loans	Percent of Total	Volume Outstanding	Percent of Total
1. Total loans and commitments outstanding at year-end	136,867	–%	$ 29,673,809	–%
2. Young farmers and ranchers	20,865	15.24%	$ 2,229,111	7.51%
3. Beginning farmers and ranchers	31,257	22.84%	$ 3,911,243	13.18%

The following table summarizes information regarding the combined District's loans outstanding to Small Farmers and Ranchers as of December 31, 2011:

Small Farmers and Ranchers
Number/Volume of Loans Outstanding by Loan Size
(dollars in thousands)

Number/Volume Outstanding	$0-$50,000	$50,001-$100,000	$100,001-$250,000	$250,001-and greater
1. Total number of loans and commitments outstanding at year-end	70,740	22,941	23,766	19,420
2. Total number of loans to small farmers and ranchers	48,774	13,965	12,532	5,922
3. Number of loans to small farmers and ranchers as a % of total number of loans	68.95%	60.87%	52.73%	30.49%
4. Total loan volume outstanding at year-end	$ 1,396,577	$ 1,708,392	$ 3,851,612	$ 22,717,228
5. Total loan volume to small farmers and ranchers	$ 948,404	$ 1,033,777	$ 1,972,869	$ 3,188,780
6. Loan volume to small farmers and ranchers as a % of total loan volume	67.91%	60.51%	51.22%	14.04%

The following table summarizes information regarding the combined District's new loans made to Young, and Beginning Farmers and Ranchers for the year ended December 31, 2011:

Young, and Beginning Farmers and Ranchers
Gross New Business During 2011, Number/Volume of Loans
(dollars in thousands)

Category	Number of Loans	Percent of Total	Volume Outstanding	Percent of Total
1. Total gross new loans and commitments made during 2011	54,670	–%	$ 13,282,093	–%
2. Total loans and commitments made during 2011 to young farmers and ranchers	7,942	14.53%	$ 1,060,829	7.99%
3. Total loans and commitments made during 2011 to beginning farmers and ranchers	10,543	19.28%	$ 1,586,030	11.94%

The following table summarizes information regarding the combined District's new loans made to Small Farmers and Ranchers for the year ended December 31, 2011:

Small Farmers and Ranchers
Gross New Business by Loan Size, Number/Volume of Loans
(dollars in thousands)

Number/Volume	$0-$50,000	$50,001 -$100,000	$100,001-$250,000	$250,001-and greater
1. Total number of new loans and commitments made during 2011	22,791	8,722	10,323	12,834
2. Total number of loans made to small farmers and ranchers during 2011	16,063	4,807	4,656	2,546
3. Number of loans to small farmers and ranchers as a % of total number of loans	70.48%	55.11%	45.10%	19.84%
4. Total gross loan volume of all new loans and commitments made during 2011	$ 502,856	$ 648,198	$ 1,638,482	$ 10,492,557
5. Total gross loan volume to small farmers and ranchers	$ 332,276	$ 353,135	$ 748,687	$ 1,436,519
6. Loan volume to small farmers and ranchers as a % of total gross new loan volume	66.08%	54.48%	45.69%	13.69%

LEGAL PROCEEDINGS

On the basis of information presently available, management and legal counsel are of the opinion that the ultimate liability, if any, from legal actions pending against AgFirst would be immaterial in relation to the financial position of AgFirst. Refer to Note 14, *Commitments and Contingencies*, in the Notes to the Consolidated Financial Statements for additional information.

FINANCIAL REGULATORY REFORM

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was signed into law on July 21, 2010. While the Dodd-Frank Act represents a significant overhaul of many aspects of the regulation of the financial services industry, many of the statutory provisions of the Dodd-Frank Act are not applicable to the System. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new implementing rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and consequently, many of the details and much of the impact of the Dodd-Frank Act may not be known for many more months or years.

The Dodd-Frank Act creates new regulators and expands the authority of the Federal Reserve Board over non-bank financial companies previously not subject to its or other bank regulators' direct jurisdiction, particularly those that are considered systemically important to the U.S. financial system. The legislation created the Financial Oversight Council, a coordinating body of financial regulators, which is designed to monitor and pinpoint systematic risks across the financial spectrum. Nevertheless, the Dodd-Frank Act largely preserves the authority of the Farm Credit Administration as the System's independent federal regulator by excluding System institutions from being considered non-bank financial companies and providing other exemptions and exclusions from certain of the law's provisions. Also, the rules prohibiting banking entities from engaging in proprietary trading under the so-called Volcker Rule do not apply to the debt securities issued by the System.

The provisions of the Dodd-Frank Act pertaining to the regulation of derivatives transactions will require more of these transactions to be cleared through a third-party central clearinghouse and traded on regulated exchanges or otherwise, and margin or cash collateral will be required for these transactions. Also, derivative transactions that will not be subject to mandatory trading and clearing requirements may also be subject to minimum margin and capital requirements. The Dodd-Frank Act requires the Commodity Futures Trading Commission (CFTC) to consider whether to exempt System institutions from certain of these requirements. These requirements, whether or not System institutions are directly exempt from them, have the potential of making derivative transactions more costly and less attractive as risk management tools for System institutions; and thus may impact the System's funding and hedging strategies.

The Dodd-Frank Act will also require certain financial institutions to register as swap dealers or major swap participants, as the case may be, with the CFTC and/or the Securities and Exchange Commission. Based on the proposed rules, it is possible that certain System institutions could be required to register with the CFTC as swap dealers based on swaps entered into between System institutions or between System institutions and their borrowers, which would subject these System institutions to considerable additional regulation and cost. In addition, the counterparties with which System institutions enter into derivative transactions for hedging and risk mitigation purposes will most likely be designated as swap dealers and, as a result, are subject to additional regulatory requirements. In January 2012, the CFTC signaled its intention to finalize the rules related to swap dealers and central clearing requirements during the calendar year.

As required by the Dodd-Frank Act, the U.S. Treasury and the U.S. Department of Housing and Urban Development issued in February 2011 their report to Congress entitled "Reforming America's Housing Finance Market," which sets forth recommendations to Congress related to the future of the housing GSEs, including Fannie Mae and Freddie Mac. While this report did not specifically include or relate to the System, a potential risk exists that the System, as a GSE, may directly or indirectly be impacted should Congress take legislative action with respect to Fannie Mae, Freddie Mac and federal home loan finance. Since the release, Congress, primarily the House Financial Services Committee, has considered several approaches to reforming the housing GSEs and none of these approaches would directly impact the System.

The Consumer Financial Protection Bureau (CFPB), also created as part of the Dodd-Frank Act, became a fully functioning financial regulator, with the appointment of the first Director in January 2012. The CFPB will have responsibility to regulate consumer financial protection going forward. The Farm Credit Administration retains the responsibility to oversee and enforce compliance by System institutions with relevant rules adopted by the CFPB.

In light of the foregoing, it is difficult to predict at this time the extent to which the Dodd-Frank Act or the forthcoming implementing rules and regulations will have an impact on the System. However, it is possible they could affect funding and hedging strategies and increase funding and hedging costs.

OTHER REGULATORY MATTERS

On August 18, 2011, the FCA published for comment an amendment to the regulations governing investments held by institutions of the System. Comments were due November 16, 2011. The stated objectives of the proposed rule are to:

- ensure that the Banks hold sufficient high quality, readily marketable investments to provide sufficient liquidity to continue operations and pay maturing obligations in the event of market disruption;
- strengthen the safety and soundness of System institutions;
- seek comments on how the FCA can comply with section 939A of the Dodd-Frank Act, which requires the FCA to remove all references to and requirements relating to credit ratings from its regulations and to substitute other appropriate standards of creditworthiness;
- reduce regulatory burden with respect to investments that fail to meet eligibility criteria after purchase or are unsuitable; and
- enhance the ability of the System to supply credit to agriculture and aquatic producers by ensuring adequate availability to funds.

On August 26, 2011, the FCA published for comment an advance notice of proposed rulemaking regarding various references to and requirements of reliance on crediting ratings issued by NRSROs of a security or money-market instrument. Section 939A of the Dodd-Frank Act requires Federal agencies to remove any reference to or requirement of reliance upon credit ratings, and substitute in their place standards of creditworthiness that they deem appropriate for the regulations. The FCA seeks public comment on alternatives to the use of credit ratings in the regulations. Comments were due November 25, 2011.

On November 1, 2011, the FCA published for comment the draft Second Amended and Restated Market Access Agreement (MAA), which is an Agreement between the Banks and the Funding Corporation. Comments were due December 1, 2011. No comments were received by the FCA with respect to the draft MAA. The MAA was executed by the Banks and the Funding Corporation with an effective date of January 1, 2012.

On December 27, 2011, the FCA published for comment a proposed rule to amend the liquidity regulation. The purpose of the proposed rule is to strengthen liquidity risk management at System Banks, improve the quality of assets in the liquidity reserve, and bolster the ability of System Banks to fund their obligations and continue their operations during times of economic, financial, or market adversity. Comments were due by February 27, 2012. The stated objectives of the rule are to:

- improve the capacity of Banks to pay their obligations and fund their operations by maintaining adequate liquidity to withstand various market disruptions and adverse financial or economic conditions;
- strengthen liquidity management at all Banks;
- enhance the marketability of assets that Banks hold in their liquidity reserve;
- establish a supplemental liquidity buffer that Banks can draw upon during an emergency and that is sufficient to cover the Bank's liquidity needs beyond the 90-day liquidity reserve; and
- strengthen each Bank's contingency funding plan.

DISTRICT MERGER ACTIVITY

Please refer to Note 21, *District Merger Activity*, in the Notes to the Consolidated Financial Statements for information regarding merger activity in the District.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 2, *Summary of Significant Accounting Policies*, in the Notes to the Consolidated Financial Statements for recently issued accounting pronouncements.

Additional Disclosure

REQUIRED BY
FARM CREDIT ADMINISTRATION REGULATIONS

Description of Business

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

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

Description of Property

The following table sets forth certain information regarding the properties owned by the reporting entity, all of which are located in Columbia, South Carolina:

Location	Description
1401 Hampton Street	Bank building and adjacent parking
1441 Hampton Street	Vacant
1443 Hampton Street	AgFirst Federal Credit Union
1447 Hampton Street	Vacant
1428 Taylor Street	AgFirst training center
1436 Taylor Street	Leased to a tenant

Legal Proceedings

Information, if any, to be disclosed in this section is incorporated herein by reference to Note 14 to the Consolidated Financial Statements, *Commitments and Contingencies,* included in this Annual Report to shareholders.

Description of Capital Structure

Information to be disclosed in this section is incorporated herein by reference to Note 10 to the Consolidated Financial Statements, *Shareholders' Equity,* included in this Annual Report to shareholders.

Description of Liabilities

The description of liabilities and contingent liabilities to be disclosed in this section is incorporated herein by reference to Notes 2, 7, 8, 9, 11 and 14 to the Consolidated Financial Statements included in this Annual Report to shareholders.

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

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

Senior Officers

The following represents certain information regarding the directors and senior officers of the reporting entity.

The chief executive officer and all other senior officers of the Bank, together with their length of service at their present position, as well as positions held currently and during the last five years, are as follows:

Name and Title	Time in Position	Prior Experience	Other Business Interests
F.A. Lowrey, *Chief Executive Officer*	14 years	CEO, Palmetto Farm Credit, ACA from April 1989 to January 1998. President and CEO of AgFirst from January 1998 to April 2010.	Member of the Board for Federal Farm Credit Banks Funding Corporation; University of South Carolina: member of the Board of Trustees for the Business Partnership Foundation and Chairman of the Board of Directors for the Education Foundation; member of the Board of Directors for Big Brothers Big Sisters of Greater Columbia; member of the Board of Directors and Chairman of Finance Committee for National 4H Council; member of the Board of Directors for Palmetto AgriBusiness Council.
Leon T. Amerson, *President and Chief Operating Officer*	2 years	Chief Financial Officer from March 1998 to September 2006. Chief Operating Officer from September 2006 to April 2010.	Council Member of the National Council of Farm Cooperatives; member of the Board of Directors for Midlands Business Leadership Group; member of the AgFirst Plan Sponsor Committee.
Charl L. Butler, *Senior Vice President and Chief Financial Officer*	5 years	Chief Financial Officer and Secretary at The National Bank of South Carolina from 1991 until 2007.	Advisory Board Member of the Farm Credit System Captive Insurance Company; member on the AgFirst/FCBT Plan Fiduciary Committee.
Benjamin F. Blakewood, *Senior Vice President and Chief Information Officer*	13 years	Director of Information Technology from 1996 to 1998 at Affinity Technology Group.	
William L. Melton, *Senior Vice President and Chief Lending Officer*	8 years	Senior Executive Officer/Bank Lending from January to July 2003, prior to that Lending Services Manager.	
Christopher L. Jones, *Senior Vice President and Chief Credit Officer*	1 year	Senior Vice President and Chief Credit Officer South at United Community Banks from 2004 until 2011.	
Frederick T. Mickler, III, *Senior Vice President and General Counsel*	14 years	Assistant General Counsel July 1989 until April 1998.	

The total amount of compensation earned by the CEO and the senior officers as a group during the years ended December 31, 2011, 2010 and 2009, is as follows:

Name of Individual or Number in Group	Year	Annual Salary	Annual Bonus	Deferred Comp.	Perq./ Other*	Total
F. A. Lowrey	2011	$ 636,824	$ 257,213	$ 138,688	$ 22,783	$ 1,055,508
F. A. Lowrey	2010	$ 615,285	$ 344,621	$ 14,862	$ 22,601	$ 997,369
F. A. Lowrey	2009	$ 600,279	$ 338,619	$ 14,654	$ 21,448	$ 975,000
6 Officers	2011	$ 1,661,852	$ 771,973	$ 25,394	$ 99,640	$ 2,558,859
6 Officers	2010	$ 1,682,943	$ 905,678	$ 17,865	$ 144,854	$ 2,751,340
6 Officers	2009	$ 1,554,648	$ 556,293	$ 84,973	$ 109,211	$ 2,305,125

* *Primarily comprised of company contributions to thrift plan (see Note 11 to the Consolidated Financial Statements – Employee Benefit Plans), group life insurance premiums and bank-provided automobile.*

In addition to a base salary, senior officers may earn additional compensation under either the Bank's CEO/COO Bonus Plan or the Corporate Bonus Plan based on the senior officer's position. The plans' payments are based upon the Bank's achievement of minimum performance thresholds for net collateral ratio and patronage and dividend distributions and the senior officers' overall performance achievement as determined from their performance evaluation. Bonuses are shown in the year earned. Payment of the 2011 bonus was made in the first quarter of 2012.

Senior officers may also participate in the Bank's Long Term Bonus Plan which is designed to attract, recognize, and retain senior officers and other key employees. Participation in the plan is at the sole discretion of the CEO or in the case of the CEO at the sole discretion of the Board of Directors. Bonus amounts are shown in the year accrued and are vested over a full three-year period. Bonus amounts are forfeited if the participant fails to remain employed until December 31 of the two-year period immediately following the plan year.

Bank compensation plans are reviewed annually by the Board of Directors' Compensation Committee.

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

Disclosure of information on the total compensation paid during 2011 to any senior officer, or to any other individual included in the aggregate, is available to shareholders upon request.

AgFirst Farm Credit Bank Board of Directors

Name	Position	Term of Office
M. Wayne Lambertson	Chairman	December 31, 2013
Robert H. Spiers, Jr.	Vice Chairman	December 31, 2013
Gary L. Alexander	Director	December 31, 2015*
Jack W. Bentley, Jr.	Director	December 31, 2013
James C. Carter, Jr.	Director	December 31, 2014
Bonnie V. Hancock	Director	December 31, 2013
Dale R. Hershey	Director	December 31, 2015*
Paul M. House	Director	December 31, 2015*
Thomas W. Kelly	Director	December 31, 2012
Lyle Ray King	Director	December 31, 2012
John S. Langford	Director	December 31, 2015**
S. Alan Marsh	Director	December 31, 2013
James L. May	Director	December 31, 2013
Bobby E. McCollum, Jr.	Director	December 31, 2013
James M. Norsworthy, III	Director	December 31, 2015*
Katherine A. Pace	Director	December 31, 2015***
Jimmy D. Poston	Director	December 31, 2014
Walter L. Schmidlen, Jr.	Director	December 31, 2012
Robert G. Sexton	Director	December 31, 2011
William H. Voss	Director	December 31, 2014
J. Mark Wheeler	Director	December 31, 2012

* *These directors were re-elected in 2011 to a new 4-year term commencing 1/1/12.*

** *This director was newly elected in 2011 to a 4-year term commencing 1/1/12.*

*** *This director was re-appointed in 2011 to a new 4-year term commencing 1/1/12.*

M. Wayne Lambertson, Chairman of the Board, from Pocomoke City, Maryland, owns and operates with his son a 2,700-acre farm of corn, soybeans, and wheat, and a 300,000 capacity pullet operation. He is co-owner of a restaurant, Green Turtle, and partner in a development and construction company, J.W.L. Enterprise, LLC. He currently serves on the boards of the national Farm Credit Council (the Farm Credit System's national trade organization), MidAtlantic Farm Credit, ACA, and the Delmarva Poultry Industry (DPI), a trade organization.

Robert H. Spiers, Jr., Vice Chairman of the Board, is a full-time farmer, with a tobacco, corn, wheat, and soybean operation on 1,400 acres in Dinwiddie County, Virginia. Mr. Spiers sells tobacco at a warehouse operated by an association borrower. He currently serves on the boards of Colonial Farm Credit, ACA, Tobacco Associates, Inc. and Dinwiddie County Farm Bureau. He is also a director on the Virginia Flue-cured Tobacco Board, and a governor appointed member of the Virginia Tobacco Indemnification Commission. He has been active on a number of Virginia Farm Bureau advisory committees. Mr. Spiers serves on the Board Compensation Committee. He is Chairman of the AgFirst/FCBT Plan Sponsor Committee.

Gary L. Alexander from Westminster, South Carolina is owner and operator of Alexander Farms, Inc., a poultry production and property development business. He markets 3.2 million broilers a year through his 18-broiler house farm and develops residential properties. He currently serves on the board of directors of AgSouth Farm Credit, ACA, the national Farm Credit Council, and is a director of the S. C. Poultry Federation. Mr. Alexander serves as chair of the Board Governance Committee.

Jack W. Bentley, Jr., a dairy farmer in Tignall, Georgia, owns and operates A&J Dairy, a 270-cow dairy that includes 583 acres of pasture, crops and timberland, and an additional 500 acres of leased farmland. Mr. Bentley is a director of AgGeorgia Farm Credit, ACA, Southeast United Dairy Industry Association, and the Wilkes County Farm Bureau. He is also a member of the Wilkes County Board of Tax Assessors and is past board chair for Farm Service Agency. Mr. Bentley serves on the Board Compensation Committee. Mr. Bentley is also the Board appointed member of the AgFirst/FCBT Plan Sponsor Committee.

James "Jimmy" C. Carter, Jr., owns and operates with his son, Southern Belle Farm, Inc., located in McDonough, Georgia. The 200-acre beef cattle and hay farm, includes fruit and vegetable crops, and agriculturally related educational activities. Mr. Carter also operates a feed, mineral, and supplement business from the farm and provides artificial insemination services and supplies for cattle. Mr. Carter is a director of AgSouth Farm Credit and serves as chairman of the Henry County Water and Sewage Authority. He is a representative on the Ocmulgee River Basin Advisory Council and serves as vice president of the Henry County Farm Bureau. He is a member of the board for the Henry County Cattleman's Association. In 2011, Mr. Carter served on the Board Audit Committee, and currently serves as chair of the Board Audit Committee.

Bonnie V. Hancock is Executive Director of the Enterprise Risk Management Initiative at North Carolina State University (NCSU). She also teaches courses in financial management, enterprise risk management, strategy and financial statement analysis. Prior to joining NCSU, she worked with Progress Energy, as senior vice president of finance and information technology and later as president of Progress Fuels, a subsidiary that produces and markets gas, coal and synthetic fuels, and operates fuel terminals and ash management facilities. Ms. Hancock is a graduate of Georgetown University with a master's degree in taxation. She is also a graduate of the College of William and Mary with a bachelor's degree in business administration with an accounting major. She lives in Wake Forest, North Carolina, and is a member of the boards of Powell Industries, designer and manufacturer of electrical equipment and computer systems that monitor the flow of electricity in industrial facilities, where she serves on the compensation committee and the North Carolina Coastal Pines Girl Scout Council, where she serves as chair of the audit committee. Ms. Hancock is a board designated financial expert and serves as chair of the Board Credit Committee.

Dale R. Hershey from Manheim, Pennsylvania is the senior partner in Hershey Brothers Dairy Farms, managing the operations' real estate and cropping enterprises. The operation includes a dairy operation which milks 300 cows, raises 250 dairy replacements, and grows 650 acres of corn, alfalfa, soybeans, barley, and rye and grass hay. He serves on the board of directors of MidAtlantic Farm Credit, ACA. He is a member of Pennsylvania Farm Bureau, the Pennsylvania Holstein Association, Lancaster County Blue Ribbon Commission for Agriculture and the Penn Township Ag Advisory Committee. Mr. Hershey serves on the Board Credit Committee.

Paul M. House, is from Nokesville, Virginia, where he grows corn, soybeans, wheat, hay and turf grass on 4,000 acres. He also operates a dairy and milks 340 cows. He serves as a director of the Farm Credit of the Virginias, ACA. Mr. House serves on the Board Compensation Committee.

Thomas W. Kelly from Tyrone, Pennsylvania, is owner and manager of a livestock and crop farm, raising dairy heifers and growing corn and soybeans. Along with his son, he handles land management for Spring Lane Hunt Club. He currently is an elected delegate to the Penn State Agricultural Council and a director of Mid-Atlantic Master Farmer Association and is a former director of Holstein Association, USA. He is a member of AgChoice Farm Credit, ACA. Mr. Kelly serves on the Board Governance Committee.

Lyle Ray King of Ash, North Carolina, owns and operates a farm where he grows timber, corn, soybeans and wheat. He currently serves on the boards of Cape Fear Farm Credit, ACA, Atlantic Telephone Membership Cooperative, and Landbank Resource Management, a real estate company. Mr. King serves on the Board Credit Committee.

John S. Langford, 62, from Lakeland, Florida, has been a citrus grower for 45 years. Mr. Langford has also been a realtor for 32 years, specializing in agricultural lands. He currently serves as a director on the Farm Credit of Central Florida board and the boards of Community

Southern Bank, Lake Wales Citrus Growers Association, and Polk County Florida Farm Bureau. Mr. Langford obtained his B.A. degree from Emory University and his MBA from Harvard Business School. He serves on the Board Audit Committee.

S. Alan Marsh, a third-generation farmer, is owner and operator of Marsh Farms in Madison, Alabama. His operation consists of 3,000 acres of row crops, including cotton, soybeans, wheat and corn. Mr. Marsh is a director of First South Farm Credit, ACA and Limestone County Farmers Federation, and is president and stockholder of South Limestone Co-op Gin, an Association borrower. He is also a delegate on the national Cotton Council, a member of the Alabama Cattlemen's Association and an advisory board member for Staplecotn, a cotton cooperative association. Mr. Marsh serves on the Board Credit Committee.

James L. May is owner and operator of Mayhaven Farm in Waynesburg, Kentucky, where he owns 330 acres and leases another 700 acres, where he has beef heifer back grounding program, utilizing rotational grazing for 500 head of cattle. Mr. May's operation also includes 150 acres of alfalfa hay, 500 acres of corn and soybeans, and 100 acres of wheat. He also operates an on farm seed business offering many types of farm seeds. He currently serves as a member of the Central Kentucky Ag Credit board, Lincoln County Extension Council, and the Lincoln County Farm Bureau Board. Mr. May serves on the Board Credit Committee.

Bobby E. McCollum, Jr., is a poultry operator in Polkton, North Carolina. His operation includes eight broiler houses that produce 750,000 heavy broilers per year. Mr. McCollum also has a 100-head brood cow/calf commercial herd, and grows 100 acres of timber as well as hay, soybeans, wheat and corn. He is a member of Anson County Cattlemen's Association and serves on Anson County Agriculture Advisory Board. He is a member of Carolina Farm Credit, ACA. Mr. McCollum serves on the Board Audit Committee.

James M. Norsworthy, III, from Jackson, Louisiana runs 100 Cedars Cattle Farm, a 250-head cow-calf operation. He also has a commercial hay operation with 125 acres in Alicia Bermuda hay and 150 acres in Bahia Grass hay and manages a 500 acre pine and hardwood timber operation. He is a member of the board of directors of First South Farm Credit, ACA, and serves on the board of Louisiana State Farm Bureau. He is a member of Feliciana Farm Bureau, East Feliciana Cattlemen's Association, American Angus Association and the Feliciana Forestry Association. Mr. Norsworthy served as a former mayor of the town of Jackson, Louisiana. In 2011, Mr. Norsworthy served on the Board Audit Committee, and currently serves on the Board Governance Committee.

Katherine A. Pace from Orlando, Florida, is a certified public accountant. Prior to forming her company, Family Business Consulting, LLC, she was a tax partner with KPMG, LLP, an audit, tax and advisory service firm, from 1985-2005. While at KPMG, her practice included a variety of cooperative and agribusiness clients as well as participation in trade associations such as the National Society of Accountants for Cooperatives. Ms. Pace obtained her B.S. degree in accounting from Furman University. She is a member of the American Institute of Certified Public Accountants, the Florida Institute of Certified Public Accountants and current and past member and director of numerous trade and charitable organizations. Ms. Pace served as chair of and is the board designated financial expert on the Board Audit Committee.

Jimmy D. Poston from Johnsonville, South Carolina, owns and operates Triple P Farms together with his brother. His operation consists of 2,500 acres of corn, peanuts, soybeans, tobacco, turf grass, strawberries and timber. Mr. Poston is a director of ArborOne Farm Credit, chairman of the Florence County Farm Service Agency Committee, a member of the Florence County Soil and Water Conservation District and a member of the SC Corn Growers Association and the SC Soybean Growers Association. Mr. Poston serves on the Board Governance Committee.

Walter L. Schmidlen, Jr., from Elkins, West Virginia, is a past dairy farmer and now continues his cow-calf operation along with growing hay and corn on a 700 acre farm with lease/rented land. He is owner/operator of a farm equipment business. He is a member of Farm Credit of the Virginias, ACA, and was a former director of Southern States Cooperative and Sire Power. Mr. Schmidlen served on the Board Governance Committee, and is currently serving on the Board Compensation Committee.

Robert G. Sexton is from Vero Beach, Florida. He is President of Oslo Citrus Growers Association and co-owner of Lost Legend, LLC, and owner of Orchid Island Juice Company. He serves as a director of Farm Credit of Florida, ACA; Oslo Citrus Growers Association; Lost Legend, LLC; Florida Citrus Packers; Indian River Citrus League; Highland Exchange Service Co-op, a packinghouse supply cooperative; McArthur Management Company, a management company for a large dairy, cattle and citrus agribusiness; and an association borrower; Sexton Grove Holdings, a family citrus company; Sexton Properties, Oslo Packing Company, Patio Restaurant and Sexton, Inc., family commercial real estate companies; and Dancing Pigs, LLC, which owns Red, Hot and Blue BBQ restaurants. In addition, he is a member of the Indian River Farm Bureau. He obtained both his B.S. degree in business administration and his MBA finance from the University of Florida. Mr. Sexton served on the Board Compensation Committee. He was a board designated financial expert, and was the Board appointed member of the AgFirst/FCBT Plan Sponsor Committee.

William H. Voss is from McComb, Mississippi. He has commercial cattle, hay and timber operations in Southwest Mississippi and is involved in land and commercial property management. His career includes production agriculture, agribusiness and real estate. He obtained his B.S. degree from the University of Southern Mississippi, and currently serves on the board of directors of First South Farm Credit, ACA, and the national Farm Credit Council. He is a former agricultural commodities and securities broker and has served as Chairman of the Mississippi Real Estate Commission and Chairman of the Pike County Farm Service Committee. Mr. Voss serves as chair of the Board Compensation Committee and is a member of the AgFirst/FCBT Plan Sponsor Committee.

J. Mark Wheeler from Bradenton, Florida is chief financial officer of Wheeler Farms, Inc., which grows citrus in several counties in Florida. He serves on the boards of Farm Credit of Florida, ACA, Florida Citrus Mutual, an industry trade association, and Wheeler Brothers, Inc., a family-held citrus contract harvesting corporation. Mr. Wheeler is president of Boston Mining Company, a citrus, real estate and cash investment organization. Mr. Wheeler is a board member of Hardee Livestock Market (HLM), a wholly-owned subsidiary of Wheeler Farms, Inc., a cattle auction company that conducts business with several association borrowers. Wheeler Farms, Inc. also brokered citrus for an association borrower. Mr. Wheeler is a board designated financial expert, serves on the Board Audit Committee and is a member of the AgFirst/FCBT Plan Sponsor Committee.

Committees

The board has established an audit committee, compensation committee, credit committee and governance committee. All members of the board, other than the chairman, serve on a committee. The chairman of the board serves as an ex officio member of all board committees, and the vice chairman serves as a member of the board compensation committee. The Board has four designated financial experts, two of which serve on the audit committee. The responsibilities for each committee are set forth in its respective board approved charter.

Compensation of Directors

Directors were compensated in 2011 in cash at the rate of $52,800 per year, payable at $4,400 per month. This is compensation for attendance at board meetings, board committee meetings, certain other meetings pre-approved by the board, and other duties as assigned. FCA regulations also allow additional compensation to be paid to a director in exceptional circumstances where extraordinary time and effort are involved. In this regard, the Chairman of the Board and the Chair of the Board Audit Committee were paid an additional $1,250 per quarter for their service. Total cash compensation paid to all directors as a group during 2011 was $1,066,000. Directors received no non-cash compensation during 2011. Additional information for each director who served during 2011 is provided below.

	Number of Days Served			
Name of Director	Board Meetings	Other Official Activities*	Farm Credit Council Bd. Activities	Total Comp. Paid During 2011
Gary L. Alexander	26.00	13.50	6.75	$ 52,800
Jack W. Bentley, Jr.	26.00	15.75	6.75	52,800
James C. Carter, Jr.	26.00	19.74	6.75	52,800
Bonnie V. Hancock	25.50	9.75	6.75	52,800
Dale R. Hershey	26.00	18.75	6.75	52,800
Paul M. House	25.00	15.75	4.50	52,800
Thomas W. Kelly	26.00	17.75	6.75	52,800
Lyle Ray King**	20.50	15.50	4.50	52,800
M. Wayne Lambertson	25.00	17.00	4.50	57,800
S. Alan Marsh	23.00	16.00	6.75	52,800
James L. May	26.00	18.75	6.75	52,800
Bobby E. McCollum, Jr.	26.00	18.25	6.75	52,800
James M. Norsworthy, III	26.00	17.00	6.75	52,800
Katherine A. Pace	26.00	14.25	6.75	57,800
Jimmy D. Poston	26.00	16.25	6.75	52,800
Walter L. Schmidlen, Jr.***	10.00	1.50	4.00	52,800
Robert G. Sexton****	26.00	15.75	6.75	52,800
Robert H. Spiers, Jr.	26.00	21.00	6.75	52,800
William H. Voss	26.00	12.75	6.75	52,800
J. Mark Wheeler	25.50	14.00	6.75	52,800
Total				$ 1,066,000

* *Other official activities include board committee meetings and board training.*

** *Director King was unable to attend board meetings from May to July 2011.*

*** *Director Schmidlen was unable to attend board meetings from March to October 2011.*

**** *Does not include 3.5 days served on AgFirst and AgFirst/FCBT Plan Sponsor Committees.*

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

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was $243,537 for 2011, $218,331 for 2010, and $236,458 for 2009.

Transactions with Senior Officers and Directors

The reporting entity's policies on loans to and transactions with its officers and directors, to be disclosed in this section, are incorporated herein by reference to Note 12 to the Consolidated Financial Statements, *Related Party Transactions,* included in this Annual Report to shareholders. There have been no transactions between the Bank and senior officers or directors which require reporting per FCA regulations.

Involvement in Certain Legal Proceedings

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

Relationship with Independent Certified Public Accountant

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

Aggregate fees expensed by the Bank for services rendered by its independent certified public accountant for the year ended December 31, 2011 were as follows:

	2011
Independent Certified Public Accountant	
PricewaterhouseCoopers LLP	
Audit services	$ 476,835
Non-audit services	159,435
Total	$ 636,270

Audit fees were for the annual audits of financial statements.

Non-audit fees were for agreed upon procedures for Financial Institution Shared Assessments Program, Farmer Mac minimum servicing standards attestation, and agreed upon procedures for Board of Directors elections.

All non-audit service engagements of $50,000 or more for the Bank require pre-approval by the Audit Committee.

Consolidated Financial Statements

The Consolidated Financial Statements, together with the report thereon of PricewaterhouseCoopers LLP, dated March 13, 2012, and the Report of Management, which appear in this Annual Report to shareholders are incorporated herein by reference.

Borrower Information Regulations

Farm Credit Administration (FCA) regulations require that borrower information be held in strict confidence by Farm Credit institutions, their directors, officers, and employees. These regulations provide Farm Credit institutions clear guidelines for protecting their borrowers' nonpublic personal information.

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

Shareholder Investment

Shareholder investment in a District Association is materially affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's Annual and Quarterly Reports are available upon request free of charge by calling 1-800-845-1745, ext. 2832, or writing Susanne Caughman, Financial Reporting Manager, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Combined information concerning AgFirst Farm Credit Bank and District Associations can also be obtained at the Bank's website, **www.agfirst.com**.The Bank prepares an electronic version of the Annual Report, which is available on the website, within 75 days after the end of the fiscal year and distributes the Annual Report to shareholders within 90 days after the end of the fiscal year. The Bank prepares an electronic version of each Quarterly Report within 40 days after the end of each fiscal quarter, except that no report is prepared for the fiscal quarter that coincides with the end of the fiscal year of the Bank.

Report of the

Audit Committee

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

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

PricewaterhouseCoopers LLP (PwC), the Bank's independent certified public accountant for 2011, is responsible for expressing an opinion on the conformity of the Bank's audited financial statements with accounting principles generally accepted in the United States of America. The Committee has discussed with PwC the matters that are required to be discussed by Statement on Auditing Standards No. 114 *(The Auditor's Communication With Those Charged With Governance)*. PwC has provided to the Committee the written disclosures and the letter required by Independence Standards Board Standard No. 1 *(Independence Discussions with Audit Committees)*, and the Committee has discussed with PwC that firm's independence.

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

Based on the considerations referred to above, the Committee recommended to the Board of Directors that the audited financial statements be included in the Company's Annual Report for 2011. The foregoing report is provided by the following independent directors, who constitute the Committee:

James C. Carter, Jr.

James C. Carter, Jr.
Chairman of the Audit Committee

Members of Audit Committee

John S. Langford
Bobby E. McCollum, Jr.
Katherine A. Pace
J. Mark Wheeler

March 13, 2012

REPORT OF

Independent Certified Public Accountants

Report of Independent Certified Public Accountants

To the Board of Directors and Shareholders
of AgFirst Farm Credit Bank

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income, of changes in shareholders' equity and of cash flows present fairly, in all material respects, the financial position of AgFirst Farm Credit Bank (the Bank) at December 31, 2011, 2010 and 2009, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

March 13, 2012

PricewaterhouseCoopers LLP, 401 E. Las Olas Boulevard, Suite 1800, Fort Lauderdale, FL 33301
T: (954) 764-7111, F: (954)525-4453, www.pwc.com/us

Consolidated

Balance Sheets

		As of December 31,	
(dollars in thousands)	**2011**	**2010**	**2009**
Assets			
Cash and cash equivalents	**$ 1,301,569**	$ 1,427,033	$ 938,884
Investment securities:			
Available for sale (amortized cost of $6,792,584, $6,980,661, and $6,959,113, respectively)	**6,925,410**	7,024,364	6,838,025
Held to maturity (fair value of $928,053, $1,114,064, and $1,426,740, respectively)	**854,862**	1,052,314	1,388,184
Total investment securities	**7,780,272**	8,076,678	8,226,209
Loans	**20,152,066**	20,905,165	21,327,319
Less: allowance for loan losses	**27,714**	14,873	32,292
Net loans	**20,124,352**	20,890,292	21,295,027
Accrued interest receivable	**78,906**	84,692	94,756
Investments in other Farm Credit System institutions	**65,964**	65,300	76,635
Premises and equipment, net	**13,706**	11,361	14,489
Other property owned	**44,157**	39,719	25,909
Due from associations	**17,318**	20,550	37,345
Other assets	**151,262**	165,941	158,290
Total assets	**$ 29,577,506**	$ 30,781,566	$ 30,867,544
Liabilities			
Bonds and notes	**$ 27,086,148**	$ 28,325,569	$ 28,694,013
Mandatorily redeemable preferred stock	—	225,000	225,000
Accrued interest and dividends payable	**42,418**	57,816	83,038
Patronage distribution payable	**180,726**	190,543	182,724
Other liabilities	**118,944**	79,857	102,439
Total liabilities	**27,428,236**	28,878,785	29,287,214
Commitments and contingencies (Note 14)			
Shareholders' Equity			
Perpetual preferred stock	**400,000**	400,000	400,000
Capital stock and participation certificates	**405,767**	417,333	438,707
Retained earnings			
Allocated	**858**	871	965
Unallocated	**1,218,648**	1,052,248	863,862
Accumulated other comprehensive income (loss)	**123,997**	32,329	(123,204)
Total shareholders' equity	**2,149,270**	1,902,781	1,580,330
Total liabilities and equity	**$ 29,577,506**	$ 30,781,566	$ 30,867,544

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

Consolidated Statements of Income

	For the year ended December 31,		
(dollars in thousands)	**2011**	**2010**	**2009**
Interest Income			
Investment securities and other	**$ 196,349**	$ 192,839	$ 200,785
Loans	**691,762**	760,681	830,778
Total interest income	**888,111**	953,520	1,031,563
Interest Expense	**293,334**	382,274	541,902
Net interest income	**594,777**	571,246	489,661
Provision for loan losses	**80,222**	40,002	46,648
Net interest income after provision for loan losses	**514,555**	531,244	443,013
Noninterest Income			
Loan fees	**12,267**	16,309	13,312
Gains (losses) from other property owned, net	**(12,192)**	(5,392)	(2,824)
Gains (losses) on investments, net (Note 3)	**3,048**	1,568	9,918
Total other-than-temporary impairment losses on investments (Note 3)	**(7,368)**	(9,250)	(60,412)
Portion of loss recognized in other comprehensive income (loss) (Note 3)	**(1,885)**	(2,662)	34,244
Net other-than-temporary impairment losses on investments included in earnings	**(9,253)**	(11,912)	(26,168)
Gains (losses) on derivatives, net	**—**	—	469
Gains (losses) on sales of rural home loans, net	**(262)**	(112)	1
Patronage refunds from other Farm Credit System institutions	**2,632**	2,928	5,327
Insurance premium refund	**—**	10,440	—
Other noninterest income	**2,587**	4,760	7,366
Total noninterest income	**(1,173)**	18,589	7,401
Noninterest Expenses			
Salaries and employee benefits	**46,881**	43,105	40,960
Occupancy and equipment	**14,360**	15,675	14,720
Insurance Fund premiums	**5,360**	5,147	20,605
Other operating expenses	**24,920**	21,401	21,873
Called debt expense	**27,450**	38,420	36,531
Correspondent lending servicing expense	**8,847**	8,413	6,303
Other noninterest expense	**106**	277	279
Total noninterest expenses	**127,924**	132,438	141,271
Net income	**$ 385,458**	$ 417,395	$ 309,143

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

Consolidated Statements of

Changes in Shareholders' Equity

(dollars in thousands)	Perpetual Preferred Stock	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at December 31, 2008	$ 400,000	$ 434,929	$ 805	$ 762,550	$ (357,192)	$ 1,241,092
Cumulative-effect adjustment for investment impairment accounting change				3,474	(3,474)	—
Comprehensive income						
Net income				309,143		309,143
Unrealized gains (losses) on investments available for sale:						
Other-than-temporarily impaired (Note 3)					(31,606)	
Not other-than-temporarily impaired (Note 3)					269,783	
Total unrealized gains (losses) on investments available for sale						238,177
Employee benefit plans adjustments (Note 11)					(715)	(715)
Total comprehensive income						546,605
Capital stock/participation certificates issued/(retired), net		3,205				3,205
Stock dividends declared/paid		573		(573)		—
Perpetual preferred stock dividends paid				(27,413)		(27,413)
Patronage distribution						
Cash distributions declared				(183,116)		(183,116)
Nonqualified allocated retained earnings			160	(160)		—
Patronage distribution adjustment				(43)		(43)
Balance at December 31, 2009	$ 400,000	$ 438,707	$ 965	$ 863,862	$ (123,204)	$ 1,580,330
Comprehensive income						
Net income				417,395		417,395
Unrealized gains (losses) on investments available for sale:						
Other-than-temporarily impaired (Note 3)					14,432	
Not other-than-temporarily impaired (Note 3)					150,359	
Total unrealized gains (losses) on investments available for sale						164,791
Employee benefit plans adjustments (Note 11)					(507)	(507)
Change in value of firm commitments - when issued securities (Note 18)					(8,751)	(8,751)
Total comprehensive income						572,928
Capital stock/participation certificates issued/(retired), net		(22,095)				(22,095)
Stock dividends declared/paid		721		(721)		—
Perpetual preferred stock dividends paid				(27,413)		(27,413)
Patronage distribution						
Cash distributions declared				(200,772)		(200,772)
Nonqualified allocated retained earnings			(94)	94		—
Patronage distribution adjustment				(197)		(197)
Balance at December 31, 2010	$ 400,000	$ 417,333	$ 871	$ 1,052,248	$ 32,329	$ 1,902,781
Comprehensive income						
Net income				**385,458**		**385,458**
Unrealized gains (losses) on investments available for sale:						
Other-than-temporarily impaired (Note 3)					**2,396**	
Not other-than-temporarily impaired (Note 3)					**86,726**	
Total unrealized gains (losses) on investments available for sale						**89,122**
Employee benefit plans adjustments (Note 11)					**(639)**	**(639)**
Change in value of firm commitments - when issued securities (Note 18)					**3,185**	**3,185**
Total comprehensive income						**477,126**
Capital stock/participation certificates issued/(retired), net		**(12,207)**				**(12,207)**
Stock dividends declared/paid		**648**		**(648)**		**—**
Perpetual preferred stock dividends paid				**(27,413)**		**(27,413)**
Patronage distribution						
Cash distributions declared				**(191,060)**		**(191,060)**
Nonqualified allocated retained earnings			**14**	**(14)**		**—**
Retained earnings retired			**(27)**			**(27)**
Patronage distribution adjustment		**(7)**		**77**		**70**
Balance at December 31, 2011	**$ 400,000**	**$ 405,767**	**$ 858**	**$ 1,218,648**	**$ 123,997**	**$ 2,149,270**

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

CONSOLIDATED STATEMENTS OF

Cash Flows

	For the year ended December 31,		
(dollars in thousands)	2011	2010	2009
Cash flows from operating activities:			
Net income	**$ 385,458**	$ 417,395	$ 309,143
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	**6,614**	8,346	8,619
Premium amortization (discount accretion) on investment securities	**18,678**	37,654	17,266
(Premium amortization) discount accretion on bonds and notes	**144**	(4,670)	(4,631)
Provision for loan losses	**80,222**	40,002	46,648
(Gains) losses on other property owned, net	**12,192**	5,392	2,824
Net impairment losses on investments	**9,253**	11,912	26,168
(Gains) losses on investments, net	**(3,048)**	(1,568)	(9,918)
(Gains) losses on derivatives, net	**—**	—	(469)
(Gains) losses on sales of rural home loans, net	**262**	112	(1)
Net change in loans held for sale	**22,793**	33,477	43,068
Changes in operating assets and liabilities:			
(Increase) decrease in accrued interest receivable	**5,786**	10,064	11,837
(Increase) decrease in due from associations	**3,232**	16,795	3,326
(Increase) decrease in other assets	**4,762**	(15,447)	(8,025)
Increase (decrease) in accrued interest and dividends payable	**(15,398)**	(25,222)	(71,105)
Increase (decrease) in other liabilities	**38,448**	(22,860)	24,519
Total adjustments	**183,940**	93,987	90,126
Net cash provided by (used in) operating activities	**569,398**	511,382	399,269
Cash flows from investing activities:			
Investment securities purchased	**(1,177,332)**	(2,028,038)	(2,597,275)
Investment securities sold or matured	**1,537,976**	2,294,362	2,474,057
(Increase) decrease in firm commitments - when issued securities	**3,185**	(8,751)	—
Net (increase) decrease in loans	**626,360**	301,533	(132,306)
(Increase) decrease in investments in other Farm Credit System institutions	**(664)**	11,335	(1,580)
Purchase of premises and equipment, net	**(8,959)**	(5,218)	(5,047)
Proceeds from sale of other property owned	**19,673**	10,409	5,489
Net cash provided by (used in) investing activities	**1,000,239**	575,632	(256,662)
Cash flows from financing activities:			
Bonds and notes issued	**41,651,117**	56,271,307	108,805,294
Bonds and notes retired	**(42,880,764)**	(56,627,514)	(108,104,360)
Redemption of mandatorily redeemable preferred stock	**(225,000)**	—	—
Capital stock and participation certificates issued/retired, net	**(12,207)**	(22,095)	3,205
Cash distribution to shareholders	**(200,807)**	(193,150)	(157,452)
Dividends paid on perpetual preferred stock	**(27,413)**	(27,413)	(27,413)
Retained earnings retired	**(27)**	—	—
Net cash provided by (used in) financing activities	**(1,695,101)**	(598,865)	519,274
Net increase (decrease) in cash and cash equivalents	**(125,464)**	488,149	661,881
Cash and cash equivalents, beginning of period	**1,427,033**	938,884	277,003
Cash and cash equivalents, end of period	**$ 1,301,569**	$ 1,427,033	$ 938,884
Supplemental schedule of non-cash investing and financing activities:			
Financed sales of other property owned	**$ —**	$ —	$ 19,289
Receipt of property in settlement of loans	**36,303**	29,611	52,971
Investments transferred to loans (Note 2)	**—**	—	91,353
Change in unrealized gains (losses) on investments, net	**89,122**	164,791	238,177
Change in fair value of derivative instruments (Note 18)	**(9,100)**	8,781	—
Employee benefit plans adjustments (Note 11)	**639**	507	715
Cumulative-effect adjustment for investment impairment accounting change	**—**	—	3,474
Non-cash changes related to hedging activities:			
Increase (decrease) in bonds and notes	**$ (9,917)**	$ (7,567)	$ (55,313)
Decrease (increase) in other assets	**9,917**	7,796	54,941
Increase (decrease) in other liabilities	**—**	(229)	(240)
Supplemental information:			
Interest paid	**$ 307,749**	$ 412,166	$ 617,638

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

Notes

TO THE CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — Organization and Operations

A. **Organization:** AgFirst Farm Credit Bank (the Bank or AgFirst) is one of the banks of the Farm Credit System (the System), a nationwide system of cooperatively owned banks and associations and related service organizations. The System was established by Acts of Congress and is subject to the provisions of the Farm Credit Act of 1971, as amended (the Farm Credit Act).

At December 31, 2011, the nation was served by four Farm Credit Banks (FCBs) and one Agricultural Credit Bank (ACB). With the merger of CoBank, ACB and U.S. AgBank, FCB effective January 1, 2012, the nation is currently served by three FCBs and one ACB, each of which has specific lending authorities within its chartered territory. The ACB also has additional specific nationwide lending authorities. AgFirst is chartered to serve the states of Pennsylvania, Delaware, Maryland, Virginia, West Virginia, North Carolina, South Carolina, Georgia, Florida, Alabama, Mississippi, the Commonwealth of Puerto Rico and portions of the states of Ohio, Tennessee, Kentucky and Louisiana.

Each FCB and the ACB serves one or more Production Credit Associations (PCAs) that originate and service short- and intermediate-term loans, Federal Land Credit Associations (FLCAs) that originate and service long-term real estate mortgage loans, and/or Agricultural Credit Associations (ACAs) that originate both long-term and short- and intermediate-term loans. PCAs, FLCAs, and ACAs are collectively referred to as associations. AgFirst and its related associations (Associations or District Associations) are collectively referred to as the District. The District Associations jointly own all of AgFirst's voting stock. As of December 31, 2011, the District consisted of the Bank and twenty District Associations. All twenty were structured as ACA holding companies, with FLCA and PCA subsidiaries. Effective January 1, 2011, Farm Credit of North Florida, ACA, and Farm Credit of Southwest Florida, ACA, merged with and into Farm Credit of South Florida, ACA, which then changed its name to Farm Credit of Florida, ACA, reducing the number of Associations in the District to twenty.

Each FCB and the ACB are responsible for supervising the activities of the Associations within their districts. The FCBs and/or Associations make loans to or for the benefit of eligible borrowers/shareholders for qualified agricultural and rural purposes. District Associations borrow the majority of their funds from their related bank. The FCBs and the ACB obtain a substantial majority of funds for their lending operations through the sale of consolidated Systemwide bonds and notes to the public, but also obtain a portion of their funds from internally generated earnings, from the issuance of common and preferred stock and, to a lesser extent, from the issuance of subordinated debt.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the System banks and associations. The FCA examines the activities of System institutions to ensure their compliance with the Farm Credit Act, FCA regulations, and safe and sound banking practices.

The Farm Credit Act established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is required to be used: (1) to ensure the timely payment of principal and interest on Systemwide debt obligations (Insured Debt), (2) to ensure the retirement of protected borrower capital at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for discretionary uses by the Insurance Corporation to provide assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System bank has been required to pay premiums, which may be passed on to the Associations, into the Insurance Fund, based on its annual average adjusted outstanding Insured Debt until the assets in the Insurance Fund reach the "secure base amount." The secure base amount is defined in the Farm Credit Act as 2.0 percent of the aggregate insured obligations (adjusted to reflect the reduced risk on loans or investments guaranteed by federal or state governments) or such other percentage of the aggregate obligations as the Insurance Corporation in its sole discretion determines to be actuarially sound. When the amount in the Insurance Fund exceeds the secure base amount, the Insurance Corporation is required to reduce premiums and may return excess funds above the secure base amount to System institutions.

Premiums are charged based upon each bank's pro rata share of outstanding Insured Debt. Premiums of up to 20 basis points on adjusted Insured Debt obligations can be assessed along with a risk surcharge of 10 basis points on nonaccrual loans and other-than-temporarily impaired investments. For 2009, 2010 and 2011, the premium was 20, 5, and 6 basis points, respectively. Effective January 1, 2012, the premium was decreased to 5 basis points.

B. **Operations:** The Farm Credit Act sets forth the types of authorized lending activity and financial services which can be offered by the Bank and the persons eligible to borrow.

The Bank primarily lends to the District Associations in the form of a line of credit to fund the Associations' loan portfolios and operations. These lines of credit (or Direct Notes) are collateralized by a pledge of substantially all of each Association's assets. The terms of the Direct Notes are governed by a general financing agreement between the Bank and each Association. Each advance is structured such that the principal cash flow, repricing characteristics, and underlying index (if any) of the advance match those of the assets being funded. By match-funding the Association loans, the Associations' exposure to interest rate risk is minimized.

The Associations borrow from the Bank and in turn may originate and service both long-term real estate mortgage and short- and intermediate-term loans to their members.

In addition to providing loan funds to District Associations, the Bank provides the District Associations with banking and support services such as: accounting, human resources, information systems, and marketing. The costs of these support services are included in the interest charges to the Associations, or in some cases billed directly to certain Associations that use a specific service.

The Bank is also authorized to provide, in participation with other lenders and the secondary market, credit, credit commitments, and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents, and farm-related businesses. The Bank may also lend to other financial institutions qualified to engage in lending to eligible borrowers.

The Bank owns the Farm Credit Finance Corporation of Puerto Rico (the Finance Corporation). The Finance Corporation borrowed funds from the Bank and eligible funds from qualified companies doing business in Puerto Rico under Section 2(j) of the Puerto Rico Tax Incentive Act of 1987, as amended, or the Puerto Rico Tax Incentive Act of 1998, including corporations that had elections under Section 936 and 30(A) of the Internal Revenue Code of 1986, as amended (Code). The funds borrowed were primarily used to acquire from AgFirst the note receivable from Puerto Rico Farm Credit, ACA, and to acquire eligible loans originated by other System institutions. Savings in interest costs were, in part, passed along to borrowers in Puerto Rico who met certain eligibility requirements. The operations of the Finance Corporation were suspended and placed into inactive status effective December 31, 2005. All assets and liabilities of the

Finance Corporation were transferred to its sole shareholder, AgFirst, on December 31, 2005.

The Bank, in conjunction with other System banks, jointly owns service organizations, which were created to provide a variety of services for the System:

- *Federal Farm Credit Banks Funding Corporation (Funding Corporation)* – provides for the issuance, marketing and processing of Systemwide Debt Securities using a network of investment dealers and dealer banks. The Funding Corporation also provides financial management and reporting services.

- *FCS Building Association* – leases premises and equipment to the FCA.

- *Farm Credit System Association Captive Insurance Company* – being a reciprocal insurer, provides insurance services to its member organizations.

These investments are accounted for using the cost method. In addition, the *Farm Credit Council* acts as a full-service federated trade association, which represents the System before Congress, the Executive Branch and others, and provides support services to System institutions on a fee basis.

Note 2 — Summary of Significant Accounting Policies

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

The accompanying Consolidated Financial Statements include the accounts of the Bank (including the Finance Corporation), and reflect the investments in and allocated earnings of the service organizations in which the Bank has partial ownership interests. There were no significant transactions or balances between the Bank and the Finance Corporation for the years presented.

Certain amounts in prior years' financial statements have been reclassified to conform to the current year's presentation. Also, during the second quarter of 2009, the Bank reclassified from investments to loans certain financial instruments which totaled $91.4 million. These instruments were secondary market acquisitions of either private placement or senior secured notes transacted under the scope of the Bank's lending authority. The reclassification better reflects the nature of these notes and provides for consistent presentation across the Farm Credit System. This reclassification of $91.4 million is reflected as a non-cash item in the Consolidated Statements of Cash Flows and did not have a significant impact on the Financial Statements or the regulatory ratios.

A. **Cash and Cash Equivalents:** Cash and Cash Equivalents include cash on hand and short-term investments with original maturities of three months or less.

B. **Investment Securities**: The Bank, as permitted under the FCA regulations, holds investments for purposes of maintaining a liquidity reserve, managing short-term surplus funds, managing interest rate risk and, in the case of certain Mission-Related Investments, to stimulate economic growth and development in rural areas. Investments are classified based on management's intention on the date of purchase and are generally recorded on the Consolidated Balance Sheets as securities on the trade date. Investment securities which management has the intent and ability to hold to maturity are classified as held-to-maturity and reported at amortized cost. Investment securities classified as available-for-sale (AFS) are carried at fair value with net unrealized gains and losses included in other comprehensive income (OCI) in Shareholders' Equity.

The Bank reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered an impairment, is temporary or other-than-temporary. As mentioned above, changes in the fair value of AFS investments are reflected as direct charges or credits to other comprehensive income, unless the investment is deemed to be other than temporarily impaired. Impairment is considered to be other-than-temporary if the present value of cash flows expected to be collected from the debt security is less than the amortized cost basis of the security (any such shortfall is referred to as a "credit loss"). If the Bank intends to sell an impaired debt security or is more likely than not to be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the impairment is other-than-temporary and should be recognized currently in earnings in an amount equal to the entire difference between fair value and amortized cost. If a credit loss exists, but the Bank does not intend to sell the impaired debt security and is not more likely than not to be required to sell before recovery, the impairment is other-than-temporary and should be separated into (i) the estimated amount relating to credit loss, and (ii) the amount relating to all other factors. Only the estimated credit loss amount is recognized currently in earnings, with the remainder of the loss amount recognized in other comprehensive income.

In subsequent periods, if the present value of cash flows expected to be collected is less than the amortized cost basis, the Bank would record an additional other-than-temporary impairment and adjust the yield of the security prospectively. The amount of total other-than-temporary impairment for an available-for-sale security that previously was impaired is determined as the difference between its carrying amount prior to the determination of other-than-temporary impairment and its fair value. Interest on investment securities, including amortization of premiums and accretion of discounts, is included in Interest Income. Realized gains and losses from the sales of investment securities are recognized in current earnings using the specific identification method.

C. **Loans and Allowance for Loan Losses:** Long-term real estate mortgage loans generally have original maturities up to 30 years. Substantially all short- and intermediate-term loans for agricultural production or operating purposes have maturities of 10 years or less.

Loans are carried at their principal amount outstanding adjusted for charge-offs, premiums, discounts, deferred loan fees or costs, and derivative instruments and hedging valuation adjustments, if any. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding. The difference in the total investment in a loan and its principal amount is deferred as part of the carrying amount of the loan and the net difference is amortized over the life of the related loan as an adjustment to interest income using the effective interest method.

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

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

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

Loans are charged-off at the time they are determined to be uncollectible.

In cases where a borrower experiences financial difficulties and the Bank makes certain monetary concessions to the borrower through modifications to the contractual terms of the loan, the loan is classified as a restructured loan. A restructured loan constitutes a troubled debt restructuring if for economic or legal reasons related to the debtor's financial difficulties the Bank grants a concession to the debtor that it would not otherwise consider. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

The Bank uses a two-dimensional loan rating model based on internally generated combined system risk rating guidance that incorporates a 14-point risk rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan assuming default has occurred or is expected to occur within the next 12 months.

Each of the probability of default categories carries a distinct percentage of default probability. The 14-point risk rating scale provides for granularity of the probability of default, especially in the acceptable ratings. There are nine acceptable categories that range from a borrower of the highest quality to a borrower of minimally acceptable quality. The probability of default between 1 and 9 is very narrow and would reflect almost no default to a minimal default percentage. The probability of default grows more rapidly as a loan moves from a "9" rating to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain.

The credit risk rating methodology is a key component of the Bank's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals. A review of individual loans in each respective portfolio is performed periodically to determine the appropriateness of risk ratings and to ensure loss exposure to the Bank has been identified. Certain loan pools acquired from several of the District Associations are analyzed in accordance with the selling Association's allowance methodologies for assigning general and specific allowances. The allowance for loan losses is a valuation account used to reasonably estimate loan losses as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss.

The Bank considers the following factors, among others, when determining the allowance for loan losses:

- Credit risk classifications,
- Collateral values,
- Risk concentrations,
- Weather related conditions,
- Current production and economic conditions, and
- Prior loan loss experience.

A specific allowance may be established for impaired loans under Financial Accounting Standards Board (FASB) guidance on accounting by creditors for impairment of a loan. Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable market price, or fair value of the collateral if the loan is collateral dependent.

A general allowance may also be established under FASB guidance on accounting for contingencies, to reflect estimated probable credit losses incurred in the remainder of the loan portfolio at the financial statement date, which excludes loans included under the specific allowance discussed above. A general allowance can be evaluated on a pool basis for those loans with similar characteristics. The level of the general allowance may be based on management's best estimate of the likelihood of default adjusted for other relevant factors reflecting the current environment.

D. **Investments in Other Farm Credit System Institutions:** Investments in other Farm Credit System institutions are generally nonmarketable investments consisting of stock and participation certificates, allocated surplus, and reciprocal investments in other institutions regulated by the FCA.

E. **Premises and Equipment:** Premises and equipment are carried at cost less accumulated depreciation. Land is carried at cost. Depreciation is provided on the straight-line method over the estimated useful lives of the assets, which range from 3 to 40 years. Gains and losses on dispositions are reflected in current operations. Maintenance and repairs are charged to operating expense and improvements that extend the useful life of the asset are capitalized.

F. **Other Property Owned:** Other property owned, consisting of real and personal property acquired through foreclosure or deed in lieu of foreclosure, is recorded upon acquisition at fair value less estimated selling costs. Any initial reduction in the carrying amount of a loan to the fair value of the collateral received is charged to the allowance for loan losses. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income and expenses from operations and carrying value adjustments related to other property owned are included in Gains (Losses) from Other Property Owned, Net in the Consolidated Statements of Income.

G. **Debt Issuance Cost:** Direct expenses incurred in issuing debt and mandatorily redeemable preferred stock are deferred and amortized using the straight-line method (which approximates the interest method) over the term of the related indebtedness or term of the mandatorily redeemable preferred stock.

H. **Employee Benefit Plans:** The Bank participates in District and multi-District sponsored benefit plans. These plans include a defined benefit final average pay retirement plan, a defined benefit cash balance retirement plan, a defined benefit other postretirement benefits plan, and a defined contribution 401(k) plan.

Substantially all employees of the Bank may participate in either the AgFirst Farm Credit Retirement Plan or the AgFirst Farm Credit Cash Balance Retirement Plan (collectively referred to as the "Plans"), which are defined benefit plans and considered multi-employer plans under FASB accounting guidance. These two Plans are noncontributory and include eligible Bank and other District employees. The "Projected Unit Credit" actuarial method is used for financial reporting purposes. For participants hired prior to January 1, 2003, benefits are based on eligible compensation and years of service. For participants hired on or after January 1, 2003, benefits are determined using a percent of eligible compensation formula. The actuarially-determined costs of these Plans are allocated to each participating entity, including the Bank, by multiplying the Plans' net pension expense by each institution's eligible service cost and accumulated benefit obligation as a percentage of the total eligible service cost and total accumulated benefit obligation for all Plans' participants. The cumulative excess of amounts funded by the Bank over the cost allocated to the Bank is reflected as prepaid retirement expense, a component of other assets in the Bank's Consolidated Balance Sheets.

In addition to providing pension benefits, the Bank provides certain health care and life insurance benefits for retired employees (other postretirement benefits) through a multi-District sponsored retiree healthcare plan. Substantially all of the Bank's employees are eligible for those benefits when they reach early retirement age while working for the Bank. Early retirement age is defined as a minimum of age 55 and 10 years of service. Employees hired after December 31, 2002, and employees who separate from service between age 50 and age 55, are required to pay the full cost of their retiree health insurance coverage. Employees who retire subsequent to December 1, 2007 are no longer provided retiree life insurance benefits. Certain Bank charges related to this plan are an allocation of District charges based on the Bank's proportional share of the plan liability. Authoritative accounting guidance requires the accrual of the expected cost of providing these benefits to an employee and an employee's beneficiaries and covered dependents during the years that the employee renders service necessary to become eligible for these benefits. The cumulative excess of cost allocated to the Bank over the amounts funded by the Bank is reflected as postretirement benefits other than pensions, a component of Other Liabilities in the Bank's Consolidated Balance Sheets.

Since the foregoing defined benefit plans are multi-employer plans, the Bank does not apply the provisions of FASB guidance on employers' accounting for defined benefit pension and other postretirement plans in its stand-alone financial statements. Rather, the effects of this guidance are reflected in the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations.

Substantially all Bank employees are eligible to participate in the defined contribution Farm Credit Benefit Alliance (FCBA) 401(k) Plan, subsequently referred to as the 401(k) Plan, which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Bank contributes $0.50 for each $1.00 of the employee's first 6.00 percent of contribution up to the maximum employer contribution of 3.00 percent of eligible compensation. For employees hired on or after January 1, 2003, the Bank contributes $1.00 for each $1.00 of the employee's first 6.00 percent of contribution up to the maximum employer contribution of 6.00 percent of eligible compensation. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. The 401(k) Plan costs are expensed as funded.

Additional financial information for the above three plans may be found in Note 11 and in the Notes to the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations' 2011 Annual Report.

In addition to the multi-employer plans above, the Bank sponsors a single employer defined benefit supplemental retirement plan and offers a FCBA supplemental 401(k) plan for certain key employees. These plans are nonqualified; therefore, the associated liabilities are included in the Bank's Consolidated Balance Sheets in Other Liabilities. See Note 11 for additional financial information for these plans, including the impact of FASB guidance on the defined benefit supplemental retirement plan.

I. **Income Taxes:** The Bank is exempt from federal and other income taxes as provided in the Farm Credit Act.

J. **Derivative Instruments and Hedging Activity:** The Bank is party to derivative financial instruments, primarily interest rate swaps, which are principally used to reduce funding costs. The Bank may also enter into forward contracts to create a fixed purchase price. Derivatives are included in the Consolidated Balance Sheets as assets and liabilities and reflected at fair value.

Changes in the fair value of a derivative are recorded in current period earnings or accumulated other comprehensive income (loss) (AOCI) depending on the risk being hedged. For fair-value hedge transactions, which hedge changes in the fair value of assets, liabilities, or firm commitments, changes in the fair value of the derivative will generally be offset by changes in the hedged item's fair value and changes reported in earnings. For cash-flow hedge transactions, which hedge the variability of future cash flows related to a variable-rate asset, liability, or a forecasted transaction, changes in the fair value of the derivative will generally be deferred and reported in AOCI. The gains and losses on the derivative that are deferred and reported in AOCI will be reclassified into earnings in the periods in which earnings are impacted by the variability of the cash flows of the hedged item. The ineffective portion of all hedges is recorded in current period earnings. For derivatives not designated as a hedging instrument, if any, the related change in fair value is recorded in current period earnings.

The Bank formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as fair value or cash flow hedges to (1) specific assets or liabilities on the balance sheet or (2) firm commitments or forecasted transactions. The Bank also formally assesses at the hedge's inception whether the derivatives that are used in hedging transactions will be highly effective in offsetting changes in the fair value or cash flows of hedged items and whether those derivatives may be expected to remain highly effective in future periods. The Bank uses regression analysis (or other statistical analysis) to assess the effectiveness of its hedges on an ongoing basis. The Bank discontinues hedge accounting prospectively when the Bank determines that a hedge has not been or is not expected to be effective as a hedge. For cash flow hedges, any remaining AOCI would be amortized into earnings over the remaining life of the original hedged item. For fair value hedges, changes in the fair value of the derivative will be recorded in current period earnings. In all situations in which hedge accounting is discontinued and the derivative remains outstanding, the Bank will carry the derivative at its fair value on the balance sheet, recognizing changes in fair value in current period earnings.

The Bank may occasionally purchase a financial instrument in which a derivative instrument is "embedded." Upon purchasing the financial instrument, the Bank assesses whether the economic characteristics of the embedded derivative are clearly and closely related to the economic characteristics of the remaining component of the financial instrument and whether a separate, non-embedded instrument with the same terms as the embedded instrument would meet the definition of a derivative instrument. When it is determined that (1) the embedded derivative possesses economic characteristics that are not clearly and closely related to the economic characteristics of the host contract and (2) a separate, stand-alone instrument with the same terms would qualify as a derivative instrument, the embedded derivative is separated from the host contract, carried at fair value, and may be designated as either a fair value or cash flow hedge. However, if the entire contract were to be measured at fair value, with changes in fair value reported in current earnings, or if the Bank could not reliably identify and measure the embedded derivative for purposes of separating that derivative from its host contract, the entire contract would be carried on the balance sheet at fair value and not be designated as a hedging instrument.

K. **Valuation Methodologies:** Management applies various valuation methodologies to assets and liabilities that often involve a significant degree of judgment, particularly when active markets do not exist for the particular items being valued. Quoted market prices are referred to when estimating fair values for certain assets for which an observable active market exists. Management utilizes third party valuation services to obtain fair value prices for the majority of the Bank's investment securities. Management also utilizes significant estimates and assumptions to value items for which an observable active market does not exist. Examples of these items include: impaired loans, other property owned, pension and other postretirement benefit obligations, certain derivatives, certain investment securities and other financial instruments. These valuations require the use of various assumptions, including, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing, and liquidation values. The use of different assumptions could produce significantly different asset or liability values, which could have material positive or negative effects on the Bank's results of operations.

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability. This guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. It describes three levels of inputs that may be used to measure fair value as discussed in Note 15.

L. **Off-balance-sheet Credit Exposures:** Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses that may require payment of a fee. Commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These letters of credit are issued to facilitate commerce and typically result in the commitment being funded when the underlying transaction is consummated between the customer and third party. The credit risk associated with commitments to extend credit and commercial letters of credit is essentially the same as that involved with extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer's creditworthiness.

M. **Recent Accounting Developments:** In December 2011, the FASB issued Accounting Standards Update (ASU) 2011-11, "Balance Sheet (Topic 220) - Disclosures about Offsetting Assets and Liabilities." The guidance requires an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. This includes the effect or potential effect of rights of setoff associated with an entity's recognized assets and recognized liabilities. The requirements apply to recognized financial instruments and derivative instruments that are offset in accordance with accounting guidance and for those recognized financial instruments and derivative instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset or not. This guidance is to be applied retrospectively for all comparative periods and is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The adoption of this guidance will not impact the Bank's financial condition or its results of operations, but will result in additional disclosures.

In September 2011, the FASB issued ASU 2011-09 , "Compensation (Topic 715): Retirement Benefits – Multiemployer Plans." The amendment is intended to provide for more information about an employer's financial obligations to multiemployer pension and other postretirement benefit plans, which should help financial statement users better understand the financial health of significant plans in which the employer participates. The additional disclosures include the following: (1) a description of the nature of plan benefits; (2) a qualitative description of the extent to which the employer could be responsible for the obligations of the plan, including benefits earned by employees during employment with another employer, and (3) other quantitative information to help users understand the financial information about the plan. The amendments are effective for annual periods for fiscal years ending after December 15, 2011 for public entities. The amendments should be applied retrospectively for all prior periods presented. The adoption did not impact the Bank's financial condition or results of operations but did result in additional disclosures (see Note 11).

In June 2011, the FASB issued ASU 2011-05, "Comprehensive Income (Topic 220): Presentation of Comprehensive Income." This amendment is intended to increase the prominence of other comprehensive income in financial statements. The current option that permits the presentation of other comprehensive income in the statement of changes in equity has been eliminated. The main provisions of the guidance provides that an entity that reports items of other comprehensive income has the option to present comprehensive income in either one or two consecutive financial statements: (1) A single statement must present the components of net income and total net income, the components of other comprehensive income and total other comprehensive income, and a total for comprehensive income; (2) In a two-statement approach, an entity must present the components of net income and total net income in the first statement. That statement must be immediately followed by a financial statement that presents the components of other comprehensive income, a total for other comprehensive income, and a total for comprehensive income. With either approach, an entity is required to present reclassification adjustments for items reclassified from other comprehensive income to net income in the statement(s). This guidance is to be applied retrospectively. For public entities, it is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance will not impact the Bank's financial condition or results of operations, but will result in changes to the presentation of comprehensive income. In December 2011, the FASB issued guidance (ASU 2011-12; Topic 220) to defer the new requirement to present components of accumulated other comprehensive income reclassified as components of net income on the face of the financial statements. All other requirements in the guidance for comprehensive income are required to be adopted as set forth in the June 2011 guidance. The deferral is effective at the same time the new standard on comprehensive income is adopted.

In May 2011, the FASB issued ASU 2011-04, "Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs." The amendments change the wording used to describe the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments include the following: (1) Application of the highest and best use and valuation premise is only relevant when measuring the fair value of nonfinancial assets (does not apply to financial assets and liabilities); (2) Aligns the fair value measurement of instruments classified within an entity's shareholders' equity with the guidance for liabilities. As a result, an entity should measure the fair value of its own equity instruments from the perspective of a market participant that holds the instruments as assets; (3) Clarifies that a reporting entity should disclose quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy; (4) An exception to the requirement for measuring fair value when a reporting entity manages its financial instruments on the basis of its net exposure, rather than its gross exposure, to those risks; (5) Clarifies that the application of premiums and discounts in a fair value measurement is related to the unit of account for the asset or liability being measured at fair value. Premiums or discounts related to size as a characteristic of the entity's holding (that is, a blockage factor) instead of as a characteristic of the asset or liability (for example, a control premium), are not permitted. A fair value measurement that is not a Level 1 measurement may include premiums or discounts other than blockage factors when market participants would incorporate the premium or discount into the measurement at the level of the unit of account specified in other guidance; (6) Expansion of the disclosures about fair value measurements. The most significant change will require entities, for their recurring Level 3 fair value measurements, to disclose quantitative information about unobservable inputs used, a description of the valuation processes used by the entity, and a qualitative discussion about the sensitivity of the measurements. New disclosures are required about the use of a nonfinancial asset measured or disclosed at fair value if its use differs from its highest and best use. In addition, entities must report the level in the fair value hierarchy of assets and liabilities not recorded at fair value but where fair value is disclosed. The amendments are to be applied prospectively. The amendments are effective during interim and annual periods beginning after December 15, 2011. Early application is not permitted. The adoption of this guidance will not impact the Bank's financial condition or results of operations, but will result in additional disclosures.

In April 2011, the FASB issued ASU 2011-02, "Receivables (Topic 310): A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring," which provides for clarification on whether a restructuring constitutes a troubled debt restructuring (TDR). In evaluating whether a restructuring is a TDR, a creditor must separately conclude that both of the following exists: (1) the restructuring constitutes a concession, and (2) the debtor is experiencing financial difficulties. The guidance is effective for nonpublic entities, including the Bank, for annual periods ending on or after December 15, 2012, including interim periods within those annual periods. The guidance should be applied retrospectively to the beginning of the annual period of adoption. The new disclosures about TDR activity required by the guidance on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses," as discussed below, are effective for annual reporting periods ending after December 15, 2011.

In January 2011, the FASB issued ASU 2011-01, "Receivables (Topic 310): Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings." This amendment temporarily delayed the effective date of the disclosures about TDRs required by the guidance previously issued on "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses." The effective date of the new disclosures about TDRs coincides with the guidance for determining what constitutes a TDR as described above. The adoption of this guidance had no material impact on the Bank's financial condition and results of operations but resulted in significant additional disclosures (see Note 4).

In July 2010, the FASB issued ASU 2010-20, "Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses." This amendment provides additional information to assist financial statement users in assessing an entity's credit risk exposures and evaluating the adequacy of its allowance for credit losses. Existing disclosures were amended to include additional disclosures of financing receivables on both a portfolio segment and class of financing receivable basis. This includes a rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the period on a portfolio segment basis, with the ending balance further disclosed on the basis of the method of impairment (individually or collectively evaluated). The guidance also calls for new disclosures including but not limited to credit quality indicators at the end of the reporting period by class of financing receivables, the aging of past due financing receivables, nature and extent of financing receivables modified as troubled debt restructurings by class and the effect on the allowance for credit losses. For public entities, the disclosures as of the end of a reporting period were effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period were effective for interim and annual reporting periods beginning on or after December 15, 2010. The adoption of this guidance had no impact on the Bank's financial condition and results of operations but resulted in significant additional disclosures (see Note 4).

Effective January 1, 2010, the Bank adopted ASU 2010-06, "Fair Value Measurements and Disclosures (Topic 820)" which is intended to improve disclosures about fair value measurement by increasing transparency in financial reporting. The changes provide a greater level of disaggregated information and more detailed disclosures of valuation techniques and inputs to fair value measurement. The new disclosures and clarification of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the rollforward of activity in Level 3 fair value measurements. Those disclosures were effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of this guidance had no impact on the Bank's financial condition and results of operations but resulted in additional disclosures (see Note 15).

Note 3 — Investment Securities

Available-for-sale

A summary of the amortized cost and fair value of debt securities held as available-for-sale investments at December 31, 2011, 2010, and 2009, follows:

	December 31, 2011				
(dollars in thousands)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Yield**
U.S. Govt. GNMA MBS/CMOs	$ 4,831,529	$174,101	$ (3,129)	$ 5,002,501	2.46%
U.S. Govt. Agency MBS	1,634,942	26,459	(10,572)	1,650,829	1.50
Non-Agency CMOs (a)	291,377	248	(49,869)	241,756	0.83
Asset-Backed Securities (a)	34,736	2,239	(6,651)	30,324	0.70
Total	$ 6,792,584	$203,047	$ (70,221)	$ 6,925,410	2.15%

	December 31, 2010				
(dollars in thousands)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Yield**
U.S. Govt. GNMA MBS/CMOs	$ 4,836,617	$116,377	$ (5,983)	$ 4,947,011	2.19%
U.S. Govt. Agency MBS	1,743,192	26,768	(22,570)	1,747,390	1.46
Non-Agency CMOs (b)	357,648	59	(62,181)	295,526	0.67
Asset-Backed Securities (b)	43,204	2,354	(11,121)	34,437	0.70
Total	$ 6,980,661	$145,558	$(101,855)	$ 7,024,364	1.92%

	December 31, 2009				
(dollars in thousands)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Yield**
U.S. Govt. GNMA MBS/CMOs	$ 3,835,830	$ 34,286	$ (12,958)	$ 3,857,158	2.04%
U.S. Govt. Agency MBS	2,595,257	22,374	(44,256)	2,573,375	1.58
Non-Agency CMOs (c)	460,866	–	(100,839)	360,027	0.56
Asset-Backed Securities(c)	67,160	–	(19,695)	47,465	0.48
Total	$ 6,959,113	$ 56,660	$ (177,748)	$ 6,838,025	1.75%

(a) *Gross unrealized losses include non-credit related other-than-temporary impairment recognized in AOCI of $15.7 million for Non-Agency CMOs and $5.0 million for Asset-Backed Securities.*

(b) *Gross unrealized losses include non-credit related other-than temporary impairment recognized in AOCI of $13.9 million for Non-Agency CMOs and $9.1 million for Asset-Backed Securities.*

(c) *Gross unrealized losses include non-credit related other-than temporary impairment recognized in AOCI of $18.0 million for Non-Agency CMOs and $17.3 million for Asset-Backed Securities.*

Held-to-maturity

A summary of the amortized cost and fair value of debt securities held as held-to-maturity investments at December 31, 2011, 2010, and 2009, follows:

	December 31, 2011				
(dollars in thousands)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Yield**
U.S. Govt. Agency MBS	$ 691,331	$ 59,389	$ (188)	$ 750,532	5.35%
Mission Related Investments	163,531	14,112	(122)	177,521	6.07
Total	$ 854,862	$ 73,501	$ (310)	$ 928,053	5.49%

	December 31, 2010				
(dollars in thousands)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Yield**
U.S. Govt. Agency MBS	$ 913,648	$ 57,611	$ (248)	$ 971,011	5.35%
Mission Related Investments	138,666	5,476	(1,089)	143,053	6.15
Total	$ 1,052,314	$ 63,087	$ (1,337)	$ 1,114,064	5.46%

	December 31, 2009				
(dollars in thousands)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Yield**
U.S. Govt. Agency MBS	$ 1,250,051	$ 47,751	$ (289)	$ 1,297,513	5.19%
Mission Related Investments	138,133	1,403	(10,309)	129,227	5.99
Total	$ 1,388,184	$ 49,154	$ (10,598)	$ 1,426,740	5.27%

A summary of the expected maturity, estimated fair value, and amortized cost of investment securities at December 31, 2011 follows:

Available-for-sale

	Due in 1 year or less		Due after 1 year through 5 years		Due after 5 years through 10 years		Due after 10 years		Total	
(dollars in thousands)	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
U.S. Govt. GNMA MBS/CMOs	$ –	– %	$ –	– %	$ 1,596	1.17 %	$ 5,000,905	2.46 %	$ 5,002,501	2.46 %
U.S. Govt. Agency MBS	–	–	13,608	4.68	24,613	0.78	1,612,608	1.49	1,650,829	1.50
Non-Agency CMOs	–	–	–	–	–	–	241,756	0.83	241,756	0.83
Asset-Backed Securities	–	–	–	–	–	–	30,324	0.70	30,324	0.70
Total fair value	$ –	– %	$ 13,608	4.68 %	$ 26,209	0.80 %	$ 6,885,593	2.15 %	$ 6,925,410	2.15 %
Total amortized cost	$ –		$ 12,539		$ 26,096		$ 6,753,949		$ 6,792,584	

Held-to-maturity

	Due in 1 year or less		Due after 1 year through 5 years		Due after 5 years through 10 years		Due after 10 years		Total	
(dollars in thousands)	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
U.S. Govt. Agency MBS	$ –	– %	$ –	– %	$ 1,361	4.93 %	$ 689,970	5.36 %	$ 691,331	5.35 %
Mission Related Investments	–	–	24,089	6.63	31,451	6.09	107,991	5.94	163,531	6.07
Total amortized cost	$ –	– %	$ 24,089	6.63 %	$ 32,812	6.04 %	$ 797,961	5.44 %	$ 854,862	5.49 %
Total fair value	$ –		$ 25,485		$ 35,666		$ 866,902		$ 928,053	

Included in the available-for-sale investments are collateralized mortgage obligations (CMOs). Substantially all CMO securities have contractual maturities in excess of ten years. However, expected maturities for CMO securities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

Proceeds from sales and realized gains and losses on sales of investment securities are as follows:

	Year Ended December 31,		
(dollars in thousands)	2011	2010	2009
Proceeds from sales	$ 56,957	$ 57,468	$ 167,262
Realized gains	3,048	1,568	9,918
Realized losses	–	–	–

AgFirst's investments include primarily mortgage-backed securities (MBSs) and asset-backed securities (ABSs). These securities are held to maintain a liquidity reserve, manage short-term surplus funds, and manage interest rate risk. These securities must meet the applicable FCA regulatory guidelines, which require these securities to be high quality, senior class, and rated in the top category (AAA/Aaa) by Nationally Recognized Statistical Rating Organizations (NRSROs) at the time of purchase. To achieve the ratings, these securities have a guarantee of timely payment of principal and interest, credit enhancements achieved through over-collateralization or other means, and the priority of payments of senior classes over junior classes. All ABSs have credit enhancement features including senior/subordinate structure and/or are backed by a bond insurer.

The FCA considers a MBS or ABS ineligible if it falls below the AAA/Aaa credit rating criteria and requires System institutions to divest of such an investment unless the FCA grants specific approval to continue to hold an ineligible security.

The Bank's MBSs are collateralized by U.S. government or U.S. agency guaranteed residential mortgages and all were rated AAA/Aaa at December 31, 2011. Non-agency CMO securities not rated in the top category by at least one of the NRSROs at December 31, 2011 had a fair value of $240.0 million. ABSs not rated in the top category by at least one of the NRSROs at December 31, 2011 had a fair value of $21.3 million. For each of these investment securities in the Bank's portfolio rated below AAA/Aaa, the Bank has developed and submitted plans for approval by the FCA that provide that the securities may be held to maturity. The FCA has approved, with conditions, the Bank's plans for all but seven investments that have recently become ineligible. The Bank has submitted a plan to hold four of these recently ineligible securities and is in the process of submitting a plan to obtain approval from the FCA to hold the remaining three investments.

Mission related investments consist primarily of Rural America Bonds, which are private placement securities purchased under the Mission Related Program approved by the FCA.

An investment is considered impaired if its fair value is less than its cost. This also applies to those securities other-than-temporarily impaired for which a credit loss has been recognized but noncredit-related losses continue to remain unrealized. The following tables show the fair value and gross unrealized losses for investments that have been in a continuous unrealized loss position aggregated by investment category at December 31, 2011, 2010, and 2009. A continuous unrealized loss position for an investment is measured from the date the impairment was first identified.

	December 31, 2011					
	Less than 12 Months		Greater than 12 Months		Total	
(dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Govt. GNMA MBS/CMOs	$ 50,348	$ (29)	$ 260,965	$ (3,101)	$ 311,313	$ (3,130)
U.S. Govt. Agency MBS	227,889	(1,646)	442,142	(9,114)	670,031	(10,760)
Non-Agency CMOs	–	–	241,092	(49,868)	241,092	(49,868)
Asset-Backed Securities	–	–	27,356	(6,651)	27,356	(6,651)
Mission Related Investments	11,987	(122)	–	–	11,987	(122)
Total	$ 290,224	$ (1,797)	$ 971,555	$ (68,734)	$ 1,261,779	$ (70,531)

	December 31, 2010					
	Less than 12 Months		Greater than 12 Months		Total	
(dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Govt. GNMA MBS/CMOs	$ 602,933	$ (2,529)	$ 325,506	$ (3,454)	$ 928,439	$ (5,983)
U.S. Govt. Agency MBS	219,661	(1,492)	627,100	(21,327)	846,761	(22,819)
Non-Agency CMOs	–	–	292,015	(62,180)	292,015	(62,180)
Asset-Backed Securities	–	–	30,328	(11,121)	30,328	(11,121)
Mission Related Investments	43,895	(864)	4,784	(225)	48,679	(1,089)
Total	$ 866,489	$ (4,885)	$ 1,279,733	$ (98,307)	$ 2,146,222	$ (103,192)

	December 31, 2009					
	Less than 12 Months		Greater than 12 Months		Total	
(dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Govt. GNMA MBS/CMOs	$ 186,492	$ (1,242)	$ 1,269,486	$ (11,716)	$ 1,455,978	$ (12,958)
U.S. Govt. Agency MBS	213,231	(2,014)	1,369,665	(42,531)	1,582,896	(44,545)
Non-Agency CMOs	12,042	(2,395)	347,985	(98,444)	360,027	(100,839)
Asset-Backed Securities	–	–	47,465	(19,695)	47,465	(19,695)
Mission Related Investments	27,762	(4,145)	71,709	(6,164)	99,471	(10,309)
Total	$ 439,527	$ (9,796)	$ 3,106,310	$ (178,550)	$ 3,545,837	$ (188,346)

FASB guidance for other-than-temporary impairment contemplates numerous factors in determining whether an impairment is other-than-temporary. These factors include: (1) whether or not management intends to sell the security, (2) whether it is more likely than not that management would be required to sell the security before recovering its costs, or (3) whether management expects to recover the security's entire amortized cost basis (even if there is no intention to sell). If the Bank intends to sell the security or it is more likely than not that it would be required to sell the security, the impairment loss equals the full difference between amortized cost and fair value of the security. When the Bank does not intend to sell securities in an unrealized loss position and it is not more likely than not that it would be required to sell the securities, other-than-temporary impairment loss is separated into credit loss and non-credit loss. Credit loss is defined as the shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis.

The Bank performs periodic credit reviews, including other-than-temporary impairment analyses, on its investment securities portfolio. The objective is to quantify future possible loss of principal or interest due on securities in the portfolio. Factors considered in determining whether an impairment is other-than-temporary include among others: (1) the length of time and the extent to which the fair value is less than cost, (2) adverse conditions specifically related to the industry, (3) geographic area and the condition of the underlying collateral, (4) payment structure of the security, (5) ratings by rating agencies, (6) the credit worthiness of bond insurers, and (7) volatility of the fair value changes. Based on the results of all analyses, the Bank has recognized total other-than-temporary impairment during 2011 of $7.4 million in connection with ABS securities and non-agency CMO securities in its portfolio, which is included in Impairment Losses on Investments in the Consolidated Statements of Income.

Since the Bank does not intend to sell these other-than-temporarily impaired debt securities and is not more likely than not to be required to sell before recovery, the other-than temporary impairment of $7.4 million is separated into: (1) the estimated amount relating to credit loss ($9.3 million reflected in Net Income in the Consolidated Statements of Income), which is partially offset by (2) the amount relating to all other factors ($1.9 million reflected in other comprehensive income in the Consolidated Statements of Changes in Shareholders' Equity).

The Bank uses the present value of cash flows expected to be collected from the debt security to determine the amount of credit loss. This technique requires assumptions related to the underlying collateral, including default rates, degree and timing of prepayments, and loss severity. Assumptions can vary widely from security to security and are influenced by such factors as loan interest rate, geographical location of the borrower, borrower characteristics, and collateral type.

Significant inputs used in this technique to measure the amount related to the credit loss include, but are not limited to, performance indicators of the underlying assets in the security (including default rates, delinquency rates, and percentage of nonperforming assets), loan-to-collateral value ratios, third-party guarantees, current levels of subordination, vintage, geographic concentration, and credit ratings. The Bank obtains assumptions for the default rate, prepayment rate, and loss severity rate from an independent third party. Default rate assumptions are generally estimated using historical loss and performance information to estimate future defaults. The forecasted cumulative default rates used at December 31, 2011 ranged from 1.39 percent to 40.59 percent for non-agency CMO securities and from 21.42 percent to 82.87 percent for ABS securities. Prepayment rate assumptions are based on forecasted prepayments and resulted in prepayment rates that ranged from 6.73 percent to 19.96 percent for non-agency CMO securities and from 3.85 percent to 6.31 percent for ABS securities at December 31, 2011. At December 31, 2011, the loss severity rates estimated from assumptions ranged from 4.27 percent to 60.03 percent for non-agency CMO securities and from 59.59 percent to 100.00 percent for ABS securities.

For all investments other than the other-than-temporarily impaired securities discussed above, the Bank has not recognized any other-than-temporary impairment as the unrealized losses resulted from non-credit related factors. The Bank has the ability and intent to hold these investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities. Substantially all of these investments were in U.S. government agency securities and the Bank expects these securities would not be settled at a price less than their amortized cost. For the year ended December 31, 2011, net unrealized gains of $86.7 million were recognized in other comprehensive income for not other-than-temporarily impaired available-for-sale investments.

The following schedule details the activity related to cumulative credit losses on investments recognized in earnings as of December 31, 2011, 2010, and 2009:

	For the Year Ended December 31,		
(dollars in thousands)	2011	2010	2009
Beginning balance at January 1	$ 44,791	$ 33,159	$ –
Adjustment to beginning balance due to application of investment impairment accounting change	–	–	6,991
Adjusted beginning balance at January 1	44,791	33,159	6,991
Additions for the amount related to credit loss for which other-than-temporary impairment was not previously recognized	1,943	1,327	24,086
Additions for the amount related to credit loss for which other-than-temporary impairment was previously recognized	7,310	10,585	2,082
Reductions for increases in expected cash flows	(1,064)	(280)	–
Ending balance at December 31	$ 52,980	$ 44,791	$ 33,159

Note 4 — Loans and Allowance for Loan Losses

For a description of the Bank's accounting for loans, including impaired loans, and the allowance for loan losses, see Note 2, subsection C., above.

Credit risk arises from the potential inability of an obligor to meet its repayment obligation which exists in outstanding loans. The Bank manages credit risk associated with lending activities through an assessment of the credit risk profile of an individual obligor. The Bank sets its own underwriting standards and lending policies that provide direction to loan officers and are approved by the board of directors.

The credit risk management process begins with an analysis of the obligor's credit history, repayment capacity and financial position. Repayment capacity focuses on the obligor's ability to repay the obligation based on cash flows from operations or other sources of income, including non-farm income. Real estate mortgage loans must be secured by first liens on the real estate collateral. As required by FCA regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures.

The credit risk rating process for loans uses a two-dimensional loan rating structure, incorporating a 14-point risk rating scale (see further discussion in Note 2, subsection C. above) to identify and track a borrower's probability of default and a separate scale addressing loss given default. The loan rating structure calculates estimates of loss through two components, borrower risk and transaction risk. Borrower risk is the risk of loss driven by factors intrinsic to the borrower. The transaction risk or facility risk is related to the structure of a credit (tenor, terms, and collateral).

The Bank's loan portfolio, which includes purchased interests in loans, has been segmented by the following loan types as defined by the FCA:

- Direct Notes —direct loans to District Associations (see further discussion in Note 1).
- Real estate mortgage loans —generally to purchase farm real estate, refinance existing mortgages, construct various facilities used in agricultural operations, or purchase other rural residential/lifestyle real estate for both full-time and part-time farmers. In addition, credit for other agricultural purposes and family needs is available to full-time and part-time farmers. Real estate mortgage loans have maturities ranging from five to thirty years and must be secured by first liens on the real estate. These loans may be made only in amounts up to 85 percent of the appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a federal, state, or other governmental agency. The actual percentage of loan-to-appraised value when loans are made is generally lower than the statutory maximum percentage.
- Production and intermediate-term loans —for operating funds, equipment and other purposes. Eligible financing needs include operating inputs (such as labor, feed, fertilizer, and repairs), livestock, family living expenses, income taxes, debt payments on machinery or equipment, and other business-related expenses. Production loans may be made on a secured or unsecured basis and are most often made for a period of time that matches the borrower's normal production and marketing cycle, which is typically less than 12 months. Intermediate-term loans typically finance depreciable capital assets of a farm or ranch. Examples of the uses of intermediate-term loans are to purchase or refinance farm machinery, vehicles, equipment, breeding livestock, or farm buildings, to make improvements, or to provide working capital. Intermediate-term loans are made for a specific term, generally 10 years or less. These loans may be made on a secured or unsecured basis, but are normally secured.
- Agribusiness loans — may be made on a secured or unsecured basis.
  - Loans to cooperatives — loans for any cooperative purpose other than for communication, energy, and water and waste disposal.
  - Processing and marketing loans — for operations to process or market the products produced by a farmer, rancher, or producer or harvester of aquatic products, or by a cooperative.
  - Farm-related business loans — loans to eligible borrowers that furnish certain farm-related business services to farmers or ranchers that are directly related to their agricultural production.
- Rural residential real estate loans — to purchase a single-family dwelling that will be the primary residence in open country, which may include a town or village that has a population of not more than 2,500 persons. In addition, the loan may be to remodel, improve, or repair a rural home, or to refinance existing debt. These loans must be secured by a first lien on the property, except that it may be secured by a second lien if the institution also holds the first lien on the property.
- Communication loans — primarily to finance rural communication companies.
- Energy loans — primarily to finance electric generation, transmission and distribution systems serving rural areas.
- Water and waste disposal loans —primarily to finance water and waste disposal systems serving rural areas.
- International loans — primarily loans or credit enhancements to other banks to support the export of U.S. agricultural commodities or supplies. The federal government guarantees a substantial portion of these loans.
- Lease receivables — the net investment for all finance leases (such as direct financing leases, leveraged leases, and sales-type leases) where the Bank is the lessor.
- Loans to other financial institutions (OFIs) — loans to other financial institutions with which the Bank has a lending relationship.
- Other (including mission-related) — In addition to making loans to accomplish the System's Congressionally mandated mission to finance agriculture and rural America, the Bank may make investments in rural America to address the diverse needs of agriculture and rural communities across the country. The FCA approves these investments on a program or a case-by-case basis. Examples of investment programs that the FCA will consider include partnerships with agricultural and rural community lenders, investments in rural economic development and infrastructure, and investments in obligations and mortgage securities that increase the availability of affordable housing in rural America.

A summary of loans outstanding follows:

	December 31,		
(dollars in thousands)	**2011**	**2010**	**2009**
Direct notes	$ 14,094,384	$ 14,778,448	$ 14,890,794
Real estate mortgage	1,207,221	1,401,285	1,686,948
Production and intermediate-term	1,382,659	1,486,639	1,708,861
Agribusiness			
Loans to cooperatives	174,552	162,167	181,336
Processing and marketing	684,300	712,171	773,263
Farm-related business	114,826	61,801	59,173
Total agribusiness	973,678	936,139	1,013,772
Communication	136,899	113,021	104,208
Energy	246,930	296,213	304,517
Water and waste disposal	28,000	28,000	28,000
Rural residential real estate	2,060,025	1,831,928	1,548,829
Lease receivables	–	6,331	9,121
Loans to other financial institutions (OFIs)	5,250	5,000	7,000
Other (including mission-related)	17,020	22,161	25,269
Total Loans	$ 20,152,066	$ 20,905,165	$ 21,327,319

A substantial portion of the Bank's loan portfolio consists of notes receivable from District Associations. As described in Note 1, these notes are used by the Associations to fund their loan portfolios, which collateralize the notes. Therefore the Bank's concentration of credit risk in various agricultural commodities associated with these notes approximates that of the District as a whole. Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities, which would cause them to be similarly impacted by economic or other conditions. A substantial portion of the Associations' lending activities is collateralized, and their exposure to credit loss associated with lending activities is reduced accordingly, which further mitigates credit risk to the Bank.

The Bank may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with Farm Credit Administration regulations. The following tables present the principal balance of participations purchased and sold at December 31, 2011 and 2010:

	December 31, 2011							
	Within AgFirst District		**Within Farm Credit System**		**Outside Farm Credit System**		**Total**	
(dollars in thousands)	**Participations Purchased**	**Participations Sold**	**Participations Purchased**	**Participations Sold**	**Participations Purchased**	**Participations Sold**	**Participations Purchased**	**Participations Sold**
Real estate mortgage	$ 1,055,560	$ 41,469	$ 107,889	$ 39,820	$ 17,806	$ –	$ 1,181,255	$ 81,289
Production and intermediate-term	1,470,251	287,117	244,382	245,785	204,505	–	1,919,138	532,902
Agribusiness								
Loans to cooperatives	12,355	29,805	164,560	–	28,717	–	205,632	29,805
Processing and marketing	130,893	266,819	251,802	29,271	618,541	8,750	1,001,236	304,840
Farm-related business	34,077	33,339	93,958	–	21,089	–	149,124	33,339
Total agribusiness	177,325	329,963	510,320	29,271	668,347	8,750	1,355,992	367,984
Communication	–	43,562	181,323	–	–	–	181,323	43,562
Energy	167	16,675	257,196	–	7,510	–	264,873	16,675
Water and waste disposal	–	–	28,000	–	–	–	28,000	–
Rural residential real estate	269	–	–	–	–	–	269	–
Loans to OFIs	–	–	–	–	5,250	–	5,250	–
Other (including mission-related)	57,171	13,913	–	22,022	–	3,240	57,171	39,175
Total	$ 2,760,743	$ 732,699	$ 1,329,110	$ 336,898	$ 903,418	$ 11,990	$ 4,993,271	$ 1,081,587

	December 31, 2010							
	Within AgFirst District		**Within Farm Credit System**		**Outside Farm Credit System**		**Total**	
(dollars in thousands)	**Participations Purchased**	**Participations Sold**	**Participations Purchased**	**Participations Sold**	**Participations Purchased**	**Participations Sold**	**Participations Purchased**	**Participations Sold**
Real estate mortgage	$ 1,215,653	$ 33,245	$ 94,208	$ 25,581	$ 27,907	$ –	$ 1,337,768	$ 58,826
Production and intermediate-term	1,618,738	252,700	219,653	312,263	217,047	–	2,055,438	564,963
Agribusiness								
Loans to cooperatives	14,183	46,352	174,689	8,438	28,798	–	217,670	54,790
Processing and marketing	168,277	337,988	370,508	79,608	634,583	28,599	1,173,368	446,195
Farm-related business	41,374	10,580	27,764	5,866	9,523	–	78,661	16,446
Total agribusiness	223,834	394,920	572,961	93,912	672,904	28,599	1,469,699	517,431
Communication	–	30,579	149,082	4,796	–	–	149,082	35,375
Energy	245	18,805	298,508	4,765	22,434	–	321,187	23,570
Water and waste disposal	–	–	28,000	–	–	–	28,000	–
Lease receivables	6,331	–	–	–	–	–	6,331	–
Loans to OFIs	–	–	–	–	5,000	–	5,000	–
Other (including mission-related)	22,364	–	–	–	–	–	22,364	–
Total	$ 3,087,165	$ 730,249	$ 1,362,412	$ 441,317	$ 945,292	$ 28,599	$ 5,394,869	$ 1,200,165

A significant source of liquidity for the Bank is the repayments and maturities of loans. The following table presents the contractual maturity distribution of loans by loan type at December 31, 2011 and indicates that approximately 11.70 percent of loans had maturities of less than one year:

(dollars in thousands)	**Due less than 1 year**	**Due 1 Through 5 years**	**Due after 5 years**	**Total**
Direct notes	$ 1,667,096	$ 4,659,627	$ 7,767,661	$ 14,094,384
Real estate mortgage	124,489	419,678	663,054	1,207,221
Production and intermediate-term	421,840	657,651	303,168	1,382,659
Agribusiness				
Loans to cooperatives	10,102	78,328	86,122	174,552
Processing and marketing	98,272	486,196	99,832	684,300
Farm-related business	20,896	64,443	29,487	114,826
Total agribusiness	129,270	628,967	215,441	973,678
Communication	–	86,658	50,241	136,899
Energy	14,017	92,591	140,322	246,930
Water and waste disposal	–	–	28,000	28,000
Rural residential real estate	6	1,023	2,058,996	2,060,025
Lease receivables	–	–	–	–
Loans to OFIs	–	5,250	–	5,250
Other (including mission-related)	1,152	–	15,868	17,020
Total Loans	$ 2,357,870	$ 6,551,445	$ 11,242,751	$ 20,152,066

The following table shows loans and related accrued interest classified under the Farm Credit Administration Uniform Loan Classification System as a percentage of total loans and related accrued interest receivable by loan type as of December 31, 2011, 2010, and 2009:

	2011	2010	2009
Direct notes:			
Acceptable	85.65%	83.96%	86.13%
OAEM	11.38	11.28	11.26
Substandard/doubtful/loss	2.97	4.76	2.61
	100.00%	100.00%	100.00%
Real estate mortgage:			
Acceptable	84.03%	82.93%	85.26%
OAEM	9.86	8.28	5.16
Substandard/doubtful/loss	6.11	8.79	9.58
	100.00%	100.00%	100.00%
Production and intermediate-term:			
Acceptable	78.21%	79.49%	82.62%
OAEM	15.09	14.46	10.47
Substandard/doubtful/loss	6.70	6.05	6.91
	100.00%	100.00%	100.00%
Agribusiness:			
Loans to cooperatives:*			
Acceptable	98.40%	95.12%	
OAEM	1.60	4.88	
Substandard/doubtful/loss	–	–	
	100.00%	100.00%	
Processing and marketing:*			
Acceptable	88.78%	78.10%	
OAEM	5.05	11.48	
Substandard/doubtful/loss	6.17	10.42	
	100.00%	100.00%	
Farm-related business:*			
Acceptable	99.43%	99.42%	
OAEM	0.57	0.58	
Substandard/doubtful/loss	–	–	
	100.00%	100.00%	
Total agribusiness:			
Acceptable	91.76%	82.46%	76.57%
OAEM	3.90	9.61	7.39
Substandard/doubtful/loss	4.34	7.93	16.04
	100.00%	100.00%	100.00%

	2011	2010	2009
Communication:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Energy/water and waste disposal:			
Acceptable	99.25%	97.94%	100.00%
OAEM	0.75	0.80	–
Substandard/doubtful/loss	–	1.26	–
	100.00%	100.00%	100.00%
Rural residential real estate:			
Acceptable	100.00%	100.00%	99.89%
OAEM	–	–	0.11
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Lease receivables:			
Acceptable	–%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	–%	100.00%	100.00%
Loans to OFIs:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Other (including mission-related):			
Acceptable	87.15%	73.93%	68.91%
OAEM	1.79	1.41	11.40
Substandard/doubtful/loss	11.06	24.66	19.69
	100.00%	100.00%	100.00%
Total Loans:			
Acceptable	87.09%	85.21%	86.60%
OAEM	9.79	10.00	9.48
Substandard/doubtful/loss	3.12	4.79	3.92
	100.00%	100.00%	100.00%

**Disaggregated Agribusiness data is not available for 2009.*

The following tables provide an aging analysis of past due loans and related accrued interest as of December 31, 2011 and 2010:

	December 31, 2011					
(dollars in thousands)	**30 Through 89 Days Past Due**	**90 Days or More Past Due**	**Total Past Due**	**Not Past Due or Less Than 30 Days Past Due**	**Total Loans**	**Recorded Investment 90 Days or More Past Due and Accruing Interest**
Direct notes	$ –	$ –	$ –	$ 14,126,861	$ 14,126,861	$ –
Real estate mortgage	7,842	32,463	40,305	1,175,866	1,216,171	799
Production and intermediate-term	3,042	28,384	31,426	1,359,086	1,390,512	–
Agribusiness						
Loans to cooperatives	–	–	–	175,260	175,260	–
Processing and marketing	7	(319)	(312)	687,383	687,071	–
Farm-related business	–	–	–	115,135	115,135	–
Total agribusiness	7	(319)	(312)	977,778	977,466	–
Communication	–	–	–	137,126	137,126	–
Energy/water and waste disposal	–	–	–	276,488	276,488	–
Rural residential real estate	42,505	8,066	50,571	2,015,626	2,066,197	4,553
Lease receivables	–	–	–	–	–	–
Loans to OFIs	–	–	–	5,259	5,259	–
Other (including mission-related)	–	–	–	17,170	17,170	–
Total	$ 53,396	$ 68,594	$ 121,990	$ 20,091,260	$ 20,213,250	$ 5,352

	December 31, 2010					
(dollars in thousands)	**30 Through 89 Days Past Due**	**90 Days or More Past Due**	**Total Past Due**	**Not Past Due or Less Than 30 Days Past Due**	**Total Loans**	**Recorded Investment 90 Days or More Past Due and Accruing Interest**
Direct notes	$ –	$ –	$ –	$ 14,814,929	$ 14,814,929	$ –
Real estate mortgage	5,488	63,507	68,995	1,341,963	1,410,958	686
Production and intermediate-term	260	16,807	17,067	1,477,746	1,494,813	–
Agribusiness						
Loans to cooperatives	–	–	–	162,885	162,885	–
Processing and marketing	9	97	106	714,297	714,403	–
Farm-related business	–	–	–	61,960	61,960	–
Total agribusiness	9	97	106	939,142	939,248	–
Communication	–	–	–	113,221	113,221	–
Energy/water and waste disposal	–	–	–	326,091	326,091	–
Rural residential real estate	36,734	5,889	42,623	1,795,675	1,838,298	5,889
Lease receivables	–	–	–	6,378	6,378	–
Loans to OFIs	–	–	–	5,008	5,008	–
Other (including mission-related)	–	65	65	22,278	22,343	–
Total	$ 42,491	$ 86,365	$ 128,856	$ 20,842,431	$ 20,971,287	$ 6,575

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.

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

	December 31,		
(dollars in thousands)	**2011**	**2010**	**2009**
Nonaccrual loans:			
Real estate mortgage	$ 40,293	$ 74,838	$ 124,890
Production and intermediate-term	32,986	35,002	54,691
Agribusiness			
Processing and marketing *	4,316	3,825	
Farm-related business *	–	–	
Total agribusiness	4,316	3,825	37,147
Rural residential real estate	5,727	509	579
Other (including mission-related)	1,900	1,546	–
Total nonaccrual loans	$ 85,222	$ 115,720	$ 217,307
Accruing restructured loans:			
Real estate mortgage	$ 4,134	$ 5,010	$ –
Production and intermediate-term	10,017	9,610	–
Agribusiness			
Processing and marketing *	24,606	30,683	
Total agribusiness	24,606	30,683	–
Total accruing restructured loans	$ 38,757	$ 45,303	$ –
Accruing loans 90 days or more past due:			
Real estate mortgage	$ 799	$ 686	$ 1,526
Production and intermediate-term	–	–	21
Rural residential real estate	4,553	5,889	8,664
Total accruing loans 90 days or more past due	$ 5,352	$ 6,575	$ 10,211
Total nonperforming loans	$ 129,331	$ 167,598	$ 227,518
Other property owned	44,157	39,719	25,909
Total nonperforming assets	$ 173,488	$ 207,317	$ 253,427
Nonaccrual loans as a percentage of total loans	0.42%	0.55%	1.02%
Nonperforming assets as a percentage of total loans and other property owned	0.86%	0.99%	1.19%
Nonperforming assets as a percentage of capital	8.07%	10.90%	16.04%

** Disaggregated Agribusiness data is not available for 2009.*

The following table presents information relating to impaired loans (including accrued interest) as defined in Note 2:

	December 31,		
(dollars in thousands)	**2011**	**2010**	**2009**
Impaired nonaccrual loans:			
Current as to principal and interest	$ 16,133	$ 33,894	$ 186,768
Past due	69,089	81,826	30,539
Total impaired nonaccrual loans	85,222	115,720	217,307
Impaired accrual loans:			
Restructured	38,757	45,303	–
90 days or more past due	5,352	6,575	10,211
Total impaired accrual loans	44,109	51,878	10,211
Total impaired loans	$ 129,331	$ 167,598	$ 227,518

Additional impaired loan information is as follows:

	December 31, 2011			Year Ended December 31, 2011	
(dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ 19,149	$ 22,763	$ 3,851	$ 21,932	$ –
Production and intermediate-term	19,390	25,027	4,002	15,989	132
Agribusiness					
Processing and marketing	4,636	4,971	1,050	7,329	6
Total agribusiness	4,636	4,971	1,050	7,329	6
Energy/water and waste disposal	–	–	–	920	–
Rural residential real estate	104	104	36	52	–
Other (including mission-related)	542	1,879	110	932	–
Total	$ 43,821	$ 54,744	$ 9,049	$ 47,154	$ 138
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 26,077	$ 45,426	$ –	$ 56,445	$ 518
Production and intermediate-term	23,613	43,473	–	46,060	370
Agribusiness					
Loans to cooperatives	–	–	–	601	–
Processing and marketing	24,286	29,771	–	33,556	1,774
Total agribusiness	24,286	29,771	–	34,157	1,774
Energy/water and waste disposal	–	–	–	248	22
Rural residential real estate	10,176	10,055	–	6,710	161
Other (including mission-related)	1,358	9,641	–	1,390	–
Total	$ 85,510	$ 138,366	$ –	$ 145,010	$ 2,845
Total impaired loans:					
Real estate mortgage	$ 45,226	$ 68,189	$ 3,851	$ 78,377	$ 518
Production and intermediate-term	43,003	68,500	4,002	62,049	502
Agribusiness					
Loans to cooperatives	–	–	–	601	–
Processing and marketing	28,922	34,742	1,050	40,885	1,780
Total agribusiness	28,922	34,742	1,050	41,486	1,780
Energy/water and waste disposal	–	–	–	1,168	22
Rural residential real estate	10,280	10,159	36	6,762	161
Other (including mission-related)	1,900	11,520	110	2,322	–
Total	$ 129,331	$ 193,110	$ 9,049	$ 192,164	$ 2,983

	December 31, 2010			Year Ended December 31, 2010	
(dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
Impaired loans with a related allowance for credit losses:					
Real estate mortgage	$ 8,687	$ 8,959	$ 1,788	$ 23,982	$ –
Production and intermediate-term	14,822	52,326	2,129	15,266	462
Other (including mission-related)	1,546	1,546	600	1,454	–
Total	$ 25,055	$ 62,831	$ 4,517	$ 40,702	$ 462
Impaired loans with no related allowance for credit losses:					
Real estate mortgage	$ 71,848	$ 123,223	$ –	$ 104,189	$ 606
Production and intermediate-term	29,790	2,803	–	55,141	1,658
Agribusiness					
Processing and marketing	34,508	40,809	–	46,317	3,194
Total agribusiness	34,508	40,809	–	46,317	3,194
Rural residential real estate	6,397	6,397	–	6,000	129
Other (including mission-related)	–	–	–	84	–
Total	$ 142,543	$ 173,232	$ –	$ 211,731	$ 5,587
Total impaired loans:					
Real estate mortgage	$ 80,535	$ 132,182	$ 1,788	$ 128,171	$ 606
Production and intermediate-term	44,612	55,129	2,129	70,407	2,120
Agribusiness					
Processing and marketing	34,508	40,809	–	46,317	3,194
Total agribusiness	34,508	40,809	–	46,317	3,194
Rural residential real estate	6,397	6,397	–	6,000	129
Other (including mission-related)	1,546	1,546	600	1,538	–
Total	$ 167,598	$ 236,063	$ 4,517	$ 252,433	$ 6,049

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

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at December 31, 2011.

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

	Year Ended December 31,		
(dollars in thousands)	2011	2010	2009
Interest income which would have been recognized under the original loan terms	$ 17,492	$ 10,691	$ 16,747
Less: interest income recognized	2,903	5,955	4,369
Foregone interest income	$ 14,589	$ 4,736	$ 12,378

A summary of changes in the allowance for loan losses and period end recorded investment in loans is as follows:

	December 31, 2011								
(dollars in thousands)	Direct Note	Real Estate Mortgage	Production and Intermediate-term	Agribusiness	Communication	Energy/ Water and Waste Disposal	Rural Residential Real Estate	Other (including mission related)	Total
Allowance for credit losses:									
Balance at December 31, 2010	$ –	$ 4,836	$ 5,938	$ 2,722	$ 69	$ 307	$ –	$ 1,001	$ 14,873
Charge-offs	–	(24,572)	(26,023)	(3,847)	–	(3,218)	(36)	(10,083)	(67,779)
Recoveries	–	320	78	–	–	–	–	–	398
Provision of loan losses	–	28,298	32,661	6,099	164	3,216	73	9,711	80,222
Balance at December 31, 2011	$ –	$ 8,882	$ 12,654	$ 4,974	$ 233	$ 305	$ 37	$ 629	$ 27,714
December 31, 2011 allowance ending balance:									
Loans individually evaluated for impairment	$ –	$ 3,851	$ 4,002	$ 1,050	$ –	$ –	$ 36	$ 110	$ 9,049
Loans collectively evaluated for impairment	$ –	$ 5,031	$ 8,652	$ 3,924	$ 233	$ 305	$ 1	$ 519	$ 18,665
Recorded investment in loans outstanding:									
Ending Balance at December 31, 2011	$ 14,126,861	$ 1,216,171	$ 1,390,512	$ 977,466	$ 137,126	$ 276,488	$ 2,066,197	$ 22,429	$ 20,213,250
December 31, 2011 recorded investment ending balance:									
Loans individually evaluated for impairment	$ 14,126,861	$ 137,024	$ 27,206	$ 4,317	$ –	$ –	$ 2,065,928	$ 1,517	$ 16,362,853
Loans collectively evaluated for impairment	$ –	$ 1,079,147	$ 1,363,306	$ 973,149	$ 137,126	$ 276,488	$ 269	$ 20,912	$ 3,850,397

	December 31, 2010									
(dollars in thousands)	**Direct Note**	**Real Estate Mortgage**	**Production and Intermediate-term**	**Agribusiness**	**Communication**	**Energy/ Water and Waste Disposal**	**Rural Residential Real Estate**	**Lease Receivables**	**Other (including mission related)**	**Total**
Allowance for credit losses:										
Balance at December 31, 2009	$ –	$ 11,583	$ 11,606	$ 8,286	$ 72	$ 274	$ 12	$ –	$ 459	$ 32,292
Charge-offs	–	(42,430)	(8,590)	(7,379)	–	–	–	–	–	(58,399)
Recoveries	–	799	19	160	–	–	–	–	–	978
Provision for loan losses	–	34,884	2,903	1,655	(3)	33	(12)	–	542	40,002
Balance at December 31, 2010	$ –	$ 4,836	$ 5,938	$ 2,722	$ 69	$ 307	$ –	$ –	$ 1,001	$ 14,873
December 31, 2010 allowance ending balance:										
Loans individually evaluated for impairment	$ –	$ 1,788	$ 2,129	$ –	$ –	$ –	$ –	$ –	$ 600	$ 4,517
Loans collectively evaluated for impairment	$ –	$ 3,048	$ 3,809	$ 2,722	$ 69	$ 307	$ –	$ –	$ 401	$ 10,356
Recorded investment in loans outstanding:										
Ending Balance at December 31, 2010	$ 14,814,929	$ 1,410,958	$ 1,494,813	$ 939,248	$ 113,221	$ 326,091	$ 1,838,298	$ 6,378	$ 27,351	$ 20,971,287
December 31, 2010 recorded investment ending balance:										
Loans individually evaluated for impairment	$ 14,814,929	$ 243,593	$ 325,708	$ 257,290	$ –	$ 79,917	$ 1,838,298	$ 6,348	$ 10,190	$ 17,576,273
Loans collectively evaluated for impairment	$ –	$ 1,167,365	$ 1,169,105	$ 681,958	$ 113,221	$ 246,174	$ –	$ 30	$ 17,161	$ 3,395,014

To mitigate risk of loan losses, District Associations have entered into Long-Term Standby Commitments to Purchase agreements with the Federal Agricultural Mortgage Corporation (Farmer Mac) through an arrangement with the Bank. The agreements, which are effectively credit guarantees that will remain in place until the loans are paid in full, give the Associations the right to sell the loans identified in the agreements to the Bank, which can, in turn, sell them to Farmer Mac in the event of default (typically four months past due), subject to certain conditions. The balance of loans under Long-Term Standby Commitments to Purchase held by the Associations was $349.8 million, $251.1 million, and $204.9 million at December 31, 2011, 2010, and 2009, respectively. Fees paid to Farmer Mac, Federal National Mortgage Association (FNMA), and other government-sponsored enterprises (GSEs) for such commitments are paid by the Bank and Associations and totaled $9.8 million, $9.2 million, and $7.1 million for 2011, 2010, and 2009, respectively. These amounts are classified as noninterest expense.

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The following table presents additional information regarding troubled debt restructurings as of the restructuring date that occurred during the year ended December 31, 2011. The table does not include purchased credit impaired loans.

	Pre-modification Outstanding Recorded Investment			
(dollars in thousands)	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**
Troubled debt restructurings:				
Real estate mortgage	$ −	$ 10,236	$ 8,706	$ 18,942
Production and intermediate-term	18,000	30,475	25,798	74,273
Other (including mission-related)	−	−	1,554	1,554
Total	$ 18,000	$ 40,711	$ 36,058	$ 94,769

	Post-modification Outstanding Recorded Investment				Effects of Modification	
(dollars in thousands)	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Provisions**	**Charge-offs**
Troubled debt restructurings:						
Real estate mortgage	$ −	$ 11,886	$ 8,502	$ 20,388	$ 1,322	$ (1,322)
Production and intermediate-term	18,000	29,522	25,476	72,998	2,856	(13,276)
Other (including mission-related)	−	−	1,554	1,554	−	(679)
Total	$ 18,000	$ 41,408	$ 35,532	$ 94,940	$ 4,178	$ (15,277)

Interest concessions include interest forgiveness and interest deferment. Principal concessions include principal forgiveness, principal deferment, and maturity extension. Other concessions include additional compensation received which might be in the form of cash or other assets.

The following table presents information regarding troubled debt restructurings that occurred during the previous twelve months and for which there was a subsequent payment default during this same period. Payment default is defined as a payment that was thirty days or more past due.

(dollars in thousands)	Outstanding Recorded Investment at December 31, 2011
Defaulted troubled debt restructurings:	
Real estate mortgage	$ 6,500
Production and intermediate-term	13,287
Other (including mission-related)	–
Total	$ 19,787

TDRs outstanding at December 31, 2011 totaled $69.8 million, of which $31.0 million were in nonaccrual status.

Note 5 — Premises and Equipment

Premises and equipment consisted of the following:

	December 31,		
(dollars in thousands)	2011	2010	2009
Land	$ 888	$ 896	$ 896
Buildings and improvements	9,040	7,172	7,083
Furniture and equipment	62,591	55,315	66,002
Work in progress	–	620	–
	72,519	64,003	73,981
Less: accumulated depreciation	58,813	52,642	59,492
Total	$ 13,706	$ 11,361	$ 14,489

Note 6 — Other Property Owned

Net gains (losses) on other property owned consisted of the following:

	December 31,		
(dollars in thousands)	2011	2010	2009
Gains (losses) on sale, net	$ (397)	$ 1,672	$ –
Carrying value adjustments	(11,005)	(7,197)	–
Operating income (expense), net	(790)	133	(2,824)
Total	$ (12,192)	$ (5,392)	$ (2,824)

Deferred gains on sales of other property owned totaled $7.6 million, $9.9 million, and $9.3 million at December 31, 2011, 2010, and 2009, respectively. Gains were primarily deferred as the sales involved financing from the Bank. Deferred gains of $5.3 million are included in Loans and deferred gains of $2.3 million are included in Other Liabilities in the Consolidated Balance Sheets.

Note 7 — Other Assets and Other Liabilities

A summary of other assets and other liabilities follows:

	December 31,		
(dollars in thousands)	2011	2010	2009
Other assets:			
Unamortized debt issue costs	$ 20,759	$ 20,661	$ 17,832
Prepaid retirement expenses	17,792	20,091	21,600
Federal Home Loan Mortgage Corporation principal receivable	3,723	5,555	6,206
Derivative assets	52,647	62,245	70,041
Receivable from third party sub-servicer	40,042	42,110	25,749
Other	16,299	15,279	16,862
Total	$ 151,262	$ 165,941	$ 158,290
Other liabilities:			
Accounts payable	$ 4,980	$ 4,395	$ 6,641
Farm Credit System Ins. Corp. payable	13,788	12,268	48,029
Derivative liabilities	–	8,781	229
Postretirement benefits other than pensions	15,856	15,559	15,483
Cash collateral pledged from derivative counterparties	22,139	18,315	14,065
Payroll liabilities	6,181	6,194	6,071
Investments traded not settled	25,719	–	–
Bank drafts payable	11,579	–	–
Other	18,702	14,345	11,921
Total	$ 118,944	$ 79,857	$ 102,439

Note 8 — Bonds and Notes

The System, unlike commercial banks and other depository institutions, obtains funds for its lending operations primarily from the sale of Systemwide Debt Securities issued by the banks through the Funding Corporation. Certain conditions must be met before AgFirst can participate in the issuance of Systemwide Debt Securities. As one condition of participation, AgFirst is required by the Farm Credit Act and FCA regulations to maintain specified eligible assets, at least equal in value to the total amount of debt obligations outstanding for which it is primarily liable. This requirement does not provide holders of Systemwide Debt Securities with a security interest in any assets of the banks. The System banks and the Funding Corporation have entered into the Second Amended and Restated Market Access Agreement (MAA), which establishes criteria and procedures for the banks to provide certain information and, under certain circumstances, for restricting or prohibiting an individual bank's participation in Systemwide debt issuances, thereby reducing other System banks' exposure to statutory joint and several liabilities. At December 31, 2011, AgFirst was in compliance with the conditions of participation for the issuances of Systemwide Debt Securities.

Each issuance of Systemwide Debt Securities ranks equally, in accordance with the FCA regulations, with other unsecured Systemwide Debt Securities. Systemwide Debt Securities are not issued under an indenture and no trustee is provided with respect to these securities. Systemwide Debt Securities are not subject to acceleration prior to maturity upon the occurrence of any default or similar event.

The System may issue the following types of Systemwide Debt Securities:

- Federal Farm Credit Banks Consolidated Systemwide Bonds,
- Federal Farm Credit Banks Consolidated Systemwide Discount Notes,
- Federal Farm Credit Banks Consolidated Systemwide Master Notes,
- Federal Farm Credit Banks Global Debt Securities, and
- Federal Farm Credit Banks Consolidated Systemwide Medium-Term Notes.

Additional information regarding Systemwide Debt Securities can be found in their respective offering circulars.

In the following table, regarding AgFirst's participation in outstanding Systemwide Debt Securities, weighted average interest rates include the effect of related derivative financial instruments.

	Bonds		Discount Notes		Total	
Maturities	Amortized Cost	Weighted Average Interest Rate	Amortized Cost	Weighted Average Interest Rate	Amortized Cost	Weighted Average Interest Rate
			(dollars in thousands)			
2012	$ 8,594,066	0.42%	$ 3,158,888	0.14%	$ 11,752,954	0.34%
2013	5,823,057	0.58	–	–	5,823,057	0.58
2014	2,848,961	0.89	–	–	2,848,961	0.89
2015	1,761,741	1.43	–	–	1,761,741	1.43
2016	1,235,979	2.01	–	–	1,235,979	2.01
2017 and after	3,663,456	2.68	–	–	3,663,456	2.68
Total	$ 23,927,260	1.02%	$ 3,158,888	0.14%	$ 27,086,148	0.92%

Discount notes are issued with maturities ranging from 1 to 365 days. The average maturity of discount notes at December 31, 2011, was 76 days.

Systemwide debt includes callable bonds consisting of the following:

Amortized Cost	First Call Date	Year of Maturity
(dollars in thousands)		
$ 11,582,340	2012	2013 – 2025
10,000	2013	2018
$ 11,592,340	Total	

Most callable debt may be called on the first call date and any time thereafter.

As described in Note 1, the Insurance Fund is available to ensure the timely payment of principal and interest on Systemwide Debt Securities (Insured Debt) of System banks to the extent net assets are available in the Insurance Fund and not designated for specific use. All other liabilities on the financial statements are uninsured. At December 31, 2011, the assets of the Insurance Fund aggregated $3.392 billion; however, due to the other authorized uses of the Insurance Fund there is no assurance that any available amount in the Insurance Fund will be sufficient to fund the timely payment of principal or interest on an Insured Debt obligation in the event of a default by any System bank having primary liability thereon.

Note 9 — Mandatorily Redeemable Preferred Stock

On May 17, 2001, AgFirst issued $225.0 million of Mandatorily Redeemable Cumulative Preferred Stock at a par value of $1 thousand per share. This stock was redeemed on December 15, 2011. The stock carried a stated annual dividend rate of 8.393 percent, with dividends paid semi-annually in arrears on June 15th and December 15th. The Mandatorily Redeemable Preferred Stock was reported as a liability in 2010 and 2009 and the related dividends are reported as interest expense. Although the Mandatorily Redeemable Preferred Stock was required to be reported as a liability under GAAP, it qualified as capital for certain regulatory purposes.

Note 10 — Shareholders' Equity

Descriptions of the Bank's capitalization requirements, protection mechanisms, regulatory capitalization requirements and restrictions, and equities are provided below:

A. **Description of Equities:** In accordance with the Farm Credit Act and the Bank's capitalization bylaws, the Bank is authorized to issue and have outstanding Classes B, C, and D Common Stock, Participation Certificates, Preferred Stock, and other classes of equity as may be provided for in the bylaws. All Common Stock and Participation Certificates have a par or face value of five dollars ($5.00) per share.

The Bank had the following shares of common equities outstanding at December 31, 2011:

		Shares Outstanding *(dollars in thousands)*	
Class	Protected Status	Number	Aggregate Par Value
B Common/Nonvoting	No	1,599,937	$ 8,000
C Common/Voting	No	77,401,238	387,006
D Common/Nonvoting	No	2,105,000	10,525
Participation Certificates/Nonvoting	No	47,228	236
Total Capital Stock and Participation Certificates		81,153,403	$ 405,767

B. **Perpetual Preferred Stock:** On October 14, 2003, AgFirst issued $150.0 million of Perpetual Non-Cumulative Preferred Stock at a par value of $1 thousand per share. Dividends on the stock are non-cumulative and payable on the 15th day of June and December in each year, commencing December 15, 2003, at an annual rate equal to 7.30 percent. In the event dividends are not declared on the preferred stock for payment on any dividend payment date, then such dividends shall not cumulate and shall cease to accrue and be payable. On or after the dividend payment date in December 2008, AgFirst may, at its option, redeem the preferred stock in whole or in part at any time at the redemption price of $1 thousand per share plus accrued and unpaid dividends for the then current dividend period to the date of redemption.

On June 8, 2007, AgFirst issued $250.0 million of Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock, Series 1. Dividends on the stock are non-cumulative and are payable semi-annually in arrears on the 15th day of June and December in each year, commencing December 15, 2007, and ending on June 15, 2012, at an annual rate equal to 6.585 percent of the par value of $1 thousand per share, and will thereafter, commencing September 15, 2012, be payable quarterly in arrears on the 15th day of March, June, September, and December in each year, at an annual rate equal to 3-Month USD LIBOR plus 1.13 percent. In the event dividends are not declared on the Class B, Series 1 Preferred Stock for payment on any dividend payment date, then such dividends shall not cumulate and shall cease to accrue and be payable.

Payment of dividends or redemption price on the Preferred Stock may be restricted if the Bank fails to satisfy applicable minimum capital adequacy, surplus, and collateral requirements.

C. **Capital Stock:** District Associations are required to maintain ownership in the Bank in the form of Class B or Class C Common Stock as determined by the Bank. The Associations' minimum stock requirement is 1.75 percent of Association Direct Note balances, and a stock equalization computation is made annually. The Bank may require additional capital contributions to maintain its capital levels.

Additionally, the Bank has issued Class D Common Stock in connection with participations purchased by the Bank from other System institutions. Class D Common Stock issued in connection with participations has no voting rights. Such Stock may be retired at the discretion of the Board, and if retired, shall be retired at book value not to exceed its par value.

Class D Common Stock shall also be purchased by borrowers eligible to hold it as a condition for obtaining a loan in an amount as may be determined by the Board at its discretion within a range between a minimum of two percent (2.00%) of the loan amount or $1 thousand, whichever is less, and a maximum not to exceed ten percent (10.00%) of the loan amount. The Bank currently has no such loans outstanding.

D. **Other Equity:** At the inception of each Other Financing Institution (OFI) loan, the Bank requires OFIs to make cash purchases of participation certificates in the Bank. The Bank has a first lien on these equities for the repayment of any indebtedness to the Bank.

E. **Order of Priority Upon Impairment or Liquidation:**

Impairment

Net losses, to the extent they exceed unallocated surplus, shall, except as otherwise provided in the Act, be treated as impairing Stock in the following order:

First, Class B Common Stock, Class C Common Stock, Class D Common Stock, and Participation Certificates, pro rata, in proportion to the number of shares or units of each such class of Stock then issued and outstanding, until such Stock is fully impaired; and

Second, Preferred Stock in proportion to the number of shares of each class and series thereof then issued and outstanding (applied, as among series that rank differently upon liquidation or dissolution of AgFirst, in reverse order of priority first to the most junior ranking series and then successively to each next most junior ranking series) and consistent with the terms of each such class or series until such Stock is fully impaired; and

Third, subject to the Act, as amended, and the regulations thereunder, in such manner as shall be determined by the Board.

Liquidation

In the event of liquidation or dissolution of AgFirst, any assets of AgFirst remaining after payment or retirement of all liabilities shall be distributed in the following order or priority:

First, to the holders of Preferred Stock, in proportion to the number of shares of each class and series thereof then issued and outstanding and consistent with the terms of each such series until an amount equal to the liquidation preference provided for in the terms of such series of Preferred Stock has been distributed to such holders (applied, as among series that rank differently upon liquidation or dissolution of AgFirst, in order of priority first to the most senior ranking series and then successively to each next most senior ranking series); and

Second, to the holders of Class B Common Stock, Class C Common Stock, Class D Common Stock, and Participation Certificates, pro rata, in proportion to the number of shares or units of each such class of Stock then issued and outstanding, until an amount equal to the aggregate par or face value of all such shares or units has been distributed to such holders; and

Third, in accordance with the memorandum accounting established in the Agreement and Plan of Consolidation between The Farm Credit Bank of Columbia and The Farm Credit Bank of Baltimore, dated as of October 31, 1994; and

Fourth, all remaining assets of AgFirst after such distributions shall be to the extent practicable distributed to all Stockholders and holders of Participation Certificates on a patronage basis.

F. **Regulatory Capitalization Requirements and Restrictions:** FCA's capital adequacy regulations require the Bank to achieve permanent capital of seven percent of risk-adjusted assets and off-balance-sheet commitments. Failure to meet the seven percent permanent capital requirement can lead to the initiation of certain mandatory and possibly additional discretionary actions by FCA that, if undertaken, could have a direct material effect on the Bank's operations and Consolidated Financial Statements. The Bank is prohibited from reducing permanent capital by retiring stock or making certain other distributions to shareholders unless the prescribed capital standard is met. FCA Regulations also require all System institutions to achieve and maintain additional capital adequacy ratios as defined by FCA Regulations. These required ratios are total surplus as a percentage of risk-adjusted assets of seven percent and core surplus as a percentage of risk-adjusted assets of three and one-half percent. The Bank's permanent capital, total surplus and core surplus ratios at December 31, 2011 were 24.27 percent, 24.24 percent and 17.08 percent, respectively. The FCA notified AgFirst that the June 2007 issuance of $250.0 million of Perpetual Non-Cumulative Subordinated Preferred Stock could be included in core surplus only up to an amount not to exceed 25.00 percent of total core surplus, inclusive of the preferred stock component. At December 31, 2011, the full amount of this preferred stock issuance could be included in core surplus. Subsequent to the redemption of the $225.0 million of Mandatorily Redeemable Cumulative Preferred Stock on December 15, 2011, the FCA further notified AgFirst that the October 2003 issuance of $150.0 million of Perpetual Non-Cumulative Preferred Stock could also be included in core surplus up to an amount not to exceed 25.00 percent of total core surplus, inclusive of the preferred stock component. Prior to December 15, 2011, the $150.0 million Perpetual Non-Cumulative Preferred Stock was not included in core surplus.

Capital adequacy is also evaluated using a ratio of net collateral to total liabilities. FCA requires a minimum net collateral ratio of 103.00 percent. Subsequent to the issuance of the mandatorily redeemable preferred stock and until its redemption on December 15, 2011, FCA required AgFirst to maintain a minimum net collateral ratio of 104.00 percent. At December 31, 2011, the Bank's net collateral ratio was 106.49 percent. For purposes of calculating this ratio, net collateral is not risk adjusted.

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

G. **Accumulated Other Comprehensive Income (Loss):** Accumulated other comprehensive income (loss) at December 31 was comprised of the following components.

(dollars in thousands)	2011	2010	2009
Unrealized (losses) gains on investments available-for-sale	$ 132,825	$ 43,703	$ (121,088)
Employee benefit plan adjustments	(3,263)	(2,623)	(2,116)
Cash flow hedges	(5,565)	(8,751)	–
Total accumulated other comprehensive income (loss)	$ 123,997	$ 32,329	$ (123,204)

Note 11 — Employee Benefit Plans

The Bank participates in four District sponsored benefit plans. These plans include two multiemployer defined benefit pension plans, the AgFirst Farm Credit Retirement Plan which is a final average pay plan (FAP) and the AgFirst Farm Credit Cash Balance Retirement Plan which is a cash balance plan (CB). In addition the Bank participates in a multiemployer defined benefit other postretirement benefits plan (OPEB), the Farm Credit Benefits Alliance Retiree and Disabled Medical and Dental Plan and a defined contribution 401(k) plan. The risks of participating in these multiemployer plans are different from single-employer plans in the following aspects:

a) Assets contributed to multiemployer plans by one employer may be used to provide benefits to employees of other participating employers.

b) If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.

c) If the Bank chooses to stop participating in some of its multiemployer plans, the Bank may be required to contribute to eliminate the underfunded status of the plan related to its participants.

The Bank's participation in the multiemployer defined benefit plans for the annual period ended December 31, 2011, 2010 and 2009 is outlined in the table below. The "Percentage Funded to Projected Benefit Obligation" or "Percentage Funded to Accumulated Postretirement Benefit Obligation" represents the funded amount for the entire plan and the "Contributions" and "Percentage of Total Contributions" columns represent the Bank's respective amounts.

Pension Plan	**Percentage Funded to Projected Benefit Obligation**			**Contributions**			**Percentage of Total Contributions**		
	2011	**2010**	**2009**	**2011**	**2010**	**2009**	**2011**	**2010**	**2009**
AgFirst Farm Credit Retirement Plan	74.82%	75.75%	71.65%	$6,281	$6,678	$8,056	15.83%	16.20%	17.16%
AgFirst Farm Credit Cash Balance Retirement Plan	81.77%	115.95%	145.01%	$230	$104	$241	27.90%	22.61%	27.64%

Other Postretirement Benefit Plan	**Percentage Funded to Accumulated Postretirement Benefit Obligation**			**Contributions**			**Percentage of Total Contribution**		
	2011	**2010**	**2009**	**2011**	**2010**	**2009**	**2011**	**2010**	**2009**
Farm Credit Benefits Alliance Retiree and Disabled Medical and Dental Plans	0.00%	0.00%	0.00%	$885	$913	$910	14.84%	15.55%	15.82%

The District's multiemployer plans are not subject to ERISA and no Form 5500 is required. As such, the following information is neither available for nor applicable to the plans:

1. The Employee Identification Number (EIN) and three-digit Pension Plan Number.
2. The most recent Pension Protection Act (PPA) zone status. Among other factors, plans in the red zone are generally less than 65 percent funded, plans in the yellow zone are less than 80 percent funded, and plans in the green zone are at least 80 percent funded.
3. The "FIP/RP Status" indicating whether a financial improvement plan (FIP) or a rehabilitation plan (RP) is either pending or has been implemented.
4. The expiration date(s) of collective-bargaining agreement(s).

Substantially all employees of the Bank are eligible to participate in either the FAP Plan or the CB Plan. These two Plans are noncontributory and include eligible Bank and other District employees. For participants hired prior to January 1, 2003, benefits are provided under the FAP Plan and are based on eligible compensation and years of service. For participants hired on or after January 1, 2003, benefits are provided under the CB Plan and are determined using a percent of eligible compensation formula. The employer contribution into the CB Plan is based on a formula of 3.00-5.00 percent of eligible compensation (depending on years of service) and interest credits as allocated to an employee's theoretical account balance. The actuarially-determined costs of these plans are allocated to each participating entity, including the Bank, by multiplying the plans' net pension expense by each institution's eligible service cost and accumulated benefit obligation as a percentage of the total eligible service cost and total accumulated benefit obligation for all plan participants. Plan expenses included in employee benefit costs were $8.8 million for 2011, $8.3 million for 2010, and $7.8 million for 2009. The cumulative excess of amounts funded by the Bank over the cost allocated to the Bank is reflected as prepaid retirement expense, a component of Other Assets in the Consolidated Balance Sheets.

In addition to providing pension benefits, the Bank provides certain medical and dental benefits for eligible retired employees through the OPEB Plan. Substantially all of the Bank employees may become eligible for the benefits if they reach early retirement age while working for the Bank. Early retirement age is defined as a minimum of age 55 and 10 years of service. Employees hired after December 31, 2002, and employees who separate from service between age 50 and age 55, are required to pay the full cost of their retiree health insurance coverage. Employees who retire subsequent to December 1, 2007 are no longer provided retiree life insurance benefits. Certain Bank charges related to this plan are an allocation of District charges based on the Bank's proportional share of the plan liability. This plan is unfunded with expenses paid as incurred. Postretirement benefits other than pensions included in employee benefit costs were $1.2 million for 2011, $989 thousand for 2010, and $884 thousand for 2009. The cumulative excess of cost allocated to the Bank over the amounts funded by the Bank is reflected as postretirement benefits other than pensions, a component of Other Liabilities in the Bank's Consolidated Balance Sheets.

The Bank also participates in the defined contribution 401(k) Plan, as described in Note 2, which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2002, the Bank contributes $0.50 for each $1.00 of the employee's first 6.00 percent of contribution (based on total compensation) up to the maximum employer contribution of 3.00 percent of total compensation. For employees hired on or after January 1, 2003, the Bank contributes $1.00 for each $1.00 of the employee's first 6.00 percent of contribution up to the maximum employer contribution of 6.00 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. The 401(k) Plan costs are expensed as funded. Employer contributions to this plan included in salaries and employee benefit costs were $1.2 million, $1.0 million, and $973 thousand for the years ended December 31, 2011, 2010, and 2009, respectively.

In addition to the multi-employer plans above, the Bank sponsors a single employer defined benefit supplemental retirement plan and offers a FCBA supplemental 401(k) plan for certain key employees. These plans are nonqualified; therefore, the associated liabilities are included in the Bank's Consolidated Balance Sheets in Other Liabilities. The Bank funded the benefit payments of $292 thousand for 2011 and $252 each for 2010 and 2009 for the defined benefit supplemental retirement plan. The expenses of these nonqualified plans included in the Bank's employee benefit costs were $72 thousand, $62 thousand, and $55 thousand for the years ended December 31, 2011, 2010, and 2009, respectively.

FASB guidance further requires the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of AOCI. Under the guidance, these amounts are subsequently recognized as components of net periodic benefit costs over time. For 2011, 2010, and 2009, $639 thousand, $507 thousand and $715 thousand, respectively, has been recognized as a net debit to AOCI to reflect these elements.

The supplemental retirement plan is unfunded and had a projected benefit obligation of $9.3 million and a net under-funded status of $9.3 million at December 31, 2011. Net periodic pension cost for 2011 was $911 thousand. Assumptions used to determine the projected benefit obligation as of December 31, 2011 included a discount rate of 5.20 percent and a rate of compensation increase of 4.50 percent.

Additional financial information for the four District sponsored multi-employer plans may be found in the Notes to the Combined Financial Statements of AgFirst Farm Credit Bank and District Associations' 2011 Annual Report.

Note 12 — Related Party Transactions

As discussed in Note 1, the Bank lends funds to the District Associations primarily to fund their loan portfolios. Further disclosure regarding these related party transactions is found in Notes 4, 10, and 14.

Interest income recognized on direct notes receivable from District Associations was $411.2 million, $465.8 million and $536.9 million for 2011, 2010, and 2009, respectively.

The Bank has had participation loans outstanding during the last year to certain of its directors, their immediate family members, and organizations with which the directors are affiliated. These loans were made in the ordinary course of business, and were made on the same terms, including interest rate, amortization schedule and collateral, as those prevailing at the time for comparable transactions with unaffiliated persons. No loan to a director, or to any organization affiliated with such person, or to any immediate family member who resides in the same household as such person or in whose loan or business operation such person has a material financial or legal interest, involved more than the normal risk of collectability.

Note 13 — Regulatory Enforcement Matters

At December 31, 2011, there were no regulatory enforcement matters or agreements in place with the Bank and FCA.

Note 14 — Commitments and Contingencies

The Bank has various contingent liabilities and commitments outstanding as discussed elsewhere in these notes to the Consolidated Financial Statements. While primarily liable for its portion of System bonds and notes, the Bank is jointly and severally liable for the bonds and notes of the other System banks. The total bonds and notes of the System at December 31, 2011, were $184.780 billion.

In the normal course of business, the Bank may participate in credit related financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers or the borrowers of the District Associations. These financial instruments include standby letters of credit, various guarantees and commitments to extend credit.

The Bank participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. At December 31, 2011, the Bank had outstanding $123.1 million of standby letters of credit issued on behalf of District and non-district customers, with expiration dates ranging from March 2012 to December 2016. The maximum potential amount of future payments the Bank may be required to make under these existing guarantees is $123.1 million.

A guarantor is required to recognize, at the inception of the guarantee, a liability for the fair value of a guarantee commitment. The Bank has determined the fair value of the guarantee commitment based upon the fees to be earned over the life of the guarantee. The fair value is updated periodically to reflect changes in individual guarantee amounts and the remaining life to maturity of the individual guarantees in the Bank's inventory. At December 31, 2011, the Bank's inventory of standby letters of credit had a fair value of $1.8 million and was included in Other Liabilities in the Consolidated Balance Sheets.

The Bank also guarantees certain loans held by District Associations in the amount of $4.4 million expiring in less than one year and $1.8 million expiring in one to three years. The notional amounts of these guarantees represent the maximum amount of exposure the Bank has related to these instruments as of December 31, 2011.

At December 31, 2011, $1.472 billion of commitments to extend credit were outstanding with a related loss reserve of $2.0 million included in Other Liabilities in the Consolidated Balance Sheets. Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these financial instruments have off-balance-sheet credit risk because their amounts could be drawn upon at the option of the borrower. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and the same credit policies are applied by management. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the loan collateral is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower.

Legal actions are pending against the Bank in which claims for money damages are asserted. On at least a quarterly basis, the Bank assesses its liabilities and contingencies in connection with outstanding legal proceedings utilizing the latest information available. While the outcome of legal proceedings is inherently uncertain, on the basis of information presently available, management and legal counsel are of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the Bank. Since it is not probable that the Bank will incur a loss or the loss is not estimable, no liability has been recorded for these claims.

Note 15 — Fair Value Measurement

FASB guidance on fair value measurements defines fair value, establishes a framework for measuring fair value, and requires fair value disclosures for certain assets and liabilities measured at fair value on a recurring and non-recurring basis. For the Bank, these assets and liabilities consist primarily of investments available-for-sale, highly-liquid funds, derivative assets and liabilities, assets held in trust funds, standby letters of credit, impaired loans, other property owned, and collateral liabilities.

This guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability.

This guidance establishes a fair value hierarchy for disclosure of fair value measurements to maximize the use of observable inputs, that is, inputs that reflect the assumptions market participants would use in pricing an asset or liability based on market data obtained from sources independent of the reporting entity. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

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

Level 1

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. Level 1 assets and liabilities could include investment securities and derivative contracts that are traded in an active exchange market, in addition to certain U.S. Treasury securities that are highly-liquid and are actively traded in over-the-counter markets.

The Bank's Level 1 assets at December 31, 2011 consist of assets held in trust funds related to deferred compensation and supplemental retirement plans. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

Level 2

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability. Level 2 assets and liabilities could include investment securities that are traded in active, non-exchange markets and derivative contracts that are traded in active, over-the-counter markets.

The fair value of substantially all of the Bank's investment securities is determined from third-party valuation services that estimate current market prices. Inputs and assumptions related to third-party market valuation services are typically observable in the marketplace. Such services incorporate prepayment assumptions and underlying mortgage- or asset-backed collateral information to generate cash flows that are discounted using appropriate benchmark interest rate curves and volatilities. Third-party valuations also incorporate information regarding broker/dealer quotes, available trade information, historical cash flows, credit ratings, and other market information. Such valuations represent an estimated exit price, or price to be received by a seller in active markets to sell the investment securities to a willing participant.

The fair value of the Bank's derivative financial instruments is the estimated amount to be received to sell a derivative asset or paid to transfer a derivative liability in active markets among willing participants at the reporting date. Estimated fair values are determined through internal market valuation models which use an income approach. These models incorporate benchmark interest rate curves (primarily the LIBOR swap curve), potential volatilities of future interest rate movements, and other inputs which are observable directly or indirectly in the marketplace. The Bank compares internally calculated derivative valuations to broker/dealer quotes to substantiate the results.

The Bank's Level 2 assets and liabilities at December 31, 2011 include derivative contracts and investments in U.S. government and agency mortgage-backed securities and U.S. agency debt securities, all of which have unadjusted values from third-party or internal pricing models. The underlying loans for these investment securities are residential mortgages. Level 2 assets also include federal funds sold, securities purchased under resale agreements, and other highly-liquid funds, all of which are non-exchange-traded instruments. The market value of these federal funds sold and other instruments is generally their face value, plus accrued interest, as these instruments are highly-liquid, readily convertible to cash, and short-term in nature.

The Bank's Level 2 liabilities also include collateral liabilities. The majority of derivative contracts are supported by bilateral collateral agreements with counterparties requiring the posting of collateral in the event certain dollar thresholds of credit exposure are reached. The market value of collateral liabilities is face value plus accrued interest that approximates fair value.

Level 3

Level 3 inputs to the valuation methodology are unobservable and supported by little or no market activity. Level 3 assets and liabilities could include investments and derivative contracts whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, and other instruments for which the determination of fair value requires significant management judgment or estimation. Level 3 assets and liabilities could also include investments and derivative contracts whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

Level 3 assets at December 31, 2011 include certain loans evaluated for impairment under FASB guidance which have fair values based upon the underlying collateral as the loans were collateral-dependent loans. Since the value of the collateral, less estimated costs to sell, was less than the principal balance of the loan, specific reserves were established for these loans. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral, and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy.

Level 3 assets at December 31, 2011 also include the Bank's mortgage-related asset-backed investment portfolio and non-agency CMO investment portfolio. The underlying loans for the asset-backed securities are mortgage related. The underlying loans for the non-agency CMO securities are residential mortgages. Based on the currently illiquid marketplace for these investments and the lack of marketplace information available as inputs and assumptions to the valuation process, the Bank classified the mortgage-related asset-backed investment portfolio and non-agency CMO investment portfolio as Level 3 assets. The fair value measurement of these assets involved management's judgment and was based on multiple factors, including information obtained from third-party valuation services using both Level 2 and Level 3 inputs. The significant inputs for the valuation models include yields, probability of default, loss severity, and prepayment rates.

Other property owned is classified as a Level 3 asset at December 31, 2011. The fair value for other property owned is based upon the collateral fair value. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned.

Level 3 liabilities at December 31, 2011 include standby letters of credit whose market value is internally calculated based on information that is not observable either directly or indirectly in the marketplace.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following tables present the assets and liabilities that are measured at fair value on a recurring basis at December 31, 2011, 2010, and 2009 for each of the fair value hierarchy levels.

	December 31, 2011			
(dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Assets:				
Investments available-for-sale:				
U.S. Govt. GNMA MBS/CMOs	$ –	$ 5,002,501	$ –	$ 5,002,501
U.S. Govt. Agency MBS	–	1,650,829	–	1,650,829
Non-Agency CMOs	–	–	241,756	241,756
Asset-Backed Securities	–	–	30,324	30,324
Total Investments available-for-sale	–	6,653,330	272,080	6,925,410
Commercial paper, Bankers' Acceptances, CD's & Others	–	–	–	–
Federal funds sold, securities purchased under resale agreements, and other	–	83,822	–	83,822
Interest rate swaps and other financial instruments	–	52,647	–	52,647
Assets held in trust funds	3,151	–	–	3,151
Total Assets	$ 3,151	$ 6,789,799	$ 272,080	$ 7,065,030
Liabilities:				
Interest rate swaps and other financial instruments	$ –	$ –	$ –	$ –
Collateral liabilities	–	22,139	–	22,139
Standby letters of credit	–	–	1,787	1,787
Total Liabilities	$ –	$ 22,139	$ 1,787	$ 23,926

	December 31, 2010			
(dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Assets:				
Investments available-for-sale:				
U.S. Govt. GNMA MBS/CMOs	$ –	$ 4,947,011	$ –	$ 4,947,011
U.S. Govt. Agency MBS	–	1,747,390	–	1,747,390
Non-Agency CMOs	–	–	295,526	295,526
Asset-Backed Securities	–	–	34,437	34,437
Total Investments available-for-sale	–	6,694,401	329,963	7,024,364
Commercial paper, Bankers' Acceptances, CD's & Others	–	52,000	–	52,000
Federal funds sold, securities purchased under resale agreements, and other	–	8,744	–	8,744
Interest rate swaps and other financial instruments	–	62,245	–	62,245
Assets held in trust funds	2,983	–	–	2,983
Total Assets	$ 2,983	$ 6,817,390	$ 329,963	$ 7,150,336
Liabilities:				
Interest rate swaps and other financial instruments	$ –	$ 8,781	$ –	$ 8,781
Collateral liabilities	–	18,315	–	18,315
Standby letters of credit	–	–	1,263	1,263
Total Liabilities	$ –	$ 27,096	$ 1,263	$ 28,359

	December 31, 2009			
(dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Assets:				
Investments available-for-sale:				
U.S. Govt. GNMA MBS/CMOs	$ –	$ 3,857,158	$ –	$ 3,857,158
U.S. Govt. Agency MBS	–	2,573,375	–	2,573,375
Non-Agency CMOs	–	–	360,027	360,027
Asset-Backed Securities	–	–	47,465	47,465
Total Investments available-for-sale	–	6,430,533	407,492	6,838,025
Commercial paper, Bankers' Acceptances, CD's & Others	–	86,690	–	86,690
Federal funds sold, securities purchased under resale agreements, and other	–	146,201	–	146,201
Interest rate swaps and other financial instruments	–	70,041	–	70,041
Assets held in trust funds	2,825	–	–	2,825
Total Assets	$ 2,825	$ 6,733,465	$ 407,492	$ 7,143,782
Liabilities:				
Interest rate swaps and other financial instruments	$ –	$ 229	$ –	$ 229
Collateral liabilities	–	14,065	–	14,065
Standby letters of credit	–	–	2,461	2,461
Total Liabilities	$ –	$ 14,294	$ 2,461	$ 16,755

The following tables present the changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the years ended December 31, 2011, 2010, and 2009. Non-agency CMO securities were transferred from Level 2 to Level 3 assets effective March 31, 2009, as the Bank began adjusting the valuation obtained from a third-party pricing service for this portfolio to reflect, in part, the valuation obtained from a cash flow modeling process. The Bank had no other transfers of assets or liabilities into or out of Level 1 or Level 2 during 2009 and the Bank had no transfers of assets or liabilities into or out of Level 1 or Level 2 during 2010 or 2011.

(dollars in thousands)	**Asset-Backed Investment Securities**	**Non-Agency CMOs**	**Standby Letters Of Credit**
Balance at January 1, 2011	$ 34,437	$ 295,526	$ 1,263
Total gains or (losses) realized/unrealized:			
Included in earnings	(3,583)	(5,670)	–
Included in other comprehensive income (loss)	4,355	12,502	–
Purchases	–	–	–
Sales	–	–	–
Issuances	–	–	524
Settlements	(4,885)	(60,602)	–
Transfers in and/or out of level 3	–	–	–
Balance at December 31, 2011	$ 30,324	$ 241,756	$ 1,787

(dollars in thousands)	**Asset-Backed Investment Securities**	**Non-Agency CMOs**	**Standby Letters Of Credit**
Balance at January 1, 2010	$ 47,465	$ 360,027	$ 2,461
Total gains or (losses) realized/unrealized:			
Included in earnings	(7,959)	(3,953)	–
Included in other comprehensive income (loss)	10,928	38,716	–
Purchases, sales, issuances and settlements, net	(15,997)	(99,264)	(1,198)
Transfers in and/or out of level 3	–	–	–
Balance at December 31, 2010	$ 34,437	$ 295,526	$ 1,263

(dollars in thousands)	**Asset-Backed Investment Securities**	**Non-Agency CMOs**	**Standby Letters Of Credit**
Balance at January 1, 2009	$ 79,961	$ –	$ 2,301
Total gains or (losses) realized/unrealized:			
Included in earnings	(20,949)	(3,775)	–
Included in other comprehensive income (loss)	27,955	46,108	–
Purchases, sales, issuances and settlements, net	(39,502)	(79,626)	160
Transfers in and/or out of level 3	–	397,320	–
Balance at December 31, 2009	$ 47,465	$ 360,027	$ 2,461

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

Assets and liabilities measured at fair value on a non-recurring basis at December 31, 2011, 2010, and 2009 for each of the fair value hierarchy levels are summarized below.

	December 31, 2011				
(dollars in thousands)	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)
Assets:					
Impaired loans	$ –	$ –	$ 34,771	$ 34,771	$ (71,913)
Other property owned	$ –	$ –	$ 48,014	$ 48,014	$ (11,402)

	December 31, 2010				
(dollars in thousands)	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)
Assets:					
Impaired loans	$ –	$ –	$ 20,538	$ 20,538	$ (40,232)
Other property owned	$ –	$ –	$ 40,269	$ 40,269	$ (5,526)

	December 31, 2009				
(dollars in thousands)	Level 1	Level 2	Level 3	Total Fair Value	YTD Total Gains (Losses)
Assets:					
Impaired loans	$ –	$ –	$ 77,417	$ 77,417	$ (48,218)
Other property owned	$ –	$ –	$ 27,969	$ 27,969	$ –

Note 16 — Disclosures about Fair Value of Financial Instruments

The following table presents the carrying amounts and fair values of the Bank's financial instruments at December 31, 2011, 2010, and 2009. Carrying amounts include accrued interest if applicable.

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

.	December 31, 2011		December 31, 2010		December 31, 2009	
(dollars in thousands)	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:						
Loans, net of allowance	$ 20,124,352	$ 20,406,083	$ 20,890,292	$ 21,007,236	$ 21,295,027	$ 21,434,395
Derivative assets	$ 52,647	$ 52,647	$ 62,245	$ 62,245	$ 70,041	$ 70,041
Cash and cash equivalents	$ 1,301,569	$ 1,301,569	$ 1,427,033	$ 1,427,033	$ 938,884	$ 938,884
Investment securities	$ 7,780,272	$ 7,835,742	$ 8,076,678	$ 8,119,858	$ 8,226,209	$ 8,245,233
Accrued interest Receivable	$ 78,906	$ 78,906	$ 84,692	$ 84,692	$ 94,756	$ 94,756
Assets held in trust funds	$ 3,151	$ 3,151	$ 2,983	$ 2,983	$ 2,825	$ 2,825
Financial liabilities:						
Systemwide Debt Securities	$ 27,128,566	$ 27,263,779	$ 28,382,546	$ 28,284,708	$ 28,776,211	$ 28,794,187
Derivative liabilities	$ –	$ –	$ 8,781	$ 8,781	$ 229	$ 229

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

A. **Loans:** Because no active market exists for the Bank's loans, fair value is estimated by discounting the expected future cash flows using the Bank's current interest rates at which similar loans currently would be made to borrowers with similar credit risk.

   For purposes of determining fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool. Fair values of loans in a nonaccrual status are estimated to be the carrying amount of the loan less specific reserves.

B. **Accrued Interest Receivable:** The carrying value of accrued interest receivable approximates its fair value.

C. **Cash and Cash Equivalents:** The carrying value is primarily utilized as a reasonable estimate of fair value.

D. **Investment Securities:** Fair value is primarily based upon prices obtained from a third party valuation service. See additional information in Note 15.

E. **Systemwide Debt Securities:** Bonds and notes are not regularly traded; thus, quoted market prices are not available. Fair value of these instruments is estimated by discounting expected future cash flows based on the quoted market price of similar maturity Treasury notes, assuming a constant estimated spread relationship between Systemwide bonds and notes and comparable Treasury notes.

F. **Derivative Instruments:** The fair value of derivatives is the estimated amount to be received or paid to replace the instruments at the reporting date, considering current and projected interest rates. Where actively quoted market prices do not exist, estimated fair values are determined through internal market valuation models. See additional information in Note 15.

G. **Assets Held In Trust Funds:** See Note 15 for discussion of estimation of fair value for these assets.

Note 17 — Derivative Financial Instruments and Hedging Activities

The Bank's goal is to minimize interest rate sensitivity by managing the repricing characteristics of assets and liabilities so that the net interest margin is not adversely affected by movements in interest rates. The Bank maintains an overall interest rate risk management strategy that may incorporate the use of derivative instruments to lower cost of funding or to reduce interest rate risk. Currently, the primary derivative type used by the Bank is interest rate swaps, which convert fixed interest rate debt to a lower floating interest rate than was achievable from issuing floating rate debt with identical repricing characteristics. They may allow the Bank to lower funding costs, allow it to diversify sources of funding, or alter interest rate exposures arising from mismatches between assets and liabilities. Interest rate swaps enable the Bank to raise long-term borrowings at fixed rates and swap them into floating rates that are lower than those available to the Bank if floating rate borrowings were made directly. Under these arrangements, the Bank agrees with other parties to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating rate index.

The Bank may also purchase interest rate derivatives such as caps, in order to reduce the impact of rising interest rates on its floating-rate debt, and floors, in order to reduce the impact of falling interest rates on its floating-rate assets. In addition, the Bank may also fix a price to be paid in the future which qualifies as a derivative forward contract.

As a result of interest rate fluctuations, interest income and interest expense related to hedged variable-rate assets and liabilities, respectively, will increase or decrease. Another result of interest rate fluctuations is that hedged fixed-rate assets and liabilities will appreciate or depreciate in market value. The effects of any earnings variability or unrealized changes in market value are expected to be substantially offset by the Bank's gains or losses on the derivative instruments that are linked to these hedged assets and liabilities. The Bank considers its strategic use of derivatives to be a prudent method of managing interest rate sensitivity, as it prevents earnings from being exposed to undue risk posed by changes in interest rates.

The primary type of derivative instrument used and the amount of activity for the year ended December 31, 2011 is summarized in the following table:

Notional Amounts *(dollars in millions)*	**Receive-Fixed Swaps**	**Forward Contracts**
Balance at beginning of period	$ 1,135	$ 445
Additions	–	330
Maturities/amortization	(600)	(709)
Terminations	–	–
Balance at end of period	$ 535	$ 66

By using derivative instruments, the Bank exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, the Bank's credit risk will equal the fair value gain in the derivative. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes the Bank, thus creating a repayment risk for the Bank. When the fair value of the derivative contract is negative, the Bank owes the counterparty and, therefore, assumes no repayment risk.

To minimize the risk of credit losses, the Bank deals with counterparties that have an investment grade credit rating from a major rating agency and also monitors the credit standing of and levels of exposure to individual counterparties. The estimated gross credit risk exposure at December 31, 2011 of $52.3 million was with five counterparties and represented approximately 9.78 percent of the total notional amount of interest rate swaps. The Bank held $22.1 million of interest-bearing cash collateral posted by one counterparty related to these swaps. The Bank does not anticipate nonperformance by any of these counterparties. The estimated gross credit risk exposure at December 31, 2010 of $62.2 million was with seven counterparties and represented approximately 5.48 percent of the total notional amount of interest rate swaps. The Bank held $18.3 million of interest-bearing cash collateral at December 31, 2010, posted by one counterparty related to these swaps. The estimated gross credit risk exposure at December 31, 2009 of $70.0 million was with eight counterparties and represented approximately 5.08 percent of the total notional amount of interest rate swaps. The Bank held $14.1 million of interest-bearing cash collateral at December 31, 2009, posted by one counterparty related to these swaps. The Bank typically enters into master agreements that contain netting provisions. These provisions allow the Bank to require the net settlement of covered contracts with the same counterparty in the event of default by the counterparty on one or more contracts. A number of swaps are supported by collateral arrangements with counterparties. At December 31, 2011, the Bank had not posted collateral with respect to any of these arrangements.

The Bank's derivative activities are monitored by its Asset-Liability Management Committee (ALCO) as part of the Committee's oversight of the Bank's asset/liability and treasury functions. The Bank's ALCO is responsible for approving hedging strategies that are developed within parameters established by the Bank's Board of Directors through the Bank's analysis of data derived from financial simulation models and other internal and industry sources. The resulting hedging strategies are then incorporated into the Bank's overall interest rate risk-management strategies.

Fair-Value Hedges

For derivative instruments designated as fair value hedges, the gains or losses on the derivative, as well as the offsetting loss or gain on the hedged item attributable to the hedged risk, are recognized in current earnings. The Bank includes the gain or loss on the hedged items in the same line item (interest expense) as the offsetting loss or gain on the related interest rate swaps. The amount of the loss on interest rate swaps recognized in interest expense for the year ended December 31, 2011 was $9.9 million, while the amount of the gain on the Systemwide Debt Securities was $9.9 million. Gains and losses on each derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Cash Flow Hedges

From time to time, the Bank may acquire when-issued securities, generally Government National Mortgage Association (GNMA) bonds. The when-issued transactions are contracts to purchase securities that will not be delivered until 30, or more, days in the future. These purchase commitments are considered derivatives (cash flow hedges) in the form of forward contracts. Changes in market value of the contracted securities, between purchase and settlement date, represent the effective portion of the Bank's forward contracts. These amounts are included in Other Comprehensive Income (OCI), and Other Liabilities or Other Assets as appropriate, as firm commitments in the Bank's Balance Sheet for each period end.

At December 31, 2011, the Bank had committed to purchase $66.4 million in when-issued GNMA bonds that had a market value of $66.7 million, a $319 thousand increase in value. At December 31, 2010, the Bank had committed to purchase $444.5 million in when-issued GNMA bonds that had a market value of $435.7 million, an $8.8 million decline in value.

For derivative instruments that are designated and qualify as a cash flow hedge, such as the Bank's forward contracts, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Note 18 - Fair Values of Derivative Instruments

The following tables represent the fair value of derivative instruments at December 31, 2011, 2010 and 2009:

(dollars in thousands)	**Balance Sheet Classification Assets**	**12/31/11 Fair Value**	**Balance Sheet Classification Liabilities**	**12/31/11 Fair Value**
Derivatives designated as hedging instruments:				
Receive-fixed swaps	Other Assets	$ 52,328	Other Liabilities	$ –
Forward contracts	Other Assets	319	Other Liabilities	–
Total		$ 52,647		$ –

(dollars in thousands)	**Balance Sheet Classification Assets**	**12/31/10 Fair Value**	**Balance Sheet Classification Liabilities**	**12/31/10 Fair Value**
Derivatives designated as hedging instruments:				
Receive-fixed swaps	Other Assets	$ 62,245	Other Liabilities	$ –
Forward contracts	Other Assets	–	Other Liabilities	8,781
Total		$ 62,245		$ 8,781

(dollars in thousands)	**Balance Sheet Classification Assets**	**12/31/09 Fair Value**	**Balance Sheet Classification Liabilities**	**12/31/09 Fair Value**
Derivatives designated as hedging instruments:				
Receive-fixed swaps	Other Assets	$ 70,041	Other Liabilities	$ 229
Total		$ 70,041		$ 229

The following tables set forth the amount of net gain (loss) recognized in the Consolidated Statements of Income for the years ended December 31, 2011, 2010, and 2009.

(dollars in thousands)	**Location of Gain or (Loss) Recognized in the Statement of Income**	**2011 Amount of Gain or (Loss) Recognized in the Statement of Income**	**2010 Amount of Gain or (Loss) Recognized in the Statement of Income**	**2009 Amount of Gain or (Loss) Recognized in the Statement of Income**
Derivatives – Fair Value Hedging Relationships:				
Receive-fixed swaps	Noninterest Income	$ –	$ –	$ 469
Total		$ –	$ –	$ 469

The following table sets forth the amount of net gain (loss) recognized in the Statements of Income for the years ended December 31, 2011 and 2010 and the amount of net gain (loss) recognized in the Balance Sheets for December 31, 2011 and December 31, 2010.

(dollars in thousands)	**Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)**		**Location of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)**	**Amount of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)**		**Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)**	**Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)**	
	2011	**2010**		**2011**	**2010**		**2011**	**2010**
Derivatives – Cash Flow Hedging Relationships:								
Firm Commitments	$ 3,035	$ (8,751)	Interest Income	$ (150)	$ –	Interest Income	$ –	$ –

Note 19 — Additional Derivative Financial Instruments and Other Financial Instruments Disclosures

The table below provides information about derivative financial instruments and other financial instruments that are sensitive to changes in interest rates, including debt obligations and interest rate swaps. The debt information below represents the principal cash flows and related weighted average interest rates by expected maturity dates. The derivative information below represents the notional amounts and weighted average interest rates by expected maturity dates.

December 31, 2011 *(dollars in millions)*	**Maturities of 2011 Interest Rate Derivative Products and Other Financial Instruments** **2012**	**2013**	**2014**	**2015**	**2016**	**2017 and after**	**Total**	**Fair Value**
Systemwide Debt Securities:								
Fixed rate	$ 6,409	$ 3,644	$ 2,724	$ 1,746	$ 1,217	$ 3,654	$ 19,394	$ 19,559
Weighted average interest rate	0.45%	0.79%	0.92%	1.44%	2.04%	2.69%	1.19%	
Variable rate	5,344	2,179	125	16	19	9	7,692	7,662
Weighted average interest rate	0.21%	0.22%	0.20%	0.14%	0.13%	0.15%	0.22%	
Derivative Instruments:								
Receive fixed swaps								
Notional value	$ 175	$ 110	$ –	$ 100	$ 100	$ 50	$ 535	$ 54
Weighted average receive rate	3.07%	3.02%	–%	5.01%	3.45%	1.65%	3.99%	
Weighted average pay rate	0.58%	0.90%	–%	1.77%	1.48%	0.84%	1.36%	
Total notional value	$ 175	$ 110	$ –	$ 100	$ 100	$ 50	$ 535	$ 54
Total weighted average rates on swaps:								
Receive rate	3.07%	3.02%	–%	5.01%	3.45%	1.65%	3.99%	
Pay rate	0.58%	0.90%	–%	1.77%	1.48%	0.84%	1.36%	

The total notional value and fair value of forward contracts at December 31, 2011 was $66.4 million and $66.7 million, respectively. The forward contracts expire in 2012.

Note 20 — Quarterly Financial Information (Unaudited)

Quarterly results of operations for the years ended December 31, 2011, 2010, and 2009 follow:

(dollars in thousands)	**2011** **First**	**Second**	**Third**	**Fourth**	**Total**
Net interest income	$ 143,949	$ 147,611	$ 150,367	$ 152,850	$ 594,777
Provision for (reversal of allowance for) loan losses	10,896	19,380	27,997	21,949	80,222
Noninterest income (expense), net	(30,148)	(23,126)	(35,864)	(39,959)	(129,097)
Net income	$ 102,905	$ 105,105	$ 86,506	$ 90,942	$ 385,458

	2010 **First**	**Second**	**Third**	**Fourth**	**Total**
Net interest income	$ 140,354	$ 140,292	$ 140,511	$ 150,089	$ 571,246
Provision for (reversal of allowance for) loan losses	4,430	18,052	11,144	6,376	40,002
Noninterest income (expense), net	(19,324)	(32,173)	(28,837)	(33,515)	(113,849)
Net income	$ 116,600	$ 90,067	$ 100,530	$ 110,198	$ 417,395

	2009 **First**	**Second**	**Third**	**Fourth**	**Total**
Net interest income	$ 107,547	$ 117,654	$ 124,173	$ 140,287	$ 489,661
Provision for (reversal of allowance for) loan losses	16,701	18,194	19,493	(7,740)	46,648
Noninterest income (expense), net	(38,332)	(35,531)	(27,141)	(32,866)	(133,870)
Net income	$ 52,514	$ 63,929	$ 77,539	$ 115,161	$ 309,143

Note 21 – District Merger Activity

Effective January 1, 2011, Farm Credit of North Florida, ACA, and Farm Credit of Southwest Florida, ACA, merged with and into Farm Credit of South Florida, ACA, after the FCA granted final approval of the merger on December 20, 2010. Farm Credit of South Florida then changed its name to Farm Credit of Florida, ACA. The merger was accounted for under the acquisition method of accounting guidance.

Prior to the merger, those Associations entered into an agreement with the Bank under which the Bank would provide limited financial assistance to the merged Association in the event of substantial further deterioration in the combined high risk asset portfolio of the merged Association. This agreement relates only to a finite pool of high risk assets of the merged Association existing at the merger date, which had a net total of approximately $176.2 million and $250.0 million at December 31, 2011 and January 1, 2011, respectively. Through this agreement, the merged Association will absorb substantial losses on these high risk assets in advance of the Bank providing financial assistance. This financial "safety net" from the Bank does not include losses that are sustained outside of the high risk asset pool. The agreement provides protection to the Bank, such as limitation on the Association's ability to make patronage distributions and certain other restrictions which are imposed if the merged Association's capital levels fail to meet minimum established levels. Assistance under the agreement, if any, is not expected to have a material impact on the financial condition of the Bank or District.

In February 2012, the Boards of Directors of Jackson Purchase, ACA, and Chattanooga, ACA (collectively referred to as the "Merger Associations") approved a proposed Plan of Merger ("Merger"). The Merger has been approved by AgFirst and has been submitted to the FCA for approval. Upon FCA approval, the Merger will be submitted to shareholders of the Merger Associations for their review and approval. Pending the necessary approvals, the Merger is anticipated to be effective July 1, 2012. The Merger will be accounted for under the acquisition method of accounting guidance.

Note 22 - Subsequent Events

The Bank has evaluated subsequent events and has determined that, except as described below, there are none requiring disclosure through March 13, 2012, which is the date the financial statements were issued.

On February 17, 2012, the Bank repurchased, through privately negotiated transactions, and cancelled 90,550 shares of Class B Perpetual Non-Cumulative Fixed-to-Floating Rate Subordinated Preferred Stock issued by the Bank in June 2007 at a par value of $1 thousand per share. The effect of this transaction was to reduce preferred stock outstanding by $90.6 million and increase additional paid-in capital by $26.3 million.

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