AgSouth Farm Credit, ACA

SECOND QUARTER 2016

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CERTIFICATION

The undersigned certify that we have reviewed the June 30, 2016 quarterly report of AgSouth Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.

William P. Spigener, Jr.
Chief Executive Officer

Alisa D. Gunter
Chief Financial Officer

William T. Robinson
Chairman of the Board

August 8, 2016

AgSouth Farm Credit, ACA

Report on Internal Control Over Financial Reporting

The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's Consolidated Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by, or under the supervision of the Association's principal executives and principal financial officers, or persons performing similar functions, and affected 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 Association, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial information in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Association's assets that could have a material effect on its Consolidated Financial Statements.

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of June 30, 2016. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association's management concluded that as of June 30, 2016, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association's management determined that there were no material weaknesses in the internal control over financial reporting as of June 30, 2016.

William P. Spigener
William P. Spigener
Chief Executive Officer

Alisa D. Gunter
Alisa D. Gunter
Chief Financial Officer

August 8, 2016

AgSouth Farm Credit, ACA

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

(dollars in thousands)

The following commentary reviews the financial condition and results of operations of AgSouth Farm Credit, ACA (Association) for the period ended June 30, 2016. This information should be read in conjunction with the accompanying financial statements, notes to the financial statements, and the 2015 Annual Report of AgSouth Farm Credit. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

FORWARD LOOKING INFORMATION

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

- political, legal, regulatory and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international, and farm-related business sectors;
- weather-related, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry; and
- actions taken by the Federal Reserve System in implementing monetary policy.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a wide range of agricultural commodities produced in our region, including poultry (broilers, turkeys and eggs), timber, sod and nursery, field grains, soybeans and hay, cotton, horses, blueberries, fruits, nuts and beef cattle. Loans to producers of these commodities total $1,386,038 or 85.54 percent of the Association's portfolio. Farm size varies, and many of the Association customers have diversified farming operations. These factors, along with the numerous opportunities for non-farm income in the area, reduce to some degree the level of income dependency on any given commodity.

Georgia Region

The second quarter of 2016 has presented generally favorable growing conditions for almost all crops grown in AgSouth's Georgia region. As usual there have been some isolated areas that have not received adequate rainfall; however, the significant expansion of irrigation over the past several years has helped mitigate this risk to a great extent.

USDA's crop condition report as of July 3, 2016 rate Georgia's corn crop as 69 percent good to excellent and 24 percent fair, the cotton crop is rated 67 percent good to excellent with 27 percent fair, the Georgia peanut crop is 74 percent good to excellent with 21 percent rated fair and soybeans are rated 64 percent good to excellent with 28 percent fair. The major row crops within the region are in good condition at the end of the second quarter.

Of course favorable conditions will be needed during the third quarter as well to complete a successful season with these major row crops. Corn acreage in Georgia is up 21 percent over 2015 with 400,000 acres planted. Cotton acreage is up 15 percent over last year with 1,300,000 acres planted. Peanuts are down slightly from 2015's high of 785,000 acres planted to 760,000 acres and soybean acreage is down 19 percent with 265,000 planted this year.

Blueberries continue to be a significant crop in the southeastern part of our territory and most growers appear to have had a good year with about 92 percent of the crop harvested at this time. Some early season high bush yields were hurt due to some pollination issues; however, the later season rabbit-eye varieties have produced excellent yields and prices have been about average throughout the season.

The yield and prices for the Vidalia sweet onion season has also been good. The market opened at around $18.00 per 40 lb. unit and dropped down to the $12.00 range during early June. Prices rebounded as of the end of June to the $16.00-$18.00 range. Current sales are coming out of cold storage inventories which were filled to capacity. The 2016 yield and market price should equate to a profitable year for most growers.

The forest products industry continues to be stable with improving economic conditions noted. Timber prices for southern yellow pine are presently $15-$20 per ton for pulpwood, $20-$25 per ton for chip-n-saw, and $26-$34 per ton for saw timber. These prices are down slightly from mid-year 2015 primarily due to drier conditions allowing access to a larger wood supply. Pine lumber prices have improved and reached $394 per thousand board feet as of June 2016. This is 21 percent above the January 2016 price and 16 percent above where it was in June 2015. Improvements in the housing market and increased housing starts appear to be pushing lumber prices higher. Saw mills and wood pellet mills in the region are operating profitably.

The poultry industry also continues to do well. Feed costs remain low and profits to integrators are strong. Some integrators within the region are increasing their number of broiler houses as well as adding new growers although it is a relatively slow expansion.

The dairy industry is experiencing low milk prices which have fallen approximately 35 percent from the highs of 2014. Current milk prices received by most dairies in the area is approximately $17.00 cwt. Margins have decreased, but low feed costs have kept profit margins from declining commensurate to the decline in milk prices. Increased production and global oversupply have depressed prices. Milk production in the United States is expected to hit 212.7 billion pounds this year. This is up 2 percent over 2015. Lower milk prices are expected to continue through 2016 as oversupply will remain for the near future.

Georgia's unemployment rate improved to 5.3 percent in May dropping from 5.5 percent in April of 2016. This is slightly higher than the national average of 4.9 percent although the national rate increased slightly during this same period. New businesses continue to find Georgia an attractive location given our infrastructure, workforce, and very active ports in Savannah and Brunswick.

The agricultural and rural land markets continue to improve and sales activity remains fairly strong in most counties. This increase in sales transactions increases loan demand and overall loan activity has been extremely good in 2016

South Carolina Region

Agriculture in the South Carolina region experienced extreme weather problems in 2015 in the form of drought and excess moisture within the growing season for the state. Fortunately, the weather conditions observed in 2016 have proven mostly positive. Timely rain has led to most row crops exhibiting fair to excellent production prospects at second quarter end. The only area of the state serviced by AgSouth lacking in moisture is the northwest corner of the state where rainfall has been lower than normal with pasture and hay crops primarily affected. During the second quarter, most row crop prices improved, which should enhance the potential profitability of many farms.

Given the flooding in 2015, there were two initiatives put into place in South Carolina during early 2016. *Plant it Forward South Carolina* was a private fundraising project designed to provide farmers grant money to cover losses related to seed costs on their farm. AgSouth contributed significantly to this project and substantial funds were distributed to approximately 530 farm entities throughout the state during the second quarter. On a much larger scale, the South Carolina General Assembly approved a $40 million South Carolina Farm Aid Bill proposed by several agricultural organizations in the state and led by the South Carolina Department of Agriculture. The process of applying for and distributing is underway at this time.

Poultry integrators serving the South Carolina region continue to do well. DHEC permitting issues continue to persist in some areas of the state. Some broiler producers are contemplating changes in their operations that could lead to producing some smaller broilers compared to the size birds presently grown. As this is considered and potentially implemented, the number of new poultry houses needed would likely be affected with less houses potentially required.

Beef cattle produced in the state continue to do well despite some drop in prices compared to the historical highs recognized over the past few years. Some cattle operations located in the upstate will be affected by the lack of late spring and early summer rain on grazing and hay, but most remain in satisfactory financial condition to deal with any adversity experienced.

Timber producers in the state continue to experience some improvement in pine pulpwood, pine sawtimber and hardwood pulpwood prices into the second quarter, while pine chip-n-saw and hardwood sawtimber prices contracted to some degree. The drier weather experienced in many areas of the state during the late spring and early summer has allowed for logging to improve to more typical levels after the extreme wet conditions last fall and winter, and many timberland owners have increased tree plantings. Tree plantings in many areas of the southeast had been delayed to gauge the timber markets. With many timberland owners now recognizing the markets will not likely return to pre-2008 levels, previously postponed harvest plans are now proceeding.

Through the beginning of the second quarter, both housing permits issued and housing starts have held steady at well above 1.1 million each. Residential construction has continued to improve with the end of the first quarter projecting an annualized pace for 2016 of $446 billion, which far exceeds the levels observed over at least the past five years. Lumber prices continue to trade in the range noted since 2013 of $357 to $396 per thousand board feet. Likewise, mortgage rates remain at low levels. These factors bode well for the southeastern timber markets for the foreseeable future.

Midway through the second quarter, South Carolina unemployment is tracking at 5.6 percent, which is above the national rate of 4.9 percent but below the unemployment rate of 5.9 reported for the second quarter of 2015. Recognizing the significant level of non-farm lending within the South Carolina region, the employment rate continues to be monitored closely.

ASSOCIATION BALANCE SHEET

The gross loan volume of the Association as of June 30, 2016, was $1,620,278, an increase of $62,397 or 4.01 percent as compared to $1,557,881 at December 31, 2015. Net loans outstanding at June 30, 2016 were $1,606,720 as compared to $1,544,782 at December 31, 2015. Net loans accounted for 94.78 percent of total assets at June 30, 2016, as compared to 93.56 percent of total assets at December 31, 2015.

The increase in gross loan volume during the reporting period is attributed to several large loans as well as new term loans and advances on operating lines of credit made during the reporting period. Competition for good, quality loans remains strong from some commercial banks, but the Association has remained competitive.

The Association typically structures loans to meet the needs of the borrower. Many term loans are made for ten years or less allowing the borrower to build equity faster and thus reducing the risk in the loan portfolio.

At December 31, 2015, the Association held Investment securities totaling $8,395. These investments are Rural America Bonds made under the authority for Mission Related Investments granted by the Farm Credit Administration. At June 30, 2016, investment securities totaled $8,229, a decrease of $166 from December 31, 2015. The 1.98 percent decrease is from payments made year to date in 2016.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level and credit administration remains satisfactory. Nonaccrual loans increased from $10,694 at December 31, 2015, to $13,474 at June 30, 2016. The balance of nonaccrual loans is increased by transfers to nonaccrual status offset by liquidations, loans returning to accrual status, or transfer of assets to other property owned. Association staff is working diligently to work out all nonaccrual debt situations, and additional transfers may occur as the economy remains sluggish.

As of the end of the second quarter of 2016 the Association had originated $66,395 in loans for the secondary market. Originations for the same period 2015 were $62,893. The 5.57 percent increase is the result of the increase in demand for home loans and refinances during the reporting period. As of June 30, 2016, the Association held $1,453 in qualifying loans for sale. At December 31, 2015, loans held for sale totaled $3,302.

Other property owned decreased to $4,905 at June 30, 2016 from $5,425 at December 31, 2015. The decrease of $520 or 9.59 percent in other property owned is the result of sales and write-downs of existing other property owned exceeding transfers to other property owned during the reporting period. The Association is actively marketing all properties for sale. For details, please visit our website at ***www.agsouthfc.com*** and click on *Property For Sale*.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at June 30, 2016, was $13,558 compared to $13,099 at December 31, 2015, and was considered by management to be adequate to cover possible losses. The increase in the allowance account is the result of an addition to the allowance for loan loss account exceeding any charge offs net of recoveries during the reporting period. The Asset/Liability Committee (ALCO) of the Association, which is comprised of members of senior management and staff assigned to special assets management, met in June to review the allowance account. The ALCO determined that an addition to the allowance account was needed at this time. The ALCO considered the general economic conditions, the potential for deterioration in the existing portfolio and the loan growth in the portfolio in determining the level of allowance.

Investments in other Farm Credit institutions increased from $22,145 at December 31, 2015 to $22,225 at June 30, 2016. The increase of $80 or less than one percent is the result of a slightly higher balance of receivables from other Farm Credit institutions related to participations sold on a patronage basis. This includes loans sold to CoBank.

Premises and equipment net increased $1,140 from $16,339 at December 31, 2015 to $17,479 at June 30, 2016. The increase of 6.98 percent is the result of the acquisition of a new office building in Carrollton, Georgia and new property in Statesboro, Georgia. The Association intends to relocate the Carrollton staff to the new facility after renovations are complete in late August. In Statesboro plans have begun to consolidate all Administrative staff into one location. A building adjacent to the current branch office was purchased in the second quarter to allow for some temporary offices while a new building is constructed. This project will take through the majority of 2017 to complete.

Accounts receivable decreased $12,725 from $19,565 at December 31, 2015 to $6,840 at June 30, 2016. The decrease is the result of the patronage distribution receivable at December 31, 2015 from AgFirst, which totaled $9,290 in regular distribution and $8,178 in a special distribution. As of June 30, 2016, this line item included only two quarters of accrual of patronage from AgFirst totaling $4,783.

Other assets decreased $2,588 from $11,599 at December 31, 2015 to $9,011 at June 30, 2016. The majority of other assets is made up of prepaid retirement expense which decreased $2,900 between December 31, 2015 and June 30, 2016.

On the liability side of the balance sheet, Notes payable to AgFirst Farm Credit Bank increased from $1,286,760 at December 31, 2015 to $1,342,275 at June 30, 2016. The $55,515 increase, or 4.31 percent, is tied to the higher amount of loans outstanding between the two reporting periods.

Accrued interest payable increased $81 or 2.82 percent from $2,870 to $2,951. The increase is tied to the higher notes payable balance outstanding.

Patronage refunds payable decreased $8,053 from $8,144 at December 31, 2015 to $91 at June 30, 2016. The decrease is the result of the estimated cash portion of the 2015 Patronage distribution on the Association's records at December 31, 2015 moving from Patronage refund payable to Other liabilities. This amount totaled $7,945 at December 31, 2015 compared to $188 at June 30, 2016.

Accounts payable increased $1,036 from $2,008 at December 31, 2015 to $3,044 at June 30, 2016. The 51.59 percent increase is due to the payable established to pay the insurance premiums on loans to the FCSIC and a payable established to resolve disputed claims. Please see *Note 8* for more details. At December 31, 2015, the payable related to the FCSIC totaled $1,458, and at June 30, 2016 the payable had been reduced to $922.

Other liabilities decreased $1,367 from $26,779 at December 31, 2015 to $25,412 at June 30, 2016. The 5.10 percent decrease is due to the liability established for the projected 2016 incentive payment of $1,474. At December 31, 2015 the projected incentive amount was $2,796.

Protected borrower stock did not change between the two reporting periods and remained at $2.

Unprotected borrower stock increased from $7,972 at December 31, 2015 to $8,246 at June 30, 2016. The increase of $274 or 3.44 percent is due to new borrowers purchasing stock during the reporting period in excess of liquidations of stock when loans pay out.

Allocated surplus decreased from $116,777 at December 31, 2015 to $98,644 at June 30, 2016. This is a decrease of $18,133 or 15.53 percent. The reduction is from the decision made by the Board of Directors to revolve the 2010 series of Allocated Surplus in late February 2016. The checks and notices for this revolvement were generated and mailed in early March 2016.

Unallocated surplus increased $14,542 or 7.26 percent. The balance of $214,922 at June 30, 2016 includes the retention of a portion of 2015 fiscal year end earnings and earnings year to date in 2016.

RESULTS OF OPERATIONS

For the three months ended June 30, 2016

Net income for the three months ended June 30, 2016, totaled $5,754 as compared to $8,042 for the same period in 2015. This is a decrease of $2,288 or 28.45 percent. The following commentary explains the variance.

At June 30, 2016, interest income increased $832 from $22,160 at June 30, 2015 to $22,992. This increase of 3.75 percent is primarily due to the increase in average earning assets between the two reporting periods. For the quarter ending June 30, 2015 the year to date average daily balance of interest earning assets was $1,472,061 compared to $1,565,093 for the same period in 2016. For the three months ending June 30, 2015, interest income on investments totaled $139 compared to $134 for the three months ended June 30, 2016. Nonaccrual income, which is included in interest income, was $105 for the three months ended June 30, 2016, as compared to $366 for the same period in 2015.

Interest expense for the three months ended June 30, 2016 increased $888 from $7,911 at June 30, 2015 to $8,799 at June 30, 2016. The variance is 11.22 percent and is tied to the increase in the average daily direct note balance between the two reporting periods. As of June 30, 2015, the average daily direct note was 1,202,487 compared to an average direct note balance of 1,282,509 as of June 30, 2016.

Net interest income before the provision for loan loss decreased $56 for the three months ended June 30, 2016, as compared to the same period in 2015 due primarily to the increased balance in the direct note.

Net interest income after the provision for loan losses decreased $603 during the quarter ending June 30, 2016. A provision of $435 was made in the quarter ending June 30, 2016. The provision was necessary to increase the general allowance. A portion of the provision is to increase the allowance on unfunded commitments which is booked to Other Liabilities. In the same period in 2015 a provision reversal of $112 was necessary. The 2015 entry was needed to decrease the general allowance and increase the Other Liability for undrawn loan commitment.

Noninterest income decreased $577 over the same period last year. Loan fees increased $62 or 7.64 percent. The loan fee variance can be tied to the increase in fees earned on loans sold on the secondary market and a slight increase in portfolio fee income.

Fees for financially related services increased $31 from $142 at June 30, 2015 compared to $173 at June 30, 2016. The increase of 21.83 percent is due to an increase in commissions earned on leasing services offered by the Association.

Patronage refunds from other Farm Credit institutions increased $404 from $2,655 at June 30, 2015 to $3,059 at June 30, 2016. The increase of 15.22 percent is the result of the increase in loans sold to CoBank and AgFirst on a patronage basis.

Gains on the sale of rural home loans increased $42 from $521 at June 30, 2015 compared to $563 at June 30, 2016. Increased originations and the yield premiums between the two reporting periods increased resulting in the gains. Demand for home loans has improved due to the low interest rate environment and an increase in the new construction market during the reporting period.

Gains on the sale of premises and equipment for the period ending June 30, 2016 totaled $244 compared to $15 for the period ending June 30, 2015. During the 2016 reporting period, the Association recorded a gain on the sale of the Carrollton, Georgia office building. A new building has been purchased for Carrollton and is undergoing some renovations with an anticipated relocation by the end of August.

Losses on the sale of other transactions totaled $1,435 at June 30, 2016. This is an increase of $1,332 over a loss of $103 in the same period in 2015. In June 2016 the Association established a liability of $1,500 and offsetting loss to resolve disputed claims. See *Note* 8 for additional information. The loss was offset by gains on investments in the Rabbi Trust for some current employees and retirees.

Other noninterest income was $31 during the three months ended June 30, 2016, compared to $44 for the three months ending June 30, 2015. This line item captures the volume premium paid by AgFirst for secondary market loans sold to AgFirst. The volume premiums were slightly lower in 2016 when compared to 2015.

Noninterest expense for the three months ended June 30, 2016, increased $1,106 or 10.63 percent when compared to the same period of 2015. Salaries and employee benefits expense increased $700 between the two reporting periods. The increase in salaries and employee benefits is due to the accrual of incentive based upon Association results at June 30, 2016. The Association Incentive Plan includes several key components and is measured on a monthly basis. Using the May 2016 results the Asset/Liability Committee recommended to the board the accrual of a portion of the incentive totaling $1,473. The plan will be monitored continually throughout the year with payment occurring in January 2017 provided that performance continues to be met according to the plan.

Occupancy and equipment expense at June 30, 2016 was $533 compared to $495 for the same period in 2015. This is an increase of $38 or 7.68 percent. The increase is tied to items expensed rather than depreciated over the life of the assets.

The Insurance Fund premiums increased $115 from $358 at June 30, 2015 to $473 at June 30, 2016. The variance is due to the higher premium on accruing loans assessed in 2016 by the Insurance Fund and a higher balance of accruing loans outstanding. The FCSIC board recently announced an increase in the premium from 16 basis points to 18 basis points on accruing volume for the remaining six months of 2016.

In the three months ending June 30, 2016, the Association experienced losses and expenses on the sale of Other Property Owned in the amount of $204. During the same period of 2015, the Association booked losses and expenses on the sale of Other Property Owned of $68. The losses in the 2016 reporting period were write-downs on several pieces of Other Property Owned held by the Association as well as losses recorded at the time of the sale. Some pieces are under contract for less than the current carrying value, while other write-downs were needed due to new appraisals.

Other operating expenses increased $117 from $1,615 at June 30, 2015, compared to $1,732 at June 30, 2016. The increase of 7.24 percent is attributed to an increase in purchased services, advertising and public and member relations expenses between the reporting periods. The Farm Credit System is celebrating its 100th year and the Association has been actively advertising and promoting the centennial celebration. Other operating expenses also include communications, data processing, and all other expenses necessary to run the business.

For the six months ended June 30, 2016

Net income for the six months ended June 30, 2016, totaled $14,514 as compared to $15,890 for the same period in 2015. This is a decrease of $1,376 or 8.66 percent. The following narrative will explain the variance.

At June 30, 2016, interest income increased $1,910 compared to the same period in 2015. The increase was due to the amount of interest income earned on loans. Interest income on loans increased $1,919. The increase is tied to the increase in accruing loan volume between the reporting periods. Nonaccrual income, which is included in interest income, was $309 for the six months ended June 30, 2016, as compared to $594 for the same period in 2015. The decrease of $285 is the result of a decrease in the recognition of interest income when nonaccrual loans pay off or pay down.

Interest expense increased $1,745 for the six months ended June 30, 2016. The increase is attributable to the higher direct note balance between the reporting periods.

Net interest income before the provision for loan loss increased $165 or less than one percent for the six months ended June 30, 2016 as compared to the same period in 2015 primarily due to the increase in loan volume. Net interest income after the provision for loan losses decreased $294 in the period ending June 30, 2016.

The provision for loan loss amount in the 2016 reporting period totaled $341 and there was a provision reversal in the 2015 reporting period of $118. In June 2016, the Association's ALCO made the decision that the allowance account required an increase, therefore, the small provision was booked. An adjustment to Other Liabilities was also needed to cover the allowance for loss on unfunded commitment balances. These decisions were made after analyzing the risk in the current portfolio. The ALCO analysis included reviewing historical trends, loan size, loan performance and credit quality reports.

Noninterest income increased $109 over the same period last year. Loan fees increased $117 or 7.86 percent. In the first six months of 2016, fees earned on loans sold in the secondary market have been significantly higher than the same period in 2015. The volume of loans sold increased between the two reporting periods due to the new construction market. Loan fees on portfolio activity also increased during the reporting period.

Fees for financially related services increased $66 from $391 at June 30, 2015 compared to $457 at June 30, 2016. The 16.88 percent increase in fees for financially related services is the result of an increase in fee income earned on the sale of multi-peril crop insurance and lease commissions.

The patronage refunds from other Farm Credit institutions increased $1,040 from $5,498 at June 30, 2015 to $6,538 at June 30, 2016. The increase is due to the higher amount of patronage earned on loans sold to AgFirst and CoBank and the higher direct note balance between the reporting periods.

Gains on the sale of rural home loans increased $59 from $935 at June 30, 2015 to $994 at June 30, 2016. Gains increased due to the increase in loan originations sold on the secondary market between the reporting periods.

Gains on the sale of premises and equipment increased $221 from $37 for the period ending June 30, 2015 to $258 at June 30, 2016. The gains were recorded when Association automobiles were replaced and from the sale of the Carrollton, Georgia office building. A new building in Carrollton on Highway 27 is currently being renovated and the staff will move to the new location by the end of August.

Losses on other transactions totaled $1,552 for the six months ended June 30, 2016 compared to a loss of $166 for the same period in 2015. The loss recorded in the 2016 reporting period is related to a liability and offsetting loss established for disputed claims. Please reference *Note 8* for additional information. The loss recorded in 2015 was the result of the need to establish a contingent liability for undrawn commitment loans.

Other noninterest income decreased $8 from $61 at June 30, 2015 compared to $53 at June 30, 2016. The variance of 13.11 percent is due to volume premiums paid by AgFirst for secondary market activity. In 2015, the Association earned $25 in volume premiums and for the period ending June 30, 2016, the Association has earned $16 in volume premiums.

Noninterest expense for the six months ended June 30, 2016, increased $1,190 compared to the same period of 2015. Salaries and employee benefit expense increased $400 between the two reporting periods. The 2.64 percent increase in salaries and employee benefits is tied to the increase in health care expense and an overall increase in the number of employees between the two reporting periods. The Association has a significant number of employees eligible to retire and has, in some cases, hired replacements to begin the training and transition process.

Additionally, the Association booked an accrual for the 2016 incentive payment based upon plan results which is included in salary and benefit expense. The Association evaluated 2016 performance measures for incentive purposes and determined that some employees could earn incentive in 2016. Based upon this information, the Association accrued $1,473 in incentive in June 2016. Association results will be re-evaluated prior to the end of the fourth quarter 2016 to determine if an additional accrual is warranted.

Occupancy and equipment expense at June 30, 2016 was $1,226 compared to $1,193 for the same period in 2015. The increase is from the normal cost of operations and some timing differences of expenses. Also, the Association has purchased additional property in Statesboro, Georgia to construct additional office space.

The Insurance Fund premium increased from $703 at June 30, 2015 to $922 at June 30, 2016. The increase of 31.15 percent is tied to the increase in the premium on loans in accrual and an increase in loan volume.

Losses on the sale or write down of other property owned totaled $244 for the six months ending June 30, 2016. When compared to the same period in 2015, losses on other property owned totaled $75. The losses or write downs were required after new contracts, sale closings, and/or new appraisals were obtained and the book value needed to more accurately reflect the current market value. Other property owned activity has increased over the past few months.

Other operating expenses increased $369 from $3,456 at June 30, 2015, compared to $3,825 at June 30, 2016. The increase is primarily an increase in purchased services expenses, and some additional expenses for advertising and public and member relations.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (the Bank) through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances the funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at June 30, 2016 was $1,342,275 as compared to $1,286,760 at December 31, 2015. The increase in the notes payable correlates to the increase in gross loans during the reporting period.

CAPITAL RESOURCES

Total members' equity at December 31, 2015 totaled $324,619. At June 30, 2016 total members' equity had decreased by $3,243 to $321,376. The decrease in total members' equity is due to the decrease in allocated retained earnings offset by an increase in unallocated retained earnings between the two reporting periods. At December 31, 2015, allocated retained earnings totaled $116,777 compared to $98,644 at June 30, 2016. The decrease is due to the revolvement of the 2010 series of allocated surplus in the first quarter of 2016. At December 31, 2015, unallocated retained earnings totaled $200,380. At June 30, 2016, the unallocated retained earnings had increased to $214,922. The increase in unallocated retained earnings is due to the decision to retain earnings from 2015 earnings for capital purposes and year to date earnings.

Total capital stock and participation certificates were $8,248 on June 30, 2016, compared to $7,974 on December 31, 2015. The increase is attributed to the purchase of new stock and participation certificates for new borrowing entities offset by the retirement of stock and participation certificates on loans liquidated in the normal course of business.

FCA regulations require all Farm Credit Institutions to maintain minimum permanent capital, total surplus, and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus, and core surplus, as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2016, the Association's total surplus ratio and core surplus ratio were 19.46 percent and 15.47 percent, respectively, and the permanent capital ratio was 20.00 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

The Association has a portion of the portfolio in an in-portfolio guarantee program with Farmer Mac. The purpose of these guarantees is to improve the Association's capital position. At June 30, 2016, the Association had loans totaling $10,943 in this program. The cost of the guarantees year to date was $31. The use of the Farmer Mac in-portfolio guarantees had a positive effect on the Association's capital ratios.

At the present time, the Association's capital position remains strong and well above regulatory minimums. At December 31, 2015, the Association's permanent capital ratio was 20.68 percent. The decrease to 20.00 percent permanent capital at June 30, 2016 is the result of the growth in the Association's portfolio. The Association continues to utilize various loan guarantee programs, including FSA, SBA and Farmer Mac to offset risk and improve the capital position. The Association has other tools available to strengthen the capital position. These options include selling additional loans to AgFirst and others, placing additional pools of loans with Farmer Mac in the in-portfolio guarantee program, and participating with AgFirst in a capitalized participation pool. Should additional measures be needed to improve the Association's capital ratios, Association management will study all options and make a recommendation to the Board for consideration.

REGULATORY MATTERS

On March 10, 2016, the FCA adopted a final regulation to modify the regulatory capital requirements for System banks and associations. The stated objectives of the rule are as follows:

- To modernize capital requirements while ensuring that institutions continue to hold sufficient regulatory capital to fulfill their mission as a government-sponsored enterprise,
- To ensure that the System's capital requirements are comparable to the Basel III framework and the standardized approach that the federal banking regulatory agencies have adopted, but also to ensure that the rules recognize the cooperative structure and the organization of the System,
- To make System regulatory capital requirements more transparent, and
- To meet the requirements of section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).

The final rule will replace existing core surplus and total surplus requirements with Common Equity Tier 1, Tier 1 and Total Capital risk-based capital ratio requirements. The final rule will also replace the existing net collateral ratio with a Tier 1 Leverage ratio and is applicable to all banks and associations. The Permanent Capital Ratio will remain in effect with the final rule. The following sets forth the new regulatory capital ratios:

Ratio	Primary Components of Numerator	Denominator	Minimum Requirement	Minimum Requirement with Conservation Buffer
Common Equity Tier 1 (CET1) Capital	Unallocated retained earnings/surplus (URE), Common Stock (subject to certain conditions)	Risk-weighted assets	4.5%	7.0%
Tier 1 Capital	CET1 Capital, Non-cumulative perpetual preferred stock	Risk-weighted assets	6.0%	8.5%
Total Capital	Tier 1 Capital, Allowance for Loan Losses, other equity securities not included in Tier 1 Capital	Risk-weighted assets	8.0%	10.5%
Tier 1 Leverage	Tier 1 Capital (1.5% must be URE or URE equivalents)	Total assets	4.0%	5.0%

On July 28, 2016, the FCA published the final regulation in the Federal Register, and it is anticipated that the effective date of the new capital requirements will be January 1, 2017, with a three-year phase-in of the capital conservation buffer applied to the risk-adjusted capital ratios. District institutions are well-positioned to be in compliance with the new requirements at adoption.

On November 30, 2015, the FCA, along with four other federal agencies, published in the Federal Register a final rule to establish capital and margin requirements for covered swap entities as required by the Dodd-Frank Act. See below for further information regarding the Dodd-Frank Act.

On July 25, 2014, the FCA published a proposed rule in the Federal Register to revise the requirements governing the eligibility of investments for System banks and associations. The public comment period ended on October 23, 2014. The FCA expects to issue a final regulation in 2016. The stated objectives of the proposed rule are as follows:

- To strengthen the safety and soundness of System banks and associations,
- To ensure that System banks hold sufficient liquidity to continue operations and pay maturing obligations in the event of market disruption,
- To enhance the ability of the System banks to supply credit to agricultural and aquatic producers,
- To comply with the requirements of section 939A of the Dodd-Frank Act,
- To modernize the investment eligibility criteria for System banks, and
- To revise the investment regulation for System associations to improve their investment management practices so they are more resilient to risk.

Other Matters

The Board of Directors has established a CEO Search Committee as CEO Bill Spigener has announced his intent to retire in March 2017.

FINANCIAL REGULATORY REFORM

See discussion of the Dodd-Frank Act in the Financial Regulatory Reform section of the Association's 2015 Annual Report.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1, *"Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements",* in the Notes to the Financial Statements, and the 2015 Annual Report to Shareholders for recently issued accounting pronouncements.

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NOTE: Shareholder investment in the 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, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, ***www.agfirst.com***. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-310-4805, ext. 6737, writing Alisa D. Gunter, CFO, AgSouth Farm Credit, ACA, PO Box 4966, Spartanburg, SC 29305, or accessing the website ***www.agsouthfc.com***. The Association prepares an electronic version of the Annual Report which is available on the Association's web site within 75 days after the end of the fiscal year and distributes the Annual report to Shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

AgSouth Farm Credit, ACA

Consolidated Balance Sheets

(dollars in thousands)	June 30, 2016 *(unaudited)*	December 31, 2015 *(audited)*
Assets		
Cash	**$ 3,633**	$ 4,191
Investment securities:		
Held to maturity (fair value of $8,467 and $8,265, respectively)	**8,229**	8,395
Loans	**1,620,278**	1,557,881
Allowance for loan losses	**(13,558)**	(13,099)
Net loans	**1,606,720**	1,544,782
Loans held for sale	**1,453**	3,302
Accrued interest receivable	**14,654**	15,437
Investments in other Farm Credit institutions	**22,225**	22,145
Premises and equipment, net	**17,479**	16,339
Other property owned	**4,905**	5,425
Accounts receivable	**6,840**	19,565
Other assets	**9,011**	11,599
Total assets	**$ 1,695,149**	$ 1,651,180
Liabilities		
Notes payable to AgFirst Farm Credit Bank	**$ 1,342,275**	$ 1,286,760
Accrued interest payable	**2,951**	2,870
Patronage refunds payable	**91**	8,144
Accounts payable	**3,044**	2,008
Other liabilities	**25,412**	26,779
Total liabilities	**1,373,773**	1,326,561
Commitments and contingencies (Note 8)		
Members' Equity		
Protected borrower stock	**2**	2
Capital stock and participation certificates	**8,246**	7,972
Retained earnings		
Allocated	**98,644**	116,777
Unallocated	**214,922**	200,380
Accumulated other comprehensive income (loss)	**(438)**	(512)
Total members' equity	**321,376**	324,619
Total liabilities and members' equity	**$ 1,695,149**	$ 1,651,180

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

AgSouth Farm Credit, ACA

Consolidated Statements of Income

(unaudited)

(dollars in thousands)	For the three months ended June 30, 2016	For the three months ended June 30, 2015	For the six months ended June 30, 2016	For the six months ended June 30, 2015
Interest Income				
Loans	**$ 22,858**	$ 22,021	**$ 45,222**	$ 43,303
Investments	**134**	139	**269**	278
Total interest income	**22,992**	22,160	**45,491**	43,581
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	**8,765**	7,855	**17,129**	15,411
Other	**34**	56	**113**	86
Total interest expense	**8,799**	7,911	**17,242**	15,497
Net interest income	**14,193**	14,249	**28,249**	28,084
Provision for (reversal of allowance for) loan losses	**435**	(112)	**341**	(118)
Net interest income after provision for (reversal of allowance for) loan losses	**13,758**	14,361	**27,908**	28,202
Noninterest Income				
Loan fees	**873**	811	**1,606**	1,489
Fees for financially related services	**173**	142	**457**	391
Patronage refunds from other Farm Credit institutions	**3,059**	2,655	**6,538**	5,498
Gains (losses) on sales of rural home loans, net	**563**	521	**994**	935
Gains (losses) on sales of premises and equipment, net	**244**	15	**258**	37
Gains (losses) on other transactions	**(1,435)**	(103)	**(1,552)**	(166)
Other noninterest income	**31**	44	**53**	61
Total noninterest income	**3,508**	4,085	**8,354**	8,245
Noninterest Expense				
Salaries and employee benefits	**8,568**	7,868	**15,524**	15,124
Occupancy and equipment	**533**	495	**1,226**	1,193
Insurance Fund premiums	**473**	358	**922**	703
(Gains) losses on other property owned, net	**204**	68	**244**	75
Other operating expenses	**1,732**	1,615	**3,825**	3,456
Total noninterest expense	**11,510**	10,404	**21,741**	20,551
Income before income taxes	**5,756**	8,042	**14,521**	15,896
Provision for income taxes	**2**	—	**7**	6
Net income	**$ 5,754**	$ 8,042	**$ 14,514**	$ 15,890

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

AgSouth Farm Credit, ACA

Consolidated Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the three months ended June 30, 2016	For the three months ended June 30, 2015	For the six months ended June 30, 2016	For the six months ended June 30, 2015
Net income	**$ 5,754**	$ 8,042	**$ 14,514**	$ 15,890
Other comprehensive income net of tax				
Employee benefit plans adjustments	**37**	28	**74**	55
Comprehensive income	**$ 5,791**	$ 8,070	**$ 14,588**	$ 15,945

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

AgSouth Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)	Protected Borrower Stock	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2014	$ 3	$ 7,527	$ 112,635	$187,002	$ (530)	$ 306,637
Comprehensive income				15,890	55	15,945
Capital stock/participation certificates issued/(retired), net		219				219
Retained earnings retired			(14,347)			(14,347)
Balance at June 30, 2015	$ 3	$ 7,746	$ 98,288	$202,892	$ (475)	$ 308,454
Balance at December 31, 2015	$ 2	$ 7,972	$ 116,777	$200,380	$ (512)	$ 324,619
Comprehensive income				**14,514**	**74**	**14,588**
Capital stock/participation certificates issued/(retired), net		**274**				**274**
Retained earnings retired			**(18,113)**			**(18,113)**
Patronage distribution adjustment			**(20)**	**28**		**8**
Balance at June 30, 2016	**$ 2**	**$ 8,246**	**$ 98,644**	**$214,922**	**$ (438)**	**$ 321,376**

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

AgSouth Farm Credit, ACA

Notes to the Consolidated Financial Statements

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

Note 1 — Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements

Organization

The accompanying financial statements include the accounts of AgSouth Farm Credit, ACA and its Production Credit Association (PCA) and Federal Land Credit Association (FLCA) subsidiaries (collectively, the Association). A description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations for the Association as of and for the year ended December 31, 2015, are contained in the 2015 Annual Report to Shareholders. These unaudited interim consolidated financial statements should be read in conjunction with the latest Annual Report to Shareholders.

Basis of Presentation

In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary for a fair statement of results for the periods presented. These adjustments are of a normal recurring nature, unless otherwise disclosed.

Certain amounts in the prior period's consolidated financial statements have been reclassified to conform to the current period presentation. Such reclassifications had no effect on the prior period net income or total capital as previously reported.

The results of any interim period are not necessarily indicative of those to be expected for a full year.

Significant Accounting Policies

The Association's accounting and reporting policies conform with U.S. generally accepted accounting principles (GAAP) and practices in the financial services industry. To prepare the financial statements in conformity with GAAP, management must make estimates based on assumptions about future economic and market conditions (for example, unemployment, market liquidity, real estate prices, etc.) that affect the reported amounts of assets and liabilities at the date of the financial statements, income and expenses during the reporting period, and the related disclosures. Although these estimates contemplate current conditions and expectations of change in the future, it is reasonably possible that actual conditions may be different than anticipated, which could materially affect results of operations and financial condition.

Management has made significant estimates in several areas, including loans and allowance for loan losses (Note 2, *Loans and Allowance for Loan Losses*), investment securities and other-than-temporary impairment (Note 3, *Investments*), and financial instruments (Note 6, *Fair Value Measurement*). Actual results could differ from those estimates.

For further details of significant accounting policies, see Note 2, *Summary of Significant Accounting Policies*, from the latest Annual Report.

Accounting Standards Updates (ASUs) Issued During the Period

The following ASUs were issued by the Financial Accounting Standards Board (FASB) since the most recent Annual Report:

- In June, 2016, the FASB issued ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The Update improves financial reporting by requiring timelier recording of credit losses on financial instruments. It requires an organization to measure all expected credit losses for financial assets held at the reporting date. Financial institutions and other organizations will use forward-looking information to better estimate their credit losses. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. The ASU requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The Update will take effect for U.S. Securities and Exchange Commission (SEC) filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. For public companies that are not SEC filers, it will take effect for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. For all other organizations, the ASU will take effect for fiscal years beginning after December 15, 2020, and for interim periods within fiscal years beginning after December 15, 2021. Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018.

- In May, 2016, the FASB issued ASU 2016-12 Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients. The guidance addresses certain issues identified by the Transition Resource Group (TRG) in the guidance on assessing collectibility, presentation of sales taxes, noncash consideration, and completed contracts and contract modifications at transition. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements for Topic 606 (and any other Topic amended by Update 2014-09).

- In April, 2016, the FASB issued ASU 2016-10 Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing. The Update clarifies the following two aspects of Topic 606: identifying performance obligations and the licensing implementation guidance, while retaining the related principles for those areas. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements for Topic 606 (and any other Topic amended by Update 2014-09).

- In March, 2016, the FASB issued ASU 2016-08 Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net). The amendments clarify the implementation guidance on principal versus agent considerations. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements for Topic 606 (and any other Topic amended by Update 2014-09).

- In March, 2016, the FASB issued ASU 2016-07 Investments Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting. To simplify the accounting for equity method investments, the amendments in the Update eliminate the requirement that an entity retroactively adopt the equity method of accounting if an investment qualifies for use of the equity method as a result of an increase in the level of ownership or degree of influence. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. The guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. Earlier application is permitted. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method.

ASUs Pending Effective Date

For a detailed description of the ASUs below, see the latest Annual Report.

Potential effects of ASUs issued in previous periods:

- 2016-02 Leases (Topic 842): In February, 2016, the FASB issued an update that requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

- 2016-01 Financial Instruments – Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities: In January, 2016, the FASB issued an update that is intended to improve the recognition and measurement of financial instruments. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

- 2015-14 Revenue from Contracts with Customers (Topic 606) – Deferral of the Effective Date: In August, 2015, the FASB issued an update that defers by one year the effective date of ASU 2014-09, Revenue from Contracts with Customers. The new ASU reflects decisions reached by the FASB at its meeting on July 9, 2015. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

Accounting Standards Effective During the Period

There were no changes in the accounting principles applied from the latest Annual Report, other than any discussed below.

No recently adopted accounting guidance issued by the FASB had a significant effect on the current period reporting. See the most recent Annual Report for a detailed description of each of the standards below:

- 2015-07 Fair Value Measurement (Topic 820): Disclosure for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent) – The amendment was adopted prospectively. There were no changes to the Association's statements of financial condition or results of operations as a result of this guidance. See Note 6, *Fair Value Measurement*, for the disclosures required by this guidance.

- 2015-01 Income Statement – Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items – The amendment was adopted retrospectively. There were no changes to the

Association's statements of financial condition or results of operations as a result of this guidance.

- 2014-15 Income Statement – Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern: This amendment is effective for the annual reporting period ended December 31, 2016 and interim and annual periods thereafter. It may require additional disclosures but will not have a material impact on the Association's financial condition or results of operations.

Note 2 — Loans and Allowance for Loan Losses

The Association maintains an allowance for loan losses 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 Association has been identified. See Note 3, *Loans and Allowance for Loan Losses*, from the latest Annual Report for further discussion.

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

A summary of loans outstanding at period end follows:

	June 30, 2016	December 31, 2015
Real estate mortgage	$ 1,265,688	$ 1,240,201
Production and intermediate-term	282,439	253,321
Processing and marketing	9,374	4,644
Farm-related business	9,841	6,344
Rural residential real estate	50,627	50,996
Other (including Mission Related)	2,309	2,375
Total Loans	$ 1,620,278	$ 1,557,881

A substantial portion of the Association's lending activities is collateralized, and exposure to credit loss associated with lending activities is reduced accordingly.

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with Farm Credit Administration (FCA) regulations. The following tables present the principal balance of participation loans at periods ended:

June 30, 2016	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ –	$ 230,834	$ –	$ 20,029	$ –	$ –	$ –	$ 250,863
Production and intermediate-term	–	89,522	1,023	1,949	1,906	–	2,929	91,471
Processing and marketing	–	8,683	–	43,519	–	–	–	52,202
Farm-related business	–	7,500	–	11,250	–	–	–	18,750
Total	$ –	$ 336,539	$ 1,023	$ 76,747	$ 1,906	$ –	$ 2,929	$ 413,286

December 31, 2015	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ –	$ 213,860	$ –	$ 12,453	$ –	$ –	$ –	$ 226,313
Production and intermediate-term	–	28,463	1,137	3,446	2,202	–	3,339	31,909
Processing and marketing	–	9,463	–	14,243	–	–	–	23,706
Farm-related business	–	6,875	–	6,975	–	–	–	13,850
Total	$ –	$ 258,661	$ 1,137	$ 37,117	$ 2,202	$ –	$ 3,339	$ 295,778

A significant source of liquidity for the Association is the repayments of loans. The following table presents the contractual maturity distribution of loans by loan type at the latest period end:

	June 30, 2016			
	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 59,782	$ 249,231	$ 956,675	$ 1,265,688
Production and intermediate-term	145,989	94,158	42,292	282,439
Processing and marketing	2,276	3,053	4,045	9,374
Farm-related business	1,587	5,312	2,942	9,841
Rural residential real estate	5,443	2,034	43,150	50,627
Other (including Mission Related)	918	888	503	2,309
Total Loans	$ 215,995	$ 354,676	$ 1,049,607	$ 1,620,278
Percentage	13.33%	21.89%	64.78%	100.00%

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

The following table shows the recorded investment of loans, classified under the FCA Uniform Loan Classification System, as a percentage of the recorded investment of total loans by loan type as of:

	June 30, 2016	December 31, 2015
Real estate mortgage:		
Acceptable	96.51%	95.76%
OAEM	1.55	2.25
Substandard/doubtful/loss	1.94	1.99
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	96.54%	97.66%
OAEM	1.88	1.23
Substandard/doubtful/loss	1.58	1.11
	100.00%	100.00%
Processing and marketing:		
Acceptable	95.78%	100.00%
OAEM	4.22	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Farm-related business:		
Acceptable	97.86%	100.00%
OAEM	2.02	–
Substandard/doubtful/loss	0.12	–
	100.00%	100.00%

	June 30, 2016	December 31, 2015
Rural residential real estate:		
Acceptable	97.73%	96.49%
OAEM	1.58	1.92
Substandard/doubtful/loss	0.69	1.59
	100.00%	100.00%
Other (including Mission Related):		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Total Loans:		
Acceptable	96.56%	96.13%
OAEM	1.63	2.06
Substandard/doubtful/loss	1.81	1.81
	100.00%	100.00%

The following tables provide an age analysis of the recorded investment of past due loans as of:

	June 30, 2016					
	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
Real estate mortgage	$ 9,170	$ 5,409	$ 14,579	$ 1,261,875	$ 1,276,454	$ –
Production and intermediate-term	1,579	1,040	2,619	283,318	285,937	–
Processing and marketing	–	–	–	9,441	9,441	–
Farm-related business	247	12	259	9,611	9,870	–
Rural residential real estate	632	31	663	50,192	50,855	–
Other (including Mission Related)	–	–	–	2,331	2,331	–
Total	$ 11,628	$ 6,492	$ 18,120	$ 1,616,768	$ 1,634,888	$ –

	December 31, 2015					
	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
Real estate mortgage	$ 8,106	$ 3,995	$ 12,101	$ 1,239,130	$ 1,251,231	$ –
Production and intermediate-term	1,534	621	2,155	255,306	257,461	–
Processing and marketing	–	–	–	4,657	4,657	–
Farm-related business	–	–	–	6,360	6,360	–
Rural residential real estate	492	131	623	50,546	51,169	–
Other (including Mission Related)	–	–	–	2,394	2,394	–
Total	$ 10,132	$ 4,747	$ 14,879	$ 1,558,393	$ 1,573,272	$ –

Nonperforming assets (including the recorded investment for loans) and related credit quality statistics at period end were as follows:

	June 30, 2016	December 31, 2015
Nonaccrual loans:		
Real estate mortgage	$ 10,956	$ 8,266
Production and intermediate-term	2,363	2,048
Farm-related business	12	–
Rural residential real estate	143	379
Total	$ 13,474	$ 10,693
Accruing restructured loans:		
Real estate mortgage	$ 7,481	$ 8,164
Production and intermediate-term	1,094	1,049
Rural residential real estate	376	446
Total	$ 8,951	$ 9,659
Accruing loans 90 days or more past due:		
Total	$ –	$ –
Total nonperforming loans	$ 22,425	$ 20,352
Other property owned	4,905	5,425
Total	$ 27,330	$ 25,777
Nonaccrual loans as a percentage of total loans	0.83%	0.69%
Nonperforming assets as a percentage of total loans and other property owned	1.68%	1.65%
Nonperforming assets as a percentage of capital	8.50%	7.94%

The following table presents information related to the recorded investment of impaired loans at period end. 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.

	June 30, 2016	December 31, 2015
Impaired nonaccrual loans:		
Current as to principal and interest	$ 5,178	$ 4,614
Past due	8,296	6,079
Total	13,474	10,693
Impaired accrual loans:		
Restructured	8,951	9,659
90 days or more past due	–	–
Total	8,951	9,659
Total impaired loans	$ 22,425	$ 20,352
Additional commitments to lend	$ –	$ –

The following tables present additional impaired loan information at period end. Unpaid principal balance represents the contractual principal balance of the loan.

	June 30, 2016			Quarter Ended June 30, 2016		Six Months Ended June 30, 2016	
Impaired loans:	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**
With a related allowance for credit losses:							
Real estate mortgage	$ –	$ –	$ –	$ –	$ –	$ –	$ –
Production and intermediate-term	11	11	1	11	–	11	–
Farm-related business	–	–	–	–	–	–	–
Rural residential real estate	–	–	–	–	–	–	–
Total	$ 11	$ 11	$ 1	$ 11	$ –	$ 11	$ –
With no related allowance for credit losses:							
Real estate mortgage	$ 18,437	$ 20,265	$ –	$ 19,715	$ 174	$ 19,033	$ 428
Production and intermediate-term	3,446	4,988	–	3,686	33	3,558	80
Farm-related business	12	30	–	12	–	12	–
Rural residential real estate	519	548	–	554	5	535	12
Total	$ 22,414	$ 25,831	$ –	$ 23,967	$ 212	$ 23,138	$ 520
Total:							
Real estate mortgage	$ 18,437	$ 20,265	$ –	$ 19,715	$ 174	$ 19,033	$ 428
Production and intermediate-term	3,457	4,999	1	3,697	33	3,569	80
Farm-related business	12	30	–	12	–	12	–
Rural residential real estate	519	548	–	554	5	535	12
Total	$ 22,425	$ 25,842	$ 1	$ 23,978	$ 212	$ 23,149	$ 520

	December 31, 2015			Year Ended December 31, 2015	
Impaired loans:	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**	**Average Impaired Loans**	**Interest Income Recognized on Impaired Loans**
With a related allowance for credit losses:					
Real estate mortgage	$ –	$ –	$ –	$ –	$ –
Production and intermediate-term	15	16	1	16	1
Rural residential real estate	–	–	–	–	–
Total	$ 15	$ 16	$ 1	$ 16	$ 1
With no related allowance for credit losses:					
Real estate mortgage	$ 16,431	$ 19,314	$ –	$ 17,814	$ 940
Production and intermediate-term	3,082	3,533	–	3,341	176
Rural residential real estate	824	976	–	895	47
Total	$ 20,337	$ 23,823	$ –	$ 22,050	$ 1,163
Total:					
Real estate mortgage	$ 16,431	$ 19,314	$ –	$ 17,814	$ 940
Production and intermediate-term	3,097	3,549	1	3,357	177
Rural residential real estate	824	976	–	895	47
Total	$ 20,352	$ 23,839	$ 1	$ 22,066	$ 1,164

A summary of changes in the allowance for loan losses and recorded investment in loans for each reporting period follows. Prior to issuance of the Association's 2015 Annual Report, management identified errors in classification of the loan portfolio among the various FCA loan type categories that are used to report disaggregated loan information in footnote disclosures. As discussed in Note 3, *Loans and Allowance for Loan Losses*, of the Association's 2015 Annual Report, FCA loan type classifications prior to December 31, 2015 have been revised as necessary to reflect these loan type classifications, as adjusted. In the table below, activity for the quarter and six months ended June 30, 2015 is presented as revised.

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Rural Residential Real Estate	Other (including Mission Related)	Total
Activity related to the allowance for credit losses:						
Balance at March 31, 2016	$ 10,585	$ 1,915	$ 94	$ 421	$ 20	$ 13,035
Charge-offs	(29)	(11)	–	–	–	(40)
Recoveries	48	74	1	–	5	128
Provision for loan losses	(32)	403	67	2	(5)	435
Balance at June 30, 2016	$ 10,572	$ 2,381	$ 162	$ 423	$ 20	$ 13,558
Balance at December 31, 2015	$ 10,369	$ 2,177	$ 92	$ 423	$ 38	$ 13,099
Charge-offs	(78)	(36)	–	–	–	(114)
Recoveries	104	116	2	–	10	232
Provision for loan losses	177	124	68	–	(28)	341
Balance at June 30, 2016	$ 10,572	$ 2,381	$ 162	$ 423	$ 20	$ 13,558
Balance at March 31, 2015	$ 9,929	$ 1,817	$ 76	$ 354	$ 36	$ 12,212
Charge-offs	(67)	–	–	–	–	(67)
Recoveries	313	69	3	1	5	391
Provision for loan losses	(146)	69	(9)	(19)	(7)	(112)
Balance at June 30, 2015	$ 10,029	$ 1,955	$ 70	$ 336	$ 34	$ 12,424
Balance at December 31, 2014	$ 9,916	$ 1,957	$ 89	$ 358	$ 37	$ 12,357
Charge-offs	(175)	(90)	–	–	–	(265)
Recoveries	356	79	4	1	10	450
Provision for loan losses	(68)	9	(23)	(23)	(13)	(118)
Balance at June 30, 2015	$ 10,029	$ 1,955	$ 70	$ 336	$ 34	$ 12,424
Allowance on loans evaluated for impairment:						
Individually	$ –	$ 1	$ –	$ –	$ –	$ 1
Collectively	10,572	2,380	162	423	20	13,557
Balance at June 30, 2016	$ 10,572	$ 2,381	$ 162	$ 423	$ 20	$ 13,558
Individually	$ –	$ 1	$ –	$ –	$ –	$ 1
Collectively	10,378	2,173	115	428	4	13,098
Balance at December 31, 2015	$ 10,378	$ 2,174	$ 115	$ 428	$ 4	$ 13,099
Recorded investment in loans evaluated for impairment:						
Individually	$ 18,457	$ 2,721	$ 12	$ 519	$ –	$ 21,709
Collectively	1,257,997	283,216	19,299	50,336	2,331	1,613,179
Balance at June 30, 2016	$ 1,276,454	$ 285,937	$ 19,311	$ 50,855	$ 2,331	$ 1,634,888
Individually	$ 14,639	$ 2,766	$ 181	$ 753	$ –	$ 18,339
Collectively	1,231,961	257,969	13,657	50,836	510	1,554,933
Balance at December 31, 2015	$ 1,246,600	$ 260,735	$ 13,838	$ 51,589	$ 510	$ 1,573,272

**Includes the loan types; Loans to cooperatives, Processing and marketing, and Farm-related business.*

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 tables present additional information about pre-modification and post-modification outstanding recorded investment and the effects of the modifications that occurred during the periods presented. In the tables below, activity for the quarter and six months ended June 30, 2015 is presented as revised for FCA loan reclassifications discussed above.

	Three months ended June 30, 2016				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ 158	$ 652	$ –	$ 810	
Production and intermediate-term	4	914	–	918	
Total	$ 162	$ 1,566	$ –	$ 1,728	
Post-modification:					
Real estate mortgage	$ 158	$ 652	$ –	$ 810	$ –
Production and intermediate-term	4	542	–	546	–
Total	$ 162	$ 1,194	$ –	$ 1,356	$ –

Outstanding Recorded Investment	Six months ended June 30, 2016 Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ 1,949	$ 1,682	$ –	$ 3,631	
Production and intermediate-term	172	1,054	–	1,226	
Total	$ 2,121	$ 2,736	$ –	$ 4,857	
Post-modification:					
Real estate mortgage	$ 1,866	$ 1,692	$ –	$ 3,558	$ –
Production and intermediate-term	156	712	–	868	–
Total	$ 2,022	$ 2,404	$ –	$ 4,426	$ –

Outstanding Recorded Investment	Three Months Ended June 30, 2015 (as revised) Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ 147	$ –	$ –	$ 147	
Production and intermediate term	26	110	106	242	
Total	$ 173	$ 110	$ 106	$ 389	
Post-modification:					
Real estate mortgage	$ 148	$ –	$ –	$ 148	$ –
Production and intermediate term	26	112	106	244	–
Total	$ 174	$ 112	$ 106	$ 392	$ –

Outstanding Recorded Investment	Six Months Ended June 30, 2015 (as revised) Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ 368	$ 2,896	$ –	$ 3,264	
Production and intermediate-term	26	110	106	242	
Total	$ 394	$ 3,006	$ 106	$ 3,506	
Post-modification:					
Real estate mortgage	$ 385	$ 2,980	$ –	$ 3,365	$ (43)
Production and intermediate-term	26	112	106	244	–
Total	$ 411	$ 3,092	$ 106	$ 3,609	$ (43)

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

The following table presents outstanding recorded investment for TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the period. Payment default is defined as a payment that was thirty days or more past due.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015 (as revised)	2016	2015 (as revised)
Real estate mortgage	$ 936	$ 2,847	$ 969	$ 3,443
Production and intermediate-term	–	–	38	–
Total	$ 936	$ 2,847	$ 1,007	$ 3,443

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

	Total TDRs		Nonaccrual TDRs	
	June 30, 2016	December 31, 2015	June 30, 2016	December 31, 2015
Real estate mortgage	$ 12,648	$ 12,689	$ 5,167	$ 4,525
Production and intermediate-term	1,673	1,868	579	819
Farm-related business	12	–	12	–
Rural residential real estate	376	614	–	168
Total Loans	$ 14,709	$ 15,171	$ 5,758	$ 5,512
Additional commitments to lend	$ –	$ –		

The following table presents information as of period end:

	June 30, 2016	December 31, 2015
Carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession	$ –	$ –
Recorded investment of consumer mortgage loans secured by residential real estate for which formal foreclosure proceedings are in process	$ 17	$ –

Note 3 — Investments

Investment Securities

The Association's investments consist primarily of Rural America Bonds (RABs), which are private placement securities purchased under the Mission Related Investment program approved by the FCA. In its Conditions of Approval for the program, the FCA considers a RAB ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9 and requires System institutions to provide notification to FCA when a security becomes ineligible. At June 30, 2016, the Association held no RABs whose credit quality has deteriorated beyond the program limits.

A summary of the amortized cost and fair value of investment securities held-to-maturity follows:

	June 30, 2016				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 8,229	$ 325	$ (87)	$ 8,467	6.36%

	December 31, 2015				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 8,395	$ 41	$ (171)	$ 8,265	6.27%

A summary of the contractual maturity, amortized cost and estimated fair value of investment securities held-to-maturity follows:

	June 30, 2016		
	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	$ –	$ –	–%
After one year through five years	–	–	–
After five years through ten years	–	–	–
After ten years	8,229	8,467	6.36
Total	$ 8,229	$ 8,467	6.36%

All of these investments have contractual maturities in excess of ten years. However, expected maturities for these types of securities can differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

An investment is considered impaired if its fair value is less than its cost. The following tables show the fair value and gross unrealized losses for investments that were in a continuous unrealized loss position aggregated by investment category at each reporting period. A continuous unrealized loss position for an investment is measured from the date the impairment was first identified.

	June 30, 2016			
	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ 3,466	$ (87)	$ –	$ –

	December 31, 2015			
	Less than 12 Months		12 Months or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ 3,480	$ (171)	$ –	$ –

The recording of an impairment is predicated on: (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, and (3) whether management expects to recover the security's entire amortized cost basis (even if there is no intention to sell). If the Association 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 Association 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 Association 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.

The Association uses the present value of cash flows expected to be collected from each debt security to determine the amount of credit loss. This technique requires assumptions related to the underlying collateral, including default rates, amount 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 to estimate the amount of 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 Association may obtain assumptions for the default rate, prepayment rate, and loss severity rate from an independent third party, or generate the assumptions internally.

The Association has not recognized any credit losses as any impairments were deemed temporary and resulted from non-credit related factors. The Association has the ability and intent to hold these temporarily impaired investments until a recovery of unrealized losses occurs, which may be at maturity, and at this time expects to collect the full principal amount and interest due on these securities, especially after considering credit enhancements.

Investments in other Farm Credit Institutions

The Association is required to maintain ownership in AgFirst Farm Credit Bank (AgFirst or the Bank) of Class B and Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association owned 6.78 percent of the issued stock of the Bank as of June 30, 2016 net of any reciprocal investment. As of that date, the Bank's assets totaled $31.6 billion and shareholders' equity totaled $2.4 billion. The Bank's earnings were $144 million for the first six months of 2016. In addition, the Association held investments of $4,948 related to other Farm Credit institutions.

Note 4 — Debt

Notes Payable to AgFirst Farm Credit Bank

The Association's indebtedness to the Bank represents borrowings by the Association to fund its earning assets. This indebtedness is collateralized by a pledge of substantially all of the Association's assets. The contractual terms of the revolving line of credit are contained in the General Financing Agreement (GFA). The GFA also defines Association performance criteria for borrowing from the Bank, which includes borrowing base margin, earnings and capital covenants, among others.

Note 5 — Members' Equity

Accumulated Other Comprehensive Income (AOCI)

Changes in Accumulated Other Comprehensive Income by Component *(a)*

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Employee Benefit Plans:				
Balance at beginning of period	$ (475)	$ (503)	$ (512)	$ (530)
Other comprehensive income before reclassifications	–	–	–	–
Amounts reclassified from AOCI	37	28	74	55
Net current period other comprehensive income	37	28	74	55
Balance at end of period	$ (438)	$ (475)	$ (438)	$ (475)

Reclassifications Out of Accumulated Other Comprehensive Income *(b)*

	Three Months Ended June 30,		Six Months Ended June 30,		
	2016	2015	2016	2015	Income Statement Line Item
Defined Benefit Pension Plans:					
Periodic pension costs	$ (37)	$ (28)	$ (74)	$ (55)	See Note 7.
Net amounts reclassified	$ (37)	$ (28)	$ (74)	$ (55)	

(a) Amounts in parentheses indicate debits to AOCI.
(b) Amounts in parentheses indicate debits to profit/loss.

Note 6 — Fair Value Measurement

Fair value is defined 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.

Accounting guidance establishes a 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 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 hierarchy tiers is based upon the lowest level of input that is significant to the fair value measurement.

The classifications within the fair value hierarchy are as follows:

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2 inputs 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 3 inputs are unobservable and supported by little or no market activity. Valuation is determined using pricing models, discounted cash flow methodologies, or similar techniques, and could include significant management judgment or estimation. Level 3 assets and liabilities also could include instruments whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

For a complete discussion of the inputs and other assumptions considered in assigning various assets and liabilities to the fair value hierarchy levels, see the latest Annual Report to Shareholders.

There were no Level 3 assets or liabilities measured at fair value on a recurring basis for the periods presented. The Association had no transfers of assets or liabilities into or out of Level 1 or Level 2 during the periods presented.

Fair values are estimated at each period end date for assets and liabilities measured at fair value on a recurring basis. Fair values are estimated at least annually, or when information suggests a significant change in value, for assets measured at fair value on a nonrecurring basis. Other Financial Instruments are not measured at fair value in the statement of financial position, but their fair values are estimated as of each period end date. The following tables summarize the carrying amounts of these assets and liabilities at period end, and their related fair values.

	At or for the Six Months Ended June 30, 2016					
	Total Carrying Amount	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**	**Fair Value Effects On Earnings**
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 1,655	$ 1,655	$ –	$ –	$ 1,655	
Recurring Assets	$ 1,655	$ 1,655	$ –	$ –	$ 1,655	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 22,424	$ –	$ –	$ 22,424	$ 22,424	$ 117
Other property owned	4,905	–	–	5,132	5,132	(234)
Nonrecurring Assets	$ 27,329	$ –	$ –	$ 27,556	$ 27,556	$ (117)
Other Financial Instruments						
Assets:						
Cash	$ 3,633	$ 3,633	$ –	$ –	$ 3,633	
Investment securities, held-to-maturity	8,229	–	–	8,467	8,467	
Loans	1,585,749	–	–	1,599,437	1,599,437	
Other Financial Assets	$ 1,597,611	$ 3,633	$ –	$ 1,607,904	$ 1,611,537	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 1,342,275	$ –	$ –	$ 1,348,392	$ 1,348,392	
Other Financial Liabilities	$ 1,342,275	$ –	$ –	$ 1,348,392	$ 1,348,392	

	At or for the Year ended December 31, 2015					
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value	Fair Value Effects On Earnings
Recurring Measurements						
Assets:						
Assets held in Trust funds	$ 1,410	$ 1,410	$ –	$ –	$ 1,410	
Recurring Assets	$ 1,410	$ 1,410	$ –	$ –	$ 1,410	
Liabilities:						
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –	
Nonrecurring Measurements						
Assets:						
Impaired loans	$ 20,352	$ –	$ –	$ 20,352	$ 20,352	$ (384)
Other property owned	5,425	–	–	5,667	5,667	(342)
Nonrecurring Assets	$ 25,777	$ –	$ –	$ 26,019	$ 26,019	$ (726)
Other Financial Instruments						
Assets:						
Cash	$ 4,191	$ 4,191	$ –	$ –	$ 4,191	
Investment securities, held-to-maturity	8,395	–	–	8,265	8,265	
Loans	1,527,732	–	–	1,544,279	1,544,279	
Other Financial Assets	$ 1,540,318	$ 4,191	$ –	$ 1,552,544	$ 1,556,735	
Liabilities:						
Notes payable to AgFirst Farm Credit Bank	$ 1,286,760	$ –	$ –	$ 1,283,141	$ 1,283,141	
Other Financial Liabilities	$ 1,286,760	$ –	$ –	$ 1,283,141	$ 1,283,141	

SENSITIVITY TO CHANGES IN SIGNIFICANT UNOBSERVABLE INPUTS

Discounted cash flow or similar modeling techniques are generally used to determine the recurring fair value measurements for Level 3 assets and liabilities. Use of these techniques requires determination of relevant inputs and assumptions, some of which represent significant unobservable inputs as indicated in the tables that follow. Accordingly, changes in these unobservable inputs may have a significant impact on fair value.

Certain of these unobservable inputs will (in isolation) have a directionally consistent impact on the fair value of the instrument for a given change in that input. Alternatively, the fair value of the instrument may move in an opposite direction for a given change in another input. Where multiple inputs are used within the valuation technique of an asset or liability, a change in one input in a certain direction may be offset by an opposite change in another input having a potentially muted impact to the overall fair value of that particular instrument. Additionally, a change in one unobservable input may result in a change to another unobservable input (that is, changes in certain inputs are interrelated with one another), which may counteract or magnify the fair value impact.

Investment Securities

The fair values of predominantly all Level 3 investment securities have consistent inputs, valuation techniques and correlation to changes in underlying inputs. The models used to determine fair value for these instruments use certain significant unobservable inputs within a discounted cash flow or market comparable pricing valuation technique. Such inputs generally include discount rate components including risk premiums, prepayment estimates, default estimates and loss severities.

These Level 3 assets would decrease (increase) in value based upon an increase (decrease) in discount rates, defaults, or loss severities. Conversely, the fair value of these assets would generally increase (decrease) in value if the prepayment input were to increase (decrease).

Generally, a change in the assumption used for defaults is accompanied by a directionally similar change in the risk premium component of the discount rate (specifically, the portion related to credit risk) and a directionally opposite change in the assumption used for prepayments. Unobservable inputs for loss severities do not normally increase or decrease based on movements in the other significant unobservable inputs for these Level 3 assets.

Inputs to Valuation Techniques

Management determines the Association’s valuation policies and procedures. The Bank performs the majority of the Association’s valuations, and its valuation processes are calibrated annually by an independent consultant. The fair value measurements are analyzed on a quarterly basis. For other valuations, documentation is obtained for third party information, such as pricing, and periodically evaluated alongside internal information and pricing that is available.

Quoted market prices are generally not available for the instruments presented 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.

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Fair Value	Valuation Technique(s)	Unobservable Input	Range
Impaired loans and other property owned	$ 27,556	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement cost	*
			Comparability adjustments	*

** Ranges for this type of input are not useful because each collateral property is unique.*

Information about Other Financial Instrument Fair Value Measurements

	Valuation Technique(s)	Input
Cash	Carrying Value	Par/Principal and appropriate interest yield
Loans	Discounted cash flow	Prepayment forecasts Probability of default Loss severity
Investment securities, held-to-maturity	Discounted cash flow	Prepayment rates Risk adjusted discount rate
Notes payable to AgFirst Farm Credit Bank	Discounted cash flow	Prepayment forecasts Probability of default Loss severity

Note 7 — Employee Benefit Plans

The following is a table of retirement and other postretirement benefit expenses for the Association:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Pension	$ 1,523	$ 1,528	$ 3,047	$ 3,055
401(k)	245	224	454	477
Other postretirement benefits	340	445	680	890
Total	$ 2,108	$ 2,197	$ 4,181	$ 4,422

The following is a table of retirement and other postretirement benefit contributions for the Association:

	Actual YTD Through 6/30/16	Projected Contributions For Remainder of 2016	Projected Total Contributions 2016
Pension	$ 43	$ 3,182	$ 3,225
Other postretirement benefits	390	404	794
Total	$ 433	$ 3,586	$ 4,019

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the Association participates. These amounts may change when a total funding amount and allocation is determined by the respective Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change contributions necessary before the next plan measurement date of December 31, 2016.

Further details regarding employee benefit plans are contained in the 2015 Annual Report to Shareholders, including a discussion of benefit plan changes related to the termination of the AgFirst Farm Credit Cash Balance Retirement Plan.

Note 8 — Commitments and Contingent Liabilities

From time to time, legal actions are pending against the Association in which claims for money damages are asserted. On at least a quarterly basis, the Association assesses its liabilities and contingencies in connection with outstanding legal proceedings utilizing the latest information available. In June 2016, the Association resolved a group of disputed claims in the aggregate amount of approximately $1,500. The amounts were reflected as loss on other transactions and a corresponding liability.

While the outcome of legal proceedings is inherently uncertain, on the basis of information presently available, management, after consultation with legal counsel, is of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the Association.

Note 9 — Subsequent Events

The Association evaluated subsequent events and determined there were none requiring disclosure through August 8, 2016, which was the date the financial statements were issued.