

TEXAS FARM CREDIT SERVICES

2023 Quarterly Report First quarter



For the Quarter Ended March 31, 2023

REPORT OF MANAGEMENT

The consolidated financial statements of Texas Farm Credit Services (Association) are prepared by management, who is responsible for the statements' integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America appropriate in the circumstances. Other financial information included in the quarterly report is consistent with that in the consolidated financial statements and there are no significant changes in the Association's internal controls or in other factors that could significantly affect such controls during the year.

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

/s/ Mark Miller

Mark Miller, Chief Executive Officer
May 5, 2023

/s/ Bobby Hobson

Bobby Hobson, Chairman, Board of Directors
May 5, 2023

/s/ Keith A. Ibrom

Keith A. Ibrom, Chief Financial Officer
May 5, 2023

TEXAS FARM CREDIT SERVICES MANAGEMENT'S DISCUSSION AND ANALYSIS

The following commentary reviews the financial performance of the Texas Farm Credit Services (ACA), referred to as the Association, for the quarter ended March 31, 2023. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2022 Annual Report to Stockholders.

The Association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial associations established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association's audit committee.

Loan Portfolio

Total loans outstanding at March 31, 2023, including nonaccrual loans and sales contracts, were \$2,245,621,098 compared to \$2,218,378,245 at December 31, 2022, reflecting an increase of 1.2 percent. Nonaccrual loans as a percentage of total loans outstanding were 0.4 percent at March 31, 2023, compared to 0.4 percent at December 31, 2022.

The Association recorded \$0 in recoveries and \$0 in charge-offs for the quarter ended March 31, 2023, and \$21,217 in recoveries and \$0 in charge-offs for the same period in 2022. The Association's allowance for loan losses was 0.2 percent and 0.1 percent of total loans outstanding as of March 31, 2023, and December 31, 2022, respectively.

Risk Exposure

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest and other property owned. The following table illustrates the Association's components and trends of high-risk assets.

	March 31, 2023		December 31, 2022	
	Amount	%	Amount	%
Nonaccrual	\$ 9,770,355	97.4%	\$ 10,503,174	86.8%
90 days past due and still accruing interest	263,493	2.6%	1,598,991	13.2%
Other property owned, net	-	0.0%	-	0.0%
Total	<u>\$ 10,033,848</u>	<u>100.0%</u>	<u>\$ 12,102,165</u>	<u>100.0%</u>

Results of Operations

The Association had net income of \$11,369,416 for the three months ended March 31, 2023, as compared to net income of \$10,801,058 for the same period in 2022, reflecting an increase of 5.3 percent. Net interest income was \$14,790,028 for the three months ended March 31, 2023, compared to \$13,487,069 for the same period in 2022.

	Three Months Ended			
	March 31, 2023		March 31, 2022	
	Average Balance	Interest	Average Balance	Interest
Loans	\$ 2,218,593,874	\$ 29,941,405	\$ 2,048,025,342	\$ 22,240,271
Investments	413,417	7,224	691,285	9,908
Total interest-earning assets	<u>2,219,007,291</u>	<u>29,948,629</u>	2,048,716,627	22,250,179
Interest-bearing liabilities	<u>1,993,957,586</u>	<u>15,158,601</u>	1,834,074,345	8,763,110
Impact of capital	<u>\$ 225,049,705</u>		<u>\$ 214,642,282</u>	
Net interest income		<u>\$ 14,790,028</u>		<u>\$ 13,487,069</u>

	2023	2022
	<u>Average Yield</u>	<u>Average Yield</u>
Yield on loans	5.47%	4.40%
Yield on investments	7.09%	5.81%
Total yield on interest-earning assets	5.47%	4.40%
Cost of interest-bearing liabilities	3.08%	1.94%
Interest rate spread	2.39%	2.46%
Net interest income as a percentage of average earning assets	2.70%	2.67%

**Three months ended:
March 31, 2023 vs. March 31, 2022**

	<u>Increase (decrease) due to</u>		
	<u>Volume</u>	<u>Rate</u>	<u>Total</u>
Interest income - loans	\$ 1,852,276	\$ 5,848,858	\$ 7,701,134
Interest income - investments	(3,983)	1,299	(2,684)
Total interest income	1,848,293	5,850,157	7,698,450
Interest expense	763,905	5,631,586	6,395,491
Net interest income	<u>\$ 1,084,388</u>	<u>\$ 218,571</u>	<u>\$ 1,302,959</u>

Interest income for the three months ended March 31, 2023, increased by \$7,698,450, or 34.6 percent from the same period of 2022, primarily due to increases in yields on earning assets and an increase in average loan volume. Interest expense for the three months ended March 31, 2023, increased by \$6,395,491, or 73.0 percent from the same period of 2022 due to an increase in the cost of funding as well as an increase in average debt volume. Average loan volume for the first quarter of 2023 was \$2,218,593,874, compared to \$2,048,025,342 in the first quarter of 2022. The average net interest rate spread on the loan portfolio for the first quarter of 2023 was 2.39 percent, compared to 2.46 percent in the first quarter of 2022.

The Association's return on average assets for the three months ended March 31, 2023, was 2.01 percent compared to 2.08 percent for the same period in 2022. The Association's return on average equity for the three months ended March 31, 2023, was 17.35 percent, compared to 18.22 percent for the same period in 2022.

Noninterest income for the three months ended March 31, 2023, increased by \$208,971, or 3.4 percent, compared to the same period of 2022, primarily due to an increase in financially related services income. Noninterest expense for the three months ended March 31, 2023, increased by \$1,051,464, or 11.9 percent, compared to the same period of 2022, primarily due to an increase in salaries and employee benefits and insurance fund premiums.

Liquidity and Funding Sources

The Association secures the majority of its lendable funds from the Farm Credit Bank of Texas (the Bank), which obtains its funds through the issuance of System-wide obligations and with lendable equity. The following schedule summarizes the Association's borrowings.

	<u>March 31, 2023</u>	<u>December 31, 2022</u>
Note payable to the Bank	\$ 2,016,531,581	\$ 1,991,062,303
Accrued interest on note payable	5,380,393	4,876,398
Total	<u>\$ 2,021,911,974</u>	<u>\$ 1,995,938,701</u>

The Association operates under a general financing agreement (GFA) with the Bank. The current GFA is effective through September 30, 2023. The primary source of liquidity and funding for the Association is a direct loan from the Bank. The outstanding balance of \$2,016,531,581 as of March 31, 2023, is recorded as a liability on the Association's balance sheet. The note carried a weighted average interest rate of 3.08 percent at March 31, 2023. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by the GFA. The increase in note payable to the Bank and related accrued interest payable since

December 31, 2022, is due to the Association's increase in debt related to its match funding of new loans. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were \$229,735,497 at March 31, 2023. The maximum amount the Association may borrow from the Bank as of March 31, 2023, was \$2,257,047,801 as defined by the GFA. The indebtedness continues in effect until the expiration date of the GFA, unless sooner terminated by the Bank upon the occurrence of an event of default, or by the Association, in the event of a breach of this agreement by the Bank, upon giving the Bank 30 calendar days' prior written notice, or in all other circumstances, upon giving the Bank 120 days' prior written notice.

The liquidity policy of the Association is to manage cash balances, to maximize debt reduction and to increase accrual loan volume. This policy will continue to be pursued in 2023. As borrower payments are received, they are applied to the Association's note payable to the Bank.

Capital Resources

The Association's capital position increased by \$9,552,081 at March 31, 2023, compared to December 31, 2022. The Association's debt in relation to members' equity was 7.56:1 as of March 31, 2023, compared to 7.75:1 as of December 31, 2022.

FCA regulations require us to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and unallocated retained earnings and equivalents (UREE) ratios. The permanent capital ratio continues to remain in effect, with some modifications to align with the new regulations. As of March 31, 2023, the Association exceeded all regulatory capital requirements.

Significant Recent Accounting Pronouncements

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

Relationship With the Farm Credit Bank of Texas

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the 2022 Annual Report of Texas Farm Credit Services more fully describe the Association's relationship with the Bank.

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

The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Texas Farm Credit Services, 545 South Hwy. 77, Robstown, TX 78380 or calling (361) 387-8563. The annual and quarterly stockholder reports for the Association are also available on its website at www.texasfcs.com. Copies of the Association's quarterly stockholder reports can also be requested by e-mailing kibrom@texasfcs.com.

TEXAS FARM CREDIT SERVICES

CONSOLIDATED BALANCE SHEETS

	March 31, 2023 (unaudited)	December 31, 2022
<u>ASSETS</u>		
Cash	\$ 25,824	\$ 26,159
Investments	387,317	424,737
Loans	2,245,621,098	2,218,378,245
Less: allowance for loan losses	4,793,041	3,051,962
Net loans	<u>2,240,828,057</u>	<u>2,215,326,283</u>
Accrued interest receivable	21,242,990	18,151,458
Investment in and receivable from the Farm		
Credit Bank of Texas:		
Capital stock	38,507,685	38,519,130
Other	4,302,592	563,151
Deferred taxes, net	81,250	163,570
Premises and equipment, net	17,436,135	17,895,655
Other assets	3,721,110	3,363,181
Total assets	<u><u>\$ 2,326,532,960</u></u>	<u><u>\$ 2,294,433,324</u></u>
<u>LIABILITIES</u>		
Note payable to the Farm Credit Bank of Texas	\$ 2,016,531,581	\$ 1,991,062,303
Advance conditional payments	441,122	2,136,930
Accrued interest payable	5,380,393	4,876,398
Drafts outstanding	1,299,069	150,749
Patronage distributions payable	20,539,000	20,539,000
Other liabilities	10,487,234	13,365,464
Total liabilities	<u>2,054,678,399</u>	<u>2,032,130,844</u>
<u>MEMBERS' EQUITY</u>		
Capital stock and participation certificates	4,568,965	4,580,185
Additional paid-in capital	47,596,495	47,596,495
Allocated retained earnings	53,219,859	53,219,859
Unallocated retained earnings	165,626,806	156,044,338
Accumulated other comprehensive income	842,436	861,603
Total members' equity	<u>271,854,561</u>	<u>262,302,480</u>
Total liabilities and members' equity	<u><u>\$ 2,326,532,960</u></u>	<u><u>\$ 2,294,433,324</u></u>

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

TEXAS FARM CREDIT SERVICES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(unaudited)

	Quarter Ended	
	March 31,	
	<u>2023</u>	<u>2022</u>
<u>INTEREST INCOME</u>		
Loans	\$ 29,941,405	\$ 22,240,271
Investments	7,224	9,908
Total interest income	<u>29,948,629</u>	<u>22,250,179</u>
<u>INTEREST EXPENSE</u>		
Note payable to the Farm Credit Bank of Texas	15,156,602	8,763,085
Advance conditional payments	1,999	25
Total interest expense	<u>15,158,601</u>	<u>8,763,110</u>
Net interest income	14,790,028	13,487,069
(Reversal of) provision for loan losses and other property owned	<u>(51,020)</u>	<u>64,542</u>
Net interest income after provision for loan losses	14,841,048	13,422,527
<u>NONINTEREST INCOME</u>		
Income from the Farm Credit Bank of Texas:		
Patronage income	4,115,133	3,881,810
Loan fees	771,302	1,014,358
Refunds from Farm Credit System Insurance Corporation		
Financially related services income	1,244,884	1,119,702
Gain on sale of premises and equipment, net	25,522	21,002
Other noninterest income	235,285	146,283
Total noninterest income	<u>6,392,126</u>	<u>6,183,155</u>
<u>NONINTEREST EXPENSES</u>		
Salaries and employee benefits	5,177,072	4,450,837
Directors' expense	177,954	146,600
Purchased services	312,237	309,570
Travel	327,196	319,934
Occupancy and equipment	1,504,028	1,499,066
Communications	114,448	96,728
Advertising	105,572	51,521
Public and member relations	255,160	273,891
Supervisory and exam expense	141,681	258,202
Insurance Fund premiums	880,330	682,680
Other noninterest expense	866,972	722,157
Total noninterest expenses	<u>9,862,650</u>	<u>8,811,186</u>
Income before income taxes	<u>11,370,524</u>	<u>10,794,496</u>
Provision for (benefit from) income taxes	<u>1,108</u>	<u>(6,562)</u>
NET INCOME	<u>11,369,416</u>	<u>10,801,058</u>
Other comprehensive income:		
Change in postretirement benefit plans	<u>(19,167)</u>	<u>(5,430)</u>
COMPREHENSIVE INCOME	<u>\$ 11,350,249</u>	<u>\$ 10,795,628</u>

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

TEXAS FARM CREDIT SERVICES

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY
(unaudited)

	Capital Stock/ Participation Certificates	Additional Paid-in-Capital	Retained Earnings		Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2021	\$ 4,364,895	\$ 47,596,495	\$ 54,627,414	\$ 129,133,773	\$ (315,716)	\$ 235,406,861
Comprehensive income	-	-	-	10,801,058	(5,430)	10,795,628
Capital stock/participation certificates and allocated retained earnings issued	175,165	-	-	-	-	175,165
Capital stock/participation certificates and allocated retained earnings retired	(66,810)	-	-	-	-	(66,810)
Balance at March 31, 2022	<u>\$ 4,473,250</u>	<u>\$ 47,596,495</u>	<u>\$ 54,627,414</u>	<u>\$ 139,934,831</u>	<u>\$ (321,146)</u>	<u>\$ 246,310,844</u>
Balance at December 31, 2022	\$ 4,580,185	\$ 47,596,495	\$ 53,219,859	\$ 156,044,338	\$ 861,603	\$ 262,302,480
Comprehensive income	-	-	-	11,369,416	(19,167)	11,350,249
Capital stock/participation certificates and allocated retained earnings issued	64,035	-	-	-	-	64,035
Capital stock/participation certificates and allocated retained earnings retired	(75,255)	-	-	-	-	(75,255)
Adjustment due to CECL adoption	-	-	-	(1,786,948)	-	(1,786,948)
Balance at March 31, 2023	<u>\$ 4,568,965</u>	<u>\$ 47,596,495</u>	<u>\$ 53,219,859</u>	<u>\$ 165,626,806</u>	<u>\$ 842,436</u>	<u>\$ 271,854,561</u>

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

TEXAS FARM CREDIT SERVICES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Unaudited

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

The Texas Farm Credit Services (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Anderson, Angelina, Aransas, Atascosa, Austin, Bandera, Bee, Bexar, Bowie, Brooks, Cameron, Camp, Cass, Chambers, Cherokee, Collin, Cook, Dallas, Delta, Denton, DeWitt, Dimmit, Duval, Edwards, Fannin, Fayette, Franklin, Freestone, Frio, Goliad, Gonzales, Grayson, Gregg, Guadalupe, Hardin, Harrison, Henderson, Hidalgo, Hopkins, Houston, Hunt, Jasper, Jefferson, Jim Hogg, Jim Wells, Karnes, Kaufman, Kenedy, Kerr, Kinney, Kleberg, Lamar, LaSalle, Lavaca, Leon, Liberty, Limestone, Live Oak, Marion, Maverick, McMullen, Medina, Montgomery, Morris, Nacogdoches, Newton, Nueces, Orange, Panola, Polk, Rains, Real, Red River, Rockwall, Rusk, Sabine, San Augustine, San Jacinto, San Patricio, Shelby, Smith, Starr, Titus, Trinity, Tyler, Upshur, Uvalde, Val Verde, Van Zandt, Walker, Waller, Washington, Webb, Willacy, Wilson, Wood, Zapata, and Zavala, parts of Refugio, and the lower half of Lee in the State of Texas. The Association is a lending association of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2022, as contained in the 2022 Annual Report to Stockholders.

In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with GAAP, except for the inclusion of a statement of cash flows. GAAP require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements. These interim financial statements should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2022, as contained in the 2022 Annual Report to Stockholders. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2023. Descriptions of the significant accounting policies are included in the 2022 Annual Report to Stockholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the Banking industry.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management's estimates. The results for the quarter ended March 31, 2023, are not necessarily indicative of the results to be expected for the year ended December 31, 2023. Certain amounts in the prior period's financial statements have been reclassified to conform to current financial statement presentation.

Recently Adopted Accounting Pronouncements

The Association adopted the Financial Accounting Standards Board (FASB) guidance entitled "Measurement of Credit Losses on Financial Instruments" and other subsequently issued accounting standards updates related to credit losses on January 1, 2023. This guidance replaced the current incurred loss impairment methodology with a single allowance framework for financial assets carried at amortized cost and certain off-balance sheet credit exposures. This guidance requires management to consider in its estimate of the allowance for credit losses (ACL) relevant historical events, current conditions and reasonable and supportable forecasts that affect the collectability of the assets. In addition, the guidance amends existing impairment guidance for held-to-maturity and available-for-sale investments to incorporate an allowance for credit losses related to these securities, which will allow for the reversal of credit impairments in the event that the credit of an issuer improves.

Also adopted effective January 1, 2023, was the updated guidance entitled "Financial Instruments – Credit Losses: Troubled Debt Restructurings and Vintage Disclosure." This guidance requires the creditor to determine whether a modification results in a new loan or a continuation of an existing loan, among other disclosures specific to modifications with borrowers that are experiencing financial difficulties. The update eliminated the accounting guidance for troubled debt restructurings by creditors. The update also requires disclosure of current period gross write-offs by year of origination for financing receivables and net investments in leases.

The following table presents the impact to the allowance for credit losses and retained earnings upon adoption of this guidance on January 1, 2023:

	December 31, 2022	CECL adoption impact	January 1, 2023
Assets:			
Allowance for credit losses on loans	\$ (3,051,962)	\$ (1,735,440)	\$ (4,787,402)
Deferred tax assets	\$ 163,570	\$ (81,212)	\$ 82,358
Liabilities:			
Allowance for credit losses on unfunded commitments	\$ (203,392)	\$ 29,704	\$ (173,688)
Retained earnings:			
Unallocated retained earnings, net of tax	\$ 156,044,338	\$ (1,786,948)	\$ 154,257,390

Investments

The Association's investments include mortgage-backed securities issued by Federal Agricultural Mortgage Corporation (Farmer Mac) for which the Association has the intent and ability to hold to maturity and which are consequently classified as held to maturity. As more fully described in the 2022 Annual Report, the Association may hold additional investments in accordance with other investment programs approved by the FCA. These programs allow the Association to make investments that further the mission to support rural America.

Upon adoption of CECL guidance, the investments held-to-maturity are presented net of an allowance for credit losses on investments. The guidance also amended the previous other-than-temporary impairment (OTTI) model for investments available-for-sale to incorporate an allowance for credit losses.

Impairment may result from credit deterioration of the issuer or collateral underlying the security. In performing an assessment of whether any decline in fair value is due to a credit loss, all relevant information is considered at the individual security level. For mortgage-backed and asset-backed securities, performance indicators considered relate to the underlying assets include default rates, delinquency rates, percentage of nonperforming assets, debt-to-collateral ratios, third-party guarantees, current levels of subordination, vintage, geographic concentration, analyst reports and forecasts, credit ratings and other market data.

With respect to certain classes of debt securities, primarily U.S. Treasuries and government guaranteed agency securities, management considers the history of credit losses, current conditions and reasonable and supportable forecasts, which may indicate that the expectation that nonpayment of the amortized cost basis is or continues to be zero, even if the U.S. government were to technically default. Therefore, for those securities, System associations do not record expected credit losses.

Available-for-sale debt securities in unrealized loss positions are evaluated for impairment related to credit losses at least quarterly. For available-for-sale debt securities, a decline in fair value due to estimated credit loss results in recording an allowance for credit losses to the extent the fair value is less than the amortized cost basis. Declines in fair value that have not been recorded through an allowance for credit losses, such as declines due to changes in market interest rates, are recorded through other comprehensive income, net of applicable taxes.

In assessing whether a credit loss exists for held-to-maturity investments, the present value of cash flows expected to be collected from the security is compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis for the security, a credit loss exists and an allowance for credit losses is recorded, limited to the amount the fair value is less than amortized cost basis.

If the intention is to sell a debt security or it is more likely than not to be required to sell the security before recovery of its amortized cost basis, the debt security is written down to its fair value and the write down is charged against the allowance for credit losses with any incremental impairment reported in earnings.

To the extent that debt securities in the held-to-maturity portfolio share common risk characteristics, estimated expected credit losses are calculated in a manner like that used for loans held for investment. That is, for pools of such securities with common risk characteristics, the historical lifetime probability of default and severity of loss in the event of default is derived or obtained from external sources and adjusted for the expected effects of reasonable and supportable forecasts over the expected lives of the securities on those historical credit losses.

Expected credit loss on each security in the held-to-maturity portfolio that do not share common risk characteristics with any of the pools of debt securities is individually measured based on net realizable value, or the difference between the discounted value of the expected future cash flows, based on the original effective interest rate, and the recorded amortized cost basis of the security.

Loans and Allowance for Credit Losses

Loans are generally carried at their principal amount outstanding adjusted for charge-offs, deferred loan fees or costs, and valuation adjustments relating to hedging activities. Loan origination fees and direct loan origination costs are netted and capitalized and the net fee or cost is amortized over the average life of the related loan as an adjustment to interest income. Loan prepayment fees are reported in interest income. Interest on loans is accrued and credited to interest income based on the daily principal amount outstanding.

Nonaccrual Loans

Nonaccrual loans are loans for which there is reasonable doubt that all principal and interest will not be collected according to the original contractual terms and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is modified or until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full.

Consistent with prior practice, loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately secured and in the process of collection), circumstances indicate that collection of principal and interest is in doubt or legal action, including foreclosure or other forms of collateral conveyance, has been initiated to collect the outstanding principal and interest. At the time a loan is placed in nonaccrual status, accrued interest that is considered uncollectible is reversed (if accrued in the current year) or charged against the allowance for loan losses (if accrued in prior years). Loans are charged-off at the time they are determined to be uncollectible.

When loans are in nonaccrual status, interest payments received in cash are generally recognized as interest income if the collectability of the loan principal is fully expected and certain other criteria are met. Otherwise, payments received on nonaccrual loans are applied against the recorded investment in the loan asset. Nonaccrual loans are returned to accrual status if all contractual principal and interest is current, the borrower is fully expected to fulfill the contractual repayments terms and after remaining current as to principal and interest for a sustained period or have a recent repayment pattern demonstrating future repayment capacity to make on-time payments. If previously unrecognized interest income exists at the time the loan is transferred to accrual status, cash received at the time of or subsequent to the transfer should first be recorded as interest income until such time as the recorded balance equals the contractual indebtedness of the borrower.

Accrued interest receivable

The entity elected to continue classifying accrued interest on loans and investment securities in accrued interest receivable and not as part of loans or investments on the Condensed Statement of Condition. The Association also elected to not estimate an allowance on interest receivable balances because the nonaccrual policies in place provide for the accrual of interest to cease on a timely basis when all contractual amounts are not expected

Loan Modifications to Borrowers Experiencing Financial Difficulty

Loan modifications may be granted to borrowers experiencing financial difficulty. Modifications can be in the form of one or a combination of principal forgiveness, interest rate reduction, other-than-insignificant payment delay or a term extension. Covenant waivers and modifications of contingent acceleration clauses are not considered term extensions.

Collateral dependent loans

Collateral dependent loans are loans secured by collateral, including but not limited to agricultural real estate, crop inventory, equipment and livestock. CECL requires the Association to measure the expected credit losses based on fair value of the collateral at the reporting date when the Association determines that foreclosure is probable. Additionally, CECL allows a fair value practical expedient as a measurement approach for loans when the repayment is expected to be provided substantially through the operation or sale of the collateral when the borrower is experiencing financial difficulties. Under the practical expedient measurement approach, the expected credit losses is based on the difference between the fair value of the collateral less estimated costs to sell and the amortized cost basis of the loan.

Allowance for Credit Losses

Beginning January 1, 2023, the allowance for credit losses (ACL) represents the estimated current expected credit losses over the remaining contractual life of financial assets measured at amortized cost and certain off-balance sheet credit exposures. The ACL takes into consideration relevant information about past events, current conditions and reasonable and supportable macroeconomic

forecasts of future conditions. The contractual term excludes expected extensions, renewals and modifications unless the extension or renewal options are not unconditionally cancellable. The ACL comprises:

- the allowance for credit losses on loans (ACLL)
- the allowance for unfunded commitments, which is presented on the balance sheet in other liabilities, and
- the allowance for credit losses on investment securities, which covers held-to-maturity and available-for-sale securities and is recognized within each investment securities classification on the Condensed Statement of Condition.

Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio, considering macroeconomic conditions, forecasts and other factors prevailing at the time, may result in significant changes in the ACL in those future periods.

Methodology for Allowance for Credit Losses on Loans

The ACLL represents management's estimate of credit losses over the remaining expected life of loans. Loans are evaluated on the amortized cost basis, including premiums, discounts and fair value hedge accounting adjustments.

The entity employs a disciplined process and methodology to establish its ACLL that has two basic components: first, an asset-specific component involving individual loans that do not share risk characteristics with other loans and the measurement of expected credit losses for such individual loans; and second, a pooled component for estimated expected credit losses for pools of loans that share similar risk characteristics.

Asset-specific loans are generally collateral-dependent loans (including those loans for which foreclosure is probable) and nonaccrual loans. For an asset-specific loan, expected credit losses are measured as the difference between the amortized cost basis in the loan and the present value of expected future cash flows discounted at the loan's effective interest rate except that, for collateral-dependent loans, credit loss is measured as the difference between the amortized cost basis in the loan and the fair value of the underlying collateral. The fair value of the collateral is adjusted for the estimated cost to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral. In accordance with the Association's appraisal policy, the fair value of collateral-dependent loans is based upon independent third-party appraisals. When an updated appraisal or collateral valuation is received, management reassesses the need for adjustments to the loan's expected credit loss measurements and, where appropriate, records an adjustment. If the calculated expected credit loss is determined to be permanent, fixed or non-recoverable, the credit loss portion of the loan will be charged off against the allowance for credit losses.

In estimating the component of the ACLL that share common risk characteristics, loans are evaluated collectively and segregated into loan pools considering the risk associated with the specific pool. Relevant risk characteristics include loan type, commodity, credit quality rating, delinquency category or business segment or a combination of these classes. The allowance is determined based on a quantitative calculation of the expected life-of-loan loss percentage for each loan category by considering the probability of default, based on the migration of loans from performing to loss by credit quality rating or delinquency buckets using historical life-of-loan analysis periods for loan types, and the severity of loss, based on the aggregate net lifetime losses incurred per loan pool.

The component of the ACLL also considers factors for each loan pool to adjust for differences between the historical period used to calculate historical default and loss severity rates and expected conditions over the remaining lives of the loans in the portfolio related to:

- lending policies and procedures;
- national, regional and local economic business conditions and developments that affect the collectability of the portfolio, including the condition of various markets;
- the nature of the loan portfolio, including the terms of the loans;
- the experience, ability and depth of the lending management and other relevant staff;
- the volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans;
- the quality of the loan review and process;
- the value of underlying collateral for collateral-dependent loans;
- the existence and effect of any concentrations of credit and changes in the level of such concentrations; and
- the effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

The entity uses multiple scenarios over reasonable and supportable forecast period of two years. Subsequent to the forecast period, the Association reverts to long run historical loss experience beyond the two years on a straight-line basis over a one year reversion period to inform the estimate of losses for the remaining contractual life of the loan portfolio.

The economic forecasts incorporate macroeconomic variables, including unemployment rates, real gross domestic product levels and corporate bond spreads, as well as net farm income and agricultural commodity prices. Also considered are loan and borrower characteristics, such as internal risk ratings, delinquency status, collateral type, and the remaining term of the loan, adjusted for expected prepayments.

In addition to the quantitative calculation, the Association considers the imprecision inherent in the process and methodology, emerging risk assessments and other subjective factors, which may lead to a management adjustment to the modeled ACLL results. Expected credit loss estimates also include consideration of expected cash recoveries on loans previously charged-off or expected recoveries on collateral dependent loans where recovery is expected through sale of the collateral. The economic forecasts are updated on a quarterly basis.

Prior to January 1, 2023, the allowance for loan losses was maintained at a level considered adequate to provide for probable losses existing in and inherent in the loan portfolio. The allowance was based on a periodic evaluation of the loan portfolio in which numerous factors are considered, including economic conditions, collateral values, borrowers' financial conditions, loan portfolio composition and prior loan loss experience. The allowance for loan losses encompassed various judgments, evaluations and appraisals with respect to the loans and their underlying collateral that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity would cause these various judgments, evaluations and appraisals to change over time. Management considered a number of factors in determining and supporting the levels of the allowances for loan losses, which include, but are not limited to, the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences.

Allowance for Credit Losses on Unfunded Commitments

The entity evaluates the need for an allowance for credit losses on unfunded under CECL and, if required, an amount is recognized and included in other liabilities on the Combined Statement of Condition. The amount of expected losses is determined by calculating a commitment usage factor over the contractual period for exposures that are not unconditionally cancellable by the Association and applying the loss factors used in the ACLL methodology to the results of the usage calculation. No allowance for credit losses are recorded for commitments that are unconditionally cancellable.

NOTE 2 — INVESTMENTS:

The following is a summary of Farmer Mac agricultural mortgage-backed securities:

	March 31, 2023				
	Amortized Cost	Gross Unrealized Losses	Fair Value	Weighted Average Yield	Weighted Average Life
Agricultural mortgage-backed securities	\$ 387,317	\$ (14,218)	\$ 373,099	6.04%	4.42 Years
	December 31, 2022				
	Amortized Cost	Gross Unrealized Losses	Fair Value	Weighted Average Yield	Weighted Average Life
Agricultural mortgage-backed securities	\$ 424,737	\$ (16,159)	\$ 408,578	5.80%	4.64 Years

NOTE 3 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans follows:

Loan Type	March 31,	December 31,
	2023	2022
	Amount	Amount
Production agriculture:		
Real estate mortgage	\$ 1,793,675,775	\$ 1,801,949,287
Production and intermediate-term	271,561,815	257,966,403
Agribusiness:		
Processing and marketing	77,769,646	69,301,464
Farm-related business	42,202,717	36,011,762
Loans to cooperatives	19,146,536	22,640,041
Communication	21,042,121	16,267,788
Water and waste water	7,134,489	7,073,081
Agricultural export finance	5,949,289	3,440,131
Energy	5,292,695	1,858,635
Rural residential real estate	1,052,223	1,070,269
Mission-related investments	793,792	799,384
Total	<u>\$ 2,245,621,098</u>	<u>\$ 2,218,378,245</u>

The Association purchases or sells participation interests with other parties in order to diversify risk, manage loan volume and comply with FCA regulations. The following table presents information regarding the balances of participations purchased and sold at March 31, 2023:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations	Participations	Participations	Participations	Participations	Participations
	Purchased	Sold	Purchased	Sold	Purchased	Sold
Real estate mortgage	\$ 56,314,262	\$ 90,937,962	\$ 8,829,602	\$ -	\$ 65,143,864	\$ 90,937,962
Production and intermediate-term	33,059,414	21,371,888	-	-	33,059,414	21,371,888
Agribusiness	88,861,295	1,921,249	-	-	88,861,295	1,921,249
Communication	21,042,121	-	-	-	21,042,121	-
Water and waste water	7,134,489	-	-	-	7,134,489	-
Agricultural export finance	5,949,289	-	-	-	5,949,289	-
Energy	5,292,695	-	-	-	5,292,695	-
Total	<u>\$ 217,653,565</u>	<u>\$ 114,231,099</u>	<u>\$ 8,829,602</u>	<u>\$ -</u>	<u>\$ 226,483,167</u>	<u>\$ 114,231,099</u>

The Association is authorized under the Farm Credit Act to accept “advance conditional payments” (ACPs) from borrowers. To the extent the borrower’s access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against the borrower’s related loan balance. Unrestricted advance conditional payments are included in other liabilities. ACPs are not insured, and interest is generally paid by the Association on such balances. Balances of ACPs were \$441,122 and \$2,136,930 at March 31, 2023, and December 31, 2022, respectively.

Credit Quality

Credit risk arises from the potential inability of an obligor to meet its payment obligation and exists in our outstanding loans, letters of credit and unfunded loan commitments. The entity manages credit risk associated with the retail lending activities through an analysis of the credit risk profile of an individual borrower using its own set of underwriting standards and lending policies, approved by its board of directors, which provides direction to its loan officers. The retail credit risk management process begins with an analysis of the borrower’s credit history, repayment capacity, financial position and collateral, which includes an analysis of credit scores for smaller loans. Repayment capacity focuses on the borrower’s ability to repay the loan based on cash flows from operations or other sources of income, including off-farm income. Real estate mortgage loans must be secured by first liens on the real estate (collateral). As required by FCA regulations, each association that makes loans on a secured basis must have collateral evaluation policies and procedures. Real estate mortgage loans may be made only in amounts up to 85 percent of the original appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a state, federal, or other governmental agency. The actual

loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Loans other than real estate mortgage may be made on a secured or unsecured basis.

The entity uses a two-dimensional risk rating model based on an internally generated combined System risk rating guidance that incorporates a 14-point probability of default rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default. Probability of default is the probability that a borrower will experience a default during the life of the loan. The loss given default is management's estimate as to the anticipated principal loss on a specific loan assuming default occurs during the remaining life of the loan. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower or the loan is classified nonaccrual. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses and risks in a particular relationship. The Association reviews, at least on an annual basis, or when a credit action is taken the probability of default category.

Each of the probability of default categories carries a distinct percentage of default probability. The probability of default rate between one and nine of the acceptable categories is very narrow and would reflect almost no default to a minimal default percentage. The probability of default rate grows more rapidly as a loan moves from acceptable to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain. These categories are defined as follows:

- acceptable — assets are expected to be fully collectible and represent the highest quality,
- other assets especially mentioned (OAEM) — assets are currently collectible but exhibit some potential weakness,
- substandard — assets exhibit some serious weakness in repayment capacity, equity, or collateral pledged on the loan,
- doubtful — assets exhibit similar weaknesses to substandard assets; however, doubtful assets have additional weaknesses in existing facts, conditions and values that make collection in full highly questionable, and
- loss — assets are considered uncollectible.

The following table presents credit quality indicators by loan type and the related principal balance:

	Term Loans						Revolving Loans Amortized Cost Basis	Revolving Loans Converted to Term Loans Amortized Cost Basis	Total
	Amortized Cost by Origination Year								
	2023	2022	2021	2020	2019	Prior			
Real estate mortgage									
Acceptable	\$ 58,421,862	\$ 404,529,778	\$ 604,009,143	\$ 301,098,491	\$ 112,631,298	\$ 297,703,057	\$ -	\$ -	\$ 1,778,393,629
OAEM	-	-	4,516,948	894,632	1,537,534	1,434,934	-	-	8,384,048
Substandard/Doubtful	-	-	3,000,115	708,463	264,008	2,925,512	-	-	6,898,098
	58,421,862	404,529,778	611,526,206	302,701,586	114,432,840	302,063,503	-	-	1,793,675,775
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Production and intermediate-term									
Acceptable	5,996,983	99,593,551	17,159,289	21,403,627	1,973,290	9,285,641	-	109,009,573	264,421,954
OAEM	3,199,490	15,101	-	-	80,929	51,847	-	1,339,696	4,687,063
Substandard/Doubtful	746,343	350,000	1,356,455	-	-	-	-	-	2,452,798
	9,942,816	99,958,652	18,515,744	21,403,627	2,054,219	9,337,488	-	110,349,269	271,561,815
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Agribusiness									
Acceptable	11,587,814	47,300,370	13,426,447	11,986,038	5,174,051	6,028,219	1,756,800	24,063,066	121,322,805
OAEM	-	-	-	-	-	-	-	1,050,000	1,050,000
Substandard/Doubtful	-	-	-	5,003,839	-	8,327,423	-	3,414,832	16,746,094
	11,587,814	47,300,370	13,426,447	16,989,877	5,174,051	14,355,642	1,756,800	28,527,898	139,118,899
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Communication									
Acceptable	6,989,538	-	431,575	13,621,008	-	-	-	-	21,042,121
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	6,989,538	-	431,575	13,621,008	-	-	-	-	21,042,121
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Energy									
Acceptable	3,494,943	-	-	-	-	1,389,171	-	-	4,884,114
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	408,581	-	-	408,581
	3,494,943	-	-	-	-	1,797,752	-	-	5,292,695
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Water and waste water									
Acceptable	-	3,022,545	2,496,309	-	-	-	-	1,615,635	7,134,489
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	-	3,022,545	2,496,309	-	-	-	-	1,615,635	7,134,489
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Rural residential real estate									
Acceptable	-	-	87,538	-	-	526,174	-	-	613,712
OAEM	-	-	-	-	-	353,298	-	-	353,298
Substandard/Doubtful	-	-	-	-	-	85,213	-	-	85,213
	-	-	87,538	-	-	964,685	-	-	1,052,223
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Agricultural export finance									
Acceptable	-	4,484,021	-	-	-	-	-	1,465,268	5,949,289
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	-	4,484,021	-	-	-	-	-	1,465,268	5,949,289
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Mission-related investments									
Acceptable	-	-	-	-	-	793,792	-	-	793,792
OAEM	-	-	-	-	-	-	-	-	-
Substandard/Doubtful	-	-	-	-	-	-	-	-	-
	-	-	-	-	-	793,792	-	-	793,792
Current period gross charge-offs	-	-	-	-	-	-	-	-	-
Total Loans									
Acceptable	86,491,140	558,930,265	637,610,301	348,109,164	119,778,639	315,726,054	1,756,800	136,153,542	2,204,555,905
OAEM	3,199,490	15,101	4,516,948	894,632	1,618,463	1,840,079	-	2,389,696	14,474,409
Substandard/Doubtful	746,343	350,000	4,356,570	5,712,302	264,008	11,746,729	-	3,414,832	26,590,784
	\$ 90,436,973	\$ 559,295,366	\$ 646,483,819	\$ 354,716,098	\$ 121,661,110	\$ 329,312,862	\$ 1,756,800	\$ 141,958,070	\$ 2,245,621,098
Total current period gross charge-offs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

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

	March 31, 2023	December 31, 2022
Real estate mortgage		
Acceptable	99.1 %	99.4 %
OAEM	0.5 %	0.2 %
Substandard/doubtful	0.4 %	0.4 %
	100.0 %	100.0 %
Production and intermediate-term		
Acceptable	97.4 %	97.8 %
OAEM	1.7 %	1.3 %
Substandard/doubtful	0.9 %	0.9 %
	100.0 %	100.0 %
Loans to cooperatives		
Acceptable	100.0 %	100.0 %
OAEM	-	-
Substandard/doubtful	-	-
	100.0 %	100.0 %
Processing and marketing		
Acceptable	93.9 %	92.1 %
OAEM	1.4 %	1.7 %
Substandard/doubtful	4.7 %	6.2 %
	100.0 %	100.0 %
Farm-related business		
Acceptable	69.0 %	63.6 %
OAEM	-	-
Substandard/doubtful	31.0 %	36.4 %
	100.0 %	100.0 %
Communication		
Acceptable	100.0 %	100.0 %
OAEM	-	-
Substandard/doubtful	-	-
	100.0 %	100.0 %
Energy		
Acceptable	92.3 %	76.0 %
OAEM	-	-
Substandard/doubtful	7.7 %	24.0 %
	100.0 %	100.0 %
Water and waste water		
Acceptable	100.0 %	100.0 %
OAEM	-	-
Substandard/doubtful	-	-
	100.0 %	100.0 %
Rural residential real estate		
Acceptable	58.3 %	58.1 %
OAEM	33.6 %	33.6 %
Substandard/doubtful	8.1 %	8.3 %
	100.0 %	100.0 %
Agricultural export finance		
Acceptable	100.0 %	100.0 %
OAEM	-	-
Substandard/doubtful	-	-
	100.0 %	100.0 %
Mission-related investments		
Acceptable	100.0 %	100.0 %
OAEM	-	-
Substandard/doubtful	-	-
	100.0 %	100.0 %
Total loans		
Acceptable	98.1 %	98.4 %
OAEM	0.7 %	0.4 %
Substandard/doubtful	1.2 %	1.2 %
	100.0 %	100.0 %

The Association wrote off \$0 accrued interest receivable for the three months ended March 31, 2023 and 2022.

The following table reflects nonperforming assets, which consist of nonaccrual loans, accruing loans 90 days or more delinquent and other property owned and related credit quality statistics:

	March 31, 2023	December 31, 2022
Nonaccrual loans:		
Real estate mortgage	\$ 4,540,421	\$ 4,577,106
Production and intermediate-term	1,174,329	1,174,329
Agribusiness	3,647,025	4,306,286
Energy	408,580	445,453
Total nonaccrual loans	<u>9,770,355</u>	<u>10,503,174</u>
Accruing loans 90 days or more past due:		
Real estate mortgage	263,449	144,591
Production and intermediate-term	44	31
Agribusiness	-	1,454,369
Total accruing loans 90 days or more past due	<u>263,493</u>	<u>1,598,991</u>
Total nonperforming loans	10,033,848	12,102,165
Other property owned	-	-
Total nonperforming assets	<u>\$ 10,033,848</u>	<u>\$ 12,102,165</u>
Nonaccrual loans as a percentage of total loans	0.44%	0.47%
Nonperforming assets as a percentage of total loans and other property owned	0.45%	0.55%
Nonperforming assets as a percentage of capital	3.69%	4.61%

The following table provides the amortized cost for nonaccrual loans with and without a related allowance for loan losses, as well as interest income recognized on nonaccrual during the period:

	March 31, 2023			Interest Income Recognized For the Three Months Ended March 31, 2023
	Amortized Cost with Allowance	Amortized Cost without Allowance	Total	
Nonaccrual loans:				
Real estate mortgage	\$ -	\$ 4,540,421	\$ 4,540,421	\$ 1,458
Production and intermediate-term	-	1,174,329	1,174,329	-
Agribusiness	3,647,025	-	3,647,025	-
Energy	408,580	-	408,580	-
Total nonaccrual loans	<u>\$ 4,055,605</u>	<u>\$ 5,714,750</u>	<u>\$ 9,770,355</u>	<u>\$ 1,458</u>

The following tables provide an aging analysis of past due loans at amortized cost by portfolio segment as of:

March 31, 2023	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment >90 Days and Accruing
Real estate mortgage	\$ 3,199,395	\$ 275,638	\$ 3,475,033	\$ 1,790,200,742	\$ 1,793,675,775	\$ 263,449
Production and intermediate term	686,123	44	686,167	270,875,648	271,561,815	44
Processing and marketing	37,301	-	37,301	77,732,345	77,769,646	-
Farm-related business	-	-	-	42,202,717	42,202,717	-
Loans to cooperatives	-	-	-	19,146,536	19,146,536	-
Communication	-	-	-	21,042,121	21,042,121	-
Water and waste water	-	-	-	7,134,489	7,134,489	-
Agricultural export finance	-	-	-	5,949,289	5,949,289	-
Energy	-	-	-	5,292,695	5,292,695	-
Rural residential real estate	-	-	-	1,052,223	1,052,223	-
Mission-related investments	-	-	-	793,792	793,792	-
Total	\$ 3,922,819	\$ 275,682	\$ 4,198,501	\$ 2,241,422,597	\$ 2,245,621,098	\$ 263,493

Prior to the adoption of CECL, the aging analysis of past due loans reported included accrued interest as follows:

December 31, 2022	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	Recorded Investment >90 Days and Accruing
Real estate mortgage	\$ 6,483,859	\$ 156,780	\$ 6,640,639	\$ 1,807,972,579	\$ 1,814,613,218	\$ 144,591
Production and intermediate term	619,803	31	619,834	261,172,301	261,792,135	31
Processing and marketing	1,301,882	334,156	1,636,038	67,964,141	69,600,179	-
Farm-related business	-	-	-	36,747,924	36,747,924	-
Loans to cooperatives	-	1,454,368	1,454,368	21,695,143	23,149,511	1,454,369
Communication	-	-	-	16,324,645	16,324,645	-
Water and waste water	-	-	-	7,080,959	7,080,959	-
Agricultural export finance	-	-	-	3,472,533	3,472,533	-
Energy	-	-	-	1,866,118	1,866,118	-
Rural residential real estate	89,670	-	89,670	984,652	1,074,322	-
Mission-related investments	-	-	-	803,664	803,664	-
Total	\$ 8,495,214	\$ 1,945,335	\$ 10,440,549	\$ 2,226,084,659	\$ 2,236,525,208	\$ 1,598,991

A loan is considered collateral dependent when the borrower is experiencing financial difficulty and repayment is expected to be provided substantially through the operation or sale of the collateral. The collateral dependent loans are primarily real estate mortgage and rural residential real estate loans.

Allowance for Credit Losses

The credit risk rating methodology is a key component of the Association's allowance for credit losses evaluation, and is generally incorporated into the Association's loan underwriting standards and internal lending limits. In addition, borrower and commodity concentration lending and leasing limits have been established to manage credit exposure. The regulatory limit to a single borrower or lessee is 15 percent of the Association's lending and leasing limit base but the Association has established more restrictive lending limits.

Effective January 1, 2023, the System adopted the CECL accounting guidance as described in Note 1. A summary of changes in the allowance for credit losses by portfolio segment are as follows:

	Real estate mortgage	Production and intermediate- term	Agribusiness	Communication	Energy	Water and waste water	Rural residential real estate	Agricultural export finance	Mission-related investments	Total
Allowance for Loan Losses:										
Balance at December 31, 2022	\$ 1,579,691	\$ 628,543	\$ 712,761	\$ 14,214	\$ 105,928	\$ 6,166	\$ 935	\$ 3,024	\$ 700	\$ 3,051,962
Cumulative effect of a change in accounting principle	2,027,349	(291,909)	-	-	-	-	-	-	-	1,735,440
Balance at January 1, 2023	3,607,040	336,634	712,761	14,214	105,928	6,166	935	3,024	700	4,787,402
Charge-offs	-	-	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-	-	-
Provision for loan losses (loan loss reversal)	(196,943)	(1,943)	153,004	25,606	8,387	7,311	1,057	8,333	827	5,639
Balance at March 31, 2023	\$ 3,410,097	\$ 334,691	\$ 865,765	\$ 39,820	\$ 114,315	\$ 13,477	\$ 1,992	\$ 11,357	\$ 1,527	\$ 4,793,041
Allowance for Unfunded Commitments:										
Balance at December 31, 2022	\$ 53,032	\$ 150,360	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 203,392
Cumulative effect of a change in accounting principle	65,109	(94,813)	-	-	-	-	-	-	-	(29,704)
Balance at January 1, 2023	118,141	55,547	-	-	-	-	-	-	-	173,688
Provision for unfunded commitments	(53,326)	(3,333)	-	-	-	-	-	-	-	(56,659)
Balance at March 31, 2023	\$ 64,815	\$ 52,214	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 117,029
Total allowance for credit losses	\$ 3,474,912	\$ 386,905	\$ 865,765	\$ 39,820	\$ 114,315	\$ 13,477	\$ 1,992	\$ 11,357	\$ 1,527	\$ 4,910,070

Allowance for Loan Losses ¹ :										
Balance at December 31, 2021	\$ 1,899,626	\$ 761,376	\$ 145,857	\$ 18,606	\$ 162,348	\$ 3,577	\$ 1,316	\$ 4,724	\$ 19,106	\$ 3,016,536
Charge-offs	-	-	-	-	-	-	-	-	-	-
Recoveries	20,349	868	-	-	-	-	-	-	-	21,217
Provision for loan losses (loan loss reversal)	71,311	78,618	8,572	390	(50,501)	1,909	13	116	352	110,780
Balance at March 31, 2022	\$ 1,991,286	\$ 840,862	\$ 154,429	\$ 18,996	\$ 111,847	\$ 5,486	\$ 1,329	\$ 4,840	\$ 19,458	\$ 3,148,533
Balance at December 31, 2021	\$ 50,672	\$ 188,880	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 239,552
Provision for unfunded commitments	1,998	(48,236)	-	-	-	-	-	-	-	(46,238)
Balance at March 31, 2022	\$ 52,670	\$ 140,644	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 193,314
Total allowance for credit losses	\$ 2,043,956	\$ 981,506	\$ 154,429	\$ 18,996	\$ 111,847	\$ 5,486	\$ 1,329	\$ 4,840	\$ 19,458	\$ 3,341,847

¹ For periods prior to January 1, 2023, the allowance for loan losses was based on probable and estimable losses inherent in the loan portfolio

There were no loan modifications granted to borrowers experiencing financial difficulty, during the quarter ended March 31, 2023.

Troubled Debt Restructurings

Prior to January 1, 2023, the adoption of updated FASB guidance on loan modifications, a restructuring of a loan constituted a troubled debt restructuring, also known as formally restructured, if the creditor for economic or legal reasons related to the borrower's financial difficulties granted a concession to the borrower that it would not otherwise consider. Concessions varied by program and were borrower-specific and could include interest rate reductions, term extensions, payment deferrals or the acceptance of additional collateral in lieu of payments. In limited circumstances, principal may have been forgiven. When a restructured loan constituted a troubled debt restructuring, these loans were included within our impaired loans under nonaccrual or accruing restructured loans.

There were no troubled debt restructurings that occurred during the quarter ending March 31, 2022.

There were no loans that met the accounting criteria as a troubled debt restructuring and that occurred within the previous 12 months and for which there was a payment default during the period:

The following table provides information on outstanding loans restructured in troubled debt restructurings:

	December 31, 2022	
	Loans Modified as Troubled Debt Restructurings	Troubled Debt Restructurings in Nonaccrual
Real estate mortgage	\$ 35,983	\$ 35,983

NOTE 4 —LEASES:

The components of lease expense were as follows:

Classification	For the Three Months Ended	
	March 31, 2023	March 31, 2022
Operating lease cost	\$ 69,613	\$ 23,036
Short-term lease cost	35,400	3,600
Finance lease cost:		
Amortization of right-of-use assets	(13,600)	8,542
Net lease cost	\$ 91,413	\$ 35,178

Other information related to leases was as follows:

	For the Three Months Ended	
	March 31, 2023	March 31, 2022
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows from operating leases	\$ 56,013	\$ 31,578
Right-of-use assets obtained in exchange for lease obligations:		
Operating leases	\$ 69,613	\$ 23,036

Lease term and discount rate are as follows:

	<u>March 31, 2023</u>	<u>December 31, 2022</u>
Weighted average remaining lease term in years		
Operating leases	7.23	7.33
Weighted average discount rate		
Operating leases	4.76%	4.01%

Future minimum lease payments under non-cancellable leases as of March 31, 2023 were as follows:

	<u>Operating Leases</u>
2023	\$ 153,545
2024	212,466
2025	165,381
2026	96,646
Thereafter	474,674
Total	<u>\$ 1,102,712</u>

NOTE 5 — CAPITAL:

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

<u>Risk-adjusted:</u>	<u>Regulatory Requirements Including Capital Conservation Buffers</u>	<u>As of March 31, 2023</u>
Common equity tier 1 ratio	7.00%	11.85%
Tier 1 capital ratio	8.50%	11.85%
Total capital ratio	10.50%	12.10%
Permanent capital ratio	7.00%	11.88%
<u>Non-risk-adjusted:</u>		
Tier 1 leverage ratio	5.00%	10.01%
UREE leverage ratio	1.50%	7.43%

The details for the amounts used in the calculation of the regulatory capital ratios as of March 31, 2023:

	Common equity tier 1 ratio	Tier 1 capital ratio	Total capital ratio	Permanent capital ratio
Numerator:				
Unallocated retained earnings	\$ 94,298,178	\$ 94,298,178	\$ 94,298,178	\$ 94,298,178
Paid-in capital	47,596,495	47,596,495	47,596,495	47,596,495
Common Cooperative Equities:				
Statutory minimum purchased borrower stock	4,567,150	4,567,150	4,567,150	4,567,150
Allocated equities:				
Allocated equities held ≥ 7	53,652,556	53,652,556	53,652,556	53,652,556
Nonqualified allocated equities not subject to retirement	64,937,342	64,937,342	64,937,342	64,937,342
Allowance for loan losses and reserve for credit losses subject to certain limitations	-	-	4,764,339	-
Regulatory Adjustments and Deductions:				
Amount of allocated investments in other System institutions	(37,674,655)	(37,674,655)	(37,674,655)	(37,674,655)
Other regulatory required deductions	(1,601,427)	(1,601,427)	(1,601,427)	(1,601,427)
	<u>\$ 225,775,639</u>	<u>\$ 225,775,639</u>	<u>\$ 230,539,978</u>	<u>\$ 225,775,639</u>
Denominator:				
Risk-adjusted assets excluding allowance	\$ 1,943,939,563	\$ 1,943,939,563	\$ 1,943,939,563	\$ 1,943,939,563
Regulatory Adjustments and Deductions:				
Regulatory deductions included in total capital	(39,276,081)	(39,276,081)	(39,276,081)	(39,276,081)
Allowance for loan losses	-	-	-	(4,588,889)
	<u>\$ 1,904,663,482</u>	<u>\$ 1,904,663,482</u>	<u>\$ 1,904,663,482</u>	<u>\$ 1,900,074,593</u>
Calculated Ratio	11.85%	11.85%	12.10%	11.88%

	Tier 1 leverage ratio	UREE leverage ratio
Numerator:		
Unallocated retained earnings	\$ 94,298,178	\$ 94,298,178
Paid-in capital	47,596,495	47,596,495
Common Cooperative Equities:		
Statutory minimum purchased borrower stock	4,567,150	-
Allocated equities:		
Allocated equities held ≥ 7	53,652,556	-
Nonqualified allocated equities not subject to retirement	64,937,342	64,937,342
Regulatory Adjustments and Deductions:		
Amount of allocated investments in other System institutions	(37,674,655)	(37,674,655)
Other regulatory required deductions	(1,601,427)	(1,601,427)
	<u>\$ 225,775,639</u>	<u>\$ 167,555,933</u>
Denominator:		
Total Assets	\$ 2,294,335,975	\$ 2,294,335,975
Regulatory Adjustments and Deductions:		
Regulatory deductions included in tier 1 capital	(39,489,768)	(39,489,768)
	<u>\$ 2,254,846,207</u>	<u>\$ 2,254,846,207</u>
Calculated Ratio	10.01%	7.43%

	<u>March 31, 2023</u>	<u>December 31, 2022</u>
Capital stock and participation certificates	\$ 4,568,965	\$ 4,580,185
Additional paid-in-capital	47,596,495	47,596,495
Accumulated other comprehensive income	842,436	861,603
Retained earnings ¹	<u>218,846,665</u>	<u>209,264,197</u>
Total capital	<u>\$ 271,854,561</u>	<u>\$ 262,302,480</u>

¹ Retained earnings for the quarter ended March 31, 2023, reflects a decrease from the cumulative effect of a change in accounting principle for CECL on January 1, 2023.

The following tables present the activity in the accumulated other comprehensive income (loss), net of tax by component:

<u>Accum Other Comp Income (Loss)</u>	
<u>March 31, 2023</u>	<u>Net of Tax</u>
Nonpension postretirement benefits	\$ 842,436
March 31, 2022	<u>Net of Tax</u>
Nonpension postretirement benefits	\$ (321,146)

The Association's accumulated other comprehensive income (loss) relates entirely to its nonpension other postretirement benefits. Amortization of prior service (credits) cost and of actuarial (gain) loss are reflected in "Salaries and employee benefits" in the Consolidated Statements of Comprehensive Income. The following table summarizes the change in accumulated other comprehensive income (loss) for the three months ended March 31:

	<u>2023</u>	<u>2022</u>
Accumulated other comprehensive income (loss) at January 1	\$ 861,603	\$ (315,716)
Amortization of prior service credit included		
in salaries and employee benefits	(5,429)	(5,430)
Amortization of actuarial gain included		
in salaries and employee benefits	<u>(13,738)</u>	-
Other comprehensive loss, net of tax	<u>(19,167)</u>	<u>(5,430)</u>
Accumulated other comprehensive income (loss) at March 31	<u>\$ 842,436</u>	<u>\$ (321,146)</u>

NOTE 6 — INCOME TAXES:

The Association conducts its business activities through two wholly-owned subsidiaries. Long-term mortgage lending activities are conducted through a wholly-owned FLCA subsidiary which is exempt from federal and state income tax. Short and intermediate term lending activities are conducted through a wholly-owned PCA subsidiary. The PCA subsidiary and the ACA holding company are subject to income tax. The Association operates as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage dividends in the form of cash, stock or allocated retained earnings. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage dividends. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the Association and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized. The Association has no valuation allowance on its deferred tax assets because management estimates full utilization of these assets.

NOTE 7 — FAIR VALUE MEASUREMENTS:

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 15 to the 2022 Annual Report to Stockholders for a more complete description.

Assets and liabilities measured at fair value on a non-recurring basis for each of the fair value hierarchy values are summarized below:

<u>March 31, 2023</u>	<u>Fair Value Measurement Using</u>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Assets:			
Loans	\$ -	\$ -	\$ 3,351,303
Other property owned	-	-	-
<u>December 31, 2022</u>	<u>Fair Value Measurement Using</u>		
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Assets:			
Loans	\$ -	\$ -	\$ 4,047,437
Other property owned	-	-	-

Uncertainty of Fair Value Measurements

With regard to nonrecurring measurements for impaired loans and other property owned, it is not practicable to provide specific information on inputs, as each collateral property is unique. System associations utilize appraisals to value these loans and other property owned and take into account unobservable inputs, such as income and expense, comparable sales, replacement cost and comparability adjustments.

Valuation Techniques

As more fully discussed in Note 15 to the 2022 Annual Report to Stockholders, authoritative guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Association's assets and liabilities. For a more complete description, see Notes to the 2022 Annual Report to Stockholders.

Loans Evaluated for Impairment

For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon the underlying collateral since the loans are collateral-dependent loans for which real estate is the collateral. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, a majority of these loans have fair value measurements that fall within Level 3 of the fair value hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

Other Property Owned

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

Cash

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

Loans

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

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

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

NOTE 8 — EMPLOYEE BENEFIT PLANS:

The following table summarizes the components of net periodic benefit costs for the three months ended March 31:

	Other Benefits	
	2023	2022
Service cost	\$ 6,897	\$ 11,330
Interest cost	42,827	34,959
Amortization of prior service credits	(5,429)	(5,430)
Amortization of net actuarial gain	(13,738)	-
Net periodic benefit cost	<u>\$ 30,557</u>	<u>\$ 40,859</u>

The Association’s liability for the unfunded accumulated obligation for these benefits at March 31, 2023, was \$3,387,848 and is included in other liabilities on the balance sheet.

The components of net periodic benefit cost other than the service cost component are included in the line item "other components of net periodic postretirement benefit cost" in the income statement.

The structure of the district’s defined benefit pension plan is characterized as multiemployer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (Bank and associations). The Association recognizes its amortized annual contributions to the plan as an expense. The Association previously disclosed in its financial statements for the year ended December 31, 2022, that it expected to contribute \$309,219 to the district’s defined benefit pension plan in 2023. As of March 31, 2023, \$77,305 of contributions have been expensed. The Association presently does not anticipate additional contributions over \$309,219 will be required in 2023.

NOTE 9 — COMMITMENTS AND CONTINGENT LIABILITIES:

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

NOTE 10 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through May 5, 2023, which is the date the financial statements were issued. There are no other significant events requiring disclosure as of this date.