

**AG**   
**TEXAS**  
**FARM CREDIT SERVICES**  
**Quarterly Report**

**The First Quarter Ended  
March 31, 2020**



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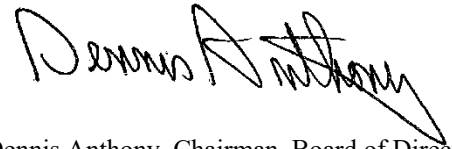
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The consolidated financial statements of *AgTexas Farm Credit Services* (“**Association**”) are prepared by management, who is responsible for the statements’ integrity and objectivity, including amounts that must necessarily be based on judgments 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 affects such controls during the quarter.

The undersigned certify that this quarterly report has been reviewed and 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 his knowledge and belief.



Tim McDonald, Chief Executive Officer  
April 29, 2020



Dennis Anthony, Chairman, Board of Directors  
April 29, 2020



Jeff Fairchild, Chief Financial Officer  
April 29, 2020

## Management's Discussion & Analysis

The first quarter consolidated financial statements of AgTexas Farm Credit Services, including its wholly-owned subsidiaries AgTexas, PCA and AgTexas, FLCA (collectively referred to herein as the “**Association**”), is unaudited, but contains all adjustments necessary for a fair presentation of the interim financial condition and results of operations. The statements are prepared in conformity with generally accepted accounting principles and prevailing practices within the banking industry. In preparing these consolidated statements and meeting its responsibility for reliable financial information, management depends upon the Association's accounting and internal control systems which have been designed to provide reasonable assurance that assets are safeguarded and transactions are properly authorized and recorded.

The Association is a member of the *Farm Credit System* (“**System**”), a nationwide network of cooperatively owned financial institutions 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 following commentary explains management's assessment of the principal aspects of the consolidated financial condition and results of operations of the Association for the three months ended March 31, 2020, and should be read in conjunction with the accompanying *unaudited consolidated financial statements* (“**CFS**”) and the *Association's 2019 Annual Report to Stockholders* (“**2019 Annual Report**”). Management prepared the accompanying CFS under the oversight of the Association's Audit Committee.

### Significant Events.

The United States has been operating under a presidentially declared emergency since March 13, 2020 due to the Coronavirus Disease 2019 (also referred to as COVID-19). The Association continues during these unprecedented times to fulfill its mission to support agriculture and rural communities by providing access to reliable and consistent credit. The Association has implemented a response related to the COVID-19 pandemic. The Association continues to operate with minimal staff on-site as to potentially limit the spread, but still provide customer service. Capital levels remained strong to support any adversity or continuing loan demand. As it relates to the Association's internal controls over financial reporting and disclosure controls and procedures, the controls and procedures continue to operate effectively and no material changes to the controls or financial systems have occurred or are contemplated.

The overall impact of COVID-19 is evolving rapidly, and future events are uncertain. Challenging economic conditions are likely ahead, however, as COVID-19 has caused many countries, including the U.S., to impose restrictions on travel and public gatherings. It is too early to accurately assess the potential impact of COVID-19 on the global, U.S. and district economies. The Association will continue to closely monitor the situation in the coming quarters.

The Association will continue to keep abreast of information that may impact future performance. West Texas Intermediate oil prices closed March 2020 at about \$20 per barrel, down from about \$62 per barrel in December 2019. Oil prices were negatively impacted during the first quarter of 2020 by reductions in global demand due to COVID-19 and increasing supply, as a production-limiting agreement between OPEC and other global oil exporters, including Russia, collapsed in March 2020. According to the March 2020 Short Term Energy Outlook released by the U.S. Energy Information Administration, the West Texas Intermediate oil price is projected to average about \$38 per barrel during 2020. Respondents to the Federal Reserve Bank of Dallas Energy Survey indicated in March 2020 that they could profitably drill a new well in the Permian Basin with oil prices at about \$49 per barrel, on average. Consequently, activity in the oil and gas sector is likely to decline substantially if oil prices remain under significant pressure.

The U.S. Secretary of Agriculture announced in March 2020 that China has continued its progress toward meeting its agriculture-related commitments under the U.S.-China Phase One Trade Agreement. During the first quarter of 2020, the U.S.-Mexico-Canada Agreement (USMCA) was signed into law by the U.S. government and approved by the Canadian Parliament. According to the U.S. Secretary of Agriculture, Canada and Mexico are the two largest export markets for U.S. food and agricultural products.

In its March 2020 World Agricultural Supply and Demand Estimate (WASDE) report, the U.S. Department of Agriculture (USDA) lowered the 2019/20 expected season-average prices for several crops, including corn, soybeans and cotton. Similarly, near-term price expectations for other commodities, such as hogs and pork, were adjusted downward. USDA expects live cattle prices to average slightly lower in 2020 than reported in 2019. Milk prices are also anticipated to decline in 2020 after rising by more than 10% during the previous year. While consumer demand for food products has generally been high during the early weeks of the COVID-19 outbreak in the U.S. and abroad, stay-at-home orders and other macroeconomic forces are disrupting typical purchasing patterns. This has caused volatility in agricultural commodity markets and could lead to challenges for food processing companies and material revisions in USDA forecasts in the coming months.

## Management's Discussion & Analysis

Association borrowers utilize risk management tools, such as federally-sponsored crop insurance programs and forward, futures and options contracts, to mitigate risk and enhance margins. The Association's portfolio continues to be supported by strong credit quality, high levels of capital, and diversification. In order to provide necessary and timely relief to borrowers affected by COVID-19, the Association has implemented a loan payment deferral and covenant relief program whereby a borrower can defer up to 6 months of loan payments or covenants. In addition, the Association has become an approved SBA lender for the Paycheck Protection Program loans. The Association has undertaken these programs while maintaining appropriate internal controls and oversight measures.

The Association distributed patronage of approximately \$15.1 million in cash and an additional \$3.2 million in allocated equities in the first quarter of 2020. This represented the 2019 patronage declared by the Association.

### Loan and Investment Portfolio.

Total loans outstanding at March 31, 2020, including nonaccrual loans, were \$1,974,847,509 compared to 2,013,703,362 at December 31, 2019, reflecting a decrease of 1.9 percent. Nonaccrual loans as a percentage of total loans outstanding were 0.4 percent at March 31, 2020, compared to 0.4 percent at December 31, 2019.

The Association recorded \$958,559 in recoveries and \$625,125 in charge-offs for the three months ended March 31, 2020, and \$287,498 in recoveries and \$33,930 in charge-offs for the same period in 2019. The Association's allowance for credit losses, which consists of the allowance for loan losses and the reserve for unfunded credit commitments, was 0.38 percent and 0.36 percent of total loans outstanding as of March 31, 2020, and December 31, 2019, respectively. The increase is due to changes in the stresses applied in calculating the allowance for credit losses.

The financial performance of the Association may be significantly impacted by the quality of loans within the loan portfolio. Internal policies and procedures, as well as third party credit reviews and examinations help to ensure asset quality is properly reflected. Additional detail on credit quality is illustrated in the following table.

	March 31, 2020	March 31, 2019	December 31, 2019
Acceptable	94.1%	95.4%	94.1%
OAEM	3.5%	3.0%	3.4%
Substandard/doubtful	2.4%	1.6%	2.5%
	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Changes in the Association's loan portfolio from December 31, 2019 to March 31, 2020 follow:

Loan Type	March 31, 2020		December 31, 2019	
	Amount	%	Amount	%
Real estate mortgage	\$ 1,110,682,146	56.1%	\$ 1,084,069,296	53.7%
Production and intermediate term	595,303,944	30.1%	659,679,343	32.8%
Agribusiness:				
Loans to cooperatives	11,527,105	0.6%	3,538,860	0.2%
Processing and marketing	129,384,324	6.6%	132,037,952	6.6%
Farm-related business	24,910,821	1.3%	22,600,552	1.1%
Communication	19,213,736	1.0%	19,222,731	1.0%
Energy	7,522,778	0.4%	7,271,541	0.4%
Rural residential real estate	8,020,904	0.4%	8,362,492	0.4%
Lease receivables	1,031,002	0.1%	913,850	0.0%
Mission-related investments	67,250,749	3.4%	76,006,745	3.8%
Total	<b>\$ 1,974,847,509</b>	<b>100.0%</b>	<b>\$ 2,013,703,362</b>	<b>100.0%</b>

## Management's Discussion & Analysis

The Association's portfolio includes significant mission-related investments authorized under the FCA approved *Rural America Bond Pilot Program* ("RAB"). The RAB program was designed to meet the growing and changing needs of agricultural enterprises, agribusinesses, and various infrastructure needs in rural communities through investment in these areas. The RAB pilot program ended as of December 31, 2014. FCA approved new investment regulations that became effective January 1, 2019. Effective February 25, 2019, the Association began purchasing USDA 100% unconditional guaranteed loans that are considered mission-related investments included in the above table.

Effective January 1, 2019, FCA new investment regulations provided authorization for the Association to invest in *Small Business Administration* ("SBA") pool securities. As a part of the conditions of the authorization, the investments are required to be 100% unconditionally guaranteed by the federal government or its agencies. For more information and see Note 2 in the "Notes to Unaudited Consolidated Financial Statements".

**Risk Exposure.** High risk assets include impaired loans and other property owned. Impaired loans are comprised of nonaccrual, past due  $\geq 90$  days and still accruing interest, and formally restructured loans. The following table illustrates the Association's components and trends of high risk assets:

	March 31, 2020		December 31, 2019	
	Amount	%	Amount	%
Nonaccrual	\$ 8,328,540	30.4%	\$ 7,722,827	30.1%
90 days past due and still accruing interest	1,136,532	4.2%	-	0.0%
Formally restructured	17,899,176	65.4%	17,924,921	69.9%
Other property owned, net	-	0.0%	-	0.0%
Total	\$ 27,364,248	100.0%	\$ 25,647,748	100.0%

**Results of Operations.** Changes in the Association's results of operations for the three months ended March 31, 2020 and March 31, 2019 follow:

	For the three months ended	
	March 31, 2020	March 31, 2019
Interest income	\$ 23,696,117	\$ 24,587,140
Interest expense	(12,172,748)	(13,005,863)
(Provision for) reversal of loan losses	134,573	(435,499)
Net interest margin	11,657,942	11,145,778
Noninterest income	5,233,139	5,040,519
Noninterest expense	(8,247,933)	(8,133,481)
Net income	\$ 8,643,148	\$ 8,052,816

Net interest margin (interest income less interest expense) is the principal source of earnings and results from relative volumes of interest-earning assets and interest-bearing liabilities, yields on interest-earning assets, and rates on interest-bearing liabilities. Decreases in interest income and expense are due to decreasing interest rates offset by growth in volume. The decrease in "(Provision for) reversal of loan losses" is due recovery in the current year. Noninterest income increase is due to increases in patronage income offset by decreases in crop insurance income. Noninterest expense increased over the prior period due to salaries but is in line with budget projections.

The effects of changes in average volumes, yields, and rates on interest margin follow:

## Management's Discussion & Analysis

	For the three months ended March 31, 2020		For the three months ended March 31, 2019	
	Average		Average	
	Balance	Interest	Balance	Interest
Total loans and investments	2,048,733,903	23,696,117	1,957,046,468	24,587,140
Interest-bearing liabilities	1,829,714,560	12,172,748	1,755,231,807	13,005,863
Impact of capital	<u>\$ 219,019,343</u>		<u>\$ 201,814,661</u>	
Net interest income		<u>\$ 11,523,369</u>		<u>\$ 11,581,277</u>

	2020	2019
	Average Yield	Average Yield
Yield on loans and investments	4.69%	5.10%
Cost of interest-bearing	2.70%	3.01%
Interest rate spread	1.99%	2.09%
Interest rate margin	2.28%	2.40%

	Three months ended March 31:		
	2020 vs. 2019		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest income	\$ 1,153,001	\$ (2,044,024)	\$ (891,023)
Interest expense	552,805	(1,385,920)	(833,115)
Net interest income	<u>\$ 600,196</u>	<u>\$ (658,104)</u>	<u>\$ (57,908)</u>

The Association's return on average assets was 1.64% and 1.60% for the three months ended March 31, 2020 and 2019, respectively. The Association's return on average equity was 12.56% and 12.40% for the three months ended March 31, 2020 and 2019, respectively. These ratios for the three months ended March 31, 2020 have remained relatively stable.

**Liquidity and Funding Sources.** *Interest rate risk* ("IRR") inherent in the loan portfolio is substantially mitigated through the funding relationship with the FCBT. FCBT manages IRR through direct loan pricing and asset/liability management. The Association's primary source of liquidity and funding is a direct note payable to FCBT. The following schedule summarizes the Association's borrowings:

	March 31, 2020	December 31, 2019
Note payable to the Bank	\$ 1,823,022,275	\$ 1,872,168,788
Accrued interest on note payable	4,102,873	4,358,348
Total	<u>\$ 1,827,125,148</u>	<u>\$ 1,876,527,136</u>

The Association operates under a *general financing agreement* ("GFA") with the bank. The current GFA is effective through September 30, 2020. The primary source of liquidity and funding for the Association is a direct loan from the bank. The outstanding balance of \$1,823,022,275 as of March 31, 2020, is recorded as a liability on the Association's balance sheet. The note carried a weighted average interest rate of 2.57 percent at March 31, 2020. 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 since December 31, 2019, is due to the Association's increase in investment volume. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were \$212,230,505 at March 31, 2020. The maximum amount the Association may borrow from the bank as of March 31, 2020, was \$2,038,043,569 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.

## Management's Discussion & Analysis

**Capital Resources.** The Association's members' equity was \$283,797,296 and \$275,570,321 at March 31, 2020 and December 31, 2019, respectively, a \$8,226,975 increase, which approximates current earnings. The Association's debt as a percentage of members' equity was 6.53:1 as of March 31, 2020, compared to 6.96:1 as of December 31, 2019. FCA regulations require associations 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. See note 4 in the "Notes to Unaudited Consolidated Financial Statements". As of March 31, 2020, the Association exceeded all regulatory capital requirements.

**Significant Recent Accounting Pronouncements.** See Note 1 in CFS.

**Relationship With FCBT.** The Association has a statutory obligation to borrow only from FCBT, which is discussed in note 10, *Note Payable to FCBT*, in the Association's consolidated financial statements in the 2019 Annual Report.

FCBT's ability to access Association capital is discussed in note 2, *Summary of Significant Accounting Policies*, in the Association's consolidated financial statements in the 2019 Annual Report, within the *Farm Credit Bank of Texas Capital Stock* section.

FCBT's role to help mitigate Association exposure to IRR is described in the *Liquidity and Funding Sources* section of *Management's Discussion and Analysis of Financial Condition and Results of Operations* and note 10, *Note Payable to FCBT*, in the Association's consolidated financial statements in the 2019 Annual Report.

FCBT provides computer systems to support the critical operations of all *10th Farm Credit District* ("District") associations. In addition, each association has operating systems and facility-based systems that are not supported by FCBT. As disclosed in note 14, *Related Party Transactions*, in the Association's consolidated financial statements in the 2019 Annual Report, FCBT provides many services to the Association, which include administrative, marketing, and accounting services and information systems.

The Association's financial condition may be impacted by factors that affect FCBT. The financial condition and results of operations of FCBT may materially affect Association stockholders' investment in the Association.

**Annual and Quarterly Stockholder Report Availability.** FCBT's annual and quarterly stockholder reports 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 FCBT are also available on its website at [www.farmcreditbank.com](http://www.farmcreditbank.com).

Annual and quarterly stockholder reports for the Association are available free of charge on the Association's website [www.agtexas.com](http://www.agtexas.com) or by *i*) writing to AgTexas Farm Credit Services, 5004 N. Loop 289, Lubbock, Texas 79416, *ii*) calling (806) 687-4068, or *iii*) e-mailing [jeff.fairchild@agtexas.com](mailto:jeff.fairchild@agtexas.com).





## Consolidated Balance Sheets

	March 31, 2020	December 31, 2019
	Unaudited	Audited
<b><u>Assets</u></b>		
Cash	\$ 244,481	\$ 8,995
Investments	77,390,364	82,342,471
Loans	1,974,847,509	2,013,703,362
Less: allowance for loan losses	5,928,537	6,074,288
Net loans	1,968,918,972	2,007,629,074
Accrued interest receivable	21,382,722	25,109,254
Investment in and receivable from the Farm Credit Bank of Texas:		
Capital stock	37,014,485	37,072,250
Other	5,607,647	15,355,572
Other property owned, net	-	-
Premises and equipment	23,920,951	23,845,668
Other assets	1,970,931	1,165,473
	\$ 2,136,450,553	\$ 2,192,528,757
<b><u>Liabilities</u></b>		
Note payable to the Farm Credit Bank of Texas	\$ 1,823,022,275	\$ 1,872,168,788
Advance conditional payments	11,209,389	8,757,369
Accrued interest payable	4,102,873	4,358,348
Accrued postretirement benefit liability	7,572,965	7,530,780
Patronage distributions payable	318	15,065,059
Other liabilities	6,745,437	9,078,092
	1,852,653,257	1,916,958,436
<b><u>Members' Equity</u></b>		
Capital stock and participation certificates	4,184,125	4,160,515
Preferred stock	20,000,000	20,000,000
Allocated retained earnings	21,422,838	21,422,837
Unallocated retained earnings	163,322,539	155,179,391
Additional paid-in capital	75,310,003	75,310,003
Accumulated other comprehensive income	(442,209)	(502,425)
	283,797,296	275,570,321
	\$ 2,136,450,553	\$ 2,192,528,757

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



## Unaudited Consolidated Statements of Comprehensive Income

	For the three months ended	
	March 31, 2020	March 31, 2019
	Unaudited	Unaudited
<b><u>Interest income</u></b>		
Loans	\$ 23,369,431	\$ 24,293,201
Investments	326,686	293,939
Total interest income	23,696,117	24,587,140
<b><u>Interest expense</u></b>		
Note payable to the Farm Credit Bank of Texas	12,159,925	12,989,340
Advance conditional payments	12,823	16,523
Total interest expense	12,172,748	13,005,863
Net interest income	11,523,369	11,581,277
Provision for loan losses	(134,573)	435,499
Net interest income after provision for losses	11,657,942	11,145,778
<b><u>Noninterest income</u></b>		
Farm Credit Bank of Texas patronage income	3,916,638	3,344,700
Loan fees	188,420	145,174
Fees for financially related services	401,178	1,045,340
Other	726,903	505,305
Total noninterest income	5,233,139	5,040,519
<b><u>Noninterest expenses</u></b>		
Salaries and employee benefits	5,478,977	5,438,788
Directors' expense	98,018	118,528
Purchased services	586,885	509,326
Travel	290,546	284,888
Occupancy and equipment	485,430	436,296
Communication	82,614	89,202
Advertising	135,132	137,301
Public and member relations	275,670	260,976
Federally regulated examination fees	141,831	133,137
FCSIC insurance premiums	279,171	306,863
Other components of net periodic postretirement benefit cost	55,285	65,289
Other noninterest expense	338,374	352,887
Total noninterest expenses	8,247,933	8,133,481
<b>Net income</b>	8,643,148	8,052,816
Other comprehensive income (loss):		
Change in postretirement benefit plans	(8,658)	(11,967)
Change in fair value of available for sale investments	68,874	248,238
Total other comprehensive income (loss)	60,216	236,271
<b>Comprehensive income</b>	\$ 8,703,364	\$ 8,289,087

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



## Unaudited Consolidated Statements of Changes in Members' Equity

	Capital Stock/ Participation Certificates	Preferred Stock	Retained Earnings		Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
			Allocated	Unallocated			
Balance at December 31, 2018	\$ 4,090,470	\$ 20,000,000	\$ 20,738,085	\$ 139,586,873	\$ 75,310,003	\$ 105,270	\$ 259,830,701
Comprehensive income	-	-	-	8,052,816	-	236,271	8,289,087
Capital stock/participation certificates issued	211,695	-	-	-	-	-	211,695
Capital stock/participation certificates retired	(184,910)	-	-	-	-	-	(184,910)
Preferred stock dividends: Paid				(500,000)			(500,000)
Patronage dividends: Paid or accrued	-	-	(371)	-	-	-	(371)
Balance at March 31, 2019	<u>\$ 4,117,255</u>	<u>\$ 20,000,000</u>	<u>\$ 20,737,714</u>	<u>\$ 147,139,689</u>	<u>\$ 75,310,003</u>	<u>\$ 341,541</u>	<u>\$ 267,646,202</u>
Balance at December 31, 2019	\$ 4,160,515	\$ 20,000,000	\$ 21,422,837	\$ 155,179,391	\$ 75,310,003	\$ (502,425)	\$ 275,570,321
Comprehensive income	-	-	-	8,643,148	-	60,216	8,703,364
Capital stock/participation certificates issued	215,795	-	-	-	-	-	215,795
Capital stock/participation certificates retired	(192,185)	-	-	-	-	-	(192,185)
Preferred stock dividends: Paid	-	-	-	(500,000)	-	-	(500,000)
Patronage dividends: Paid or accrued	-	-	1	-	-	-	1
Paid/declared payable	-	-	-	-	-	-	-
Balance at March 31, 2020	<u>\$ 4,184,125</u>	<u>\$ 20,000,000</u>	<u>\$ 21,422,838</u>	<u>\$ 163,322,539</u>	<u>\$ 75,310,003</u>	<u>\$ (442,209)</u>	<u>\$ 283,797,296</u>

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

## Notes to Unaudited Consolidated Financial Statements

### Note 1: Organization, Operations and Significant Accounting Policies

AgTexas Farm Credit Services (“AgTX ACA”) and its wholly-owned subsidiaries, AgTexas, PCA (“PCA”) and AgTexas, FLCA (“FLCA”), are collectively referred to herein as the “Association.” AgTX ACA provides financing and related services through FLCA and PCA. FLCA makes secured long-term agricultural real estate and rural home mortgage loans. PCA makes short- and intermediate-term loans for agricultural production or operating purposes.

These notes and the encompassing unaudited consolidated financial statements for AgTX ACA (collectively referred to herein as “CFS”), include the accounts of PCA and FLCA. All significant intercompany balances and transactions are eliminated in consolidation. In management’s opinion, the CFS reflect all adjustments necessary to fairly state results for the interim periods presented, which are of a normal recurring nature.

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, 2019, as contained in the 2019 Annual Report to Stockholders.

In the opinion of management, the CFS 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 *Farm Credit Administration* (“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, 2019 as contained in the 2019 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, 2020. Descriptions of the significant accounting policies are included in the 2019 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.

**Significant Recent Accounting Pronouncements.** In December 2019, the Financial Accounting Standards Board (“FASB”) issued guidance entitled “Simplifying the Accounting for Income Taxes.” This guidance eliminates certain intra period tax allocations, foreign deferred tax recognition and interim period tax calculations. In addition, the guidance simplifies disclosure regarding capital and franchise taxes, the allocation of goodwill in business combinations, subsidiary financial statements and other disclosures. The new guidance is intended to eliminate and/or simplify certain aspects of income tax accounting that are complex or that require significant judgment in application or presentation. The guidance becomes effective for fiscal years beginning after December 15, 2021. Early adoption of the guidance is permitted and the institution adopted this guidance on January 1, 2020. The adoption of this guidance did not materially impact the Associations’s financial condition or results of operations.

In August 2018, FASB issued guidance entitled “Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Cost.” The guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by this guidance. This guidance became effective for interim and annual periods beginning after December 15, 2019. The guidance also requires an entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. It further specifies where to present expense and payments in the financial statements. The guidance is to be applied on a retrospective or prospective basis to all implementation costs incurred after the date of adoption. The adoption of this guidance did not materially impact the Association’s financial condition or its results of operations.

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Defined Benefit Plans.” The guidance modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance becomes effective for fiscal years ending after December 15, 2020. Early adoption is permitted. The guidance is to be applied on a retrospective basis for all periods. The adoption of this guidance will not impact the Association’s financial condition or its results of operations, but will impact the employee benefit plan disclosures.

## Notes to Unaudited Consolidated Financial Statements

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement.” The guidance modifies the requirements on fair value measurements by removing, modifying or adding to the disclosures. This guidance became effective for interim and annual periods beginning after December 15, 2019. Early adoption was permitted and an entity was permitted to early adopt any removal or modified disclosures and delay adoption of the additional disclosures until their effective date. The Association early adopted the removal and modified disclosures during the fourth quarter of 2018. The adoption of this guidance did not impact the Association’s financial condition or its results of operations but did impact the fair value measurements disclosures.

In June 2016, the FASB issued guidance entitled “Measurement of Credit Losses on Financial Instruments.” The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange Commission filers this guidance was to become effective for interim and annual periods beginning after December 15, 2020, with early application permitted. In November 2019, the FASB issued an update that amends the mandatory effective date for this guidance for certain institutions. The change resulted from a change in the effective date philosophy that extends and simplifies the adoption by staggering the dates between large public entities and other entities. As a result of the change, the new credit loss standard, for those institutions qualifying for the delay, becomes effective for interim and annual reporting periods beginning after December 15, 2022, with early adoption permitted. The Association qualifies for the delay in the adoption date. The Association continues to evaluate the impact of adoption on the Association’s financial condition and its results of operations.

**Reclassifications.** Certain prior year amounts have been aggregated and/or reclassified to conform with the current financial statement presentation.

### Note 2: Investment Securities

#### *Held to Maturity (“HTM”)*

*Federal Agricultural Mortgage Corporation (“Farmer Mac”)* guaranteed *agricultural mortgage-backed securities (“AMBS”)* comprise the Association’s HTM investment portfolio, and the Association services the underlying loans. Additional information follows:

	AMBS				Weighted Average Yield
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	
March 31, 2020	\$ 1,464,082	\$ 51,987	\$ -	\$ 1,516,069	5.88%
December 31, 2019	1,575,855	29,154	-	1,605,009	5.88%

The Association has not experienced impairments of these securities. Farmer Mac guarantees the underlying mortgages, and the Association has the ability and intent to hold these securities to maturity or pay-off and it is unlikely the Association would be required to sell these securities. These AMBS have contractual weighted average maturities of 3.37 years as of March 31, 2020, however, expected maturities differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

## Notes to Unaudited Consolidated Financial Statements

### Available for sale (“AFS”)

The Association’s AFS investment securities consists entirely of *Small Business Administration* (“SBA”) pool securities. A summary of the amortized cost and fair value of AFS investment securities is as follows:

	SBA pool securities				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
March 31, 2020	\$75,735,850	\$ 190,432	\$ -	\$75,926,282	4.74%
December 31, 2019	80,645,058	121,558	-	80,766,616	5.00%

The following table is a summary of the contractual maturity, fair value, amortized cost and weighted average yield of AFS investments securities at March 31, 2020:

	SBA pool securities				
	Due in 1 Year or Less	Due After 1 Year Through 5 Years	Due After 5 Years Through 10 Years	Due After 10 Years	Total
Fair value	\$ -	\$ -	\$ 28,227,435	\$ 47,698,847	\$ 75,926,282
Amortized cost	-	-	28,242,894	47,492,956	75,735,850
Weighted average yield	0.00%	0.00%	5.40%	4.35%	4.74%

### Note 3: Loans and Allowance for Loan Losses (“ALL”)

**Loans.** Loan carrying amounts (outstanding principal adjusted as applicable for capitalized accrued interest, direct partial charge-offs, deferred fees or costs on originated loans, and unamortized purchase premiums and discounts; excludes uncapitalized accrued interest) by portfolio segment follows:

Loan Type	March 31, 2020		December 31, 2019	
	Amount	%	Amount	%
Real estate mortgage	\$ 1,110,682,146	56.1%	\$ 1,084,069,296	53.7%
Production and intermediate term	595,303,944	30.1%	659,679,343	32.8%
Agribusiness:				
Loans to cooperatives	11,527,105	0.6%	3,538,860	0.2%
Processing and marketing	129,384,324	6.6%	132,037,952	6.6%
Farm-related business	24,910,821	1.3%	22,600,552	1.1%
Communication	19,213,736	1.0%	19,222,731	1.0%
Energy	7,522,778	0.4%	7,271,541	0.4%
Rural residential real estate	8,020,904	0.4%	8,362,492	0.4%
Lease receivables	1,031,002	0.1%	913,850	0.0%
Mission-related investments	67,250,749	3.4%	76,006,745	3.8%
Total	<u>\$ 1,974,847,509</u>	<u>100.0%</u>	<u>\$ 2,013,703,362</u>	<u>100.0%</u>

Mission-related investment and real estate mortgage loans purchased with 100% U.S. government agency or government sponsored enterprise guarantees present essentially no credit risk other than purchase premiums, which are forfeited when borrowers prepay or refinance their loans before the premiums are fully amortized. Management anticipates and considers potential prepayments to estimate an appropriate amortization period. Net purchased premiums included in the mission-related investment and real estate mortgage loan balances above as of March 31, 2020 and December 31, 2019, follow:

## Notes to Unaudited Consolidated Financial Statements

	March 31, 2020	December 31, 2019
Real estate mortgage	\$ 6,319,747	\$ 6,559,731
Mission-related investments	1,337,606	1,238,501
Total premium	\$ 7,657,353	\$ 7,798,232

The Association may purchase or sell participations in loans to diversify risk, manage loan volume, and comply with FCA regulations. Participation carrying amount details as of March 31, 2020 follow:

	Other Farm Credit Institutions		Non-Farm Credit Institutions		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
	Real estate mortgage	\$ 70,311,887	\$ 242,153,918	\$ 174,851,851	\$ 2,515,512	\$ 245,163,738
Production and intermediate term	45,441,166	343,457,440	-	-	45,441,166	343,457,440
Agribusiness	109,268,021	40,566,821	-	-	109,268,021	40,566,821
Communication	19,213,736	-	-	-	19,213,736	-
Energy	7,522,778	-	-	-	7,522,778	-
Lease receivables	1,031,002	-	-	-	1,031,002	-
Total	\$ 252,788,590	\$ 626,178,179	\$ 174,851,851	\$ 2,515,512	\$ 427,640,441	\$ 628,693,691

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 \$25,481,912 and \$26,801,404 at March 31, 2020 and December 31, 2019, respectively.

**Credit Quality.** Loans are the Association’s primary asset. Collectability of these assets is critical to the Association’s financial position and results of operations. Collectability is primarily a function of credit quality.

Loans that have not performed in accordance with terms demonstrate heightened credit risk, and the level and trends in non-performing loans is a strong indicator of credit quality. Non-performing loans and *other property owned* (“OPO”) comprise non-performing assets.

The recorded investment in a loan, as defined by GAAP, includes the outstanding principal adjusted, as applicable, for accrued interest, direct partial charge-offs, deferred fees or costs on originated loans, and unamortized purchase premiums and discounts; the recorded investment in a loan does not include an allocation of the ALL or any specific valuation adjustments. The recorded investment in non-performing asset balances by loan portfolio segment and OPO follow:

## Notes to Unaudited Consolidated Financial Statements

	March 31, 2020	December 31, 2019
<b>Nonaccrual loans:</b>		
Real estate mortgage	\$ 3,814,987	\$ 3,587,809
Production and intermediate term	3,186,132	2,955,200
Agribusiness	32,624	35,624
Rural residential real estate	180,603	-
Mission-related investments	1,114,194	1,144,194
Total nonaccrual loans	<u>8,328,540</u>	<u>7,722,827</u>
<b>Accruing restructured loans:</b>		
Real estate mortgage	17,014,967	17,016,301
Production and intermediate term	884,209	908,620
Total accruing restructured loans	<u>17,899,176</u>	<u>17,924,921</u>
<b>Accruing loans 90 days or more past due:</b>		
Real estate mortgage	930,216	-
Mission-related investments	206,316	-
Total accruing loans 90 days or more past due	<u>1,136,532</u>	<u>-</u>
Total non-performing loans	27,364,248	25,647,748
Other property owned	-	-
Total non-performing assets	<u>\$ 27,364,248</u>	<u>\$ 25,647,748</u>

Age analysis of the recorded investment (including accrued interest) in past due loans by loan segment follows:

March 31, 2020	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	\$ 10,548,412	\$ 2,070,686	\$ 12,619,098	\$ 1,110,839,527	\$ 1,123,458,625	\$ 930,516
Production and intermediate-term	15,991,798	876,199	16,867,997	585,094,419	601,962,416	-
Loans to cooperatives	-	-	-	11,542,410	11,542,410	-
Processing and marketing	-	-	-	129,983,782	129,983,782	-
Farm-related business	603,651	32,624	636,275	24,404,462	25,040,737	-
Communication	-	-	-	19,223,741	19,223,741	-
Energy	-	-	-	7,546,837	7,546,837	-
Rural residential real estate	-	180,603	180,603	7,872,544	8,053,147	-
Lease receivables	-	-	-	1,034,693	1,034,693	-
Mission-related investments	-	1,320,510	1,320,510	66,450,835	67,771,345	206,316
Total	<u>\$ 27,143,861</u>	<u>\$ 4,480,622</u>	<u>\$ 31,624,483</u>	<u>\$ 1,963,993,250</u>	<u>\$ 1,995,617,733</u>	<u>\$ 1,136,832</u>



## Notes to Unaudited Consolidated Financial Statements

December 31, 2019	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	\$ 2,308,279	\$ 1,141,591	\$ 3,449,870	\$ 1,094,886,611	\$ 1,098,336,481	\$ -
Production and intermediate-term	2,186,443	1,122,026	3,308,469	665,192,865	668,501,334	-
Loans to cooperatives	-	-	-	3,540,043	3,540,043	-
Processing and marketing	-	-	-	132,738,468	132,738,468	-
Farm-related business	-	35,624	35,624	22,630,461	22,666,085	-
Communication	-	-	-	19,224,171	19,224,171	-
Energy	-	-	-	7,295,894	7,295,894	-
Rural residential real estate	-	-	-	8,389,729	8,389,729	-
Lease receivables	-	-	-	917,007	917,007	-
Mission-related investments	1,044,151	1,055,186	2,099,337	74,439,121	76,538,458	-
Total	\$ 5,538,873	\$ 3,354,427	\$ 8,893,300	\$ 2,029,254,370	\$ 2,038,147,670	\$ -

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

Management has rated each loan in the portfolio using the System's 14-point rating system. These aggregated classifications are a significant indicator of credit quality. The classification 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 and/or collateral pledged on the loan;
- Doubtful – assets exhibit similar weaknesses to substandard assets; however, doubtful assets have additional weaknesses in existing factors, conditions and values that make collection in full highly questionable; and
- Loss – assets are considered uncollectible.

## Notes to Unaudited Consolidated Financial Statements

The following table presents the Association's loan portfolio segment balances, including accrued interest thereon, as a percentage of the total category, as classified by management and aggregated under the FCA's Uniform Loan Classification System:

	<u>March 31, 2020</u>	<u>December 31, 2019</u>
Real estate mortgage		
Acceptable	95.9%	95.9%
OAEM	2.2%	2.2%
Substandard/doubtful	1.9%	1.9%
	<u>100.0%</u>	<u>100.0%</u>
Production and intermediate term		
Acceptable	91.5%	91.9%
OAEM	4.5%	3.8%
Substandard/doubtful	4.1%	4.3%
	<u>100.0%</u>	<u>100.0%</u>
Loans to cooperatives		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Processing and marketing		
Acceptable	85.1%	86.4%
OAEM	14.9%	13.6%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Farm-related business		
Acceptable	99.9%	99.8%
OAEM	0.0%	0.0%
Substandard/doubtful	0.1%	0.2%
	<u>100.0%</u>	<u>100.0%</u>
Communication		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Energy		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Rural residential real estate		
Acceptable	97.8%	97.8%
OAEM	0.0%	2.2%
Substandard/doubtful	2.2%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Lease receivables		
Acceptable	100.0%	100.0%
OAEM	0.0%	0.0%
Substandard/doubtful	0.0%	0.0%
	<u>100.0%</u>	<u>100.0%</u>
Mission-related investments		
Acceptable	98.3%	98.5%
OAEM	0.0%	0.0%
Substandard/doubtful	1.7%	1.5%
	<u>100.0%</u>	<u>100.0%</u>
Total Loans		
Acceptable	94.1%	94.1%
OAEM	3.5%	3.4%
Substandard/doubtful	2.4%	2.5%
	<u>100.0%</u>	<u>100.0%</u>

## Notes to Unaudited Consolidated Financial Statements

Based on current information and events, management has determined it is probable that scheduled payments of principal or interest on the following loans will not be collected when due according to the contractual terms of the loan agreements and has classified these loans as impaired. Once classified as impaired, management then determines the amount of impairment, if any, on each individual impaired loan; aggregated impairment on individual impaired loans is included in management's estimate of an appropriate ALL at each reporting date.

Impaired loan information, by loan portfolio segment, follows:

	March 31, 2020			December 31, 2019		
	Recorded Investment	Unpaid Principal Balance <sup>a</sup>	Related Allowance	Recorded Investment	Unpaid Principal Balance <sup>a</sup>	Related Allowance
Impaired loans with a related allowance for credit losses:						
Real estate mortgage	\$ 1,081,478	\$ 1,329,769	\$ 172,000	\$ 1,081,478	\$ 1,329,769	\$ 172,000
Production and intermediate term	1,083,237	1,106,847	674,800	1,102,911	1,126,521	636,800
Farm-related business	-	-	-	-	-	-
Mission-related investments	-	-	-	-	-	-
Total	\$ 2,164,715	\$ 2,436,616	\$ 846,800	\$ 2,184,389	\$ 2,456,290	\$ 808,800
Impaired loans with no related allowance for credit losses:						
Real estate mortgage	\$20,678,692	\$21,794,215	\$ -	\$ 19,522,632	\$ 20,700,734	\$ -
Production and intermediate term	2,987,104	8,570,778	-	2,760,909	8,675,203	-
Farm-related business	32,624	32,624	-	35,624	35,624	-
Rural residential real estate	180,603	180,603	-	-	-	-
Mission-related investments	1,320,510	1,315,519	-	1,144,194	1,144,194	-
Total	\$25,199,533	\$31,893,739	\$ -	\$ 23,463,359	\$ 30,555,755	\$ -
Total impaired loans:						
Real estate mortgage	\$21,760,170	\$23,123,984	\$ 172,000	\$ 20,604,110	\$ 22,030,503	\$ 172,000
Production and intermediate term	4,070,341	9,677,625	674,800	3,863,820	9,801,724	636,800
Farm-related business	32,624	32,624	-	35,624	35,624	-
Rural residential real estate	180,603	180,603	-	-	-	-
Mission-related investments	1,320,510	1,315,519	-	1,144,194	1,144,194	-
Total	\$27,364,248	\$34,330,355	\$ 846,800	\$25,647,748	\$33,012,045	\$ 808,800

## Notes to Unaudited Consolidated Financial Statements

	For the three months ended March 31, 2020		For the three months ended March 31, 2019		For the Year Ended December 31, 2019	
	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized	Average Impaired Loans	Interest Income Recognized
Impaired loans with a related allowance for credit losses:						
Real estate mortgage	\$ 1,081,478	\$ -	\$ 2,793,748	\$ -	\$ 1,265,758	\$ -
Production and intermediate term		-	25,673	-	749,737	5,194
Farm-related business	1,096,921	-	123,847	-	-	-
Mission-related investments	-	-	-	-	-	-
Total	<u>\$ 2,178,399</u>	<u>\$ -</u>	<u>\$ 2,943,268</u>	<u>\$ -</u>	<u>\$ 2,015,495</u>	<u>\$ 5,194</u>
Impaired loans with no related allowance for credit losses:						
Real estate mortgage	\$20,120,874	\$ 246,075	\$ 8,293,049	\$ 6,911	\$18,693,048	\$ 914,073
Production and intermediate term	2,683,844	31,712	2,734,782	-	2,771,003	115,768
Farm-related business	34,074	-	-	-	94,994	-
Rural residential real estate	59,646	-	-	-	-	-
Mission-related investments	1,328,706	2,214	1,240,871	-	1,177,951	5,430
Total	<u>\$24,227,144</u>	<u>\$ 280,001</u>	<u>\$12,268,702</u>	<u>\$ 6,911</u>	<u>\$22,736,996</u>	<u>\$ 1,035,271</u>
Total impaired loans:						
Real estate mortgage	\$21,202,352	\$ 246,075	\$11,086,797	\$ 6,911	\$19,958,806	\$ 914,073
Production and intermediate term	2,683,844	31,712	2,760,455	-	3,520,740	120,962
Farm-related business	1,130,995	-	123,847	-	94,994	-
Mission-related investments	1,328,706	2,214	1,240,871	-	1,177,951	5,430
Total	<u>\$26,405,543</u>	<u>\$ 280,001</u>	<u>\$15,211,970</u>	<u>\$ 6,911</u>	<u>\$24,752,491</u>	<u>\$ 1,040,465</u>

<sup>a</sup> Unpaid principal balance represents the recorded principal balance of the loan.

A restructuring of a debt constitutes a troubled debt restructuring 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. Troubled debt restructurings are undertaken in order to improve the likelihood of recovery on the loan and may include, but are not limited to, forgiveness of principal or interest, interest rate reductions that are lower than the current market rate for new debt with similar risk, or significant term or payment extensions.

The following table provides additional information on troubled debt restructurings that occurred in the three months ended March 31, 2019. There were no troubled debt restructurings that occurred in the three months ended March 31, 2020. The premodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end prior to the restructuring. The postmodification outstanding recorded investment represents the recorded investment of the loans as of the quarter end the restructuring occurred.

For the three months ended March 31, 2020	Premodification Outstanding Recorded Investment	Postmodification Outstanding Recorded Investment
Troubled debt restructurings:		
Production and intermediate term	<u>\$ 955,501</u>	<u>\$ 1,003,918</u>

As of March 31, 2020, the total recorded investment of troubled debt restructured loans was \$19,960,904, of which \$2,061,728 was classified as nonaccrual, with specific allowance for loan losses of \$0. Commitments to lend funds to borrowers whose loan terms have been modified in a troubled debt restructuring were \$0 at March 31, 2020 and \$0 at December 31, 2019.

## Notes to Unaudited Consolidated Financial Statements

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:

	Loans Modified as TDRs		TDRs in Nonaccrual Status*	
	March 31, 2020	December 31, 2019	March 31, 2020	December 31, 2019
Real estate mortgage	\$ 17,014,967	\$ 17,016,301	\$ -	\$ -
Production and intermediate term	1,888,127	908,620	1,003,918	-
Farm-related business	32,624	35,624	32,624	35,624
Mission-related investments	1,025,186	1,055,186	1,025,186	1,055,186
Total	<u>\$ 19,960,904</u>	<u>\$ 19,015,731</u>	<u>\$ 2,061,728</u>	<u>\$ 1,090,810</u>

\*represents the portion of loans modified as TDRs that are in nonaccrual status

The predominant form of concession granted for troubled debt restructuring includes modifications to extend the term and delay payments. At times, these terms might be offset with incremental payments, collateral or new borrower guarantees, in which case management assesses all of the modified terms to determine if the overall modification qualifies as a troubled debt restructuring.

There were no loans that met the accounting criteria as a troubled debt restructuring and that occurred within the previous 12 months for which there was a subsequent payment default during the period. A payment default is defined as a payment that is 30 days past due after the date the loan was restructured.

**Allowance for Loan Losses (“ALL”).** A summary of changes in ALL and period end recorded investment in loans is as follows:

	Real Estate Mortgage	Production and Intermediate Term	Agri- business	Commun- ication	Energy	Rural Residential Real Estate	Lease Receivable	Mission- Related Investments	Total
<b>Allowance for Credit Losses:</b>									
Balance at									
December 31, 2019	\$ 1,525,554	\$ 3,748,407	\$ 730,161	\$ 38,983	\$ 18,383	\$ 7,676	\$ 4,170	\$ 954	\$ 6,074,288
Charge-offs	(125)	(625,000)	-	-	-	-	-	-	(625,125)
Recoveries	-	958,559	-	-	-	-	-	-	958,559
Provision for loan losses	20,805	(152,159)	(2,277)	(1,024)	(46)	(371)	524	(25)	(134,573)
Other	1,855	(369,796)	21,599	74	1,613	43	-	-	(344,612)
Balance at									
March 31, 2020	<u>\$ 1,548,089</u>	<u>\$ 3,560,011</u>	<u>\$ 749,483</u>	<u>\$ 38,033</u>	<u>\$ 19,950</u>	<u>\$ 7,348</u>	<u>\$ 4,694</u>	<u>\$ 929</u>	<u>\$ 5,928,537</u>
Ending Balance:									
Individually evaluated for impairment	\$ 172,000	\$ 674,800	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 846,800
Collectively evaluated for impairment	\$ 1,376,089	\$ 2,885,211	\$ 749,483	\$ 38,033	\$ 19,950	\$ 7,348	\$ 4,694	\$ 929	\$ 5,081,737
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Recorded Investment in Loans Outstanding:</b>									
Ending Balance at									
March 31, 2020	\$ 1,123,458,625	\$ 601,962,416	\$ 166,566,929	\$ 19,223,741	\$ 7,546,837	\$ 8,053,147	\$ 1,034,693	\$ 67,771,345	\$ 1,995,617,733
Individually evaluated for impairment	\$ 21,760,170	\$ 4,070,341	\$ 32,624	\$ -	\$ -	\$ 180,603	\$ -	\$ 1,320,510	\$ 27,364,248
Collectively evaluated for impairment	\$ 1,101,698,455	\$ 597,892,075	\$ 166,534,305	\$ 19,223,741	\$ 7,546,837	\$ 7,872,544	\$ 1,034,693	\$ 66,450,835	\$ 1,968,253,485
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

## Notes to Unaudited Consolidated Financial Statements

	Real Estate Mortgage	Production and Intermediate Term	Agri- business	Commun- ication	Energy	Rural Residential Real Estate	Lease Receivable	Mission- Related Investments	Total
<b>Allowance for Credit Losses:</b>									
Balance at									
December 31, 2018	\$ 1,787,292	\$ 2,341,392	\$ 350,374	\$ 37,020	\$ 23,802	\$ 5,693	\$ 1,982	\$ 12,653	\$ 4,560,208
Charge-offs	-	(33,930)	-	-	-	-	-	-	(33,930)
Recoveries	12,500	274,998	-	-	-	-	-	-	287,498
Provision for loan losses	(10,747)	356,932	86,371	95	3,526	899	3	(1,580)	435,499
Other	(1,146)	(273,623)	17,291	169	(583)	75	-	-	(257,817)
Balance at									
March 31, 2019	\$ 1,787,899	\$ 2,665,769	\$ 454,036	\$ 37,284	\$ 26,745	\$ 6,667	\$ 1,985	\$ 11,073	\$ 4,991,458
Ending Balance:									
Individually evaluated for impairment	\$ 720,000	\$ 269,320	\$ 55,500	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,044,820
Collectively evaluated for impairment	\$ 1,067,899	\$ 2,396,449	\$ 398,536	\$ 37,284	\$ 26,745	\$ 6,667	\$ 1,985	\$ 11,073	\$ 3,946,638
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Recorded Investment in Loans Outstanding:</b>									
Ending Balance at									
March 31, 2019	\$ 1,066,282,831	\$ 638,436,319	\$ 138,747,322	\$ 12,233,676	\$ 6,152,363	\$ 6,426,582	\$ 553,934	\$ 74,066,017	\$ 1,942,899,044
Individually evaluated for impairment	\$ 11,080,670	\$ 2,368,454	\$ 116,624	\$ -	\$ -	\$ -	\$ -	\$ 1,180,982	\$ 14,746,730
Collectively evaluated for impairment	\$ 1,055,202,161	\$ 636,067,865	\$ 138,630,698	\$ 12,233,676	\$ 6,152,363	\$ 6,426,582	\$ 553,934	\$ 72,885,035	\$ 1,928,152,314
Acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

### Note 4: 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 institution'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 institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, 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.

## Notes to Unaudited Consolidated Financial Statements

### Regulatory Capitalization Requirements.

	Regulatory	Capital	Total	As of	As of
	Minimums	Conservation Buffer		March 31, 2020	December 31, 2019
Risk-adjusted:					
Common equity tier 1 ratio	4.50%	2.50%	7.00%	12.18%	12.16%
Tier 1 capital ratio	6.00%	2.50%	8.50%	12.18%	12.16%
Total capital ratio	8.00%	2.50%	10.50%	13.66%	13.62%
Permanent capital ratio	7.00%	0.00%	7.00%	13.31%	13.29%
Non-risk-adjusted:					
Tier 1 leverage ratio	4.00%	1.00%	5.00%	10.66%	10.41%
UREE leverage ratio	1.50%	0.00%	1.50%	10.64%	10.36%

Following are the amounts included in the calculation of the capital ratios as of March 31, 2020:

	Regulatory Capital		Risk weighted assets/ Adjusted average total assets	
	3/31/2020	12/31/2019	3/31/2020	12/31/2019
Risk-adjusted capital ratios				
Common equity tier 1 ratio	\$ 223,911,920	\$ 223,393,367	\$ 1,838,786,000	\$ 1,837,865,372
Tier 1 capital ratio	223,911,920	223,393,367	1,838,786,000	1,837,865,372
Total capital ratio	251,255,239	250,359,946	1,838,786,000	1,837,865,372
Permanent capital ratio	243,911,920	243,393,367	1,832,600,679	1,832,011,014
Non-risk-adjusted capital ratios				
Tier 1 leverage ratio	223,911,920	223,393,367	2,100,359,172	2,145,227,470
UREE leverage ratio	223,421,278	222,296,229	2,100,359,172	2,145,227,470

**Preferred stock issuance.** In January 2017, the Association received clearance from FCA and the board approved the issuance of 20 million shares of a series of preferred stock, par value of \$1.00 per share. The stock was issued March 24, 2017. The stock is designated as *Fixed-to-Floating Rate Perpetual Cumulative Preferred Stock, Series A* (“**Series A Preferred Stock**”). The Series A Preferred stock has a fixed rate dividend of 5% for ten years, payable semi-annually. After ten years, the dividend rate becomes a floating rate at 5.00% above 6-month LIBOR. On or after 5 years, the Association may, at its option, redeem all or part of the Series A Preferred Stock. The Series A Preferred Stock is non-voting, except: (i) to materially change the Association’s Charter or Bylaws that would materially adversely affect the holder of Series A Preferred Stock, (ii) to create, issue or authorize any class of stock ranking senior to the Series A Preferred Stock as to dividends or liquidation.

### Note 5: Income taxes

The Association is subject to federal and certain other income taxes. The Association is eligible to operate as cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue code. Under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those earnings that will not be distributed as qualified patronage refunds. During 2020, the Association is participating in a patronage program. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution 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 subsidiary, AgTexas, FLCA, is exempt from federal and other income taxes as provided in the Farm Credit Act of 1971.

## Notes to Unaudited Consolidated Financial Statements

### Note 6: 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 2019 Annual Report to Stockholders for a more complete description.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

March 31, 2020	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Assets held in nonqualified benefit trusts	\$ 153,333	\$ -	\$ -	\$ 153,333
SBA pool securities	-	75,926,282	-	75,926,282
December 31, 2019	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Assets held in nonqualified benefit trusts	\$ 157,739	\$ -	\$ -	\$ 157,739
SBA pool securities	-	80,766,616	-	80,766,616

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

March 31, 2020	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Loans*	\$ -	\$ -	\$ 1,317,915	\$ 1,317,915
December 31, 2019	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Loans*	\$ -	\$ -	\$ 1,375,589	\$ 1,375,589

\*Represents the fair value of certain loans that were evaluated for impairment under authoritative guidance “*Accounting by Creditors for Impairment of a Loan*.” The fair value was based upon the underlying collateral since these were collateral-dependent loans for which real estate is the collateral.

### Information About Recurring and Nonrecurring Level 3 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 institutions 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.



## Notes to Unaudited Consolidated Financial Statements

### Information About Recurring and Nonrecurring Level 2 Fair Value Measurements

SBA pool securities are valued using a third-party pricing vendor. The Association's vendor utilizes major pricing services including Reuters and Intercontinental Exchange. The market values are based on inputs other than quoted prices, including:

- Quoted prices for similar assets in active markets
- Quoted prices for identical or similar assets in markets that are not active
- Inputs other than quoted prices, which provide a reasonable basis for fair value determination. Such inputs may include interest rates and yield curves, volatilities, prepayment speeds, credit risks and default rates.
- Inputs derived principally from observable market data.

### Valuation Techniques

As more fully discussed in note 2 to the 2019 Annual Report, 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 2019 Annual Report.

**Assets Held in Nonqualified Benefits Trusts.** Assets held in trust funds related to deferred compensation and supplemental retirement plans are classified within Level 1. The trust funds include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

**Loans Evaluated for Impairment.** For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon the underlying real estate collateral since the loans were collateral dependent. 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. The fair value of these loans would fall under Level 2 of the hierarchy if the process uses independent appraisals and other market-based information.

**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.

### Note 7: Employee Benefit Plans

**Employee Retirement Benefits.** The following table summarizes the components of net periodic benefit costs of nonpension other postretirement employee benefits for the three months ended March 31:

	2020	2019
Service cost	\$ 29,673	\$ 27,240
Interest cost	63,941	77,257
Amortization of prior service credits	(11,970)	(11,967)
Amortization of net actuarial loss	3,312	-
Net periodic benefit cost	<u>\$ 84,956</u>	<u>\$ 92,530</u>

The Association's liability for the unfunded accumulated obligation for these benefits at March 31, 2020, was \$7,572,965 and is included in "Accrued postretirement benefit liability" in 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.

## Notes to Unaudited Consolidated Financial Statements

The structure of the Association'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 contributed \$1,115,458 to the District's defined benefit pension plan in 2020. Pension plan funding expense was \$278,864 and \$447,901 for the three months ended March 31, 2020 and 2019, respectively.

### Note 8: 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 9: Accumulated Other Comprehensive Income (Loss) ("AOCI")

AOCI includes the accumulated balance of certain gains, losses or costs for which values are included in assets or liabilities on the balance sheets, but which have not yet been recognized in earnings. For the Association, these elements include unrealized gains or losses on the AFS investment securities and amortization of retirement benefit elements. The following table summarizes the changes in the components of AOCI for the three months ended March 31, 2020 and 2019.

	Total	Unrealized gain on SBA pool securities	Retirement benefit plans
AOCI at			
December 31, 2019	\$ (502,425)	\$ 121,558	\$ (623,983)
SBA pool securities:			
Net change in unrealized gains	68,874	68,874	-
Retirement benefit plans:			
Amortization of prior service credits	(11,970)	-	(11,970)
Amortization of net actuarial loss	3,312	-	3,312
AOCI at			
March 31, 2020	<u>\$ (442,209)</u>	<u>\$ 190,432</u>	<u>\$ (632,641)</u>
	Total	Unrealized gain on SBA pool securities	Retirement benefit plans
AOCI at			
December 31, 2018	\$ 105,270	\$ -	\$ 105,270
SBA pool securities:			
Net change in unrealized gains	248,238	248,238	-
Retirement benefit plans:			
Amortization of prior service credits and net actuarial loss	(11,967)	-	(11,967)
AOCI at			
March 31, 2019	<u>\$ 341,541</u>	<u>\$ 248,238</u>	<u>\$ 93,303</u>

### Note 10: Subsequent Events

Association management has evaluated subsequent events through April 29, 2020, which is the date the CFS were issued or available to be issued, with no significant events to report.