First South Farm Credit, ACA

FIRST QUARTER 2023

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CERTIFICATION

The undersigned certify that we have reviewed the March 31, 2023 quarterly report of First South Farm Credit, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.

James F. Martin III
Chairman of the Board

Gines Pérez, III
Chief Executive Officer

Sarah F. Lutz
Chief Financial Officer

May 9, 2023

First South Farm Credit, ACA

Report on Internal Control Over Financial Reporting

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

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

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of March 31, 2023. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association's management concluded that as of March 31, 2023, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association's management determined that there were no material weaknesses in the internal control over financial reporting as of March 31, 2023.

Gines Pérez, III
Chief Executive Officer

Sarah F. Lutz
Chief Financial Officer

May 9, 2023

First South Farm Credit, ACA

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

(dollars in thousands)

The following commentary reviews the financial condition and results of operations of *First South Farm Credit, ACA* (Association) for the period ended March 31, 2023. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2022 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities including poultry, soybeans, livestock and forestry. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm income in the area, somewhat reduces the level of dependency on any single commodity.

Comparison of March 31, 2023 to December 31, 2022

The gross loan volume of the Association as of March 31, 2023, was $2,873,845 as compared to $2,935,532 at December 31, 2022. Net loans outstanding at March 31, 2023, were $2,858,922 as compared to $2,914,910 at December 31, 2022. Net loans accounted for 95.67 percent of total assets at March 31, 2023, as compared to 95.20 percent of total assets at December 31, 2022.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level and credit administration remains satisfactory. Nonaccrual loans totaled $11,107 on March 31, 2023 as compared to $3,361 on December 31, 2022, an increase of $7,746.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at March 31, 2023, was $14,923 compared to $20,622 at December 31, 2022, and was considered by management to be adequate to cover possible losses. The decrease in allowance for loan losses was due to a change in accounting method that occurred during the first quarter of 2023.

RESULTS OF OPERATIONS

For the three months ended March 31, 2023

Net income for the three months ended March 31, 2023, totaled $13,776, as compared to $11,403 for the same period in 2022. The increase in net income primarily relates to an increase in net interest income due to higher loan volume and an increase in general patronage paid to the Association by AgFirst. A more detailed explanation of other changes will be discussed below.

Noninterest income for the three months ended March 31, 2023 totaled $7,582 as compared to $5,515 for the same period of 2022, an increase of $2,067. The increase is primarily the result of an increase of $1,985 in patronage refunds due to loan growth.

Noninterest expense for the three months ended March 31, 2023 increased $1,146 compared to the same period of 2022. The change is primarily attributable to an increase of $1,223 in other operating expenses, the majority of which is pension expense that fluctuates based on actuarial adjustments and changes in the investment portfolio.

The Association recorded a provision for loan loss of $359 for the three months ended March 31, 2023 compared to $250 for the same period of 2022. The Association recorded a provision for income taxes of $1 for the three months ended March 31, 2023, compared to $4 for the same period of 2022.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with the AgFirst Farm Credit Bank (Bank) through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at March 31, 2023 was $2,324,769 as compared to $2,411,438 at December 31, 2022, a decrease of $86,669. The decrease in notes payable from December 31, 2022 to March 31, 2023 is due to a decrease in gross loan volume during the period.

CAPITAL RESOURCES

Total members' equity at March 31, 2023 and December 31, 2022 was $606,625 and $590,689, respectively. Allocated and unallocated retained earnings changes reflect the impact of normal earnings and patronage payments, as well as a change in accounting method.

The capital regulations ensure that the System's capital requirements are comparable to the Basel III framework and the standardized approach that the federal banking regulatory agencies have adopted. Regulatory ratios include common equity tier 1 (CETI) capital, tier 1 capital, and total regulatory capital risk-based ratios. The regulations also include a tier 1 leverage ratio which includes an unallocated retained earnings (URE) and URE equivalents (UREE) component. The permanent capital ratio (PCR) remains in effect.

The Association's regulatory ratios are shown in the following table:

Ratio	Minimum Requirement with Capital Conservation Buffer	Capital Ratios as of March 31, 2023	Capital Ratios as of December 31, 2022
Risk-adjusted ratios:			
CET1 Capital	7.00%	17.57%	16.81%
Tier 1 Capital	8.50%	17.57%	16.81%
Total Capital	10.50%	18.06%	17.47%
Permanent Capital Ratio	7.00%	17.70%	16.97%
Non-risk-adjusted:			
Tier 1 Leverage Ratio	5.00%	18.30%	17.41%
UREE Leverage Ratio	1.50%	12.22%	11.47%

If the capital ratios fall below the minimum regulatory requirements, including the buffer amounts, capital distributions (equity redemptions, dividends, and patronage) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval.

LIBOR Transition

The Association has exposure to LIBOR arising from loans made to customers, investments, and Systemwide Debt Securities that are issued by the Funding Corporation on the Bank's and Association's behalf.

The FCA has issued guidelines with similar guidance as the U.S. prudential regulators but applicable for System institutions to follow as they prepare for the expected phase-out of LIBOR. The guidelines direct each System institution to develop a LIBOR transition plan designed to provide an orderly roadmap of actions that will reduce LIBOR exposure, stop the inflow of new LIBOR volume, and adjust operating processes to implement alternative reference rates.

The Association has implemented LIBOR transition plans and continues to analyze potential risks associated with the LIBOR transition, including, but not limited to, financial, market, accounting, operational, legal, tax, reputational, and compliance risks. See the Association's 2022 Annual Report for further discussion on the LIBOR transition.

The following is a summary of outstanding variable-rate financial instruments tied to LIBOR at March 31, 2023:

dollars in millions)	Due in 2022	Due in 2023 and Thereafter	Total
Loans	$ –	$ 23,413	$ 23,413
Total	$ –	$ 23,413	$ 23,413
Note Payable to AgFirst Farm Credit Bank	$ –	$ 19,178	$ 19,178
Total	$ –	$ 19,178	$ 19,178

The LIBOR transition plan includes implementing fallback language into variable-rate financial instruments maturing after June 30, 2023 which provides the ability to move these instruments to another index if the LIBOR market is no longer viable.

REGULATORY MATTERS

On April 14, 2022, the FCA approved a final rule that amends certain regulations to address changes in accounting principles generally accepted in the United States. Such changes reflect the Current Expected Credit Losses (CECL) methodology that replaced the incurred loss methodology upon adoption. Credit loss allowances related to loans, lessor's net investments in leases, and held-to-maturity debt securities are included in a System institution's Tier 2 capital up to 1.25 percent of the System institution's total risk weighted assets. Credit loss allowances for available-for-sale debt securities and purchased credit impaired assets are not eligible for inclusion in a System institution's Tier 2 capital. The regulation did not include a transition phase-in period for the CECL day 1 cumulative effect adjustment to retained earnings on a System institution's regulatory capital ratios. In addition, the regulation did not include an exclusion for the CECL day 1 cumulative effective adjustment from the "safe harbor" deemed prior approval provision. The final rule became effective on January 1, 2023.

On August 26, 2021, the FCA issued a proposed rule to revise its regulatory capital requirements to define and establish risk-weightings for High Volatility Commercial Real Estate (HVCRE) by assigning a 150 percent risk-weighting to such exposures, instead of the current 100 percent. The proposed rule would ensure that the FCA's rule remains comparable with the capital rule of other federal banking regulatory agencies and recognizes the increased risk posed by HVCRE exposures. The public comment period ended on January 24, 2022.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1, *Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements*, in the Notes to the Financial Statements, and the 2022 Annual Report to Shareholders for recently adopted accounting pronouncements.

There were no ASUs issued by the Financial Accounting Standards Board (FASB) during the quarter that impacted the Association's Financial Statements.

SHAREHOLDER INVESTMENT

Shareholder investment in the Association could be materially affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst Farm Credit Bank's Quarterly and Annual Reports are on the AgFirst website, *www.agfirst.com*, or may be obtained at no charge by calling 1-800-845-1745, extension 2764, or writing Matthew Miller, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Copies of the Association's Annual and Quarterly reports are also on the Association's website, *www.firstsouthfarmcredit.com*, or may be obtained upon request free of charge by calling 1-800-955-1722 or writing Sarah Lutz, First South Farm Credit, ACA, 574 Highland Colony Parkway, Three Paragon Centre, Suite 100, Ridgeland, MS 39157. The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

First South Farm Credit, ACA

Consolidated Balance Sheets

(dollars in thousands)	**March 31, 2023**	**December 31, 2022**
	(unaudited)	*(audited)*
Assets		
Cash	**$ 133**	$ 125
Loans	**2,873,845**	2,935,532
Allowance for loan losses	**(14,923)**	(20,622)
Net loans	**2,858,922**	2,914,910
Accrued interest receivable	**24,338**	26,107
Equity investments in other Farm Credit institutions	**79,041**	79,041
Premises and equipment, net	**18,241**	18,251
Other property owned	**35**	35
Accounts receivable	**6,472**	22,179
Other assets	**1,152**	1,224
Total assets	**$ 2,988,334**	$ 3,061,872
Liabilities		
Notes payable to AgFirst Farm Credit Bank	**$ 2,324,769**	$ 2,411,438
Accrued interest payable	**6,165**	6,329
Patronage refunds payable	**116**	21,048
Accounts payable	**3,136**	7,024
Other liabilities	**47,523**	25,344
Total liabilities	**2,381,709**	2,471,183
Commitments and contingencies (Note 8)		
Members' Equity		
Capital stock and participation certificates	**52,544**	52,613
Retained earnings		
Allocated	**256,357**	256,357
Unallocated	**310,777**	294,889
Accumulated other comprehensive income (loss)	**(13,053)**	(13,170)
Total members' equity	**606,625**	590,689
Total liabilities and members' equity	**$ 2,988,334**	$ 3,061,872

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

First South Farm Credit, ACA

Consolidated Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the Three Months Ended March 31, 2023	2022
Interest Income		
Loans	**$ 35,876**	$ 29,530
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	**17,683**	12,895
Net interest income	**18,193**	16,635
Provision for credit losses	**359**	250
Net interest income after provision for credit losses	**17,834**	16,385
Noninterest Income		
Loan fees	**932**	1,158
Fees for financially related services	**34**	33
Patronage refunds from other Farm Credit institutions	**6,234**	4,249
Gains (losses) on sales of premises and equipment, net	**376**	75
Other noninterest income	**6**	—
Total noninterest income	**7,582**	5,515
Noninterest Expense		
Salaries and employee benefits	**7,601**	7,596
Occupancy and equipment	**484**	447
Insurance Fund premiums	**1,005**	847
Purchased services	**141**	409
Data processing	**108**	107
Other operating expenses	**2,300**	1,077
(Gains) losses on other property owned, net	**—**	10
Total noninterest expense	**11,639**	10,493
Income before income taxes	**13,777**	11,407
Provision for income taxes	**1**	4
Net income	**$ 13,776**	$ 11,403
Other comprehensive income net of tax		
Employee benefit plans adjustments	**117**	81
Comprehensive income	**$ 13,893**	$ 11,484

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

First South Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2021	$ 53,098	$ 256,357	$ 248,756	$ (15,257)	$ 542,954
Comprehensive income			11,403	81	11,484
Capital stock/participation certificates issued/(retired), net	184				184
Balance at March 31, 2022	$ 53,282	$ 256,357	$ 260,159	$ (15,176)	$ 554,622
Balance at December 31, 2022	**$ 52,613**	**$ 256,357**	**$ 294,889**	**$ (13,170)**	**$ 590,689**
Cumulative effect of change in accounting principle			**5,570**		**5,570**
Comprehensive income			**13,776**	**117**	**13,893**
Capital stock/participation certificates issued/(retired), net	**(69)**				**(69)**
Patronage distribution adjustment			**(3,458)**		**(3,458)**
Balance at March 31, 2023	**$ 52,544**	**$ 256,357**	**$ 310,777**	**$ (13,053)**	**$ 606,625**

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

First South Farm Credit, ACA

Notes to the Consolidated Financial Statements

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

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

Organization

The accompanying financial statements include the accounts of First South Farm Credit, ACA and its Production Credit Association (PCA) and Federal Land Credit Association (FLCA) subsidiaries (collectively, the Association). A description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations for the Association as of and for the year ended December 31, 2022, are contained in the 2022 Annual Report to Shareholders. These unaudited interim consolidated financial statements should be read in conjunction with the latest Annual Report to Shareholders.

Basis of Presentation

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

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

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

Significant Accounting Policies

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

Management has made significant estimates in several areas, including loans and allowance for credit losses (Note 2, *Loans and Allowance for Credit Losses*) and financial instruments (Note 6, *Fair Value Measurement*). Actual results could differ from those estimates.

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

Accounting Standards Effective During the Period

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 current expected credit losses (CECL) 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	$ 20,622	$ (5,930)	$ 14,692
Liabilities:			
Allowance for credit losses on unfunded commitments	$ –	$ 360	$ 360
Retained earnings:			
Unallocated retained earnings	$ 294,889	$ 5,570	$ 300,459

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 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 ACL (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 repayment 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 Association 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 Consolidated Balance Sheets. 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 an entity to measure the expected credit losses based on fair value of the collateral at the reporting date when the entity 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 loss 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 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 Consolidated Balance Sheets in Other Liabilities, and
- (if applicable) 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 Consolidated Balance Sheets.

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 Association 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 or on collateral valuations prepared by in-house appraisers. 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 for loans 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 Association's macroeconomic forecast includes a weighted selection of the Moody's baseline, upside 10th percent and downside 90th percent over reasonable and supportable forecast periods of three years. Subsequent to the forecast period, the Association reverts to long run historical loss experience beyond two years gradually after the determined forecast horizon using a transition function to inform the estimate of losses for the remaining contractual life of the loan portfolio.

The economic forecasts incorporate macroeconomic variables, including unemployment rates, Dow Jones Total Stock Market Index and corporate bond spreads. 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 were 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 allowance for loan losses, which included, but were 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 Association evaluates the need for an allowance for credit losses on unfunded commitments under CECL and, if required, an amount is recognized and included in Other Liabilities on the Consolidated Balance Sheets. 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 is recorded for commitments that are unconditionally cancellable.

Note 2 — Loans and Allowance for Credit Losses

A summary of loans outstanding at period end follows:

	March 31, 2023	December 31, 2022
Real estate mortgage	$ 2,348,042	$ 2,359,912
Production and intermediate-term	386,704	424,215
Agribusiness:		
Loans to cooperatives	8,384	5,564
Processing and marketing	75,258	88,401
Farm-related business	21,700	23,992
Rural infrastructure:		
Communication	10,353	10,377
Power and water/waste disposal	3,420	3,420
Rural residential real estate	19,984	19,651
Total loans	$ 2,873,845	$ 2,935,532

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

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

	March 31, 2023							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 13,573	$ 9,389	$ –	$ –	$ 7,798	$ –	$ 21,371	$ 9,389
Production and intermediate-term	11,096	745,443	125	–	152	–	11,373	745,443
Agribusiness	37,749	23,001	41	1,435	13,910	–	51,700	24,436
Rural infrastructure	13,806	–	–	–	–	–	13,806	–
Rural residential real estate	–	–	–	–	35	–	35	–
Total	$ 76,224	$ 777,833	$ 166	$ 1,435	$ 21,895	$ –	$ 98,285	$ 779,268

	December 31, 2022							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 12,600	$ 9,389	$ –	$ –	$ 8,257	$ –	$ 20,857	$ 9,389
Production and intermediate-term	11,043	749,851	126	–	156	–	11,325	749,851
Agribusiness	32,399	23,899	9,292	2,736	16,739	–	58,430	26,635
Rural infrastructure	13,833	–	–	–	–	–	13,833	–
Rural residential real estate	–	–	–	–	35	–	35	–
Total	$ 69,875	$ 783,139	$ 9,418	$ 2,736	$ 25,187	$ –	$ 104,480	$ 785,875

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

	March 31, 2023	December 31, 2022*
Real estate mortgage:		
Acceptable	98.05%	98.19%
OAEM	1.26	1.30
Substandard/doubtful/loss	0.69	0.51
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	94.53%	94.90%
OAEM	3.25	3.62
Substandard/doubtful/loss	2.22	1.48
	100.00%	100.00%
Agribusiness:		
Acceptable	99.12%	99.19%
OAEM	–	0.81
Substandard/doubtful/loss	0.88	–
	100.00%	100.00%
Rural infrastructure:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Rural residential real estate:		
Acceptable	99.21%	99.18%
OAEM	0.18	0.18
Substandard/doubtful/loss	0.61	0.64
	100.00%	100.00%
Total loans:		
Acceptable	97.63%	97.77%
OAEM	1.47	1.60
Substandard/doubtful/loss	0.90	0.63
	100.00%	100.00%

**Prior to adoption of CECL on January 1, 2023, loans were presented with accrued interest receivable.*

Accrued interest receivable on loans of $24,338 and $26,107 at March 31, 2023 and December 31, 2022, respectively, has been excluded from the amortized cost of loans and reported separately in the Consolidated Balance Sheets.

The following table provides an aging analysis of past due loans as of:

	March 31, 2023					
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	90 Days or More Past Due and Accruing
Real estate mortgage	$ 5,619	$ 2,427	$ 8,046	$ 2,339,996	$ 2,348,042	$ –
Production and intermediate-term	1,095	1,153	2,248	384,456	386,704	–
Agribusiness	18	–	18	105,324	105,342	–
Rural infrastructure	–	–	–	13,773	13,773	–
Rural residential real estate	–	–	–	19,984	19,984	–
Total	$ 6,732	$ 3,580	10,312	$ 2,863,533	$ 2,873,845	$ –

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

	December 31, 2022					
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans	90 Days or More Past Due and Accruing
Real estate mortgage	$ 7,210	$ 781	$ 7,991	$ 2,371,111	$ 2,379,102	$ –
Production and intermediate-term	1,277	272	1,549	428,491	430,040	5
Agribusiness	959	–	959	117,999	118,958	–
Rural infrastructure	–	–	–	13,803	13,803	–
Rural residential real estate	19	–	19	19,717	19,736	–
Total	$ 9,465	$ 1,053	$ 10,518	$ 2,951,121	$ 2,961,639	$ 5

The following tables reflect nonperforming assets and related credit quality statistics as of:

	March 31, 2023
Nonaccrual loans:	
Real estate mortgage	$ 5,756
Production and intermediate-term	4,421
Agribusiness	930
Total	$ 11,107
Accruing loans 90 days or more past due:	
Total	$ –
Total nonperforming loans	$ 11,107
Other property owned	35
Total nonperforming assets	$ 11,142
Nonaccrual loans as a percentage of total loans	0.39%
Nonperforming assets as a percentage of total loans and other property owned	0.39%
Nonperforming assets as a percentage of capital	1.84%

	December 31, 2022*
Nonaccrual loans:	
Real estate mortgage	$ 1,549
Production and intermediate-term	1,812
Total	$ 3,361
Accruing restructured loans:	
Production and intermediate-term	$ 272
Total	$ 272
Accruing loans 90 days or more past due:	
Production and intermediate-term	$ 5
Total	$ 5
Total nonperforming loans	$ 3,638
Other property owned	35
Total nonperforming assets	$ 3,673
Nonaccrual loans as a percentage of total loans	0.11%
Nonperforming assets as a percentage of total loans and other property owned	0.13%
Nonperforming assets as a percentage of capital	0.62%

**Prior to adoption of CECL, nonperforming assets included accruing restructured loans and loans were presented including accrued interest receivable.*

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

	March 31, 2023			Three Months Ended March 31, 2023
Nonaccrual loans:	**Amortized Cost with Allowance**	**Amortized Cost without Allowance**	**Total**	**Interest Income Recognized on Nonaccrual Loans**
Real estate mortgage	$ 1,672	$ 4,084	$ 5,756	$ 7
Production and intermediate-term	2,807	1,614	4,421	6
Agribusiness	930	–	930	1
Total	$ 5,409	$ 5,698	$ 11,107	$ 14

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

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness	Rural Infrastructure	Rural Residential Real Estate	Other	Total
Allowance for Loan Losses:							
Balance at December 31, 2022	$ 15,717	$ 4,025	$ 687	$ 73	$ 120	$ –	$ 20,622
Cumulative effect of a change in accounting principle	(2,788)	(2,665)	(347)	(63)	(67)	–	(5,930)
Balance at January 1, 2023	$ 12,929	$ 1,360	$ 340	$ 10	$ 53	$ –	$ 14,692
Charge-offs	–	–	–	–	–	–	–
Recoveries	–	2	–	–	–	–	2
Provision for loan losses	67	136	27	3	(4)	–	229
Balance at March 31, 2023	$ 12,996	$ 1,498	$ 367	$ 13	$ 49	$ –	$ 14,923
Allowance for Unfunded Commitments:							
Balance at December 31, 2022	$ –	$ –	$ –	$ –	$ –	$ –	$ –
Cumulative effect of a change in accounting principle	127	120	113	–	–	–	360
Balance at January 1, 2023	$ 127	$ 120	$ 113	$ –	$ –	$ –	$ 360
Provision for unfunded commitments	71	72	(13)	–	–	–	130
Balance at March 31, 2023	$ 198	$ 192	$ 100	$ –	$ –	$ –	$ 490
Total allowance for credit losses	$ 13,194	$ 1,690	$ 467	$ 13	$ 49	$ –	$ 15,413
Allowance for Loan Losses*:							
Balance at December 31, 2021	$ 15,138	$ 3,650	$ 719	$ 38	$ 119	$ –	$ 19,664
Charge-offs	–	–	–	–	–	–	–
Recoveries	–	102	–	–	–	–	102
Provision for loan losses	669	(508)	70	11	8	–	250
Balance at March 31, 2022	$ 15,807	$ 3,244	$ 789	$ 49	$ 127	$ –	$ 20,016

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

Loan modifications may be granted to borrowers experiencing financial difficulty. Qualifying disclosable modifications are one, or a combination of, principal forgiveness, interest rate reduction, or a term or payment extension. Covenant waivers and modifications of contingent acceleration clauses are not considered term extensions. Modified loans to borrowers experiencing financial difficulty and activity on these loans were not material during the three months ended March 31, 2023. There were no material commitments to lend to borrowers experiencing financial difficulty whose loans have been modified at March 31, 2023.

The Association had no loans held for sale at March 31, 2023 and December 31, 2022.

Troubled Debt Restructurings

Prior to the adoption of updated FASB guidance on loan modifications on January 1, 2023, a restructuring of a loan constituted a troubled debt restructuring (TDR) 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, 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 TDR, these loans were included within impaired loans under nonaccrual or accruing restructured loans. There were no new TDRs that occurred during the three months ended March 31, 2022.

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

There were no TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the three months ended March 31, 2022. Payment default is defined as a payment that was thirty days or more past due.

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

	December 31, 2022*	
	Total TDRs	Nonaccrual TDRs
Real estate mortgage	$ 23	$ 23
Production and intermediate-term	643	371
Total loans	$ 666	$ 394
Additional commitments to lend	$ –	

Prior to adoption of CECL on January 1, 2023, loans were presented with accrued interest receivable.

Note 3 — Investments

Equity Investments in Other Farm Credit System Institutions

Equity investments in other Farm Credit System institutions are generally nonmarketable investments consisting of stock and participation certificates, allocated surplus, and reciprocal investments in other institutions regulated by the FCA. These investments are carried at cost and evaluated for impairment based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value.

Associations are required to maintain ownership in AgFirst (AgFirst or the Bank) in the form of Class B or Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association owned 9.59 percent of the issued stock and allocated retained earnings of the Bank as of March 31, 2023 net of any reciprocal investment. As of that date, the Bank's assets totaled $42.6 billion and shareholders' equity totaled $1.6 billion. The Bank's earnings were $70 million for the first three months of 2023. In addition, the Association held investments of $1,501 related to other Farm Credit institutions.

Note 4 — Debt

Notes Payable to AgFirst Farm Credit Bank

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

Note 5 — Members' Equity

Accumulated Other Comprehensive Income

	Changes in Accumulated Other Comprehensive Income by Component *(a)*			
	Three Months Ended March 31,			
	2023		2022	
Employee Benefit Plans:				
Balance at beginning of period	$	(13,170)	$	(15,257)
Other comprehensive income before reclassifications		–		–
Amounts reclassified from AOCI		117		81
Net current period other comprehensive income		117		81
Balance at end of period	$	(13,053)	$	(15,176)

	Reclassifications Out of Accumulated Other Comprehensive Income *(b)*				
	Three Months Ended March 31,				
	2023		2022		Income Statement Line Item
Defined Benefit Pension Plans:					
Periodic pension costs	$	(117)	$	(81)	See Note 7.
Net amounts reclassified	$	(117)	$	(81)	

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

Note 6 — Fair Value Measurement

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

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

The classifications within the fair value hierarchy are as follows:

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

Level 2 inputs include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability.

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

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

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

Fair values are estimated at each period end date for assets and liabilities measured at fair value on a recurring basis. The following tables summarize assets measured at fair value at period end.

	March 31, 2023			
	Fair Value Measurement Using			Total Fair
	Level 1	Level 2	Level 3	Value
Recurring assets				
Assets held in trust funds	$ –	$ –	$ –	$ –
Nonrecurring assets				
Nonaccrual loans	$ –	$ –	$ 3,881	$ 3,881
Other property owned	$ –	$ –	$ 39	$ 39

	December 31, 2022			
	Fair Value Measurement Using			Total Fair
	Level 1	Level 2	Level 3	Value
Recurring assets				
Assets held in trust funds	$ –	$ –	$ –	$ –
Nonrecurring assets				
Impaired loans*	$ –	$ –	$ 96	$ 96
Other property owned	$ –	$ –	$ 39	$ 39

**Prior to the adoption of CECL on January 1, 2023, the fair value of impaired loans included accruing restructured loans and loans past due 90 days and accruing.*

Valuation Techniques

Assets held in trust funds

Assets held in trust funds, related to deferred compensation plans, are classified as Level 1. The trust funds include investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

Nonaccrual loans

Fair values of nonaccrual loans are estimated to be the carrying amount of the loan less specific reserves. Certain loans evaluated for impairment under FASB guidance have fair values based upon the underlying collateral, as the loans were collateral-dependent. Specific reserves were established for these loans when the value of the collateral, less estimated cost to sell, was less than the principal balance of the loan. 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.

Other property owned

For other property owned, the fair value is generally determined using formal appraisals of each individual property. These assets are held for sale. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned. If the process uses observable market-based information, the assets are classified as Level 2. If the process requires significant input based upon management's knowledge of and judgment about current market conditions, specific issues relating to the property and other matters, the assets are classified as Level 3.

Note 7 — Employee Benefit Plans

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

	Three Months Ended March 31,	
	2023	2022
Pension	$ 266	$ (293)
401(k)	369	332
Other postretirement benefits	196	168
Total	$ 831	$ 207

Expenses in the above table are computed using allocated estimates of funding for multi-employer plans in which the Association participates. These amounts may change when a total funding amount and allocation is determined by the respective Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change contributions necessary before the next plan measurement date of December 31, 2023.

Further details regarding employee benefit plans are contained in the 2022 Annual Report to Shareholders.

Note 8 — Commitments and Contingent Liabilities

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

Note 9 — Subsequent Events

The Association evaluated subsequent events and determined there were none requiring disclosure through May 9, 2023, which was the date the financial statements were issued.