


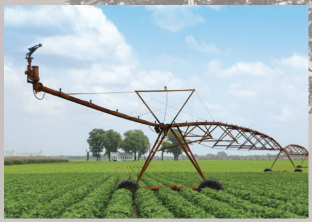

It's About GROWTH




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First South
Farm Credit

Annual Report
2018

FIRST SOUTH FARM CREDIT, ACA
2018 ANNUAL REPORT

Contents

Management

John W. Barnard........President & Chief Executive Officer
Bryan Applewhite........Senior Vice President/Chief Financial Officer/Treasurer
Sells J. Newman, Jr........Senior Vice President/Legislative Affairs/Public Relations
Gines Pérez, III........Senior Vice President/Chief Lending Officer
Randall H. Underwood........Senior Vice President/Chief Credit Officer
Rodney Brantley........President, Mississippi Division
Mike Pigg........President, Alabama Division
David Wilson........President, Louisiana Division
John Hurt........President, Capital Markets Division

Board of Directors

Michael W. Patrick........Chairman
Daniel C. Mattingly........Vice Chairman
Paul G. Briscoe........Director
John R. Burden........Director
Paul Clark........Director
Amy C. Ellender........Director
Dr. Marty J. Fuller........Director
John Ingraffia........Director
Wilson E. Judice........Director
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Timothy L. Leonard........Director
Ray Makamson........Director
Alan Marsh........Director
James F. Martin, III.........Director
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Shepherd Morris........Director
Thomas H. Nelson, Jr.........Director
James M. Norsworthy, III........Director
Thomas A. Parker........Director
Ted S. Passmore........Director
Walter R. Richardson........Director
Robert D. Thibodeaux........Director
Dan West........Director

Message from the Chief Executive Officer

On behalf of the Board of Directors, Management and Employees of First South Farm Credit, I am pleased to present the 2018 Annual Report of your Association. In 2018, we achieved our performance objectives and this continued success enabled us to again return earnings to our stockholders in the form of patronage refunds.

2018 continued to reflect sound loan growth with our average daily balance of loans increasing 5.9%. We also saw another record year of new loan production, with new loans closed reaching $271 million. The average daily balance of loans exceeded $2 billion for the first time in our history, reaching $2.07 billion at December 31, 2018.

Earnings exceeded our projections with net income of $45.1 million and we saw improvement in the quality of loan assets with acceptable loan volume at 95.1% at December 31st. Additionally, our permanent capital improved from 16.92% to 17.85%.

In keeping with our continued commitment to the cooperative principle of returning earnings to our member borrowers, our Board of Directors approved cash patronage of $17.5 million to our stockholders. This distribution will be made in April of 2019 and represents approximately 16.5% of the interest paid by our customers. It is also a record cash distribution for First South and is the 24th consecutive year that we have paid a patronage refund to our stockholders. Total patronage paid over that 24 year period is $246.8 million.

By all metrics, this was another successful year for First South and your Association is well positioned as we move forward in 2019 and beyond. In order to take advantage of the opportunities that lay ahead, we have established strategic priorities to provide direction, bring clarity, and challenge us as we plan future goals and performance objectives.

Our strategic priorities are:

- Strong Capital
- An Exceptional Customer Experience
- Operational Excellence
- Enhanced Employee Development

Our Annual Report cover has the theme “It’s About Growth”. We are continually focused on growing our loan assets and market share, but we are also focused on growing each of these strategic priorities. A strong capital position allows us to continue to grow loan volume as well as positons us to be a reliable source of credit to our member borrowers in the future. With a sound capital base we also remain in a positon to continue our commitment of returning a portion of our profits to our stockholders.

We have also made a commitment to continue to improve access to our products and services. The first step in this process was the improvement and functionality of our web site. We will launch our new web site in the first quarter of 2019. Investing in industry leading technology and increasing ease of access are essential elements for improving our customers’ experience with First South.

In 2019, we will also begin the implementation of a new credit origination platform. As a part of this implementation, we are developing processes to grow and improve our efficiency and substantially enhance our credit delivery function. The scope and scale of the project will require a great deal effort and teamwork from our employees and I am confident our people are up for the challenge.

We are also committed to the growth and development of our employees. Changes in our workforce coupled with rapidly changing technology require us to continually invest in training and employee education. A well trained workforce is an essential competitive advantage and a critical component of establishing meaningful, long lasting, and valuable relationships with our customers.

As reflected in these strategic priorities, we strive to have healthy growth and must have a willingness to continually improve. First South is fortunate to have employees who are dedicated to cooperative principles, motivated to successfully grow our business, and have the courage to embrace change.

We look forward to both the challenges and opportunities the future has in store for us. By staying focused on growing all aspects of First South and the commitment of your Board of Directors and employees, 2019 will be another successful year for your Association.

John W. Barnard
President and Chief Executive Officer

March 13, 2019

Report of Management

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

Management maintains and depends upon an internal accounting control system designed to provide reasonable assurance that transactions are properly authorized and recorded, that the financial records are reliable as the basis for the preparation of all financial statements, and that the assets of the Association are safeguarded. The design and implementation of all systems of internal control are based on judgments required to evaluate the costs of controls in relation to the expected benefits and to determine the appropriate balance between these costs and benefits. The Association maintains an internal audit program to monitor compliance with the systems of internal accounting control. Audits of the accounting records, accounting systems and internal controls are performed and internal audit reports, including appropriate recommendations for improvement, are submitted to the Board of Directors. The Consolidated Financial Statements have been audited by independent auditors, whose report appears elsewhere in this annual report. The Association is also subject to examination by the Farm Credit Administration.

The Consolidated Financial Statements, in the opinion of management, fairly present the financial condition of the Association. The undersigned certify that we have reviewed the 2018 Annual 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.

Michael W. Patrick
Chairman of the Board

John W. Barnard
Chief Executive Officer

Bryan Applewhite
Chief Financial Officer

March 13, 2019

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, to provide 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 and 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 December 31, 2018. 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 December 31, 2018, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of December 31, 2018.

John W. Barnard
Chief Executive Officer

Bryan Applewhite
Chief Financial Officer

March 13, 2019

Consolidated Five - Year Summary of Selected Financial Data

(dollars in thousands)	December 31, 2018	2017	2016	2015	2014
Balance Sheet Data					
Cash	**$ 11,502**	$ 9,097	$ 6,574	$ 5,617	$ 15,609
Loans	**2,072,774**	1,976,968	1,859,238	1,597,587	1,440,403
Allowance for loan losses	**(13,941)**	(13,618)	(12,466)	(10,637)	(10,127)
Net loans	**2,058,833**	1,963,350	1,846,772	1,586,950	1,430,276
Equity investments in other Farm Credit institutions	**67,309**	67,363	67,303	78,012	80,339
Other property owned	**2,879**	551	1,098	974	2,247
Other assets	**59,500**	57,018	51,805	48,184	55,301
Total assets	**$ 2,200,023**	$2,097,379	$ 1,973,552	$ 1,719,737	$1,583,772
Notes payable to AgFirst Farm Credit Bank*	**$ 1,717,671**	$1,639,346	$ 1,543,099	$ 1,314,927	$1,194,897
Accrued interest payable and other liabilities with maturities of less than one year	**58,652**	57,698	73,108	63,868	65,885
Total liabilities	**1,776,323**	1,697,044	1,616,207	1,378,795	1,260,782
Capital stock and participation certificates	**52,969**	54,174	56,531	58,523	60,348
Retained earnings					
Allocated	**259,012**	261,054	221,800	203,534	186,287
Unallocated	**138,687**	111,152	108,424	106,358	106,543
Accumulated other comprehensive income (loss)	**(26,968)**	(26,045)	(29,410)	(27,473)	(30,188)
Total members' equity	**423,700**	400,335	357,345	340,942	322,990
Total liabilities and members' equity	**$ 2,200,023**	$2,097,379	$ 1,973,552	$ 1,719,737	$1,583,772
Statement of Income Data					
Net interest income	**$ 54,273**	$ 51,636	$ 46,899	$ 43,884	$ 42,346
Provision for loan losses	**1,080**	1,285	1,549	1,180	1,044
Noninterest income (expense), net	**(8,087)**	8,882	(11,170)	(11,907)	239
Net income	**$ 45,106**	$ 59,233	$ 34,180	$ 30,797	$ 41,541
Key Financial Ratios					
Rate of return on average:					
Total assets	**2.12%**	2.92%	1.88%	1.87%	2.72%
Total members' equity	**10.89%**	16.00%	9.71%	9.30%	12.92%
Net interest income as a percentage of average earning assets	**2.68%**	2.67%	2.73%	2.85%	2.99%
Net (chargeoffs) recoveries to average loans	**(0.037)%**	(0.007)%	0.016%	(0.043)%	(0.007)%
Total members' equity to total assets	**19.26%**	19.09%	18.11%	19.83%	20.39%
Debt to members' equity (:1)	**4.19**	4.24	4.52	4.04	3.90
Allowance for loan losses to loans	**0.67%**	0.69%	0.67%	0.67%	0.70%
Permanent capital ratio	**17.85%**	16.92%	17.48%	17.78%	18.32%
Total surplus ratio	**	**	16.55%	17.19%	17.62%
Core surplus ratio	**	**	16.55%	16.60%	16.95%
Common equity tier 1 capital ratio	**17.50%**	16.43%	**	**	**
Tier 1 capital ratio	**17.50%**	16.43%	**	**	**
Total regulatory capital ratio	**18.29%**	17.35%	**	**	**
Tier 1 leverage ratio	**17.45%**	16.42%	**	**	**
Unallocated retained earnings (URE) and URE equivalents leverage ratio	**11.34%**	10.91%	**	**	**
Net Income Distribution					
Estimated patronage refunds:					
Cash	**$ 17,500**	$ 15,000	$ 10,700	$ 9,400	$ 11,541
Nonqualified allocated retained earnings	—	20,815	10,804	9,849	12,613
Nonqualified retained earnings	—	20,815	10,804	9,849	12,613

** General financing agreement is renewable on a one-year cycle. The next renewal date is December 31, 2019.*
*** Not applicable due to changes in regulatory capital requirements effective January 1, 2017.*

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

(dollars in thousands, except as noted)

GENERAL OVERVIEW

The following commentary summarizes the financial condition and results of operations of First South Farm Credit, ACA, (Association) for the year ended December 31, 2018 with comparisons to the years ended December 31, 2017 and December 31, 2016. This information should be read in conjunction with the Consolidated Financial Statements, Notes to the Consolidated Financial Statements and other sections in this Annual Report. The accompanying Consolidated Financial Statements were prepared under the oversight of the Audit Committee of the Board of Directors. For a list of the Audit Committee members, refer to the "Report of the Audit Committee" reflected in this Annual Report. Information in any part of this Annual Report may be incorporated by reference in answer or partial answer to any other item of the Annual Report.

The Association is an institution of the Farm Credit System (System), which was created by Congress in 1916 and has served agricultural producers for over 100 years. The System's mission is to maintain and improve the income and well-being of American farmers, ranchers, and producers or harvesters of aquatic products and farm-related businesses. The System is the largest agricultural lending organization in the United States. The System is regulated by the Farm Credit Administration, (FCA), which is an independent safety and soundness regulator.

The Association is a cooperative, which is owned by the members (also referred to throughout this Annual Report as stockholders or shareholders) served. The territory of the Association extends across a diverse agricultural region of Alabama, Louisiana and Mississippi. Refer to Note 1, *Organization and Operations*, of the Notes to the Consolidated Financial Statements for counties and parishes in the Association's territory. The Association provides credit to farmers, ranchers, rural residents, and agribusinesses. Our success begins with our extensive agricultural experience and knowledge of the market.

The Association obtains funding from AgFirst Farm Credit Bank (AgFirst or Bank). The Association is materially affected and shareholder investment in the Association could be materially affected by the financial condition and results of operations of the Bank. Copies of the Bank's Annual and Quarterly Reports are on the AgFirst website, ***www.agfirst.com,*** or may be obtained at no charge by calling 1-800-845-1745, extension 2832, or writing Susanne Caughman, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202.

Copies of the Association's Annual and Quarterly reports are also available upon request free of charge on the Association's website***, www.firstsouthland.com,*** or by calling 1-888-297-1722, or writing Bryan Applewhite, First South Farm Credit, ACA, Three Paragon Centre, Suite 100, 574 Highland Colony Parkway, Ridgeland, MS 39157. The Association prepares an electronic version of the Annual Report, within 75 days after the end of the fiscal year and distributes the Annual Reports to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly report, which is available on the internet, within 40 days after the end of each fiscal quarter, except that no report needs to be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

FORWARD LOOKING INFORMATION

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

- political, legal, regulatory and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international, and farm-related business sectors;
- weather-related, disease, and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry and the Farm Credit System, as a government-sponsored enterprise, as well as investor and rating-agency reactions to events involving other government-sponsored enterprises and other financial institutions; and
- actions taken by the Federal Reserve System in implementing monetary policy.

AGRICULTURAL OUTLOOK

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

U.S. agricultural market data and are not limited to information/data in the Association's territory.

Production agriculture is a cyclical business that is heavily influenced by commodity prices, weather, tax and trade policies, interest rates and various other factors. From 2010 through 2014, the U.S. farm sector generally experienced favorable economic conditions driven by high commodity and livestock prices and increasing farmland values. This generally fostered improved financial strength across the farm sector, with farmer working capital peaking in 2012. Working capital is defined as the amount of cash and cash convertible assets minus liabilities due to creditors within 12 months. However, since 2014, the agricultural environment has been more challenging. Currency fluctuations, large inventories and current U.S. trade policies, including the retaliatory action by other countries, have begun to adversely impact demand and prices for agricultural exports, which have reduced net farm income (a broad measure of profits) and eroded farmer working capital. Higher interest rates could exacerbate the reduction in net farm income by increasing interest expense for farmers with floating-rate loans or other liabilities that reprice periodically to current market interest rates. The following table illustrates USDA data on net farm income and farmer working capital:

	Year Ended December 31,			
(dollars in billions)	**2018***	**2017**	**2016**	**2015**
Net Farm Income	$66.295	$75.381	$61.542	$81.053
Farmer Working Capital	$49.879	$72.279	$65.197	$82.657

**Forecasted*

The substantial risk-bearing capacity, gained prior to 2015, has afforded U.S. crop producers time to transition their operations to the new environment of lower commodity prices, compressed margins and higher interest rates. Optimal input usage, adoption of cost-saving technologies, negotiation of adjustments to various business arrangements, such as rental cost of agriculture real estate, and effective use of hedging and other price risk management strategies are all critical in yielding positive net farm income for producers. Producers who are able to realize cost of production efficiencies and market their farm products effectively are most likely to adapt to the current price environment. However, if these current market conditions persist, farm sector financial strength will continue to weaken, challenging a greater number of producers who may not be able to sufficiently adjust their operations to avoid loan repayment challenges.

The February 2019 USDA forecast estimates 2018 farmers' net cash income, which is a measure of the cash income after payment of business expenses, at $95.0 billion, down $9.0 billion from 2017. The forecasted decrease in farmers' net cash income for 2018 is primarily due to an expected increase in cash expenses of $11.9 billion, led by increases in fuels/oil, interest, feed, and hired labor.

The February 2019 USDA outlook for the farm economy, as a whole, projects 2019 farmers' net cash income to increase to $97.7 billion, a $2.7 billion increase from 2018. The forecasted increase in farmers' net cash income for 2019 is primarily due to an expected decrease in cash expenses of $4.4 billion and increase in cash receipts for crops of $2.2 billion, partially offset by a decrease in direct government payments of $2.8 billion.

As estimated by the USDA in November 2018, the System's market share of farm business debt (defined as debt incurred by those involved in on-farm agricultural production) decreased slightly to 40.4 percent at December 31, 2017 (the latest available data), as compared with 40.9 percent at December 31, 2016.

While 2018 net farm income and working capital have declined, a healthy U.S. economy is expected to support domestic demand for most agricultural commodities in the foreseeable future. The primary area of risk will remain the export component of the demand for U.S. agricultural commodities, with a stronger dollar and ongoing uncertainty surrounding the future of U.S. trade policy. Major cash crops in the U.S. are projected to remain at elevated supply levels resulting from a combination of factors, including overall excellent crop conditions, tariffs and strong harvests in recent years. In addition to cash crops, pork and dairy are heavily dependent upon exports and most susceptible to foreign trade-related disruptions. The risk in the export component of the demand for U.S. agricultural commodities has been minimally mitigated by Market Facilitation Program assistance to producers impacted by retaliatory tariffs. Additionally, the revised Dairy Margin Protection Program in the 2018 Farm Bill and the new Dairy Revenue Protection Program will provide some support for dairy farmers. Mid-sized dairies, especially operations that are more highly leveraged or have high relative costs, will continue to face financial challenges at least into mid-2019.

The following table sets forth the commodity prices per bushel for certain crops, by hundredweight for hogs, milk, and beef cattle, and by pound for broilers and turkeys from December 31, 2015 to December 31, 2018:

Commodity	12/31/18	12/31/17	12/31/16	12/31/15
Hogs	$43.40	$48.60	$43.10	$42.80
Milk	$16.40	$17.20	$18.90	$17.30
Broilers	$0.51	$0.50	$0.48	$0.47
Turkeys	$0.50	$0.53	$0.74	$0.89
Corn	$3.54	$3.23	$3.32	$3.65
Soybeans	$8.57	$9.30	$9.64	$8.76
Wheat	$5.28	$4.50	$3.90	$4.75
Beef Cattle	$117.00	$118.00	$111.00	$122.00

In a prolonged period of less favorable conditions in agriculture, the Association's financial performance and credit quality measures would likely be negatively impacted. Any negative impact from these less favorable conditions should be lessened by geographic and commodity diversification and the influence of off-farm income sources supporting agricultural-related debt. However, agricultural borrowers who are more reliant on off-farm income sources may be more adversely impacted by a weakened general economy.

CRITICAL ACCOUNTING POLICIES

The financial statements are reported in conformity with accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because management must make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2, *Summary of Significant Accounting Policies*, of the Notes to the Consolidated Financial Statements. The following is a summary of certain critical policies.

- *Allowance for loan losses* — The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through allowance reversals and loan charge-offs. The allowance for loan losses is determined based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic and political conditions, loan portfolio composition, credit quality and prior loan loss experience.

  Significant individual loans are evaluated based on the borrower's overall financial condition, resources, and payment record, the prospects for support from any financially responsible guarantor, and, if appropriate, the estimated net realizable value of any collateral. The allowance for loan losses encompasses various judgments, evaluations and appraisals with respect to the loans and their underlying security that, by nature, contains elements of uncertainty and imprecision. Changes in the agricultural economy and their borrower repayment capacity will cause these various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary from the Association's expectations and predictions of those circumstances.

  Management considers the following factors in determining and supporting the levels of allowance for loan losses: the concentration of lending in agriculture, combined with uncertainties in farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences. Changes in the factors considered by management in the evaluation of losses in the loan portfolios could result in a change in the allowance for loan losses and could have a direct impact on the provision for loan losses and the results of operations.

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

- Pensions — *Single Employer Defined Benefit Plan* Certain employees depending on date of employment may participate in the First South Farm Credit, ACA Retirement Plan (the FS Plan), a defined benefit plan. The Plan is noncontributory and includes eligible Association employees. The "Projected Unit Credit" actuarial method is used for financial reporting purposes. Since the FS Plan is a single employer plan, the Association records the FS Plan's funded status and equity items related to prior service cost, accumulated other comprehensive income (loss) and prepaid (accrued) pension expense. The adjustment to other comprehensive income (loss) would be net of deferred taxes, if significant.

  The foregoing defined benefit plan is considered single employer, therefore the Association applies the provisions of FASB guidance on employers' accounting for defined benefit pension plans in its standalone financial statements.

See Note 9 for additional information. Pension expense for all plans is recorded in accordance with FASB guidance. Pension expense for the defined benefit retirement plans is determined by actuarial valuations based on certain assumptions, including expected long-term rate of return on plan assets and the discount rate. The expected return on plan assets for the year is calculated based on the composition of assets at the beginning of the year and the expected long-term rate of return on that portfolio of assets. The discount rate is used to determine the present value of our future benefit obligations. We selected the discount rate by reference to Hewitt's (a global human resources firm) top quartile rate, actuarial analyses and industry norms.

ECONOMIC CONDITIONS

Economic conditions within the Association's territory vary, depending on the sector of the economy in question. The general economy is sound, with historically low unemployment and economic growth noted across the three states. Localized stress is seen in areas where local conditions and factors adversely impact those areas, but on a broader scale, economic conditions and indicators reflect a strong economy.

Conditions vary widely within the agricultural economy. As has been the case for the past several years, prices farmers receive for grain, timber, beef cattle and dairy commodities have presented challenges to those producers as they attempt to generate profits from their operations. Poultry remains the Association's largest individual commodity financed, and conditions within that industry have remained relatively stable. The poultry segment of our portfolio continues to perform well, as does the segment reliant on non-farm income for repayment.

Credit quality remains stable and sound as the Association's borrowers have done a good job of managing the challenges they have faced. The strength of the loan portfolio leaves the Association well positioned to weather volatility and adversity in the general and agricultural economies.

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 through numerous product types. The diversification of the Association loan volume by type for each of the past three years is shown below.

Loan Type	2018		2017		2016	
Real Estate Mortgage	$ 1,617,874	78.05%	$ 1,498,148	75.78%	$ 1,433,647	77.11%
Production and Intermediate-term	375,310	18.11	383,514	19.40	344,258	18.52
Processing and marketing	38,867	1.88	62,001	3.14	47,402	2.55
Farm-related business	12,845	.62	8,561	.43	8,707	.47
Rural residential real estate	9,745	.47	9,302	.47	8,910	.48
Loans to cooperatives	7,844	.38	3,368	.17	4,209	.22
Communication	6,664	.32	8,357	.42	12,105	.65
Energy	3,625	.17	3,717	.19	–	–
Total	$ 2,072,774	100.00%	$ 1,976,968	100.00%	$ 1,859,238	100.00%

While we make loans and provide financially related services to qualified borrowers in the agricultural and rural sectors and to certain related entities, our loan portfolio is diversified.

The geographic distribution of the loan volume by state for the past three years is as follows:

	December 31,		
State	2018	2017	2016
Alabama	52.85%	51.51%	50.61%
Mississippi	28.91	29.51	30.11
Louisiana	18.24	18.98	19.28
	100.00%	100.00%	100.00%

Commodity and industry categories are based upon the Standard Industry Classification system published by the federal government. The system is used to assign commodity or industry categories based upon the largest agricultural commodity of the customer.

The major commodities in the Association loan portfolio are shown below. The predominant commodities are poultry, real estate, livestock and forestry, which constitute 74 percent of the entire portfolio.

	December 31,					
	2018		2017		2016	
Commodity Group	Amount	%	Amount	%	Amount	%
Poultry	$ 643,350	31	$ 571,994	29	$ 552,410	30
Real Estate	435,086	21	404,188	20	362,629	20
Livestock	255,357	12	240,020	12	226,685	12
Forestry	205,249	10	208,897	11	205,588	11
Soybeans	126,524	6	138,512	7	118,537	6
Cotton	121,793	6	115,080	6	91,885	5
Rice	81,848	4	75,120	4	83,204	4
Sugar Cane	64,872	3	67,826	3	64,336	4
Catfish	28,465	1	22,719	1	19,643	1
Peanuts	19,455	1	19,945	1	15,823	1
Other	90,776	5	112,667	6	118,498	6
Total	$ 2,072,774	100	$ 1,976,968	100	$ 1,859,238	100

Repayment ability is closely related to the commodities produced by our borrowers, and increasingly, the off-farm income of borrowers. The Association's loan portfolio contains a concentration of poultry, real estate, livestock and forestry producers. Although a large percentage of the loan portfolio is concentrated in these enterprises, many of these operations are diversified within their enterprise and/or with crop production that reduces overall risk exposure. Demand for beef, prices of field grains, and international trade are some of the factors affecting the price of these commodities. Even though the concentration of large loans has increased over the past several years, the agricultural enterprise mix of these loans is diversified and similar to that of the overall portfolio. The risk in the portfolio associated with commodity concentration and large loans is reduced by the range of diversity of enterprises in the Association's territory.

The increase in gross loan volume for the twelve months ended December 31, 2018, is spread across several commodities within the portfolio.

The Association's short-term portfolio, which is heavily influenced by operating-type loans, normally reaches a peak balance in August or September and rapidly declines in the fall months as commodities are marketed and proceeds are applied to repay operating loans.

Participations remain a means for the Association to spread credit concentration risk and manage our capital position. At December 31, 2018, the Association had $56,310 in loan participations sold compared to $63,228 at December 31, 2017 and $56,440 at December 31, 2016.

	December 31,		
Loan Participations:	2018	2017	2016
	(dollars in thousands)		
Participations Purchased– FCS Institutions	$ 49,216	$ 62,281	$ 41,859
Participations Purchased– Non-FCS Institutions	21,391	32,202	40,912
Participations Sold	(56,310)	(63,228)	(56,440)
Total	$ 14,297	$ 31,255	$ 26,331

The Association did not have any loans sold with recourse, retained subordinated participation interests in loans sold, or interests in pools of subordinated participation interests for the period ended December 31, 2018.

The Association sells qualified long-term mortgage loans into the secondary market. For the period ended December 31, 2018, the Association originated loans for resale into the secondary market totaling $1,355.

INVESTMENT SECURITIES

As permitted under FCA regulations, the Association is authorized to hold eligible investments for the purposes of reducing interest rate risk and managing surplus short-term funds. The Bank is responsible for approving the investment policies of the Association. The Bank annually reviews the investment portfolio of every association that it funds. At December 31, 2018, the Association had no investment securities.

CREDIT RISK MANAGEMENT

Credit risk arises from the potential inability of an obligor to meet its repayment obligation. As part of the process to evaluate the success of a loan, the Association continues to review the credit quality of the loan portfolio on an ongoing basis. With the approval of the Association Board of Directors, the Association establishes underwriting standards and lending policies that provide direction to loan officers. Underwriting standards include, among other things, an evaluation of:

- Character – borrower integrity and credit history
- Capacity – repayment capacity of the borrower based on cash flows from operations or other sources of income
- Collateral – protection for the lender in the event of default and a potential secondary source of repayment
- Capital – ability of the operation to survive unanticipated risks
- Conditions – intended use of the loan funds

The credit risk management process begins with an analysis of the borrower's credit history, repayment capacity, and financial position. Repayment capacity focuses on the borrower's ability to repay the loan based upon cash flows from operations or other sources of income, including non-farm income. As required by FCA regulations, each institution that makes loans on a collateralized basis must have collateral evaluation policies and procedures. In addition, each loan is assigned a credit risk rating based upon the underwriting standards. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses, and risks in a particular relationship.

We review the credit quality of the loan portfolio on an ongoing basis as part of our risk management practices. Each loan is classified according to the Uniform Classification System, which is used by all Farm Credit System institutions. Below are the classification definitions.

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

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

Credit Quality	2018	2017	2016
Acceptable & OAEM	98.82%	98.79%	98.90%
Substandard	1.17	1.20	1.09
Doubtful	.01	.01	.01
Loss	–	–	–
Total	100.00%	100.00%	100.00%

Nonperforming Assets

The Association's loan portfolio is divided into performing and high-risk categories. The high-risk assets, including accrued interest, are detailed below:

	December 31,		
High-risk Assets	**2018**	**2017**	**2016**
	(dollars in thousands)		
Nonaccrual loans	$ 3,750	$ 6,405	$ 6,702
Restructured loans	2,464	3,342	8,701
Accruing loans 90 days past due	–	–	–
Total high-risk loans	6,214	9,747	15,403
Other property owned	2,879	551	1,098
Total high-risk assets	$ 9,093	$ 10,298	$ 16,501
Ratios			
Nonaccrual loans to total loans	.18%	.32%	.36%
High-risk assets to total assets	.41%	.49%	.84%

Nonaccrual loans represent all loans where there is a reasonable doubt as to the collection of principal and/or future interest accruals, under the contractual terms of the loan. In substance, nonaccrual loans reflect loans where the accrual of interest has been suspended. Total high-risk assets decreased $1,205 due to a decrease in restructured loans of $878 and a decrease in nonaccrual loans of $2,655, offset by an increase in other property owned of $2,328. It must be recognized that portions of the agricultural economy remains relatively weak and the portfolio includes accounts that remain under stress. It is possible that additional loans will transition to high risk status in 2019 and the level of high risk loans is likely to fluctuate significantly throughout the year.

Of the $3,750 in nonaccrual volume at December 31, 2018, $2,056 was current compared to $2,162 and $2,251 at December 31, 2017 and 2016, respectively. Though the aforementioned nonaccrual loans had volume current as to scheduled principal and interest payments, they did not meet all regulatory requirements to be transferred into accrual status.

Loan restructuring is available to financially distressed borrowers. Restructuring of loans occurs when the Association grants a concession to a borrower based on either a court order or good faith in a borrower's ability to return to financial viability. The concessions can be in the form of a modification of terms or rates, a compromise of amounts owed, or deed in lieu of foreclosure. Other receipts of assets and/or equity to pay the loan in full or in part are also considered restructured loans. The type of alternative financing structure chosen is based on minimizing the loss incurred by both the Association and the borrower.

Allowance for Loan Losses

The allowance for loan losses at each period end was considered by Association management to be adequate to absorb probable losses existing in and inherent to its loan portfolio.

The following table presents the activity in the allowance for loan losses for the most recent three years is shown below.

Allowance for Loan Losses Activity:	Year Ended December 31, 2018	2017	2016
	(dollars in thousands)		
Balance at beginning of year	$ 13,618	$ 12,466	$ 10,637
Charge-offs:			
Real estate mortgage	(296)	(91)	(43)
Production and intermediate-term	(531)	(83)	(30)
Rural Residential Real Estate	–	–	–
Agribusiness	–	–	–
Total charge-offs	(827)	(174)	(73)
Recoveries:			
Real estate mortgage	2	28	–
Production and intermediate-term	68	13	353
Rural Residential Real Estate	–	–	–
Agribusiness	–	–	–
Total recoveries	70	41	353
Net (charge-offs) recoveries	(757)	(133)	280
Provision for (reversal of allowance for) loan losses	1,080	1,285	1,549
Balance at end of year	$ 13,941	$ 13,618	$ 12,466
Ratio of net (charge-offs) recoveries during the period to average loans outstanding during the period	(.037)	(.007)%	.016%

The allowance for loan losses by loan type for the most recent three years is as follows:

Allowance for Loan Losses by type	December 31, 2018	2017	2016
	(dollars in thousands)		
Real estate mortgage	$ 10,411	$ 9,588	$ 9,050
Production and intermediate term	3,072	3,528	2,980
Agribusiness	334	390	325
Rural residential real estate	67	50	47
Communication	37	43	64
Energy	20	19	–
Total	$ 13,941	$ 13,618	$ 12,466

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

Allowance for Loan Losses as a Percentage of:	December 31, 2018	2017	2016
Total loans	.67%	.69%	.67%
Nonperforming assets	153.32%	139.71%	80.93%
Nonaccrual loans	371.76%	212.62%	186.00%

Please refer to Note 3, *Loans and Allowance for Loan Losses*, of the Notes to the Consolidated Financial Statements, for further information concerning the allowance for loan losses.

RESULTS OF OPERATIONS

Net Interest Income

Net interest income was $54.3 million, $51.6 million and $46.9 million in 2018, 2017 and 2016, respectively. Net interest income is the difference between interest income and interest expense. Net interest income is the principal source of earnings for the Association and is impacted by volume, yields on assets and cost of debt. The effects of changes in average volume and interest rates on net interest income over the past three years are presented in the following table:

Change in Net Interest Income	Volume*	Rate	Nonaccrual Income	Total
	(dollars in thousands)			
12/31/18 - 12/31/17				
Interest income	$ 5,151	$ 4,987	$ –	$ 10,138
Interest expense	2.275	5,226	–	7,501
Change in net interest income:	$ 2,876	$ (239)	$	$ 2,637
12/31/17- 12/31/16				
Interest income	$ 8,572	$ 3,935	$ –	$ 12,507
Interest expense	3,690	4,080	–	7,770
Change in net interest income:	$ 4,882	$ (145)	$ –	$ 4,737

**Volume variances can be the result of increased/decreased loan volume or from changes in the percentage composition of assets and liabilities between periods.*

Noninterest Income

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

Noninterest Income	For the Year Ended December 31, 2018	2017	2016	Percentage Increase (Decrease) 2018/2017	2017/2016
	(dollars in thousands)				
Loan fees	$ 1,281	$ 2,595	$ 2,877	(50.64)%	(9.80)%
Fees for financially related services	1,020	1,183	1,127	(13.78)	4.97
Patronage refund from other Farm Credit Institutions	26,807	27,940	24,625	(4.06)	13.46
Gains on sales of premises and equipment, net	75	29	–	158.62	100.00
Insurance Fund refunds	1,051	–	–	100.00	–
Other noninterest income	2	–	–	100.00	–
Total noninterest income	$ 30,236	$ 31,747	$ 28,629	(4.76)%	10.89%

Total noninterest income decreased by $1,511 from 2017 to 2018 and increased $3,118 from 2016 to 2017. The main factor contributing to the decrease in 2018 and 2017 was primarily related to decreased loan fees of $1,314 and decreased patronage refunds from other Farm Credit Institutions of $1,133. Loan fees decreased in 2018 primarily related to the implementation and the recording of deferred loan fees and related deferred costs. These decreases were partially offset by an Insurance Fund refund of $1,051. The factor contributing to the increase in 2017 over 2016 was mainly related to increased patronage refunds from other Farm Credit Institutions of $3,315.

Noninterest Expense

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

Noninterest Expense	For the Year Ended December 31, 2018	2017	2016	Percentage Increase/(Decrease) 2018/2017	2017/2016
	(dollars in thousands)				
Salaries and employee benefits	$ 22,124	$ 22,078	$ 21,955	.21%	.56%
Postretirement benefits	4,450	(11,157)	5,696	139.89	(295.87)
Occupancy and equipment	2,045	1,784	1,749	14.63	2.00
Insurance Fund premiums	1,384	2,204	2,211	(37.21)	(.32)
Losses on other property owned, net	111	82	109	35.37	(24.77)
Other operating expenses	8,231	7,758	8,024	6.10	(3.32)
Total noninterest expense	$ 38,345	$ 22,749	$ 39,744	68.56%	(42.76)%

Noninterest expenses increased overall by $15,596 in 2018 compared to 2017. Postretirement benefits increased by $15,607 in 2018 due to a change in accounting estimate from the prior year. (See next paragraph for further explanation). Insurance Fund premiums decreased $820 in 2018 as compared to 2017. The above decrease was partially offset by increases other operating expenses of $473 and increases in occupancy and equipment of $261.

Other postretirement benefits decreased $15,607 for the year ended December 31, 2018 and 2017. During 2017, the method of recording other postretirement benefits plan (OPEB) expense at participating District entities for the multi-employer other postretirement benefits plan was modified. Prior to 2017, expense was recorded based on allocations of actuarially-determined costs and any differences between recorded expense and actual contributions were recorded in Other Liabilities on the Balance Sheet. For 2017 and future years, the Association will record other postretirement benefit costs based on the actual contributions to the plan. This change caused the Association to adjust its accounting estimate recorded in Other Liabilities since the liabilities do not impact future contributions to the plan. The change in estimate resulted in a reduction of Other Liabilities of $16,202.

The total decrease of $16,995 in 2017 as compared to 2016 in total noninterest expenses is mainly related to the aforementioned change in accounting estimate.

Insurance Fund premiums remained relatively stable for the twelve months ended December 31, 2018, compared to the same period of 2017. The Farm Credit System Insurance Corporation (FCSIC) set premiums at 9 basis points for 2018, based on adjusted insured debt outstanding. FCSIC premiums were set at 15 basis points for 2017. In addition, there was a 10 basis point premium on the average principal outstanding of nonaccrual loans and any other-than-temporarily impaired investments. FCSIC premiums were set between 16 and 18 basis points in 2016.

Income Taxes

The Association recorded a benefit for income taxes of $(22) for the year ended December 31, 2018, along with a provision for income taxes of $116 and $55 for the years ended December 31, 2017 and 2016, respectively. Refer to Note 12, *Income Taxes*, of the Notes to the Consolidated Financial Statements, for more information concerning Association income taxes.

Key Results of Operations Comparisons

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

Key Results of Operations Comparisons	For the 12 Months Ended 2018	2017	2016
Return on average assets	2.12%	2.92%	1.88%
Return on average members' equity	10.89%	16.00%	9.71%
Net interest income as a percentage of average earning assets	2.68%	2.67%	2.73%
Net (charge-offs) recoveries to average loans	(.037)%	(.007)%	.016%

A key factor in the growth of net income for future years will be improvement in net interest and noninterest income while attempting to keep operating expenses under control. Our goal is to generate earnings sufficient to fund operations, adequately capitalize the Association, and achieve an adequate rate of return for our members. To meet this goal, the agricultural economy must show continued improvement in the coming years and the Association must meet certain objectives. These objectives are to attract and maintain high quality loan volume priced at competitive rates and to manage credit risk in our entire portfolio, while efficiently meeting the credit needs of our members.

LIQUIDITY AND FUNDING SOURCES

Liquidity and Funding

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement (GFA). The GFA utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances the funds to the Association, creating notes payable (or direct loans) to the Bank. The Bank manages interest rate risk through direct loan pricing and asset/liability management. The notes payable are segmented into variable rate and fixed rate components. 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. Association capital levels effectively create a borrowing margin between the amount of loans outstanding and the amount of notes payable outstanding. This margin is commonly referred to as "Loanable Funds."

Total notes payable to the Bank at December 31, 2018, was $1,717,671 as compared to $1,639,346 at December 31, 2017 and $1,543,099 at December 31, 2016. The increase of 4.78 percent compared to December 31, 2017 and the increase of 6.24 percent compared to December 31, 2016, are related to continued growth in the loan portfolio. The average volume of outstanding notes payable to the Bank was $1,667,011, $1,597,754 and $1,415,092 for the years ended December 31, 2018, 2017 and 2016, respectively. Refer to Note 6, *Notes Payable to AgFirst Farm Credit Bank*, of the Notes to the Consolidated Financial Statements, for weighted average interest rates and maturities, and additional information concerning the Association's notes payable.

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. The liquidity policy of the Association is to manage cash balances to maximize debt reduction and to increase loan volume. As borrower payments are received, they are applied to the Association's note payable to the Bank. Sufficient liquid funds have been available to meet all financial obligations. There are no known trends likely to result in a liquidity deficiency for the Association.

The Association's indebtedness to the Bank represents borrowings by the Association primarily to fund its loan portfolio. This indebtedness is collateralized by a pledge of substantially all of the Association's assets and the terms of the revolving line of credit are governed by the General Financing Agreement (GFA). The GFA defines Association performance criteria for borrowing from the Bank. As of December 31, 2018, the Association was in compliance with all GFA covenants.

The Association had no lines of credit from third party financial institutions as of December 31, 2018.

Funds Management

The Bank and the Association manage assets and liabilities to provide a broad range of loan products and funding options, which are designed to allow the Association to be competitive in all interest rate environments. The primary objective of the asset/liability management process is to provide stable and rising earnings, while maintaining adequate capital levels by managing exposure to credit and interest rate risks.

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed, adjustable and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to market indices such as the Prime Rate or the 90-day London Interbank Offered Rate (LIBOR). Adjustable rate mortgages are indexed to U.S. Treasury Rates. Fixed rate loans are priced based on the current cost of System debt of similar terms to maturity.

The majority of the interest rate risk in the Association's Consolidated Balance Sheets is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control risk associated with the loan portfolio.

Relationship with the Bank

The Association's statutory obligation to borrow only from the Bank is discussed in Note 6, *Notes Payable to AgFirst Farm Credit Bank*, of the Notes to the Consolidated Financial Statements in this Annual Report.

The Bank's ability to access capital of the Association is discussed in Note 4, Equity *Investments in Other Farm Credit Institutions*, of the Notes to the Consolidated Financial Statements in this Annual Report.

The Bank's role in mitigating the Association's exposure to interest rate risk is described in the "Liquidity and Funding Sources" section of this Management's Discussion and Analysis and in Note 6, *Notes Payable to AgFirst Farm Credit Bank*, included in this Annual Report.

CAPITAL RESOURCES

Capital serves to support asset growth and provide protection against unexpected credit and interest rate risk and operating losses. Capital is also needed for future growth and investment in new products and services.

The Association Board of Directors establishes, adopts, and maintains a formal written capital adequacy plan to ensure that adequate capital is maintained for continued financial viability, to provide for growth necessary to meet the needs of members/borrowers, and to ensure that all stockholders are treated equitably. There were no material changes to the capital plan for 2018 that would affect minimum stock purchases or would have an effect on the Association's ability to retire stock and distribute earnings.

Total members' equity at December 31, 2018 increased 5.84 percent to $423,700 from the December 31, 2017 total of $400,335. At December 31, 2017, total members' equity increased 12.03 percent from the December 31, 2016 total of $357,345. The increase in 2018 from 2017 was primarily attributable to an increase in unallocated retained earnings of $27,535, partially offset by a decrease of allocated retained earnings of $2,042.The increase in total members' equity to 2017 from 2016 was primarily attributable to an increase in allocated retained earnings of $39,254.

Total capital stock and participation certificates were $52,969 at December 31, 2018, compared to $54,174 at December 31, 2017 and $56,531 at December 31, 2016. The decreases from year to year are mainly attributable to the Board approved reduction of the borrower investment to 2 percent of the loan, or $1 thousand whichever is less. This was effective January 1, 2013. Prior to January 1, 2013 the requirement was 2 percent of the loan or $5 thousand, whichever was less.

Prior to 2018, FCA set minimum regulatory capital requirements for System banks and associations. Capital adequacy was evaluated using a number of regulatory ratios. According to the FCA regulations, each institution's permanent capital ratio was calculated by dividing permanent capital by a risk-adjusted asset base. Risk adjusted assets mean the total dollar amount of the institution's assets adjusted by an appropriate credit conversion factor as defined by regulation. For all periods represented, the Association exceeded minimum regulatory standard for all the ratios.

The Association's permanent capital ratio as of December 31 and the FCA minimum requirements follow:

	2018	2017	2016	Regulatory Minimum
Permanent capital ratio	17.85%	16.92%	17.48%	7.00%
Total surplus ratio	–	–	16.55%	7.00%
Core surplus ratio	–	–	16.55%	3.50%

The increase in the Association's permanent capital ratio for December 31, 2018, as compared to December 31, 2017, was primarily attributable to increased earnings from 2017 in the portfolio along with stable loan volume growth. The decrease in ratios for December 31, 2017 compared to December 31, 2016, was primarily attributable to improved growth in the portfolio and the reduction of loans participated with the Bank. There are no trends, commitments, contingencies, or events that are likely to affect the Association's ability to meet regulatory minimum capital standards and capital adequacy requirements.

Effective January 1, 2017, the permanent capital ratio (PCR) remained in effect and the total and core surplus ratios were eliminated.

See Note 7, *Members' Equity*, of the Consolidated Financial Statements, for further information concerning capital resources.

PATRONAGE PROGRAM

Prior to the beginning of any fiscal year, the Association's Board of Directors, by adoption of a resolution, may establish a Patronage Allocation Program to distribute its available consolidated net earnings. This resolution provides for the application of net earnings in the manner described in the Association's Bylaws. This includes the setting aside of funds to increase surplus to meet minimum capital adequacy standards established by FCA Regulations, to increase surplus to meet Association capital adequacy standards to a level necessary to support competitive pricing at targeted earnings levels, and for reasonable reserves for necessary purposes of the Association. After excluding net earnings attributable to (a) the portion of loans participated to another institution, and (b) participation loans purchased, remaining consolidated net earnings are eligible for allocation to borrowers. Refer to Note 7, *Members' Equity*, of the Notes to the Consolidated Financial Statements, for more information concerning the patronage distributions. The Association declared patronage distributions of $17,500 in 2018, $56,630 in 2017, and $32,308 in 2016.

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

The Association's mission includes providing sound and constructive credit and related services to Young, Beginning and Small (YBS) farmers and ranchers. First South's mission is directed by board and management to ensure that our Association is making every effort possible to implement our YBS program.

The Association has in place a flexible YBS program with policies and procedures that are designed to meet the needs of YBS farmers in our Association's territory. The First South Board approves the YBS policy as well as the annual business plan which outlines practices to accomplish the First South YBS mission.

YBS farmers and ranchers are defined as:

- *Young Farmer*: A farmer, rancher, or producer or harvester of aquatic products who is age 35 or younger as of the date the loan is originally made.
- *Beginning Farmer*: A farmer, rancher, or producer or harvester of aquatic products who has 10 years or less farming or ranching experience as of the date the loan is originally made.
- *Small Farmer*: A farmer, rancher, or producer or harvester of aquatic products who normally generates less than $250 in annual gross sales of agricultural or aquatic products at the date the loan is originally made.

The Association's Young, Beginning, and Small farmer and rancher program (YBS) complies with statutory and regulatory requirements which include qualitative and quantitative goals. Goals include coordinating with government agencies that offer loan guarantees for risk management purposes. First South is an FSA approved lender.

The Association business plan also outlines strategies to increase market share success, a market outreach program that generates participation and involvement by Association staff at the field level. Strategies include (1) YBS Program on the Association website, (2) First South Market Outreach Program, (3) First South Diversity and Inclusion Marketing Plan (4) Country Loan and Small Loan Program, (5) demographic information by state and county, and (6) sponsorships and educational programs. The final results of these outreach and education programs are reported to the Association Board of Directors on an annual basis.

The Association business plan also includes a budget recommended by management that is sufficient to carry out the Association's YBS mission and performance goals.

The following table outlines the loan volume and number of YBS loans in the loan portfolio as of December 31, 2018 for the Association.

	As of December 31, 2018	
	Number of Loans	Amount of Loans
Young	2,204	$345,389
Beginning	4,345	$643,221
Small	6,778	$690,619

For purposes of the above table, a loan could be included in more than one of the categories depending on the characteristics of the underlying borrower.

The 2012 USDA Ag Census data has been used as a benchmark to measure penetration of the Association YBS marketing efforts. The USDA Ag Census data prepared and provided by AgFirst Farm Credit Bank shows the number of YBS farmers in First South Farm Credit Association's territory as of December 31, 2012: Young (4,991); Beginning (20,521); Small (95,491).

The AgFirst demographics show First South segment penetration as a percentage of Association territory totals as follows: Young 27.9%; Beginning 13.7%; Small 4.7%. As of December 31, 2018, of the Association's total portfolio; 17.25% were Young farmers; 34.01% were Beginning farmers; and 53.05% were Small farmers.

Data Source: USDA-NASS 2012 Ag Census of Agriculture Volume I: Geographic Area Series Tables 2 and 45. Other data from AgFirst FCB Marquis standard reports period ending December 2018.

Slight differences between the Census and our YBS information are as follows:

- The Census shows young farmers in a group up to age 34, whereas the Association's YBS information shows young farmers up to age 35.
- The Census shows years on present farm up to nine years, whereas the Association's YBS information shows 10 years or less for a beginning farmer.
- The Census data is based on number of farms, whereas the Association's YBS information is based on number of loans.

Capital Ratios

The following sets forth the regulatory capital ratios which were effective January 1, 2017:

Ratio	Minimum Requirement	Capital Conservation Buffer*	Minimum Requirement with Capital Conservation Buffer	Capital Ratios as of December 31, 2018	2017
Risk-adjusted ratios:					
CET1 Capital	4.5%	1.25%	5.75%	17.50%	16.43%
Tier 1 Capital	6.0%	1.25%	7.25%	17.50%	16.43%
Total Capital	8.0%	1.25%	9.25%	18.29%	17.35%
Permanent Capital	7.0%	0.0%	7.0%	17.85%	16.92%
Non-risk-adjusted ratios:					
Tier 1 Leverage	4.0%	1.0%	5.0%	17.45%	16.42%
URE and UREE Leverage	1.5%	0.0%	1.5%	11.34%	10.91%

** The capital conservation buffers have a 3 year phase-in period and will become fully effective January 1, 2020. Risk-adjusted ratio minimums will increase 0.625% each year until fully phased in. There is no phase-in period for the tier 1 leverage ratio.*

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.

The following sets forth regulatory capital ratios as previously reported:

	Regulatory Minimum	2016	2015	2014	2013	2012
Permanent Capital Ratio	7.00%	17.48%	17.78%	18.32%	17.76%	16.12%
Total Surplus Ration	7.00%	16.55%	17.19%	17.62%	16.94%	14.86%
Core Surplus Ratio	3.50%	16.55%	16.60%	16.95%	16.20%	14.07%

REGULATORY MATTERS

On May 10, 2018, the Farm Credit Administration adopted a final rule that amends the regulations governing investments of System banks and associations. The final rule strengthens eligibility criteria for the investments the banks may purchase and hold. It also implements Section 939A of the Dodd-Frank Act by removing references to and requirements for credit ratings and substitutes the eligibility requirement with other appropriate standards of credit worthiness. In addition, it grants associations greater flexibility regarding the risk management purposes for investments and limits the type and amount of investments that an association may hold. Only securities that are issued by, or are unconditionally guaranteed or insured as to the timely payment of principal and interest by, the U.S. government or its agencies are eligible for association risk management purposes. An association may purchase and hold investments not to exceed 10 percent of its 90-day average daily balance of outstanding loans on the last business day of the quarter. The final rule became effective January 1, 2019.

Farm Bill

The Agricultural Improvement Act of 2018 (Farm Bill) was signed into law on December 20, 2018. This new Farm Bill will govern an array of federal farm and food programs, including commodity price support payments, farm credit, conservation programs, research, rural development and foreign and domestic food programs for five years through 2023. The new Farm Bill continues to provide support for crop insurance and commodity support programs, strengthen livestock disaster programs, and provides dairy producers with an updated voluntary margin protection program that will provide additional risk management options to dairy operations.

The Farm Bill also clarifies and updates the Insurance Corporation's authorities to act as conservator or receiver of a System institution. The Congressional Conference Committee report states that Congress intends "for the authorities of the Corporation to be functionally equivalent to the parallel authorities of the Federal Deposit Insurance Corporation." In addition, the Farm Bill provides, among other authorities, the Insurance Corporation with the authority to organize, and the Farm Credit Administration to charter, a System bridge bank, which has all the powers of a System bank with a maximum life span of five years.

Many provisions of the Farm Bill will require the United States Department of Agriculture to develop rules and procedures to fully implement these authorities. The timing for the issuance of those rules is uncertain.

LIBOR TRANSITION

On July 27, 2017, the United Kingdom Financial Conduct Authority (the Conduct Authority) announced that it will no longer persuade or compel such banks to submit rates for the calculation of the LIBOR rates after 2021. The Conduct Authority regulates the panel banks that submit quotes for the purpose of calculating LIBOR to the Intercontinental Exchange (ICE) Benchmark Administration (the entity that is responsible for calculating LIBOR). Accordingly, it is uncertain whether the ICE Benchmark Administration will continue to quote LIBOR after 2021. Furthermore, in the United States, efforts to identify a set of alternative U.S. dollar reference interest rates include proposals by the Alternative Reference Rates Committee (ARRC) of the Federal Reserve Board and the Federal Reserve Bank of New York. Specifically, the ARRC has proposed the Secured Overnight Financing Rate (SOFR) as the recommended alternative to LIBOR and the Federal Reserve Bank of New York began publishing SOFR in April of 2018. SOFR is based on a broad segment of the overnight Treasury repurchase market and is a broad measure of the cost of borrowing cash overnight collateralized by Treasury securities.

At this time, it is not possible to predict, among other uncertainties, whether (i) LIBOR will be discontinued, (ii) the effect of any changes to the methodology for calculating LIBOR, or (iii) any establishment of alternative reference rates or any other reforms to LIBOR that may be enacted in the United Kingdom, in the United States or elsewhere. Uncertainty as to the nature of such potential changes, alternative reference rates or other reforms may adversely affect the trading market for LIBOR based instruments, including certain of the Systemwide Debt Securities, System borrowings, loans, investments, derivatives, other System assets and liabilities and preferred stock that are indexed to LIBOR. Accordingly, reform of, or the replacement or disappearance of, LIBOR and the proposed regulation of LIBOR and other "benchmarks" may adversely affect the rates of interest the System pays on its Systemwide Debt Securities (including changes to their value and liquidity, return, and usefulness for intended purpose), on other borrowings and preferred stock, as well as the value of and return on loans and investments and the value and effectiveness of derivatives. This could adversely affect the System's cash flows. Moreover, if LIBOR is replaced, System institutions will need to take steps to restructure their debt and derivatives, which could adversely affect operations.

The System institutions are currently evaluating the potential impact of the eventual replacement of the LIBOR benchmark interest rate, including the possibility of using SOFR as the alternative to LIBOR. While each system institution is required by the regulator to have a transition plan, the transition from LIBOR to SOFR is expected to be complex and to include the development of term and credit adjustments to minimize, to the extent possible, discrepancies between LIBOR and SOFR. Accordingly, the transition may introduce additional basis risk for market participants, including when an alternative index, e.g., SOFR, exists in conjunction with LIBOR. There can be no guarantee that SOFR will become the dominant alternative to U.S. dollar LIBOR or that SOFR will be widely used. In addition, other alternatives may or may not be developed with additional complications.

Changes in LIBOR may result in interest rates and/or payments that are higher or lower than, or that do not otherwise correlate over time with, the interest rates and/or payments that would have been associated with LIBOR-based Systemwide Debt Securities, or loans or investments that are based on LIBOR, which may increase or decrease the payments to be made on such LIBOR-based Systemwide Debt Securities, or loans or investments that are based on LIBOR.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

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

The following Accounting Standards Updates (ASUs) were issued by the Financial Accounting Standards Board (FASB) but have not yet been adopted:

Summary of Guidance	Adoption and Potential Financial Statement Impact
ASU 2016-13 – Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	
• Replaces multiple existing impairment standards by establishing a single framework for financial assets to reflect management's estimate of current expected credit losses (CECL) over the complete remaining life of the financial assets. • Changes the present incurred loss impairment guidance for loans to a CECL model. • The Update also modifies the other-than-temporary impairment model for debt securities to require an allowance for credit impairment instead of a direct write-down, which allows for reversal of credit impairments in future periods based on improvements in credit. • Eliminates existing guidance for purchased credit impaired (PCI) loans, and requires recognition of an allowance for expected credit losses on these financial assets. • Requires a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption. • Effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early application will be permitted for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018.	• The Association has begun implementation efforts by establishing a cross-discipline governance structure and will implement a third-party model. The Association is currently identifying key interpretive issues and assessing processes against the new guidance to determine what modifications may be required. • The Association expects that the new guidance will result in an increase in its allowance for credit losses due to several factors, including: 1. The allowance related to loans and commitments will most likely increase to cover credit losses over the full remaining expected life of the portfolio, and will consider expected future changes in macroeconomic conditions, 2. An allowance will be established for estimated credit losses on any debt securities, 3. The nonaccretable difference on any PCI loans will be recognized as an allowance, offset by an increase in the carrying value of the related loans. • The extent of the increase is under evaluation, but will depend upon the nature and characteristics of the Association's portfolio at the adoption date, and the macroeconomic conditions and forecasts at that date. • The Association expects to adopt the guidance in first quarter 2021.
ASU 2016-02 – Leases (Topic 842)	
• Requires lessees to recognize leases on the balance sheet with lease liabilities and corresponding right-of-use assets based on the present value of lease payments. • Lessor accounting activities are largely unchanged from existing lease accounting. • The Update also eliminates leveraged lease accounting but allows existing leveraged leases to continue their current accounting until maturity, termination or modification. • Also, expands qualitative and quantitative disclosures of leasing arrangements. • Requires adoption using a modified cumulative-effect approach wherein the guidance is applied to all periods presented. A recent amendment provides an additional (and optional) transition method to adopt the new leases standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. • Effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted.	• The practical expedients allow entities to largely account for existing leases consistent with current guidance, except for the incremental balance sheet recognition for lessees. • The Association completed its evaluation of leasing contracts and activities and developed its methodology to estimate the right-of-use assets and lease liabilities, which is based on the present value of lease payments. There will not be a material change to the timing of expense recognition. • Given the limited changes to lessor accounting, there were no material changes to recognition or measurement for the Association. • The Association will need to provide additional disclosure information as a result of adopting the Update. • The Association will adopt the guidance in first quarter 2019 using the optional modified retrospective method and practical expedients for transition. • Upon adoption, the Association will record a cumulative-effect adjustment to equity of approximately $(305). In addition, a Right of Use Asset in the amount of $1,640 and Lease Liability in the amount of $1,945 will be recorded.

Disclosure Required by Farm Credit Administration Regulations

Description of Business

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

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

Unincorporated Business Entities

At December 31, 2018, the Association had no investment in Unincorporated Business Entities (UBEs).

Description of Property

The following table sets forth certain information regarding the properties of the reporting entity, all of which are located in Alabama, Mississippi and Louisiana:

Location	Description	Form of ownership
574 Highland Colony Pkwy. Ridgeland, MS	Administrative	Leased
2341 AL Hwy. 21 South Oxford, AL	Branch	Owned
1824 Eva Rd., NE Cullman, AL	Branch	Owned
3201 AL Hwy. 157, Suite 200 Cullman, AL	Underwriting	Leased
320 AL Hwy. 75 N Albertville, AL	Branch	Owned
One Perimeter Park South Birmingham, AL	Branch	Leased
30035 Hwy. 72 West Madison, AL	Branch	Owned
14390 Market Street Moulton, AL	Branch	Owned
970 Hwy. 20 East Tuscumbia, AL	Branch	Owned
700 Hwy. 80 West Demopolis, AL	Branch	Owned
4210 McFarland Blvd. Northport, AL	Branch	Owned
1715 West Second Street Montgomery, AL	Branch	Owned
1401 Forest Avenue Montgomery, AL	Branch	Owned
141 Lee Street Luverne, AL	Branch	Owned
1434 S. Union Ave. Ozark, AL	Branch	Owned
1613 Fredrick Road, Opelika, AL	Division/Branch	Owned
209 E. Second St. Bay Minette, AL	Branch	Leased
5070 Boll Weevil Circle Enterprise, AL	Branch	Owned
1103 Bypass West Andalusia, AL	Branch	Owned
260 Trace Colony Park Drive Ridgeland, MS	Division/Branch	Owned
914 Van Buren Ave. Oxford, MS	Branch	Owned
1626 N Veterans Memorial Blvd. Tupelo, MS	Branch	Leased
306 E. Jefferson St. Aberdeen, MS	Branch	Owned
1009 North Main Street Calhoun City, MS	Branch	Owned

Location	Description	Form of Ownership
1089D Stark Road Starkville, MS	Branch	Leased
103 Professional Plaza Greenwood, MS	Branch	Owned
1703 Hwy 82 W Frontage Rd. Greenwood, MS	Branch	Owned
203 Cossar Blvd. Charleston, MS	Branch	Owned
122 Main Street Indianola, MS	Branch	Leased
505 E. Second St. Clarksdale, MS	Branch	Owned
1021 Highway 82 East Leland, MS	Branch	Owned
9769 Eastside Drive Extension, Newton, MS	Branch	Owned
501 Apache Drive McComb, MS	Branch	Owned
749 Cosby St. Centreville, MS	Branch	Closed
4 Thompson Park Hattiesburg, MS	Branch	Owned
23 Dunnbarr Laurel, MS	Branch	Owned
19550 Old Scenic Hwy. Zachary, LA	Division/Branch	Owned
222 N. Cedar St. Tallulah, LA	Branch	Owned
1896 Hudson Circle, Suite 7, Monroe, LA	Branch	Leased
109 Davis St. Lake Providence, LA	Branch	Owned
811 Jackson St. Winnsboro, LA	Branch	Owned
2308 S. MacArthur Dr. Alexandria, LA	Branch	Owned
321 South Main St. Marksville, LA	Branch	Owned
5057 I-49 S. Service Rd. Opelousas, LA	Branch	Owned
1007 Guy Dr. St. Martinville, LA	Branch	Owned
3206 South LA 13 Crowley, LA	Branch	Owned
4925 East McNeese St. Lake Charles, LA	Branch	Owned
60050 Westway Drive Amite, LA	Branch	Owned
1725 St. Mary Hwy. Thibodaux, LA	Branch	Owned

Lease Information Disclosure:

Location	Term of Lease	Expiration Date	Monthly Lease Amount
Ridgeland, MS	5 years	03/31/2020	$16,241.76
Cullman, AL	5 years	06/01/2023	$3,100.00
Birmingham, AL	18 months	04/30/2020	$3,331.00
Bay Minette, AL	month-to-month	12/31/2019	$1,600.00
Tupelo, MS	3 years	04/30/2020	$800.00
Starkville, MS	5 years	09/30/2023	$2,220.16
Indianola, MS	2 years	07/19/2020	$300.00
Monroe, LA	1 year	09/30/2018	$1,200.00

Legal Proceedings

Information, if any, to be disclosed in this section is incorporated herein by reference to Note 11 of the Consolidated Financial Statements, "*Commitments and Contingencies*," included in this Annual Report.

Description of Capital Structure

Information to be disclosed in this section is incorporated herein by reference to Note 7 of the Consolidated Financial Statements, "*Members' Equity*," included in this Annual Report.

Description of Liabilities

The description of liabilities, contingent liabilities and obligations to be disclosed in this section is incorporated herein by reference to Notes 2, 6, 9 and 11 of the Consolidated Financial Statements included in this Annual Report.

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

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

Senior Officers

The following represents certain information regarding the senior officers of the Association and their business experience for the past five years:

Senior Officer	Position & Other Business Interests
John W. Barnard	*President & Chief Executive Officer* since January 2018. Prior to that, President, Mississippi Division, since April 1994.
Bryan Applewhite	*Senior Vice President /Chief Financial Officer /Treasurer* since November 2001.
Sells J. Newman, Jr.	*Senior Vice President/Legislative Affairs and Public Relations* since October 1987.
Gines Pérez, III	*Senior Vice President/Chief Lending Officer* since July 2018. Prior to that, *Executive Vice President/Chief Credit Officer*-AgChoice Farm Credit since February 2016 , and prior to that, *Relationship Manager and various other roles and responsibilities*-AgFirst Farm Credit Bank since June 2010.
Randall H. Underwood	*Senior Vice President/Chief Credit Officer* since April 1994.
David Wilson	*President, Louisiana Division* since January 2012. Prior to that, Branch Manager, Louisiana Division.
Rodney Brantley	*President, Mississippi Division* since July 2017. Prior to that, Division Vice President, Mississippi Division.
Mike Pigg	*President, Alabama Division* since January 2016. Prior to that, President, North Alabama Division, since July 2011.
John Hurt	*President, Capital Markets Division* since July 2018. Prior to that, *Capital Markets officer* since December 2011.

The total amount of compensation earned by the CEO and senior officers as a group during the years ended December 31, 2018, 2017 and 2016, is as follows:

Name of Individual or Number in Group	Year	Salary	Bonus	Deferred Comp.	Change in Pension Value	Perq/ Other*	Total
John W. Barnard	2018	$ 325,013	$ 80,000	$ –	$ 50,421	$ 22,617	$ 478,051
Roger F. Chappell	2017	$ 325,013	$ 109,355	$ –	$ 309,150	$ 27,455	$ 770,973
Roger F. Chappell	2016	$ 325,013	$ 144,000	$ –	$ 139,450	$ 26,579	$ 635,042
8	2018	$ 1,386,694	$ 536,021	$ –	$ 137,481	$ 103,108	$ 2,163,304
6	2017	$ 1,316,358	$ 393,100	$ –	$ 1,247,775	$ 90,320	$ 3,047,553
7	2016	$ 1,111,972	$ 245,746	$ –	$ 890,864	$ 74,535	$ 2,323,117

* *The Perquisites/Other amount disclosed in the above chart may include club memberships, automobile and travel allowance, deferred compensation, life insurance, 401(k) contributions, and relocation reimbursement.*

For the Retirement Plan, the present value of pension benefits is the value at a specific date of the benefit payment stream an individual is expected to receive upon retirement based on pay and service earned to date. These present values change year over year as (1) pension benefits increase due to an additional year of pay and service being earned under the benefit formula, (2) individuals are one year closer to receiving payments, and (3) the assumptions used to determine the present value change.

The present value of Retirement Plan pension benefits will naturally increase as the benefits earned under the plan increase. Since the pension benefit formula is dependent on base pay, pay increases directly impact the pension values.

The present values are calculated by discounting each expected future benefit payment back to the determination date at a specified interest (or discount) rate. When a year passes, there is one fewer year of discounting, which increases the present value.

Finally, the present value of the expected future benefit payment stream is based on actuarial assumptions, chiefly the discount rate mentioned above. Other assumptions are also used, such as expected retirement age and life expectancy. Changes in the actuarial assumptions can increase or decrease the pension values. The discount rate is updated every year based on the interest rate environment at December 31. A decrease in the discount rate (i.e. less discounting) increases the present values and vice versa. There was an increase in the discount rate assumption from December 31, 2017 to December 31, 2018, causing the pension values to decrease.

Other actuarial assumptions are updated periodically. At December 31, 2018, the mortality improvement assumption was updated to reflect recent mortality studies indicating a lower degree of mortality improvement (and thus slightly shorter life expectancies). This change had a minor impact and resulted in a small decrease in Retirement Plan present values.

Pension Benefits Table
As of December 31, 2018

Name of Individual or Number in Group	Year	Plan Name	Number of Years Credited Service	Actuarial Present Value of Accumulated Benefits	Payments During 2018
CEO:					
John W. Barnard	2018	First South Retirement Plan	36.83	$ 1,346,142	$ –
				$ 1,346,142	$ –
Senior Officers and Highly Compensated Employees:					
8 Officers, excluding the CEO	2018	First South Retirement Plan	29.89*	$ 7,599,390	$ –
				$ 7,599,390	$ –

**Represents the average years of credited service for the group*

In addition to base compensation, the Association offers a Business Incentive Plan to all eligible employees, not including the CEO. The Business Incentive Plan is designed to motivate employees to exceed the business plan goals established by the Board of Directors during the fiscal year. These goals are met and exceeded in three key business areas. Those key areas include return on average daily balance of loans (ROADB), credit quality and growth in average daily balance (ADB). Incentive maximums vary but no employee shall receive more than 25 percent of his or her individual base salary in the Business Incentive Plan.

The Association also provides an Executive Incentive Plan for all eligible senior officers, not including the CEO. The Executive Incentive Plan is designed to motivate and reward the senior officers to meet and exceed the financial and performance goals of the Association. The financial and performance goals for this plan are return on average daily balance of loans (ROADB) and operating efficiency in his or her respective area of responsibility. These performance areas are weighted equally. No senior officer shall receive more than 15 percent of his or her individual base salary in the Executive Incentive Plan.

The level of incentive paid to the CEO, if any, is approved by the Board of Directors upon recommendation from the Compensation Committee. The CEO incentive payment is based on various performance factors also designed to meet the goals and objectives set by the Board of Directors.

Incentives are paid within 45 days of the year end. The incentives/bonuses are shown in the year earned which may be different than the year of payment. Eight senior officers shared in the 2018 business incentive and six senior officers shared in the executive incentive.

Disclosure of information on the total compensation paid during 2018 to any senior officer, or to any other individual included in the total, is available to shareholders upon request.

Directors

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

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was $276,117 for 2018, $302,220 for 2017 and $262,730 for 2016.

Subject to approval by the board, the Association may allow directors honorarium of $800 per day for attendance at regularly scheduled board meetings and auxiliary committee meetings not held in conjunction with regularly scheduled board meetings. In addition, each director shall be paid a quarterly retainer of $500 with the exception of the board chairman and audit committee chairman which will be $750 per quarter. Auxiliary meetings such as regional advisory committee meetings, political action committee meetings and other special assignments will be $400 per day and telephone conference calls will be $100. Travel compensation to regularly scheduled board meetings and auxiliary committee meetings held at the site of the regularly scheduled board meetings will be $100 to $400 on a pro rata mileage basis and $200 per day to offsite board meetings. Total compensation paid to directors as a group was $316,960.

The following represents certain information regarding the directors of the Association, including their principal occupation and employment for the past five years.

Michael W. Patrick, Chairman, of Canton, Mississippi, is partner in Patrick Farms Joint Venture, a farming operation consisting of 3,700 acres of cotton, corn, wheat, soybeans and timber. He is former chairperson of the Madison County USDA/FSA county committee which administers farm commodity, crop insurance, credit, environmental, conservation and assistance programs for farmers and ranchers. He is a commissioner on the Madison County Soil and Water District Board, a unit of county government responsible for soil and water conservation programs within the county boundaries. Mr. Patrick is an owner/officer in Big Black Farms, Inc, Cotton Country Inc and Cotton Pickers, Inc, agricultural corporations and partners in Patrick Farms Joint Venture. He has been a member of First South for over 28 years.

Daniel C. Mattingly, Vice-Chairman, of Belle Rose, Louisiana, is the Agricultural Manager for Lula-Westfield, L.L.C. Lula Factory Division, a sugarcane processing facility (raw sugar factory). He manages over 40,000 acres of farmland, including that owned by Savoie Industries, Inc., and including sugarcane production land, timber property and hunting land. He is the voting member of the company for First South. He has ownership interests in Savoie Industries, Dugas & LeBlanc and Savoie-Mattingly Properties LLC. Mr. Mattingly serves as President of Assumption Parish Farm

Bureau which promotes agriculture in Assumption Parish, LA. He is a member and secretary of the Board of Directors of Savoie Industries Inc., a sugarcane mill, having served on that board for the past 13 years. He is active in the Knights of Columbus and the Agricultural Leaders of Louisiana. Mr. Mattingly has been a member of First South for over 18 years.

Paul Briscoe, of Oxford, Mississippi, is a partner in Briscoe and Sons Farms. The farming operation includes over 4,500 acres in Lafayette County, Mississippi, and produces cotton, soybeans, corn, timber and beef cattle. Mr. Briscoe also manages family owned rental property and is co-owner of Briscoe Properties LLC, Briscoe Family Properties LLC, PJM Properties LLC and Briscoe Construction and Realty. He has served on the Lafayette County Farm Bureau Board since 1980 and served as its president for 18 of those years. He also served three terms on the Farm Bureau State Board. Mr. Briscoe has been a member of First South for over 33 years.

John R. Burden, of Baileyton, Alabama, has a dairy operation, Burden Farms LLC. He also raises grain, beef cattle and hay. He is a director for the American Dairy Association, a former member of Patron Council for Goldkist (a poultry integrator), and he is a former director of DHIA, which serves the dairy industry. Mr. Burden has been a member of First South for over 38 years.

Paul Clark, of Decatur, Alabama, has a row crop operation, Clark Farms Partnership (Paul Clark Farms, LLC and Marilyn Clark Farms, LLC), in Courtland, Alabama, consisting of 1,875 acres of corn, soybeans and cotton. He was previously co-owner of Clark and Reed, an agricultural consulting firm. He is past president of Alabama Ag Consulting Association, which supports and promotes the profession of agricultural consulting. Mr. Clark has been a member of First South for over 28 years.

Amy C. Ellender of Mer Rouge, Louisiana serves as a board appointed director, and is not a member of the Association. She is an attorney and owner of Ellender Law Firm, APLC in Mer Rouge, with areas of practice including estate planning, successions and probate, agricultural leases, collection work for grain elevators and other ag related businesses, corporate legal work, farm restructuring and multi district litigation. She is officer and financial manager for Clark Farms, a 6,000 acre row crop operation owned and operated by members of her family, for which she prepares and manages all financial records and maintains all farm leases and crop records. She is a member of Ellender Properties, LLC, and a director of Christian Life Fellowship, Inc., a nonprofit Christian summer camp/retreat facility run by her family. Amy received both her B. S. degree in Finance and her J. D. Law degree from Louisiana State University.

Dr. Marty J. Fuller of Starkville, Mississippi, serves as a board appointed director, and is not a member of the Association. Dr. Fuller is President and CEO of Federal Solutions, LLC, a firm specializing in governmental relations. Dr. Fuller serves as Senior Consultant at Cornerstone Government Affairs, a Washington, D. C. based government/public relations firm. Prior to this role he served as the Director of Federal Relations for Mississippi State University. He also served previously as Associate Director of the Mississippi Agricultural and Forestry Experiment Station (MAFES) and is Emeritus Professor in the Department of Agricultural Economics at Mississippi State University. Dr. Fuller was formerly President and CEO of Opswatch, a business development and grant monitoring service company. He has interests in Camgian Microsystems, M and R Land LLC, High Dice LLC and Halberd Group LLC. Dr. Fuller received his B. S., M. S. and Ph. D. degrees in Agricultural Economics from Mississippi State University.

John Ingraffia, of Husser, LA, is owner/operator of a 200 head dairy operation, and produces hay. Mr. Ingraffia was formerly a member of the Regional Advisory Committee, and has been a member of First South for over 20 years.

Wilson E. Judice is president and director of Wilson Judice Farms, Inc., formerly a 1,100 acre sugarcane and soybean operation in St. Mary Parish, Louisiana. He owns and operates Bayou Teche Family Farms, a direct market vegetable operation. He is director of Judice Agricultural Services, LLC, an agricultural employment agency serving Wilson Judice Farms and Frank Martin Farms, and was a member of management of Frank Martin Farms. He also provides management assistance on the family sugarcane and soybean farm. He has served as commissioner on the St. Mary Parish Fire Protection District Two board of directors since 2008. He has served on the LFBF Sugar Advisory Committee since 2011, chairman of the Young Farmers and Ranchers for the St. Mary Parish Farm Bureau board of directors since 2005, and on the St. Mary Parish 4-H Advisory Committee since 2012. He is a board member of St. Mary Parish 4-H Foundation. He is a director of Teche Growers Association, a member of the Tri-Parish Row Crop Advisory Committee and a member of the American Sugarcane League. He has been a member of First South for over 5 years.

William T. (Bill) Kyser, of Hale County, Alabama, has a catfish, beef cattle, and timber operation. He is a member of Catfish Farmers of America, Alabama Farmers Federation, Hale County Farmers Federation, Auburn Agricultural Alumni Association, Greensboro Farmers Cooperative, and he is a director of the Hale County Cattlemen's Association and Alabama Catfish Producers. These organizations promote agriculture and agricultural commodities nationally and in Alabama. He is also a director of Falcon Protein Products LLC. He is Co-owner of Alabama Catfish Feed Mill LLC, Kyser LLC, Kyser Farms LLC, Kyser Family Farms LLC, WTK LLC, MRSWTK Inc., and Catfish Wireless LLC. Mr. Kyser has been a member of First South for over 48 years.

Timothy Leonard, of Summit, Mississippi, owns and operates Leonard Farms, a multi farm poultry operation. He also has a cattle operation and produces hay. He is owner and operator of T & G Poultry Services, which provides repairs, upgrades, litter preparation and service work to local poultry farms, and Meadow Oak Properties LLC, a residential rental company. He is owner of Leonard's Cypress Landing, Inc., d/b/a Cypress Landing, a restaurant. He has been a member of First South for over 16 years.

Ray Makamson, of Itta Bena, Mississippi, owns and operates Ray Makamson Farms, a farming operation consisting of over 3,000 acres of cotton, corn and soybeans. The operation includes Eddie & Ray Farms Inc, Emily & Jason Farms Inc, Lamar & Ray Farms Inc, and Ray & Garry Farms Inc. He is managing partner of a cotton gin, Greenwood Gin, Inc. He is part owner of Ag-Concepts, a flying service, and Makamson

Properties LLC. Mr. Makamson has been a member of First South for over 45 years.

Alan Marsh, a resident of Madison County, Alabama, is a partner and President of Marsh Farms, a 3,000-acre family farming operation consisting of cotton, soybeans and wheat. The operation includes Alan Marsh Farms Inc, Austin Marsh Farms Inc, Patty Marsh Farms Inc and South Limestone Farm Inc. He is a director of the Limestone Farmers' Federation, and a member of the National Cotton Council, Cotton Incorporated and Staplcotn, all of which support and promote the cotton industry nationally and in the state of Alabama. He is also President of South Limestone Gin, a local cotton gin. Mr. Marsh currently serves on the Board of Directors of AgFirst Farm Credit Bank. He has been a member of First South for over 42 years.

James F. Martin, III, of Enterprise, Alabama, farms 1,200 acres of corn, cotton, peanuts, soybeans and winter grains, along with raising beef cattle and hay. They recently added a small scale vegetable operation including strawberries and onions. He previously owned and operated a dairy. He is a partner in James Martin Farms, LLC and a partner in Nitram LLC, a real estate ownership company. He also is a member of the Coffee County advisory committee for ALFA and the Coffee Gin Company. He has been a member of First South for over 26 years.

Joe H. Morgan, of Hattiesburg, Mississippi, has a 3,700 acre family owned row crop operation, M & M Farms, consisting of 2,750 acres of cotton, corn and peanuts. He is a member and former officer and director of Forrest County Farm Bureau, which promotes agriculture in Forrest County, Mississippi and serves on the Forrest County FSA Committee which assists the federal farm service agency locally in administering and managing farm commodity, credit, conservation, disaster, and loan programs. He is President of Mississippi Peanut Growers Association, a trade organization, and the Mississippi delegate on the National Peanut Board. Mr. Morgan is a former recipient of the Outstanding Young Farmer of the Year Award and the Outstanding Farmer Award for Outstanding Service in soil and water conservation. Mr. Morgan has been a member of First South for over 48 years.

Shepherd (Shep) Morris**,** of Shorter, Alabama, is owner of Morris and Morris Farms, a 3,400-acre row crop operation growing cotton, corn and sesame, and a 1,000 acre timber operation. He serves as a board member of Autauga Quality Cotton Association, a marketing organization, Choice Cotton Company, a cotton marketing organization, Alabama Cotton Commission and River Bank and Trust, a community bank. He also serves as president of the Macon County Farmers Federation and a supervisor for Macon County Soil and Water District, both promoting agriculture in Macon County, AL. He is president of Milstead Farm Group, Inc., a cotton ginning operation. Mr. Morris has been a member of First South for over 39 years.

Thomas H. Nelson, Jr.**,** of Chatham, Mississippi, has a 6,500-acre row crop operation consisting of Nelson-King Farms, Nelson-King Lands LLC, E G Nelson Inc, and Everhope Plantation LLC, producing corn and soybeans. He is a director of Washington County Farm Bureau, which supports and promotes agriculture in Washington County, Mississippi, and is Chairman of the Board of Trustees of Avon United Methodist Church in Avon, MS. Mr. Nelson has been a member of First South for over 28 years.

James M. Norsworthy, III, of Jackson, Louisiana, is the owner of One Hundred Cedars Cattle Farm, a 150 head cow/calf operation, manages 500 acres of pine and hardwood timber land, and has a commercial hay operation. He is past Director of Environmental Services for Eastern Louisiana Mental Health Systems. He serves as a board member of the Feliciana Farm Bureau and Centreville Academy, and is a member of the East Feliciana Parish Cattlemen's Association, the Feliciana Forestry Association and the American Angus Association. He is former mayor of the town of Jackson, Louisiana. Mr. Norsworthy currently serves on the Board of Directors of AgFirst Farm Credit Bank, where he serves as chairman of the Governance Committee, and has been a member of First South for over 38 years.

Thomas A. Parker**,** of Lake Providence, Louisiana, has a 4,000 acre farming operation in Lake Providence, Louisiana, consisting of cotton, corn, soybeans and rice. He also operates a 4,000 acre farm consisting of cotton, corn, soybeans and rice, in Parkdale, Arkansas. Mr. Parker is a managing partner of Hollybrook Enterprises, a cotton gin, and serves as a director on the Staplcotn Board, an agricultural marketing cooperative. Mr. Parker owns and operates a farm management company, Deep Current Ag Management, that manages farms for individual and institutional investors. He previously owned a dry cleaning franchise in Monroe, Louisiana. His current business interests include Brownpark LLC, Cypress Break LLC, Tweet & Tap LLC, Parker Farms Inc., Brandy of East Carroll Inc., Hardly Able Inc., Parker Group Holdings LLC, Parker Capital Partners LLC, TM & TP LLC, RW & TP LLC, TS & TP LLC, P & H Partners LLC, County Line LLC, P&D Land Company LLC, TAP Farm LLC, JLBP Farm LLC, and NP Farm LLC. He was formerly the Louisiana member on the Cotton Board, and formerly a producer delegate on the National Cotton Council. He is currently President of East Carroll Farm Bureau and past president of Louisiana Cotton Producers all of which promote and support cotton and agriculture. He has been a member of First South for over 28 years.

Ted S. Passmore**,** of Deville, Louisiana, has a 6,000 acre row crop operation with his brother that includes Passmore Farms, Delta Farming of Avoyelles LLC, and Delta Farming General Partnership, and produces soybeans, cotton and corn. He is a member of Louisiana Farm Bureau which promotes agriculture in Louisiana. Mr. Passmore has been a member of First South for over 43 years.

Walter R. Richardson**,** of Leroy, Alabama, has a cattle farm and 1,700 acres of cotton, corn, peanuts, oats and wheat. He serves on the Washington County Soil Conservation Board, is a director of Washington County Farmers Federation, which promotes agriculture in Washington County, and a board member of the Washington County Cattlemen's Association, which promotes the cattle industry. Mr. Richardson has been a member of First South for over 38 years.

Dale Thibodeaux**,** of Midland, Louisiana, has a farming operation with his family consisting of 10,000 acres, including 5,000 acres of rice, 3,400 acres of soybeans, and 1,500 acres of crawfish. His business interests include Thibodeaux Agriculture Group, Thibodeaux Brothers Farm, Thibodeaux

Brothers Trucking, Inc., Thibodeaux Land Company, Inc., Thibodeaux Brothers Dryer, Thibodeaux Brothers Water Company, Inc., Thibodeaux Crawfish, LLC, Acadia Processors, LLC, and Krewe du Meanger. He is a director of Acadia Soil and Water Conservation District, member of the Mermentau River Harbor and Terminal Board, director of Southwest Farm Service Cooperative, and a member of the Rice Council, Acadia Rice Growers Association and Louisiana Rail Facility. Mr. Thibodeaux has been a member of First South for over 36 years.

Dan West, of Monroe County, Mississippi, is the owner of West Farms and Dan West Farms, a 3,600 acre farming operation consisting of corn, cotton, soybeans, wheat, peanuts and timber. He is managing partner of Eastside Farms Inc., a member of the Mississippi Peanut Promotion Board, Mississippi Peanut Growers Association, Farmers Gin and Monroe County Farm Bureau. He is an owner/officer of Cotton House Inc. He has served on the board of Monroe County Farm Bureau, Mississippi Boll Weevil Management Corporation and is a past president of the Mississippi Ginners Association all of which promote agriculture in Mississippi. Mr. West has been a member of First South for over 39 years.

The following chart details the number of meetings, other activities and additional compensation paid for other activities (if applicable) for each director:

		Term of Office		Number of Days Serve		Compensation		
Name of Director	**Committee Assignments**	**Election Year**	**Current Term Expiration**	**Board Meeting**	**Other Official Activities***	**Compensation Regular Board Meetings**	**Compensation for Other Activities**	**Total 2018 Compensation Paid**
Michael W. (Mike) Patrick, Chairman	Governance, Retirement, Executive	2018	2021	8	13	$ 12,550	$ 3,300	$ 15,850
Daniel Mattingly, Vice Chairman	Credit, Retirement, Compensation, Executive	2016	2019	7	15	11,100	8,100	19,200
Marty Fuller	Audit, Compensation, Executive	2017	2020	7	16	9,950	2,000	11,950
Amy Ellender	Audit	2016	2019	8	9	10,520	300	10,820
Paul Briscoe	Governance	2017	2020	7	6	9,940	1,200	11,140
John R. Burden	Credit, Compensation	2016	2019	8	12	12,080	4,100	16,180
Paul Clark	Audit, Subchapter T, Retirement, Executive	2017	2020	7	14	12,200	5,200	17,400
John G. Ingraffia	Credit	2018	2021	7	5	8,780	1,200	9,980
Wilson E. Judice	Credit, Governance	2018	2021	7	5	11,000	1,200	12,200
William T. (Bill) Kyser	Credit	2017	2020	8	6	11,200	1,600	12,800
Gaston L. Lanaux, III	Governance, Executive	2015	2018**	2	3	3,680	400	4,080
Timothy L. (Tim) Leonard	Credit, Compensation, Executive	2017	2020	9	16	13,060	5,300	18,360
Ray Makamson	Governance	2018	2021	8	6	11,520	2,000	13,520
Alan Marsh	Governance, Subchapter T, Executive	2017	2020	9	12	12,600	1,200	13,800
James F. (Trey) Martin, III	Audit	2016	2019	8	9	12,400	3,100	15,500
Joe H. Morgan	Governance, Subchapter T	2016	2019	1	2	2,940	800	3,740
Shepherd (Shep) Morris	Governance, Compensation	2018	2021	9	11	13,520	4,900	18,420
Thomas H. Nelson, Jr.	Credit	2017	2020	9	7	11,640	1,600	13,240
James M. Norsworthy, III	Audit, Retirement	2017	2020	9	11	10,830	2,000	12,830
Thomas A. Parker	Governance, Subchapter T, Executive	2016	2019	8	12	11,040	2,000	13,040
Ted S. Passmore	Subchapter T, Credit	2018	2021	6	6	8,240	1,200	9,440
Walter R.(Rod) Richardson	Credit, Retirement, Executive	2018	2021	9	13	13,730	4,900	18,630
Dale Thibodeaux	Credit, Compensation	2017	2020	8	12	11,900	4,900	16,800
Dan West	Audit, Subchapter T	2016	2019		6	7,840	200	8,040
Total						$ 254,260	$ 62,700	$ 316,960

** Includes board committee meetings and other board activities other than regular board meetings*
*** Because of age limitation, Mr. Gaston L. Lanaux, III was not eligible for re-election.*

Transactions with Senior Officers and Directors

The reporting entity's policies on loans to and transactions with its officers and directors, to be disclosed in this section are incorporated herein by reference to Note 10 of the Consolidated Financial Statements, "*Related Party Transactions*," included in this Annual Report. There have been no transactions between the Association and senior officers or directors which require reporting per FCA regulations.

Involvement in Certain Legal Proceedings

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

Relationship with Independent Auditors

There were no changes in or material disagreements with our independent auditors on any matter of accounting principles or financial statement disclosure during this period. Aggregate fees paid by the Association for services rendered by its independent auditors for the year ended December 31, 2018 were as follows:

	2018
Independent Auditors	
PricewaterhouseCoopers LLP	
Audit services	$ 72,500

Audit fees were for the annual audit of the Consolidated Financial Statements.

Consolidated Financial Statements

The Consolidated Financial Statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 13, 2019 and the report of management, which appear in this Annual Report, are incorporated herein by reference.

Copies of the Association's unaudited quarterly reports are available upon request free of charge by calling 1-888-297-1722, or writing to Bryan Applewhite, First South Farm Credit, ACA, Three Paragon Centre, Suite 100, 574 Highland Colony Parkway, Ridgeland, MS 39157. Information concerning First South Farm Credit, ACA can be obtained by visiting the association website, www.firstsouthland.com. The Association prepares an electronic version of the Annual Report which is available on the Association's web site within 75 days after the end of the fiscal year and distributes the Annual Reports to shareholders within 90 days after the end of the fiscal year. The Association prepares an electronic version of the Quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Borrower Information Regulations

Since 1972, Farm Credit Administration (FCA) regulations have required that borrower information be held in strict confidence by Farm Credit System (FCS) institutions, their directors, officers and employees. These regulations provide Farm Credit institutions clear guidelines for protecting their borrowers' nonpublic personal information.

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

Credit and Services to Young, Beginning, and Small Farmers and Ranchers and Producers or Harvesters of Aquatic Products

Information to be disclosed in this section is incorporated herein by reference to the similarly named section in the Management's Discussion and Analysis of Financial Condition and Results of Operations section included in this Annual Report to the shareholders.

Shareholder Investment

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

Report of the Audit Committee

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

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

PricewaterhouseCoopers LLP (PwC), the Association's independent auditors for 2018, is responsible for expressing an opinion on the conformity of the Association's audited financial statements with accounting principles generally accepted in the United States of America. The Committee has discussed with PwC the matters that are required to be discussed by Statement on Auditing Standards No. 114 *(The Auditor's Communication With Those Charged With Governance).* The Committee discussed with PwC its independence from the Association. The Committee also reviewed the non-audit services provided by PwC and concluded that these services were not incompatible with maintaining PwC's independence.

Based on the considerations referred to above, the Committee recommended to the Board of Directors that the audited financial statements be included in the Association's Annual Report for 2018. The foregoing report is provided by the following independent directors, who constitute the Committee:

Marty J Fuller

Dr. Marty J. Fuller
Chairman of the Audit Committee

Members of Audit Committee

Paul Clark
Amy C. Ellender
James F. Martin, III
James M. Norsworthy, III
Dan West

March 13, 2019

Report of Independent Auditors

To the Board of Directors and Management of
First South Farm Credit, ACA

We have audited the accompanying consolidated financial statements of First South Farm Credit, ACA and its subsidiaries (the "Association"), which comprise the consolidated balance sheets as of December 31, 2018, 2017 and 2016, and the related consolidated statements of income, comprehensive income, changes in members' equity and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Association's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of First South Farm Credit, ACA and its subsidiaries as of December 31, 2018, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

Miami, Florida

March 13, 2019

PricewaterhouseCoopers LLP, 333 SE 2nd Avenue, Suite 3000, Miami, FL 33131
T: (305) 375 7400, F:(305) 375 6221, www.pwc.com/us

Consolidated Balance Sheets

(dollars in thousands)	December 31, 2018	2017	2016
Assets			
Cash	**$ 11,502**	$ 9,097	$ 6,574
Loans	**2,072,774**	1,976,968	1,859,238
Allowance for loan losses	**(13,941)**	(13,618)	(12,466)
Net loans	**2,058,833**	1,963,350	1,846,772
Accrued interest receivable	**20,103**	18,789	17,804
Equity investments in other Farm Credit institutions	**67,309**	67,363	67,303
Premises and equipment, net	**12,213**	9,869	9,101
Other property owned	**2,879**	551	1,098
Accounts receivable	**26,944**	28,099	24,627
Other assets	**240**	261	273
Total assets	**$ 2,200,023**	$ 2,097,379	$ 1,973,552
Liabilities			
Notes payable to AgFirst Farm Credit Bank	**$ 1,717,671**	$ 1,639,346	$ 1,543,099
Accrued interest payable	**4,718**	3,911	3,249
Patronage refunds payable	**17,555**	15,020	10,706
Accounts payable	**5,826**	8,050	6,767
Other liabilities	**30,553**	30,717	52,386
Total liabilities	**1,776,323**	1,697,044	1,616,207
Commitments and contingencies (Note 11)			
Members' Equity			
Capital stock and participation certificates	**52,969**	54,174	56,531
Retained earnings			
Allocated	**259,012**	261,054	221,800
Unallocated	**138,687**	111,152	108,424
Accumulated other comprehensive income (loss)	**(26,968)**	(26,045)	(29,410)
Total members' equity	**423,700**	400,335	357,345
Total liabilities and members' equity	**$ 2,200,023**	$ 2,097,379	$ 1,973,552

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

Consolidated Statements of Income

(dollars in thousands)	For the year ended December 31, 2018	2017	2016
Interest Income			
Loans	**$ 105,214**	$ 95,076	$ 82,569
Interest Expense			
Notes payable to AgFirst Farm Credit Bank	**50,941**	43,440	35,670
Net interest income	**54,273**	51,636	46,899
Provision for loan losses	**1,080**	1,285	1,549
Net interest income after provision for loan losses	**53,193**	50,351	45,350
Noninterest Income			
Loan fees	**1,281**	2,595	2,877
Fees for financially related services	**1,020**	1,183	1,127
Patronage refunds from other Farm Credit institutions	**26,807**	27,940	24,625
Gains (losses) on sales of premises and equipment, net	**75**	29	—
Insurance Fund refunds	**1,051**	—	—
Other noninterest income	**2**	—	—
Total noninterest income	**30,236**	31,747	28,629
Noninterest Expense			
Salaries and employee benefits	**26,574**	25,775	26,228
Occupancy and equipment	**2,045**	1,784	1,749
Insurance Fund premiums	**1,384**	2,204	2,211
(Gains) losses on other property owned, net	**111**	82	109
Other operating expenses	**8,231**	(7,096)	9,447
Total noninterest expense	**38,345**	22,749	39,744
Income before income taxes	**45,084**	59,349	34,235
Provision (benefit) for income taxes	**(22)**	116	55
Net income	**$ 45,106**	$ 59,233	$ 34,180

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

Consolidated Statements of Comprehensive Income

(dollars in thousands)	For the year ended December 31, 2018	2017	2016
Net income	**$ 45,106**	$ 59,233	$ 34,180
Other comprehensive income net of tax			
Employee benefit plans adjustments	**(923)**	3,365	(1,937)
Comprehensive income	**$ 44,183**	$ 62,598	$ 32,243

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

Consolidated Statements of Changes in Members' Equity

(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, 2015	$ 58,523	$ 203,534	$ 106,358	$ (27,473)	$ 340,942
Comprehensive income			34,180	(1,937)	32,243
Capital stock/participation certificates issued/(retired), net	(1,992)				(1,992)
Patronage distribution					
Cash			(10,700)		(10,700)
Nonqualified allocated retained earnings		10,804	(10,804)		—
Nonqualified retained earnings		10,804	(10,804)		—
Retained earnings retired		(3,160)			(3,160)
Patronage distribution adjustment		(182)	194		12
Balance at December 31, 2016	$ 56,531	$ 221,800	$ 108,424	$ (29,410)	$ 357,345
Comprehensive income			59,233	3,365	62,598
Capital stock/participation certificates issued/(retired), net	(2,357)				(2,357)
Patronage distribution					
Cash			(15,000)		(15,000)
Nonqualified allocated retained earnings		20,815	(20,815)		—
Nonqualified retained earnings		20,815	(20,815)		—
Retained earnings retired		(2,226)			(2,226)
Patronage distribution adjustment		(150)	125		(25)
Balance at December 31, 2017	$ 54,174	$ 261,054	$ 111,152	$ (26,045)	$ 400,335
Comprehensive income			**45,106**	**(923)**	**44,183**
Capital stock/participation certificates issued/(retired), net	**(1,205)**				**(1,205)**
Patronage distribution					
Cash			**(17,500)**		**(17,500)**
Retained earnings retired		**(2,110)**			**(2,110)**
Patronage distribution adjustment		**68**	**(71)**		**(3)**
Balance at December 31, 2018	**$ 52,969**	**$ 259,012**	**$ 138,687**	**$ (26,968)**	**$ 423,700**

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

Consolidated Statements of Cash Flows

(dollars in thousands)	For the year ended December 31, 2018	2017	2016
Cash flows from operating activities:			
Net income	**$ 45,106**	$ 59,233	$ 34,180
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	**422**	418	415
Amortization (accretion) of net deferred loan costs (fees)	**(661)**	(101)	(86)
Provision for loan losses	**1,080**	1,285	1,549
(Gains) losses on other property owned	**94**	68	102
(Gains) losses on sales of premises and equipment, net	**(75)**	(29)	—
Changes in operating assets and liabilities:			
(Increase) decrease in accrued interest receivable	**(1,314)**	(985)	(3,052)
(Increase) decrease in accounts receivable	**1,155**	(3,472)	(878)
(Increase) decrease in other assets	**21**	12	36
Increase (decrease) in accrued interest payable	**807**	662	462
Increase (decrease) in accounts payable	**(2,224)**	1,283	239
Increase (decrease) in other liabilities	**(1,087)**	(18,304)	5,301
Total adjustments	**(1,782)**	(19,163)	4,088
Net cash provided by (used in) operating activities	**43,324**	40,070	38,268
Cash flows from investing activities:			
Net (increase) decrease in loans	**(98,516)**	(118,947)	(261,817)
(Increase) decrease in equity investments in other Farm Credit institutions	**54**	(60)	10,709
Purchases of premises and equipment	**(2,789)**	(1,168)	(142)
Proceeds from sales of premises and equipment	**98**	11	—
Proceeds from sales of other property owned	**192**	1,664	306
Net cash provided by (used in) investing activities	**(100,961)**	(118,500)	(250,944)
Cash flows from financing activities:			
Advances on (repayment of) notes payable to AgFirst Farm Credit Bank, net	**78,325**	96,247	228,172
Capital stock and participation certificates issued/(retired), net	**(1,205)**	(2,357)	(1,992)
Patronage refunds and dividends paid	**(14,968)**	(10,711)	(9,387)
Retained earnings retired	**(2,110)**	(2,226)	(3,160)
Net cash provided by (used in) financing activities	**60,042**	80,953	213,633
Net increase (decrease) in cash	**2,405**	2,523	957
Cash, beginning of period	**9,097**	6,574	5,617
Cash, end of period	**$ 11,502**	$ 9,097	$ 6,574
Supplemental schedule of non-cash activities:			
Receipt of property in settlement of loans	**$ 2,614**	$ 1,185	$ 532
Estimated cash dividends or patronage distributions declared or payable	**17,500**	15,000	10,700
Employee benefit plans adjustments (Note 9)	**923**	(3,365)	1,937
Supplemental information:			
Interest paid	**50,134**	42,777	35,208
Taxes (refunded) paid, net	**8**	45	(31)

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)

Note 1 — Organization and Operations

A. **Organization:** First South Farm Credit, ACA (the Association or ACA) is a member-owned cooperative that provides credit and credit-related services to qualified borrowers in all counties in the states of Alabama and Mississippi, and all but certain parishes within the northwestern portion of Louisiana. The counties and parishes in the respective states are as follows:

Alabama: Autauga, Baldwin, Barbour, Bibb, Blount, Bullock, Butler, Calhoun, Chambers, Cherokee, Chilton, Choctaw, Clarke, Clay, Cleburne, Coffee, Colbert, Conecuh, Coosa, Covington, Crenshaw, Cullman, Dale, Dallas, De Kalb, Elmore, Escambia, Etowah, Fayette, Franklin, Geneva, Greene, Hale, Henry, Houston, Jackson, Jefferson, Lamar, Lauderdale, Lawrence, Lee, Limestone, Lowndes, Macon, Madison, Marengo, Marion, Marshall, Mobile, Monroe, Montgomery, Morgan, Perry, Pickens, Pike, Randolph, Russell, St. Clair, Shelby, Sumter, Talladega, Tallapoosa, Tuscaloosa, Walker, Washington, Wilcox and Winston.

Mississippi: Adams, Alcorn, Amite, Attala, Benton, Bolivar, Calhoun, Carroll, Chickasaw, Choctaw, Claiborne, Clarke, Clay, Coahoma, Copiah, Covington, Desoto, Forrest, Franklin, George, Greene, Grenada, Hancock, Harrison, Hinds, Holmes, Humphreys, Issaquena, Itawamba, Jackson, Jasper, Jefferson, Jefferson Davis, Jones, Kemper, Lafayette, Lamar, Lauderdale, Lawrence, Leake, Lee, Leflore, Lincoln, Lowndes, Madison, Marion, Marshall, Monroe, Montgomery, Neshoba, Newton, Noxubee, Oktibbeha, Panola, Pearl River, Perry, Pike, Pontotoc, Prentiss, Quitman, Rankin, Scott, Sharkey, Simpson, Smith, Stone, Sunflower, Tallahatchie, Tate, Tippah, Tishomingo, Tunica, Union, Walthall, Warren, Washington, Wayne, Webster, Wilkinson, Winston, Yalobusha and Yazoo.

Louisiana: Acadia, Allen, Ascension, Assumption, Avoyelles, Beauregard, Calcasieu, Caldwell, Cameron, Catahoula, Concordia, East Baton Rouge, East Carroll, East Feliciana, Evangeline, Franklin, Grant, Iberia, Iberville, Jefferson, Jefferson Davis, La Salle, Lafayette, Lafourche, Livingston, Madison, Morehouse, Natchitoches, Orleans, Ouachita(parts), Plaquemines, Pointe Coupee, Rapides, Richland, Sabine, St. Bernard, St. Charles, St. Helena, St. James, St. John The Baptist, St. Landry, St. Martin, St. Mary, St. Tammany, Tangipahoa, Tensas, Terrebonne, Vermilion, Vernon, Washington, West Baton Rouge, West Carroll, West Feliciana and Winn.

The Association is a lending institution in the Farm Credit System (System), a nationwide network of cooperatively owned banks and associations. It was established by Acts of Congress and is subject to the provisions of the Farm Credit Act of 1971, as amended (Farm Credit Act). The System specializes in providing financing and related services to qualified borrowers for agricultural and rural purposes.

The nation is served by three Farm Credit Banks (FCBs) and one Agricultural Credit Bank (ACB), (collectively, the System Banks) each of which has specific lending authorities within its chartered territory. The ACB also has additional specific nationwide lending authorities.

Each System Bank serves one or more Agricultural Credit Associations (ACAs) that originate long-term, short-term and intermediate-term loans, Production Credit Associations (PCAs) that originate and service short- and intermediate-term loans, and/or Federal Land Credit Associations (FLCAs) that originate and service long-term real estate mortgage loans. These associations borrow a majority of the funds for their lending activities from their related bank. System Banks are also responsible for supervising the activities of associations within their districts. AgFirst (Bank) and its related associations (Associations or District Associations) are collectively referred to as the AgFirst District. The District Associations jointly own substantially all of AgFirst's voting stock. As of year end, the District consisted of the Bank and nineteen District Associations. All nineteen are structured as ACA holding companies, with PCA and FLCA subsidiaries. FLCAs are tax-exempt while ACAs and PCAs are taxable.

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the System banks and associations. The FCA examines the activities of the associations and certain actions by the associations are subject to the prior approval of the FCA and the supervising bank.

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

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

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

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

In addition to providing funding for earning assets, the Bank provides District Associations with banking and support services such as accounting, human resources, information systems, and marketing. The costs of these support services are included in the cost of the Direct Note, or in some cases billed directly to certain Associations that use a specific service.

The Association is authorized to provide, either directly or in participation with other lenders, credit, credit commitments, and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents, and farm-related businesses.

The Association may sell to any System borrowing member, on an optional basis, credit or term life insurance appropriate to protect the loan commitment in the event of death of the debtor(s). The sale of other insurance necessary to protect a member's farm or aquatic unit is permitted, but limited to hail and multi-peril crop insurance, and insurance necessary to protect the facilities and equipment of aquatic borrowers.

Note 2 — Summary of Significant Accounting Policies

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

The accompanying consolidated financial statements include the accounts of the ACA, PCA and FLCA.

Certain amounts in the prior year financial statements have been reclassified to conform to the current period presentation. Such reclassifications had no effect on net income or total members' equity of prior years.

A. **Cash:** Cash represents cash on hand and on deposit at banks.

B. **Loans and Allowance for Loan Losses:** The Association is authorized to make long-term real estate loans with maturities of 5 to 40 years and certain short and intermediate-term loans for agricultural production or operating purposes with maturities of not more than 10 years.

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

Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms of the loan and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. Impaired loans include nonaccrual loans, restructured loans, and loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan remains contractually past due 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. A formal restructuring may also cure a past due status.

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

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

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

The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals. A review of individual loans in each respective portfolio is performed periodically to determine the appropriateness of risk ratings and to ensure loss exposure to the Association has been identified. The allowance for loan losses is a valuation account used to reasonably estimate loan losses as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss.

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

- Changes in credit risk classifications
- Changes in collateral values
- Changes in risk concentrations
- Changes in weather-related conditions
- Changes in economic conditions

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

A general allowance may also be established under FASB guidance on accounting for contingencies, to reflect estimated probable credit losses inherent in the remainder of the loan portfolio which excludes impaired loans considered under the specific allowance discussed above. A general allowance can be evaluated on a pool basis for those loans with similar characteristics. The level of the general allowance may be based on management's best estimate of the likelihood of default adjusted for other relevant factors reflecting the current environment.
The credit risk rating methodology is a key component of the Association's allowance for loan losses evaluation, and is generally incorporated into the institution's loan underwriting standards and internal lending limit. The Association uses a two-dimensional loan rating model based on internally generated combined system risk rating guidance that incorporates a 14-point risk rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default over a period of time. Probability of default is the probability that a borrower will experience a default within 12 months from the date of the determination of the risk rating. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the borrower is past due more than 90 days. The loss given default is management's estimate as to the anticipated economic loss on a specific loan assuming default has occurred or is expected to occur within the next 12 months.

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

C. **Loans Held for Sale:** Loans are classified as held for sale when there is intent to sell the loans within a reasonable period of time. Loans intended for sale are carried at the lower of cost or fair value.

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

E. **Premises and Equipment:** Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation. Depreciation is provided on the straight-line method over the estimated useful lives of the assets. Gains and losses on dispositions are reflected in current earnings. Maintenance and repairs are charged to expense and improvements are capitalized. Premises and equipment are evaluated for impairment whenever events or circumstances indicate that the carrying value of the asset may not be recoverable.

From time to time, assets classified as premises and equipment are transferred to held for sale for various reasons. These assets are carried in Other Assets at the lower of the recorded investment in the asset or fair value less estimated cost to sell based upon the property's appraised value at the date of transfer. Any write-down of property held for sale is recorded as a loss in the period identified.

F. **Investments:** The Association may hold investments as described below.

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

Investment Income
Dividends from Investments in Other Farm Credit Institutions are generally recorded as patronage income and included in Noninterest Income.

G. **Voluntary Advance Conditional Payments:** The Association is authorized under the Farm Credit Act to accept advance payments from borrowers. To the extent the borrower's access to such advance payments is restricted, the advanced conditional payments are netted against the borrower's related loan balance. Amounts in excess of the related loan balance and amounts to which the borrower has unrestricted access are presented as other liabilities in the accompanying Consolidated Balance Sheets. Advanced conditional payments are not insured. Interest is generally paid by the Association on such accounts.

H. **Employee Benefit Plans:** The Association employees may participate in Association, District and/or multi-District sponsored benefit plans. These plans may include defined benefit final average pay retirement, defined benefit cash balance retirement, defined benefit other postretirement benefits, and defined contribution plans.

Single Employer Defined Benefit Plan
Certain employees depending on date of employment may participate in the First South Farm Credit, ACA Retirement Plan (the FS Plan), a defined benefit plan. The Plan is noncontributory and includes eligible Association employees. The "Projected Unit Credit" actuarial method is used for financial reporting purposes. Since the FS Plan is a single employer plan, the Association records the FS Plan's funded status and equity items related to prior service cost, accumulated other comprehensive income (loss) and prepaid (accrued) pension expense. The adjustment to other comprehensive income (loss) would be net of deferred taxes, if significant.

The foregoing defined benefit plan is considered single employer, therefore the Association applies the provisions of FASB guidance on employers' accounting for defined benefit pension and other postretirement plans in its standalone financial statements.

Additional information may be found in Note 9.

Multi-Employer Defined Benefit Plan
In addition to pension benefits, the Association provides certain health care and life insurance benefits for retired employees (other postretirement benefits) through a multi-district sponsored retiree healthcare plan. Substantially all employees are eligible for those benefits when they reach early retirement age while working for the Association. Authoritative accounting guidance requires the accrual of the expected cost of providing these benefits to an employee, their beneficiaries and covered dependents during the years the employee renders service necessary to become eligible for benefits. The Other Postretirement Benefits plan in unfunded with expenses paid as incurred.

Since the foregoing plan is multi-employer, the Association does not apply the provisions of FASB guidance on employers' accounting for defined benefit pension and other postretirement plans in its stand-alone financial statements. Rather, the effects of this guidance are reflected in the Annual Information Statement of the Farm Credit System.

Additional information may be found in Note 9.

Defined Contribution Plans
Substantially all employees are eligible to participate in the defined contribution Farm Credit Benefit Alliance (FCBA) 401(k) Plan, subsequently referred to as the 401(k) Plan, which qualifies as a 401(k) plan as defined by the Internal Revenue Code. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. Association contributions to the 401(k) Plan are expensed as funded.

Additional information may be found in Note 9.

I. **Income Taxes:** The Association evaluates tax positions taken in previous and current years according to FASB guidance. A tax position can result in a permanent reduction of income taxes payable, a deferral of income taxes otherwise currently payable to future years, or a change in the expected realizability of deferred tax assets. The term tax position also encompasses, but is not limited to, an entity's status, including its status as a pass-through entity or tax-exempt entity.

The Association is generally subject to Federal and certain other income taxes. As previously described, the ACA holding company has two wholly-owned subsidiaries, a PCA and a FLCA. The FLCA subsidiary is exempt from federal and state income taxes as provided in the Farm Credit Act. The ACA holding company and the PCA subsidiary are subject to federal, state and certain other income taxes.

The Association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage refunds. The Association distributes patronage on the basis of book income.

The Association accounts for income taxes under the asset and liability method, recognizing deferred tax assets and liabilities for the expected future tax consequences of the temporary differences between the carrying amounts and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled.

The Association records a valuation allowance at the balance sheet dates against that portion of the Association's deferred tax assets that, based on management's best estimates of future events and circumstances, more likely than not (a likelihood of more than 50 percent) will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of the expected patronage program, which reduces taxable earnings.

J. **Due from AgFirst Farm Credit Bank:** The Association records patronage refunds from the Bank and certain District Associations on an accrual basis.

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

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

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

Level 3 inputs to the valuation methodology 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 a third-party valuation or internal model pricing.

The Association may use the Bank, internal resources or third parties to obtain fair value prices. Quoted market prices are generally used when estimating fair values of any assets or liabilities for which observable, active markets exist. A number of methodologies may be employed to value items for which an observable active market does not exist. Examples of these items include: impaired loans, other property owned, and certain derivatives, investment securities and other financial instruments. Inputs to these valuations can involve estimates and assumptions that require a substantial degree of judgment. Some of the assumptions used include, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing, and liquidation values. The use of different assumptions could produce significantly different asset or liability values, which could have material positive or negative effects on results of operations.

Additional information may be found in Note 8.

L. **Off-Balance-Sheet Credit Exposures:** The credit risk associated with commitments to extend credit and letters of credit is essentially the same as that involved with extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's assessment of the customer's creditworthiness.

Commitments to extend credit are agreements to lend to customers, generally having fixed expiration dates or other termination clauses that may require payment of a fee.

Letters of credit are commitments issued to guarantee the performance of a customer to a third party. These letters of credit are issued to facilitate commerce and typically result in the commitment being funded when the underlying transaction is consummated between the customer and third party.

M. **Revenue Recognition:** The Association generates income from multiple sources.

Financial Instruments
The largest source of revenue for the Association is Interest Income. Interest income is recognized on an accrual basis driven by nondiscretionary formulas based on written contracts, such as loan agreements or securities contracts. Credit-related fees, including letter of credit fees, finance charges and other fees are recognized in Noninterest Income when earned. Other types of noninterest revenues, such as service charges, professional services and broker fees, are accrued and recognized into income as services are provided and the amount of fees earned is reasonably determinable.

Contracts with Customers
In May 2014, the FASB issued ASU 2014-09 Revenue from Contracts with Customers (Topic 606). This guidance, which became effective January 1, 2018, changed the recognition of revenue from contracts with customers. The core principle of the guidance is that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration the entity receives or expects to receive. The guidance also included expanded disclosure requirements that result in an entity providing users of financial statements with comprehensive information about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Based on input received from stakeholders, the FASB issued several additional Updates that generally provided clarifying guidance where there was the potential for diversity in practice, or address the cost and complexity of applying Topic 606.

The Association maintains contracts with customers to provide support services in various areas such as accounting, lending transactions, consulting, insurance, and information technology. The Association does not generally incur costs to obtain contracts. As most of the contracts are to provide access to expertise or system capacity that the Association maintains, there are no material incremental costs to fulfill these contracts that should be capitalized.

Transition Information

- The Association identified ancillary revenues affected by this Update and adopted the guidance on January 1, 2018.
- The amendments were applied using the modified retrospective approach.
- The Association elected to only apply the guidance to contracts that were not completed at the date of initial application.
- Subtopics 610-20 on gains and losses from the derecognition of nonfinancial assets, and 340-40 on other assets and deferred costs-contracts with customers were adopted using the same transition options.
- Adoption did not have an impact on the Association's financial condition or results of operations.

Gains and Losses from Nonfinancial Assets
Any gains or losses on sales of Premises and Equipment and OPO are included as part of Noninterest Income. These gains and losses are recognized, and the nonfinancial asset is derecognized, when the Association has entered into a valid contract with a noncustomer and transferred control of the asset. If the criteria to meet the definition of a contract have not been met, the Association does not derecognize the nonfinancial asset and any consideration received is recognized as a liability. If the criteria for a contract are subsequently met, or if the consideration received is or becomes nonrefundable, a gain or loss may be recognized at that time.

N. **Accounting Standards Updates (ASUs):** In August 2018, the FASB issued ASU 2018-15 Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract. The amendments align 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 the amendments in this Update. The guidance is effective for public business entities for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted, including adoption in any interim period, for all entities. The amendments should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. Adoption of the guidance will have no impact on the statements of financial condition and results of operations.

In August 2018, the FASB issued ASU 2018-14 Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans. The amendments in this Update remove disclosures that are no longer considered cost beneficial, clarify the specific requirements of certain disclosures, and add new disclosure requirements identified as relevant. Although narrow in scope, the amendments are considered an important part of the FASB's efforts to improve the effectiveness of disclosures in the notes to financial statements by applying concepts in the Concepts Statement, Conceptual Framework for Financial Reporting—Chapter 8: Notes to Financial Statements. The amendments are effective for fiscal years ending after December 15, 2020, for public business entities. Early adoption is permitted for all entities.

In August 2018, the FASB issued ASU 2018-13 Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement. The amendments are part of the FASB's disclosure framework project. The project's objective and primary focus are to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by GAAP that is most important to users of each entity's financial statements. The amendments remove, modify or add certain disclosures contained in the financial statement footnotes related to fair value. Additionally, the guidance is intended to promote the appropriate exercise of discretion by entities when considering fair value measurement disclosures and to clarify that materiality is an appropriate consideration of entities and their auditors when evaluating disclosure requirements. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Certain amendments should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. Entities may early adopt the provisions in whole upon issuance or may early adopt any removed or modified disclosures upon issuance and delay adoption of the additional disclosures until their effective date. The Association has adopted the removed disclosures effective with the 2018 Annual Report.

In July 2018, the FASB issued ASU 2018-09 Codification Improvements. The amendments affect a wide variety of Topics in the Codification. They apply to all reporting entities within the scope of the affected accounting guidance. The Board has an ongoing project on its agenda about improvements to clarify the Codification or to correct unintended application of guidance. Those items generally are not expected to have a significant effect on current accounting practice. The transition and effective date guidance is based on the facts and circumstances of each amendment.

In February 2018, the FASB issued ASU 2018-02 Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The guidance allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. The amendments eliminate the stranded tax effects resulting from the Tax Cuts and Jobs Act and are intended to improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The Update also requires certain disclosures about stranded tax effects. The guidance is effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In March 2017, the FASB issued ASU 2017-08 Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities. The guidance relates to certain callable debt securities and shortens the amortization period for any premium to the earliest call date. The Update will be effective for interim and annual periods beginning after December 15, 2018 for public business entities. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In March 2017, the FASB issued ASU 2017-07 Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost related to the income statement presentation of the components of net periodic benefit cost for an entity’s sponsored defined benefit pension and other postretirement plans. The amendments were effective January 1, 2018 for the Association. Adoption in 2018 did not have a material effect on the Association’s financial statements, but did require reclassification of certain periodic pension costs to Other Operating Expenses.

In February 2017, the FASB issued ASU 2017-06 Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): Employee Benefit Plan Master Trust Reporting (a consensus of the Emerging Issues Task Force). This Update amended the guidance related to employee benefit plan master trust reporting. The new guidance provides for presentation within the plan’s financial statements of its interest in a master trust as a single line item; disclosure of the master trust’s investments by general type as well as by the dollar amount of the plan’s interest in each type; disclosure of the master trust’s other assets and liabilities and the balances related to the plan; and elimination of required disclosures for Section 401(h) accounts that are already provided by the associated defined benefit plan. The amendments are effective for fiscal years beginning after December 15, 2018. Early adoption is permitted. The Association does not expect these amendments to have a material effect on its financial statements.

In January 2017, the FASB issued ASU 2017-01 Business Combinations (Topic 805): Clarifying the Definition of a Business. The amendments provide a more robust framework to use in determining when a set of assets and activities is a business. They also support more consistency in applying the guidance, reduce the costs of application, and make the definition of a business more operable. The ASU was effective January 1, 2018 for the Association. The amendments were applied prospectively. Adoption of the guidance in 2018 had no impact on the statements of financial condition and results of operations of the Association.

In June 2016, the FASB issued ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. This Update, and subsequent clarifying guidance issued, is intended to improve financial reporting by requiring timelier recording of credit losses on financial instruments. It requires an organization to measure all expected credit losses for financial assets held at the reporting date. Financial institutions and other organizations will use forward-looking information to better estimate their credit losses. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public companies that are not SEC filers, it will take effect for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. The Association is in the process of evaluating what effects the guidance may have on the statements of financial condition and results of operations.

In February 2016, the FASB issued ASU 2016-02 Leases (Topic 842). This Update, and subsequent clarifying guidance issued, requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Leases will be classified as either finance leases or operating leases. This distinction will be relevant for the pattern of expense recognition in the income statement. The amendments will be effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years for public business entities. The Association will implement the guidance in first quarter 2019 using the practical expedients and does not expect a material impact to the financial statements.

In January 2016, the FASB issued ASU 2016-01 Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The Update, and subsequent clarifying guidance issued, was intended to improve the recognition and measurement of financial instruments. The new guidance makes targeted improvements to existing GAAP.

Transition Information

- The Association identified investment securities affected by this Update and adopted the guidance on January 1, 2018.
- The amendments related to equity securities without readily determinable fair values were applied prospectively to equity investments that existed as of the date of adoption.
- Application of the amendments did not require a cumulative effect adjustment.
- Adoption did not have an impact on the Association's financial condition or results of operations.
- The new standard did result in changes to certain disclosures.

Note 3 — Loans and Allowance for Loan Losses

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

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

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

The credit risk rating process for loans uses a two-dimensional structure, incorporating a 14-point probability of default scale (see further discussion in Note 2 subsection B above) and a separate scale addressing estimated percentage loss in the event of default. The loan rating structure incorporates borrower risk and transaction risk. Borrower risk is the risk of loss driven by factors intrinsic to the borrower. The transaction risk or facility risk is related to the structure of a credit (tenor, terms, and collateral).

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

- Real estate mortgage loans — loans made to full-time or part-time farmers secured by first lien real estate mortgages with maturities from five to thirty years. These loans may be made only in amounts up to 85 percent of the appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a federal, state, or other governmental agency. The actual percentage of loan-to-appraised value when loans are made is generally lower than the statutory required percentage.
- Production and intermediate-term loans — loans to full-time or part-time farmers that are not real estate mortgage loans. These loans fund eligible financing needs including operating inputs (such as labor, feed, fertilizer, and repairs), livestock, living expenses, income taxes, machinery or equipment, farm buildings, and other business-related expenses. Production loans may be made on a secured or unsecured basis and are most often made for a period of time that matches the borrower's normal production and marketing cycle, which is typically one year or less. Intermediate-term loans are made for a specific term, generally greater than one year and less than or equal to ten years.
- Loans to cooperatives — loans for any cooperative purpose other than for communication, power, and water and waste disposal.
- Processing and marketing loans — loans for operations to process or market the products produced by a farmer, rancher, or producer or harvester of aquatic products, or by a cooperative.
- Farm-related business loans — loans to eligible borrowers that furnish certain farm-related business services to farmers or ranchers that are directly related to their agricultural production.
- Rural residential real estate loans — loans made to individuals, who are not farmers, to purchase a single-family dwelling that will be the primary residence in open country, which may include a town or village that has a population of not more than 2,500 persons. In addition, the loan may be to remodel, improve, or repair a rural home, or to refinance existing debt. These loans are generally secured by a first lien on the property.
- Communication loans — loans primarily to finance rural communication providers.
- Power loans — loans primarily to finance electric generation, transmission and distribution systems serving rural areas.
- Water and waste disposal loans — loans primarily to finance water and waste disposal systems serving rural areas.
- International loans — primarily loans or credit enhancements to other banks to support the export of U.S. agricultural commodities or supplies. The federal government guarantees a substantial portion of these loans.
- Lease receivables — the net investment for all finance leases such as direct financing leases, leveraged leases, and sales-type leases.
- Other (including Mission Related) — additional investments in rural America approved by the FCA on a program or a case-by-case basis. Examples of such investments include partnerships with agricultural and rural community lenders, investments in rural economic development and infrastructure, and investments in obligations and mortgage securities that increase the availability of affordable housing in rural America.

A summary of loans outstanding at period end follows:

	December 31, 2018	December 31, 2017	December 31, 2016
Real estate mortgage	$ 1,617,874	$ 1,498,148	$ 1,433,647
Production and intermediate-term	375,310	383,514	344,258
Loans to cooperatives	7,844	3,368	4,209
Processing and marketing	38,867	62,001	47,402
Farm-related business	12,845	8,561	8,707
Communication	6,664	8,357	12,105
Power and water/waste disposal	3,625	3,717	–
Rural residential real estate	9,745	9,302	8,910
Total loans	$ 2,072,774	$ 1,976,968	$ 1,859,238

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

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Real estate loans are collateralized by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in loan to value ratios in excess of the regulatory maximum.

The Association may purchase or sell participation interests with other parties in order to diversify risk, manage loan volume, and comply with FCA regulations. During 2016, the Association canceled its participation in the Capitalized Participation Pool program with the Bank. As a result, the Association repurchased $112,238 of participations previously sold to AgFirst. The following tables present the principal balance of participation loans at periods ended:

December 31, 2018	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	$ 8,284	$ 16,457	$ –	$ –	$ 20,953	$ –	$ 29,237	$ 16,457
Production and intermediate-term	4,426	16,235	31	–	396	–	4,853	16,235
Loans to cooperatives	7,873	–	–	–	–	–	7,873	–
Processing and marketing	12,310	21,610	5,995	2,008	–	–	18,305	23,618
Communication	6,661	–	–	–	–	–	6,661	–
Power and water/waste disposal	3,636	–	–	–	–	–	3,636	–
Rural residential real estate	–	–	–	–	42	–	42	–
Total	$ 43,190	$ 54,302	$ 6,026	$ 2,008	$ 21,391	$ –	$ 70,607	$ 56,310

December 31, 2017	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	$ 6,417	$ 11,998	$ –	$ –	$ 31,658	$ –	$ 38,075	$ 11,998
Production and intermediate-term	10,696	16,382	–	–	421	–	11,117	16,382
Loans to cooperatives	3,385	–	–	–	–	–	3,385	–
Processing and marketing	16,404	22,793	13,328	12,115	–	–	29,732	34,908
Communication	8,323	–	–	–	–	–	8,323	–
Power and water/waste disposal	3,728	–	–	–	–	–	3,728	–
Rural residential real estate	–	–	–	–	123	–	123	–
Total	$ 48,953	$ 51,173	$ 13,328	$ 12,115	$ 32,202	$ –	$ 94,483	$ 63,288

December 31, 2016	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ 5,422	$ 11,308	$ –	$ –	$ 40,230	$ –	$ 45,652	$ 11,308
Production and intermediate-term	1,672	11,209	–	–	508	–	2,180	11,209
Loans to cooperatives	3,991	–	222	–	–	–	4,213	–
Processing and marketing	14,782	23,978	3,726	9,945	–	–	18,508	33,923
Communication	12,045	–	–	–	–	–	12,045	–
Rural residential real estate	–	–	–	–	173	–	173	–
Total	$ 37,912	$ 46,495	$ 3,948	$ 9,945	$ 40,911	$ –	$ 82,771	$ 56,440

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

	December 31, 2018			
	Due less than 1 year	Due 1 Through 5 years	Due after 5 years	Total
Real estate mortgage	$ 49,657	$ 430,430	$ 1,137,787	$ 1,617,874
Production and intermediate-term	150,931	169,055	55,324	375,310
Loans to cooperatives	–	3,612	4,232	7,844
Processing and marketing	10,080	22,201	6,586	38,867
Farm-related business	3,349	4,855	4,641	12,845
Communication	–	3,023	3,641	6,664
Power and water/waste disposal	–	–	3,625	3,625
Rural residential real estate	108	2,009	7,628	9,745
Total loans	$ 214,125	$ 635,185	$ 1,223,464	$ 2,072,774
Percentages	10.33%	30.64%	59.03%	100.00%

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

The following table shows loans and related accrued interest classified under the FCA Uniform Loan Classification System as a percentage of total loans and related accrued interest receivable by loan type as of:

	December 31,		
	2018	2017	2016
Real estate mortgage:			
Acceptable	96.95%	96.94%	96.43%
OAEM	2.36	2.19	2.59
Substandard/doubtful/loss	0.69	0.87	0.98
	100.00%	100.00%	100.00%
Production and intermediate-term:			
Acceptable	92.08%	91.17%	89.54%
OAEM	5.91	6.36	8.80
Substandard/doubtful/loss	2.01	2.47	1.66
	100.00%	100.00%	100.00%
Loans to cooperatives:			
Acceptable	100.00%	100.00%	94.73%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	5.27
	100.00%	100.00%	100.00%
Processing and marketing:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%

	December 31,		
	2018	2017	2016
Farm-related business:			
Acceptable	97.23%	95.37%	100.00%
OAEM	2.77	4.63	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Communication:			
Acceptable	100.00%	100.00%	100.00%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	100.00%
Power and water/waste disposal:			
Acceptable	100.00%	100.00%	–%
OAEM	–	–	–
Substandard/doubtful/loss	–	–	–
	100.00%	100.00%	–%
Rural residential real estate:			
Acceptable	97.90%	99.39%	99.91%
OAEM	0.68	0.61	0.09
Substandard/doubtful/loss	1.42	–	–
	100.00%	100.00%	100.00%
Total loans:			
Acceptable	98.82%	98.79%	98.90%
OAEM	1.17	1.20	1.09
Substandard/doubtful/loss	0.01	0.01	0.01
	100.00%	100.00%	100.00%

The following tables provide an aging analysis of past due loans and related accrued interest as of:

	December 31, 2018				
	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
Real estate mortgage	$ 5,201	$ 859	$ 6,060	$ 1,626,368	$ 1,632,428
Production and intermediate-term	1,565	822	2,387	378,072	380,459
Loans to cooperatives	–	–	–	7,846	7,846
Processing and marketing	–	–	–	39,049	39,049
Farm-related business	–	–	–	12,989	12,989
Communication	–	–	–	6,665	6,665
Power and water/waste disposal	–	–	–	3,629	3,629
Rural residential real estate	23	–	23	9,789	9,812
Total	$ 6,789	$ 1,681	$ 8,470	$ 2,084,407	$ 2,092,877

	December 31, 2017				
	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
Real estate mortgage	$ 4,715	$ 1,747	$ 6,462	$ 1,505,256	$ 1,511,718
Production and intermediate-term	1,620	1,753	3,373	384,972	388,345
Loans to cooperatives	–	–	–	3,369	3,369
Processing and marketing	–	–	–	62,203	62,203
Farm-related business	–	–	–	8,667	8,667
Communication	–	–	–	8,361	8,361
Power and water/waste disposal	–	–	–	3,719	3,719
Rural residential real estate	326	–	326	9,049	9,375
Total	$ 6,661	$ 3,500	$ 10,161	$ 1,985,596	$ 1,995,757

	December 31, 2016				
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans
Real estate mortgage	$ 2,033	$ 3,658	$ 5,691	$ 1,441,218	$ 1,446,909
Production and intermediate-term	418	702	1,120	347,400	348,520
Loans to cooperatives	–	–	–	4,213	4,213
Processing and marketing	–	–	–	47,515	47,515
Farm-related business	–	–	–	8,774	8,774
Communication	–	–	–	12,111	12,111
Rural residential real estate	191	–	191	8,809	9,000
Total	$ 2,642	$ 4,360	$ 7,002	$ 1,870,040	$ 1,877,042

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

	December 31,		
	2018	2017	2016
Nonaccrual loans:			
Real estate mortgage	$ 1,552	$ 2,820	$ 4,070
Production and intermediate-term	2,198	3,585	2,624
Rural residential real estate	–	–	8
Total	$ 3,750	$ 6,405	$ 6,702
Accruing restructured loans:			
Real estate mortgage	$ 1,195	$ 1,711	$ 6,521
Production and intermediate-term	1,269	1,631	2,180
Total	$ 2,464	$ 3,342	$ 8,701
Accruing loans 90 days or more past due:			
Total	$ –	$ –	$ –
Total nonperforming loans	$ 6,214	$ 9,747	$ 15,403
Other property owned	2,879	551	1,098
Total nonperforming assets	$ 9,093	$ 10,298	$ 16,501
Nonaccrual loans as a percentage of total loans	0.18%	0.32%	0.36%
Nonperforming assets as a percentage of total loans and other property owned	0.44%	0.52%	0.89%
Nonperforming assets as a percentage of capital	2.13%	2.57%	4.62%

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

	December 31,		
	2018	2017	2016
Impaired nonaccrual loans:			
Current as to principal and interest	$ 2,056	$ 2,162	$ 2,251
Past due	1,694	4,243	4,451
Total	$ 3,750	$ 6,405	$ 6,702
Impaired accrual loans:			
Restructured	$ 2,464	$ 3,342	$ 8,701
90 days or more past due	–	–	–
Total	$ 2,464	$ 3,342	$ 8,701
Total impaired loans	$ 6,214	$ 9,747	$ 15,403
Additional commitments to lend	$ 50	$ –	$ –

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

	December 31, 2018			Year Ended December 31, 2018	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 402	$ 404	$ 117	$ 526	$ 51
Production and intermediate-term	399	434	110	523	50
Total	$ 801	$ 838	$ 227	$ 1,049	$ 101
With no related allowance for credit losses:					
Real estate mortgage	$ 2,345	$ 4,332	$ –	$ 3,072	$ 296
Production and intermediate-term	3,068	4,137	–	4,018	387
Total	$ 5,413	$ 8,469	$ –	$ 7,090	$ 683
Total:					
Real estate mortgage	$ 2,747	$ 4,736	$ 117	$ 3,598	$ 347
Production and intermediate-term	3,467	4,571	110	4,541	437
Total	$ 6,214	$ 9,307	$ 227	$ 8,139	$ 784

	December 31, 2017			Year Ended December 31, 2017	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Production and intermediate-term	$ 639	$ 642	$ 222	$ 861	$ 42
Total	$ 639	$ 642	$ 222	$ 861	$ 42
With no related allowance for credit losses:					
Real estate mortgage	$ 4,531	$ 6,306	$ –	$ 6,100	$ 295
Production and intermediate-term	4,577	5,798	–	6,160	297
Total	$ 9,108	$ 12,104	$ –	$ 12,260	$ 592
Total:					
Real estate mortgage	$ 4,531	$ 6,306	$ –	$ 6,100	$ 295
Production and intermediate-term	5,216	6,440	222	7,021	339
Total	$ 9,747	$ 12,746	$ 222	$ 13,121	$ 634

	December 31, 2016			Year Ended December 31, 2016	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 233	$ 253	$ 20	$ 213	$ 10
Production and intermediate-term	1,830	1,992	160	1,677	81
Total	$ 2,063	$ 2,245	$ 180	$ 1,890	$ 91
With no related allowance for credit losses:					
Real estate mortgage	$ 10,358	$ 12,059	$ –	$ 9,493	$ 455
Production and intermediate-term	2,974	3,871	–	2,725	130
Rural residential real estate	8	8	–	7	–
Total	$ 13,340	$ 15,938	$ –	$ 12,225	$ 585
Total:					
Real estate mortgage	$ 10,591	$ 12,312	$ 20	$ 9,706	$ 465
Production and intermediate-term	4,804	5,863	160	4,402	211
Rural residential real estate	8	8	–	7	–
Total	$ 15,403	$ 18,183	$ 180	$ 14,115	$ 676

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

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Communication	Power and water/waste disposal	Rural Residential Real Estate	Total
Activity related to the allowance for credit losses:							
Balance at December 31, 2017	$ 9,588	$ 3,528	$ 390	$ 43	$ 19	$ 50	$ 13,618
Charge-offs	(296)	(531)	–	–	–	–	(827)
Recoveries	2	68	–	–	–	–	70
Provision for loan losses	1,117	7	(56)	(6)	1	17	1,080
Balance at December 31, 2018	$ 10,411	$ 3,072	$ 334	$ 37	$ 20	$ 67	$ 13,941
Balance at December 31, 2016	$ 9,050	$ 2,980	$ 325	$ 64	$ –	$ 47	$ 12,466
Charge-offs	(91)	(83)	–	–	–	–	(174)
Recoveries	28	13	–	–	–	–	41
Provision for loan losses	601	618	65	(21)	19	3	1,285
Balance at December 31, 2017	$ 9,588	$ 3,528	$ 390	$ 43	$ 19	$ 50	$ 13,618
Balance at December 31, 2015	$ 7,494	$ 2,774	$ 269	$ 75	$ –	$ 25	$ 10,637
Charge-offs	(43)	(30)	–	–	–	–	(73)
Recoveries	–	353	–	–	–	–	353
Provision for loan losses	1,599	(117)	56	(11)	–	22	1,549
Balance at December 31, 2016	$ 9,050	$ 2,980	$ 325	$ 64	$ –	$ 47	$ 12,466
Allowance on loans evaluated for impairment:							
Individually	$ 117	$ 110	$ –	$ –	$ –	$ –	$ 227
Collectively	10,294	2,962	334	37	20	67	13,714
Balance at December 31, 2018	$ 10,411	$ 3,072	$ 334	$ 37	$ 20	$ 67	$ 13,941
Individually	$ –	$ 222	$ –	$ –	$ –	$ –	$ 222
Collectively	9,588	3,306	390	43	19	50	13,396
Balance at December 31, 2017	$ 9,588	$ 3,528	$ 390	$ 43	$ 19	$ 50	$ 13,618
Individually	$ 20	$ 160	$ –	$ –	$ –	$ –	$ 180
Collectively	9,030	2,820	325	64	–	47	12,286
Balance at December 31, 2016	$ 9,050	$ 2,980	$ 325	$ 64	$ –	$ 47	$ 12,466
Recorded investment in loans evaluated for impairment:							
Individually	$ 2,747	$ 3,467	$ –	$ –	$ –	$ –	$ 6,214
Collectively	1,629,681	376,992	59,884	6,665	3,629	9,812	2,086,663
Balance at December 31, 2018	$ 1,632,428	$ 380,459	$ 59,884	$ 6,665	$ 3,629	$ 9,812	$ 2,092,877
Individually	$ 4,260	$ 5,216	$ –	$ –	$ –	$ –	$ 9,476
Collectively	1,507,458	383,129	74,239	8,361	3,719	9,375	1,986,281
Balance at December 31, 2017	$ 1,511,718	$ 388,345	$ 74,239	$ 8,361	$ 3,719	$ 9,375	$ 1,995,757
Individually	$ 10,588	$ 4,802	$ –	$ –	$ –	$ 8	$ 15,398
Collectively	1,436,321	343,718	60,502	12,111	–	8,992	1,861,644
Balance at December 31, 2016	$ 1,446,909	$ 348,520	$ 60,502	$ 12,111	$ –	$ 9,000	$ 1,877,042

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

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. There were no new TDRs that occurred during 2018, 2017 or 2016.

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 periods presented. Payment default is defined as a payment that was thirty days or more past due.

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

	Total TDRs			Nonaccrual TDRs		
	December 31,			December 31,		
	2018	2017	2016	2018	2017	2016
Real estate mortgage	$ 1,528	$ 1,780	$ 6,599	$ 333	$ 69	$ 78
Production and intermediate-term	1,269	1,631	2,180	–	–	–
Total loans	$ 2,797	$ 3,411	$ 8,779	$ 333	$ 69	$ 78
Additional commitments to lend	$ –	$ –	$ –			

The following table presents information as of period end:

	December 31, 2018
Carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession	$ –
Recorded investment of consumer mortgage loans secured by residential real estate for which formal foreclosure proceedings are in process	$ –

Note 4 — Investments

Equity Investments in Other Farm Credit 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.

The Association is required to maintain ownership in 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's investment in the Bank totaled $22,949 for 2018, $21,654 for 2017 and $19,052 for 2016. The Association owns 8.39 percent of the issued stock of the Bank as of December 31, 2018 net of any reciprocal investment. As of that date, the Bank's assets totaled $33.1 billion and shareholders' equity totaled $2.2 billion. The Bank's earnings were $306 million for 2018. In addition, the Association had an investment of $1,257 related to other Farm Credit institutions at December 31, 2018. The Bank has a reciprocal investment in the Association of $43,103 representing 8,620,554 shares of its nonvoting common stock.

Note 5 — Real Estate and Other Property

Premises and Equipment
Premises and equipment consists of the following:

	December 31,		
	2018	2017	2016
Land	$ 3,736	$ 3,711	$ 3,067
Buildings and improvements	13,057	10,654	10,303
Furniture and equipment	2,564	2,651	2,566
	19,357	17,016	15,936
Less: accumulated depreciation	7,144	7,147	6,835
Total	$ 12,213	$ 9,869	$ 9,101

Other Property Owned
Net (gains) losses on other property owned consist of the following:

	December 31,		
	2018	2017	2016
(Gains) losses on sale, net	$ –	$ (29)	$ –
Carrying value unrealized (gains) losses	94	97	102
Operating (income) expense, net	17	14	7
(Gains) losses on other property owned, net	$ 111	$ 82	$ 109

Gains on sales of other property owned were deferred if the sales involved financing from the Association and did not meet the criteria for immediate recognition. There were no deferred gains at December 31, 2018, 2017, and 2016.

Note 6 — Debt

Notes Payable to AgFirst Farm Credit Bank
Under the Farm Credit Act, the Association is obligated to borrow only from the Bank, unless the Bank approves borrowing from other funding sources. The borrowing relationship is established with the Bank through a General Financing Agreement (GFA). The GFA utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The GFA has a one year term which expires on December 31 and is renewable each year. The Association has no reason to believe the GFA will not be renewed upon expiration. The Bank, consistent with FCA regulations, has established limitations on the Association's ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2018, the Association's notes payable were within the specified limitations.

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 and the terms of the revolving lines of credit are governed by the GFA. Interest rates on both variable and fixed rate advances are generally established loan-by-loan based on the Bank's marginal cost of funds, capital position, operating costs and return objectives. In the event of prepayment of any portion of a fixed rate advance, the Association may incur a prepayment penalty in accordance with the terms of the GFA and which will be included in interest expense. The interest rate is periodically adjusted by the Bank based upon agreement between the Bank and the Association.

The weighted average interest rates on the variable rate advances were 3.43 percent for LIBOR-based loans and 3.53 percent for Prime-based loans, and the weighted average remaining maturities were 4.2 years and 1.0 years, respectively, at December 31, 2018. The weighted-average interest rate on the fixed rate and adjustable rate mortgage (ARM) loans which are match funded by the Bank was 3.22 percent, and the weighted average remaining maturity was 8.8 years at December 31, 2018. The weighted-average interest rate on all interest-bearing notes payable was 3.26 percent and the weighted-average remaining maturity was 7.9 years at December 31, 2018. Gross notes payable consists of approximately 14.03 percent variable rate and 85.97 percent fixed rate portions, representing a match-funding of the Association's loan volume at December 31, 2018. Notes Payable to AgFirst Farm Credit Bank, as reflected on the Consolidated Balance Sheets, also includes a credit which reduces the notes payable balance and corresponding interest expense. The weighted average maturities described above are related to matched-funded loans. The direct note itself has an annual maturity as prescribed in the GFA.

Note 7 — Members' Equity

A description of the Association's capitalization requirements, protection mechanisms, regulatory capitalization requirements and restrictions, and equities are provided below:

A. **Protected Borrower Stock:** Protection of certain borrower stock is provided under the Farm Credit Act, which requires the Association, when retiring protected borrower stock, to retire such stock at par or stated value regardless of its book value. Protected borrower stock includes capital stock and participation certificates, which were outstanding as of January 6, 1988, or were issued or allocated prior to October 6, 1988. If an Association is unable to retire protected borrower stock at par value or stated value, amounts required to retire this equity would be obtained from the Insurance Fund.

B. **Capital Stock and Participation Certificates:** In accordance with the Farm Credit Act and the Association's capitalization bylaws, each borrower is required to invest in Class C stock for agricultural loans, or participation certificates in the case of rural home and farm-related business loans, as a condition of borrowing. The initial borrower investment, through either purchase or transfer, must be in an amount equal to 2 percent of the loan, or $1 thousand, whichever is less. The Board of Directors may increase the amount of investment if necessary to meet the Association's capital needs. Loans designated for sale or sold into the Secondary Market on or after April 16, 1996 will have no voting stock or participation certificate purchase requirement if sold within 180 days following the date of designation.

   The borrower acquires ownership of the capital stock or participation certificates at the time the loan is made, but usually does not make a cash investment. The aggregate par value is generally added to the principal amount of the related loan obligation. The Association retains a first lien on the stock or participation certificates owned by borrowers. Retirement of such equities will generally be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock or participation certificates.

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

   There are currently no prohibitions in place that would prevent the Association from retiring stock, distributing earnings, or paying dividends per the statutory and regulatory restrictions, and the Association has no reason to believe any such restrictions may apply in the future.

   Effective January 1, 2017, the regulatory capital requirements for System Banks and associations were modified. The new 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. New regulations replaced core surplus and total surplus ratios with common equity tier 1 (CET1) capital, tier 1 capital, and total capital risk-based ratios. The new regulations also include a tier 1 leverage ratio and an unallocated retained earnings (URE) and URE equivalents (UREE) leverage ratio. The permanent capital ratio (PCR) remains in effect.

   The ratios are calculated using three-month average daily balances, in accordance with FCA regulations, as follows:

   - The CET1 capital ratio is the sum of statutory minimum purchased borrower stock, other required borrower stock held for a minimum of 7 years, allocated equities held for a minimum of 7 years or not subject to revolvement, unallocated retained earnings, paid-in capital, less certain regulatory required deductions including the amount of investments in other System institutions, divided by average risk-adjusted assets.
   - The tier 1 capital ratio is CET1 capital plus non-cumulative perpetual preferred stock, divided by average risk-adjusted assets.
   - The total capital ratio is tier 1 capital plus other required borrower stock held for a minimum of 5 years, subordinated debt and limited-life preferred stock greater than 5 years to maturity at issuance subject to certain limitations, allowance for loan losses and reserve for unfunded commitments under certain limitations less certain investments in other System institutions under the corresponding deduction approach, divided by average risk-adjusted assets.
   - The permanent capital ratio is all at-risk borrower stock, any allocated excess stock, unallocated retained earnings, paid-in capital, subordinated debt and preferred stock subject to certain limitations, less certain investments in other System institutions, divided by PCR risk-adjusted assets.
   - The tier 1 leverage ratio is tier 1 capital, divided by average assets less regulatory deductions to tier 1 capital.
   - The URE and UREE leverage ratio is unallocated retained earnings, paid-in capital, and allocated surplus not subject to revolvement less certain regulatory required deductions including the amount of allocated investments in other System institutions divided by average assets less regulatory deductions to tier 1 capital.

The following sets forth the regulatory capital ratios which were effective January 1, 2017:

Ratio	Minimum Requirement	Capital Conservation Buffer*	Minimum Requirement with Capital Conservation Buffer	Capital Ratios as of December 31, 2018	2017
Risk-adjusted ratios:					
CET1 Capital	4.5%	1.25%	5.75%	17.50%	16.43%
Tier 1 Capital	6.0%	1.25%	7.25%	17.50%	16.43%
Total Capital	8.0%	1.25%	9.25%	18.29%	17.35%
Permanent Capital	7.0%	0.0%	7.0%	17.85%	16.92%
Non-risk-adjusted ratios:					
Tier 1 Leverage	4.0%	1.0%	5.0%	17.45%	16.42%
URE and UREE Leverage	1.5%	0.0%	1.5%	11.34%	10.91%

** The capital conservation buffers have a 3 year phase-in period and will become fully effective January 1, 2020. Risk-adjusted ratio minimums will increase 0.625% each year until fully phased in. There is no phase-in period for the tier 1 leverage ratio.*

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.

D. **Description of Equities:** The Association is authorized to issue or have outstanding Class A Nonvoting Common Stock, Class C Voting Common Stock, and Class D Preferred Stock, and nonvoting Participation Certificates. All stock and participation certificates have a par or face value of five dollars ($5.00) per share.

The Association had the following shares outstanding at December 31, 2018:

Class	Protected	Shares Outstanding: Number	Aggregate Par Value
A Common/Nonvoting	No	22,162	$ 111
C Common/Voting	No	1,912,960	9,564
A Common Issued to Bank/Nonvoting	No	8,620,554	43,103
C Participation Certificates/Nonvoting	No	38,171	191
Total Capital Stock and Participation Certificates		10,593,847	$ 52,969

Protected common stock and participation certificates are retired at par or face value in the normal course of business. At-risk common stock and participation certificates are retired at the sole discretion of the Board at book value not to exceed par or face amounts, provided the minimum capital adequacy standards established by the Board are met.

Surplus Accounts

The Association maintains an unallocated surplus account and an allocated surplus account. The minimum aggregate amounts of these two accounts shall be prescribed by the Farm Credit Act and the FCA regulations. The allocated surplus account consists of earnings held therein and allocated to borrowers on a patronage basis.

In the event of a net loss for any fiscal year, such loss shall be absorbed by, first, charges to the unallocated surplus account; second, impairment of paid-in surplus; and third, impairment of the allocated surplus account on the basis of latest allocations first.

The Association shall have a first lien on all surplus account allocations owned by any borrower, and all distributions thereof, as additional collateral for such borrower's indebtedness to the Association. When the debt of a borrower is in default or is in the process of final liquidation, the Association may, upon notice to the borrower, order any and all surplus account allocations owned by such borrower to be applied against the indebtedness. Any such retirement and application against indebtedness of surplus account allocations shall be before similar retirement and application of stock or participation certificates owned by the borrower.

When all of the stock and participation certificates of the Association owned by a borrower are retired or otherwise disposed of, any surplus account allocations owned by such borrower may also be retired upon request by the borrower and subject to the approval of the Board, and the proceeds paid to the borrower. Alternatively, if the Board so directs, upon notice to the borrower such surplus account allocations may be applied against any of the borrower's indebtedness to the Association.

Subject to the Farm Credit Act and FCA regulations, allocated surplus may be distributed in cash, oldest allocations first. The cash proceeds may be applied against the indebtedness of the borrower to the Association. In no event shall such distributions reduce the surplus account below the minimum amount prescribed by the Farm Credit Act and FCA regulations. Distributions of less than the full amount of all allocations issued as of the same date shall be on a pro rata basis.

Allocated equities shall be retired solely at the discretion of the Board, provided that minimum capital standards established by the FCA and the Board are met.

At December 31, 2018, allocated members' equity consisted of $2,655 of qualified surplus, $126,433 of nonqualified allocated surplus and $129,924 of nonqualified retained surplus.

Patronage Distributions

Prior to the beginning of any fiscal year, the Board, by adoption of a resolution, may obligate the Association to distribute to borrowers on a patronage basis all or any portion of available net earnings for such fiscal year or for that and subsequent fiscal years. Patronage distributions are based on the proportion of the borrower's interest to the amount of interest earned by the Association on its total loans unless another proportionate patronage basis is approved by the Board.

If the Association meets its capital adequacy standards after making the patronage distributions, the patronage distributions may be in cash, authorized stock of the Association, allocations of earnings retained in an allocated members' equity account, or any one or more of such forms of distribution. Patronage distributions of the Association's earnings may be paid on either a qualified or nonqualified basis, or a combination of both, as determined by the Board. A minimum of 20 percent of the total qualified patronage distribution to any borrower for any fiscal year shall always be paid in cash.

Transfer

Stock and participation certificates may be transferred only to persons eligible to purchase and hold such stock or participation certificates.

Impairment

Any net losses recorded by the Association shall first be applied against unallocated members' equity. To the extent such losses would exceed unallocated members' equity, such losses would be applied consistent with the Association's bylaws and distributed pro rata to each share and/or unit outstanding in the class, in the following order:

1. Allocated Surplus
2. Class A Nonvoting Common Stock and Class C Voting Common Stock and unit of participation certificates outstanding.
3. Class D Preferred Stock Liquidation

In the event of liquidation or dissolution of the Association, any assets of the Association remaining after payment or retirement of all liabilities shall be distributed to the holders of stock and participation certificates in the following order of priority:

1. To the holders of Class D Preferred Stock, if any, pro rata in proportion to the number of shares then issued and outstanding until an amount equal to the aggregate par value of all such shares has been distributed to all such holders.
2. To the holders of Class A Nonvoting Common Stock and Class C Voting Common Stock and participation certificates, pro rata in proportion to the number of shares or units of each such class of stock or
3. Participation certificates then issued and outstanding until an amount equal to the aggregate par value of all such shares or units have been distributed to all such holders.
4. To the holders of allocated surplus evidenced by written notices of allocation on a pro-rata basis until all such allocated surplus has been distributed to such holders.
5. Any remaining assets of the Association after such distributions shall be distributed to the holders of Class A Nonvoting Common Stock and Class C Voting Common Stock, and participation certificates, pro rata in proportion to the number of shares or units then outstanding.

E. **Accumulated Other Comprehensive Income (AOCI):**

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

	For the Years Ended December 31,		
	2018	**2017**	**2016**
Employee Benefit Plans:			
Balance at beginning of period	$ (26,045)	$ (29,410)	$ (27,473)
Other comprehensive income before reclassifications	(2,811)	927	(4,150)
Amounts reclassified from AOCI	1,888	2,438	2,213
Net current period OCI	(923)	3,365	(1,937)
Balance at end of period	$ (26,968)	$ (26,045)	$ (29,410)

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

	For the Years Ended December 31,			
	2018	**2017**	**2016**	**Income Statement Line Item**
Defined Benefit Pension Plans:				
Periodic pension costs	$ (1,888)	$ (2,438)	$ (2,213)	See Note 9.
Amounts reclassified	$ (1,888)	$ (2,438)	$ (2,213)	

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

Note 8 — 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.

Estimating the fair value of the Association's equity investments in the Bank and Other Farm Credit Institutions is not practicable because the stock is not traded. The net investment is a requirement of borrowing from the Bank and is carried at cost.

The classifications within the fair value hierarchy (See Note 2) are as follows:

Level 1
The Association had no Level 1 assets and liabilities measured at fair value on a recurring basis. For cash, the carrying value is primarily utilized as a reasonable estimate of fair value.

Level 2
The Association had no Level 2 assets and liabilities measured at fair value on a recurring basis.

Level 3
Because no active market exists for the Association's accruing loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans currently would be made to borrowers with similar credit risk. The loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

Fair values of loans in a nonaccrual status are estimated to be the carrying amount of the loan less specific reserves. 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.

Notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

Other property owned is classified as a Level 3 asset. 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. Other property owned consists of real and personal property acquired through foreclosure or deed in lieu of foreclosure and is carried as an asset held for sale, which is generally not its highest and best use. These properties are part of the Association's credit risk mitigation efforts, not its ongoing business. In addition, FCA regulations require that these types of property be disposed of within a reasonable period of time.

For commitments to extend credit, the estimated market value of off-balance-sheet commitments is minimal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics; therefore, the related credit risk is not significant.

There were no Level 3 assets and 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. Other Financial Instruments are not measured at fair value in the statement of financial position, but their fair values are estimated as of each period end date. The following tables summarize the carrying amounts of these assets and liabilities at period end, and their related fair values.

	December 31, 2018				
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Recurring Measurements					
Assets:					
Recurring Assets	$ –	$ –	$ –	$ –	$ –
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 574	$ –	$ –	$ 574	$ 574
Other property owned	2,879	–	–	3,311	3,311
Nonrecurring Assets	$ 3,453	$ –	$ –	$ 3,885	$ 3,885
Other Financial Instruments					
Assets:					
Cash	$ 11,502	$ 11,502	$ –	$ –	$ 11,502
Loans	2,058,259	–	–	2,004,519	2,004,519
Other Financial Assets	$ 2,069,761	$ 11,502	$ –	$ 2,004,519	2,016,021
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 1,717,671	$ –	$ –	$ 1,690,148	$ 1,690,148
Other Financial Liabilities	$ 1,717,671	$ –	$ –	$ 1,690,148	$ 1,690,148

	December 31, 2017				
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Recurring Measurements					
Assets:					
Recurring Assets	$ –	$ –	$ –	$ –	$ –
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 417	$ –	$ –	$ 417	$ 417
Other property owned	551	–	–	634	634
Nonrecurring Assets	$ 968	$ –	$ –	$ 1,051	$ 1,051
Other Financial Instruments					
Assets:					
Cash	$ 9,097	$ 9,097	$ –	$ –	$ 9,097
Loans	1,962,933	–	–	1,922,942	1,922,942
Other Financial Assets	$ 1,972,030	$ 9,097	$ –	$ 1,922,942	1,932,039
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 1,639,346	$ –	$ –	$ 1,620,777	$ 1,620,777
Other Financial Liabilities	$ 1,639,346	$ –	$ –	$ 1,620,777	$ 1,620,777

	December 31, 2016				
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Recurring Measurements					
Assets:					
Recurring Assets	$ –	$ –	$ –	$ –	$ –
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 1,883	$ –	$ –	$ 1,883	$ 1,883
Other property owned	1,098	–	–	1,263	1,263
Nonrecurring Assets	$ 2,981	$ –	$ –	$ 3,146	$ 3,146
Other Financial Instruments					
Assets:					
Cash	$ 6,574	$ 6,574	$ –	$ –	$ 6,574
Loans	1,844,889	–	–	1,808,574	1,808,574
Other Financial Assets	$ 1,851,463	$ 6,574	$ –	$ 1,808,574	1,815,148
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 1,543,099	$ –	$ –	$ 1,523,853	$ 1,523,853
Other Financial Liabilities	$ 1,543,099	$ –	$ –	$ 1,523,853	$ 1,523,853

SENSITIVITY TO CHANGES IN SIGNIFICANT UNOBSERVABLE INPUTS

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

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

Inputs to Valuation Techniques

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

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

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Fair Value		Valuation Technique(s)	Unobservable Input	Range
Impaired loans and other property owned	$	3,885	Appraisal	Income and expense	*
				Comparable sales	*
				Replacement costs	*
				Comparability adjustments	*

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

Information about Other Financial Instrument Fair Value Measurements

	Valuation Technique(s)	Input
Cash	Carrying Value	Par/Principal and appropriate interest yield
Loans	Discounted cash flow	Prepayment forecasts
		Probability of default
		Loss severity
Notes payable to AgFirst Farm Credit Bank	Discounted cash flow	Prepayment forecasts
		Probability of default
		Loss severity

Note 9 — Employee Benefit Plans

The Association participates in a single employer benefit plan and two District sponsored benefit plans. These plans include the First South Farm Credit, ACA Retirement Plan (FS Plan), which is a single employer final average pay plan. In addition, the Association participates in a multi-employer defined benefit other postretirement benefits plan (OPEB Plan), the Farm Credit Benefits Alliance Retiree and Disabled Medical and Dental Plan, and a defined contribution 401(k) plan. The risks of participating in these multi-employer plans are different from single-employer plans in the following aspects:

1. Assets contributed to multi-employer plans by one employer may be used to provide benefits to employees of other participating employers.
2. If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.
3. If the Association chooses to stop participating in some of its multi-employer plans, the Association may be required to contribute to eliminate the underfunded status of the plan.

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

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

Substantially all employees of the Association hired before January 1, 2009 are eligible to participate in the FS Plan which is a defined benefit plan. This plan is noncontributory, and benefits are based on eligible compensation and years of service. Contributions into the FS Plan were $2,241 for 2018, $2,980 for 2017, and $2,405 for 2016. Expenses for the FS plan included in salaries and employee benefits were $2,785 for 2018, $3,589 for 2017, and $3,611 for 2016.

In addition to providing pension benefits, the Association provides certain medical and dental benefits for eligible retired employees through the OPEB Plan. Substantially all of the Association employees may become eligible for the benefits if they reach early retirement age while working for the Association. Early retirement age is defined as a minimum of age 55 and 10 years of service. Employees hired after December 31, 2002, and employees who separate from service between age 50 and age 55, are required to pay the full cost of their retiree health insurance coverage. Employees who retire subsequent to December 1, 2007 are no longer provided retiree life insurance benefits. The OPEB Plan includes other Farm Credit System employees that are not employees of the Association or District and is accounted for as a multiemployer plan. The related net benefit plan obligations are not included in the Association's Balance Sheets but are included in the Combined Statement of Condition for the Farm Credit System. The OPEB Plan is unfunded with expenses paid as incurred. Postretirement benefits other than pensions included in employee benefit costs on the Association's Statements of Income were $710 for 2018, $589 for 2017, and $1,262 for 2016. At December 31, 2018, the total AgFirst District liability balance for the OPEB Plan presented in the Farm Credit System Combined Statement of Condition is $181,820.

During 2017, the method of recording expenses at participating District entities for the OPEB Plan was modified. Prior to 2017, expense was recorded based on allocations of actuarially-determined costs and any differences between recorded expense and actual contributions were recorded in Other Assets or Other Liabilities on the Consolidated Balance Sheets. For 2017 and future years, participating entities will record employee benefit costs based on the actual contributions to the Plans. This change caused the Association to modify its accounting estimates recorded in Other Assets and Other Liabilities since the assets and liabilities do not impact future contributions to the Plans. The change in estimate resulted in the reduction of Other Liabilities by $16,202 on the Association's Balance Sheets, and a total reduction of noninterest expenses on the Association's Statements of Income of $16,202 during 2017.

The Association also participates in a defined contribution Farm Credit Benefits Alliance (FCBA) 401(k) Plan, which qualifies as a 401(k) plan as defined by the Internal Revenue Code. For employees hired on or prior to December 31, 2008, the Association contributes $0.50 for each $1.00 of the employee's first 6.00 percent of contribution (based on total compensation) up to the maximum employer contribution of 3.00 percent of total compensation. For employees hired on or after January 1, 2009, the Association contributes $1.00 for each $1.00 of the employee's first 6.00 percent of contribution up to the maximum employer contribution of 6.00 percent of total compensation. Employee deferrals are not to exceed the maximum deferral as determined and adjusted by the Internal Revenue Service. The 401(k) Plan costs are expensed as funded. Employer contributions to this plan included in salaries and employee benefit costs were $955, $867, and $823 for the years ended December 31, 2018, 2017, and 2016, respectively. Beginning in 2015, contributions include an additional 3.00 percent of eligible compensation for employees hired after December 31, 2008.

FASB guidance further requires the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of AOCI. Under the guidance, these amounts are subsequently recognized as components of net periodic benefit costs over time. For 2018, 2017, and 2016, $(923), $3,365 and $(1,937) has been recognized as a net debit, a net credit, and a net debit to AOCI to reflect these elements.

The funding status and the amounts recognized in the Consolidated Balance Sheets of the Association at December 31, for the retirement plan follow:

	Pension Benefits		
	2018	2017	2016
Change in benefit obligation			
Benefit obligation at beginning of year	$ 110,149	$ 100,773	$ 92,783
Service cost	2,254	2,240	2,188
Interest cost	4,056	4,264	4,181
Actuarial loss (gain)	(8,968)	6,095	4,689
Benefits paid	(3,855)	(3,223)	(3,068)
Benefit obligation at end of year	$ 103,636	$ 110,149	$ 100,773
Change in plan assets			
Fair value of plan assets, beginning of year	$ 84,537	$ 72,405	$ 67,557
Actual return on plan assets	(6,144)	12,557	5,696
Employer contributions	2,241	2,980	2,405
Benefits paid	(3,855)	(3,223)	(3,068)
Expenses	(221)	(182)	(185)
Fair value of plan assets, end of year	$ 76,558	$ 84,537	$ 72,405
Funded status	$ (27,078)	$ (25,612)	$ (28,368)
Fourth quarter contributions	–	–	–
Net amount recognized	$ (27,078)	$ (25,612)	$ (28,368)
Amounts recognized consist of:			
Pension assets	$ –	$ –	$ –
Pension liabilities	(27,078)	(25,612)	(28,368)
Net amount recognized	$ (27,078)	$ (25,612)	$ (28,368)

The following represent the amounts included in accumulated other comprehensive income at December 31:

	2018	2017	2016
Net actuarial loss (gain)	$ 26,968	$ 26,045	$ 29,410
Prior service costs (credit)	–	–	–
Net transition obligation (asset)	–	–	–
Total amount recognized in OCI	$ 26,968	$ 26,045	$ 29,410

The accumulated benefit obligation for the defined benefit plans was $94,493, $98,737, and $90,332 at December 31, 2018, 2017 and 2016, respectively.

Information for pension plans with an accumulated benefit obligation in excess of plan assets:

	2018	2017	2016
Projected benefit obligation	$ 103,636	$ 110,149	$ 100,773
Accumulated benefit obligation	94,493	98,737	90,332
Fair value of plan assets	76,558	84,537	72,405

Components of net periodic benefit cost and other amounts recognized in net income for the years December 31 are as follows:

	Pension Benefits		
	2018	**2017**	**2016**
Net periodic benefit (income) cost			
Service cost	$ 2,254	$ 2,240	$ 2,188
Interest cost	4,056	4,264	4,181
Expected return on plan assets	(5,413)	(5,353)	(4,972)
Amortization of net (gain) loss	–	–	–
Amortization of prior service cost	–	–	–
Recognized net actuarial (gain)/loss	1,888	2,438	2,214
Net periodic benefit (income) cost	$ 2,785	$ 3,589	$ 3,611

Other changes in plan assets and benefit obligations recognized in other comprehensive income follows:

	2018	2017	2016
Net actuarial loss (gain)	$ 2,811	$ (927)	$ 4,151
Amortization of net actuarial loss (gain)	(1,888)	(2,438)	(2,214)
Adjustment for adoption of new accounting guidance	–	–	–
Amortization of prior service cost	–	–	–
Amortization of transition obligation (asset)	–	–	–
Total recognized in other comprehensive income	$ 923	$ (3,365)	$ 1,937
Total recognized in net periodic pension cost and other comprehensive income	$ 3,708	$ 224	$ 5,548

The total estimated net actuarial gain, transition asset/liabilities and prior service cost for the pension plan that will be amortized into income during 2019 is $2,202.

Assumptions:	**2018**	**2017**	**2016**
Weighted-average assumptions used to determine benefit obligations at December 31			
Discount rate	4.40%	3.75%	4.30%
Rate of compensation increase	5.00%	5.00%	5.00%
Weighted-average assumptions used to determine net periodic benefit cost for years ended December 31			
Discount rate	3.75%	4.30%	4.60%
Expected long-term return on plan assets	6.50%	7.50%	7.50%
Rate of compensation increase	5.00%	5.00%	5.00%

In 2018, 2017, and 2016, the Association used a long-term rate of return of 6.50 percent, 7.50 percent, and 7.50 percent, respectively. The assumption is based on the target allocation for plan assets and capital market forecasts for the asset classes employed. Prevailing market conditions and historical results were used to determine the capital market forecasts used in this 6.50 percent return assumption for 2018.

Plan Assets

Plan assets are invested in a number of different asset classes, with each asset class further diversified through the engagement of a number of independent investment managers. This diversification across asset classes and investment managers reduces the investment risk of the plan and avoids any concentration of risk. To further ensure that excessive risk concentrations are avoided, holdings and performance of fund managers is monitored quarterly by an outside pension consulting firm and by the Association retirement committee. There were no significant concentrations of investment risk as of December 31, 2018.

Target allocation for asset categories for 2018 are as follows:

Asset Category	
Equity securities	60-70%
Debt securities	30-40%
	100%

	Actual Plan Asset Allocation		
	2018	**2017**	**2016**
Equity Securities	70%	72%	71%
Debt Securities	28%	25%	28%
Other	2%	3%	1%
	100%	100%	100%

The fair values of the Association's pension plan assets by asset category are as follows. See Notes 2 and 8 regarding a description of the three levels of inputs and the classification within the fair value hierarchy.

	Fair Value Measurements at December 31, 2018			
	Level 1	Level 2	Level 3	Total Fair Value
Asset Category				
Cash and cash equivalents	$ 1,653	$ –	$ –	$ 1,653
Mutual funds:				
Domestic equity funds	27,834	–	–	27,834
International equity funds	–	–	–	
Common Collective Trust:				
Fixed income fund	–	–	–	
Fixed income securities:				
U.S. Treasuries	–	–	–	
Corporate bonds	–	–	–	
Mortgage-backed securities	–	–	–	
Collateralized mortgage obligations	–	–	–	
Foreign bonds	–	–	–	
Common stock	1	–	–	1
Total assets in the fair value hierarchy	$ 29,488	$ –	$ –	$ 29,488
Investments measured at net asset value				47,070
Total assets at fair value				$ 76,558

	Fair Value Measurements at December 31, 2017			
	Level 1	Level 2	Level 3	Total Fair Value
Asset Category				
Cash and cash equivalents	$ 2,706	$ –	$ –	$ 2,706
Mutual funds:				
Domestic equity funds	29,855	–	–	29,855
International equity funds	–	–	–	–
Common Collective Trust:				
Fixed income fund	–	–	–	–
Fixed income securities:				
U.S. Treasuries	–	–	–	–
Corporate bonds	–	–	–	–
Mortgage-backed securities	–	–	–	–
Collateralized mortgage obligations	–	–	–	–
Foreign bonds	–	–	–	–
Common stock	1	–	–	1
Total assets in the fair value hierarchy	$ 32,562	$ –	$ –	$ 32,562
Investments measured at net asset value				51,975
Total assets at fair value				$ 84,537

	Fair Value Measurements at December 31, 2016			
	Level 1	Level 2	Level 3	Total Fair Value
Asset Category				
Cash and cash equivalents	$ 427	$ –	$ –	$ 427
Mutual funds:				
Domestic equity funds	25,270	–	–	25,270
International equity funds	–	–	–	–
Common Collective Trust:				
Fixed income fund	–	–	–	–
Fixed income securities:				
U.S. Treasuries	–	–	–	–
Corporate bonds	–	–	–	–
Mortgage-backed securities	–	–	–	–
Collateralized mortgage obligations	–	–	–	–
Foreign bonds	–	–	–	–
Common stock	1	–	–	1
Total assets in the fair value hierarchy	$ 25,698	$ –	$ –	$ 25,698
Investments measured at net asset value				46,707
Total assets at fair value				$ 72,405

Cash Flows

Contributions: The total employer contribution expected during 2019 is $2,241.

Estimated Benefit Payments: Estimated future benefit payments are as follows:

2019	$ 4,605
2020	$ 5,103
2021	$ 5,846
2022	$ 6,470
2023	$ 6,766
2024-2028	$ 34,824

Additional information for the above may be found in the Notes to the Annual Information Statement of the Farm Credit System.

Note 10 — Related Party Transactions

In the ordinary course of business, the Association enters into loan transactions with officers and directors of the Association, their immediate families and other organizations with which such persons may be associated. Such loans are subject to special approval requirements contained in the FCA regulations and are made on the same terms, including interest rates, amortization schedule, and collateral, as those prevailing at the time for comparable transactions with unaffiliated borrowers.

Total loans to such persons at December 31, 2018 amounted to $45,626. During 2018, $48,247 of new loans were made and repayments totaled $37,302. In the opinion of management, none of these loans outstanding at December 31, 2018 involved more than a normal risk of collectability.

Note 11 — Commitments and Contingencies

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 not probable 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. In the normal course of business, the Association may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers. These financial instruments may include commitments to extend credit or letters of credit.

The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the financial statements. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commercial letters of credit are agreements to pay a beneficiary under conditions specified in the letter of credit. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee.

Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these credit-related financial instruments have off-balance-sheet credit risk because their amounts are not reflected on the Consolidated Balance Sheets until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and management applies the same credit policies to these commitments. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. At December 31, 2018, $293,992 of commitments to extend credit and no commercial letters of credit were outstanding. There was no reserve for unfunded commitments included in Other Liabilities in the Consolidated Balance Sheets at December 31, 2018.

The Association also participates in standby letters of credit to satisfy the financing needs of its borrowers. These letters of credit are irrevocable agreements to guarantee payments of specified financial obligations. At December 31, 2018, standby letters of credit outstanding totaled $827 with expiration dates ranging from January 1, 2019 to December 31, 2019. The maximum potential amount of future payments that may be required under these guarantees was $827.

Note 12 — Income Taxes

The provision (benefit) for income taxes follows:

	Year Ended December 31,		
	2018	2017	2016
Current:			
Federal	$ (23)	$ 108	$ 56
State	1	8	(1)
	(22)	116	55
Deferred:			
Federal	–	–	–
State	–	–	–
Total provision (benefit) for income taxes	$ (22)	$ 116	$ 55

The provision (benefit) for income tax differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to pretax income as follows:

	December 31,		
	2018	2017	2016
Federal tax at statutory rate	$ 9,468	$ 20,772	$ 11,982
State tax, net	1	8	(1)
Patronage distributions	(3,675)	(5,250)	(3,745)
Tax-exempt FLCA earnings	(5,668)	(12,689)	(8,654)
Change in valuation allowance	72	(6,421)	667
Change in future tax rate	–	821	–
Change in FASB guidance, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" Liability	(159)	2,350	(530)
Other	(61)	525	336
Provision (benefit) for income taxes	$ (22)	$ 116	$ 55

In late December 2017, federal tax legislation was enacted which, among other things, lowered the federal corporate tax rate from 35% to 21% beginning on January 1, 2018. The change to the lower corporate tax rate led to an insignificant remeasurement of the deferred tax liabilities and deferred tax assets in 2017, the period of enactment. Deferred tax assets and liabilities are comprised of the following at:

	December 31,		
	2018	2017	2016
Deferred income tax assets:			
Allowance for loan losses	$ 754	$ 798	$ 1,265
Nonaccrual loan interest	629	646	524
Pensions and other postretirement benefits	3,541	3,382	9,431
Loan origination fees	4	6	12
Depreciation	–	20	28
Acquired property write downs	1	–	13
Gross deferred tax assets	4,929	4,852	11,273
Less: valuation allowance	(4,925)	(4,852)	(11,273)
Gross deferred tax assets, net of valuation allowance	4	–	–
Deferred income tax liabilities:			
Gross deferred tax liability	(4)	–	–
Net deferred tax asset (liability)	$ –	$ –	$ –

At December 31, 2018, deferred income taxes have not been provided by the Association on approximately $55.7 million of patronage refunds received from the Bank prior to January 1, 1993.

Such refunds, distributed in the form of stock, are subject to tax only upon conversion to cash. The tax liability related to future conversions is not expected to be material.

The Association recorded a valuation allowance of $4,925, $4,852 and $11,273 as of December 31, 2018, 2017 and 2016, respectively. The Association will continue to evaluate the realizability of these deferred tax assets and adjust the valuation allowance accordingly.

There were no uncertain tax positions identified related to the current year and the Association has no unrecognized tax benefits at December 31, 2018 for which liabilities have been established. The Association recognizes interest and penalties, if any, related to unrecognized tax benefits as a component of income tax expense.

The tax years that remain open for federal and major state income tax jurisdictions are 2015 and forward.

Note 13 — Additional Financial Information

Quarterly Financial Information (Unaudited)

	2018				
	First	Second	Third	Fourth	Total
Net interest income	$ 12,922	$ 13,081	$ 13,988	$ 14,282	$ 54,273
Provision for (reversal of allowance for) loan losses	–	430	650	–	1,080
Noninterest income (expense), net	(4,642)	(5,348)	(4,803)	6,706	(8,087)
Net income	$ 8,280	$ 7,303	$ 8,535	$ 20,988	$ 45,106

	2017				
	First	Second	Third	Fourth	Total
Net interest income	$ 12,125	$ 12,826	$ 13,588	$ 13,097	$ 51,636
Provision for (reversal of allowance for) loan losses	410	450	425	–	1,285
Noninterest income (expense), net	(6,058)	(5,851)	(5,020)	25,811	8,882
Net income	$ 5,657	$ 6,525	$ 8,143	$ 38,908	$ 59,233

	2016				
	First	Second	Third	Fourth	Total
Net interest income	$ 10,868	$ 11,584	$ 12,440	$ 12,007	$ 46,899
Provision for (reversal of allowance for) loan losses	654	224	322	349	1,549
Noninterest income (expense), net	(5,462)	(5,400)	(4,708)	4,400	(11,170)
Net income	$ 4,752	$ 5,960	$ 7,410	$ 16,058	$ 34,180

Note 14 — Subsequent Events

The Association evaluated subsequent events and determined that there were none requiring disclosure through March 13, 2019, which was the date the financial statements were issued.