Cape Fear Farm Credit, ACA

FIRST QUARTER 2019

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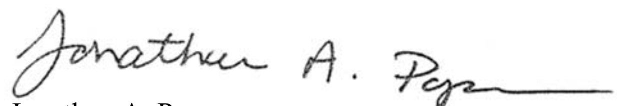
CERTIFICATION

The undersigned certify that we have reviewed the March 31, 2019 quarterly report of Cape Fear 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.



Jonathan A. Pope
Chairman of the Board

Brad Cornelius
Chief Executive Officer

Evan J. Kleinhans
Chief Financial Officer

May 9, 2019

Cape Fear Farm Credit, ACA

Report on Internal Control Over Financial Reporting

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

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

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of March 31, 2019. In making the assessment, management used the framework in *Internal Control — Integrated Framework (2013)*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association's management concluded that as of March 31, 2019, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association's management determined that there were no material weaknesses in the internal control over financial reporting as of March 31, 2019.

Brad Cornelius
Chief Executive Officer

Evan J. Kleinhans
Chief Financial Officer

May 9, 2019

Cape Fear Farm Credit, ACA

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

(dollars in thousands)

The following commentary reviews the financial condition and results of operations of Cape Fear Farm Credit ACA, (Association) for the period ended March 31, 2019. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2018 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio consists of agricultural commodities in our region, including swine, poultry, tobacco, and row crop operations. The Association's loan portfolio contains a concentration of swine and poultry loans. Demand for pork, chicken, turkey as well as prices of field grains affects the price of these commodities. Other factors including but not limited to international trade policies, political risks and nuisance lawsuits could impact these industries and the Association's corresponding loan portfolio. Continued low commodity prices, weakening demand for tobacco and cotton as well as adverse weather conditions are negatively impacting row crop farmers in our territory. Credit quality has improved slightly since the fourth quarter of 2018 and remains acceptable overall.

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. Risk exposure is reduced by many of the borrowers in the region having diversified farming operations as well as varying farm size. This factor, along with the opportunities for non-farm income in the area, lessens the level of dependency on any single given commodity. Concentration risk is further mitigated by a portfolio of participation loans purchased or originated and sold. The Association also mitigates concentration risk through the use of USDA and Farmer Mac guarantees.

The gross loan volume of the Association at March 31, 2019 was $921,998, a decrease of $6,306 or 0.68 percent as compared to $928,304 at December 31, 2018. When compared to the same period of 2018, gross loan volume increased by $18,612 or 2.06 percent from $903,386. Net loans outstanding at March 31, 2019 were $911,029, a decrease of $3,747 or 0.41 percent as compared to $914,776 at December 31, 2018. When compared to the same period of 2018, net loans outstanding increased by $15,646 or 1.75 percent from $895,383. Net loans accounted for 96.63 percent of total assets at March 31, 2019, as compared to 95.43 percent of total assets at December 31, 2018.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level and credit administration remains satisfactory. Nonaccrual loans decreased $259 to $18,561 at March 31, 2019 from $18,820 at December 31, 2018. The contraction in nonaccrual volume was primarily attributed to pay downs of nonaccrual balances during the first quarter. Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at March 31, 2019 was $10,969, which was less than the December 31, 2018 amount of $13,528 by $2,559 or 18.92 percent. The decrease in the overall allowance was primarily attributed to a decline in the specific reserve. Management considers the allowance for loan losses to be adequate to cover probable losses.

Other investments consist of Rural America Bonds which come under the Farm Credit Administration's (FCA) Mission Related Investments. The objective of Rural America Bonds is to help meet the growing and diverse financing needs of agricultural enterprises, agribusinesses, and rural communities by providing a flexible flow of money to rural areas through bond financing. At March 31, 2019, the Association had $3,544 in Rural America Bonds which were all classified as investment securities. At December 31, 2018, the Association had $3,738 in Rural America Bonds which were all classified as investment securities.

Effective December 31, 2014, the FCA concluded each pilot program approved as part of the Investment in Rural America program. Each institution participating in such programs may continue to hold its investment through the maturity dates for the investments, provided the institution continues to meet all approval conditions. Although the pilot programs have concluded, the FCA can consider future requests on a case-by-case basis.

Other property owned (OPO) at March 31, 2019 was $366, which was unchanged from December 31, 2018. The

Association is actively marketing all properties classified as other property owned for resale.

RESULTS OF OPERATIONS

For the three months ended March 31, 2019

Net income for the three months ended March 31, 2019 totaled $7,960 as compared to $5,247 for the same period in 2018, an increase of $2,713 or 51.71 percent.

For the three months ended March 31, 2019, net interest income decreased $136 or 2.04 percent compared to the same period in 2018. Interest income on loans increased by $638 while interest income from investment securities decreased by $3. Interest expense increased $771 compared to the same period last year. Provision for loan losses decreased by $2,611 in comparison with the same period in 2018. There was a reversal of allowance for loan losses of $2,464 for the three months ended March 31, 2019 as compared to a provision for loan losses of $147 for the same period in 2018. The decrease in provision for loan losses was primarily attributed to a decline in the specific reserve largely driven by the contraction in nonaccrual volume. Nonaccrual income was $38 for the three months ended March 31, 2019, as compared to $23 for the same period in 2018 which is an increase of $15.

Noninterest income for the three months ended March 31, 2019 totaled $3,020 as compared to $2,654 for the same period of 2018, an increase of $366. Positive variances for the period include a $340 increase in patronage refunds from other Farm Credit Institutions, a $265 increase in gains on sales of premises and equipment, a $52 increase in loan fee income, and a $2 increase in gains on sales of rural home loans. The overall increase was offset by a $282 decrease in insurance fund refunds, a $10 decrease in fees for financially related services, and a $1 decrease in other gains.

Noninterest expense for the three months ended March 31, 2019 totaled $4,035 as compared to $3,911 for the same period of 2018, an increase of $124. Items contributing to the increase in non-interest expense include a $48 increase in salaries and employee benefits, a $44 decrease in gains on OPO, a $22 increase in occupancy and equipment, a $7 increase in other operating expenses, and a $3 increase in insurance fund premiums.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at March 31, 2019 was $718,505 as compared to $742,744 at December 31, 2018.

See Note 5 in the Notes to the Consolidated Financial Statements for information on the status of compliance with covenants under the General Financing Agreement.

CAPITAL RESOURCES

Total members' equity at March 31, 2019 increased to $211,486 from the December 31, 2018 total of $203,519. The increase is primarily due to recognition of net income retained through the first quarter.

FCA regulations require all Farm Credit institutions to maintain minimum common equity tier 1 (CET1), tier 1 capital, total capital, and permanent capital risk-based capital ratios, along with tier 1 leverage and unallocated retained earnings equivalents leverage ratios. As of March 31, 2019, all ratios were well above the regulatory minimums.

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 March 31, 2019
Risk-adjusted ratios:				
CET1 Capital	4.5%	1.88%	6.38%	20.79%
Tier 1 Capital	6.0%	1.88%	7.88%	20.79%
Total Capital	8.0%	1.88%	9.88%	22.04%
Permanent Capital Ratio	7.0%	0.0%	7.0%	21.06%
Non-risk-adjusted:				
Tier 1 Leverage Ratio	4.0%	1.0%	5.0%	21.35%
UREE Leverage Ratio	1.5%	0.0%	1.5%	21.63%

** 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.

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.

REGULATORY MATTERS

On April 3, 2019, the Farm Credit Administration issued a proposed rule that would clarify the factors that System institutions should consider when categorizing high-risk loans and placing them in nonaccrual status. The rule would also revise the criteria by which loans are reinstated to accrual status, and would revise the application of the criteria to certain loans in nonaccrual status to distinguish between the types of risk that cause loans to be placed in nonaccrual status. The public comment period ends on June 3, 2019.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Please refer to Note 1, *Organization, Significant Accounting Policies, and Recently Issued Accounting Pronouncements*, in the Notes to the Financial Statements, and the 2018 Annual Report to Shareholders for recently issued accounting pronouncements. Additional information is provided in the following table.

The following Accounting Standards Update (ASU) was issued by the Financial Accounting Standards Board (FASB) but has 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.	• Implementation efforts have begun by establishing a cross-discipline governance structure. The implementation includes identification of key interpretive issues, scoping of financial instruments, and assessing existing credit loss forecasting models and processes against the new guidance. • The new guidance is expected to result in an increase in 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 financial instrument portfolios, and the macroeconomic conditions and forecasts at the adoption date. • The guidance is expected to be adopted in first quarter 2021.

NOTE: Shareholder investment in the Association is materially affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 2764, or writing Matthew Miller, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, *www.agfirst.com*. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-368-5819 ext. 3243, writing Evan J. Kleinhans, Cape Fear Farm Credit, P. O. Box 2405, Fayetteville, NC 28302, or accessing the website, *www.capefearfarmcredit.com*. The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Cape Fear Farm Credit, ACA

Consolidated Balance Sheets

(dollars in thousands)	March 31, 2019	December 31, 2018
	(unaudited)	*(audited)*
Assets		
Cash	**$ 1,413**	$ 2,543
Investments in debt securities:		
Held to maturity (fair value of $3,503 and $3,627, respectively)	**3,544**	3,738
Loans	**921,998**	928,304
Allowance for loan losses	**(10,969)**	(13,528)
Net loans	**911,029**	914,776
Loans held for sale	**30**	91
Accrued interest receivable	**9,416**	9,588
Equity investments in other Farm Credit institutions	**10,705**	10,673
Premises and equipment, net	**2,851**	3,277
Other property owned	**366**	366
Accounts receivable	**3,114**	13,261
Other assets	**349**	230
Total assets	**$ 942,817**	$ 958,543
Liabilities		
Notes payable to AgFirst Farm Credit Bank	**$ 718,505**	$ 742,744
Lease obligations	**444**	—
Accrued interest payable	**1,945**	1,972
Patronage refunds payable	**402**	5,385
Accounts payable	**1,481**	1,323
Other liabilities	**8,554**	3,600
Total liabilities	**731,331**	755,024
Commitments and contingencies (Note 8)		
Members' Equity		
Protected borrower stock	**3**	3
Capital stock and participation certificates	**2,469**	2,464
Retained earnings		
Allocated	**103,446**	103,116
Unallocated	**105,833**	98,205
Accumulated other comprehensive income (loss)	**(265)**	(269)
Total members' equity	**211,486**	203,519
Total liabilities and members' equity	**$ 942,817**	$ 958,543

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

Cape Fear Farm Credit, ACA

Consolidated Statements of Income

(unaudited)

(dollars in thousands)	For the three months ended March 31, 2019	2018
Interest Income		
Loans	**$ 12,252**	$ 11,614
Investments	**45**	48
Total interest income	**12,297**	11,662
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	**5,751**	4,980
Net interest income	**6,546**	6,682
Provision for (reversal of allowance for) loan losses	**(2,464)**	147
Net interest income after provision for (reversal of allowance for) loan losses	**9,010**	6,535
Noninterest Income		
Loan fees	**643**	591
Fees for financially related services	**1**	11
Patronage refunds from other Farm Credit institutions	**1,915**	1,575
Gains (losses) on sales of rural home loans, net	**5**	3
Gains (losses) on sales of premises and equipment, net	**261**	(4)
Gains (losses) on other transactions	**1**	2
Insurance Fund refunds	**194**	476
Total noninterest income	**3,020**	2,654
Noninterest Expense		
Salaries and employee benefits	**2,687**	2,639
Occupancy and equipment	**230**	208
Insurance Fund premiums	**156**	153
(Gains) losses on other property owned, net	**(4)**	(48)
Other operating expenses	**966**	959
Total noninterest expense	**4,035**	3,911
Income before income taxes	**7,995**	5,278
Provision for income taxes	**35**	31
Net income	**$ 7,960**	$ 5,247

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

Cape Fear Farm Credit, ACA

Consolidated Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the three months ended March 31, 2019	2018
Net income	**$ 7,960**	$ 5,247
Other comprehensive income net of tax		
Employee benefit plans adjustments	**4**	5
Comprehensive income	**$ 7,964**	$ 5,252

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

Cape Fear Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)	Protected Borrower Stock	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2017	$ 3	$ 2,507	$ 100,298	$ 96,833	$ (307)	$ 199,334
Comprehensive income				5,247	5	5,252
Capital stock/participation certificates issued/(retired), net		4				4
Patronage distribution adjustment			422	(423)		(1)
Balance at March 31, 2018	$ 3	$ 2,511	$ 100,720	$ 101,657	$ (302)	$ 204,589
Balance at December 31, 2018	**$ 3**	**$ 2,464**	**$ 103,116**	**$ 98,205**	**$ (269)**	**$ 203,519**
Cumulative effect of change in accounting principle				**1**		**1**
Comprehensive income				**7,960**	**4**	**7,964**
Capital stock/participation certificates issued/(retired), net		**5**				**5**
Patronage distribution adjustment			**330**	**(333)**		**(3)**
Balance at March 31, 2019	**$ 3**	**$ 2,469**	**$ 103,446**	**$ 105,833**	**$ (265)**	**$ 211,486**

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

Cape Fear Farm Credit, ACA

Notes to the Consolidated Financial Statements

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

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

Organization

The accompanying financial statements include the accounts of Cape Fear Farm Credit, ACA and its Production Credit Association (PCA) and Federal Land Credit Association (FLCA) subsidiaries (collectively, the Association). A description of the organization and operations, the significant accounting policies followed, and the financial condition and results of operations for the Association as of and for the year ended December 31, 2018, are contained in the 2018 Annual Report to Shareholders. These unaudited interim consolidated financial statements should be read in conjunction with the latest Annual Report to Shareholders.

Basis of Presentation

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

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

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

Significant Accounting Policies

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

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

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

Accounting Standards Updates (ASUs) Issued During the Period

The following ASU was issued by the Financial Accounting Standards Board (FASB) since the most recent year end:

- In March 2019, the FASB issued ASU 2019-01 Leases (Topic 842): Codification Improvements. The Update addresses potential implementation issues that could arise as organizations implement Topic 842. The amendments in the Update include the following items brought to the Board's attention through interactions with stakeholders: 1. Determining the fair value of the underlying asset by lessors that are not manufacturers or dealers; 2. Presentation on the statement of cash flows—sales-type and direct financing leases; 3. Transition disclosures related to Topic 250, Accounting Changes and Error Corrections. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

ASUs Pending Effective Date

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

Potential effects of ASUs issued in previous periods:

- 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. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

- 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. Early adoption is permitted upon issuance. Entities are permitted to early adopt any removed or modified disclosures upon issuance of this Update and delay adoption of the additional disclosures until their effective date. The removed disclosures were adopted effective with the 2018 Annual Report. Evaluation of any possible effects the additional and modified disclosures guidance may have on the statements of financial condition and results of operations is in progress.

- 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 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 31, 2018. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

Accounting Standards Effective During the Period

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

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

- 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 was effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Adoption of this guidance had no impact 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 was effective for interim and annual periods beginning after December 15, 2018 for public business entities. Adoption of this guidance had no impact 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. 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. The amendments were effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, for public business entities.

Transition Information

- The guidance was adopted using the optional modified retrospective method and practical expedients for transition. Under this 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.
- The package of practical expedients was elected, which allowed existing leases to be largely accounted for consistent with current guidance, except for the incremental balance sheet recognition for lessees.
- There will not be a material change to the timing of future expense recognition.
- Upon adoption, a cumulative-effect adjustment to equity of approximately $1 was recorded. In addition, a Right of Use Asset in the amount of $120 and Lease Liability in the amount of $119 were recognized.
- Given the limited changes to lessor accounting, there were no material changes to recognition or measurement.

Note 2 — Loans and Allowance for Loan Losses

The Association maintains an allowance for loan losses at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio as of the report date. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan charge-offs and allowance reversals. A review of individual loans in each respective portfolio is performed periodically to determine the appropriateness of risk ratings and to ensure loss exposure to the Association has been identified. See Note 3, *Loans and Allowance for Loan Losses*, from the latest Annual Report for further discussion.

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

A summary of loans outstanding at period end follows:

	March 31, 2019	December 31, 2018
Real estate mortgage	$ 631,801	$ 609,465
Production and intermediate-term	233,223	265,477
Loans to cooperatives	10,282	5,976
Processing and marketing	23,415	22,697
Farm-related business	9,812	10,553
Communication	1,279	1,296
Power and water/waste disposal	1,935	1,934
Rural residential real estate	4,549	4,658
International	3,261	3,260
Lease receivables	2,441	2,988
Total loans	$ 921,998	$ 928,304

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

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

	March 31, 2019							
	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	$ 11,329	$ 62,484	$ –	$ –	$ 13,968	$ 2,262	$ 25,297	$ 64,746
Production and intermediate-term	15,397	187,671	–	–	1,518	–	16,915	187,671
Loans to cooperatives	7,627	–	2,666	–	–	–	10,293	–
Processing and marketing	13,857	26,912	–	–	–	–	13,857	26,912
Farm-related business	–	3,290	–	14,258	–	–	–	17,548
Communication	1,282	–	–	–	–	–	1,282	–
Power and water/waste disposal	1,939	–	–	–	–	–	1,939	–
International	3,263	–	–	–	–	–	3,263	–
Lease receivables	–	–	2,442	–	–	–	2,442	–
Total	$ 54,694	$ 280,357	$ 5,108	$ 14,258	$ 15,486	$ 2,262	$ 75,288	$ 296,877

	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	$ 10,946	$ 65,285	$ –	$ –	$ 1,802	$ 2,619	$ 12,748	$ 67,904
Production and intermediate-term	12,553	261,938	–	–	1,812	–	14,365	261,938
Loans to cooperatives	3,293	–	2,693	–	–	–	5,986	–
Processing and marketing	12,008	39,824	–	–	–	–	12,008	39,824
Farm-related business	–	3,358	–	14,551	–	–	–	17,909
Communication	1,299	–	–	–	–	–	1,299	–
Power and water/waste disposal	1,939	–	–	–	–	–	1,939	–
International	3,263	–	–	–	–	–	3,263	–
Lease receivables	–	–	2,990	–	–	–	2,990	–
Total	$ 45,301	$ 370,405	$ 5,683	$ 14,551	$ 3,614	$ 2,619	$ 54,598	$ 387,575

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:

	March 31, 2019			
	Due Less Than 1 Year	Due 1 Through 5 Years	Due After 5 Years	Total
Real estate mortgage	$ 10,755	$ 95,719	$ 525,327	$ 631,801
Production and intermediate-term	84,522	85,145	63,556	233,223
Loans to cooperatives	284	6,868	3,130	10,282
Processing and marketing	5,105	9,353	8,957	23,415
Farm-related business	2,831	3,986	2,995	9,812
Communication	–	1,279	–	1,279
Power and water/waste disposal	–	–	1,935	1,935
Rural residential real estate	48	750	3,751	4,549
International	–	3,011	250	3,261
Lease receivables	–	552	1,889	2,441
Total loans	$ 103,545	$ 206,663	$ 611,790	$ 921,998
Percentage	11.23%	22.41%	66.36%	100.00%

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

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

	March 31, 2019	December 31, 2018
Real estate mortgage:		
Acceptable	96.05%	94.93%
OAEM	2.56	3.73
Substandard/doubtful/loss	1.39	1.34
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	89.53%	91.28%
OAEM	6.05	4.75
Substandard/doubtful/loss	4.42	3.97
	100.00%	100.00%
Loans to cooperatives:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Processing and marketing:		
Acceptable	88.41%	87.43%
OAEM	2.42	–
Substandard/doubtful/loss	9.17	12.57
	100.00%	100.00%
Farm-related business:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%

	March 31, 2019	December 31, 2018
Communication:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	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	90.75%	90.75%
OAEM	4.28	4.34
Substandard/doubtful/loss	4.97	4.91
	100.00%	100.00%
International:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Lease receivables:		
Acceptable	88.34%	89.33%
OAEM	0.42	0.33
Substandard/doubtful/loss	11.24	10.34
	100.00%	100.00%
Total loans:		
Acceptable	94.27%	93.78%
OAEM	3.37	3.83
Substandard/doubtful/loss	2.36	2.39
	100.00%	100.00%

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

	March 31, 2019				
	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	$ 1,946	$ 2,623	$ 4,569	$ 633,687	$ 638,256
Production and intermediate-term	6,614	3,330	9,944	225,923	235,867
Loans to cooperatives	–	–	–	10,302	10,302
Processing and marketing	–	1,787	1,787	21,793	23,580
Farm-related business	167	–	167	9,724	9,891
Communication	–	–	–	1,280	1,280
Power and water/waste disposal	–	–	–	1,936	1,936
Rural residential real estate	147	79	226	4,343	4,569
International	–	–	–	3,275	3,275
Lease receivables	291	98	389	2,061	2,450
Total	$ 9,165	$ 7,917	$ 17,082	$ 914,324	$ 931,406

	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	$ 1,708	$ 1,862	$ 3,570	$ 611,490	$ 615,060
Production and intermediate-term	3,805	5,546	9,351	259,882	269,233
Loans to cooperatives	–	–	–	5,980	5,980
Processing and marketing	–	1,936	1,936	20,893	22,829
Farm-related business	–	–	–	10,598	10,598
Communication	–	–	–	1,296	1,296
Power and water/waste disposal	–	–	–	1,936	1,936
Rural residential real estate	55	73	128	4,545	4,673
International	–	–	–	3,274	3,274
Lease receivables	213	188	401	2,597	2,998
Total	$ 5,781	$ 9,605	$ 15,386	$ 922,491	$ 937,877

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

	March 31, 2019	December 31, 2018
Nonaccrual loans:		
Real estate mortgage	$ 6,805	$ 6,044
Production and intermediate-term	9,527	10,421
Processing and marketing	1,787	1,936
Rural residential real estate	166	109
Lease receivables	276	310
Total	$ 18,561	$ 18,820
Accruing restructured loans:		
Real estate mortgage	$ 538	$ 575
Production and intermediate-term	1,095	941
Processing and marketing	570	560
Total	$ 2,203	$ 2,076
Accruing loans 90 days or more past due:		
Lease receivables	$ 98	$ 188
Total	$ 98	$ 188
Total nonperforming loans	$ 20,862	$ 21,084
Other property owned	366	366
Total nonperforming assets	$ 21,228	$ 21,450
Nonaccrual loans as a percentage of total loans	2.01%	2.03%
Nonperforming assets as a percentage of total loans and other property owned	2.30%	2.31%
Nonperforming assets as a percentage of capital	10.04%	10.54%

The following table presents information related to the recorded investment of impaired loans at period end. Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms of the loan.

	March 31, 2019	December 31, 2018
Impaired nonaccrual loans:		
Current as to principal and interest	$ 8,513	$ 7,283
Past due	10,048	11,537
Total	$ 18,561	$ 18,820
Impaired accrual loans:		
Restructured	$ 2,203	$ 2,076
90 days or more past due	98	188
Total	$ 2,301	$ 2,264
Total impaired loans	$ 20,862	$ 21,084
Additional commitments to lend	$ 1	$ 276

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

	March 31, 2019			Three Months Ended March 31, 2019	
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	$ 3,767	$ 3,931	$ 940	$ 3,844	$ 13
Production and intermediate-term	5,442	5,754	1,501	5,554	19
Processing and marketing	–	–	–	–	–
Rural residential real estate	–	–	–	–	–
Lease receivables	155	156	78	159	1
Total	$ 9,364	$ 9,841	$ 2,519	$ 9,557	$ 33
With no related allowance for credit losses:					
Real estate mortgage	$ 3,576	$ 4,616	$ –	$ 3,650	$ 13
Production and intermediate-term	5,180	6,079	–	5,286	19
Processing and marketing	2,357	2,747	–	2,405	8
Rural residential real estate	166	242	–	170	1
Lease receivables	219	220	–	223	-
Total	$ 11,498	$ 13,904	$ –	$ 11,734	$ 41
Total impaired loans:					
Real estate mortgage	$ 7,343	$ 8,547	$ 940	$ 7,494	$ 26
Production and intermediate-term	10,622	11,833	1,501	10,840	38
Processing and marketing	2,357	2,747	–	2,405	8
Rural residential real estate	166	242	–	170	1
Lease receivables	374	376	78	382	1
Total	$ 20,862	$ 23,745	$ 2,519	$ 21,291	$ 74

	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	$ 3,828	$ 3,924	$ 1,102	$ 2,712	$ 106
Production and intermediate-term	8,316	8,484	3,798	5,892	232
Processing and marketing	–	–	–	–	–
Rural residential real estate	–	–	–	–	–
Lease receivables	185	186	108	131	5
Total	$ 12,329	$ 12,594	$ 5,008	$ 8,735	$ 343
With no related allowance for credit losses:					
Real estate mortgage	$ 2,791	$ 3,841	$ –	$ 1,978	$ 78
Production and intermediate-term	3,046	3,879	–	2,158	84
Processing and marketing	2,496	2,886	–	1,769	69
Rural residential real estate	109	181	–	77	3
Lease receivables	313	313	–	221	9
Total	$ 8,755	$ 11,100	$ –	$ 6,203	$ 243
Total impaired loans:					
Real estate mortgage	$ 6,619	$ 7,765	$ 1,102	$ 4,690	$ 184
Production and intermediate-term	11,362	12,363	3,798	8,050	316
Processing and marketing	2,496	2,886	–	1,769	69
Rural residential real estate	109	181	–	77	3
Lease receivables	498	499	108	352	14
Total	$ 21,084	$ 23,694	$ 5,008	$ 14,938	$ 586

A summary of changes in the allowance for loan losses and recorded investment in loans for each reporting period follows:

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Communication	Power and Water/Waste Disposal	Rural Residential Real Estate	International	Lease Receivables	Total
Activity related to the allowance for credit losses:									
Balance at December 31, 2018	$ 6,332	$ 6,660	$ 284	$ 32	$ 3	$ 47	$ 31	$ 139	$ 13,528
Charge-offs	(17)	(90)	–	–	(1)	(1)	–	–	(109)
Recoveries	–	14	–	–	–	–	–	–	14
Provision for loan losses	(187)	(2,246)	(2)	–	1	–	–	(30)	(2,464)
Balance at March 31, 2019	$ 6,128	$ 4,338	$ 282	$ 32	$ 3	$ 46	$ 31	$ 109	$ 10,969
Balance at December 31, 2017	$ 4,534	$ 3,026	$ 233	$ 26	$ 2	$ 38	$ 26	$ 26	$ 7,911
Charge-offs	(74)	(68)	–	–	–	–	–	–	(142)
Recoveries	72	15	–	–	–	–	–	–	87
Provision for loan losses	(201)	221	(7)	(1)	–	(1)	(1)	137	147
Balance at March 31, 2018	$ 4,331	$ 3,194	$ 226	$ 25	$ 2	$ 37	$ 25	$ 163	$ 8,003
Allowance on loans evaluated for impairment:									
Individually	$ 940	$ 1,501	$ –	$ –	$ –	$ –	$ –	$ 78	$ 2,519
Collectively	5,188	2,837	282	32	3	46	31	31	8,450
Balance at March 31, 2019	$ 6,128	$ 4,338	$ 282	$ 32	$ 3	$ 46	$ 31	$ 109	$ 10,969
Individually	$ 1,102	$ 3,798	$ –	$ –	$ –	$ –	$ –	$ 108	$ 5,008
Collectively	5,230	2,862	284	32	3	47	31	31	8,520
Balance at December 31, 2018	$ 6,332	$ 6,660	$ 284	$ 32	$ 3	$ 47	$ 31	$ 139	$ 13,528
Recorded investment in loans evaluated for impairment:									
Individually	$ 7,381	$ 10,685	$ 2,368	$ –	$ –	$ 168	$ –	$ 277	$ 20,879
Collectively	630,875	225,182	41,405	1,280	1,936	4,401	3,275	2,173	910,527
Balance at March 31, 2019	$ 638,256	$ 235,867	$ 43,773	$ 1,280	$ 1,936	$ 4,569	$ 3,275	$ 2,450	$ 931,406
Individually	$ 6,661	$ 11,782	$ –	$ –	$ –	$ 109	$ –	$ 499	$ 19,051
Collectively	608,399	257,451	39,407	1,296	1,936	4,564	3,274	2,499	918,826
Balance at December 31, 2018	$ 615,060	$ 269,233	$ 39,407	$ 1,296	$ 1,936	$ 4,673	$ 3,274	$ 2,998	$ 937,877

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

A restructuring of a debt constitutes a troubled debt restructuring (TDR) if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. The following tables present additional information about pre-modification and post-modification outstanding recorded investment and the effects of the modifications that occurred during the periods presented.

	Three Months Ended March 31, 2019				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ –	$ 11	$ –	$ 11	
Production and intermediate-term	–	–	137	137	
Total	$ –	$ 11	$ 137	$ 148	
Post-modification:					
Real estate mortgage	$ –	$ 11	$ –	$ 11	$ –
Production and intermediate-term	–	–	137	137	–
Total	$ –	$ 11	$ 137	$ 148	$ –

	Three Months Ended March 31, 2018				
Outstanding Recorded Investment	**Interest Concessions**	**Principal Concessions**	**Other Concessions**	**Total**	**Charge-offs**
Pre-modification:					
Real estate mortgage	$ –	$ 315	$ –	$ 315	
Production and intermediate-term	–	522	–	522	
Total	$ –	$ 837	$ –	$ 837	
Post-modification:					
Real estate mortgage	$ –	$ 314	$ –	$ 314	$ –
Production and intermediate-term	–	505	–	505	–
Total	$ –	$ 819	$ –	$ 819	$ –

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 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	
	March 31, 2019	December 31, 2018	March 31, 2019	December 31, 2018
Real estate mortgage	$ 1,746	$ 1,804	$ 1,208	$ 1,229
Production and intermediate-term	1,944	1,903	849	962
Processing and marketing	1,144	1,283	574	723
Rural residential real estate	32	35	32	35
Total loans	$ 4,866	$ 5,025	$ 2,663	$ 2,949
Additional commitments to lend	$ –	$ –		

The following table presents information as of period end:

	March 31, 2019
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 3 — Investments

Investments in Debt Securities

The Association's investments consist primarily of Rural America Bonds (RABs), which are private placement securities purchased under the Mission Related Investment (MRI) program approved by the FCA. In its Conditions of Approval for the program, the FCA generally considers a RAB ineligible if its investment rating, based on the internal 14-point risk rating scale used to also grade loans, falls below 9 and requires System institutions to provide notification to FCA when a security becomes ineligible. Any other bonds purchased under the MRI program, approved on a case-by-case basis by FCA, may have different eligibility requirements. At March 31, 2019, the Association held no RABs whose credit quality had deteriorated beyond the program limits.

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

	March 31, 2019				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 3,544	$ –	$ (41)	$ 3,503	5.22%

	December 31, 2018				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Yield
RABs	$ 3,738	$ –	$ (111)	$ 3,627	5.09%

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

	March 31, 2019		
	Amortized Cost	Fair Value	Weighted Average Yield
In one year or less	$ –	$ –	–%
After one year through five years	752	727	2.49
After five years through ten years	–	–	–
After ten years	2,792	2,776	5.95
Total	$ 3,544	$ 3,503	5.22%

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

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

	March 31, 2019			
	Less Than 12 Months		12 Months Or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ –	$ –	$ 3,503	$ (41)

	December 31, 2018			
	Less Than 12 Months		12 Months Or Greater	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
RABs	$ –	$ –	$ 3,627	$ (111)

The recording of an impairment is predicated on: (1) whether or not management intends to sell the security, (2) whether it is more likely than not that management would be required to sell the security before recovering its costs, and (3) whether management expects to recover the security's entire amortized cost basis (even if there is no intention to sell). If the Association intends to sell the security or it is more likely than not that it would be required to sell the security, the impairment loss equals the full difference between amortized cost and fair value of the security. When the Association does not intend to sell securities in an unrealized loss position and it is not more likely than not that it would be required to sell the securities, other-than-temporary impairment loss is separated into credit loss and non-credit loss. Credit loss is defined as the shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis.

The Association performs periodic credit reviews, including other-than-temporary impairment analyses, on its investment securities portfolio. The objective is to quantify future possible loss of principal or interest due on securities in the portfolio. Factors considered in determining whether an impairment is other-than-temporary include among others: (1) the length of time and the extent to which the fair value is less than cost, (2) adverse conditions specifically related to the industry, (3) geographic area and the condition of the underlying collateral, (4) payment structure of the security, (5) ratings by rating agencies, (6) the credit worthiness of bond insurers, and (7) volatility of the fair value changes.

The Association uses the present value of cash flows expected to be collected from each debt security to determine the amount of credit loss. This technique requires assumptions related to the underlying collateral, including default rates, amount and timing of prepayments, and loss severity. Assumptions can vary widely from security to security and are influenced by such factors as loan interest rate, geographical location of the borrower, borrower characteristics, and collateral type.

Significant inputs used to estimate the amount of credit loss include, but are not limited to, performance indicators of the underlying assets in the security (including default rates, delinquency rates, and percentage of nonperforming assets), loan-to-collateral value ratios, third-party guarantees, current levels of subordination, vintage, geographic concentration, and credit ratings. The Association may obtain assumptions for the default rate, prepayment rate, and loss severity rate from an independent third party, or generate the assumptions internally.

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

Equity Investments in Other Farm Credit System Institutions

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

Associations are required to maintain ownership in AgFirst (AgFirst or the Bank) in the form of Class B or Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association owned 3.73 percent of the issued stock of the Bank as of March 31, 2019 net of any reciprocal investment. As of that date, the Bank's assets totaled $32.7 billion and shareholders' equity totaled $2.3 billion. The Bank's earnings were $67 million for the first three months of 2019. In addition, the Association held $577 in investments related to other Farm Credit institutions.

Note 4 — Debt

Notes Payable to AgFirst Farm Credit Bank

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

Note 5 — Members' Equity

Accumulated Other Comprehensive Income (AOCI)

	Changes in Accumulated Other Comprehensive Income by Component *(a)*	
	Three Months Ended March 31,	
	2019	2018
Employee Benefit Plans:		
Balance at beginning of period	$ (269)	$ (307)
Other comprehensive income before reclassifications	–	–
Amounts reclassified from AOCI	4	5
Net current period other comprehensive income	4	5
Balance at end of period	$ (265)	$ (302)

	Reclassifications Out of Accumulated Other Comprehensive Income *(b)*		
	Three Months Ended March 31,		
	2019	2018	Income Statement Line Item
Defined Benefit Pension Plans:			
Periodic pension costs	$ (4)	$ (5)	See Note 7.
Net amounts reclassified	$ (4)	$ (5)	

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

Note 6 — Fair Value Measurement

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

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

The classifications within the fair value hierarchy are as follows:

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

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

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

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

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

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

	March 31, 2019				
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Recurring Measurements					
Assets:					
Assets held in trust funds	$ 64	$ 64	$ –	$ –	$ 64
Recurring Assets	$ 64	$ 64	$ –	$ –	$ 64
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 6,845	$ –	$ –	$ 6,845	$ 6,845
Other property owned	366	–	–	399	399
Nonrecurring Assets	$ 7,211	$ –	$ –	$ 7,244	$ 7,244
Other Financial Instruments					
Assets:					
Cash	$ 1,413	$ 1,413	$ –	$ –	$ 1,413
Investments in debt securities, held-to-maturity	3,544	–	–	3,503	3,503
Loans	904,214	–	–	894,650	894,650
Other Financial Assets	$ 909,171	$ 1,413	$ –	$ 898,153	$ 899,566
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 718,505	$ –	$ –	$ 713,406	$ 713,406
Other Financial Liabilities	$ 718,505	$ –	$ –	$ 713,406	$ 713,406

	December 31, 2018				
	Total Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
Recurring Measurements					
Assets:					
Assets held in trust funds	$ 70	$ 70	$ –	$ –	$ 70
Recurring Assets	$ 70	$ 70	$ –	$ –	$ 70
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 7,321	$ –	$ –	$ 7,321	$ 7,321
Other property owned	366	–	–	429	429
Nonrecurring Assets	$ 7,687	$ –	$ –	$ 7,750	$ 7,750
Other Financial Instruments					
Assets:					
Cash	$ 2,543	$ 2,543	$ –	$ –	$ 2,543
Investments in debt securities, held-to-maturity	3,738	–	–	3,627	3,627
Loans	907,546	–	–	890,256	890,256
Other Financial Assets	$ 913,827	$ 2,543	$ –	$ 893,883	$ 896,426
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 742,744	$ –	$ –	$ 730,917	$ 730,917
Other Financial Liabilities	$ 742,744	$ –	$ –	$ 730,917	$ 730,917

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.

Investments in Debt Securities

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

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

Inputs to Valuation Techniques

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

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

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Fair Value	Valuation Technique(s)	Unobservable Input	Range
Impaired loans and other property owned	$ 7,244	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement cost	*
			Comparability adjustments	*

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

Information about Other Financial Instrument Fair Value Measurements

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

Note 7 — Employee Benefit Plans

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

	Three Months Ended March 31,	
	2019	2018
Pension	$ 298	$ 440
401(k)	137	130
Other postretirement benefits	75	71
Total	$ 510	$ 641

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

	Actual YTD Through 3/31/19	Projected Contributions For Remainder of 2019	Projected Total Contributions 2019
Pension	$ 7	$ 1,181	$ 1,188
Other postretirement benefits	75	217	292
Total	$ 82	$ 1,398	$ 1,480

Contributions in the above table include allocated estimates of funding for multi-employer plans in which the Association participates. These amounts may change when a total funding amount and allocation is determined by the respective Plan's Sponsor Committee. Also, market conditions could impact discount rates and return on plan assets which could change contributions necessary before the next plan measurement date of December 31, 2019.

Further details regarding employee benefit plans are contained in the 2018 Annual Report to Shareholders.

Note 8 — Commitments and Contingent Liabilities

From time to time, legal actions are pending against the Association in which claims for money damages are asserted. On at least a quarterly basis, the Association assesses its liabilities and contingencies in connection with outstanding legal proceedings utilizing the latest information available. While the outcome of legal proceedings is inherently uncertain, on the basis of information presently available, management, after consultation with legal counsel, is of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the Association. Because it is 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.

Note 9 — Subsequent Events

The Association evaluated subsequent events and determined there were none requiring disclosure through May 9, 2019, which was the date the financial statements were issued.