

# QUARTERLY REPORT

June 30, 2010

AgriBank, FCB & Affiliated Associations



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## MANAGEMENT'S DISCUSSION AND ANALYSIS

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The following discussion is a review of the combined financial position and results of operations of AgriBank, FCB and Affiliated Associations. This information should be read in conjunction with the accompanying financial statements, the notes to the financial statements and the 2009 annual report.

We serve customers in states across America's heartland. AgriBank provides funding to and is owned by its affiliated Associations and other financial institutions. AgriBank and its affiliated Associations are collectively referred to as the District. The Associations are chartered to serve customers in substantially all of Arkansas, Illinois, Indiana, Iowa, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, Tennessee, Wisconsin and Wyoming. The Associations provide credit and services to farmers, ranchers, rural residents and agribusinesses.

### RESULTS OF OPERATIONS

District net income for the six months ended June 30, 2010 totaled \$691.0 million compared to \$382.6 million for the same period in 2009. The return on average assets increased to 1.86% for the six months ended June 30, 2010 from 1.09% for the comparable period in 2009. The significant increase in net income and the return on average assets reflects the increase in net interest income and non-interest income recorded during the first six months of 2010.

The following table illustrates changes in the significant components of net income:

Six months ended June 30		
Increase (decrease) in net income	(in millions)	2010 vs. 2009
Net interest income		\$134.7
Provision for credit losses		40.7
Non-interest income		109.0
Operating expenses		22.4
Asset impairment		24.8
Income taxes		(23.2)
Total change in net income		<u>\$308.4</u>

Net interest income for the six months ended June 30, 2010 increased \$134.7 million or 15.5% compared to the six months ended June 30, 2009. The increase in net interest income was due to the positive effects of changes in volume of \$43.6 million, positive effects of changes in rates of \$91.2 million and a \$0.1 million decrease in nonaccrual income. Average earning assets increased to \$72.1 billion for the six months ended June 30, 2010 compared to \$68.3 billion for the same period in 2009. Loans totaled \$60.4 billion at June 30, 2010, which is \$0.1 billion more than the December 31, 2009 balance. Moderate loan growth during the first half of 2010, reflects significant pay downs during the first quarter as retail customers sold crop inventories, a softening in loan demand due to relatively lower commodity prices, continued adherence to strong credit underwriting standards and the continued impact of the recession on the U.S. and global economies. The associations continue to focus on their core traditional clients and are not pursuing certain aspects of capital markets to the extent they did prior to 2009. The positive impact of changes in rates was due to declining interest rates resulting in our debt repricing faster than assets and other funding actions as well as widening spreads on new and repricing volume.

Information regarding the year-to-date average daily balances (ADB) and annualized average rates earned and paid on our portfolio follows:

Six months ended				
June 30	2010		2009	
(in millions)	ADB	Rate	ADB	Rate
Earning assets:				
Accrual loans	\$58,600.6	5.10%	\$56,210.1	5.25%
Nonaccrual loans	1,169.5	2.30%	809.1	3.36%
Investments and federal funds	12,116.3	1.29%	10,997.3	1.89%
Other earning assets	262.0	5.35%	301.1	5.46%
Total earning assets	72,148.4	4.42%	68,317.6	4.69%
Total interest bearing liabilities	61,798.9	1.91%	59,407.5	2.46%
Total interest rate spread		2.51%		2.23%
Impact of equity financing	\$10,349.5	0.27%	\$8,910.1	0.31%
Net interest margin		2.78%		2.54%

Net interest margin has increased by 24 basis points over the same period last year due to a 28 basis point increase in interest rate spread offset by a 4 basis point decline in the impact of equity financing. Equity financing represents the benefit of non-interest bearing funding, which was negatively impacted by falling interest rates.

The District's average interest rate spread on earning assets was 2.51% for the first half of 2010, compared to 2.23% in the first half of 2009. The increased interest rate spread was due to declining interest rates on loans which was more than offset by declining interest rates on debt, including positive funding results related to exercising callable debt and other funding actions. Additionally, associations widened their spreads on new and repricing volume since one year ago, primarily in the variable rate product.

Changes in loan volumes are discussed in the Loan Portfolio section of this report.

The District's provision for credit losses for the first half of 2010 was \$118.4 million compared to \$159.1 million during the same period in 2009. The amounts reflect the continued increase in portfolio risk during the periods. At the end of the first half of 2009, there was significant stress in the ethanol industry and large specific reserves were recorded. Pork, dairy and timber sectors are of particular concern at June 30, 2010 and each of these industries have large loan specific and general industry specific reserves. At June 30, 2010, specific reserve totaled \$139.3 million compared to \$98.1 million at June 30, 2009.

The change in non-interest income for the first six months of 2010 results primarily from the following:

- a \$71.2 million increase due to our share of distributions from Allocated Insurance Reserve Accounts (AIRA). These reserve accounts were established in previous years by the Farm Credit System Insurance Corporation when premiums collected increased the level of the Insurance fund beyond the required 2% of insured debt;
- a \$12.6 million decrease in acquired property losses caused by \$7.8 million gain on the sale of ethanol plants during the first half of 2010 and \$4.8 million of losses related to expenses from holding idle ethanol plants in acquired property in 2009;
- an \$11.2 million increase in loan prepayment and fee income;
- a \$10.4 million increase in mineral income following successful well completions plus strong lease and exploration activities; and
- a \$7.6 million gain on the sale of previously impaired securities within AgriBank's liquidity investment portfolio in 2010. In prior years, we recorded \$16.6 million of impairment expense on these securities. This was offset by
- a \$2.3 million net loss related to derivative activities.

The decrease in operating expenses resulted primarily from the following:

- a \$42.9 million decrease in Farm Credit System Insurance Corporation premiums primarily due to a decrease in the premium rate to 5 basis points in June 2010 (retroactively applied to January 1, 2010) compared to 20 basis points in 2009. This was offset by
- a \$7.4 million increase in salaries due to annual merit increases as well as an increase in head count by 2.9% from June 2009 to June 2010,
- a \$9.3 million increase in benefits expense, primarily comprised of an increase in the pension expense of \$6.2 million reflecting the impact of losses in asset value and a 50 basis point decline in the discount rate, an increase in the defined contribution plan expense of \$1.1 million reflecting the increase in staffing (all new employees are in the defined contribution plan) and an increase in medical insurance expense of \$1.3 million reflecting the increased staffing and the increase in the cost of medical care.

AgriBank evaluates all investments in an unrealized loss position quarterly and determined that certain securities were in other-than-temporary loss positions at June 30, 2010. As a result of its evaluations, AgriBank has recognized \$13.4 million in impairment losses during the first half of 2010 compared to \$38.1 million for the same period in 2009. See additional discussion in the Investment Portfolio section of this report.

The change in provision for income taxes is related to the increase in taxable income.

## LOAN PORTFOLIO

The following table presents the components of loan volume:

(in millions)	June 30, 2010	December 31, 2009
Production agriculture:		
Real estate mortgage	\$33,146.6	\$32,663.8
Short and intermediate term	16,187.8	16,425.2
Agribusiness	5,424.7	5,640.2
Rural home loans	2,046.9	1,995.9
Finance leases	603.2	605.4
Other	1,805.7	1,762.2
Nonaccrual	1,149.1	1,152.8
<b>Total loan volume</b>	<b>\$60,364.0</b>	<b>\$60,245.5</b>

District loan volume totaled \$60.4 billion at June 30, 2010, a \$0.1 billion increase from December 31, 2009. Moderate loan growth during the first half of 2010, reflects significant pay downs during the first quarter as retail customers sold crop inventories, a softening in loan demand due to relatively lower commodity prices, continued adherence to strong credit underwriting standards and the continued impact of the recession on the U.S. and global economies. The associations continue to focus on their core traditional clients and are not pursuing certain aspects of capital markets to the extent they did prior to 2009.

The components of risk asset volume follow:

(in millions)	June 30, 2010	December 31, 2009
Nonaccrual	\$1,149.1	\$1,152.8
Accruing restructured	21.5	12.1
Past due 90 days or more still accruing	40.5	30.3
<b>Total risk loans</b>	<b>\$1,211.1</b>	<b>\$1,195.2</b>
Other property owned	49.8	55.8
<b>Total risk assets</b>	<b>\$1,260.9</b>	<b>\$1,251.0</b>
Risk loans as % of total loans	1.98%	1.96%
Risk assets as % of total loans plus other property owned	2.09%	2.07%
Delinquencies as a % of total loans	1.46%	1.39%

At June 30, 2010, 51.3% of nonaccrual volume was current as to principal and interest.

Based on management's analyses, all loans 90 days or more past due and still accruing interest were adequately secured and in the process of collection and, as such, were eligible to remain in accruing status.

Comparative allowance coverage of various loan categories follows:

Allowance as a percentage of:	June 30, 2010	December 31, 2009
Loans	0.69%	0.64%
Nonaccrual loans	36.00%	33.49%
<b>Total risk loans</b>	<b>34.16%</b>	<b>32.30%</b>

The District's allowance for loan losses is an estimate of losses on loans in the AgriBank and Association portfolios as of the financial statement date. AgriBank and Association management determine the appropriate allowance levels based on periodic evaluation of factors such as loan loss history, portfolio quality and current economic and environmental conditions. During the first six months of 2010 we increased our allowance for loan losses by \$27.7 million, which is net of the impact of \$87.3 million of net charge-offs. These allowance changes are reflective of further deterioration in the dairy sector and to a lesser extent, the ethanol, timber, pork and cattle sectors of our portfolio. AgriBank and Association management consider the allowance for loan losses at June 30, 2010 to be reasonable in relation to the risk in the loan portfolios.

## INVESTMENT PORTFOLIO

At June 30, 2010, investments and federal funds held for liquidity purposes by AgriBank totaled \$10.2 billion, up \$668.1 million from December 31, 2009.

AgriBank evaluates all investments in an unrealized loss position quarterly. At June 30, 2010, AgriBank determined that certain securities were in other-than-temporary loss positions. AgriBank believes underlying credit issues in the housing related mortgages that support these securities may result in not collecting all principal and interest contractually due. As a result of its evaluations, AgriBank has recognized \$13.4 million in impairment losses during the first half of 2010 representing \$3.8 million on newly impaired securities and \$9.6 million additional impairment on previously impaired securities. No other securities, including those in the housing related asset and mortgage backed sectors, were in an other-than-temporary loss position. AgriBank has not changed its methodology for identifying securities on which to run its cash flow analysis nor has AgriBank changed its methodology for determining fair value. Reflected in other gains and losses is a \$7.6 million gain from sale of three previously impaired securities in May 2010. In prior years, AgriBank recorded \$16.6 million of impairment expense on these securities.

AgriBank continues to closely monitor its housing related mortgage-backed and asset-backed securities. At June 30, 2010, investment securities included non-agency mortgage-backed securities with a fair value of \$349.0 million and housing related asset-backed securities (subprime, insurance wrapped and second liens) with a fair value of \$237.0 million. The fair value of the non-agency mortgage backed assets reflected a \$78.6 million unrealized loss, and the fair value of the housing related asset-backed securities reflected an unrealized loss of \$78.4 million. Comparatively, at June 30, 2009, AgriBank's non-agency mortgage-backed securities had a fair value of \$419.1 million and housing related asset-backed securities had a fair value of \$352.5 million. The fair value of the non-agency mortgage backed assets reflected a \$196.4 million unrealized loss, and the fair value of the housing related asset-backed securities reflected a net unrealized loss of \$131.7 million at June 30, 2009.

At June 30, 2010, AgriBank had securities that, because the ratings were downgraded below AAA, were no longer eligible under FCA regulations. The fair value of all ineligible investments totaled \$410.3 million including \$133.3 million on which AgriBank has taken impairment charges. Of the securities ineligible under the FCA regulations, securities totaling \$405.0 million have been approved by the FCA to hold beyond six months and be included in AgriBank's net collateral ratio. One security with a fair value of \$5.3 million has not yet received FCA approval. AgriBank believes it will receive approval from FCA to continue holding this security and count the fair value in its net collateral ratio.

In addition, AgriBank held split-rated non-agency mortgage-backed securities and home equity asset-backed securities with a fair value of \$90.8 million that were downgraded below AAA by at least one rating agency, including \$3.0 million on which AgriBank has taken impairment. AgriBank also held \$17.3 million of non-agency mortgage-backed securities and home equity asset-backed securities on credit watch. If any security doesn't retain an AAA rating by at least one rating agency, the security would become ineligible.

Mission-related and other investments held by Associations consisted of \$1.5 billion of government guaranteed instruments, \$425.5 million of securities issued by the Federal Agricultural Mortgage Corporation, \$24.4 million of investment notes in a trust of equipment loans, \$32.0 million of investment securities made up of Agricultural Rural Community (ARC) bonds and a \$1.2 million venture capital equity investment.

## AGRICULTURAL CONDITIONS

The United States Department of Agriculture ("USDA") currently forecasts net farm income for 2010 to be slightly higher than 2009 at \$63.0 billion. The forecasted \$6.6 billion increase in net farm income comes from increased meat and dairy margins, as net crop income continues to decline in 2010. Net farm income levels in 2009 declined significantly from record levels in 2008 reflecting declines in both crop and animal agriculture sectors. USDA estimates 2009 net farm income at \$56.4 billion, down \$30.4 billion (34.5%) from 2008.

## FUNDING, LIQUIDITY AND MEMBERS' EQUITY

AgriBank is responsible for meeting the District's funding, liquidity and asset/liability management needs. Access to funding remains the primary source of liquidity for AgriBank. AgriBank also maintains liquidity through our investment portfolio. AgriBank's liquidity policy and FCA regulations require maintaining a minimum of 90 days of liquidity on a continuous basis, assuming no access to the debt capital markets. The days of liquidity refers to the number of days of maturing debt covered by liquid investments. AgriBank currently operates with a liquidity target of 125 days. As of June 30, 2010, AgriBank had sufficient liquidity to fund all debt maturing within 137 days. AgriBank also has a contingency plan in the event that there is not ready access to traditional funding sources. This plan establishes other avenues for funding such as borrowing overnight via federal funds, using investment securities as collateral to borrow, allowing the investment portfolio to mature and selling investments. Since the fourth quarter of 2009, AgriBank has transitioned the composition of the liquidity investment portfolio to comply with voluntary guidelines AgriBank agreed upon with the other System Banks to improve the quality of liquidity portfolios. The most significant change is that each bank agreed to maintain at least 15 days of liquidity coverage in a combination of U.S. Treasury securities maturing within 3 years and cash held in Federal Reserve Banks. As of June 30, 2010, AgriBank held U.S. Treasury securities with a book value of \$3.0 billion. At June 30, 2010 AgriBank held qualifying assets in excess of that required to meet the 15 days of liquidity coverage.

In March 2010, a District Association issued \$100 million of unsecured subordinated notes due in 15 years with a fixed rate of 9.0% annum, payable semi-annually. The effect of the transaction increased certain regulatory capital ratios pursuant to the Farm Credit Administration regulations.

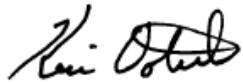
In July 2009, AgriBank issued \$500 million of 9.125% unsecured subordinated notes due 2019. The effect of the transaction increased certain regulatory capital ratios pursuant to the Farm Credit Administration regulations although the impact on our regulatory ratios declines in the last five years the notes are outstanding. These notes are unsecured and subordinate to all other categories of creditors, including general creditors, and senior to all classes of shareholders.

Total members' equity at June 30, 2010 was \$11.1 billion, compared to \$10.3 billion at December 31, 2009. Members' equity was positively impacted during the first six months of 2010 by net income, changes in other comprehensive income, increased stock and participation certificates and a cumulative effect of adoption of new accounting guidance. These increases were partially offset by earnings reserved for patronage distributions.

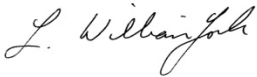
At June 30, 2010, AgriBank and each Association exceeded the regulatory minimum capital ratios, which are further discussed in Note 5 to the financial statements.

#### CERTIFICATION

The undersigned have reviewed the June 30, 2010 quarterly report of AgriBank, FCB and Affiliated Associations has been prepared under the oversight of the audit committee 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.



Keri Votruba  
Chairman of the Board  
AgriBank, FCB  
August 6, 2010



L. William York  
Chief Executive Officer  
AgriBank, FCB  
August 6, 2010



Brian J. O'Keane  
Senior Vice President and Chief Financial Officer  
AgriBank, FCB  
August 6, 2010

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**COMBINED STATEMENT OF CONDITION**

AgriBank, FCB and Affiliated Associations

(Dollars in thousands)

(Unaudited)

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	June 30, 2010	December 31, 2009
<b>Assets</b>		
Loans	\$60,364,028	\$60,245,483
Allowance for loan losses	413,720	386,002
Net loans	59,950,308	59,859,481
Investment securities - AgriBank, FCB	9,723,167	8,866,278
Mission-related and other investments	2,012,516	1,877,871
Other earning assets	262,140	321,096
Cash	40,663	196,049
Federal funds	520,008	708,805
Accrued interest receivable	782,285	818,979
Premises and equipment, net	278,546	271,940
Assets held for lease, net	401,553	415,967
Derivative assets	284,177	242,900
Deferred tax assets, net	5,527	4,729
Other property owned	49,759	55,821
Other assets	188,840	184,821
Total assets	\$74,499,489	\$73,824,737
<b>Liabilities</b>		
Bonds and notes	\$61,722,000	\$61,690,372
Subordinated notes	600,000	500,000
Accrued interest payable	295,310	326,335
Derivative liabilities	9,538	9,546
Deferred tax liabilities, net	80,297	87,813
Accounts payable	104,085	196,041
Patronage payable	22,457	93,838
Postretirement liability	258,790	268,762
Collateral pledged by counterparties	197,600	170,197
Other liabilities	142,535	138,682
Total liabilities	63,432,612	63,481,586
Contingent liabilities		
<b>Members' equity</b>		
Protected capital stock and participation certificates	3,013	3,391
Capital stock and participation certificates	242,920	240,049
Allocated surplus	247,216	229,864
Unallocated surplus	11,003,034	10,350,806
Accumulated other comprehensive loss	(429,306)	(480,959)
Total members' equity	11,066,877	10,343,151
Total liabilities and members' equity	\$74,499,489	\$73,824,737

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

## COMBINED STATEMENT OF INCOME

AgriBank, FCB and Affiliated Associations

(Dollars in thousands)

(Unaudited)

Period ended June 30,	Three months		Six months	
	2010	2009	2010	2009
<b>Interest income</b>				
Loans	\$759,278	\$744,780	\$1,508,251	\$1,488,272
Other earning assets	3,477	4,107	7,008	8,215
Investment securities and federal funds	39,678	48,715	78,150	103,853
Total interest income	802,433	797,602	1,593,409	1,600,340
<b>Interest expense</b>				
	292,800	347,877	589,497	731,080
Net interest income	509,633	449,725	1,003,912	869,260
<b>Provision for credit losses</b>				
	42,148	60,619	118,432	159,136
Net interest income after provision for credit losses	467,485	389,106	885,480	710,124
<b>Non-interest income</b>				
Financially related services	36,492	30,432	57,015	52,632
Loan prepayment fee income	11,012	3,442	17,898	6,687
Allocated insurance reserve account distribution	--	--	71,186	--
Mineral income	7,539	3,461	18,301	7,877
Miscellaneous income and other gains, net	21,211	9,828	41,408	29,629
Total non-interest income	76,254	47,163	205,808	96,825
<b>Non-interest expense</b>				
Salaries and employee benefits	112,393	104,093	224,672	208,012
Other operating expense	58,381	83,827	128,574	167,798
Impairment losses recognized in earnings:				
Total other-than-temporary impairment losses	6,243	39,362	18,603	55,428
Portion of loss recognized in other comprehensive income	(1,740)	(17,293)	(5,248)	(17,293)
Net impairment losses recognized in earnings	4,503	22,069	13,355	38,135
Total non-interest expense	175,277	209,989	366,601	413,945
Income before income taxes	368,462	226,280	724,687	393,004
<b>Provision for income taxes</b>				
	12,680	6,998	33,654	10,411
Net income	\$355,782	\$219,282	\$691,033	\$382,593

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

## COMBINED STATEMENT OF CHANGES IN MEMBERS' EQUITY

AgriBank, FCB and Affiliated Associations

(Dollars in thousands)

(Unaudited)

	Comprehensive Income	Protected Capital	Capital Stock and Participation Certificates	Allocated Surplus	Unallocated Surplus	Accumulated Other Comprehensive Income (Loss)				Total
						Non-other-than- temporarily-impaired Investments	Other-than-temporarily- Impaired Investments	Derivatives	Employee Benefits	
<b>Balance at December 31, 2008</b>		\$4,124	\$224,168	\$204,300	\$9,541,610	\$(354,731)	\$ --	\$(40,523)	\$(310,220)	\$9,268,728
Cumulative effect of adoption of new guidance					31,520		(31,520)			
Comprehensive income										
Net income	\$382,593				382,593					382,593
Other comprehensive income, net of tax:										
Change in unrealized losses on investment securities with other-than-temporary impairment recognition, net of reclassification adjustment of \$9,480	(17,293)						(17,293)			(17,293)
Change in unrealized losses on investment securities not other-than-temporarily impaired, net of reclassification adjustment of \$28,655	97,492					97,492				97,492
Change in net unrealized losses on cash flow hedges, net of reclassification adjustment of \$(3,014)	62,822							62,822		62,822
Other comprehensive income, net of tax	143,021									
Total comprehensive income	\$525,614									
Patronage reserve					(23,706)					(23,706)
Surplus allocated under patronage programs				11,988	(11,988)					--
Distribution of allocated surplus				(21)						(21)
Capital stock/participation certificates issued			13,757							13,757
Capital stock/participation certificates retired		(419)	(10,303)							(10,722)
<b>Balance at June 30, 2009</b>		\$3,705	\$227,622	\$216,267	\$9,920,029	\$(257,239)	\$(48,813)	\$22,299	\$(310,220)	\$9,773,650
<b>Balance at December 31, 2009</b>		\$3,391	\$240,049	\$229,864	\$10,350,806	\$(119,870)	\$(70,462)	\$30,800	\$(321,427)	\$10,343,151
Comprehensive income										
Net income	\$691,033				691,033					691,033
Other comprehensive income, net of tax:										
Change in unrealized losses on investment securities with other-than-temporary impairment recognition, net of reclassification adjustment of \$2,009	22,881						22,881			22,881
Change in unrealized losses on investment securities not other-than-temporarily impaired, net of reclassification adjustment of \$3,769	74,645					74,645				74,645
Change in net unrealized gains on cash flow hedges, net of reclassification adjustment of \$(3,976)	(64,574)							(64,574)		(64,574)
Change in net unrealized losses on pension and postretirement liabilities	18,701								18,701	18,701
Other comprehensive income, net of tax	51,653									
Total comprehensive income	\$742,686									
Patronage reserve					(22,484)					(22,484)
Surplus allocated under patronage programs				17,632	(17,632)					--
Distribution of allocated surplus				(280)						(280)
Cumulative effect of adoption of new accounting guidance					1,311					1,311
Capital stock/participation certificates issued			12,205							12,205
Capital stock/participation certificates retired		(378)	(9,334)							(9,712)
<b>Balance at June 30, 2010</b>		\$3,013	\$242,920	\$247,216	\$11,003,034	\$(45,225)	\$(47,581)	\$(33,774)	\$(302,726)	\$11,066,877

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

# COMBINED STATEMENT OF CASH FLOWS

AgriBank, FCB and Affiliated Associations

(Dollars in thousands)

(Unaudited)

Six months ended June 30	2010	2009
<b>Cash flows from operating activities</b>		
Net income	\$691,033	\$382,593
Adjustments to reconcile net income to cash flow from operating activities:		
Depreciation on premises and equipment	16,192	15,228
Depreciation on assets held for lease	33,116	30,330
Provision for credit losses	118,432	159,136
Decrease in accrued interest receivable	37,481	61,035
Increase in other assets	(4,902)	(33,066)
Decrease in accrued interest payable	(31,044)	(82,790)
Decrease in other liabilities	(90,549)	(125,051)
Loss (gain) on derivative activities	1,479	(811)
Impairment of investments	13,355	38,135
Gain on sale of investments	(7,577)	--
Loss on sale of premises and equipment	124	2,063
Loss (gain) on sale of other property owned	6,503	(139)
Gain on bonds held at fair value under fair value option	(249)	(2,777)
Loss on debt extinguishment	1	--
Gain on disposal of assets held for lease	(504)	(326)
Insurance refund related to FAC stock	(5,141)	--
Total adjustments	86,717	60,967
Net cash provided by operating activities	777,750	443,560
<b>Cash flows from investing activities</b>		
Increase in loans, net	(188,249)	(1,125,250)
Cash added from consolidation of variable interest entity	3,506	--
Decrease in other earning assets	58,956	48,296
Proceeds from sale of other property owned	18,019	5,946
(Increase) decrease in investment securities, net	(916,475)	319,177
Purchases of assets held for lease, net	(18,198)	(31,552)
Purchases of premises and equipment, net	(22,922)	(19,080)
Proceeds from the sale of investments	15,056	--
Proceeds from insurance refund related to FAC stock	5,141	--
Net cash used in investing activities	(1,045,166)	(802,463)
<b>Cash flows from financing activities</b>		
Consolidated bonds and notes (retired) issued, net	(112,518)	434,574
Issuance of subordinated notes	100,000	--
Sale of derivatives	--	11,973
Cash patronage paid	(94,145)	(107,070)
Increase (decrease) in cash collateral pledged by counterparties, net	27,403	(55,680)
Capital stock/participation certificates issued, net	2,493	3,034
Net cash (used in) provided by financing activities	(76,767)	286,831
Net decrease in cash and federal funds	(344,183)	(72,072)
Cash and federal funds at beginning of year	904,854	826,327
Cash and federal funds at end of period	\$560,671	\$754,255
<b>Supplemental schedule of non-cash activities</b>		
(Increase) decrease in derivative assets	\$(41,277)	\$71,505
(Decrease) increase in derivative liabilities	(8)	5,924
Increase (decrease) in bonds and notes from derivative activity	106,962	(140,749)
(Decrease) increase in members' equity from cash flow derivatives	(64,574)	62,822
Increase in members' equity from investments	97,526	80,199
Increase in members' equity from employee benefits	18,701	--
Loans transferred to other property owned	18,460	233,907
Patronage distributions payable to members	22,457	23,503
Cumulative effect of the adoption of accounting principle	1,311	--
Financed sales of other property owned	--	(30,704)
<b>Supplemental information</b>		
Interest paid	\$620,522	\$813,870
Taxes paid	42,308	15,480

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

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## NOTES TO COMBINED FINANCIAL STATEMENTS

*AgriBank, FCB and Affiliated Associations*

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### NOTE 1

#### ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

AgriBank, FCB and Affiliated Associations comprise one of the Districts of the Farm Credit System, a nationwide system of cooperatively owned banks and associations, established by Congress and subject to the provisions of the Farm Credit Act of 1971, as amended. At June 30, 2010, the District had 17 Agricultural Credit Association parent associations, each of which has wholly owned Federal Land Credit Association and Production Credit Association subsidiaries and AgriBank, FCB. AgriBank, FCB serves as the intermediary between the financial markets and the retail lending activities of the District Associations.

A description of the organization and operation of the District, significant accounting policies followed, combined financial condition, and results of operations as of and for the year ended December 31, 2009 are contained in the 2009 annual report. These unaudited second quarter 2010 combined financial statements should be read in conjunction with the annual report.

The accompanying combined financial statements include the accounts of AgriBank combined with its 17 affiliated Associations. All significant transactions and balances between AgriBank and the Associations have been eliminated in combination. The accompanying financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform to accounting principles generally accepted in the United States of America and prevailing practices within the financial services industry.

#### Recent Accounting Developments

Effective January 1, 2010, we adopted the Financial Accounting Standards Board (FASB) amended guidance on "Accounting for Transfers of Financial Assets," which amended previous guidance by providing clarification of the requirements for isolation and limitations on portions of financial assets that are eligible for sale accounting. The guidance also requires additional disclosure about transfers of financial assets and a transferor's continuing involvement with transferred assets. This guidance must be applied to transfers occurring on or after the effective date of January 1, 2010. Adoption of this guidance did not have a material impact on our financial statements.

Effective January 1, 2010, we adopted the FASB amended guidance on consolidation of variable-interest entities (VIE). These amendments require an assessment to determine the primary beneficiary of a VIE based on whether the entity:

- has the power to direct matters that most significantly impact the activities of the VIE; and
- has the obligation to absorb losses or the right to receive benefits of the VIE that could potentially be significant to the VIE.

Additionally, the amendments require an ongoing reconsideration of the primary beneficiary and provide a framework for the events that trigger a reassessment of whether an entity is a VIE. As a result, a securitization transaction held by a District Association was consolidated into our financial statements effective January 1, 2010 and will no longer be an off-balance sheet transaction. The effect of the new guidance was an increase in loans and related assets totaling approximately \$39 million and a related increase in notes payable and related liabilities of approximately \$38 million with a \$1 million members' equity impact of the cumulative effect of adoption. For purposes of this disclosure, the assets and liabilities of this transaction have been measured at their unpaid principal balances and the District Association did not use the fair value measurement. In April 2010, the District Association entered into an agreement to terminate the securitization transaction. This termination did not have a material impact on our financial statements.

Effective January 1, 2010, we adopted FASB amended guidance on "Fair Value Measurements and Disclosures," which is to improve disclosures about fair value measurements by increasing transparency in financial reporting. The guidance provides for a greater level of disaggregated information and more robust disclosures of valuation techniques and inputs to fair value measurements. The adoption of this guidance had no impact on our financial condition and results of operations but resulted in additional disclosures.

## NOTE 2

## LOANS AND ALLOWANCE FOR LOAN LOSSES

A summary of changes in the combined allowance for loan losses is presented in the following table:

Six months ended June 30		
(in thousands)	2010	2009
Balance at beginning of period	\$386,002	\$211,254
Provision for loan losses	114,828	159,136
Charge-offs	(98,474)	(74,943)
Recoveries	11,192	2,739
Other	172	--
Balance at end of period	<u>\$413,720</u>	<u>\$298,186</u>

The provision for loan losses above does not include a \$3.6 million provision on an adverse commitment not yet disbursed upon at a District Association. Additional other allowance of \$0.2 million is related to consolidating a securitization transaction held by a District Association. The charge-offs and provision expenses are reflective of adverse volume in the dairy, pork, poultry, timber and ethanol sectors of the portfolio. We consider the allowance for loan losses at June 30, 2010 to be reasonable in relation to the risk in our loan portfolio.

The following table presents information concerning risk loans (risk loans include nonaccrual loans, accruing restructured loans, and loans past due 90 days or more and still accruing interest):

	June 30	December 31
(in thousands)	2010	2009
Volume with specific reserves	\$594,253	\$641,919
Volume without specific reserves	616,833	553,219
Total risk loans	<u>\$1,211,086</u>	<u>\$1,195,138</u>
Total specific reserves	\$139,343	\$166,521
(in thousands)		
For the six months ended June 30,	2010	2009
Income on accrual risk loans	\$1,416	\$6,407
Income on nonaccrual loans	13,459	13,599
Total income on risk loans	<u>\$14,875</u>	<u>\$20,006</u>
Average recorded investment	\$1,222,669	\$871,667

The increase in risk loans reflects continued stress in the dairy, pork and ethanol sectors of the portfolio.

## NOTE 3

## INVESTMENT SECURITIES AND FEDERAL FUNDS

## AgriBank Investment Securities and Federal Funds

A summary of the amortized cost and fair value of investment securities and federal funds held by AgriBank follows. Commercial paper and other is primarily corporate and municipal obligations, certificates of deposit and term federal funds. All securities are classified as available for sale.

As of June 30, 2010					Weighted
(in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Average Yield
Mortgage-backed securities	\$3,577,222	\$37,741	\$80,780	\$3,534,183	1.5%
U.S. Treasury securities	3,005,597	5,317	68	3,010,846	1.7%
Commercial paper and other	2,541,974	892	27	2,542,839	0.6%
Federal funds	520,008	--	--	520,008	0.1%
U.S. Agencies	344,356	22,578	--	366,934	4.6%
Asset-backed securities	346,824	1,556	80,015	268,365	0.6%
Total	<u>\$10,335,981</u>	<u>\$68,084</u>	<u>\$160,890</u>	<u>\$10,243,175</u>	<u>1.4%</u>

As of December 31, 2009					Weighted
(in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	Average Yield
Mortgage-backed securities	\$3,605,892	\$25,621	\$141,033	\$3,490,480	1.7%
U.S. Treasury securities	1,161,173	--	1,905	1,159,268	2.1%
Commercial paper and other	3,480,818	1,960	156	3,482,622	0.4%
Federal funds	708,805	--	--	708,805	0.1%
U.S. Agencies	345,831	17,819	--	363,650	4.6%
Asset-backed securities	462,896	6,580	99,218	370,258	0.6%
Total	<u>\$9,765,415</u>	<u>\$51,980</u>	<u>\$242,312</u>	<u>\$9,575,083</u>	<u>1.3%</u>

A summary of the investments in an unrealized loss position presented by the length of time that the investments have been in a continuous unrealized loss position follows:

As of June 30, 2010	Less than 12 months		More than 12 months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
(in thousands)				
Commercial paper and other	\$611,986	\$27	\$ --	\$ --
U.S. Treasury securities	205,328	68	--	--
Mortgage-backed securities	45,971	69	866,321	80,711
Asset-backed securities	--	--	249,141	80,015
Total	<u>\$863,285</u>	<u>\$164</u>	<u>\$1,115,462</u>	<u>\$160,726</u>

AgriBank evaluates its investment securities for other-than-temporary impairment on a quarterly basis. Factors considered in determining whether an impairment is other-than-temporary include: 1) the length of time and the extent to which the fair value is less than cost, 2) the financial condition and near-term prospects of the issuer and, if applicable, the financial condition of any financial guarantor, 3) the estimated cash flow projections compared to contractual cash flows, and 4) AgriBank's intent to sell the impaired security and whether AgriBank is more likely than not to be required to sell the security before recovery. In addition, AgriBank qualitatively considers other available information when assessing whether impairment is other-than-temporary. Based on the results of these evaluations, if it is determined that the impairment is other-than-temporary, the loss is separated into credit-related and non-credit-related components. The credit-related portion is recognized through earnings and the non-credit related portion is recognized in other comprehensive income. The credit-related components of the other-than-temporary impairment losses were determined by projecting cash flows using cash flow models which require certain market assumptions. The significant inputs into the models include assumptions with regard to interest rates, prepayment speeds, default rates, and loss severities. The assumptions are applied at the individual security and associated collateral pool level.

The unrealized losses primarily reflect concerns about the creditworthiness and liquidity of home mortgage related asset-backed and mortgage-backed securities. AgriBank determined that securities with a fair value of \$136.3 million at June 30, 2010 were in an other-than-temporary loss position

compared to securities with a fair value of \$137.8 million at December 31, 2009. As a result of its evaluations, AgriBank has recognized \$13.4 million in net impairment losses during the first six months of 2010, reflecting a gross impairment charge in 2010 of \$18.6 million, net of \$5.2 million which was recognized in other comprehensive income. AgriBank has determined no other securities were in an other-than-temporary loss position at June 30, 2010.

The following represents the activity during the first six months of 2010 related to the credit loss component for investments that have been written down for other-than-temporary impairment and the credit component of the loss is recognized in earnings:

(in thousands)	
Balance as of January 1, 2010 - cumulative credit losses for which a portion of an other-than-temporary impairment was recognized in OCI	\$72,129
Additions for credit loss on newly impaired securities	3,769
Reductions for securities sold during the period (realized)	(7,577)
Additional credit losses related to previously impaired securities	9,586
Cumulative credit impairments at June 30, 2010	<u>\$77,907</u>

The following represents the activity during the first six months of 2009 related to the credit loss component for investments that have been written down for other-than-temporary impairment and the credit component of the loss is recognized in earnings:

(in thousands)	
Total life to date losses on impairment of investments at March 31, 2009	\$67,869
Cumulative effect adjustment to income for adoption of FASB guidance on impairment	(31,520)
Adjusted beginning balance - credit losses at April 1, 2009	36,349
Additions for credit loss on newly impaired securities	12,589
Additional credit losses related to previously impaired securities	9,480
Cumulative credit impairments at June 30, 2009	<u>\$58,418</u>

A summary of the contractual maturity at fair value and weighted average yield by maturity of investment securities and federal funds follows:

As of June 30, 2010 (in thousands)	Year of Maturity				Total
	One Year or Less	One to Five Years	Five to Ten Years	More Than Ten Years	
Mortgage-backed securities	\$ --	\$ --	\$324,750	\$3,209,433	\$3,534,183
U.S. Treasury securities	1,334,691	1,676,155	--	--	3,010,846
Commercial paper and other	2,328,613	214,226	--	--	2,542,839
Federal funds	520,008	--	--	--	520,008
U.S. Agencies	5,715	250,385	110,834	--	366,934
Asset-backed securities	--	14,005	409	253,951	268,365
Total	<u>\$4,189,027</u>	<u>\$2,154,771</u>	<u>\$435,993</u>	<u>\$3,463,384</u>	<u>\$10,243,175</u>
Weighted Average Yield	1.1%	1.8%	1.5%	1.5%	1.4%

The expected average life is 2.1 years for asset-backed securities and 2.5 years for mortgage-backed securities. Expected maturities differ from contractual maturities because borrowers may have the right to prepay obligations.

#### Association Investment Securities

Mission-related and other investments held by Associations consisted of \$1.5 billion of government guaranteed instruments, \$425.5 million of securities issued by the Federal Agricultural Mortgage Corporation, \$24.4 million of investment notes in a trust of equipment loans, \$32.0 million of investment securities made up of Agricultural Rural Community (ARC) bonds and a \$1.2 million venture capital equity investment.

The following table presents the book value, unrealized gains and losses, and fair value of the held to maturity investments held by Associations:

As of June 30, 2010					Weighted
(in thousands)	Amortized	Unrealized	Unrealized	Fair	Average
	Cost	Gains	Losses	Value	Yield
Government guaranteed instruments	\$1,529,435	\$13,743	\$31,881	\$1,511,297	2.4%
Farmer Mac mortgage backed securities	425,529	12,174	163	437,540	4.8%
Investment notes in a trust of equipment loans	24,351	716	42	25,025	4.1%
ARC Bonds	31,965	1,921	--	33,886	6.1%
Total	<u>\$2,011,280</u>	<u>\$28,554</u>	<u>\$32,086</u>	<u>\$2,007,748</u>	<u>3.0%</u>

As of December 31, 2009					Weighted
(in thousands)	Amortized	Unrealized	Unrealized	Fair	Average
	Cost	Gains	Losses	Value	Yield
Government guaranteed instruments	\$1,359,322	\$9,933	\$22,146	\$1,347,109	2.3%
Farmer Mac mortgage backed securities	459,431	9,037	7,365	461,103	6.0%
Investment notes in a trust of equipment loans	41,132	892	107	41,917	3.7%
ARC Bonds	15,951	141	298	15,794	6.4%
Total	<u>\$1,875,836</u>	<u>\$20,003</u>	<u>\$29,916</u>	<u>\$1,865,923</u>	<u>3.3%</u>

#### NOTE 4

##### SUBORDINATED NOTES

In March 2010, a District Association issued \$100 million of unsecured subordinated notes due in 15 years with a fixed rate of 9.0% per annum, payable semi-annually. The Association may redeem all or some of the notes at any time on or after a date 10 years from the closing date. These notes are unsecured and subordinate to all other categories of creditors, including general creditors, and senior to all classes of shareholders. These notes are included in certain regulatory capital ratios subject to limitations.

In July 2009, AgriBank issued \$500 million of 9.125% unsecured subordinated notes due 2019, generating net proceeds of \$496.8 million. The effect of the transaction increased certain regulatory capital ratios. These notes are unsecured and subordinate to all other categories of creditors, including general creditors, and senior to all classes of shareholders. Interest is payable semi-annually on January 15 and July 15 beginning on January 15, 2010. Interest is deferred if, as of the fifth business day prior to an interest payment date of the notes, any applicable minimum regulatory capital ratios are not satisfied. A deferral period may not last for more than five consecutive years or beyond the maturity date of the subordinated notes. During such a period, AgriBank may not declare or pay any dividends or patronage refunds, among certain other restrictions, until interest payments are resumed and all deferred interest has been paid. The subordinated notes are not Systemwide debt and are not obligations of any of the other Banks of the Farm Credit System. Payments on the subordinated notes are not insured by the Farm Credit Insurance Fund.

The inclusion of subordinated notes in regulatory capital ratios is subject to certain limitations. The amount of subordinated notes eligible to be counted as permanent capital and total surplus may not exceed 50% of core surplus, and is reduced by 20% of the original amount at the beginning of each of the last five years of the term of the notes. Additionally, the amount of subordinated notes that may be counted in total surplus must not exceed the lower of 40% of permanent capital or 100% of core surplus. Subordinated notes that are not included in permanent capital and total surplus due to these limitations are required to be included as liabilities for the purpose of calculating AgriBank's net collateral ratio.

The subordinated notes are not Systemwide debt and are not obligations of any of the other Banks of the Farm Credit System. Payments on the subordinated notes are not insured by the Farm Credit Insurance Fund.

#### NOTE 5

##### CAPITAL

Farm Credit Administration's capital adequacy regulations require AgriBank and the Associations to maintain permanent capital of at least 7.0% of risk-adjusted assets. In addition, each System institution is required to maintain a total surplus to risk-adjusted assets ratio of at least 7.0% and a core surplus to risk-adjusted assets ratio of at least 3.5%. At June 30, 2010, AgriBank exceeded these requirements with a 20.0% permanent capital ratio, 15.9% total surplus ratio, and 9.3% core surplus ratio. All District Associations exceeded the regulatory minimums at June 30, 2010.

Farm Credit Administration regulations also require AgriBank to maintain a net collateral ratio of at least 103.0%. However, AgriBank is required by the regulator to maintain a higher minimum of 104.0% during the period in which AgriBank has subordinated notes outstanding. At June 30, 2010, AgriBank's net collateral ratio was 106.0%.

## NOTE 6

### EMPLOYEE BENEFIT PLANS

Net periodic benefit costs included the following components:

Six months ended June 30 (in thousands)	2010		2009	
	Pension Benefits	Other Benefits	Pension Benefits	Other Benefits
<b>Components of net periodic benefit cost</b>				
Service cost	\$10,692	\$308	\$9,676	\$298
Interest cost	21,409	812	20,254	851
Expected return on plan assets	(22,997)	--	(23,106)	--
Amortization of prior service cost	(518)	(312)	(516)	(312)
Amortization of loss or (gain)	10,774	(68)	6,713	(98)
Net periodic benefit cost	<u>\$19,360</u>	<u>\$740</u>	<u>\$13,021</u>	<u>\$739</u>

The District previously disclosed in our financial statements for the year ended December 31, 2009, that the District expected to contribute \$23.0 million for pension benefits and \$1.7 million for other postretirement benefits in 2010. As of June 30, 2010, District employers have contributed \$10.1 million to the pension plan. District employers presently anticipate contributing an additional \$15.2 million to fund pension benefits in 2010. As of June 30, 2010, District employers have contributed \$761 thousand for other postretirement benefits. District employers anticipate contributing an additional \$781 thousand for other postretirement benefits in 2010.

## NOTE 7

### COMMITMENTS AND CONTINGENCIES

District entities may, from time to time, be named as defendants in certain lawsuits or legal actions in the normal course of business. At the date of these financial statements, management was not aware of any such actions that would have a material impact on the entities' financial condition. However, AgriBank and Association management cannot ensure that such actions or other contingencies will not arise in the future.

While AgriBank is primarily liable for our portion of Systemwide bonds and notes, AgriBank is jointly and severally liable for the Systemwide bonds and notes of the other Farm Credit System Banks. The total bonds and notes of the Farm Credit System at June 30, 2010 were \$176.8 billion.

## NOTE 8

### FAIR VALUE MEASUREMENTS

#### Valuation Techniques

Authoritative guidance on "Fair Value Measurements and Disclosures" defines fair value, establishes a framework for measuring fair value and requires disclosures for certain assets and liabilities measured at fair value on a recurring and non-recurring basis. These assets and liabilities primarily consist of investments available-for-sale, federal funds, derivative assets and liabilities, impaired loans, other property owned, and collateral liabilities. This 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 establishes a fair value 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 valuation 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 valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The three levels of inputs and the classification of our financial instruments measured on a recurring basis within the fair value hierarchy are as follows:

#### Level 1

Level 1 inputs in the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. Level 1 assets and liabilities could include debt and equity securities and derivative contracts that are traded in an active exchange market, as well as certain U.S. Treasury, other U.S. Government and agency mortgage-backed debt securities that are highly liquid and are actively traded in over-the-counter markets. Our Level 1 assets at June 30, 2010 consist of U.S. Treasury Securities held by AgriBank.

Our Level 1 liabilities also include collateral liabilities. The majority of derivative contracts are supported by bilateral collateral agreements with counterparties requiring the posting of cash collateral in the event certain dollar thresholds of credit exposure are reached. The market value of collateral liabilities is its face value that approximates fair value.

### *Level 2*

Level 2 inputs in 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 2 assets and liabilities could include certain U.S. Government and agency mortgage-backed debt securities, corporate debt securities and derivative contracts.

The fair value of substantially all of AgriBank's investment securities is determined from third-party valuation services that estimate current market prices. Inputs and assumptions related to third-party market valuation services are typically observable in the marketplace. Such services incorporate repayment assumptions and underlying mortgage- or asset-backed collateral information to generate cash flows that are discounted using appropriate benchmark interest rate curves and volatilities including LIBOR, Treasury and other Index benchmarks. Third-party valuations also incorporate information regarding broker/dealer quotes, available trade information, historical cash flows, credit ratings, and other market information. Such valuations represent an estimated exit price, or price to be received by a seller in active markets to sell the investment securities to a willing participant.

The fair value of AgriBank's derivative financial instruments is the estimated amount to be received to sell a derivative asset or paid to transfer a derivative liability in active markets among willing participants at the reporting date. Estimated fair values are determined through internal market valuation models. These models incorporate LIBOR swap curves, market volatilities, and other inputs which are observable directly or indirectly in the marketplace. AgriBank compares internally calculated derivative valuations to broker/dealer quotes to substantiate the results.

Our Level 2 assets and liabilities at June 30, 2010 include derivative assets and liabilities, commercial paper, mortgage-backed securities and U.S. Agency securities, all of which have unadjusted values from third-party or internal pricing models. Level 2 assets also include federal funds. The market value of federal funds is generally their face value, plus accrued interest, as these instruments are highly-liquid, readily convertible to cash, and short-term in nature.

### *Level 3*

Level 3 inputs in the valuation methodology are unobservable and supported by little or no market activity. Level 3 assets and liabilities could include investments and derivative contracts whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, and other instruments for which the determination of fair value requires significant management judgment or estimation. Level 3 assets and liabilities also could include investments and derivative contracts whose price has been adjusted based on dealer quoted pricing that is different than the third-party valuation or internal model pricing.

Level 3 assets at June 30, 2010 include AgriBank's mortgage-related asset-backed investment portfolio and non-agency mortgage-backed securities. Based on the relatively illiquid marketplace for these investments and the lack of marketplace information available as inputs and assumptions to the valuation process, AgriBank classified the mortgage-related asset-backed investment portfolio and non-agency mortgage-backed securities as Level 3 assets. The fair value measurement of these assets involved management's judgment and was based on multiple factors including information obtained from third-party valuation services using both Level 2 and Level 3 inputs. These inputs include volatilities, market spreads, prepayment speeds and dealer quotes.

Level 3 liabilities at June 30, 2010 include standby letters of credit whose market value is internally calculated based on information that is not observable either directly or indirectly in the marketplace.

The classification of our financial instruments, measured at fair value on a non-recurring basis, is as follows:

Level 3 and level 2 assets at June 30, 2010 include certain loans evaluated for impairment under FASB guidance which have fair values based upon the underlying collateral as the loans were collateral-dependent. Since the value of the collateral, less estimated costs to sell, was less than the principle balance of the loan, specific reserves were established for these loans. The fair value measurement would fall under Level 2 of the hierarchy if the process uses independent appraisals and other market-based information. The fair value measurement would fall under Level 3 of the hierarchy if the process requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral, and other matters.

Other property owned is classified as a Level 3 asset at June 30, 2010. The fair value for other property owned is based upon the collateral fair value. Costs to sell represent transaction costs and are not included as a component of the fair value of other property owned.

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

As of June 30, 2010 (in thousands)	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
Federal funds sold and securities purchased				
under resale agreements	\$ --	\$520,008	\$ --	\$520,008
Investments available for sale				
Mortgage-backed securities	--	3,185,283	348,900	3,534,183
U.S. Treasury securities	3,010,846	--	--	3,010,846
Commercial paper and other	--	2,542,839	--	2,542,839
U.S Agencies	--	366,934	--	366,934
Asset-backed securities	--	--	268,365	268,365
Total investments available for sale	3,010,846	6,095,056	617,265	9,723,167
Derivative assets	--	284,177	--	284,177
Total assets	\$3,010,846	\$6,899,241	\$617,265	\$10,527,352
<b>Liabilities:</b>				
Cash collateral pledged by counterparties	\$197,600	\$ --	\$ --	\$197,600
Derivative liabilities	--	9,538	--	9,538
Stand by letters of credit	--	--	154	154
Total liabilities	\$197,600	\$9,538	\$154	\$207,292

As of December 31, 2009 (in thousands)	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
Federal funds sold and securities purchased				
under resale agreements	\$ --	\$708,805	\$ --	\$708,805
Investments available for sale				
Mortgage-backed securities	--	3,108,445	382,035	3,490,480
U.S. Treasury securities	1,159,268	--	--	1,159,268
Commercial paper and other	--	3,482,622	--	3,482,622
U.S Agencies	--	363,650	--	363,650
Asset-backed securities	--	--	371,891	371,891
Total investments available for sale	1,159,268	6,954,717	753,926	8,867,911
Derivative assets	--	242,575	325	242,900
Total assets	\$1,159,268	\$7,906,097	\$754,251	\$9,819,616
<b>Liabilities:</b>				
Systemwide debt securities	\$ --	\$100,249	\$ --	\$100,249
Cash collateral pledged by counterparties	170,197	--	--	170,197
Derivative liabilities	--	9,546	--	9,546
Stand by letters of credit	--	--	143	143
Total liabilities	\$170,197	\$109,795	\$143	\$280,135

We did not have any assets or liabilities transfer between levels during the first half of 2010.

The table below represents a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3):

Level 3 Instruments Only				
(in thousands)	Total Fair Value Measurement			
	Investments Available For Sale			
	Asset-backed Securities	Mortgage-backed Securities	Derivative Assets	Standby Letters of Credit
<b>Balance at December 31, 2009</b>	\$371,891	\$382,035	\$325	\$143
Total gains or losses realized/unrealized:				
Included in earnings	7,537	(13,315)	(325)	11
Included in other comprehensive income	14,179	50,344	--	--
Purchases, issuances and settlements	(125,242)	(70,164)	--	--
Transfers in and/or out of Level 3	--	--	--	--
<b>Balance at June 30, 2010</b>	<b>\$268,365</b>	<b>\$348,900</b>	<b>\$ --</b>	<b>\$154</b>

Level 3 Instruments Only				
(in thousands)	Total Fair Value Measurement			
	Investments Available For Sale			
	Asset-backed Securities	Mortgage-backed Securities	Derivative Assets	Standby Letters of Credit
Balance at December 31, 2008	\$625,579	\$544,613	\$1,200	\$145
Total gains or losses realized/unrealized:				
Included in earnings	(22,568)	(15,567)	(389)	(6)
Included in other comprehensive income	(4,978)	21,963	--	--
Purchases, issuances and settlements	(136,426)	(132,008)	--	--
Transfers in and/or out of Level 3	--	--	--	--
Balance at June 30, 2009	\$461,607	\$419,001	\$811	\$139

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

As of June 30, 2010 (in thousands)	Fair Value Measurement Using			Total Fair Value	Total (Gains) Losses
	Level 1	Level 2	Level 3		
Assets:					
Loans	\$ --	\$170,824	\$309,462	\$480,286	\$(27,177)
Other property owned	--	--	51,749	51,749	7,777

As of December 31, 2009 (in thousands)	Fair Value Measurement Using			Total Fair Value	Total Losses
	Level 1	Level 2	Level 3		
Assets:					
Loans	\$ --	\$233,876	\$244,340	\$478,216	\$75,696
Other property owned	--	--	58,054	58,054	3,913

## NOTE 9

### DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

#### Use of Derivatives

AgriBank maintains an overall interest rate risk management strategy that incorporates the use of derivative products to minimize significant unplanned fluctuations in earnings that are caused by interest rate volatility. AgriBank's goals are to manage interest rate sensitivity by modifying the

repricing or maturity characteristics of certain balance sheet assets and liabilities so that movements in interest rates do not adversely affect the net interest margin. As a result of interest rate fluctuations, hedged fixed-rate liabilities will appreciate or depreciate in market value. The effect of this unrealized appreciation or depreciation is expected to be substantially offset by AgriBank's gains or losses on the derivative instruments that are linked to these hedged assets and liabilities. Another result of interest rate fluctuations is that the interest income and interest expense of hedged floating-rate liabilities will increase or decrease. The effect of this variability in earnings is expected to be substantially offset by AgriBank's gains and losses on the derivative instruments that are linked to these hedged assets and liabilities. AgriBank considers the use of derivatives to be a prudent method of managing interest rate sensitivity, as it prevents earnings from being exposed to undue risk posed by changes in interest rates.

AgriBank enters into derivative transactions, particularly interest rate swaps, to lower funding costs, diversify sources of funding, alter interest rate exposures arising from mismatches between assets and liabilities, or to better manage liquidity. AgriBank may also enter into derivatives with District Associations as a service to enable them to transfer, modify or reduce their exposure to retail interest rate risk. AgriBank substantially offsets this risk by concurrently entering into offsetting agreements with non-System institutional counterparties. Interest rate swaps allow AgriBank to raise long-term borrowings at fixed rates and swap them into floating rates that are lower than those available to AgriBank if floating rate borrowings were made directly. Under interest rate swap arrangements, AgriBank agrees with other parties to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating rate index. AgriBank may purchase interest rate options, such as caps, in order to offset the impact of rising interest rates on AgriBank's floating-rate debt, and floors, in order to offset the impact of falling interest rates on related floating-rate assets.

The primary types of derivative instruments used and the amount of activity during the period (in notional amount) is summarized in the following table:

(in millions)	Receive-Fixed Swaps	Pay-Fixed and Amortizing	Floating-for-Floating and Amortizing	Interest Rate Caps	Other Derivatives	Total
		Pay-Fixed Swaps	Floating-for-Floating			
<b>Balance at January 1, 2010</b>	\$7,415	\$675	\$1,350	\$3	\$481	\$9,924
Additions	400	100	--	--	138	638
Maturities/amortization	700	16	50	--	140	906
Terminations	--	--	--	--	23	23
<b>Balance at June 30, 2010</b>	<b>\$7,115</b>	<b>\$759</b>	<b>\$1,300</b>	<b>\$3</b>	<b>\$456</b>	<b>\$9,633</b>

(in millions)	Receive-Fixed Swaps	Pay-Fixed and Amortizing	Floating-for-Floating and Amortizing	Interest Rate Caps	Other Derivatives	Total
		Pay-Fixed Swaps	Floating-for-Floating			
<b>Balance at January 1, 2009</b>	\$9,130	\$595	\$1,650	\$18	\$281	\$11,674
Additions	750	--	450	--	126	1,326
Maturities/amortization	1,640	17	250	5	143	2,055
Terminations	--	--	250	--	--	250
<b>Balance at June 30, 2009</b>	<b>\$8,240</b>	<b>\$578</b>	<b>\$1,600</b>	<b>\$13</b>	<b>\$264</b>	<b>\$10,695</b>

By using derivative products, AgriBank exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, AgriBank's credit risk will equal the fair value gain in a derivative. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes AgriBank, thus creating credit risk for AgriBank. When the fair value of the derivative contract is negative, AgriBank owes the counterparty and, therefore, AgriBank does not have credit risk to that counterparty.

To minimize the risk of credit losses, AgriBank only deals with non-customer counterparties that have an investment grade or better credit rating from a rating agency and also monitors the credit standing and levels of exposure to individual counterparties. AgriBank does not anticipate nonperformance by any of these counterparties. AgriBank typically enters into master agreements that contain netting provisions. These provisions allow AgriBank to require the net settlement of covered contracts with the same counterparty in the event of default by the counterparty on one or more contracts. Substantially all derivative contracts are supported by bilateral collateral agreements with counterparties requiring the posting of collateral in the event certain dollar thresholds of exposure of one party to the other are reached. These thresholds vary depending on the counterparty's current credit rating. At June 30, 2010, AgriBank's exposure to counterparties, net of collateral, was \$98.5 million. At June 30, 2010, AgriBank held cash collateral of \$197.6 million and \$27.7 million in pledged securities from counterparties.

AgriBank's derivative activities are monitored by its Asset-Liability Management Committee (ALCO) as part of the Committee's oversight of AgriBank's asset/liability and treasury functions. AgriBank's ALCO is responsible for approving hedging strategies that are developed within parameters established by the Bank's board of directors through AgriBank's analysis of data derived from financial simulation models and other

internal and industry sources. The resulting hedging strategies are then incorporated into AgriBank's overall interest rate risk-management strategies.

## Accounting for Derivatives

*Fair-Value Hedges:* For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current earnings. We include the gain or loss on the hedged items in the same line item (interest expense) as the offsetting loss or gain on the related interest rate swaps. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

*Cash Flow Hedges:* For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

*Derivatives not Designated as Hedges:* For derivatives not designated as a hedging instrument, the related change in fair value is recorded in current period earnings in "Miscellaneous income and other gains, net" in the Combined Statement of Income.

## Financial Statement Impact of Derivatives

The following table presents the gross fair value of derivative assets and derivative liabilities. The fair value of our derivative contracts are presented as "Derivative assets" and "Derivative liabilities" in the Combined Statement of Condition, and are presented net on the Combined Statement of Condition for counterparties with master netting agreements.

(in thousands)	June 30, 2010		December 31, 2009	
	Fair Value	Fair Value	Fair Value	Fair Value
	Assets:	Liabilities:	Assets:	Liabilities:
Derivatives designated as hedging instruments:				
Receive-fixed swaps	\$313,607	\$ --	\$223,315	\$13,759
Pay-fixed and amortizing pay-fixed swaps	18,674	46,315	48,323	21,984
Floating-for-floating and amortizing floating-for-floating swaps	--	7,743	111	1,277
Total derivatives designated as hedging instruments	332,281	54,058	271,749	37,020
Derivatives not designated as hedging instruments:				
Receive-fixed swaps	--	753	251	878
Interest rate caps	--	--	5	--
Foreign exchange contracts	126	52	--	302
Other derivative products	33	--	596	--
Total derivatives not designated as hedging instruments	159	805	852	1,180
Credit valuation adjustment	(2,938)	--	(1,047)	--
Total derivatives	\$329,502	\$54,863	\$271,554	\$38,200

The fair value of derivatives includes credit valuation adjustments (CVA) which totaled \$2.9 million at June 30, 2010 and \$1.0 million at December 31, 2009. The CVA reflects credit risk of each derivative counterparty to which AgriBank has exposure, net of any collateral posted by the counterparty, and an adjustment for our credit worthiness where the counterparty has exposure to us. The CVA is included in "Miscellaneous income and other gains, net" on the Combined Statement of Income.

AgriBank recorded \$2.9 million of losses at June 30, 2010 and \$1.5 million of gains at June 30, 2009 related to receive-fixed swaps which are designated as hedging instruments on the Combined Statement of Income. The gains and losses on the derivative instruments are recognized in "Interest expense" on the Combined Statement of Income.

The following table presents the amount of OCI recognized on derivatives. The gain or (loss) on derivatives designated as hedges reclassified from accumulated other comprehensive income into income is included in "interest expense" on the Combined Statement of Income.

For the period ended June 30, 2010 (in thousands):

Derivatives - Cash Flow Hedging Relationships	Amount of Loss Recognized in OCI on Derivatives (Effective Portion)	Amount of Gain or (Loss) reclassified from AOCI into Income (Effective Portion)	Amount of Gain recognized in Income on Derivatives (Ineffective Portion) and amount excluded from effectiveness testing
Pay-fixed and amortizing pay-fixed swaps	\$(54,113)	\$692	\$42
Floating-for-floating and amortizing floating-for-floating swaps	(6,486)	4,014	--
Other derivative products	--	(731)	--
Total	<u>\$(60,599)</u>	<u>\$3,975</u>	<u>\$42</u>

For the period ended June 30, 2009 (in thousands):

Derivatives - Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion)	Amount of Gain or (Loss) reclassified from AOCI into Income (Effective Portion)	Amount of Gain or (Loss) recognized in Income on Derivatives (Ineffective Portion) and amount excluded from effectiveness testing
Pay-fixed and amortizing pay-fixed swaps	\$66,774	\$847	\$80
Floating-for-floating and amortizing floating-for-floating swaps	(948)	2,898	(989)
Interest rate caps	10	--	--
Other derivative products	--	(731)	--
Total	<u>\$65,836</u>	<u>\$3,014</u>	<u>\$(909)</u>

The following table presents the effect of derivative instruments not designated as hedging instruments on the Combined Statement of Income. The gain or (loss) on derivatives not designated as hedges is included in "Miscellaneous income and other gains, net" on the Combined Statement of Income.

For the period ended June 30 (in thousands)	2010 Amount of Loss Recognized	2009 Amount of Loss Recognized
Derivatives Not Designated as Hedging Instruments		
Receive-fixed swaps	\$(126)	\$(2,718)
Floating-for-floating and amortizing floating-for-floating swaps	--	--
Interest rate caps	(5)	(2)
Other derivative products	(563)	(72)
Total	<u>\$(694)</u>	<u>\$(2,792)</u>

## NOTE 10 SUBSEQUENT EVENTS

We have evaluated subsequent events through August 6, 2010, which is the date the financial statements were available to be issued.

## NOTE 11

## AGRIBANK ONLY DATA

Statement of Condition (in thousands)	June 30, 2010	December 31, 2009
Loans, net	\$55,167,844	\$55,636,376
Other assets	11,125,842	10,506,955
Total assets	<u>\$66,293,686</u>	<u>\$66,143,331</u>
Liabilities	\$62,855,391	\$62,876,696
Members' equity	3,438,295	3,266,635
Total liabilities and members' equity	<u>\$66,293,686</u>	<u>\$66,143,331</u>
Statement of Income (in thousands)	Six months ended June 30	
	2010	2009
Interest income	\$849,288	\$958,193
Interest expense	586,112	731,133
Net interest income	263,176	227,060
Provision for loan losses	(5,000)	(5,634)
Other, net	25,134	(30,674)
Net income	<u>\$283,310</u>	<u>\$190,752</u>
Patronage	\$119,326	\$101,782

Substantially all patronage is paid to the Associations and is eliminated in combination.



AgriBank, FCB and Affiliated Associations

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375 Jackson Street • St. Paul, Minnesota 55101-1810 • (651) 282-8800

Visit us at [www.agribank.com](http://www.agribank.com)