





## **NOTICE**

The shareholders' investment in Oklahoma AgCredit, ACA is materially affected by the financial condition and results of operations of CoBank, ACB, (CoBank). The 2022 CoBank Annual Report to Shareholders and the CoBank quarterly shareholders' reports are available free of charge by accessing CoBank's website, <a href="https://www.cobank.com">www.cobank.com</a>, or may be obtained at no charge by contacting us at:

Oklahoma AgCredit, ACA 3033 Progressive Drive Edmond, Oklahoma 73034 405-938-1700



# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(Unaudited)

The following discussion summarizes the financial position and results of operations of Oklahoma AgCredit, ACA (the Association) for the nine months ended September 30, 2023, with comparisons to prior periods. You should read these comments along with the accompanying financial statements and footnotes and the 2022 Annual Report to Shareholders. The accompanying financial statements were prepared under the oversight of our Audit Committee.

#### **ECONOMIC OVERVIEW**

While the U.S. economy remains healthy, supply chain disruptions, labor shortages, fuel prices, inflation, rising interest rates, weather related events, and recession pressures remain a concern. The steady strengthening of labor markets and increased consumer spending through the current year have led to economic growth. The rural economy continues to benefit from the strong U.S. economy, driving higher levels of spending and investment by businesses and consumers. Most agricultural commodity prices have remained strong despite some decline from sharp increases in 2022. The Russia/Ukraine conflict has also impacted certain agricultural commodity prices and created additional volatility and uncertainty in the markets. Although inflation has continued to decline through 2023, the Fed has indicated that it will continue to fight inflationary pressure with interest rate hikes and restrictive monetary policies, resulting in four interest rate increases in 2023 of 25 basis points each. The anticipation of tighter monetary policy is contributing to a stronger dollar and changes in the shape of the yield curve.

Economic activity remained stable across Oklahoma throughout the third quarter. The state's unemployment rate of 2.7% is significantly lower than the national average of 3.8%. The stable economic activity should result in stability for our customers' repayment abilities and asset values. Agricultural real estate values remain stable and will continue to be closely monitored in the future.

The inversion of the 2-year treasury rate and 10-year treasury rate has moderated, yet still reflects the bond market's anticipation of a potential economic recession. The stock market showed a slight decline throughout the third quarter with the S&P 500 declining 3.3% compared to the end of the second quarter.

Our trade territory received above average rainfall starting in late spring through early summer but declined to below average levels during the summer months. The much-needed precipitation resulted in a good hay crop which will provide supplemental forage during the winter months. Summer crops fared from below average to average as a result of the reduced amount of late summer rainfall.

Throughout the quarter, cattle prices have strengthened. Grain prices have experienced significant volatility with a general decline in prices for most area grain crops including wheat and corn. Higher operating input prices remain a concern for state producers.

West Texas Intermediate crude, which began the quarter at \$75 per barrel, trended sharply upward closing over \$90 per barrel at quarter end and reached as high as \$94 per barrel during the quarter. Natural gas prices trended higher the last six months after falling 10% during the first quarter 2023. The Oklahoma rig count declined slightly from 40 to 37 during the third quarter. The national rig count declined at a similar rate.

Climate risk has evolved over time along with many improvements made by the agricultural sector to address potential climate changes such as global warming and increasingly arid conditions. These improvements in farming practices, seed genetics, rotational grazing, and soil aeration have mitigated some of the impact of climate change throughout the agricultural sector. Agricultural producers continue to adjust to these conditions and have implemented additional practices such as no-till planting, minimal till practices, cover crops, and other water conservation techniques to manage reduced amounts of rainfall and to keep their farm and ranch land in a state of sustainable production. Therefore, at the present time, the impact on credit risk and collateral values has been manageable, as evidenced by increasing real estate values across our territory. If severe climatic changes continue, there could be a negative effect upon real estate values.

#### **LOAN PORTFOLIO**

Loans outstanding at September 30, 2023, totaled \$1.93 billion, an increase of \$63.2 million, or 3.4%, from loans of \$1.87 billion at December 31, 2022. The increase in loans was due to increased participations purchased for diversification and growth.



Overall, the credit quality of our loan portfolio remained sound during the first nine months of 2023, with credit quality ratios improving slightly and nonaccrual balances increasing \$5.9 million since December 31, 2022.

#### OTHER PROPERTY OWNED

Other property owned is real or personal property that has been acquired through foreclosure, deed in lieu of foreclosure, or other means. We had other property owned of \$1.1 million at September 30, 2023, compared with \$47 thousand at December 31, 2022.

In the second quarter of 2023, the Association acquired land on which it held a foreclosed judgment lien, which its predecessor-in-interest, Farm Credit Services of East Central Oklahoma, ACA ("East Central"), had received in exchange for services rendered to another Farm Credit System Institution. Until this year, the likelihood of realization of any amounts under the lien was remote, therefore no amounts related to it were ever recognized in the financial statements either of East Central or of the Association. Due to the nature of its acquisition, the property has been properly classified as other property owned in the Association's Statement of Condition.

#### **RESULTS OF OPERATIONS**

Net income for the nine months ended September 30, 2023, was \$25.3 million, an increase of \$849 thousand, or 3.5%, from the same period ended one year ago. The increase was primarily due to higher net interest income and higher noninterest income, offset by an increase in provision for credit losses and higher noninterest expense.

Net interest income for the nine months ended September 30, 2023, was \$40.0 million, an increase of \$3.4 million, or 9.2%, compared with the nine months ended September 30, 2022. Interest rate spread decreased by 15 basis points. Interest income increased as a result of an increase in borrower rates and an increase in average loan volume growth of 6.4%. Interest expense increased due to an increase in rates and an average volume increase in debt to CoBank of 6.5%. Net interest margin increased 7 basis points, due to a \$3.9 million increase in the return on our own capital.

For the nine months ended September 30, 2023, the Association recognized a \$1.9 million provision for credit losses, an increase of \$1.8 million from the provision for credit losses for the same period ended one year ago. Most of the increase was attributable to \$1.8 million in specific reserves in the first nine months of 2023 for two large participations and one borrower with cattle loans, compared to a \$711 thousand provision for one large participation in the processing and marketing portfolio. In 2023, the management adjustment was a provision of \$149 thousand compared to a reversal of \$722 thousand in 2022 due to higher commodity prices and an improvement in the post-pandemic economic environment. Net charge-offs of \$27 thousand were recognized in 2023, compared to \$44 thousand of net recoveries in 2022. These increases were partially offset by a \$117 thousand increase in the reversal of credit losses from the general reserve and a \$102 thousand increase in the reversal for unfunded commitments, compared to provisions for credit losses in the same period one year ago. The change in the general reserve and the reserve for unfunded commitments was driven by a decrease in historical loss rates.

Noninterest income increased \$601 thousand during the nine months of 2023 compared with the first nine months in 2022, primarily due to a \$1.1 million contingency gain recognized by the Association upon its acquisition of other property owned in the second quarter, discussed above. The fair value of the property, less estimated costs to sell, has been recognized in the income statement as a contingency gain, rather than as a reduction of loan principal or as a recovery, since neither the Association nor East Central ever held a loan receivable related to this property, and therefore has not recorded any losses related to it. Other increases in noninterest income include a \$187 thousand increase in patronage income from CoBank as well as a \$210 thousand increase in loan fees for participations and Rural 1st fees. The increase in patronage income from CoBank is the result of higher direct note volume in 2023, offset by additional patronage of \$144 thousand paid in 2022 primarily due to CoBank's growth. These increases to noninterest income were offset by a \$703 thousand decrease in other noninterest income, which is primarily attributable to the gain of \$520 thousand on the sale of a branch office building during third quarter 2022, fewer vehicle disposals, and the decrease in our portion of FCS Association Captive Insurance Company allocated earnings.

Mineral income of \$692 thousand was recognized during the first nine months of 2023. Of this amount, \$673 thousand was received from CoBank. The decrease for the nine months ended September 30, 2023 compared with the first nine months of 2022 is related to a decrease in the price paid for production.

During the first nine months of 2023, noninterest expense increased \$1.3 million to \$21.8 million, primarily due to merit increases, pension expense, fees paid to AgVantis and other professional service providers, and lower deferred costs related to lower loan origination activity than in the prior year. These increases were offset by slightly lower Farm Credit System Insurance Corporation (FCSIC) premiums, following a decrease in the insurance premium



accrual assessment rate on Systemwide adjusted insured debt from 20 basis points to 18 basis points, partially offset by an increase in average loan volume.

#### **CAPITAL RESOURCES**

Our shareholders' equity at September 30, 2023, was \$369.9 million, an increase of \$25.6 million since December 31, 2022. This increase is due to net income of \$25.3 million and a \$321 thousand adjustment upon adoption of the new standard on current expected credit losses (CECL), offset by net stock retirements.

#### **OTHER MATTERS**

Effective January 1, 2023, our Association adopted the new standard on CECL, under which the allowance is measured based on management's best estimate of current expected credit losses over the remaining contractual life of the loan. Prior periods presented reflect measurement of the allowance based on management's estimate of probable incurred credit losses. For more information, see Note 1 – Organization and Significant Accounting Policies.

On March 5, 2021, the United Kingdom's Financial Conduct Authority (UKFCA) formally announced that all London Interbank Offered Rate (LIBOR) tenors will either be discontinued or no longer be representative immediately after December 31, 2021. As a result, the UKFCA has worked closely with market participants and regulatory authorities around the world to ensure that alternatives to LIBOR are available and that existing contracts can be transitioned onto these alternatives to safeguard financial stability and market integrity.

At September 30, 2023, our Association did not hold any legacy LIBOR indexed loans in our core portfolio and these developments did not have a material impact on the Association and our borrowers. We have adopted a transition plan to reduce LIBOR exposures and to stop the inflow of new LIBOR volume. Management has documented and worked through the LIBOR transition plan with our funding bank and service provider to address the phase out of LIBOR rates, including any updates to processes and loan servicing technology. All exposure to LIBOR related to our participations purchased portfolio was converted to other reference rates by September 30, 2023.

#### **CHANGES IN MANAGEMENT**

Our President/CEO, Patrick Zeka, resigned March 31, 2023. The Board of Directors appointed the current Chief Credit Officer, Steve Davenport, to serve as Acting CEO and Chief Credit Officer until May 24<sup>th</sup>, when Bill Davis was hired as President/CEO.

The undersigned certify they have reviewed this report, this report has been prepared in accordance with all applicable statutory or regulatory requirements, and the information contained herein is true, accurate, and complete to the best of his or her knowledge and belief.

//signature on file//	//signature on file//
Rodney Holcomb Chairman of the Audit Committee November 7, 2023	Bill Davis President/CEO November 7, 2023
//signature on file// Malinda Thimmesch CFO November 7, 2023	



# **Consolidated Statement of Condition**

(Dollars in Thousands)					
	Se	September 30		ecember 31	
		2023	2022		
	U	NAUDITED		AUDITED	
ASSETS					
Loans	\$	1,933,687	\$	1,870,507	
Less allowance for loan losses		4,949		3,547	
Net loans		1,928,738		1,866,960	
Cash		2,325		3,290	
Accrued interest receivable		25,938		20,421	
Investment in CoBank, ACB		46,983		46,913	
Investment in AgDirect		4,442		4,087	
Premises and equipment, net		16,561		16,790	
Other property owned		1,087		47	
Prepaid benefit expense		9,884		10,508	
Other assets		11,720		14,620	
Total assets	\$	2,047,678	\$	1,983,636	
Note payable to CoBank, ACB Advance conditional payments Accrued interest payable Patronage distributions payable Accrued benefits liability Deferred tax liability Reserve for unfunded commitments Other liabilities  Total liabilities	\$	1,642,696 11,688 4,886 - 282 136 479 17,639 1,677,806	\$	1,605,622 7,382 3,908 14,000 294 60 447 7,683 1,639,396	
Commitments and Contingencies  SHAREHOLDERS' EQUITY  Capital stock  Additional paid-in capital  Unallocated retained earnings		3,699 55,558 310,615		3,714 55,558 284,968	
Total shareholders' equity		369,872		344,240	
Total liabilities and shareholders' equity	\$	2,047,678	\$	1,983,636	

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



# **Consolidated Statement of Comprehensive Income**

(Dollars in Thousands)

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UNAUDITED	2023	2022	2023	2022
INTEREST INCOME				
Loans	\$27,685	\$21,029	\$81,096	\$56,669
Total interest income	27,685	21,029	81,096	56,669
INTEREST EXPENSE				
Note payable to CoBank, ACB	14,320	8,365	40,905	20,009
Other	87	12	190	33
Total interest expense	14,407	8,377	41,095	20,042
Net interest income	13,278	12,652	40,001	36,627
(Credit loss reversals)/Provision for credit losses	(264)	(512)	1,858	45
Net interest income after credit loss				
reversals/provision for credit losses	13,542	13,164	38,143	36,582
NONINTEREST INCOME				
Financially related services income	10	9	19	17
Loan fees	340	232	998	788
Patronage distribution from Farm Credit institutions	1,901	1,833	5,780	5,593
Mineral income	170	350	692	846
Contingency gain	-	-	1,059	-
Other noninterest income	181	668	384	1,087
Total noninterest income	2,602	3,092	8,932	8,331
NONINTEREST EXPENSE				
Salaries and employee benefits	3,595	3,553	10,748	10,334
Occupancy and equipment	393	389	1,238	1,116
Purchased services from AgVantis, Inc.	1,033	976	3,098	2,929
Farm Credit Insurance Fund premium	704	747	2,152	2,225
Supervisory and examination costs	167	135	502	405
Other noninterest expense	1,185	1,154	4,017	3,433
Total noninterest expense	7,077	6,954	21,755	20,442
Income before income taxes	9,067	9,302	25,320	24,471
Provision for income taxes	2	3	9	9
Net income	9,065	9,299	25,311	24,462
COMPREHENSIVE INCOME				
Amortization of retirement costs	-	40	-	120
Total comprehensive income	\$ 9,065	\$ 9,339	\$ 25,311	\$24,582

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



# **Consolidated Statement of Changes in Shareholders' Equity**

(Dollars in Thousands)

UNAUDITED	apital Stock	Additional Paid-In Capital		F	nallocated Retained Earnings	Comp	mulated other rehensive ne/(Loss)	 Total reholders' Equity
Balance at December 31, 2021	\$ 3,767	\$	55,558	\$	265,382	\$	(163)	\$ 324,544
Comprehensive income					24,462		120	24,582
Stock issued	251							251
Stock retired	(296)							(296)
Patronage distributions:								
Other					9			9
Balance at September 30, 2022	\$ 3,722	\$	55,558	\$	289,853	\$	(43)	\$ 349,090
Balance at December 31, 2022	\$ 3,714	\$	55,558	\$	284,968	\$	-	\$ 344,240
Comprehensive income					25,311		-	25,311
Stock issued	187							187
Stock retired	(202)							(202)
Patronage distributions:								
Other					15			15
Cumulative effect of CECL adoption	 				321			321
Balance at September 30, 2023	\$ 3,699	\$	55,558	\$	310,615	\$	-	\$ 369,872

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



#### **NOTES TO FINANCIAL STATEMENTS**

Dollars in Thousands, Except as Noted (Unaudited)

#### **NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

A description of the organization and operations of Oklahoma AgCredit, ACA (the Association), the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2022, are contained in the 2022 Annual Report to Shareholders. These unaudited third quarter 2023 financial statements should be read in conjunction with the 2022 Annual Report to Shareholders.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2022, as contained in the 2022 Annual Report to Shareholders.

In the opinion of management, the unaudited financial information is complete and reflects all adjustments necessary for a fair statement of results for the interim periods. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2023. Descriptions of the significant accounting policies are included in the 2022 Annual Report to Shareholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the banking industry.

#### **Recently Adopted or Issued Accounting Pronouncements**

The Association adopted the Financial Accounting Standards Board (FASB) updated guidance entitled "Financial Instruments – Credit Losses: Troubled Debt Restructurings and Vintage Disclosure" on January 1, 2023. This guidance requires the creditor to determine whether a modification results in a new loan or a continuation of an existing loan, among other disclosures specific to modifications with borrowers that are experiencing financial difficulties. The update eliminated the accounting guidance for troubled debt restructurings by creditors and requires disclosure of current period gross write-offs by year of origination for financing receivables and net investments in leases on a prospective basis.

The Association also adopted the FASB guidance entitled "Measurement of Credit Losses on Financial Instruments" (CECL) and other subsequently issued accounting standards updates related to credit losses on January 1, 2023. This guidance replaced the current incurred loss impairment methodology with a single allowance framework that estimates the current expected credit losses over the remaining contractual life for all financial assets measured at amortized cost and certain off-balance sheet credit exposures. This guidance is applied on a modified retrospective basis. This framework requires management to consider in its estimate of the allowance for credit losses (ACL) relevant historical events, current conditions, and reasonable and supportable forecasts that consider macroeconomic conditions. The adoption of this guidance did not have a material impact on our financial statements.

The following table presents the impact to the allowance for credit losses and retained earnings upon adoption of this guidance on January 1, 2023.

	Decem	nber 31, 2022	CECL Ad	loption Impact	January 1, 2023		
Assets: Allowance for credit losses on loans Deferred tax assets	\$	3,547 -	\$	(519) -	\$	3,028 -	
Liabilities: Allowance for credit losses on unfunded commitments Deferred tax liabilities	\$	447 60	\$	122 76	\$	569 136	
Retained earnings: Unallocated retained earnings, net of tax	\$	284,968	\$	321	\$	285,289	



In March 2020, the FASB issued guidance entitled "Facilitation of the Effects of Reference Rate Reform on Financial Reporting." The guidance provided optional expedients and exceptions for applying GAAP to contracts and other transactions affected by reference rate reform. The guidance simplifies the accounting evaluation of contract modifications that replace a reference rate affected by reference rate reform and contemporaneous modifications of other contracts related to the replacement of the reference rate. In December 2022, the FASB issued ASU 2022-06, "Reference Rate Reform (Topic 848): Deferral of the Sunset Date of Topic 848". This ASU defers the sunset date of the guidance in Topic 848 on reference rate reform from December 31, 2022 to December 31, 2024. This ASU is effective upon issuance. The adoption of this guidance did not have a material impact on our financial statements.

#### Loans and Allowance for Credit Losses

Loans are generally carried at their principal amount outstanding adjusted for charge-offs, deferred loan fees, or costs. Loan origination fees and direct loan origination costs are netted and capitalized, and the net fee or cost is amortized over the average life of the related loan as an adjustment to interest income. Loan prepayment fees are reported in interest income. Interest on loans is accrued and credited to interest income based on the daily principal amount outstanding.

#### Nonaccrual Loans

Nonaccrual loans are loans for which there is reasonable doubt that all principal and interest will not be collected according to the original contractual terms and are generally considered substandard or doubtful, which is in accordance with the loan rating model, as described below. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is modified or until the entire amount past due, including principal, accrued interest, and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full

Consistent with prior practice, loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately secured and in the process of collection), circumstances indicate that collection of principal and interest is in doubt or legal action, including foreclosure or other forms of collateral conveyance, has been initiated to collect the outstanding principal and interest. At the time a loan is placed in nonaccrual status, accrued interest that is considered uncollectible is reversed (if accrued in the current year) or included in the recorded nonaccrual balance (if accrued in prior years). Loans are charged-off at the time they are determined to be uncollectible.

When loans are in nonaccrual status, interest payments received in cash are generally recognized as interest income if the collectability of the loan principal is fully expected and certain other criteria are met. Otherwise, payments received on nonaccrual loans are applied against the recorded investment in the loan asset. Nonaccrual loans are returned to accrual status if all contractual principal and interest is current, the borrower is fully expected to fulfill the contractual repayments terms, and after remaining current as to principal and interest for a sustained period or have a recent repayment pattern demonstrating future repayment capacity to make on-time payments. If previously unrecognized interest income exists at the time the loan is transferred to accrual status, cash received at the time of or subsequent to the transfer should first be recorded as interest income until such time as the recorded balance equals the contractual indebtedness of the borrower.

#### Accrued Interest Receivable

The Association elected to continue classifying accrued interest on loans in accrued interest receivable and not as part of loans on the Consolidated Statement of Condition. The Association also elected not to estimate an allowance on interest receivable balances because the nonaccrual policies in place provide for the accrual of interest to cease on a timely basis when all contractual amounts are not expected.

#### Loan Modifications to Borrowers Experiencing Financial Difficulty

Loan modifications may be granted to borrowers experiencing financial difficulty. Modifications can be in the form of principal forgiveness, interest rate reduction, forbearance, other-than-insignificant payment delay, a term extension, or a combination thereof. Covenant waivers and modifications of contingent acceleration clauses are not considered term extensions.

#### Collateral-Dependent Loans

Collateral-dependent loans are loans secured by collateral, including but not limited to agricultural real estate, crop inventory, equipment, and livestock. CECL requires an Association to measure the expected credit losses based on fair value of the collateral at the reporting date when the Association determines that foreclosure is probable. Additionally, CECL allows a fair value practical expedient as a measurement approach for loans when the repayment is expected to be provided substantially through the operation or sale of the collateral when the borrower is experiencing financial difficulties. Under the practical expedient measurement approach, the expected credit losses is



based on the difference between the fair value of the collateral less estimated costs to sell and the amortized cost basis of the loan.

#### Allowance for Credit Losses

Effective January 1, 2023, the ACL represents the estimated current expected credit losses over the remaining contractual life of the loans measured at amortized cost and certain off-balance sheet credit exposures. The ACL takes into consideration relevant information about past events, current conditions, and reasonable and supportable macroeconomic forecasts of future conditions. The contractual term excludes expected extensions, renewals, and modifications, unless the extension or renewal options are not unconditionally cancellable. The ACL comprises:

- the allowance for credit losses on loans (ACLL) and
- the allowance for credit losses on unfunded commitments, which is presented as a liability on the Consolidated Statement of Condition.

Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio, considering macroeconomic conditions, forecasts, and other factors prevailing at the time, may result in significant changes in the ACL in those future periods.

#### Methodology for Allowance for Credit Losses on Loans

The ACLL represents management's estimate of credit losses over the remaining expected life of loans. Loans are evaluated on the amortized cost basis, including premiums, discounts, and fair value adjustments.

The Association employs a disciplined process and methodology to establish its ACLL that has two basic components: first, an asset-specific component involving individual loans that do not share risk characteristics with other loans and the measurement of expected credit losses for such individual loans; and second, a pooled component for estimated expected credit losses for pools of loans that share similar risk characteristics.

Asset-specific loans are generally collateral-dependent loans (including those loans for which foreclosure is probable) and nonaccrual loans. For an asset-specific loan, expected credit losses are measured as the difference between the amortized cost basis in the loan and the present value of expected future cash flows discounted at the loan's effective interest rate except that, for collateral-dependent loans, credit loss is measured as the difference between the amortized cost basis in the loan and the fair value of the underlying collateral. The fair value of the collateral is adjusted for the estimated cost to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral. In accordance with the Association's appraisal policy, the fair value of collateral-dependent loans is based upon independent third-party appraisals or on collateral valuations prepared by in-house appraisers. When an updated appraisal or collateral valuation is received, management reassesses the need for adjustments to the loan's expected credit loss measurements and, where appropriate, records an adjustment. If the calculated expected credit loss is determined to be permanent, fixed, or non-recoverable, the credit loss portion of the loan will be charged off against the allowance for credit losses.

In estimating the pooled component of the ACLL for loan pools that share common risk characteristics, loans are evaluated collectively and segregated into loan pools considering the risk associated with the specific pool. Relevant risk characteristics include loan type, commodity, and credit quality rating at origination. The allowance is determined based on a quantitative calculation of the expected life-of-loan loss percentage for each loan category by considering the probability of default and the severity of loss given default. The probability of default for each pool is based on the migration of loans from a performing state to a default state within that pool. Loss given default is determined for each pool based on the aggregate net lifetime losses incurred within that pool. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the loan is 90 days or more past due. For those pools with a limited loss history, the Association supplemented its own historical loss information with that of its peer institutions.

The pooled component of the ACLL also considers factors for each loan pool to adjust for differences between the historical period used to calculate historical default and loss severity rates and expected conditions over the remaining lives of the loans in the portfolio related to:

- lending policies and procedures,
- national, regional, and local economic business conditions, and developments that affect the collectability of the portfolio, including the condition of various markets,
- the nature of the loan portfolio, including the terms of the loans,
- the experience, ability, and depth of the lending management and other relevant staff,
- the volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans
- the quality of the loan review and process,



- the value of underlying collateral for collateral-dependent loans,
- the existence and effect of any concentrations of credit and changes in the level of such concentrations, and.
- the effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

The Association uses a single economic scenario over a reasonable and supportable forecast period of 12 months. Subsequent to the forecast period, the Association reverts to long run historical loss experience beyond the 12-month forecast period on a quarterly PD/LGD transition matrix model to inform the estimate of losses for the remaining contractual life of the loan portfolio.

The economic forecasts incorporate macroeconomic variables, including unemployment rates, real gross domestic product (GDP) levels, real consumer spending, government spending as a percentage of GDP, United States exports, inflation, and the federal funds rate, as well as agricultural commodity prices.

In addition to the quantitative calculation, the Association considers the imprecision inherent in the process and methodology, emerging risk assessments, and other subjective factors, which may lead to a management adjustment to the modeled ACLL results. Expected credit loss estimates also include consideration of expected cash recoveries on loans previously charged-off or expected recoveries on collateral-dependent loans where recovery is expected through sale of the collateral. The economic forecasts are updated on a quarterly basis.

Prior to January 1, 2023, the allowance for loan losses was maintained at a level considered adequate to provide for probable losses existing in and inherent in the loan portfolio. The allowance was based on a periodic evaluation of the loan portfolio in which numerous factors are considered, including economic conditions, collateral values, borrowers' financial conditions, loan portfolio composition, and prior loan loss experience. The allowance for loan losses encompassed various judgments, evaluations, and appraisals with respect to the loans and their underlying collateral that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity would cause these various judgments, evaluations, and appraisals to change over time. Management considered a number of factors in determining and supporting the levels of the allowances for loan losses, which include, but are not limited to, the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects, and weather-related influences.

### Allowance for Credit Losses on Unfunded Commitments

The Association evaluates the need for an allowance for credit losses on unfunded commitments under CECL and, if required, an amount is recognized and presented as a liability on the Consolidated Statement of Condition. The amount of expected losses is determined by calculating a commitment usage factor over the contractual period for exposures that are not unconditionally cancellable by the Association and applying the loss factors used in the ACLL methodology to the results of the usage calculation. No allowance for credit losses is recorded for commitments that are unconditionally cancellable.

#### NOTE 2 - LOANS AND ALLOWANCE FOR CREDIT LOSSES

A summary of loans follows.

	September 30, 2023	December 31, 2022
Real estate mortgage	\$ 1,269,246	\$ 1,276,319
Production and intermediate-term	254,012	241,585
Agribusiness	223,167	216,686
Rural infrastructure	168,709	126,759
International	18,126	8,724
Rural residential real estate	427	434
Total Loans	\$ 1,933,687	\$ 1,870,507



The Association purchases and sells participation interests with other parties in order to diversify risk, manage loan volume, and comply with Farm Credit Administration regulations. The following table presents information regarding the balances of participations purchased and sold at September 30, 2023:

	Other Farm Credit Institutions				
	Р	Sold			
Real estate mortgage	\$	40,048	\$	46,901	
Production and intermediate-term		56,577		5,578	
Agribusiness		220,609		-	
Rural infrastructure		168,709		-	
International		18,126		-	
Total	\$	504,069	\$	52,479	

#### **Credit Quality**

Credit risk arises from the potential inability of an obligor to meet its payment obligation and exists in our outstanding loans, letters of credit, and unfunded loan commitments. The Association manages credit risk associated with the retail lending activities through an analysis of the credit risk profile of an individual borrower using its own set of underwriting standards and lending policies, approved by its board of directors, which provides direction to its loan officers. The retail credit risk management process begins with an analysis of the borrower's credit history, repayment capacity, financial position, and collateral, which includes an analysis of credit scores for smaller loans. Repayment capacity focuses on the borrower's ability to repay the loan based on cash flows from operations or other sources of income, including off-farm income. Real estate mortgage loans must be secured by first liens on the real estate (collateral). As required by Farm Credit Administration regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures. Real estate mortgage loans may be made only in amounts up to 85% of the original appraised value of the property taken as security or up to 97% of the appraised value if guaranteed by a state, federal, or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Loans other than real estate mortgage may be made on a secured or unsecured basis.

The Association uses a two-dimensional risk rating model based on an internally generated combined System risk rating guidance that incorporates a 14-point probability of default rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default. Probability of default is the probability that a borrower will experience a default during the life of the loan. The loss given default is management's estimate as to the anticipated principal loss on a specific loan assuming default occurs during the remaining life of the loan. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the loan is 90 days or more past due. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths, weaknesses, and risks in a particular relationship. The Association reviews, at least on an annual basis, or when a credit action is taken, the probability of default category.

Each of the probability of default categories carries a distinct percentage of default probability. The probability of default rate between one and nine of the acceptable categories is very narrow and would reflect almost no default to a minimal default percentage. The probability of default rate grows more rapidly as a loan moves from acceptable to other assets especially mentioned and grows significantly as a loan moves to a substandard (viable) level. A substandard (non-viable) rating indicates that the probability of default is almost certain. These categories are defined as follows:

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



The following table shows loans under the Farm Credit Administration Uniform Loan Classification System as a percentage of total loans by loan type as of:

	September 30, 2023	December 31, 2022 <sup>1</sup>
Real estate mortgage		
Acceptable	98.48%	98.27%
OAEM	0.68%	0.94%
Substandard	0.84%	0.79%
Total	100.00%	100.00%
Production and intermediate-term		
Acceptable	97.82%	97.65%
OAEM	0.57%	0.74%
Substandard	1.61%	1.61%
Total	100.00%	100.00%
Agribusiness		
Acceptable	97.52%	95.94%
OAEM	1.21%	2.28%
Substandard	1.27%	1.78%
Total	100.00%	100.00%
Rural infrastructure		
Acceptable	95.07%	99.11%
OAEM	4.93%	0.59%
Substandard	-	0.30%
Total	100.00%	100.00%
Rural residential real estate		
Acceptable	100.00%	100.00%
Total	100.00%	100.00%
International		
Acceptable	100.00%	100.00%
Total	100.00%	100.00%
Total Loans		
Acceptable	98.00%	97.99%
OAEM	1.09%	1.04%
Substandard	0.91%	0.97%
Total	100.00%	100.00%

<sup>&</sup>lt;sup>1</sup> Prior to the adoption of CECL on January 1, 2023, loans were presented with accrued interest receivable.

Accrued interest receivable on all accruing loans at September 30, 2023 has been excluded from the amortized cost of loans and reported separately in the Consolidated Statement of Condition.



Nonperforming assets consist of nonaccrual loans, accruing loans 90 days or more past due, and other property owned. The following table shows these nonperforming assets and related credit quality statistics as follows:

	Septem	ber 30, 2023	Decem	ber 31, 2022
Nonaccrual loans Real estate mortgage Production and intermediate-term Agribusiness	\$	8,941 3,927 2,829	\$	5,139 750 3,875
Total nonaccrual loans	\$	15,697	\$	9,764
Accruing restructured loans Real estate mortgage Production and intermediate-term			\$	311 1
Total accruing restructured loans			\$	312
Accruing loans 90 days past due Real estate mortgage	\$	400	\$	-
Total accruing loans 90 days past due	\$	400	\$	-
Total nonperforming loans Other property owned	\$	16,097 1,087	\$	10,076 47
Total nonperforming assets <sup>1</sup>	\$	17,184	\$	10,123
Nonaccrual loans to total loans  Nonperforming assets <sup>1</sup> to total loans and other property owned  Nonperforming assets <sup>1</sup> to total shareholders' equity		0.81% 0.89% 4.65%		0.52% 0.54% 2.94%

<sup>&</sup>lt;sup>1</sup> Prior to the adoption of CECL on January 1, 2023, nonperforming assets included accruing restructured loans.

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

	September 30, 2023									
	Amortized Cost	Amortized Cost								
	with Allowance	without Allowance	Total							
Nonaccrual loans:										
Real estate mortgage	\$ 2,118	\$ 6,823	\$ 8,941							
Production and intermediate-term	3,311	616	3,927							
Agribusiness	2,829	-	2,829							
Total	\$ 8,258	\$ 7,439	\$ 15,697							

	Interest Income Recognized								
	For the Th	ree Months	For the N	line Months					
	Ended Septe	mber 30, 2023	Ended September 30, 20						
Nonaccrual loans:									
Real estate mortgage	\$	-	\$	128					
Production and intermediate-term		-		91					
Agribusiness		-		16					
Total	\$	-	\$	235					



The following tables provide an age analysis of past due loans at amortized cost.

September 30, 2023	30-89 Da Past Du	,	90 Days or More Past Due	То	otal Past Due	lot Past Due or less than 30 Days Past Due	To	otal Loans	I	Recorded nvestment Accruing Loans 90 Days or More Past Due
Real estate mortgage		2,460	\$ 738	\$	3,198	\$ 1,266,048	\$	1,269,246	\$	400
Production and intermediate-term	2	2,414	236		2,650	251,362		254,012		-
Agribusiness		-	2,829		2,829	220,338		223,167		-
Rural infrastructure		-	-		-	168,709		168,709		-
International		-	-		-	18,126		18,126		-
Rural residential real estate		-	-		-	427		427		-
Total	\$ 4	,874	\$ 3,803	\$	8,677	\$ 1,925,010	\$	1,933,687	\$	400

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

December 31, 2022	30-89 Day Past Due		90 Days or More Past Due	To	otal Past Due	Not Past Due or less than 30 Days Past Due		T	otal Loans	I	Recorded nvestment Accruing Loans 90 Days or More Past Due
Real estate mortgage	\$ 2,2	79	\$ 296	\$	2,575	\$	1,288,416	\$	1,290,991	\$	-
Production and intermediate-term	5,3	19	416		5,735		240,344		246,079		-
Agribusiness		-	126		126		217,466		217,592		-
Rural infrastructure		-	-		-		127,067		127,067		-
Rural residential real estate		-	-		-		436		436		-
International		-	-		-		8,763		8,763		-
Total	\$ 7,5	98	\$ 838	\$	8,436	\$	1,882,492	\$	1,890,928	\$	-

#### **Allowance for Credit Losses**

The credit risk rating methodology is a key component of the Association's allowance for credit losses evaluation and is generally incorporated into the Association's loan underwriting standards and internal lending limits. In addition, borrower and commodity concentration lending and leasing limits have been established by the Association to manage credit exposure. The regulatory limit to a single borrower or lessee is 15% of an institution's lending and leasing limit base. This limit applies to Associations with long-term and short- and intermediate-term lending authorities.

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

	lance at 30, 2023	Cha	rge-offs	Re	coveries	Loar (Lo	vision for n Losses/ an Loss versals)	lance at ber 30, 2023
Real estate mortgage	\$ 1,155	\$	-	\$	-	\$	(47)	\$ 1,108
Production and intermediate-term	1,264		-		-		300	1,564
Agribusiness	1,746		62		67		(447)	1,304
Rural infrastructure	1,033		-		-		(60)	973
Total	\$ 5,198	\$	62	\$	67	\$	(254)	\$ 4,949



	Dece	ance at ember 31, 2022	of	nulative Effect CECL loption	Jar	lance at nuary 1, 2023	Charg	e-offs	Reco	veries	ision for Losses	Sept	lance at ember 30, 2023
Real estate mortgage	\$	1,058	\$	(148)	\$	910	\$	-	\$	-	\$ 198	\$	1,108
Production and intermediate-term		552		(177)		375		32		-	1,221		1,564
Agribusiness		1,655		(445)		1,210		62		67	89		1,304
Rural infrastructure		279		254		533		-		-	440		973
International		3		(3)		-		-		-	-		-
Total	\$	3,547	\$	(519)	\$	3,028	\$	94	\$	67	\$ 1,948	\$	4,949

	lance at 30, 2022	Char	ge-offs	Reco	veries	Provision for Loan Losses/ (Loan Loss Reversals)		Septe	ance at mber 30, 2022
Real estate mortgage	\$ 838	\$	-	\$	-	\$	(15)	\$	823
Production and intermediate-term	576		11		-		(74)		491
Agribusiness	2,502		-		-		(345)		2,157
Rural infrastructure	179		-		-		30		209
International	4		-		-		(1)		3
Total	\$ 4,099	\$	11	\$	-	\$	(405)	\$	3,683

	Dece	ance at ember 31, 2021	Char	ge-offs	Recoveries		Provision for Loan Losses/ (Loan Loss Reversals)		Septe	ance at ember 30, 2022
Real estate mortgage	\$	888	\$	-	\$	-	\$	(65)	\$	823
Production and intermediate-term		631		62		106		(184)		491
Agribusiness		1,924		-		-		233		2,157
Rural infrastructure		159		-		-		50		209
Rural residential real estate		1		-		-		(1)		-
International		3		-		-		-		3
Total	\$	3,606	\$	62	\$	106	\$	33	\$	3,683

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

The Association maintains a separate reserve for unfunded commitments, which is included in Liabilities on the Association's Consolidated Statement of Condition. The related provision for the reserve for unfunded commitments is included as part of the provision for credit losses on the Consolidated Statement of Comprehensive Income, along with the provision for loan losses.

A summary of changes in the reserve for unfunded commitments follows:

	For the Three Months Ended September 30, 2023	For the Nine Months Ended September 30, 2023
Beginning Balance	\$ 489	\$ 447
Cumulative Effect of CECL Adoption		122
Balance at January 1, 2023		569
Reversal of reserve for unfunded commitments	(10)	(90)
Total	\$ 479	\$ 479



	For the Three Months Ended September 30, 2022	For the Nine Months Ended September 30, 2022
Beginning Balance	\$ 658	\$ 539
(Reversal of)/Provision for reserve for unfunded commitments	(107)	12
Total	\$ 551	\$ 551

#### **Loan Modifications to Borrowers Experiencing Financial Difficulties**

Loan modifications may be granted to borrowers experiencing financial difficulty. Such modifications may take the form of forgiveness of principal, an interest rate reduction, forbearance, an other-than-insignificant payment delay, a term extension, or a combination thereof. Covenant waivers and modifications of contingent acceleration clauses are not considered term extensions. Other-than-insignificant payment deferrals may provide the borrower with a temporary payment extension and are defined as a cumulative or individual forbearance or a payment delay greater than or equal to 6 months. These deferred payments may be capitalized into the principal balance of the loan and amortized with no extension of maturity or with the deferred payment due at the time of original maturity.

With the adoption of the FASB guidance on loan modifications, the Association no longer classifies loan modifications to a borrower experiencing financial difficulty as a troubled debt restructure. See Note 1 "Organization and Significant Accounting Policies" for further detail. The Association had no loan modifications to borrowers experiencing financial difficulties as of September 30, 2023.

The Association had no loans held for sale at September 30, 2023 or at December 31, 2022.

#### **Troubled Debt Restructuring**

Prior to January 1, 2023, the adoption of updated FASB guidance on loan modifications, a restructuring of a loan constituted a troubled debt restructuring, also known as formally restructured, if the creditor for economic or legal reasons related to the borrower's financial difficulties granted a concession to the borrower that it would not otherwise consider. Concessions varied by program and were borrower-specific and could include interest rate reductions, term extensions, payment deferrals, or the acceptance of additional collateral in lieu of payments. In limited circumstances, principal may have been forgiven. When a restructured loan constituted a troubled debt restructuring, these loans were included within our impaired loans under nonaccrual or accruing restructured loans.

There were no loans modified as part of a troubled debt restructuring during the nine-month period ended September 30, 2022. Of loans modified as troubled debt restructurings within the twelve months ended September 30, 2022, none defaulted during the nine-month period ended September 30, 2022. There were no additional commitments to lend to borrowers whose loans were modified in a troubled debt restructuring at December 31, 2022.

The following table provides information on outstanding loans restructured in troubled debt restructurings:

	Loans modified as TDRs December 31, 2022	TDRs in Nonaccrual Status* December 31, 2022
Real estate mortgage	\$ 2,007	\$ 1,696
Production and intermediate-term	14	13
Total	\$ 2,021	\$ 1,709

<sup>\*</sup> Represents the portion of loans modified as troubled debt restructurings that were in nonaccrual status.

#### **NOTE 3 - CAPITAL**

Retained earnings for the nine months ended September 30, 2023 reflects an increase from the cumulative effect of a change in accounting principle for CECL on January 1, 2023. The impact of adoption was not material to the Association's capital ratios.



A summary of select capital ratios based on a three-month average and minimums set by the Farm Credit Administration follows.

	As of September 30, 2023	As of December 31, 2022	Regulatory Minimums	Capital Conservation Buffer	Total
Risk Adjusted: Common equity tier 1 ratio Tier 1 capital ratio Total capital ratio Permanent capital ratio	15.19% 15.19% 15.47% 15.23%	14.87% 14.87% 15.08% 14.90%	4.5% 6.0% 8.0% 7.0%	2.5% 2.5% 2.5% -	7.0% 8.5% 10.5% 7.0%
Non-risk-adjusted: Tier 1 leverage ratio Unallocated retained earnings and equivalents leverage ratio	15.92% 15.73%	15.64% 15.44%	4.0% 1.5%	1.0% -	5.0% 1.5%

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

The following tables present the activity in the accumulated other comprehensive loss, net of tax by component:

		r the Thi					ne Months otember 30	
	<b>2023</b> 2022 <b>2023</b>			2023		2022		
Pension and other benefit plans:								
Beginning balance Amounts reclassified from accumulated other	\$	-	\$	(83)	\$	-	\$	(163)
comprehensive loss		-		40		-		120
Net current period other comprehensive income				40		•		120
Ending balance	\$	-	\$	(43)	\$	-	\$	(43)

The Association's participation in the non-qualified defined benefit Pension Restoration Plan terminated after December 31, 2022.

The following table represents reclassifications out of accumulated other comprehensive loss.

		nt Reclassified Other Compre			Location of Gain/Loss
	For the Three Months Ended September 30				Recognized in
	<b>2023</b> 2022				Statement of Income
Pension and other benefit plans:					Salaries and employee
Net actuarial loss	\$	-	\$	40	benefits
Total reclassifications	\$	-	\$	40	

		Reclassified	Location of Gain/Loss		
	For the Nine Months Ended September 30				Recognized in
	20	23	2	022	Statement of Income
Pension and other benefit plans:					Salaries and employee
Net actuarial loss	\$	-	\$	120	benefits
Total reclassifications	\$	-	\$	120	



#### **NOTE 4 - FAIR VALUE MEASUREMENTS**

Accounting guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 2 of the 2022 Annual Report to Shareholders for a more complete description.

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

		Fair V	Total Fair Value				
	Level 1 Level 2				Level 3		
Assets held in nonqualified benefits trusts							
September 30, 2023	\$	3,442	\$ -	\$	-	\$	3,442
December 31, 2022	\$	432	\$ -	\$	-	\$	432

The Association had no liabilities measured at fair value on a recurring basis at September 30, 2023 or December 31, 2022.

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

		Total Fair					
	Level 1		Level 2		Level 3	Value	
September 30, 2023 Loans Other property owned	\$	-	\$	-	\$ 5,726 1,197	\$ 5,726 1,197	
December 31, 2022 Loans Other property owned	\$	- -	\$	- -	\$ 2,956 56	\$ 2,956 56	

With regard to impaired loans and other property owned, it is not practicable to provide specific information on inputs as each collateral property is unique. The Association utilizes appraisals or other market-based information to value these loans and other property owned and takes into account unobservable inputs such as income and expense, comparable sales, replacement cost, and comparability adjustments.

The Association had no liabilities measured at fair value on a non-recurring basis at September 30, 2023 or December 31, 2022.

#### **Valuation Techniques**

As more fully discussed in Note 2 of the 2022 Annual Report to Shareholders, accounting guidance establishes a fair value hierarchy, which requires an Association to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following presents a brief summary of the valuation techniques used by the Association for assets and liabilities, subject to fair value measurement.

### Assets Held in Non-Qualified Benefits Trusts

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

#### Loans Evaluated for Impairment

For impaired loans measured on a non-recurring basis, the fair value is based upon the underlying collateral since the loans are collateral-dependent loans. The fair value measurement process uses independent appraisals and other market-based information, but in many cases, it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral, and other matters. As a result, these loans have fair value measurements that fall within Level 3 of the fair value hierarchy. When the value of the collateral, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established.

#### Other Property Owned

Other property owned measured on a non-recurring basis is generally classified as Level 3 of the fair value hierarchy. The process for measuring the fair value of other property owned involves the use of appraisals or other market-based information. Costs to sell represent transaction costs and are not included as a component of the asset's fair value.



## **NOTE 5 - SUBSEQUENT EVENTS**

The Association has evaluated subsequent events through November 7, 2023, which is the date the financial statements were issued, and no material subsequent events were identified.