Central Kentucky Agricultural Credit Association

FIRST QUARTER 2019

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CERTIFICATION

The undersigned certify that we have reviewed the March 31, 2019 quarterly report of Central Kentucky Agricultural Credit Association, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.

James W. Caldwell
Chief Executive Officer

Marcus G. Barnett
Chief Financial Officer

James A. Lyons
Chairman of the Board

May 9, 2019

Central Kentucky Agricultural Credit Association

Report on Internal Control Over Financial Reporting

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

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

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

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

James W. Caldwell

James W. Caldwell
Chief Executive Officer

Marcus G. Barnett
Chief Financial Officer

May 9, 2019

Central Kentucky Agricultural Credit Association

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

(dollars in thousands)

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

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities in our region. The predominate enterprises are beef cattle and thoroughbred horses. Overall, the outlook for the beef cattle industry has continued to be stable. There are some unknowns for the near future depending on the results of recent weather events, particularly in the Midwest. However, the effects of these events are still to be determined. The thoroughbred horse industry continues to show improvement based on recent sales. The outlook is very positive, mirroring the general economic outlook. Row crops continue to be a concern in Central Kentucky. The wet summer and fall took a toll on some crops, causing considerable damage to them as a whole. This is on top of already low commodity prices that were negatively affected by tariffs. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm employment in the area, significantly reduces the level of dependency on a given commodity.

The gross loan volume of the Association as of March 31, 2019 was $508,527, a decrease of $4,518 as compared to $513,045 at December 31, 2018. Net loans outstanding at March 31, 2019 were $504,250 as compared to $508,768 at December 31, 2018. Net loans accounted for 96.29 percent of total assets at March 31, 2019, as compared to 94.95 percent of total assets at December 31, 2018.

The decrease in gross and net loan volume during the reporting period is primarily due to seasonal paydowns on operating loans.

There is an inherent risk in the extension of any type of credit. However, portfolio credit quality continues to be maintained at an acceptable level and credit administration remains satisfactory. Nonaccrual loans increased from $2,967 at December 31, 2018, to $4,273 at March 31, 2019. This increase is primarily due to placing one larger credit into nonaccrual status.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The $4,277 allowance for loan losses at March 31, 2019 reflected a $0 increase from December 31, 2018, and was considered by management to be adequate to cover possible losses.

RESULTS OF OPERATIONS

For the three months ended March 31, 2019

Net income for the three months ended March 31, 2019 totaled $2,399, as compared to $2,504 for the same period in 2018. Net interest income increased $206 for the three months ended March 31, 2019 as compared to the same period in 2018. The Association recorded no provision for loan losses for the three months ended March 31, 2019, and no provision for loan losses for the same period in 2018.

At March 31, 2019, interest income on accruing loans increased $852 compared to March 31, 2018. The Association recorded nonaccrual income of $1 for the three months ended March 31, 2019, as compared to $1 for the same period in 2018. Interest expense increased $646 for the three months ended March 31, 2019 as compared to the comparable period of 2018. Movement in interest income and expense is primarily attributed to an increase in loan volume, a decrease in average interest rate margins, and an early-year reduction in the Association's direct note from receipt of patronage from the AgFirst Farm Credit Bank (Bank). Noninterest income for the three months ended March 31, 2019 totaled $1,111 as compared to $1,428 for the same period of 2018, a decrease of $317. The primary factor in the decrease in Noninterest income was a decreased refund from the Farm Credit System Insurance Corporation (FCSIC).

Noninterest expense for the three months ended March 31, 2019 decreased $6 compared to the same period of 2018. The decrease is due primarily to decreased loan guarantee fees.

The Association recorded a provision for income taxes of $2 for the three months ended March 31, 2019, as compared to a provision for income taxes of $2 for the same period in 2018.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at March 31, 2019 was $425,923 as compared to $441,115 at December 31, 2018. The decrease during the period is primarily attributed to a decrease in loan volume and by receipt of patronage from the Bank.

CAPITAL RESOURCES

Total members' equity at March 31, 2019 increased to $90,083 from the December 31, 2018 total of $87,726. The increase is primarily attributed to the Association's increase in retained earnings as a result of income recorded for the three months ended March 31, 2019. Total capital stock and participation certificates were $4,186 on March 31, 2019, compared to $4,225 on December 31, 2018. This decrease is attributed to a decrease in loan volume.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum levels of several regulatory capital and leverage ratios. Effective January 1, 2017, the regulatory capital requirements for System Banks and Associations were modified. The new regulations ensure that the System's capital requirements are comparable to the Basel III framework and the standardized approach that the federal banking regulatory agencies have adopted. New regulations replaced total surplus and core surplus ratios with common equity tier 1 (CET1), tier 1 capital, and total capital risk-based capital ratios, as well as a tier 1 leverage ratio and an unallocated retained earnings equivalents (UREE) leverage ratio. The permanent capital ratio remains in effect. The capital ratios are calculated by dividing various levels of capital by a risk-adjusted asset base. Risk-adjusted assets have been defined by FCA regulations as balance sheet assets and off-balance sheet commitments adjusted by various percentages, depending on the level of risk inherent in the various types of assets. Calculation of permanent capital ratio risk-adjusted assets includes the allowance for loan losses as a deduction from risk-adjusted assets. This differs from the other risk-based capital calculations. The leverage ratios are calculated by dividing various types of capital by total regulatory assets (not risk-adjusted).

As of March 31, 2019, the Association's CET1 capital ratio and Tier 1 capital ratio were 17.99 percent, the Total capital ratio was 18.94 percent, the Permanent capital ratio was 18.24 percent, The Tier 1 leverage ratio was 15.87 percent, and the UREE leverage ratio was 15.51 percent. The Association exceeded the minimum regulatory standard for all of the ratios.

REGULATORY MATTERS

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

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

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

The following Accounting Standards Update (ASU) was issued by the Financial Accounting Standards Board (FASB) but has not yet been adopted:

Summary of Guidance	Adoption and Potential Financial Statement Impact
ASU 2016-13 – Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments	
• Replaces multiple existing impairment standards by establishing a single framework for financial assets to reflect management's estimate of current expected credit losses (CECL) over the complete remaining life of the financial assets. • Changes the present incurred loss impairment guidance for loans to a CECL model. • The Update also modifies the other-than-temporary impairment model for debt securities to require an allowance for credit impairment instead of a direct write-down, which allows for reversal of credit impairments in future periods based on improvements in credit. • Eliminates existing guidance for purchased credit impaired (PCI) loans, and requires recognition of an allowance for expected credit losses on these financial assets. • Requires a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption. • Effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early application will be permitted for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018.	• Implementation efforts have begun by establishing a cross-discipline governance structure. The implementation includes identification of key interpretive issues, scoping of financial instruments, and assessing existing credit loss forecasting models and processes against the new guidance. • The new guidance is expected to result in an increase in allowance for credit losses due to several factors, including: 1. The allowance related to loans and commitments will most likely increase to cover credit losses over the full remaining expected life of the portfolio, and will consider expected future changes in macroeconomic conditions, 2. An allowance will be established for estimated credit losses on any debt securities, 3. The nonaccretable difference on any PCI loans will be recognized as an allowance, offset by an increase in the carrying value of the related loans. • The extent of the increase is under evaluation, but will depend upon the nature and characteristics of the financial instrument portfolios, and the macroeconomic conditions and forecasts at the adoption date. • The guidance is expected to be adopted in first quarter 2021.

NOTE: Shareholder investment in the Association is materially affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and unaudited quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 2764, or by writing Matthew Miller, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, *www.agfirst.com.* Copies of the Association's annual and unaudited quarterly reports are also available upon request free of charge by calling 1-859-253-3249, or writing Marcus Barnett, Chief Financial Officer, Central Kentucky Agricultural Credit Association, P.O. Box 1290, Lexington, KY 40588-1290, or accessing the website *www.agcreditonline.com.* The Association prepares an unaudited quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

Central Kentucky Agricultural Credit Association

Consolidated Balance Sheets

(dollars in thousands)	March 31, 2019	December 31, 2018
	(unaudited)	*(audited)*
Assets		
Cash	**$ 1,225**	$ 3,046
Loans	**508,527**	513,045
Allowance for loan losses	**(4,277)**	(4,277)
Net loans	**504,250**	508,768
Accrued interest receivable	**7,106**	7,155
Equity investments in other Farm Credit institutions	**7,124**	7,099
Premises and equipment, net	**2,971**	2,927
Accounts receivable	**989**	6,815
Other assets	**33**	27
Total assets	**$ 523,698**	$ 535,837
Liabilities		
Notes payable to AgFirst Farm Credit Bank	**$ 425,923**	$ 441,115
Lease obligations	**47**	—
Accrued interest payable	**1,230**	1,259
Patronage refunds payable	**324**	4,141
Accounts payable	**348**	652
Other liabilities	**5,743**	944
Total liabilities	**433,615**	448,111
Commitments and contingencies (Note 7)		
Members' Equity		
Capital stock and participation certificates	**4,186**	4,225
Retained earnings		
Allocated	**61,257**	61,064
Unallocated	**24,640**	22,437
Total members' equity	**90,083**	87,726
Total liabilities and members' equity	**$ 523,698**	$ 535,837

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

Central Kentucky Agricultural Credit Association

Consolidated Statements of Comprehensive Income

(unaudited)

(dollars in thousands)	For the three months ended March 31, 2019	2018
Interest Income		
Loans	**$ 6,814**	$ 5,962
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	**3,584**	2,938
Net interest income	**3,230**	3,024
Provision for loan losses	**—**	—
Net interest income after provision for loan losses	**3,230**	3,024
Noninterest Income		
Loan fees	**142**	178
Lease income	**12**	8
Patronage refunds from other Farm Credit institutions	**862**	780
Gains (losses) on sales of rural home loans, net	**(5)**	2
Insurance Fund refunds	**99**	460
Other noninterest income	**1**	—
Total noninterest income	**1,111**	1,428
Noninterest Expense		
Salaries and employee benefits	**1,363**	1,368
Occupancy and equipment	**89**	72
Insurance Fund premiums	**81**	75
(Gains) losses on other property owned, net	**—**	(1)
Other operating expenses	**407**	432
Total noninterest expense	**1,940**	1,946
Income before income taxes	**2,401**	2,506
Provision for income taxes	**2**	2
Net income	**2,399**	2,504
Other comprehensive income	**—**	—
Comprehensive income	**$ 2,399**	$ 2,504

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

Central Kentucky Agricultural Credit Association

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)	Capital Stock and Participation Certificates	Retained Earnings: Allocated	Retained Earnings: Unallocated	Total Members' Equity
Balance at December 31, 2017	$ 4,698	$ 54,453	$ 20,884	$ 80,035
Comprehensive income			2,504	2,504
Capital stock/participation certificates issued/(retired), net	8			8
Patronage distribution adjustment		20	(25)	(5)
Balance at March 31, 2018	$ 4,706	$ 54,473	$ 23,363	$ 82,542
Balance at December 31, 2018	**$ 4,225**	**$ 61,064**	**$ 22,437**	**$ 87,726**
Comprehensive income			**2,399**	**2,399**
Capital stock/participation certificates issued/(retired), net	**(39)**			**(39)**
Patronage distribution adjustment		**193**	**(196)**	**(3)**
Balance at March 31, 2019	**$ 4,186**	**$ 61,257**	**$ 24,640**	**$ 90,083**

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

Central Kentucky Agricultural Credit Association

Notes to the Consolidated Financial Statements

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

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

Organization

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

Basis of Presentation

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

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

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

Significant Accounting Policies

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

Management has made significant estimates in several areas, including loans and allowance for loan losses (Note 2, *Loans and Allowance for Loan Losses*), investment securities and other-than-temporary impairment (Note 3, *Investments*), and financial instruments (Note 5, *Fair Value Measurement*). Actual results could differ from those estimates.

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

Accounting Standards Updates (ASUs) Issued During the Period

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

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

ASUs Pending Effective Date

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

Potential effects of ASUs issued in previous periods:

- In August 2018, the FASB issued ASU 2018-15 Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract. The amendments align the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by the amendments in this Update. The guidance is effective for public business entities for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted, including adoption in any interim period, for all entities. The amendments should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

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

- In June 2016, the FASB issued ASU 2016-13 Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. This Update, and subsequent clarifying guidance issued, is intended to improve financial reporting by requiring timelier recording of credit losses on financial instruments. It requires an organization to measure all expected credit losses for financial assets held at the reporting date. Financial institutions and other organizations will use forward-looking information to estimate their credit losses. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public companies that are not SEC filers, it will take effect for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 31, 2018. Evaluation of any possible effects the guidance may have on the statements of financial condition and results of operations is in progress.

Accounting Standards Effective During the Period

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

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

- In February 2018, the FASB issued ASU 2018-02 Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The guidance allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. The amendments eliminate the stranded tax effects resulting from the Tax Cuts and Jobs Act and are intended to improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The Update also requires certain disclosures about stranded tax effects. The guidance was effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Adoption of this guidance had no impact on the statements of financial condition and results of operations.

- In March 2017, the FASB issued ASU 2017-08 Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities. The guidance relates to certain callable debt securities and shortens the amortization period for any premium to the earliest call date. The Update was effective for interim and annual periods beginning after December 15, 2018 for public business entities. Adoption of this guidance had no impact on the statements of financial condition and results of operations.

- In February 2016, the FASB issued ASU 2016-02 Leases (Topic 842). This Update, and subsequent clarifying guidance issued, requires organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Leases will be classified as either finance leases or operating leases. This distinction will be relevant for the pattern of expense recognition in the income statement. Lessor accounting activities are largely unchanged from existing lease accounting. The Update also eliminates leveraged lease accounting but allows existing leveraged leases to continue their current accounting until maturity, termination or modification. The amendments were effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, for public business entities.

Transition Information

- The guidance was adopted using the optional modified retrospective method and practical expedients for transition. Under this transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption.
- The package of practical expedients was elected, which allowed existing leases to be largely accounted for consistent with current guidance, except for the incremental balance sheet recognition for lessees.
- There will not be a material change to the timing of future expense recognition.
- Upon adoption, a cumulative-effect adjustment to equity of less than $1 was recorded. In addition, a Right of Use Asset in the amount of $50 and Lease Liability in the amount of $50 were recognized.
- Given the limited changes to lessor accounting, there were no material changes to recognition or measurement.

Note 2 — Loans and Allowance for Loan Losses

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

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

A summary of loans outstanding at period end follows:

	March 31, 2019	December 31, 2018
Real estate mortgage	$ 329,152	$ 331,734
Production and intermediate-term	162,771	165,054
Processing and marketing	1,261	1,114
Farm-related business	6,956	6,593
Rural residential real estate	8,387	8,550
Total loans	$ 508,527	$ 513,045

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

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

	March 31, 2019							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ –	$ 17,305	$ –	$ –	$ –	$ 6,506	$ –	$ 23,811
Production and intermediate-term	–	2,762	–	–	–	2,287	–	5,049
Processing and marketing	1,037	–	–	–	–	5	1,037	5
Farm-related business	–	7,885	–	–	–	936	–	8,821
Total	$ 1,037	$ 27,952	$ –	$ –	$ –	$ 9,734	$ 1,037	$ 37,686

	December 31, 2018							
	Within AgFirst District		Within Farm Credit System		Outside Farm Credit System		Total	
	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold	Participations Purchased	Participations Sold
Real estate mortgage	$ –	$ 17,516	$ –	$ –	$ –	$ 6,578	$ –	$ 24,094
Production and intermediate-term	–	4,974	–	–	–	2,312	–	7,286
Processing and marketing	993	–	–	–	–	8	993	8
Farm-related business	–	7,997	–	–	–	946	–	8,943
Total	$ 993	$ 30,487	$ –	$ –	$ –	$ 9,844	$ 993	$ 40,331

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

	March 31, 2019			
	Due Less Than 1 Year	Due 1 Through 5 Years	Due After 5 Years	Total
Real estate mortgage	$ 4,505	$ 30,604	$ 294,043	$ 329,152
Production and intermediate-term	52,471	88,006	22,294	162,771
Processing and marketing	–	1,033	228	1,261
Farm-related business	755	1,561	4,640	6,956
Rural residential real estate	672	874	6,841	8,387
Total loans	$ 58,403	$ 122,078	$ 328,046	$ 508,527
Percentages	11.48%	24.01%	64.51%	100.00%

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

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

	March 31, 2019	December 31, 2018
Real estate mortgage:		
Acceptable	95.59%	95.81%
OAEM	3.39	2.81
Substandard/doubtful/loss	1.02	1.38
	100.00%	100.00%
Production and intermediate-term:		
Acceptable	95.08%	95.65%
OAEM	3.65	3.08
Substandard/doubtful/loss	1.27	1.27
	100.00%	100.00%
Processing and marketing:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%

	March 31, 2019	December 31, 2018
Farm-related business:		
Acceptable	100.00%	100.00%
OAEM	–	–
Substandard/doubtful/loss	–	–
	100.00%	100.00%
Rural residential real estate:		
Acceptable	93.20%	92.93%
OAEM	2.71	2.69
Substandard/doubtful/loss	4.09	4.38
	100.00%	100.00%
Total loans:		
Acceptable	95.46%	95.77%
OAEM	3.41	2.86
Substandard/doubtful/loss	1.13	1.37
	100.00%	100.00%

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

	March 31, 2019				
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans
Real estate mortgage	$ 2,197	$ 1,117	$ 3,314	$ 329,491	$ 332,805
Production and intermediate-term	1,634	2,094	3,728	162,425	166,153
Processing and marketing	–	–	–	1,264	1,264
Farm-related business	3	–	3	7,000	7,003
Rural residential real estate	–	–	–	8,408	8,408
Total	$ 3,834	$ 3,211	$ 7,045	$ 508,588	$ 515,633

	December 31, 2018				
	30 Through 89 Days Past Due	90 Days or More Past Due	Total Past Due	Not Past Due or Less Than 30 Days Past Due	Total Loans
Real estate mortgage	$ 645	$ 598	$ 1,243	$ 334,359	$ 335,602
Production and intermediate-term	918	2,413	3,331	164,958	168,289
Processing and marketing	–	–	–	1,117	1,117
Farm-related business	3	–	3	6,618	6,621
Rural residential real estate	30	–	30	8,541	8,571
Total	$ 1,596	$ 3,011	$ 4,607	$ 515,593	$ 520,200

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

	March 31, 2019	December 31, 2018
Nonaccrual loans:		
Real estate mortgage	$ 923	$ 735
Production and intermediate-term	3,085	1,961
Rural residential real estate	265	271
Total	$ 4,273	$ 2,967
Accruing restructured loans:		
Real estate mortgage	$ 1,200	$ 1,093
Production and intermediate-term	582	43
Total	$ 1,782	$ 1,136
Accruing loans 90 days or more past due:		
Real estate mortgage	$ 615	$ 91
Production and intermediate-term	232	604
Total	$ 847	$ 695
Total nonperforming loans	$ 6,902	$ 4,798
Other property owned	–	–
Total nonperforming assets	$ 6,902	$ 4,798
Nonaccrual loans as a percentage of total loans	0.84%	0.58%
Nonperforming assets as a percentage of total loans and other property owned	1.36%	0.94%
Nonperforming assets as a percentage of capital	7.66%	5.47%

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

	March 31, 2019	December 31, 2018
Impaired nonaccrual loans:		
Current as to principal and interest	$ 1,808	$ 511
Past due	2,465	2,456
Total	$ 4,273	$ 2,967
Impaired accrual loans:		
Restructured	$ 1,782	$ 1,136
90 days or more past due	847	695
Total	$ 2,629	$ 1,831
Total impaired loans	$ 6,902	$ 4,798
Additional commitments to lend	$ –	$ 57

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

	March 31, 2019			Three Months Ended March 31, 2019	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ 201	$ 365	$ –	$ 167	$ –
Production and intermediate-term	1,412	1,345	166	1,176	3
Rural residential real estate	–	–	–	–	–
Total	$ 1,613	$ 1,710	$ 166	$ 1,343	$ 3
With no related allowance for credit losses:					
Real estate mortgage	$ 2,537	$ 2,545	$ –	$ 2,113	$ 5
Production and intermediate-term	2,487	2,490	–	2,071	4
Rural residential real estate	265	349	–	221	–
Total	$ 5,289	$ 5,384	$ –	$ 4,405	$ 9
Total impaired loans:					
Real estate mortgage	$ 2,738	$ 2,910	$ –	$ 2,280	$ 5
Production and intermediate-term	3,899	3,835	166	3,247	7
Rural residential real estate	265	349	–	221	–
Total	$ 6,902	$ 7,094	$ 166	$ 5,748	$ 12

	December 31, 2018			Year Ended December 31, 2018	
Impaired loans:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Impaired Loans	Interest Income Recognized on Impaired Loans
With a related allowance for credit losses:					
Real estate mortgage	$ –	$ –	$ –	$ –	$ –
Production and intermediate-term	299	293	91	273	9
Rural residential real estate	–	–	–	–	–
Total	$ 299	$ 293	$ 91	$ 273	$ 9
With no related allowance for credit losses:					
Real estate mortgage	$ 1,919	$ 2,127	$ –	$ 1,752	$ 55
Production and intermediate-term	2,309	2,322	–	2,106	66
Rural residential real estate	271	350	–	247	8
Total	$ 4,499	$ 4,799	$ –	$ 4,105	$ 129
Total impaired loans:					
Real estate mortgage	$ 1,919	$ 2,127	$ –	$ 1,752	$ 55
Production and intermediate-term	2,608	2,615	91	2,379	75
Rural residential real estate	271	350	–	247	8
Total	$ 4,798	$ 5,092	$ 91	$ 4,378	$ 138

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

	Real Estate Mortgage	Production and Intermediate-term	Agribusiness*	Rural Residential Real Estate	Total
Activity related to the allowance for credit losses:					
Balance at December 31, 2018	$ 3,114	$ 1,068	$ 45	$ 50	$ 4,277
Charge-offs	–	–	–	–	–
Recoveries	–	–	–	–	–
Provision for loan losses	(52)	50	3	(1)	–
Balance at March 31, 2019	$ 3,062	$ 1,118	$ 48	$ 49	$ 4,277
Balance at December 31, 2017	$ 2,466	$ 1,460	$ 48	$ 63	$ 4,037
Charge-offs	–	–	–	–	–
Recoveries	–	1	–	–	1
Provision for loan losses	394	(371)	(9)	(14)	–
Balance at March 31, 2018	$ 2,860	$ 1,090	$ 39	$ 49	$ 4,038
Allowance on loans evaluated for impairment:					
Individually	$ –	$ 166	$ –	$ –	$ 166
Collectively	3,062	952	48	49	4,111
Balance at March 31, 2019	$ 3,062	$ 1,118	$ 48	$ 49	$ 4,277
Individually	$ –	$ 91	$ –	$ –	$ 91
Collectively	3,114	977	45	50	4,186
Balance at December 31, 2018	$ 3,114	$ 1,068	$ 45	$ 50	$ 4,277
Recorded investment in loans evaluated for impairment:					
Individually	$ 2,738	$ 3,899	$ –	$ 265	$ 6,902
Collectively	330,067	162,254	8,267	8,143	508,731
Balance at March 31, 2019	$ 332,805	$ 166,153	$ 8,267	$ 8,408	$ 515,633
Individually	$ 1,919	$ 2,608	$ –	$ 271	$ 4,798
Collectively	333,683	165,681	7,738	8,300	515,402
Balance at December 31, 2018	$ 335,602	$ 168,289	$ 7,738	$ 8,571	$ 520,200

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

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

	Three Months Ended March 31, 2019				
Outstanding Recorded Investment	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Real estate mortgage	$ –	$ 92	$ –	$ 92	
Production and intermediate-term	–	538	–	538	
Total	$ –	$ 630	$ –	$ 630	
Post-modification:					
Real estate mortgage	$ –	$ 92	$ –	$ 92	$ –
Production and intermediate-term	–	538	–	538	–
Total	$ –	$ 630	$ –	$ 630	$ –

	Three Months Ended March 31, 2018				
Outstanding Recorded Investment	Interest Concessions	Principal Concessions	Other Concessions	Total	Charge-offs
Pre-modification:					
Production and intermediate-term	$ –	$ 45	$ –	$ 45	
Total	$ –	$ 45	$ –	$ 45	
Post-modification:					
Production and intermediate-term	$ –	$ 45	$ –	$ 45	$ –
Total	$ –	$ 45	$ –	$ 45	$ –

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

There were no TDRs that occurred during the previous twelve months and for which there was a subsequent payment default during the periods presented. Payment default is defined as a payment that was thirty days or more past due.

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

	Total TDRs		Nonaccrual TDRs	
	March 31, 2019	December 31, 2018	March 31, 2019	December 31, 2018
Real estate mortgage	$ 1,200	$ 1,093	$ –	$ –
Production and intermediate-term	582	43	–	–
Total loans	$ 1,782	$ 1,136	$ –	$ –
Additional commitments to lend	$ –	$ –		

The following table presents information as of period end:

	March 31, 2019
Carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession	$ –
Recorded investment of consumer mortgage loans secured by residential real estate for which formal foreclosure proceedings are in process	$ 66

Note 3 — Investments

Equity Investments in Other Farm Credit System Institutions

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

Associations are required to maintain ownership in AgFirst (AgFirst or the Bank) in the form of Class B or Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements. The Association owned 2.10 percent of the issued stock of the Bank as of March 31, 2019 net of any reciprocal investment. As of that date, the Bank's assets totaled $32.7 billion and shareholders' equity totaled $2.3 billion. The Bank's earnings were $67 million for the first three months of 2019. In addition, the Association held investments of $217 related to other Farm Credit institutions.

Note 4 — Debt

Notes Payable to AgFirst Farm Credit Bank

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

Note 5 — Fair Value Measurement

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

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

The classifications within the fair value hierarchy are as follows:

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

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

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

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

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

Fair values are estimated at each period end date for assets and liabilities measured at fair value on a recurring basis. Other Financial Instruments are not measured at fair value in the statement of financial position, but their fair values are estimated as of each period end date. The following tables summarize the carrying amounts of these assets and liabilities at period end, and their related fair values.

	March 31, 2019				
	Total Carrying Amount	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Recurring Measurements					
Assets:					
Recurring Assets	$ –	$ –	$ –	$ –	$ –
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 1,447	$ –	$ –	$ 1,447	$ 1,447
Other property owned	–	–	–	–	–
Nonrecurring Assets	$ 1,447	$ –	$ –	$ 1,447	$ 1,447
Other Financial Instruments					
Assets:					
Cash	$ 1,225	$ 1,225	$ –	$ –	$ 1,225
Loans	502,803	–	–	493,309	493,309
Other Financial Assets	$ 504,028	$ 1,225	$ –	$ 493,309	$ 494,534
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 425,923	$ –	$ –	$ 421,586	$ 421,586
Other Financial Liabilities	$ 425,923	$ –	$ –	$ 421,586	$ 421,586

	December 31, 2018				
	Total Carrying Amount	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Recurring Measurements					
Assets:					
Recurring Assets	$ –	$ –	$ –	$ –	$ –
Liabilities:					
Recurring Liabilities	$ –	$ –	$ –	$ –	$ –
Nonrecurring Measurements					
Assets:					
Impaired loans	$ 208	$ –	$ –	$ 208	$ 208
Other property owned	–	–	–	–	–
Nonrecurring Assets	$ 208	$ –	$ –	$ 208	$ 208
Other Financial Instruments					
Assets:					
Cash	$ 3,046	$ 3,046	$ –	$ –	$ 3,046
Loans	508,560	–	–	493,247	493,247
Other Financial Assets	$ 511,606	$ 3,046	$ –	$ 493,247	$ 496,293
Liabilities:					
Notes payable to AgFirst Farm Credit Bank	$ 441,115	$ –	$ –	$ 431,598	$ 431,598
Other Financial Liabilities	$ 441,115	$ –	$ –	$ 431,598	$ 431,598

SENSITIVITY TO CHANGES IN SIGNIFICANT UNOBSERVABLE INPUTS

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

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

Inputs to Valuation Techniques

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

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

Quantitative Information about Recurring and Nonrecurring Level 3 Fair Value Measurements

	Fair Value	Valuation Technique(s)	Unobservable Input	Range
Impaired loans and other property owned	$ 1,447	Appraisal	Income and expense	*
			Comparable sales	*
			Replacement cost	*
			Comparability adjustments	*

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

Information about Other Financial Instrument Fair Value Measurements

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

Note 6 — Employee Benefit Plans

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

	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Pension	$ 150	$ 277
401(k)	59	51
Other postretirement benefits	23	19
Total	$ 232	$ 347

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

	Actual YTD Through 3/31/19	Projected Contributions For Remainder of 2019	Projected Total Contributions 2019
Pension	$ –	$ 600	$ 600
Other postretirement benefits	23	65	88
Total	$ 23	$ 665	$ 688

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

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

Note 7 — Commitments and Contingent Liabilities

From time to time, legal actions are pending against the Association in which claims for money damages are asserted. On at least a quarterly basis, the Association assesses its liabilities and contingencies in connection without standing legal proceedings utilizing the latest information available. While the outcome of legal proceedings is inherently uncertain, on the basis of information presently available, management, after consultation with legal counsel, is of the opinion that the ultimate liability, if any, from these actions, would not be material in relation to the financial position of the Association. Because it is not probable that the Association will incur a loss or the loss is not estimable, no liability has been recorded for any claims that may be pending.

Note 8 — Subsequent Events

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