FARM CREDIT 100
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# Cultivating the next century of agriculture.

**AgriBank 2016 Quarterly Report**
**June 30, 2016**

AgriBank
FARM CREDIT BANK

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# Message from the Chair

**AgriBank, FCB**

Effective August 1, 2016, William J. Thone was named interim Chief Executive Officer (CEO) of AgriBank following the departure of Bill York, who left AgriBank as CEO on July 25, 2016. Mr. Thone began his Farm Credit career at the Farm Credit Bank of St. Louis in 1979. In 1999, Mr. Thone was named AgriBank's vice president and general counsel responsible for board secretary duties and governance oversight, as well as corporate legal counsel and management of the Bank's legal team. As vice president and general counsel, Mr. Thone was also a member of AgriBank's executive leadership team until his retirement in 2015.

AgriBank's financial position remains strong and our strategic direction remains unchanged. The focus of our business remains on creating competitive advantages for affiliated Farm Credit Associations, so they can provide the best financial solutions for farmers and ranchers. The board's search for the new CEO begins immediately and will focus on the leadership necessary to carry our strategic direction forward.

# Management's Discussion and Analysis

The following discussion is a review of the financial position and results of operations of AgriBank, FCB (AgriBank). This information should be read in conjunction with the accompanying Financial Statements, the Notes to the Financial Statements and the 2015 Annual Report.

AgriBank is one of the Banks of the Farm Credit System (the System). We serve customers in states across America's heartland. AgriBank provides funding to, and is primarily owned by, its affiliated Associations. AgriBank and its affiliated Associations are collectively referred to as the District. The affiliated Associations are chartered to serve customers in substantially all of Arkansas, Illinois, Indiana, Iowa, Kentucky, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, Tennessee, Wisconsin and Wyoming. In this position, with its prime location in America's agricultural heartland and over 100 years of experience, AgriBank and affiliated Associations are respected partners for rural America based on our collective expertise in providing financial products and services for rural communities and agriculture.

## Forward-Looking Information

Any forward-looking statements in this Quarterly Report are based on current expectations and are subject to uncertainty and changes in circumstances. Actual results may differ materially from expectations due to a number of risks and uncertainties. More information about these risks and uncertainties is contained in our 2015 Annual Report. We undertake no duty to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

## Financial Overview

Net income grew $18.5 million to $260.2 million for the six months ended June 30, 2016, as compared to the same period of the prior year driven primarily by an increase in net interest income. This increase in net interest income was partially offset by a reduction in mineral income due to continued low oil prices. Refer to the Results of Operations section for further discussion.

Loan portfolio credit quality remains sound with 99.6 percent of our total loan portfolio in the acceptable category. Credit quality of our retail loan portfolio declined to 95.5 percent acceptable as of June 30, 2016, but remained in a sound position. Robust capital levels ensure we are well positioned to manage the cyclicality that is characteristic of the agricultural market. Refer to the Loan Portfolio and Funding, Liquidity and Shareholders' Equity sections for further discussion.

## Economic Conditions

**Interest Rate Environment**

U.S. economic activity is expected to continue advancing at a steady pace despite a backdrop of international headwinds, including the recent Brexit vote. For 2016, the U.S. economy is forecasted to grow at 1.9 percent, supported by consumer spending as a result of job market improvement and continued recovery in housing prices. A strong dollar is reducing demand for U.S. exports, while business investment growth is slowing due to the large declines in oil prices experienced over the past 24 months.

After seven years of record low policy rates, in December 2015 the Federal Open Market Committee (FOMC) of the Federal Reserve raised the target range for the federal funds rate by 25 basis points (bps), in an effort to kick-start the process toward normalization in the level of interest rates. The path for policy rates is expected to remain data-dependent and, according to Federal Reserve communication, anticipated economic conditions will warrant only very gradual increases in policy rates. Global economic weakness and heightened uncertainty as a result of the Brexit vote has raised doubts about the future path of policy rates and most economist now project U.S. Treasury rates to end the year close to current levels, much lower than their beginning of the year forecasts.

We manage interest rate risk consistent with policies established by the Board of Directors and limits established by AgriBank's Asset and Liability Committee (ALCO) (refer to Interest Rate Risk Management section). While many factors can impact our net interest income, it is management's expectation that financial performance will remain relatively consistent under most interest rate environments over the next 12 months.

**Agricultural Conditions**

The U.S. Department of Agriculture's Economic Research Service's (USDA-ERS) projects both net cash and net farm income to decline for the third consecutive year in 2016, after reaching a record high in 2013. Net farm income is projected to fall by 3.0 percent to $54.8 billion for 2016 compared to 2015. The total aggregate value of farm assets is projected to decline while the amount of assumed debt is projected to increase over the next year, resulting in an increase in the aggregate farm debt-to-asset ratio to 13.2 percent, after bottoming out at 11.3 percent in 2012 and 2013. Net cash income for all U.S. farming operations, on a combined basis, is projected to fall due to a decline in 2016 cash receipts of $9.6 billion (2.5 percent) compared to the same period last year, primarily related to feed crops, dairy and most protein sectors. Crop producers may benefit somewhat from a projected increase in direct government farm payments as well as reduced expenses, primarily related to energy cost savings.

Macroeconomic events of recent concern to agriculture include the recent Brexit referendum vote by the British public to begin the process of leaving the European Union and the resulting political and economic fallout from the decision. For U.S. agriculture, the immediate risk is through the impact of the decision on exchange rates and the potential for continued appreciation in the U.S. dollar which has had a negative impact upon U.S. agricultural exports. To date, however, this impact has been limited. Of longer term concern is the impact of splitting the 4th largest U.S. agricultural export market into two markets representing approximately eight percent (EU without UK) and one percent (UK only). Also, it is uncertain how this event

will impact the progress of the ongoing Transatlantic Trade and Investment Partnership (TTIP) negotiations with U.S. agriculture as one of the primary beneficiaries of the trade pact.

*Land Values*

The AgriBank District continues to closely monitor agricultural land values. As part of this monitoring, the District conducts an annual Benchmark Survey, completed by licensed real estate appraisers, of a sample of benchmark farms selected to represent the lending footprint of the affiliated Associations throughout the District. The District will complete its annual survey as of June 30, 2016, which will be released during the third quarter of 2016.

Qualitative surveys of lending officers compiled by the Federal Reserve Banks of Chicago, Kansas City, and St. Louis as of the end of the first quarter 2016 indicated declining farmland values. The Federal Reserve Banks surveys cited a year-over-year change in the average value of non-irrigated farmland from a decrease of 4.0 percent to a decrease of 7.0 percent.

Declining land values are a potential lending risk following periods of sustained, rapid land value increases. Nominal and real (inflation-adjusted) agricultural land values increased in proportions greater than other asset classes such as stocks and urban residential and commercial land during the past decade. This is largely because the agricultural sector, particularly crop farming, remained profitable throughout the economic crisis period, and demand for agricultural income-producing land remained strong. However, with the prospects for lower commodity prices, we do expect the moderation of land values to continue.

AgriBank District credit risk policies focus on loan repayment capacity in addition to conservative loan-to-value levels (LTVs) on the collateral that secures loans. Although FCA regulations allow real estate mortgage loans of up to 85 percent of appraised value, our underwriting standards generally limit lending to no more than 65 percent at origination. Due to very strong land values in much of our District in recent years, many affiliated Associations implemented risk management practices that incorporate loan-to-appraised value thresholds below the 65 percent level. In addition, many District lenders impose lending caps per acre based on the land's sustainable income-producing capacity. While underwriting exceptions on loan-to-appraised-value are sometimes granted, in such cases, loans are typically structured with shorter amortization schedules and/or additional principal payments in the early years to reduce risk.

*Updated Industry Conditions*

The following are industry conditions for which we have updated our outlook since December 31, 2015. For further analysis of industry conditions which have not experienced a change in outlook since December 31, 2015, refer to the Agricultural Conditions section of Management's Discussion and Analysis of the 2015 Annual Report.

<u>Cow-Calf</u>

The USDA estimates the U.S. beef cow herd has increased 3.5 percent compared to the prior year as a result of improved pasture conditions the past two years and significantly lower calf prices. Despite our expectation that the credit quality of the District's cow-calf portfolio will remain strong, the increase in supply and resulting price decline are expected to have an overall negative impact on producers. Based on these projections we have downgraded our cow-calf outlook to neutral as of June 30, 2016, from the positive outlook discussed in our 2015 Annual Report.

Timber

Housing starts have increased year over year, consumer confidence remains cautiously optimistic and the U.S. labor market has continued to improve, all of which have contributed to the District's timber customers, especially mills, showing strong profits. These factors are slightly offset by the strength of the U.S. Dollar which has increased timber imports and caused some price compression. Based on these overall conditions we have upgraded our timber outlook to neutral-to-positive as of June 30, 2016, from the neutral outlook discussed in our 2015 Annual Report.

## Loan Portfolio

**Components of Loans**

| (in thousands) | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Accrual loans: | | |
| Wholesale | **$76,747,416** | $74,697,130 |
| Retail loans: | | |
| Real estate mortgage | **3,595,007** | 3,832,879 |
| Production and intermediate term | **3,391,786** | 3,425,439 |
| Agribusiness | **82,227** | 96,709 |
| Loans to other financing institutions (OFIs) | **573,321** | 685,083 |
| Other | **55,002** | 39,018 |
| Total retail loans | **7,697,343** | 8,079,128 |
| Nonaccrual retail loans | **51,648** | 43,394 |
| Total loans | **$84,496,407** | $82,819,652 |

The Other category is primarily comprised of communication, rural residential real estate and energy-related loans.

Loans totaled $84.5 billion at June 30, 2016, an increase of $1.7 billion, or 2.0 percent, from December 31, 2015. The increase in total loans was driven primarily by increases to our wholesale loans, partially offset by repayments received on real estate mortgage and production and intermediate term retail participations purchased. Wholesale loans increased due to loan growth at our affiliated Associations, primarily in the real estate mortgage and agribusiness sectors.

Credit quality on loans remained sound with 99.6 percent of our portfolio in the acceptable category at June 30, 2016, compared to 99.7 percent at December 31, 2015. Adversely classified loans were 0.2 percent at June 30, 2016, and December 31, 2015. As a majority of our loans are wholesale loans, we expect our credit quality will remain sound even when affiliated Associations experience declines in their retail credit quality. Credit quality of our retail loan portfolio declined to 95.5 percent acceptable as of June 30, 2016 compared to 97.3 percent acceptable at December 31, 2015, but remained in a sound position. Given the current outlook for commodity prices, we anticipate special mention and substandard/doubtful loan volume in both our retail and affiliated Associations' loan portfolios will continue to revert to more normal levels as we move through this agriculture efficiency cycle.

**Components of Risk Assets**

| (in thousands) | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Nonaccrual loans | **$51,648** | $43,394 |
| Accruing restructured loans | **4,448** | 4,429 |
| Accruing loans 90 days or more past due | **1,825** | 1,240 |
| Total risk loans | **57,921** | 49,063 |
| Other property owned | **427** | 565 |
| Total risk assets | **$58,348** | $49,628 |
| | | |
| Risk loans as a % of total loans | **0.07%** | 0.06% |
| Nonaccrual loans as a % of total loans | **0.06%** | 0.05% |
| Delinquencies as a % of total loans | **0.05%** | 0.08% |

Note: Accruing loans include accrued interest receivable.

Risk assets have increased from December 31, 2015, primarily due to an increase in nonaccrual loans related to equipment financing loans purchased through our AgDirect portfolio, but remain at acceptable levels. Total risk loans as a percentage of total loans remains within our established risk management guidelines. At June 30, 2016, 57.8 percent of nonaccrual loans were current as to principal and interest, compared to 63.9 percent at December 31, 2015.

Our accounting policy requires loans past due 90 days to be transferred into nonaccrual status unless adequately secured and in the process of collection. Based on our analysis, all accruing loans 90 days or more past due were eligible to remain in accruing status.

As of June 30, 2016, no affiliated Associations were declared in default of any covenants. No affiliated Associations are currently paying a risk premium.

**Allowance Coverage Ratios**

| | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Allowance as a percentage of: | | |
| Loans | **0.02%** | 0.02% |
| Nonaccrual loans | **39.64%** | 41.66% |
| Total risk loans | **35.35%** | 36.84% |
| Adverse assets to risk funds* | **3.35%** | 2.72% |

*Risk funds includes total capital and allowance for loan losses.

The allowance for loan losses is an estimate of losses on loans in our portfolio as of the financial statement date. We determine the appropriate level of allowance for loan losses based on the periodic evaluation of factors such as loan loss history, estimated probability of default, estimated loss severity, portfolio quality, and current economic and environmental conditions. As of June 30, 2016, the allowance increased $2.4 million, compared to December 31, 2015. This was driven by $4.5 million of provisions for loan losses, partially offset by $2.1 million of net charge-offs during the period, primarily related to the AgDirect portfolio in the production and intermediate term loan sector. We believe the allowance for loan losses is reasonable in relation to the risk in the portfolio at June 30, 2016.

## Funding, Liquidity and Shareholders' Equity

We are responsible for meeting the District's funding, liquidity and asset/liability management needs. Access to the unsecured debt capital markets remains our primary source of liquidity. The System continues to have reliable access to the debt capital markets to support its mission of providing credit to farmers, ranchers and other eligible borrowers. During the six months ended June 30, 2016, investor demand for System-wide debt securities remained favorable.

We also maintain a secondary source of liquidity through a high-quality investment portfolio and other short-term liquid assets. We manage liquidity for our operating and debt repayment needs through managing debt maturities, as well as forecasting and anticipating seasonal demands. We maintain maturing investments and bank balances of at least $500 million on hand each day to meet cash management and loan disbursements needs in the normal course of business.

The composition of the liquidity investment portfolio is structured to meet both regulatory requirements and our operational demands. Specifically, we provide at least 15 days of liquidity coverage from cash, overnight investments and U.S. Treasury securities less than three years in maturity. Other short-term money market investments, as well as government and agency mortgage-backed securities (MBS), are positioned to cover regulatory requirements for 30- and 90-day intervals. Additionally, a supplemental liquidity buffer provides days coverage in excess of 90 days from money market instruments greater than 90 days in maturity, asset-backed securities (ABS) and non-agency MBS. At June 30, 2016, we held qualifying assets in excess of each incremental level to meet the liquidity coverage intervals.

Farm Credit Administration (FCA) regulations require maintaining a minimum of 90 days of liquidity on a continuous basis. The days of liquidity measurement refers to the number of days that maturing debt is covered by liquid investments. As of June 30, 2016, we had sufficient liquidity to fund all debt maturing within 151 days.

We maintain a contingency funding plan (CFP) that helps inform our operating and funding needs and addresses actions we would consider in the event that there is not ready access to traditional funding sources. These potential actions include borrowing overnight via federal funds, using investment securities as collateral to borrow, using the proceeds from maturing investments and selling our liquid investments. We size our investment portfolio using the CFP to cover all operating and funding needs for a minimum of 30 days with a targeted $500 million buffer.

Total shareholders' equity at June 30, 2016 was $5.3 billion, a $92.5 million increase from December 31, 2015. The increase was primarily driven by comprehensive income for the period, partially offset by earnings reserved for patronage distributions and preferred stock dividends.

At June 30, 2016, we exceeded the regulatory minimum capital ratios. Refer to the Additional Regulatory Information section as well as Note 4 in the accompanying Financial Statements for further discussion of capital ratios and the recently approved revised regulations.

On April 26, 2016, we announced the intention to redeem our subordinated notes, which were redeemable on any interest payment date at any time following FCA notification of certain changes to our regulatory capital requirements. On July 15, 2016, we redeemed all $500 million of outstanding subordinated notes at par value.

## Results of Operations

Net income for the six months ended June 30, 2016 was $260.2 million, a 7.7 percent increase, compared to $241.7 million for the same period in 2015. The return on average assets was 0.53 percent for the six months ended June 30, 2016 and 2015.

**Changes in Significant Components of Net Income**

| (in thousands)<br>**For the six months ended June 30,** | **2016** | 2015 | Increase (decrease) in net income |
|---|---|---|---|
| Net interest income | **$280,764** | $255,259 | $25,505 |
| Provision for loan losses | **4,500** | 3,000 | (1,500) |
| Non-interest income | **44,021** | 48,351 | (4,330) |
| Non-interest expense | **60,087** | 58,909 | (1,178) |
| Net income | **$260,198** | $241,701 | $18,497 |

Net interest income (NII) for the six months ended June 30, 2016 increased compared to the same period of 2015. NII was positively impacted by increased loan volume, as well as increases in interest rates primarily related to our wholesale loans to affiliated Associations and other financing institutions (OFIs), and equipment financing loans purchased through the AgDirect program. These positive variances were partially offset by an increase in interest expense on System-wide debt securities, driven by an increase in interest rates as well as increases in volume.

**Changes in NII**

| (in thousands)<br>**For the six months ended June 30,** | **2016 vs 2015** | | |
|---|---|---|---|
| Increase (decrease) due to: | **Volume** | **Rate** | **Total** |
| Interest income: | | | |
| Loans | **$62,948** | **$55,057** | **$118,005** |
| Investments | **(213)** | **19,146** | **18,933** |
| Total interest income | **62,735** | **74,203** | **136,938** |
| Interest expense: | | | |
| System-wide debt securities and other | **(35,269)** | **(76,164)** | **(111,433)** |
| Net change in NII | **$27,466** | **$(1,961)** | **$25,505** |

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

| (in thousands)<br>**For the six months ended June 30,** | **2016** | | | 2015 | | |
|---|---|---|---|---|---|---|
| | **ADB** | **Rate** | **NII** | ADB | Rate | NII |
| Interest earning assets: | | | | | | |
| Wholesale loans | **$74,858,751** | **1.75%** | **$653,357** | $68,191,042 | 1.60% | $539,828 |
| Retail accrual loans | **7,819,870** | **3.69%** | **143,915** | 7,739,535 | 3.65% | 140,054 |
| Retail nonaccrual loans | **48,153** | **8.21%** | **1,972** | 40,559 | 6.75% | 1,357 |
| Investment securities and federal funds | **15,777,412** | **0.88%** | **69,068** | 15,843,128 | 0.64% | 50,135 |
| Total earning assets | **98,504,186** | **1.77%** | **868,312** | 91,814,264 | 1.61% | 731,374 |
| Interest bearing liabilities | **93,542,878** | **1.26%** | **587,548** | 87,242,191 | 1.10% | 476,115 |
| Interest rate spread | **$4,961,308** | **0.51%** | | $4,572,073 | 0.51% | |
| Impact of equity financing | | **0.06%** | | | 0.05% | |
| Net interest margin | | **0.57%** | | | 0.56% | |
| Net interest income | | | **$280,764** | | | $255,259 |

Net interest margin increased one basis point for the six months ended June 30, 2016, compared to the same period last year. The positive impact of increased rates on our wholesale loans, along with higher loan volume compared to the prior year, was partially offset by increases in interest expense related to System-wide debt securities as well as our changing earning asset mix. The earning asset mix changes were driven by increases in lower yielding loans to affiliated Associations relative to higher yielding retail participations purchased. To a lesser extent, competitive pressures on the retail loan portfolio, excluding AgDirect and Asset Pool portfolios, contributed to compressed spreads. Equity financing represents the benefit of non-interest rate bearing funding, which increased slightly from the prior year primarily due to an increase in interest rates. The benefit of equity financing is greater when interest rates are higher as this equity allows the Bank to fund higher earning assets with equity rather than higher rate funding.

We recorded a $4.5 million provision for loan loss during the six months ended June 30, 2016. Refer to the Loan portfolio section for further discussion.

The decrease in non-interest income was primarily due to a decline in mineral income for the six months ended June 30, 2016, compared to the same period of 2015, a result of continued low oil prices. Based on oil futures, we anticipate oil prices may continue to remain low throughout 2016, resulting in further declines in mineral income compared to the prior year. The decrease was offset by net gains on sales of investments and increased refinance and prepayment fees for the six months ended June 30, 2016, compared to the same period of 2015.

The increase in non-interest expense was primarily due to an increase Farm Credit System Insurance Corporation (FCSIC) expense. The increase was due to increase in the premium rate charged on accrual loans by FCSIC from 13 basis points in 2015 to 16 basis points for the first half and 18 basis points for the second half of 2016.

## Additional Regulatory Information

**Regulatory Capital Requirements**

On March 10, 2016, the FCA Board approved a final rule to modify the regulatory capital requirements for System Banks and Associations. The stated objectives of the rule are to:

- Modernize capital requirements while ensuring that institutions continue to hold sufficient regulatory capital to fulfill their mission as a government-sponsored enterprise
- 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, but also to ensure that the rules recognize the cooperative structure and the organization of the System
- Make System regulatory capital requirements more transparent
- Meet the requirements of section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act

The final rule replaces existing core surplus and total surplus ratios with common equity tier 1, tier 1 and total capital risk-based capital ratios. The final rule also replaces the existing net collateral ratio with a tier 1 leverage ratio. The permanent capital ratio continues to remain in effect with the final rule. Refer to note 4 for additional information regarding the revised capital ratios. The effective date of the new capital requirements is January 1, 2017. We are currently evaluating the impact of the changes.

The final rule to modify regulatory capital requirements changes the capital treatment of our subordinated notes. The terms of our subordinated notes provide that, at any time following FCA notification of certain changes to regulatory capital requirements, the subordinated notes are redeemable in whole at par on any interest payment date. On July 15, 2016, we redeemed all $500 million of outstanding subordinated notes at par value. The Permanent Capital Ratio and Total Surplus Ratio are expected to each decrease approximately 1.1 percentage points, but will remain above required levels. The Net Collateral Ratio is expected to decrease approximately 0.3 percentage points, but will also remain above required levels.

**Investment Securities Eligibility**

On June 12, 2014, the FCA Board approved a proposed rule to revise the requirements governing the eligibility of investment securities for System Banks and Associations. The stated objectives of the proposed rule are to:

- Strengthen the safety and soundness of System Banks and Associations
- Ensure that System Banks hold sufficient liquidity to continue operations and pay maturing obligations in the event of market disruption
- Enhance the ability of the System Banks to supply credit to agricultural and aquatic producers
- Comply with the requirements of section 939A of the Dodd-Frank Act
- Modernize the investment eligibility criteria for System Banks
- Revise the investment regulation for System Associations to improve their investment management practices so they are more resilient to risk

The public comment period ended on October 23, 2014.

## Certification

The undersigned have reviewed the June 30, 2016 Quarterly Report of AgriBank, FCB, which has been prepared under the oversight of the Audit Committee and in accordance with all applicable statutory or regulatory requirements. The information contained herein is true, accurate and complete to the best of our knowledge and belief.

Matthew D. Walther
Chair of the Board
August 9, 2016

William J. Thone
Interim Chief Executive Officer
August 9, 2016

Brian J. O'Keane
Executive Vice President, Banking and Finance and Chief Financial Officer
August 9, 2016

# Statements of Condition

## AgriBank, FCB

| *(in thousands)*<br>*(unaudited)* | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| **Assets** | | |
| Loans | **$84,496,407** | $82,819,652 |
| Allowance for loan losses | **20,474** | 18,076 |
| Net loans | **84,475,933** | 82,801,576 |
| Investment securities | **15,290,472** | 14,262,883 |
| Cash | **203,863** | 533,711 |
| Federal funds | **410,009** | 1,427,125 |
| Accrued interest receivable | **412,769** | 381,104 |
| Derivative assets | **1,823** | 698 |
| Other property owned | **427** | 565 |
| Allocated prepaid pension costs | **29,726** | 30,002 |
| Cash collateral pledged to counterparties | **104,005** | 32,023 |
| Other assets | **31,441** | 37,147 |
| Total assets | **$100,960,468** | $99,506,834 |
| **Liabilities** | | |
| Bonds and notes | **$94,681,315** | $93,404,251 |
| Subordinated notes | **498,490** | 498,283 |
| Accrued interest payable | **230,491** | 231,464 |
| Derivative liabilities | **163,605** | 52,002 |
| Accounts and other payables | **105,634** | 130,060 |
| Other liabilities | **14,333** | 16,658 |
| Total liabilities | **95,693,868** | 94,332,718 |
| Commitments and contingencies (Note 6) | | |
| **Shareholders' equity** | | |
| Perpetual preferred stock | **250,000** | 250,000 |
| Capital stock and participation certificates | **2,112,355** | 2,063,343 |
| Unallocated surplus | **3,050,462** | 2,945,638 |
| Accumulated other comprehensive loss | **(146,217)** | (84,865) |
| Total shareholders' equity | **5,266,600** | 5,174,116 |
| Total liabilities and shareholders' equity | **$100,960,468** | $99,506,834 |

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

# Statements of Comprehensive Income

## AgriBank, FCB

| *(in thousands)*<br>*(unaudited)*<br>**For the periods ended June 30,** | Three months<br>**2016** | <br>2015 | Six months<br>**2016** | <br>2015 |
|---|---|---|---|---|
| **Interest income** | | | | |
| Loans | **$403,131** | $344,378 | **$799,245** | $681,239 |
| Investment securities | **35,532** | 24,071 | **69,067** | 50,135 |
| Total interest income | **438,663** | 368,449 | **868,312** | 731,374 |
| **Interest expense** | **298,454** | 241,395 | **587,548** | 476,115 |
| Net interest income | **140,209** | 127,054 | **280,764** | 255,259 |
| **Provision for loan losses** | **1,500** | 1,000 | **4,500** | 3,000 |
| Net interest income after provision for loan losses | **138,709** | 126,054 | **276,264** | 252,259 |
| **Non-interest income** | | | | |
| Mineral income | **8,680** | 13,680 | **17,215** | 30,566 |
| Loan prepayment and fee income | **8,829** | 3,814 | **12,021** | 8,248 |
| Business services income | **4,164** | 3,737 | **8,264** | 7,412 |
| Miscellaneous income and other gains, net | **5,668** | 665 | **6,521** | 2,125 |
| Total non-interest income | **27,341** | 21,896 | **44,021** | 48,351 |
| **Non-interest expense** | | | | |
| Salaries and employee benefits | **9,694** | 9,889 | **19,425** | 19,530 |
| Other operating expenses | **8,958** | 9,154 | **17,118** | 17,708 |
| Loan servicing and other fees paid to affiliated Associations | **8,408** | 8,439 | **16,977** | 16,258 |
| Farm Credit System insurance expense | **3,237** | 2,622 | **6,567** | 5,340 |
| Net impairment losses recognized in earnings | **--** | -- | **--** | 73 |
| Total non-interest expense | **30,297** | 30,104 | **60,087** | 58,909 |
| **Net income** | **$135,753** | $117,846 | **$260,198** | $241,701 |
| **Other comprehensive (loss) income** | | | | |
| Investments available-for-sale: | | | | |
| Not-other-than-temporarily-impaired investments | **$19,318** | $(10,687) | **$60,225** | $4,681 |
| Other-than-temporarily-impaired investments | **(6,234)** | (2,861) | **(6,316)** | (2,989) |
| Derivatives and hedging activity | **(43,929)** | 43,704 | **(115,261)** | 20,988 |
| Total other comprehensive (loss) income | **(30,845)** | 30,156 | **(61,352)** | 22,680 |
| **Comprehensive income** | **$104,908** | $148,002 | **$198,846** | $264,381 |

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

# Statements of Changes in Shareholders' Equity

## AgriBank, FCB

| *(in thousands)*<br>*(unaudited)* | Perpetual Preferred Stock | Capital Stock and Participation Certificates | Unallocated Surplus | Accumulated Other Comprehensive Loss | Total |
|---|---|---|---|---|---|
| Balance at December 31, 2014 | $250,000 | $1,944,292 | $2,766,818 | $(45,065) | $4,916,045 |
| Net income | | | 241,701 | | 241,701 |
| Other comprehensive income | | | | 22,680 | 22,680 |
| Patronage | | | (139,252) | | (139,252) |
| Perpetual preferred stock dividends | | | (8,594) | | (8,594) |
| Capital stock/participation certificates issued | | 48,971 | | | 48,971 |
| Capital stock/participation certificates retired | | (39,634) | | | (39,634) |
| Balance at June 30, 2015 | $250,000 | $1,953,629 | $2,860,673 | $(22,385) | $5,041,917 |
| Balance at December 31, 2015 | $250,000 | $2,063,343 | $2,945,638 | $(84,865) | $5,174,116 |
| Net income | | | **260,198** | | **260,198** |
| Other comprehensive loss | | | | **(61,352)** | **(61,352)** |
| Patronage | | | **(146,780)** | | **(146,780)** |
| Perpetual preferred stock dividends | | | **(8,594)** | | **(8,594)** |
| Capital stock/participation certificates issued | | **86,948** | | | **86,948** |
| Capital stock/participation certificates retired | | **(37,936)** | | | **(37,936)** |
| **Balance at June 30, 2016** | **$250,000** | **$2,112,355** | **$3,050,462** | **$(146,217)** | **$5,266,600** |

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

# Statements of Cash Flows

## AgriBank, FCB

*(in thousands)*

*(unaudited)*

| For the six months ended June 30, | 2016 | 2015 |
|---|---|---|
| **Cash flows from operating activities** | | |
| Net income | **$260,198** | $241,701 |
| Adjustments to reconcile net income to cash flows from operating activities: | | |
| Depreciation on premises and equipment | **1,746** | 1,459 |
| Provision for loan losses | **4,500** | 3,000 |
| Loss on sales of other property owned | **77** | 9 |
| Net impairment losses recognized in earnings | **--** | 73 |
| Gain on sale of investment securities, net | **(5,981)** | (1,324) |
| Amortization of (discounts) premiums on investments, net | **(6,670)** | 8,188 |
| Amortization of discounts (premiums) on debt and deferred debt issuance costs, net | **41,788** | 15,706 |
| Loss (gain) on derivative activities | **371** | (364) |
| Changes in operating assets and liabilities: | | |
| Increase in accrued interest receivable | **(646,653)** | (540,124) |
| Decrease in other assets | **10,056** | 1,087 |
| (Decrease) increase in accrued interest payable | **(973)** | 17,996 |
| Decrease in other liabilities | **(23,376)** | (5,274) |
| Net cash used in operating activities | **(364,917)** | (257,867) |
| **Cash flows from investing activities** | | |
| (Increase) decrease in loans, net | **(1,064,200)** | 528,984 |
| Proceeds from sales of other property owned | **392** | 1,799 |
| Increase in investment securities, net | **(969,764)** | (225,021) |
| Proceeds from the sale of investment securities | **8,735** | 29,669 |
| Purchases of premises and equipment, net | **(1,523)** | (1,000) |
| Net cash (used in) provided by investing activities | **(2,026,360)** | 334,431 |
| **Cash flows from financing activities** | | |
| Consolidated bonds and notes issued | **99,109,322** | 93,948,370 |
| Consolidated bonds and notes retired | **(97,878,993)** | (94,499,118) |
| (Increase) decrease in cash collateral pledged to counterparties | **(71,982)** | 1,364 |
| Decrease in cash collateral pledged by counterparties | **--** | (3,620) |
| Patronage distributions paid | **(154,452)** | (181,878) |
| Preferred stock dividends paid | **(8,594)** | (8,594) |
| Capital stock/participation certificates issued, net | **49,012** | 9,337 |
| Net cash provided by (used) in financing activities | **1,044,313** | (734,139) |
| Net decrease in cash and federal funds | **(1,346,964)** | (657,575) |
| Cash and federal funds at beginning of period | **1,960,836** | 2,117,728 |
| Cash and federal funds at end of period | **$613,872** | $1,460,153 |
| | | |
| **Supplemental schedule of non-cash activities** | | |
| (Increase) decrease in derivative assets | **$(1,125)** | $2,793 |
| Increase (decrease) in derivative liabilities | **111,603** | (15,995) |
| Increase (decrease) in bonds from derivative activity | **5,154** | (8,150) |
| (Decrease) increase in shareholders' equity from cash flow derivatives | **(115,261)** | 20,988 |
| Increase in shareholders' equity from investment securities | **53,909** | 1,692 |
| Loans transferred to other property owned | **331** | 316 |
| Interest capitalized to loan principal | **614,988** | 530,023 |
| Preferred stock dividends accrued | **4,297** | 4,297 |
| Patronage refunds payable to owners | **79,407** | 74,995 |
| **Supplemental information** | | |
| Interest paid | **$588,521** | $458,119 |

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

# Notes to Financial Statements

**AgriBank, FCB**

## NOTE 1

## Organization and Significant Accounting Policies

AgriBank, FCB (AgriBank) is one of the Banks of the Farm Credit System (the System), a nationwide system of cooperatively owned Banks and Associations, established by Congress and subject to the provisions of the Farm Credit Act of 1971, as amended. The System specializes in providing financing and related services to qualified borrowers for agricultural and rural purposes. AgriBank and its affiliated Associations are collectively referred to as the District. At June 30, 2016, the District had 17 Agricultural Credit Association parent Associations, each of which has wholly owned Federal Land Credit Association and Production Credit Association subsidiaries. AgriBank serves as the intermediary between the financial markets and the retail lending activities of the District Associations.

A description of our organization and operation, significant accounting policies followed, financial condition and results of operations as of and for the year ended December 31, 2015 are contained in the 2015 Annual Report. These unaudited second quarter 2016 Financial Statements should be read in conjunction with the Annual Report. The results for the six months ended June 30, 2016 are not necessarily indicative of the results to be expected for the year ended December 31, 2016.

The accompanying Financial Statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform to accounting principles generally accepted in the United States of America and prevailing practices within the financial services industry.

We adopted ASU 2015-03 “Interest-Imputation of Interest,” as of December 31, 2015 which required retroactive reclassification of certain line items in the Statement of Cash Flows for the six months ended June 30, 2015.

**Recently Issued or Adopted Accounting Pronouncements**

We have assessed the potential impact of accounting standards that have been issued by the Financial Accounting Standards Board (FASB), but are not yet effective, and have determined the following standards to be applicable to our business:

| Standard | Description | Effective date and financial statement impact |
|---|---|---|
| In June 2016, the Financial Accounting Standards Board (FASB) issued ASU 2016-13 “Financial Instruments - Credit Losses." | The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. | The guidance is effective for non-U.S. Securities Exchange Commission filers for annual reporting periods beginning after December 15, 2020 including interim periods within those annual periods. Early adoption is permitted as of annual reporting periods beginning after December 15, 2018, including interim periods within those annual periods. We are currently evaluating the impact of the guidance on the financial condition, results of operations, cash flows, and financial statement disclosures. |
| In March 2016, the FASB issued ASU 2016-06 "Contingent Put and Call Options in Debt Instruments." | The guidance clarifies the steps required when assessing the economic characteristics and risks of call (put) options and their relationship with the economic characteristics and risks of their debt hosts. When a call (put) option is contingently exercisable, an entity does not have to assess whether the event that triggers the ability to exercise a call (put) option is related to interest rates or credit risks. The guidance is an improvement to GAAP because it eliminates diversity in practice in assessing embedded contingent call (put) options in debt instruments. | The guidance is effective for public entities for the first interim reporting period within the annual reporting periods beginning after December 15, 2016. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. We are currently evaluating the impact of the guidance on the financial condition, results of operations, cash flows, and financial statement disclosures. |
| In February 2016, the FASB issued ASU 2016-02 "Leases." | The guidance modifies the recognition and accounting for lessees and lessors and requires expanded disclosures regarding assumptions used to recognize revenue and expenses related to leases. | The guidance is effective for public entities for annual reporting periods beginning after December 15, 2018 including interim periods within that year. Early adoption is permitted and modified retrospective adoption is required. We are currently evaluating the impact of the guidance on the financial condition, results of operations, cash flows, and financial statement disclosures. |
| In January 2016, the FASB issued ASU 2016-01 “Recognition and Measurement of Financial Assets and Financial Liabilities.” | The guidance is intended to enhance the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The amendments address certain aspects of recognition, measurement, presentation, and disclosure of financial statements. | The guidance is effective for public entities for annual reporting periods beginning after December 15, 2017 including interim periods within that year. Early adoption is permitted for only a portion of the guidance, but that guidance does not apply to the Financial Statements. We are currently evaluating the impact of the remaining guidance on the financial condition, results of operations, cash flows, and financial statement disclosures. |

| Standard | Description | Effective date and financial statement impact |
|---|---|---|
| In May 2015, the FASB issued ASU 2015-07 "Disclosures of Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)." | The guidance removes the requirements to categorize assets valued using net asset value per share within the fair value hierarchy (Levels 1 - 3) as well as certain other disclosures. | The guidance is effective for public entities for interim and annual reporting periods beginning after December 15, 2015. We have not elected early adoption and the disclosures impacted are only required for annual reporting. The adoption of this guidance does not impact results of operations, financial condition or cash flows. We are in process of revising the disclosures in accordance with the guidance for the 2016 Annual Report. |
| In February 2015, the FASB issued ASU 2015-02 “Consolidation-Amendments to the Consolidation Analysis.” | The guidance modifies the assessment of Variable Interest Entity (VIE) characteristics as well as the assessment of related parties. | The guidance is effective for public entities for annual periods beginning after December 15, 2015. Early adoption is allowed, including in any interim period. We are currently evaluating the impact on the financial condition, results of operations, cash flows and financial statement disclosures. |
| In August 2014, the FASB issued ASU 2014-15 “Presentation of Financial Statements-Going Concern.” | The guidance requires management to perform interim and annual assessments of an entity’s ability to continue as a going concern within one year after the date the Financial Statements are issued or within one year after the Financial Statements are available to be issued, when applicable. Substantial doubt to continue as a going concern exists if it is probable that the entity will be unable to meet its obligations for the assessed period. | This guidance becomes effective for all entities for interim and annual periods ending after December 15, 2016, and early application is permitted. The adoption of this guidance will not have a material impact on the financial statement disclosures. |
| In May 2014, the FASB issued ASU 2014-09 “Revenue from Contracts with Customers." | The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. In this regard, a majority of contracts within the District would be excluded from the scope of this new guidance. | The guidance is effective for public entities for the first interim reporting period within the annual reporting periods beginning after December 15, 2017. In March 2016, the FASB issued ASUs 2016-08 and 2016-10 which provided further clarifying guidance on the previously issued standard. We are in the process of reviewing contracts to determine the effect, if any, on the financial condition and results of operations. |

## NOTE 2

# Loans and Allowance for Loan Losses

**Loans by Type**

| (in thousands) | June 30, 2016 Amount | June 30, 2016 % | December 31, 2015 Amount | December 31, 2015 % |
|---|---|---|---|---|
| Wholesale loans | **$76,747,416** | **90.8%** | $74,697,131 | 90.1% |
| Retail loans: | | | | |
| Real estate mortgage | **3,620,996** | **4.3%** | 3,859,885 | 4.7% |
| Production and intermediate term | **3,417,046** | **4.0%** | 3,441,472 | 4.2% |
| Agribusiness | **82,227** | **0.1%** | 96,709 | 0.1% |
| Loans to other financing institutions (OFIs) | **573,321** | **0.7%** | 685,083 | 0.8% |
| Other | **55,401** | **0.1%** | 39,372 | 0.1% |
| Total retail Loans | **7,748,991** | **9.2%** | 8,122,521 | 9.9% |
| Total loans | **$84,496,407** | **100.0%** | $82,819,652 | 100.0% |

The Other category is primarily comprised of communication, rural residential real estate and energy-related, loans.

**Participations**

We may purchase participations from and sell participations to others, primarily affiliated Associations. We had no purchases outside of the System in the periods presented. We did not have any participation interests sold as of June 30, 2016 or December 31, 2015.

**Retail Loan Participations Purchased**

| (in thousands) | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Real estate mortgage | **$3,620,609** | $3,859,466 |
| Production and intermediate term | **3,417,046** | 3,441,472 |
| Agribusiness | **82,227** | 96,709 |
| Other | **55,401** | 39,372 |
| Total loans | **$7,175,283** | $7,437,019 |

**Portfolio Performance**

One credit quality indicator we utilize is the Farm Credit Administration (FCA) Uniform Loan Classification System that categorizes loans into five categories. The categories are defined as follows:

- Acceptable – assets are non-criticized assets representing the highest quality. They are expected to be fully collectible. This category is further differentiated into various probabilities of default.
- Other Assets Especially Mentioned (Special Mention) – are currently collectible but exhibit some potential weakness. These assets involve increased credit risk, but not to the point of justifying a substandard classification.
- Substandard – assets exhibit some serious weakness in repayment capacity, equity and/or collateral pledged on the loan.
- Doubtful – assets exhibit similar weaknesses as 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.

**Credit Quality of Loans**

| (in thousands)<br>**As of June 30, 2016** | **Acceptable** | | **Special mention** | | **Substandard/Doubtful** | | **Total** | |
|---|---|---|---|---|---|---|---|---|
| Wholesale loans | **$77,077,179** | **100.0%** | **$ --** | **--** | **$ --** | **--** | **$77,077,179** | **100.0%** |
| Retail loans: | | | | | | | | |
| Real estate mortgage | **3,459,353** | **94.5%** | **113,091** | **3.1%** | **87,280** | **2.4%** | **3,659,724** | **100.0%** |
| Production and intermediate term | **3,293,762** | **95.9%** | **59,334** | **1.7%** | **81,406** | **2.4%** | **3,434,502** | **100.0%** |
| Agribusiness | **75,509** | **91.4%** | **--** | **--** | **7,132** | **8.6%** | **82,641** | **100.0%** |
| Loans to OFIs | **575,471** | **100.0%** | **--** | **--** | **--** | **--** | **575,471** | **100.0%** |
| Other | **54,123** | **97.6%** | **249** | **0.4%** | **1,093** | **2.0%** | **55,465** | **100.0%** |
| Total retail loans | **7,458,218** | **95.5%** | **172,674** | **2.2%** | **176,911** | **2.3%** | **7,807,803** | **100.0%** |
| Total loans | **$84,535,397** | **99.6%** | **$172,674** | **0.2%** | **$176,911** | **0.2%** | **$84,884,982** | **100.0%** |

| (in thousands)<br>As of December 31, 2015 | Acceptable | | Special mention | | Substandard/Doubtful | | Total | |
|---|---|---|---|---|---|---|---|---|
| Wholesale loans | $74,990,957 | 100.0% | $ -- | -- | $ -- | -- | $74,990,957 | 100.0% |
| Retail loans: | | | | | | | | |
| Real estate mortgage | 3,766,278 | 96.5% | 56,983 | 1.5% | 78,955 | 2.0% | 3,902,216 | 100.0% |
| Production and intermediate term | 3,385,379 | 97.8% | 24,837 | 0.7% | 53,106 | 1.5% | 3,463,322 | 100.0% |
| Agribusiness | 89,568 | 92.3% | -- | -- | 7,487 | 7.7% | 97,055 | 100.0% |
| Loans to OFIs | 686,841 | 100.0% | -- | -- | -- | -- | 686,841 | 100.0% |
| Other | 37,866 | 96.0% | 400 | 1.0% | 1,168 | 3.0% | 39,434 | 100.0% |
| Total retail loans | 7,965,932 | 97.3% | 82,220 | 1.0% | 140,716 | 1.7% | 8,188,868 | 100.0% |
| Total loans | $82,956,889 | 99.7% | $82,220 | 0.1% | $140,716 | 0.2% | $83,179,825 | 100.0% |

Note: Accruing loans include accrued interest receivable.

We had no loans categorized as loss at June 30, 2016 or December 31, 2015.

**Aging Analysis of Loans**

| (in thousands)<br>**As of June 30, 2016** | **30-89 Days Past Due** | **90 Days or More Past Due** | **Total Past Due** | **Not Past Due or Less than 30 Days Past Due** | **Total Loans** | **Accruing loans 90 days or more past due** |
|---|---|---|---|---|---|---|
| Wholesale loans | **$ --** | **$ --** | **$ --** | **$77,077,179** | **$77,077,179** | **$ --** |
| Real estate mortgage | **8,245** | **9,780** | **18,025** | **3,641,699** | **3,659,724** | **1,728** |
| Production and intermediate term | **18,702** | **8,759** | **27,461** | **3,407,041** | **3,434,502** | **97** |
| Agribusiness | **--** | **--** | **--** | **82,641** | **82,641** | **--** |
| Loans to OFIs | **--** | **--** | **--** | **575,471** | **575,471** | **--** |
| Other | **--** | **--** | **--** | **55,465** | **55,465** | **--** |
| Total loans | **$26,947** | **$18,539** | **$45,486** | **$84,839,496** | **$84,884,982** | **$1,825** |

| (in thousands)<br>As of December 31, 2015 | 30-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Not Past Due or Less than 30 Days Past Due | Total Loans | Accruing loans 90 days or more past due |
|---|---|---|---|---|---|---|
| Wholesale loans | $ -- | $ -- | $ -- | $74,990,957 | $74,990,957 | $ -- |
| Real estate mortgage | 14,203 | 8,585 | 22,788 | 3,879,428 | 3,902,216 | 932 |
| Production and intermediate term | 31,391 | 3,785 | 35,176 | 3,428,146 | 3,463,322 | 308 |
| Agribusiness | -- | -- | -- | 97,055 | 97,055 | -- |
| Loans to OFIs | -- | -- | -- | 686,841 | 686,841 | -- |
| Other | 5,463 | 243 | 5,706 | 33,728 | 39,434 | -- |
| Total loans | $51,057 | $12,613 | $63,670 | $83,116,155 | $83,179,825 | $1,240 |

Note: Accruing loans include accrued interest receivable.

## Risk Assets

Risk loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms.

**Risk Loan Information**

| (in thousands) | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Nonaccrual loans: | | |
| Current as to principal and interest | **$29,829** | $27,739 |
| Past due | **21,819** | 15,655 |
| Total nonaccrual loans | **51,648** | 43,394 |
| Accruing restructured loans | **4,448** | 4,429 |
| Accruing loans 90 days or more past due | **1,825** | 1,240 |
| Total risk loans | **$57,921** | $49,063 |
| | | |
| Volume with specific reserves | **$25,372** | $18,441 |
| Volume without specific reserves | **32,549** | 30,622 |
| Total risk loans | **$57,921** | $49,063 |
| | | |
| Specific reserves | **$4,235** | $3,564 |

| **For the six months ended June 30,** | **2016** | 2015 |
|---|---|---|
| Income on accrual risk loans | **$124** | $110 |
| Income on nonaccrual loans | **1,972** | 1,357 |
| Total income on risk loans | **$2,096** | $1,467 |
| | | |
| Average recorded risk loans | **$53,702** | $45,819 |

Note: Accruing loans include accrued interest receivable.

**Risk Assets by Loan Type**

| (in thousands) | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Nonaccrual loans: | | |
| Real estate mortgage | **$25,989** | $27,006 |
| Production and intermediate term | **25,260** | 16,033 |
| Other | **399** | 355 |
| Total nonaccrual loans | **$51,648** | $43,394 |
| | | |
| Accruing restructured loans: | | |
| Real estate mortgage | **$4,263** | $4,247 |
| Production and intermediate term | **185** | 182 |
| Total accruing restructured loans | **$4,448** | $4,429 |
| | | |
| Accruing loans 90 days or more past due: | | |
| Real estate mortgage | **$1,728** | $932 |
| Production and intermediate term | **97** | 308 |
| Total accruing loans 90 days or more past due | **$1,825** | $1,240 |
| | | |
| Total risk loans | **$57,921** | $49,063 |
| Other property owned | **427** | 565 |
| Total risk assets | **$58,348** | $49,628 |

Note: Accruing loans include accrued interest receivable.

We had no wholesale loans classified as risk loans at June 30, 2016 or December 31, 2015.

All risk loans are considered to be impaired loans.

**Additional Impaired Loan Information by Loan Type**

| | As of June 30, 2016 | | | For the six months ended June 30, 2016 | |
|---|---|---|---|---|---|
| (in thousands) | Recorded Investment * | Unpaid Principal Balance** | Related Allowance | Average Impaired Loans | Interest Income Recognized |
| Impaired loans with a related allowance for loan losses: | | | | | |
| Real estate mortgage | $5,434 | $6,525 | $1,296 | $5,273 | $ -- |
| Production and intermediate term | 19,896 | 20,089 | 2,916 | 17,402 | -- |
| Other | 42 | 43 | 23 | 34 | -- |
| Total loans | $25,372 | $26,657 | $4,235 | $22,709 | $ -- |
| Impaired loans with no related allowance for loan losses: | | | | | |
| Real estate mortgage | $26,545 | $43,780 | $ -- | $25,765 | $1,192 |
| Production and intermediate term | 5,647 | 6,338 | -- | 4,939 | 904 |
| Other | 357 | 585 | -- | 289 | -- |
| Total loans | $32,549 | $50,703 | $ -- | $30,993 | $2,096 |
| Total impaired loans: | | | | | |
| Real estate mortgage | $31,979 | $50,305 | $1,296 | $31,038 | $1,192 |
| Production and intermediate term | 25,543 | 26,427 | 2,916 | 22,341 | 904 |
| Other | 399 | 628 | 23 | 323 | -- |
| Total loans | $57,921 | $77,360 | $4,235 | $53,702 | $2,096 |

| | As of December 31, 2015 | | | For the six months ended June 30, 2015 | |
|---|---|---|---|---|---|
| (in thousands) | Recorded Investment* | Unpaid Principal Balance** | Related Allowance | Average Impaired Loans | Interest Income Recognized |
| Impaired loans with a related allowance for loan losses: | | | | | |
| Real estate mortgage | $5,109 | $5,641 | $1,119 | $4,697 | $ -- |
| Production and intermediate term | 13,111 | 13,542 | 2,357 | 9,693 | -- |
| Other | 221 | 220 | 88 | -- | -- |
| Total loans | $18,441 | $19,403 | $3,564 | $14,390 | $ -- |
| Impaired loans with no related allowance for loan losses: | | | | | |
| Real estate mortgage | $27,076 | $44,625 | $ -- | $28,321 | $1,034 |
| Production and intermediate term | 3,412 | 5,142 | -- | 2,917 | 433 |
| Other | 134 | 379 | -- | 191 | -- |
| Total loans | $30,622 | $50,146 | $ -- | $31,429 | $1,467 |
| Total impaired loans: | | | | | |
| Real estate mortgage | $32,185 | $50,266 | $1,119 | $33,018 | $1,034 |
| Production and intermediate term | 16,523 | 18,684 | 2,357 | 12,610 | 433 |
| Other | 355 | 599 | 88 | 191 | -- |
| Total loans | $49,063 | $69,549 | $3,564 | $45,819 | $1,467 |

*The recorded investment in the receivable is the face amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges and acquisition costs and may also reflect a previous direct write-down of the investment. The recorded investment may be less than the unpaid principal balance as payments on non-cash basis nonaccrual loans reduce the recorded investment.
**Unpaid principal balance represents the contractual principal balance of the loan.

We did not have any material commitments to lend additional money to borrowers whose loans were at risk as of June 30, 2016.

**Troubled Debt Restructurings**

Included within our loans are troubled debt restructurings (TDRs). These loans have been modified by granting a concession in order to maximize the collection of amounts due when a borrower is experiencing financial difficulties. All risk loans, including TDRs, are analyzed within our allowance for loan losses.

There were no TDRs that occurred during the six months ended June 30, 2016 or 2015. The primary types of modification typically include forgiveness of interest, interest rate reduction below market or extension of maturity.

We had no TDRs that defaulted during the six months ended June 30, 2016 or 2015, in which the modifications were within 12 months of the respective reporting period.

**TDRs Outstanding**

| (in thousands) | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Accrual Status | | |
| Real estate mortgage | **$4,263** | $4,247 |
| Production and intermediate term | **185** | 182 |
| Total TDRs in accrual status | **$4,448** | $4,429 |
| Nonaccrual Status | | |
| Real estate mortgage | **$3,963** | $5,378 |
| Production and intermediate term | **7** | 11 |
| Total TDRs in nonaccrual status | **$3,970** | $5,389 |
| Total TDRs | **$8,418** | $9,818 |

We have no additional commitments to lend to borrowers whose loans have been modified as TDRs as of June 30, 2016.

**Allowance for Loan Losses**

**Changes in Allowance for Loan Losses**

| (in thousands)<br>**For the six months ended June 30,** | **2016** | 2015 |
|---|---|---|
| Balance at beginning of period | **$18,076** | $12,520 |
| Provision for loan losses | **4,500** | 3,000 |
| Charge-offs | **(2,703)** | (2,035) |
| Recoveries | **601** | 669 |
| Balance at end of period | **$20,474** | $14,154 |

Our allowance for loan losses increased from December 31, 2015, to $20.5 million at June 30, 2016, reflecting $4.5 million of provision expense recorded for the period, partially offset by net charge-offs of $2.1 million. The provision expense and net charge-offs were primarily related to declines in credit quality of equipment financing loans in the AgDirect portfolio, driven by continued low commodity prices.

**Changes in Allowance for Loan Losses and Year End Recorded Investments by Loan Type**

| (in thousands) | Wholesale loans | Real estate mortgage | Production and intermediate term | Agribusiness | Loans to OFIs | Other | Total |
|---|---|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | | | |
| Balance at December 31, 2015 | $ -- | $1,928 | $15,381 | $269 | $278 | $220 | $18,076 |
| Provision for (reversal of) loan losses | -- | 865 | 3,489 | 149 | (49) | 46 | 4,500 |
| Charge-offs | -- | (650) | (1,997) | -- | -- | (56) | (2,703) |
| Recoveries | -- | 100 | 497 | -- | -- | 4 | 601 |
| Balance at June 30, 2016 | $ -- | $2,243 | $17,370 | $418 | $229 | $214 | $20,474 |
| At June 30, 2016: | | | | | | | |
| Ending balance: individually evaluated for impairment | $ -- | $1,296 | $2,916 | $ -- | $ -- | $23 | $4,235 |
| Ending balance: collectively evaluated for impairment | $ -- | $947 | $14,454 | $418 | $229 | $191 | $16,239 |
| Recorded investments in loans outstanding: | | | | | | | |
| Ending balance at June 30, 2016 | $77,077,179 | $3,659,724 | $3,434,502 | $82,641 | $575,471 | $55,465 | $84,884,982 |
| Ending balance for loans individually evaluated for impairment | $77,077,179 | $31,979 | $25,543 | $ -- | $ -- | $399 | $77,135,100 |
| Ending balance for loans collectively evaluated for impairment | $ -- | $3,627,745 | $3,408,959 | $82,641 | $575,471 | $55,066 | $7,749,882 |

| (in thousands) | Wholesale loans | Real estate mortgage | Production and intermediate term | Agribusiness | Loans to OFIs | Other | Total |
|---|---|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | | | |
| Balance at December 31, 2014 | $ -- | $2,003 | $9,710 | $457 | $235 | $115 | $12,520 |
| (Reversal of) provision for loan losses | -- | (315) | 3,459 | (160) | (11) | 27 | 3,000 |
| Charge-offs | -- | (219) | (1,815) | -- | -- | (1) | (2,035) |
| Recoveries | -- | 84 | 581 | -- | -- | 4 | 669 |
| Balance at June 30, 2015 | $ -- | $1,553 | $11,935 | $297 | $224 | $145 | $14,154 |
| At December 31, 2015: | | | | | | | |
| Ending balance: individually evaluated for impairment | $ -- | $1,118 | $2,358 | $ -- | $ -- | $88 | $3,564 |
| Ending balance: collectively evaluated for impairment | $ -- | $810 | $13,023 | $269 | $278 | $132 | $14,512 |
| Recorded investments in loans outstanding: | | | | | | | |
| Ending balance at December 31, 2015 | $74,990,957 | $3,902,216 | $3,463,322 | $97,055 | $686,841 | $39,434 | $83,179,825 |
| Ending balance for loans individually evaluated for impairment | $74,990,957 | $32,185 | $16,523 | $ -- | $ -- | $355 | $75,040,020 |
| Ending balance for loans collectively evaluated for impairment | $ -- | $3,870,031 | $3,446,799 | $97,055 | $686,841 | $39,079 | $8,139,805 |

Note: Accruing loans include accrued interest receivable.

## NOTE 3

# Investment Securities

All investment securities are classified as available-for-sale (AFS).

**Investment Securities**

| (in thousands)<br>**As of June 30, 2016** | **Amortized Cost** | **Unrealized Gains** | **Unrealized Losses** | **Fair Value** | **Weighted Average Yield** |
|---|---|---|---|---|---|
| Mortgage-backed securities | **$5,631,084** | **$33,266** | **$18,825** | **$5,645,525** | **1.2%** |
| Commercial paper and other | **5,077,071** | **921** | **22** | **5,077,970** | **0.8%** |
| U.S. Treasury securities | **3,840,502** | **17,627** | **102** | **3,858,027** | **1.0%** |
| Asset-backed securities | **708,349** | **682** | **81** | **708,950** | **1.0%** |
| Total | **$15,257,006** | **$52,496** | **$19,030** | **$15,290,472** | **1.0%** |

| (in thousands)<br>As of December 31, 2015 | Amortized Cost | Unrealized Gains | Unrealized Losses | Fair Value | Weighted Average Yield |
|---|---|---|---|---|---|
| Mortgage-backed securities | $5,774,742 | $15,807 | $33,538 | $5,757,011 | 1.1% |
| Commercial paper and other | 4,914,613 | 213 | 441 | 4,914,385 | 0.5% |
| U.S. Treasury securities | 2,822,368 | 129 | 7,240 | 2,815,257 | 1.1% |
| Asset-backed securities | 771,602 | 6,036 | 1,408 | 776,230 | 0.8% |
| Total | $14,283,325 | $22,185 | $42,627 | $14,262,883 | 0.9% |

Commercial paper and other is primarily corporate commercial paper, certificates of deposit and term federal funds.

**Contractual Maturities of Investment Securities**

| | **Year of Maturity** | | | | |
|---|---|---|---|---|---|
| (in thousands)<br>**As of June 30, 2016** | **One Year or Less** | **One to Five Years** | **Five to Ten Years** | **More Than Ten Years** | **Total** |
| Mortgage-backed securities | **$84** | **$21,322** | **$98,270** | **$5,525,849** | **$5,645,525** |
| Commercial paper and other | **5,077,970** | **--** | **--** | **--** | **5,077,970** |
| U.S. Treasury securities | **1,104,738** | **2,753,289** | **--** | **--** | **3,858,027** |
| Asset-backed securities | **4,549** | **704,401** | **--** | **--** | **708,950** |
| Total | **$6,187,341** | **$3,479,012** | **$98,270** | **$5,525,849** | **$15,290,472** |
| Weighted average yield | **0.8%** | **1.1%** | **1.5%** | **1.2%** | **1.0%** |

The expected average life is 0.7 years for asset-backed securities (ABS) and 3.2 years for mortgage-backed securities (MBS) at June 30, 2016. Expected maturities differ from contractual maturities because borrowers may have the right to prepay obligations.

**Additional Investment Security Information**

| (in thousands)<br>**For the six months ended June 30,** | **2016** | 2015 |
|---|---|---|
| Proceeds from sales | **$8,735** | $29,669 |
| Realized gross gains on sales | **6,155** | 2,560 |
| Realized gross losses on sales | **174** | 1,236 |

The proceeds from sales in 2016 and 2015 were related to the sale of home-equity ABS and non-agency MBS investments.

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

| | **Less than 12 months** | | **More than 12 months** | |
|---|---|---|---|---|
| (in thousands)<br>**As of June 30, 2016** | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** |
| Mortgage-backed securities | **$2,112,126** | **$9,598** | **$1,174,732** | **$9,227** |
| Commercial paper and other | **541,929** | **22** | **--** | **--** |
| U.S. Treasury securities | **220,773** | **102** | **--** | **--** |
| Asset-backed securities | **164,901** | **51** | **81,012** | **30** |
| Total | **$3,039,729** | **$9,773** | **$1,255,744** | **$9,257** |

| | Less than 12 months | | More than 12 months | |
|---|---|---|---|---|
| (in thousands)<br>As of December 31, 2015 | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| Mortgage-backed securities | $3,484,228 | $21,377 | $693,595 | $12,161 |
| Commercial paper and other | 2,461,453 | 441 | -- | -- |
| U.S. Treasury securities | 2,413,587 | 7,240 | -- | -- |
| Asset-backed securities | 709,820 | 1,254 | 59,641 | 154 |
| Total | $9,069,088 | $30,312 | $753,236 | $12,315 |

We evaluate our investment securities for other-than-temporary impairment (OTTI) on a quarterly basis. The impairments primarily reflect recent performance of underlying collateral for these securities. We have determined no other securities were in an OTTI loss position at June 30, 2016.

**OTTI Investments**

| (in thousands) | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Fair Value of OTTI Investments | **$31,318** | $41,848 |

| **For the six months ended June 30,** | **2016** | 2015 |
|---|---|---|
| Gross impairment charges on OTTI Investments | **$ --** | $128 |
| Non-credit component recognized in other comprehensive income | **--** | $(55) |
| Net impairment charges on OTTI investments | **$ --** | $73 |

Of the securities sold during the six months ended June 30, 2016 and 2015, $8.7 million and $9.7 million were OTTI AFS securities resulting in gains of $6.2 million and $2.6 million, respectively.

Securities totaling $57.5 million were sold in July 2016, including all remaining OTTI securities, at a net gain of $4.1 million.

The following represents the activity related to the credit-loss component for investment securities that have been written down for OTTI that has been recognized in earnings:

| (in thousands)<br>**For the six months ended June 30,** | **2016** | 2015 |
|---|---|---|
| Credit-loss component, beginning of period | **$25,160** | $42,062 |
| Additions: | | |
| Initial credit impairment | **--** | 73 |
| Reductions: | | |
| For gain on securities sold | **(6,155)** | (2,560) |
| For impairment previously recognized on securities sold | **(8,174)** | (2,968) |
| For increases in expected cash flows | **(464)** | (4,104) |
| Credit-loss component, end of period | **$10,367** | $32,503 |

## NOTE 4

# Capital

**AgriBank Regulatory Capital Requirements and Ratios**

| | **Regulatory Minimums** | **June 30, 2016** | December 31, 2015 |
|---|---|---|---|
| Permanent capital ratio | 7.0% | **21.2%** | 20.8% |
| Total surplus ratio | 7.0% | **18.0%** | 17.9% |
| Core surplus ratio | 3.5% | **12.3%** | 12.1% |
| Net collateral ratio* | 104.0% | **105.8%** | 105.8% |

* FCA regulations require us to maintain a net collateral ratio of at least 103.0%. However, we are required by FCA to maintain a higher minimum of 104.0% during the period in which we have subordinated notes outstanding.

On March 10, 2016, the FCA Board approved a final rule to modify the regulatory capital requirements for System Banks and Associations. The final rule replaces existing core surplus and total surplus ratios with common equity tier 1, tier 1 and total capital risk-based capital ratios. The final rule also replaces the existing net collateral ratio with a tier 1 leverage ratio. The permanent capital ratio continues to remain in effect with the final rule. The effective date of the new capital requirements is January 1, 2017.

**FCA Revised Capital Requirements**

| | **Regulatory Minimums** | **Capital Conservation Buffer** | **Total** |
|---|---|---|---|
| Risk adjusted: | | | |
| Common equity Tier 1 capital ratio | 4.5% | 2.5% | 7.0% |
| Tier 1 capital ratio | 6.0% | 2.5% | 8.5% |
| Total capital ratio | 8.0% | 2.5% | 10.5% |
| | | | |
| Non-risk adjusted: | | | |
| Tier 1 leverage ratio | 4.0% | 1.0% | 5.0% |

If the capital ratios fall below the total requirements, including the buffer amounts, capital distributions (equity redemptions, dividends and patronage) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval.

The final rule to modify regulatory capital requirements changed the capital treatment of our subordinated notes. The terms of our subordinated notes provide that, at any time following FCA notification of certain changes to regulatory capital requirements, the subordinated notes are redeemable in whole at par on any interest payment date. On July 15, 2016, we redeemed all $500 million of outstanding subordinated notes at par value.

Protected participation certificates of $241 thousand are included in Capital Stock and Participation Certificates on the Statements of Changes in Shareholders' Equity as of June 30, 2016 and December 31, 2015.

Beginning in 2016, certain affiliated Associations and OFIs began paying additional spread on their wholesale loans. This additional spread paid will be returned in the form of patronage if approved by our Board.

## NOTE 5

# Employee Benefit Plans

We participate in District-wide employee benefit plans. The funded status of the post-employment benefit plans is recorded at the District-level only.

**District Components of Net Periodic Benefit Cost**

| | **2016** | | 2015 | |
|---|---|---|---|---|
| (in thousands) | **Pension** | **Other** | Pension | Other |
| **For the six months ended June 30,** | **Benefits** | **Benefits** | Benefits | Benefits |
| Service cost | **$15,303** | **$226** | $15,043 | $279 |
| Interest cost | **23,168** | **542** | 25,297 | 696 |
| Expected return on plan assets | **(29,668)** | **--** | (27,810) | -- |
| Amortization of prior service cost | **(560)** | **(222)** | (632) | (230) |
| Actuarial loss (gain) | **20,045** | **(221)** | 21,890 | (10) |
| Settlements | **2,330** | **--** | -- | -- |
| Net periodic benefit cost | **$30,618** | **$325** | $33,788 | $735 |

Certain employees in the AgriBank District participate in the AgriBank District Retirement Plan, a District-wide multi-employer defined benefit retirement plan. The employers contribute amounts necessary on an actuarial basis to provide the plan with sufficient assets to meet the benefits to be paid to participants. Refer to Note 8 in the 2015 Annual Report for a more complete description of the Employee Benefit Plans.

For the six months ended June 30, 2016, District employers have contributed $30.0 million to fund Pension Benefits and our share was $2.5 million. District employers anticipate contributing an additional $35.0 million to fund Pension Benefits in 2016. District employers typically fund 40 percent of their annual contributions to the AgriBank District Retirement Plan in June and the remaining 60 percent in December.

For the six months ended June 30, 2016, District employers have contributed $697 thousand for Other Benefits and our share was $146 thousand. District employers anticipate contributing an additional $922 thousand for Other Benefits in 2016.

Our allocated portion of the District benefit expenses for the six months ended June 30, 2016 was $2.3 million for Pension Benefits and income of $59 thousand for Other Benefits.

## NOTE 6

## Commitments and Contingencies

In the normal course of business, we have various contingent liabilities and commitments outstanding, primarily commitments to extend credit, which may not be reflected in the Financial Statements. We do not anticipate any material losses because of the contingencies or commitments.

We may, from time to time, be named as defendants in certain lawsuits or legal actions in the normal course of business. At the date of these Financial Statements, our management team was not aware of any material actions. However, management cannot ensure that such actions or other contingencies will not arise in the future.

While primarily liable for our portion of System-wide bonds and notes, we are jointly and severally liable for the System-wide bonds and notes of the other System Banks. The total bonds and notes of the System at June 30, 2016 was $254.6 billion.

## NOTE 7

## Fair Value Measurements

We use fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Assets and liabilities measured at fair value on a recurring and non-recurring basis consist of federal funds, investments available-for-sale, derivative assets and liabilities, collateral assets and liabilities, impaired loans and other property owned. The fair value is also calculated and disclosed for other financial instruments that are not measured at fair value on the Statements of Condition. These assets and liabilities consist of cash, non-impaired loans, bonds and notes, subordinated notes and commitments to extend credit and letters of credit. Refer to Note 13 in the 2015 Annual Report for descriptions of the valuation methodologies we use for asset and liabilities recorded at fair value on a recurring or non-recurring basis and for estimating fair value for financial instruments not recorded at fair value.

A fair value hierarchy is used for disclosure of fair value measurements to maximize the use of observable inputs. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Refer to Note 2 within the 2015 Annual Report for a more complete description of these input levels.

## Recurring Measurements

**Assets and Liabilities Measured at Fair Value on a Recurring Basis**

| (in thousands) | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| **As of June 30, 2016** | **Level 1** | **Level 2** | **Level 3** | **Value** |
| **Assets:** | | | | |
| Federal funds | **$ --** | **$410,009** | **$ --** | **$410,009** |
| Investments available-for-sale: | | | | |
| Mortgage-backed securities | **--** | **5,583,974** | **61,551** | **5,645,525** |
| Commercial paper and other | **--** | **5,077,970** | **--** | **5,077,970** |
| U.S. Treasury securities | **--** | **3,858,027** | **--** | **3,858,027** |
| Asset-backed securities | **--** | **708,950** | **--** | **708,950** |
| Total investments available-for-sale | **--** | **15,228,921** | **61,551** | **15,290,472** |
| Cash collateral pledged to counterparties | **104,005** | **--** | **--** | **104,005** |
| Derivative assets | **--** | **1,823** | **--** | **1,823** |
| Total assets | **$104,005** | **$15,640,753** | **$61,551** | **$15,806,309** |
| **Liabilities:** | | | | |
| Derivative liabilities | **--** | **163,605** | **--** | **163,605** |
| Total liabilities | **$ --** | **$163,605** | **$ --** | **$163,605** |

| (in thousands) | Fair Value Measurement Using | | | Total Fair |
|---|---|---|---|---|
| As of December 31, 2015 | Level 1 | Level 2 | Level 3 | Value |
| **Assets:** | | | | |
| Federal funds | $ -- | $1,427,125 | $ -- | $1,427,125 |
| Investments available-for-sale: | | | | |
| Mortgage-backed securities | -- | 5,686,573 | 70,438 | 5,757,011 |
| Commercial paper and other | -- | 4,914,385 | -- | 4,914,385 |
| U.S. Treasury securities | -- | 2,815,257 | -- | 2,815,257 |
| Asset-backed securities | -- | 768,272 | 7,958 | 776,230 |
| Total investments available-for-sale | -- | 14,184,487 | 78,396 | 14,262,883 |
| Cash collateral pledged to counterparties | 32,023 | -- | -- | 32,023 |
| Derivative assets | -- | 698 | -- | 698 |
| Total assets | $32,023 | $15,612,310 | $78,396 | $15,722,729 |
| **Liabilities:** | | | | |
| Derivative liabilities | -- | 52,002 | -- | 52,002 |
| Total liabilities | $ -- | $52,002 | $ -- | $52,002 |

**Fair Value Measurement Activity of Level 3 Instruments**

| (in thousands) | Investments Available-For-Sale | | |
|---|---|---|---|
| | **Mortgage-backed Securities** | **Asset-backed Securities** | **Total** |
| Balance at December 31, 2015 | $70,438 | $7,958 | $78,396 |
| Total gains (losses) realized/unrealized: | | | |
| Included in earnings | **415** | **5,566** | **5,981** |
| Included in other comprehensive income | **(280)** | **(5,957)** | **(6,237)** |
| Sales | **(1,417)** | **(7,318)** | **(8,735)** |
| Settlements | **(7,605)** | **(249)** | **(7,854)** |
| **Balance at June 30, 2016** | **$61,551** | **$ --** | **$61,551** |
| Balance at December 31, 2014 | $124,890 | $33,716 | $158,606 |
| Total gains (losses) realized/unrealized: | | | |
| Included in earnings | 1,146 | 105 | 1,251 |
| Included in other comprehensive income | (1,384) | (402) | (1,786) |
| Sales | (16,729) | (12,940) | (29,669) |
| Settlements | (9,981) | (4,267) | (14,248) |
| Balance at June 30, 2015 | $97,942 | $16,212 | $114,154 |

There were no assets or liabilities transferred between levels during the six months ended June 30, 2016 or 2015.

## Non-Recurring Measurements

**Assets Measured at Fair Value on a Non-recurring Basis**

| (in thousands) | As of June 30, 2016 | | | | For the six months ended June 30, 2016 |
|---|---|---|---|---|---|
| | Fair Value Measurement Using | | | Total Fair | Total |
| | **Level 1** | **Level 2** | **Level 3** | **Value** | **Losses** |
| Impaired loans | **$ --** | **$ --** | **$22,194** | **$22,194** | **$(3,374)** |
| Other property owned | **--** | **--** | **444** | **444** | **(77)** |

| (in thousands) | As of December 31, 2015 | | | | For the six months ended June 30, 2015 |
|---|---|---|---|---|---|
| | Fair Value Measurement Using | | | Total Fair | Total |
| | Level 1 | Level 2 | Level 3 | Value | Losses |
| Impaired loans | $ -- | $ -- | $15,621 | $15,621 | $(2,139) |
| Other property owned | -- | -- | 588 | 588 | (9) |

## Other Financial Instrument Measurements

**Financial Instruments Not Measured at Fair Value on the Statements of Condition**

| (in thousands)<br>**As of June 30, 2016** | **Total Carrying Amount** | **Fair Value Measurement Using** | | | **Total Fair Value** |
|---|---|---|---|---|---|
| | | **Level 1** | **Level 2** | **Level 3** | |
| Assets: | | | | | |
| Cash | **$203,863** | **$203,863** | **$ --** | **$ --** | **$203,863** |
| Net non-impaired loans | **84,454,796** | **--** | **--** | **85,474,136** | **85,474,136** |
| Total assets | **$84,658,659** | **$203,863** | **$ --** | **$85,474,136** | **$85,677,999** |
| Liabilities: | | | | | |
| Bonds and notes | **$94,681,315** | **$ --** | **$ --** | **$95,200,607** | **$95,200,607** |
| Subordinated notes | **498,490** | **--** | **--** | **500,000** | **500,000** |
| Total liabilities | **$95,179,805** | **$ --** | **$ --** | **$95,700,607** | **$95,700,607** |
| Unrecognized financial instruments: | | | | | |
| Commitments to extend credit and letters of credit | | **$ --** | **$ --** | **$(12,598)** | **$(12,598)** |

| (in thousands)<br>As of December 31, 2015 | Total Carrying Amount | Fair Value Measurement Using | | | Total Fair Value |
|---|---|---|---|---|---|
| | | Level 1 | Level 2 | Level 3 | |
| Assets: | | | | | |
| Cash | $533,711 | $533,711 | $ -- | $ -- | $533,711 |
| Net non-impaired loans | 82,786,699 | -- | -- | 82,692,611 | 82,692,611 |
| Total assets | $83,320,410 | $533,711 | $ -- | $82,692,611 | $83,226,322 |
| Liabilities: | | | | | |
| Bonds and notes | $93,404,251 | $ -- | $ -- | $93,319,254 | $93,319,254 |
| Subordinated notes | 498,283 | -- | -- | 604,885 | 604,885 |
| Total liabilities | $93,902,534 | $ -- | $ -- | $93,924,139 | $93,924,139 |
| Unrecognized financial instruments: | | | | | |
| Commitments to extend credit and letters of credit | | $ -- | $ -- | $(10,996) | $(10,996) |

## NOTE 8

# Derivative and Hedging Activity

### Use of Derivatives

We maintain an overall interest rate risk management strategy that incorporates the use of derivative products to minimize significant unplanned fluctuations in earnings that are caused by interest rate volatility. Our goals are to manage interest rate sensitivity by modifying the repricing or maturity characteristics of certain balance sheet assets and liabilities so that movements in interest rates do not adversely affect net interest margin. We consider the use of derivatives to be a prudent method of managing interest rate sensitivity, as it prevents earnings from being exposed to undue risk posed by changes in interest rates.

We primarily enter into derivative transactions, particularly interest rate swaps, to lower funding costs, diversify sources of funding, alter interest rate exposures arising from mismatches between assets and liabilities or better manage liquidity. We use various derivative instruments as follows:

- Interest rate swaps allow us to change the characteristics of fixed or floating debt we issue by swapping to a synthetic fixed or floating rate lower than those available to us if borrowings were made directly. Under interest rate swap arrangements, we agree with other parties to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating rate index.
- Interest rate options allow us to manage the impact of changing interest rates on certain assets and liabilities.
- We also facilitate interest rate swaps to qualified borrowers of the affiliated Associations. These swaps allow qualified borrowers to manage their interest rate risk and lock in a fixed interest rate similar to a fixed rate loan. We manage the interest rate risk from customer swaps with the execution of offsetting interest rate swap transactions.

**Derivative Instruments Activity (in notional amount)**

| (in millions) | Receive-Fixed Swaps | Pay-Fixed and Amortizing Pay-Fixed Swaps | Floating-for-Floating and Amortizing Floating-for Floating | Other Derivatives | Total |
|---|---|---|---|---|---|
| Balance at December 31, 2015 | $1,550 | $1,523 | $2,500 | $35 | $5,608 |
| Additions | **664** | **390** | **1,400** | **--** | **2,454** |
| Maturities/amortization | **--** | **--** | **(800)** | **--** | **(800)** |
| **Balance at June 30, 2016** | **$2,214** | **$1,913** | **$3,100** | **$35** | **$7,262** |
| | | | | | |
| Balance at December 31, 2014 | $1,550 | $1,235 | $1,150 | $40 | $3,975 |
| Additions | 500 | 115 | -- | 615 | 1,230 |
| Maturities/amortization | (250) | (100) | (100) | -- | (450) |
| Forward starting becoming effective | -- | 20 | 600 | (620) | -- |
| Balance at June 30, 2015 | $1,800 | $1,270 | $1,650 | $35 | $4,755 |

Other derivatives consisted of forward starting swaps and retail customer derivative products.

By using derivative products, we expose ourselves to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, our credit risk will equal the fair value gain in a derivative. To minimize the risk of credit losses, for non-customer bilateral derivatives we deal only with counterparties that have an investment-grade or better credit rating from a rating agency and we monitor the credit standing and levels of exposure to individual counterparties. At June 30, 2016 we do not anticipate nonperformance by any of these counterparties. We typically enter into master agreements that contain netting provisions. All derivative contracts are supported by bilateral collateral agreements with counterparties. As of June 30, 2016, certain derivatives were in a negative fair value position, requiring us to post cash collateral of $14.2 million to counterparties.

We may also clear derivative transactions through a futures commission merchant (FCM) with a clearinghouse or a central counterparty (CCP). CCPs have several layers of protection against default including margin, member capital contributions and FCM guarantees of their customers' transactions with the CCP. FCMs also pre-qualify the credit worthiness of counterparties to all swaps that are sent to the CCP, set limits for each counterparty, and collect initial and variation margin daily from each counterparty for changes in the value of

cleared derivatives. At June 30, 2016, initial margin pledged to counterparties was $21.3 million, and variation margin pledged to counterparties was $68.5 million, compared to initial margin pledged to counterparties of $17.8 million and variation margin pledged to counterparties of $14.3 million as of December 31, 2015.

Our derivative activities are monitored by our Asset-Liability Committee (ALCO) as part of the Committee's oversight of our asset/liability and treasury functions. Our hedging strategies are developed within limits established by our Board of Directors through our analysis of data derived from financial simulation models and other internal and industry sources. The resulting hedging strategies are then incorporated into our overall interest rate risk-management strategies. Refer to Note 13 of the 2015 Annual Report for additional information regarding counterparty risk and our risk mitigation practices.

**Financial Statement Impact of Derivatives**

Refer to Notes 2 and 13 of the 2015 Annual Report for additional information regarding the accounting for derivatives.

The following tables present the gross fair value, offsetting and net exposure amounts of derivative assets and derivative liabilities. The fair value of our derivative contracts are presented as "Derivative assets" and "Derivative liabilities" on the Statements of Condition, and are presented net for counterparties with master netting agreements.

| | **June 30, 2016** | | December 31, 2015 | |
|---|---|---|---|---|
| (in thousands) | **Fair Value Assets** | **Fair Value Liabilities** | Fair Value Assets | Fair Value Liabilities |
| Derivatives designated as hedging instruments: | | | | |
| Receive-fixed swaps | **$17,479** | **$ --** | $13,480 | $649 |
| Pay-fixed and amortizing pay-fixed swaps | **--** | **172,941** | 3,380 | 64,587 |
| Floating-for-floating and amortizing floating-for-floating swaps | **--** | **6,743** | 151 | 3,368 |
| Total derivatives designated as hedging instruments | **17,479** | **179,684** | 17,011 | 68,604 |
| Derivatives not designated as hedging instruments: | | | | |
| Pay-fixed and amortizing pay-fixed swaps | **--** | **1,400** | 40 | 305 |
| Other derivative products | **1,598** | **--** | 483 | -- |
| Total derivatives not designated as hedging instruments | **1,598** | **1,400** | 523 | 305 |
| Credit valuation adjustments | **225** | **--** | 71 | -- |
| Total gross amounts of derivatives | **$19,302** | **$181,084** | $17,605 | $68,909 |
| Gross amounts offset in Statements of Condition | **(17,479)** | **(17,479)** | (16,907) | (16,907) |
| Net amounts in Statements of Condition | **$1,823** | **$163,605** | $698 | $52,002 |

| (in thousands) | **June 30, 2016** | December 31, 2015 |
|---|---|---|
| Derivative assets, net | **$1,823** | $698 |
| Derivative liabilities, net | **(163,605)** | (52,002) |
| Accrued interest receivable on derivatives, net | **2,572** | 2,426 |
| Gross amounts not offset in Statements of Condition: | | |
| Cash collateral pledged to counterparties | **104,005** | 32,023 |
| Net exposure amounts | **$(55,205)** | $(16,855) |

The fair value of derivatives includes credit valuation adjustments (CVA). The CVA reflects credit risk of each derivative counterparty to which we have exposure, net of any collateral posted by the counterparty, and an

adjustment for our credit worthiness where the counterparty has exposure to us. The change in the CVA for the period is included in "Miscellaneous income and other gains, net" on the Statements of Comprehensive Income.

*Fair-Value Hedges:* We recorded $506 thousand of losses related to swaps compared to $411 thousand of gains for the same period in 2015. The gains and losses on the derivative instruments are recognized in "Interest expense" on the Statements of Comprehensive Income.

*Cash Flow Hedges:* The following table presents the amount of other comprehensive income (OCI) recognized on derivatives, the amount reclassified from accumulated other comprehensive income (AOCI) into earnings on effective cash flow hedges and amount excluded from effectiveness testing. These net losses reclassified into earnings are expected to reduce net interest income related to the respective hedged items.

| (in thousands)<br>**For the six months ended June 30, 2016**<br>**Cash Flow Hedging Relationships** | **Amount of Loss Recognized in OCI on Derivatives (Effective Portion)** | **Amount of Loss Reclassified from AOCI into Income (Effective Portion)** | **Amount of Loss Recognized in Income on Derivatives (Ineffective Portion) and Amount Excluded from Effectiveness Testing** |
|---|---|---|---|
| Pay-fixed and amortizing pay-fixed swaps | **$(111,735)** | **$ --** | **$ --** |
| Floating-for-floating and amortizing floating-for-floating swaps | **(3,526)** | **--** | **(47)** |
| Total | **$(115,261)** | **$ --** | **$(47)** |

| (in thousands)<br>For the six months ended June 30, 2015<br>Cash Flow Hedging Relationships | Amount of Gain (Loss) Recognized in OCI on Derivatives (Effective Portion) | Amount of (Loss) Reclassified from AOCI into Income (Effective Portion) | Amount of Gain Recognized in Income on Derivatives (Ineffective Portion) and Amount Excluded from Effectiveness Testing |
|---|---|---|---|
| Pay-fixed and amortizing pay-fixed swaps | $19,897 | $(27) | $2 |
| Floating-for-floating and amortizing floating-for-floating swaps | 1,064 | -- | -- |
| Other derivative products | (36) | (36) | -- |
| Total | $20,925 | $(63) | $2 |

*Derivatives not Designated as Hedges:* We recorded $1.1 million of losses on swaps for the six months ended June 30, 2016, compared to $110 thousand of gains for same period in 2015. The gains and losses on the derivative instruments are recognized in "Miscellaneous income and other gains, net" on the Statements of Comprehensive Income.

## NOTE 9

# Accumulated Other Comprehensive Income

**Changes in Components of Accumulated Other Comprehensive Income (Loss)**

| (in thousands) | Not-other-than-temporarily-impaired Investments | Other-than-temporarily-impaired Investments | Derivatives and Hedging Activity | Total |
|---|---|---|---|---|
| Balance at December 31, 2014 | $4,605 | $15,191 | $(64,861) | $(45,065) |
| Other comprehensive income (loss) before reclassifications | 3,372 | (429) | 20,925 | 23,868 |
| Amounts reclassified from accumulated other comprehensive income | 1,309 | (2,560) | 63 | (1,188) |
| Net other comprehensive income (loss) | 4,681 | (2,989) | 20,988 | 22,680 |
| Balance at June 30, 2015 | $9,286 | $12,202 | $(43,873) | $(22,385) |
| Balance at December 31, 2015 | $(31,002) | $10,561 | $(64,424) | $(84,865) |
| Other comprehensive income (loss) before reclassifications | **60,051** | **(161)** | **(115,261)** | **(55,371)** |
| Amounts reclassified from accumulated other comprehensive income | **174** | **(6,155)** | **--** | **(5,981)** |
| Net other comprehensive income (loss) | **60,225** | **(6,316)** | **(115,261)** | **(61,352)** |
| **Balance at June 30, 2016** | **$29,223** | **$4,245** | **$(179,685)** | **$(146,217)** |

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

| (in thousands)<br>Accumulated Other Comprehensive Income Components | Amount Reclassified from Accumulated Other Comprehensive Income | | Affected Line Item in the Statements of Comprehensive Income |
|---|---|---|---|
| **For the six months ended June 30,** | **2016** | 2015 | |
| Not-other-than-temporarily-impaired investments: | | | |
| Impairment losses | **$ --** | $73 | Net impairment losses recognized in earnings |
| Realized loss on sale of investment securities | **174** | 1,236 | Miscellaneous income and other gains, net |
| | **174** | 1,309 | |
| Other-than-temporarily-impaired investments: | | | |
| Realized gain on sale of investment securities | **(6,155)** | (2,560) | Miscellaneous income and other gains, net |
| Derivatives and hedging activity: | | | |
| Interest rate contracts | **--** | 63 | Interest expense |
| Total reclassifications | **$(5,981)** | $(1,188) | |

## NOTE 10

# Subsequent Events

We have evaluated subsequent events through August 9, 2016, which is the date the Financial Statements were available to be issued.

- On July 15, 2016, we redeemed all $500 million of outstanding subordinated notes at par value. Refer to Note 4 for additional information related to the redemption of our subordinated notes.
- Effective August 1, 2016, William J. Thone has been named interim Chief Executive Officer (CEO) of AgriBank following the departure of Bill York, who left AgriBank as CEO on July 25, 2016.

There have been no other material subsequent events that would require recognition in the Quarterly Financial Statements or disclosure in the Notes to those Financial Statements.

AgriBank
FARM CREDIT BANK

30 East 7th Street, Suite 1600 | St. Paul, MN 55101 | www.AgriBank.com