

# **SECOND QUARTER 2007**

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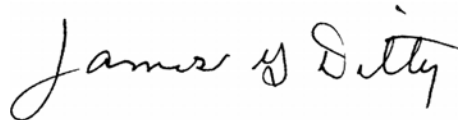
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James R. Alberts  
Chief Executive Officer



James G. Ditty  
Chairman of the Board

July 27, 2007

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

*(dollars in thousands)*

The following commentary reviews the financial condition and results of operations of Farm Credit of Northwest Florida, ACA (Association) for the period ended June 30, 2007. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2006 Annual Report of the Association.

## **LOAN PORTFOLIO**

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities including forestry, row crops, livestock peanuts, horticulture, dairies and rural homes. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm income in the area, somewhat reduces the level of dependency on any single commodity.

The gross loan volume of the Association as of June 30, 2007, was \$519,926, an increase of \$22,479, as compared to \$497,447 at December 31, 2006. Net loans outstanding (gross loans net of the allowance for loan losses) at June 30, 2007, were \$518,352 as compared to \$495,873 at December 31, 2006. Net loans accounted for 95.98 percent of total assets at June 30, 2007, as compared to 95.07 percent of total assets at December 31, 2006.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level, however, and credit administration remains satisfactory. Nonaccrual loan volume was \$1,370 at June 30, 2007 and \$940 at December 31, 2006.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at June 30, 2007 was \$1,574, unchanged from the allowance for loan losses at December 31, 2006. The allowance for loan loss of \$1,574 at June 30, 2007 was considered by management to be adequate to cover probable losses.

## **RESULTS OF OPERATIONS**

### ***For the three months ended June 30, 2007***

Net income for the three months ended June 30, 2007, totaled \$3,574 as compared to \$3,110 for the same period in 2006. Net interest income increased \$61 for the three months ended June 30, 2007, as compared to the same period in 2006. Increased loan volume was the primary reason for this increase in net interest income.

Noninterest income for the three months ended June 30, 2007, totaled \$1,211, as compared to \$988 for the same period of 2006, an increase of \$223. The increase is primarily the result of an increase of \$268 in Equity in Earnings of other Farm Credit institutions and a decrease of \$48 in loan fee income. Noninterest expense for the three months ended June 30, 2007, decreased \$111 compared to the same period of 2006. Income tax expense increased by \$61 for the three months ended June 30, 2007 as compared to the same period of 2006.

### ***For the six months ended June 30, 2007***

Net income for the six months ended June 30, 2007, totaled \$7,105, as compared to \$6,111 for the same period in 2006. At June 30, 2007, net interest income increased by \$311 or 4.42 percent compared to June 30, 2006. At June 30, 2007 interest income on loans increased by \$2,372 and interest expense on notes payable increased by \$2,006 compared to June 30, 2006. This change in net interest income is the result of increased loan volume.

The Association recorded no provision for loan loss for the six months ended June 30, 2007, as compared to \$177 for the same period in 2006.

Noninterest income for the six months ended June 30, 2007, totaled \$2,424, as compared to \$1,952 for the same period of 2006, an increase of \$472. The increase is primarily the result of an increase of \$658 in Equity in Earnings of other Farm Credit institutions and a decrease of \$201 in loan fee income. Noninterest expense for the six months ended June 30, 2007, decreased \$151 compared to the same period of 2006. The primary reasons for the decrease in noninterest expense were a decrease in salaries and benefits of \$211, an increase of \$33 in Insurance Fund premiums, an increase in occupancy and equipment of \$13 and an increase of \$14 in other operating expenses.

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## FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (the Bank) through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at June 30, 2007, was \$462,759 as compared to \$445,110 at December 31, 2006.

## CAPITAL RESOURCES

Total members' equity at June 30, 2007, increased to \$71,091 from the December 31, 2006, total of \$64,272. The increase is primarily attributed to net income of \$7,105 for the six months ended June 30, 2007.

Total capital stock and participation certificates were \$1,320 on June 30, 2007, compared to \$1,415 on December 31, 2006. This decrease is attributed to capital stock and participation certificates retirements of \$178 and issuances of \$83.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2007, the Association's total surplus ratio and core surplus ratio were 11.48 percent and 10.91 percent, respectively, and the permanent capital ratio was 11.74 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

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**NOTE:** Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 316, or writing Wanda Martin, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, [www.agfirst.com](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 850-526-4910 ext. 103, or writing Bruce C. Harrison, Chief Financial Officer, Farm Credit of Northwest Florida, ACA, P.O. Box 7000, Marianna, FL 32447, or accessing the website, [www.farmcredit-fl.com](http://www.farmcredit-fl.com). The Association prepares a quarterly report within 45 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

*Farm Credit fo Northwest Florida, ACA*  
**Consolidated Balance Sheets**

<i>(dollars in thousands)</i>	<b>June 30, 2007</b> <i>(unaudited)</i>	<b>December 31, 2006</b> <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 103	\$ 968
Loans	519,926	497,447
Less: allowance for loan losses	1,574	1,574
Net loans	518,352	495,873
Accrued interest receivable	5,639	6,325
Investment in other Farm Credit institutions	9,399	9,591
Premises and equipment, net	1,777	1,804
Prepaid retirement expense	1,935	2,071
Due from AgFirst Farm Credit Bank	2,264	4,300
Other assets	618	662
Total assets	<u>\$ 540,087</u>	<u>\$ 521,594</u>
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 462,759	\$ 445,110
Accrued interest payable	2,239	2,233
Patronage refund payable	7	5,549
Other liabilities	3,991	4,430
Total liabilities	<u>468,996</u>	<u>457,322</u>
Commitments and contingencies		
<b>Members' Equity</b>		
Protected borrower equity	24	33
Capital stock and participation certificates	1,296	1,382
Retained earnings		
Allocated	42,756	43,299
Unallocated	27,015	19,558
Total members' equity	<u>71,091</u>	<u>64,272</u>
Total liabilities and members' equity	<u>\$ 540,087</u>	<u>\$ 521,594</u>

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

*Farm Credit of Northwest Florida, ACA*  
**Consolidated Statements of Income**

(unaudited)

<i>(dollars in thousands)</i>	<b>For the three months ended June 30,</b>		<b>For the six months ended June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>Interest Income</b>				
Loans	\$ 10,437	\$ 9,816	\$ 20,671	\$ 18,299
<b>Interest Expense</b>				
Notes payable to AgFirst Farm Credit Bank	6,689	6,162	13,174	11,168
Other	81	48	156	101
Total interest expense	6,770	6,210	13,330	11,269
Net interest income	3,667	3,606	7,341	7,030
Provision for (reversal of allowance for) loan losses	—	130	—	177
Net interest income after provision for (reversal of allowance for) loan losses	3,667	3,476	7,341	6,853
<b>Noninterest Income</b>				
Loan fees	68	116	108	309
Equity in earnings of other Farm Credit institutions	1,138	870	2,271	1,613
Other noninterest income	5	2	45	30
Total noninterest income	1,211	988	2,424	1,952
<b>Noninterest Expense</b>				
Salaries and employee benefits	699	801	1,377	1,588
Occupancy and equipment	81	72	163	150
Insurance Fund premium	189	181	373	340
Other operating expenses	264	290	613	599
Total noninterest expense	1,233	1,344	2,526	2,677
Income before income taxes	3,645	3,120	7,239	6,128
Provision (benefit) for income taxes	71	10	134	17
Net income	\$ 3,574	\$ 3,110	\$ 7,105	\$ 6,111

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

*Farm Credit fo Northwest Florida, ACA*

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

*(dollars in thousands)*

	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings		Total Members' Equity
			Allocated	Unallocated	
Balance at December 31, 2005	\$ 45	\$ 1,419	\$ 37,394	\$ 17,164	\$ 56,022
Net income				6,111	6,111
Protected borrower equity retired	(12)				(12)
Capital stock/participation certificates issued		118			118
Capital stock/participation certificates retired		(228)			(228)
Retained earnings retired			(658)		(658)
Distribution adjustment			(195)	275	80
Balance at June 30, 2006	\$ 33	\$ 1,309	\$ 36,541	\$ 23,550	\$ 61,433
Balance at December 31, 2006	\$ 33	\$ 1,382	\$ 43,299	\$ 19,558	\$ 64,272
Net income				7,105	7,105
Protected borrower equity retired	(9)				(9)
Capital stock/participation certificates issued		83			83
Capital stock/participation certificates retired		(169)			(169)
Retained earnings retired			(632)		(632)
Distribution adjustment			89	352	441
Balance at June 30, 2007	\$ 24	\$ 1,296	\$ 42,756	\$ 27,015	\$ 71,091

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

# Notes to the Consolidated Financial Statements

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

## NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

A description of the organization and operations of Farm Credit of Northwest Florida, ACA (the Association), the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2006, are contained in the 2006 Annual Report to Shareholders. These unaudited second quarter 2007 consolidated financial statements should be read in conjunction with the 2006 Annual Report to Shareholders.

On September 29, 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 – Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans. The Standard requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in that funded status in the year in which the changes occur through comprehensive income. The Standard is effective for employers with publicly traded securities for the fiscal year ending after December 15, 2006 and for employers without publicly traded securities for the fiscal year ending after June 15, 2007. The Association will be required to implement the Standard for the year ended December 31, 2007. In addition, this Standard requires that the funded status of a plan be measured as of the date of the year-end financial statements. Currently, the Association uses a measurement date of September 30th. The requirement to measure the funded status as of the fiscal year-end is effective for fiscal years ending after December 15, 2008. The Association is currently evaluating the impact of implementing this Standard. It is anticipated that the impact from the implementation of this Standard will have no impact on the consolidated income statement and, based on the current funded status of the defined benefit plans, it is not expected to have a material or significant impact on the consolidated balance sheet.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles. The results for the six months ended June 30, 2007, are not necessarily indicative of the results to be expected for the year ending December 31, 2007.

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

The Association maintains an allowance for loan losses in accordance with generally accepted accounting principles. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of June 30, 2007, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

## NOTE 2 – ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses follows:

	For the six months ended June 30,	
	2007	2006
Balance at beginning of period	\$ 1,574	\$ 1,409
Provision for (reversal of) loan losses	–	177
Loans (charged off), net of recoveries	–	–
Balance at end of period	<u>\$ 1,574</u>	<u>\$ 1,586</u>

## NOTE 3 – COMMITMENTS AND CONTINGENT LIABILITIES

Actions are pending against the Association in which money damages are sought. However, on the basis of information now at hand, management and legal counsel are of the opinion that the ultimate liability, if any, resulting therefrom, would not be material in relation to the overall financial position of the Association.

## NOTE 4 – EMPLOYEE BENEFIT PLANS

The Association participates in a Districtwide defined benefit retirement plan. The costs of the plan are not segregated by participating entities but are allocated among the participating entities. Pension costs are allocated by multiplying the District's net pension expense times each institution's salary expense as a percentage of the District's salary expense. The Association also participates in Districtwide Thrift and other postretirement benefit plans.

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The following is a table of retirement and postretirement benefit expense:

	<b>For the six months ended June 30,</b>	
	<b>2007</b>	<b>2006</b>
Pension	\$ 137	\$ 177
Thrift/deferred compensation	43	40
Other postretirement benefits	38	39
Total	<u>\$ 218</u>	<u>\$ 256</u>

As of June 30, 2007, no contributions have been made to the pension plan for 2007. Actuarial projections as of the last plan measurement date (September 30, 2006) did not anticipate any contributions for 2007; however, market conditions could impact discount rates and return on plan assets which could change this expectation, making contributions necessary before the next plan measurement date.