2023

Second Quarter
Report To Shareholders

Colusa-Glenn Farm Credit

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(Unaudited)

The following discussion summarizes the financial position and results of operations of Farm Credit Services of Colusa-Glenn, ACA (the "Association") and subsidiaries for the six months ended June 30, 2023, with comparisons to prior periods. You should read these comments along with the accompanying financial statements and footnotes and the 2022 Annual Report to Shareholders. The accompanying financial statements were prepared under the oversight of our Audit Committee.

The shareholders' investment in Farm Credit Services of Colusa-Glenn, ACA is materially affected by the financial condition and results of operations of CoBank, ACB, (CoBank). The 2022 CoBank Annual Report to Shareholders and the CoBank quarterly shareholders' reports are available free of charge by accessing CoBank's website, www.cobank.com, or may be obtained at no charge by contacting us at Farm Credit Services of Colusa-Glenn, ACA, 2970 Davison Court, Colusa, California 95932, or calling (530) 458-2163.

GENERAL

We have continued to grow and diversify our loan portfolio, maintain good credit quality, effectively manage operating costs, and remain well capitalized through the six months ended June 30, 2023. Our success is due, in part, to our conservative lending approach, the financial stability and support of our member-base, proactive portfolio risk management, and our commitment to providing excellent customer service. The Association and its members continue to face challenges from commodity price and supply instability, uncertainty of long-term water supplies, the high cost of farm inputs, and interest rate volatility. The most significant factors currently impacting our portfolio are the deterioration of economic conditions and market volatility. Our primary concern is their impact on our members' working capital, overall financial position, and the collateral values supporting our loans. We continue to monitor changes in market conditions impacting the agricultural products we finance to ensure that we provide the best customer service to our members while operating in a safe and sound manner.

While the U.S. economy remains healthy, supply chain disruptions, labor shortages, fuel prices, inflation, rising interest rates, weather related events, and recession pressures remain a concern. Although inflation has remained high in 2023, it has remained relatively stable in the second quarter of 2023, leading to an increase in consumer spending. The rural economy continues to benefit from the strong U.S. economy, driving higher levels of spending and investment by businesses and consumers. Most agricultural commodity prices have remained strong despite some decline from the sharp increases in 2022. The Russia/Ukraine conflict has also impacted certain agricultural commodity prices and created additional volatility and uncertainty in the markets. From a monetary policy perspective, the Fed has continued to fight inflationary pressure with interest rate hikes, resulting in three interest rate increases in 2023 of 25 basis points each and more expected in the future. Anticipation of tighter monetary policy is contributing to a stronger dollar and changes in the shape of the yield curve.

LOAN PORTFOLIO

Loans outstanding at June 30, 2023, totaled $687.7 million, an increase of $12.7 million, or 1.9%, from loans of $675.0 million at December 31, 2022. The increase was attributable to increased participations purchased combined with increased commercial loan utilization.

RESULTS OF OPERATIONS

Net income for the six months ended June 30, 2023, was $7.5 million, an increase of $2.3 million, or 44.5%, from $5.2 million for the six months ended June 30, 2022. The increase was due to increased net interest income and noninterest income, partially offset by increased provision for credit losses and noninterest expense.

Net interest income for the six months ended June 30, 2023, was $10.6 million, an increase of $2.8 million, or 37.2%, from $7.8 million for the six months ended June 30, 2022. The increase was driven by higher earnings on our own capital.

The provision for credit losses for the six months ended June 30, 2023, was $564 thousand, an increase of $373 thousand from $191 thousand for the same period ended one year ago. The provision for credit losses through June 30, 2023, was primarily due to specific reserves totaling $429 thousand related to one participation borrower, with the remaining provision driven by deteriorated credit quality. The provision for credit losses for the six months ended June 30, 2022, was due to increased commitments and increased reserves associated with probable incurred losses related to sustained drought conditions and frost damage to the almond crop in early 2022. The increased reserves as of June 30, 2022, were partially offset by loan loss recoveries of $205 thousand.

Noninterest income for the six months ended June 30, 2023, was $1.5 million, an increase of $231 thousand, or 17.9%, from $1.3 million for the same period ended one year ago. This was primarily due to increased patronage income and other noninterest income. Patronage distribution from Farm Credit institutions increased in the first six months ended June 30, 2023, compared with the first six months in 2022 primarily due to increased patronage from CoBank and from other association participation partners. Patronage income from CoBank has increased due to an increase in our direct note volume. Other noninterest income increased year over year primarily due to increased loan fee income and gains on the disposal of fixed assets, partially offset by decreased earnings from our captive insurance.

Noninterest expense for the six months ended June 30, 2023, was $4.1 million, an increase of $440 thousand, or 12.0%, from $3.7 million for the six months ended June 30, 2022. The increase was primarily due to increased salary and employee benefits, purchased services, Farm Credit insurance fund premiums, and decreased other noninterest income. Salaries and employee benefits expense increased due to annual merit and cost of living adjustments. Purchased services have increased due to outsourced appraisal costs and increased audit fees. Farm Credit System Insurance Corporation (FCSIC) premiums increased $11 thousand for the six months ended June 30, 2023, compared with the same period in 2022 primarily due an increase in average loan volume. Other noninterest income decreased due to increased director expenses, training, and travel expenses.

CAPITAL RESOURCES

Our shareholders' equity at June 30, 2023, was $142.6 million, an increase of $5.6 million, or 4.0%, from shareholders' equity of $137.0 million at December 31, 2022. This increase is due to net income, a one-time increase in unallocated retained earnings for the adoption of the new standard on current expected credit losses (CECL), and net stock issuances, offset by accrued patronage distributions.

OTHER MATTERS

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

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

While our Association currently holds legacy LIBOR indexed loans in our portfolio, we have adopted a transition plan to reduce LIBOR exposures and stop the inflow of new LIBOR volume. We have analyzed potential risks associated with the LIBOR transition, including financial, operational, legal, tax, reputational, and compliance risks. Since we engage in transactions involving financial instruments that reference LIBOR, these developments did not have a material impact on the Association and our borrowers. Management has documented and worked through the LIBOR transition plan with our funding bank and service provider to address the phase out of LIBOR rates, including any updates to processes and loan servicing technology. All exposure to LIBOR is related to our participations purchased portfolio.

FORWARD LOOKING INFORMATION

This discussion contains forward looking statements. These statements are not guarantees of future performance; future operations involve certain risks, uncertainties, and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," or "will" are intended to identify forward-looking statements. These statements are based on management's assumptions and analyses made in light of experience and other historical trends, current conditions, and expected future developments. However, actual results and developments may differ materially from our expectations and predictions due to a number of risks and uncertainties, many of which are beyond our control. Readers are cautioned not to place undue reliance on these forward-looking statements. We will not update any forward-looking statements to reflect events or circumstances arising after they are made.

CERTIFICATION

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

Michael Doherty
Chairman of the Board
August 9, 2023

Tim Elrod
President & Chief Executive Officer
August 9, 2023

Amy Ceballos
Chief Financial Officer
August 9, 2023

CONSOLIDATED STATEMENTS OF CONDITION

(In Thousands)

	June 30, 2023 *Unaudited*	December 31, 2022 *Audited*
ASSETS		
Loans	$ 687,672	$ 675,007
Less allowance for loan losses	1,938	2,075
Net loans	685,734	672,932
Cash	221	3,436
Accrued interest receivable	12,981	9,754
Investment in CoBank, ACB	14,026	13,975
Premises and equipment, net	6,746	6,608
Other assets	3,458	4,965
Total assets	$ 723,166	$ 711,670
LIABILITIES		
Note payable to CoBank, ACB	$ 534,237	$ 519,700
Advance conditional payments	37,780	42,551
Accrued interest payable	1,908	1,423
Patronage distributions payable	2,468	5,000
Accrued benefits liability	93	95
Deferred tax liability	439	333
Unfunded disbursements	1,260	1,624
Reserve for unfunded commitments	499	407
Other liabilities	1,921	3,504
Total liabilities	580,605	574,637
Commitments and Contingencies		
SHAREHOLDERS' EQUITY		
Capital stock and participation certificates	549	544
Unallocated retained earnings	142,012	136,489
Total shareholders' equity	142,561	137,033
Total liabilities and shareholders' equity	$ 723,166	$ 711,670

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited and in Thousands)

	For the Three Months Ended June 30		For the Six Months Ended June 30	
	2023	2022	2023	2022
INTEREST INCOME				
Loans	$ 11,374	$ 5,493	$ 21,950	$ 10,151
Total interest income	11,374	5,493	21,950	10,151
INTEREST EXPENSE				
Note payable to CoBank, ACB	5,622	1,470	10,509	2,316
Other	429	45	792	73
Total interest expense	6,051	1,515	11,301	2,389
Net interest income	5,323	3,978	10,649	7,762
Provision for credit losses	17	174	564	191
Net interest income after provision for credit losses	5,306	3,804	10,085	7,571
NONINTEREST INCOME				
Financially related services income	2	2	2	2
Patronage distribution from Farm Credit Institutions	611	559	1,375	1,233
Mineral income	1	-	1	1
Other noninterest income	85	23	143	54
Total noninterest income	699	584	1,521	1,290
NONINTEREST EXPENSE				
Salaries and employee benefits	1,050	974	2,178	1,996
Occupancy and equipment	158	134	297	274
Purchased services	163	132	404	272
Farm Credit Insurance Fund premium	211	251	424	413
Supervisory and examination costs	66	60	132	120
Data processing services	358	346	719	693
Other noninterest income, net	(21)	(79)	(40)	(94)
Total noninterest expense	1,985	1,818	4,114	3,674
Income before income taxes	4,020	2,570	7,492	5,187
Provision for income taxes	2	3	4	5
Net income/Comprehensive income	$ 4,018	$ 2,567	$ 7,488	$ 5,182

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS’ EQUITY

(Unaudited and in Thousands)

	Capital Stock and Participation Certificates	Unallocated Retained Earnings	Total Shareholders' Equity
Balance at December 31, 2021	$ 538	$ 128,924	$ 129,462
Net income/Comprehensive income		5,182	5,182
Capital stock and participation certificates issued	30		30
Capital stock and participation certificates retired	(25)		(25)
Patronage distributions: Cash		(2,210)	(2,210)
Balance at June 30, 2022	$ 543	$ 131,896	$ 132,439
Balance at December 31, 2022	$ 544	$ 136,489	$ 137,033
Net income/Comprehensive income		7,488	7,488
Capital stock and participation certificates issued	22		22
Capital stock and participation certificates retired	(17)		(17)
Patronage distributions: Cash		(2,468)	(2,468)
Cumulative effect of CECL adoption		503	503
Balance at June 30, 2023	$ 549	$ 142,012	$ 142,561

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited and in Thousands, Except Where Noted)

NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

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

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

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

Recently Adopted or Issued Accounting Pronouncements

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

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

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

	December 31, 2022	CECL Adoption Impact	January 1, 2023
Assets:			
Allowance for credit losses on loans	$ 2,075	$ (830)	$ 1,245
Deferred tax assets	-	-	-
Liabilities:			
Allowance for credit losses on unfunded commitments	$ 407	$ 221	$ 628
Deferred tax liabilities	333	106	439
Retained earnings:			
Unallocated retained earnings, net of tax	$ 136,489	$ 503	$ 136,992

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

Loans and Allowance for Credit Losses

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

Nonaccrual Loans

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

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

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

Accrued Interest Receivable

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

Loan Modifications to Borrowers Experiencing Financial Difficulty

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

Collateral-Dependent Loans

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

Allowance for Credit Losses

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

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

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

Methodology for Allowance for Credit Losses on Loans

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

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

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

In estimating the pooled component of the ACLL for loan pools that share common risk characteristics, loans are evaluated collectively and segregated into loan pools considering the risk associated with the specific pool. Relevant risk characteristics include loan type, commodity, quality rating, delinquency category, or business segment or a combination of these classes. The allowance is determined based on a quantitative calculation of the expected life-of-loan loss percentage for each loan category by considering the probability of default and the severity of loss given default. Loss given default is determined for each pool based on the aggregate net lifetime losses incurred within that pool. A default is considered to have occurred if the lender believes the borrower will not be able to pay its obligation in full or the loan is 90 days or more past due. Due to limited loss history across the portfolio, the Association used peer data within their quantitative adjustment component for loan pools that have experienced minimal loss history.

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

- lending policies and procedures,
- national, regional, and local economic business conditions, and developments that affect the collectability of the portfolio, including the condition of various markets,
- the nature of the loan portfolio, including the terms of the loans,
- the experience, ability, and depth of the lending management and other relevant staff,
- the volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans,
- the quality of the loan review and process,
- the value of underlying collateral for collateral-dependent loans,
- the existence and effect of any concentrations of credit and changes in the level of such concentrations, and,
- the effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

The Association uses a single economic scenario over reasonable and supportable forecast period of 12 months. Subsequent to the forecast period, the Association reverts to long-run historical loss experience beyond the 12 months, utilizing an accumulated quarter method to inform the estimate of losses for the remaining contractual life of the loan portfolio.

The economic forecasts are updated on a quarterly basis and incorporate macroeconomic variables, including agricultural commodity prices, unemployment rates, Gross Domestic Product (GDP) annual growth rates, government spending to GDP, real consumer spending, United States exports, inflation, and Fed Funds rates. Also considered are portfolio trends, competition and legal factors, collateral values, nature and volume of loan concentrations, and loan underwriting and collection reviews.

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

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

Allowance for Credit Losses on Unfunded Commitments

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

NOTE 2 - LOANS AND ALLOWANCE FOR CREDIT LOSSES

Loan Portfolio

A summary of the Association's loan portfolio as of June 30, 2023, and December 31, 2022, is as follows:

	June 30, 2023	December 31, 2022
Real estate mortgage	$ 365,486	$ 368,375
Production and intermediate-term	121,473	124,361
Agribusiness	144,274	129,477
Rural infrastructure	51,439	47,794
Agricultural export finance	5,000	5,000
Total loans	$ 687,672	$ 675,007

Participations Purchased and Sold

The Association purchases and sells participation interests with other parties in order to diversify risk, manage loan volume, and comply with Farm Credit Administration regulations. The following table presents information regarding the principal balances of participations purchased and sold as of June 30, 2023, and December 31, 2022:

	June 30, 2023		December 31, 2022	
	Purchased	Sold	Purchased	Sold
Other Farm Credit Institutions:				
Real estate mortgage	$ 73,387	$ 63,185	$ 71,871	$ 64,121
Production and intermediate-term	26,036	7,413	29,151	6,727
Agribusiness	84,098	22,097	76,190	6,522
Rural infrastructure	51,439	-	47,794	-
Agricultural export finance	5,000	-	5,000	-
Subtotal	239,960	92,695	230,006	77,370
Other Non-Farm Credit Institutions:				
Agribusiness	7,957	-	8,987	-
Subtotal	7,957	-	8,987	-
All Institutions:				
Real estate mortgage	73,387	63,185	71,871	64,121
Production and intermediate-term	26,036	7,413	29,151	6,727
Agribusiness	92,055	22,097	85,177	6,522
Rural infrastructure	51,439	-	47,794	-
Agricultural export finance	5,000	-	5,000	-
Total	$ 247,917	$ 92,695	$ 238,993	$ 77,370

Credit Quality

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

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

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

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

The following table shows loans under the Farm Credit Administration Uniform Loan Classification System as a percentage of total loans by loan type as of June 30, 2023, and December 31, 2022:

	June 30, 2023	December 31, 2022[1]
Real estate mortgage:		
Acceptable	92.54%	96.74%
OAEM	3.56%	3.13%
Substandard	3.90%	0.13%
Subtotal	100.00%	100.00%
Production and intermediate-term:		
Acceptable	86.75%	92.45%
OAEM	5.65%	7.55%
Substandard	7.60%	-
Subtotal	100.00%	100.00%
Agribusiness:		
Acceptable	96.48%	98.35%
OAEM	2.24%	1.65%
Substandard	1.28%	0.00%
Subtotal	100.00%	100.00%
Rural infrastructure:		
Acceptable	100.00%	100.00%
Subtotal	100.00%	100.00%
Agricultural export finance:		
Acceptable	100.00%	100.00%
Subtotal	100.00%	100.00%
Total Loans:		
Acceptable	92.96%	96.52%
OAEM	3.36%	3.41%
Substandard	3.68%	0.07%
Total	100.00%	100.00%

[1] Prior to the adoption of CECL on January 1, 2023, loans were presented with accrued interest receivable.

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

Nonperforming Assets

Nonperforming assets consist of nonaccrual loans, accruing loans 90 days or more past due, and other property owned. The following table shows these nonperforming assets and related credit quality statistics as of June 30, 2023.

	June 30, 2023
Nonaccrual loans:	
Agribusiness	$ 1,842
Total nonperforming assets	$ 1,842
Nonaccrual loans to total loans	0.27%
Nonperforming assets to total loans and other property owned	0.27%
Nonperforming assets to total shareholders' equity	1.29%

The Association had no accruing loans 90 days past due and no other property owned as of June 30, 2023, and no nonaccrual loans, no accruing loans 90 days past due, and no other property owned as of December 31, 2022.

The following tables provide the amortized cost for nonaccrual loans with and without a related allowance for loan losses:

	June 30, 2023		
	Amortized Cost with Allowance	Amortized Cost without Allowance	Total
Nonaccrual loans:			
Agribusiness	$ 1,842	$ -	$ 1,842
Total	$ 1,842	$ -	$ 1,842

The Association recognized no interest income on nonaccrual loans during the three and six months ended June 30, 2023.

Past Due Loans

The following tables provide an age analysis of past due loans at amortized cost as of June 30, 2023, and December 31, 2022:

As of June 30, 2023	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	Recorded Investment Accruing Loans 90 Days or More Past Due
Real estate mortgage	$ -	$ -	$ -	$ 365,486	$ 365,486	$ -
Production and intermediate-term	-	-	-	121,473	121,473	-
Agribusiness	-	1,842	1,842	142,432	144,274	-
Rural infrastructure	-	-	-	51,439	51,439	-
Agricultural export finance	-	-	-	5,000	5,000	-
Total	$ -	$ 1,842	$ 1,842	$ 685,830	$ 687,672	$ -

Prior to the adoption of CECL on January 1, 2023, the age analysis of past due loans included accrued interest as follows:

As of December 31, 2022	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	Recorded Investment Accruing Loans 90 Days or More Past Due
Real estate mortgage	$ 188	$ -	$ 188	$ 375,613	$ 375,801	$ -
Production and intermediate-term	2	-	2	125,379	125,381	-
Agribusiness	-	-	-	130,661	130,661	-
Rural infrastructure	-	-	-	47,878	47,878	-
Agricultural export finance	-	-	-	5,040	5,040	-
Total	$ 190	$ -	$ 190	$ 684,571	$ 684,761	$ -

Allowance for Loan Losses

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

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

	Balance at March 31, 2023	Charge-offs	Recoveries	Provision for Loan Losses/ (Loan Loss Reversals)	Balance at June 30, 2023
Real estate mortgage	$ 531	$ -	$ -	$ 11	$ 542
Production and intermediate-term	476	-	-	(36)	440
Agribusiness	709	-	-	(1)	708
Rural infrastructure	88	-	-	160	248
Total	$ 1,804	$ -	$ -	$ 134	$ 1,938

	Balance at December 31, 2022	Cumulative Effect of CECL Adoption	Balance at January 1, 2023	Charge-offs	Recoveries	Provision for Loan Losses	Balance at June 30, 2023
Real estate mortgage	$ 689	$ (167)	$ 522	$ -	$ -	$ 20	$ 542
Production and intermediate-term	843	(517)	326	-	-	114	440
Agribusiness	481	(178)	303	-	-	405	708
Rural infrastructure	56	38	94	-	-	154	248
Agricultural export finance	6	(6)	-	-	-	-	-
Total	$ 2,075	$ (830)	$ 1,245	$ -	$ -	$ 693	$ 1,938

	Balance at March 31, 2022	Charge-offs	Recoveries	Provision for Loan Losses/ (Loan Loss Reversals)	Balance at June 30, 2022
Real estate mortgage	$ 507	$ -	$ -	$ (19)	$ 488
Production and intermediate-term	1,123	-	-	51	1,174
Agribusiness	319	-	-	164	483
Rural infrastructure	55	-	-	(2)	53
Agricultural export finance	6	-	-	(1)	5
Total	$ 2,010	$ -	$ -	$ 193	$ 2,203

	Balance at December 31, 2021	Charge-offs	Recoveries	Provision for Loan Losses/ (Loan Loss Reversals)	Balance at June 30, 2022
Real estate mortgage	$ 291	$ -	$ -	$ 197	$ 488
Production and intermediate-term	1,226	18	205	(239)	1,174
Agribusiness	279	-	-	204	483
Rural infrastructure	55	-	-	(2)	53
Agricultural export finance	6	-	-	(1)	5
Total	$ 1,857	$ 18	$ 205	$ 159	$ 2,203

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

Reserve for Unfunded Commitments

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

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

	For the Three Months Ended June 30, 2023	For the Six Months Ended June 30, 2023
Balance at beginning of period	$ 616	$ 407
Cumulative Effect of CECL Adoption		221
Balance at January 1, 2023		628
Reversal of reserves for unfunded commitments	(117)	(129)
Total	$ 499	$ 499

	For the Three Months Ended June 30, 2022	For the Six Months Ended June 30, 2022
Balance at December 31, 2021	$ 355	$ 304
(Reversal of)/Provision for reserves for unfunded commitments	(19)	32
Total	$ 336	$ 336

Loan Modifications to Borrowers Experiencing Financial Difficulties

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

The following tables show the amortized cost basis at June 30, 2023, for loan modifications granted to borrowers experiencing financial difficulty, disaggregated by loan type and type of modification granted:

	Term or Payment Extension			
	For the Three Months Ended		For the Six Months Ended	
	June 30, 2023	% of Total Loans by Type	June 30, 2023	% of Total Loans by Type
Real estate mortgage	$ -	-	$ 3,995	1.09%
Production and intermediate-term	9,227	7.60%	9,227	7.60%
Total	$ 9,227	7.60%	$ 13,222	8.69%

Accrued interest receivable related to loan modifications granted to borrowers experiencing financial difficulty as of the three and six months ended June 30, 2023, was $168 thousand and $303 thousand, respectively.

The following table describes the financial effect of the modifications made to borrowers experiencing financial difficulty during the three and six months ended June 30, 2023:

	Term or Payment Extension (in Days)	
	For the Three Months Ended June 30, 2023	For the Six Months Ended June 30, 2023
Real estate mortgage	-	365
Production and intermediate-term	333	333

None of the loans to borrowers experiencing financial difficulty that received a modification during the three and six months ended June 30, 2023, defaulted in the period presented.

The following table sets forth an aging analysis of loans to borrowers experiencing financial difficulty that were modified on or after January 1, 2023, the date of the adoption of the guidance noted above, through June 30, 2023:

	Payment Status of Loans Modified in the Past Six Months		
	Current	30-89 Days Past Due	90 Days or More Past Due
Real estate mortgage	$ 3,995	$ -	$ -
Production and intermediate-term	9,227	-	-
Total	$ 13,222	$ -	$ -

Additional commitments to lend to borrowers experiencing financial difficulty whose loans have been modified were $272 thousand at June 30, 2023.

Troubled Debt Restructuring

Prior to January 1, 2023, the adoption of updated FASB guidance on loan modifications, a restructuring of a loan constituted a troubled debt restructuring, also known as formally restructured, if the creditor for economic or legal reasons related to the borrower's financial difficulties granted a concession to the borrower that it would not otherwise consider. Concessions varied by program and were borrower-specific and could include interest rate reductions, term extensions, payment deferrals, or the acceptance of additional collateral in lieu of payments. In limited circumstances, principal may have been forgiven. When a restructured loan constituted a troubled debt restructuring, these loans were included within our impaired loans under nonaccrual or accruing restructured loans. The Association had no troubled debt restructures during 2022.

NOTE 3 - CAPITAL

The Association's unallocated retained earnings for the quarter ended June 30, 2023, reflects an increase from the cumulative effect of a change in accounting principle for CECL on January 1, 2023. The impact of adoption was not material to the Association's capital ratios. A summary of select capital ratios based on a three-month average and minimums set by the Farm Credit Administration is as follows:

	As of June 30, 2023	As of December 31, 2022	Regulatory Minimums	Capital Conservation Buffer	Total
Risk Adjusted:					
Common equity tier 1 ratio	15.79%	15.73%	4.5%	2.5%	7.0%
Tier 1 capital ratio	15.79%	15.73%	6.0%	2.5%	8.5%
Total capital ratio	16.09%	16.07%	8.0%	2.5%	10.5%
Permanent capital ratio	15.82%	15.78%	7.0%	-	7.0%
Non-Risk-Adjusted:					
Tier 1 leverage ratio	18.79%	18.65%	4.0%	1.0%	5.0%
Unallocated retained earnings and equivalents leverage ratio	18.71%	18.57%	1.5%	-	1.5%

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

NOTE 4 – FAIR VALUE MEASUREMENTS

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

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

	Fair Value Measurement Using			
	Level 1	Level 2	Level 3	Total Fair Value
Assets held in nonqualified benefits trusts:				
June 30, 2023	$ 4	$ -	$ -	$ 4
December 31, 2022	$ 4	$ -	$ -	$ 4

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

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

	Fair Value Measurement Using			
	Level 1	Level 2	Level 3	Total Fair Value
Loans:				
June 30, 2023	$ -	$ -	$ 1,413	$ 1,413
December 31, 2022	$ -	$ -	$ -	$ -

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

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

Valuation Techniques

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

Assets Held in Non-Qualified Benefits Trusts

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

Loans Evaluated for Impairment

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

NOTE 5 - SUBSEQUENT EVENTS

The Association has evaluated subsequent events through August 9, 2023, which is the date the financial statements were issued, and no material subsequent events were identified.

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