
PEE DEE FARM CREDIT, ACA

2002 ANNUAL REPORT

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Management

Jasper W. Shuler	President and Chief Executive Officer
Kathy S. Heustess.	Chief Financial Officer
William H. Wise, Jr.....	Chief Operating Officer
Richard H. Horn.....	Chief Credit Officer

Board of Directors

Dale W. Player	Chairman
Harry B. DuRant	Vice Chairman
DuPree Atkinson.....	Director
Leroy W. Baxley.....	Director
Dr. Morgan B. Coker	Director
W. Edwin Dargan, Jr.....	Director
Jimmy Poston.....	Director
James M. Ward	Director

Message from the President

Dear Stockholders and Friends of Pee Dee Farm Credit:

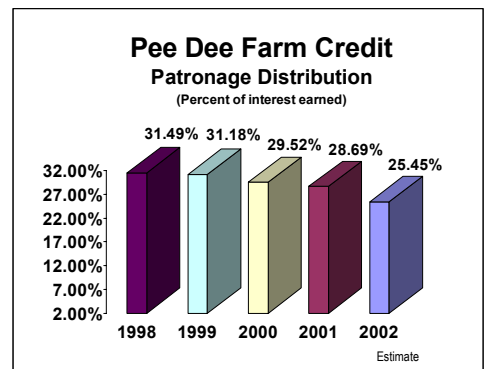
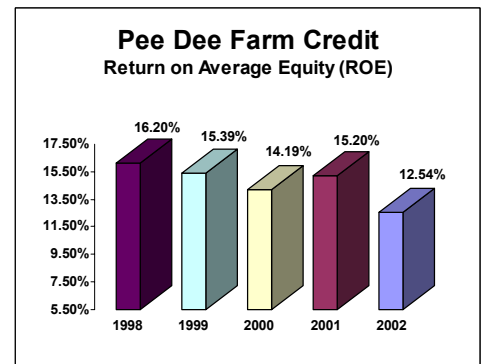
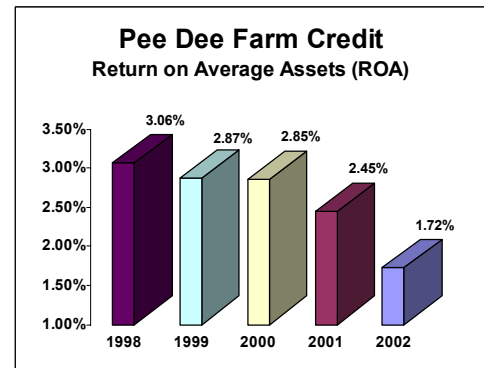
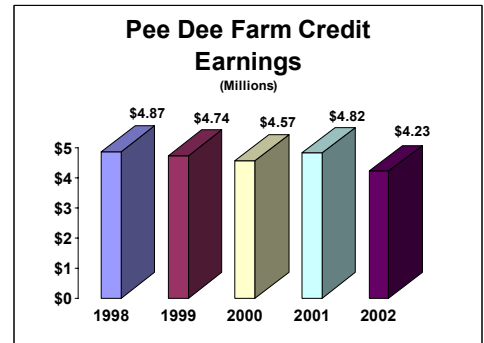
For many of our farmers, 2002 will be recorded as a challenging production year, possibly the most since the mid-80's or even the mid-50's. Many farmers were able to manage due to their financial position and by taking full advantage of risk management tools such as crop insurance. Despite last summer's drought and low prices, spirits are somewhat lifted looking down the road. We expect some rebound in the agricultural economy in 2003. Land values are expected to remain strong and interest rates stable, but may rise slightly toward the fourth quarter of 2003. We encourage farmers to take maximum advantage of the USDA farm programs, seek to understand the new farm bill and protect their investments with crop insurance.

Agriculture is moving in exciting directions. Biotechnology has just celebrated a 20-year milestone. The past 20 years has been an era of discovery to improve food, fiber and crop production. Nutraceuticals, pharmaceuticals, bio-engineering and alternative energy sources hold much promise for agriculture. Farmers of the future must think "outside the box" in relation to current commodities, supply chains and geographic distribution areas. The future belongs to those who see the possibilities before they become obvious. I believe biotechnology offers hope and growth for agriculture in South Carolina and the Pee Dee region.

Niche markets are also areas of interest for South Carolina agriculture including horticulture, turf grass and fruits and vegetable crops. The Pee Dee area and South Carolina have strong transportation systems in place including I-95, I-20, I-26, and I-85 as well as our port system. We must take advantage of these systems and expand our markets.

Agriculturalists must work to strengthen the cooperative network and move farmers up the value chain. There are so many advantages to farming cooperatives. Area farmers must appreciate how cooperatives can assist them by representing products, understand the services and structures provided by cooperatives such as globalization, complex business arrangements, technology and supply chains and realize how cooperatives can supply adequate capital to market products and services. Agriculture must hold strong to the competitive advantage cooperatives offer and learn to adapt, always looking for opportunities in the marketplace.

As did the industry we serve, Pee Dee Farm Credit had many challenges in 2002. We will not deny or ignore this fact. The weaknesses in our markets, the stressed agricultural economy as well as the rising cost of operations; more specifically employee health insurance, retirement benefits, increased loan portfolio insurance and additional funding



to the allowance for loan loss; all hurt earnings last year. In 2002, the Association's earnings slightly exceeded \$4.2 million, which translates into an ROE of 12.54 percent and a ROA of 1.72 percent. Given the downside, we still distributed the 1996 allocated surplus of \$1.7 million in December of 2002 and plan to distribute \$1.7 million of the 1997 allocated surplus in the fourth quarter of 2003. In April of 2003, we will pay 100 percent of patronage-sourced earnings from 2002 - 40 percent in cash. Fortunately, credit quality remained high at 98.51 percent acceptable, delinquencies low at .43 percent and our capital position is adequate at 13.53 percent. We grew our portfolio ADB (average daily balance) by \$49 million, exceeding our projections. The participations market contributed much of the growth to our portfolio in 2002. Another challenging year is ahead due to more uncontrollable expenses.

We continue investing in technology, features and services that benefit our customers and operating efficiencies. In 2002, we upgraded all systems to Windows 2000, adopted loan analysis and portfolio management software programs, introduced a customer information system (BERT), and an electronic filing system (ELF). We continued and will continue to improve and promote our customer conveniences including Account Access, Loan Line, AutoDraft and Agriline. These services help us serve our new and existing customers at the highest possible level. In the fall of 2002, we introduced our secondary mortgage market division, Carolina Home and Land. This new service will allow us to compete with commercial banks in the financing of homes especially those with acreage.

As we move into 2003, Pee Dee Farm Credit will continue to invest in projects that help us meet our performance goals, keying in on the growth of existing customers and new markets while producing profits. We will continue to manage our business soundly. Achieving revenue, growth and efficiency enhancements are number one priorities going forward.

Our management team ensures a work environment that fosters success of employees and we recognize the importance of personal growth and career enhancements. It involves adequate training and a high level of accountability. We know that at the core of our success are the deeds of our people. In the past year and over the next several to come, we have a number of employees reaching retirement after 30 to 35 years of service. We believe the tenure of our staff says a lot about the environment where our employees can learn, grow and be fulfilled in their work.

While there are many challenges ahead in both the agricultural and economic future, we will move forward with confidence and continue to be a high performance association. The future of our association depends on our ability to deliver superior value and returns to our stockholders along with unmatched quality service. We will continue to do our homework, consider all options complete with possible pitfalls and traps, and develop a strategy of opportunities that will expand and grow our business.

In closing, I'd like to express my sincere gratitude to the determination and wisdom of our board of directors, the diligent stewardship of our employees whose actions are rooted in integrity which reflects so positively on Pee Dee Farm Credit and to the first-rate customers we've had the privilege of serving. Best wishes on a prosperous 2003.



Jasper W. Shuler
President and Chief Executive Officer

February 19, 2003

Report of Management

The accompanying consolidated financial statements and related financial information appearing throughout this annual report have been prepared by management of Pee Dee Farm Credit, ACA (the Association) in accordance with generally accepted accounting principles appropriate in the circumstances. Amounts which must be based on estimates represent the best estimates and judgments of management. Management is responsible for the integrity, objectivity, consistency, and fair presentation of the consolidated financial statements and financial information contained in this report.

Management maintains and depends upon an internal accounting control system designed to provide reasonable assurance that transactions are properly authorized and recorded, that the financial records are reliable as the basis for the preparation of all financial statements, and that the assets of the Association are safeguarded. The design and implementation of all systems of internal control are based on judgments required to evaluate the costs of controls in relation to the expected benefits and to determine the appropriate balance between these costs and benefits. The Association maintains an internal audit program to monitor compliance with the systems of internal accounting control. Audits of the accounting records, accounting systems and internal controls are performed and internal audit reports including appropriate recommendations for improvement, are submitted to the Board of Directors.

The consolidated financial statements have been examined by independent public accountants, whose report appears elsewhere in this annual report. The Association is also subject to examination by the Farm Credit Administration.

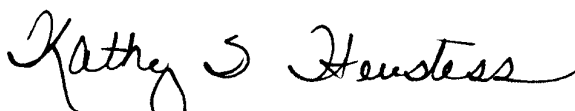
The consolidated financial statements, in the opinion of management, fairly present the financial condition of the Association. The undersigned certify that the 2002 Annual Report has been prepared in accordance with all applicable statutory or regulatory requirements and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



Dale W. Player
Chairman of the Board



Jasper W. Shuler
Chief Executive Officer



Kathy S. Heustess
Chief Financial Officer

February 19, 2003

Consolidated Five - Year Summary of Selected Financial Data

(UNAUDITED)

<i>(dollars in thousands)</i>	2002	2001	December 31, 2000	1999	1998
Balance Sheet Data					
Cash	\$ 2	\$ 3	\$ 3	\$ 3	\$ 3
Loans	240,891	223,041	152,268	149,484	149,776
Less: allowance for loan losses	5,320	5,459	5,447	5,531	5,577
Net loans	235,571	217,582	146,821	143,953	144,199
Investment in other Farm Credit institutions	4,212	4,216	4,209	4,209	4,209
Other assets	5,537	6,113	6,016	5,965	5,790
Total assets	\$ 245,322	\$ 227,914	\$ 157,049	\$ 154,130	\$ 154,201
Notes payable to AgFirst Farm Credit Bank*	\$ 206,383	\$ 190,993	\$ 120,470	\$ 118,129	\$ 118,581
Accrued interest payable and other liabilities with maturities of less than one year	9,017	5,038	5,209	5,142	5,298
Total liabilities	215,400	196,031	125,679	123,271	123,879
Protected borrower equity	818	1,053	1,194	1,341	1,548
Capital stock and participation certificates	1,188	1,194	1,152	1,156	1,166
Retained earnings					
Allocated	15,735	15,124	14,577	14,016	13,297
Unallocated	14,865	14,512	14,447	14,346	14,311
Accumulated other comprehensive income (loss)	(2,684)	—	—	—	—
Total members' equity	29,922	31,883	31,370	30,859	30,322
Total liabilities and members' equity	\$ 245,322	\$ 227,914	\$ 157,049	\$ 154,130	\$ 154,201
Statement of Income Data					
Net interest income	\$ 6,516	\$ 6,550	\$ 6,621	\$ 6,304	\$ 6,587
Provision for (reversal of) loan losses	1,150	150	—	—	—
Noninterest income (expense), net	(1,130)	(1,584)	(2,051)	(1,567)	(1,710)
Net income	\$ 4,236	\$ 4,816	\$ 4,570	\$ 4,737	\$ 4,877
Key Financial Ratios					
Rate of return on average:					
Total assets	1.72%	2.45%	2.85%	2.87%	3.06%
Total members' equity	12.54%	15.20%	14.19%	15.39%	16.20%
Net interest income as a percentage of average earning assets	2.71%	3.42%	4.26%	3.92%	4.26%
Net chargeoffs (recoveries) to average loans	0.53%	0.07%	0.05%	0.03%	0.01%
Total members' equity to total assets	12.20%	13.99%	19.97%	20.02%	19.66%
Debt to members' equity (:1)	7.20	6.15	4.01	3.99	4.09
Allowance for loan losses to loans	2.21%	2.45%	3.58%	3.70%	3.72%
Permanent capital ratio	13.53%	15.52%	19.13%	17.71%	18.43%
Total surplus ratio	12.49%	14.85%	18.43%	16.88%	17.55%
Core surplus ratio	10.06%	12.64%	15.61%	13.91%	14.44%
Net Income Distribution					
Estimated patronage refunds:					
Cash dividend	\$ 1,590	\$ 1,868	\$ 1,809	\$ 1,890	\$ 1,923
Qualified allocated retained earnings	1,741	2,802	2,714	2,835	2,885
Nonqualified allocated retained earnings	643	—	—	—	—

* General financing agreement is renewable on three-year cycles. The next renewal date is December 31, 2004.

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

(dollars in thousands, except as noted)

The following commentary reviews the financial condition and results of operations of Pee Dee Farm Credit (Association) for the years ended December 31, 2002 and December 31, 2001. This information should be read in conjunction with the Consolidated Financial Statements, Notes to the Consolidated Financial Statements and other sections in this Annual Report.

The agricultural economy of the territory serviced by the Association includes the major commodities of tobacco, cotton, forestry and broilers. There has been significant change in our market base over the past year, with the Association buying and selling loan participations as well as the Association's involvement in Farmer Mac guarantee programs. During 2002, the Association targeted certain segments of our business with hopes of increasing market share. Continued efforts are being made to expand services, increase public knowledge of our services and streamline our current delivery of products to enhance our existing portfolio.

Effective January 1, 2002, pursuant to a plan of restructuring approved by the Farm Credit Administration (FCA) and Association shareholders, the Association reorganized its existing organizational structure. Pursuant to this restructuring, a Federal Land Credit Association (FLCA) and Production Credit Association (PCA) were formed as wholly owned subsidiaries of the Association. The formation of these subsidiaries enables the Association to take advantage of the tax-exempt status of net income from long-term mortgage operations of the FLCA. Please refer to Note 1 of the Notes to the Consolidated Financial Statements in this Annual Report for additional information relating to the Association organization.

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 geographic distribution of the loans is as follows:

State	12/31/02	12/31/01
South Carolina	80.2%	73.7%
California	.6	.7
Florida	15.7	19.8
Georgia	.9	2.4
Maryland	.7	.9
Minnesota	—	.7
New York	.2	.3
North Carolina	1.7	1.5
	100.0%	100.0%

The diversification of the Association loan volume by type is shown below:

Loan Type	12/31/02	12/31/01
Long-term farm mortgage	25.06%	20.60%
Production and intermediate-term	52.17	53.96
Rural home	4.72	5.18
Farm-related business	3.31	2.63
Basic processing	15.28	.83
Nonaccrual	.76	.23
Sales contracts/purchase money mortgages	.15	.21
Participations purchased	22.97	26.94
Less: participations sold	(24.42)	(10.58)
	100.00%	100.00%

The Association's loan portfolio is diversified over a range of agricultural commodities in our region. Predominant commodities in the portfolio are livestock, poultry, tobacco, forestry, and row crops that constitute over 63 percent of the entire portfolio. Please refer to Note 3 in the Notes to the Consolidated Financial Statements section of this Annual Report for additional information concerning the loan types and loan portfolio.

The gross loan volume of the Association as of December 31, 2002, was \$240,891 an increase of \$17,850 or 8.00 percent as compared to \$223,041 at December 31, 2001. Net loans outstanding on December 31, 2002, were \$235,571 as compared to \$217,582 at December 31, 2001. Net loans accounted for 96.03 percent of total assets on December 31, 2002 as compared to 95.47 percent of total assets at December 31, 2001.

The increase in gross and net loan volume during the reporting period is primarily attributed to large corporate loans including participations sold and purchases of participation loans.

During 2002, the Association increased activity in the buying and selling of loan participations within and outside of the Farm Credit System (FCS). This provides a means for the Association to spread credit concentration risk and realize non-patronage sourced interest and fee income, which may strengthen their capital position. As of December 31, 2002, the Association had \$55,333 participation loans purchased from other FCS institutions and no participation loans purchased from non-FCS institutions, offset by \$58,832 in participation loans sold.

The Association also participates in the Federal Agricultural Mortgage Corporation (Farmer Mac) program, which was established by Congress to provide liquidity to agricultural lenders. At December 31, 2002, the Association had loans amounting to \$22,396 which were 100 percent guaranteed by Farmer Mac.

The Association's loan portfolio is divided into performing and high-risk categories. A Special Assets Management Department is responsible for servicing loans classified as high-risk. The high-risk assets, including accrued interest, are detailed below:

	<u>12/31/02</u>	<u>12/31/01</u>
High-risk Assets		
Nonaccrual loans	\$ 1,828	\$ 514
Restructured loans	10	27
Accruing loans 90 days past due	—	—
Total high-risk loans	<u>1,838</u>	<u>541</u>
Other property owned	—	—
Total high-risk assets	<u>\$ 1,838</u>	<u>\$ 541</u>
Ratios		
Nonaccrual loans to total loans	0.76%	.23%
High-risk assets to total assets	0.75%	.24%

Nonaccrual loans increased \$1,314, or 255.64 percent in 2002. The increase is primarily the result of the increased stress in the agricultural economy. Drought conditions effected lower than normal yields while commodity prices continued to be low. There are no significant potential credit risks within the loan portfolio that could adversely impact the performance of the loan portfolio in the near future.

Loan restructuring is available to financially distressed borrowers. Restructuring of loans occurs when the Association grants a concession to a borrower based on either a court order or good faith in a borrower's ability to return to financial viability. The concessions can be in the form of a modification of terms or rates, a compromise of

amounts owed, or deed in lieu of foreclosure. Other receipts of assets and/or equity to pay the loan in full or in part are also considered restructured loans. The type of alternative financing structure chosen is based on minimizing the loss incurred by both the Association and the borrower.

There is an inherent risk in the extension of any type of credit. Association management analyzes credit quality, loan performance, concentration, and other forms of risk, maintaining an allowance for loan losses in an amount sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The Association made an addition of \$1,150 to the allowance for loan losses in 2002, primarily to replenish risk funds due to charge-offs. Charge-offs for the period ended December 31, 2002 amounted to \$1,292. The ratio of net charge-offs to average loans was 0.53 percent at December 31, 2002. The allowance for loan losses at December 31, 2002 was \$5,320, which was 2.21 percent of total loans outstanding and was considered by management to be adequate to cover possible losses. Please refer to Note 2 in the Notes to the Consolidated Financial Statements of this Annual Report for further information concerning the allowance for loan losses.

RESULTS OF OPERATIONS

Net income for the year ended December 31, 2002, totaled \$4,236, a decrease of \$580 or 12.04 percent, as compared to \$4,816 for the same period of 2001. Interest income for the year ended December 31, 2002, was \$15,289, a decrease of \$929 or 5.73 percent as compared to \$16,218 for the same period of 2001. Major components of the changes in net income for the past two years are outlined in the following table.

Changes in Net Income:

	<u>2002-2001</u>	<u>2001-2000</u>
Net income (prior year)	\$ 4,816	\$ 4,570
Increase (decrease) in net income due to:		
Interest income	(929)	544
Interest expense	895	(615)
Net interest income	(34)	(71)
Provision for loan losses	(1,000)	(150)
Noninterest income	604	1,126
Noninterest expense	(189)	(674)
Benefit (provision) for income taxes	39	15
Total changes in income	<u>(580)</u>	<u>246</u>
Net income	<u>\$ 4,236</u>	<u>\$ 4,816</u>

Net interest income decreased by \$34 or 0.52 percent in 2002 compared to 2001. The primary reason for this decrease was due to the decline in interest rates. Net interest income, excluding interest income from nonaccrual loans, decreased \$1,102 as a result of interest rate spreads and increased \$1,223 as a result in loan

volume changes in 2002, compared to the same period of 2001. Interest income on nonaccrual loans for the twelve months ended December 31, 2002, totaled \$176, a decrease of \$155, compared to \$331 at the previous year-end. Please refer to the Consolidated Five-Year Summary of Selected Financial Data in this Annual Report to review key financial ratios pertaining to earnings and net interest income. The sources of change in net interest income are illustrated, as follows:

Change in Net Interest Income:

	Volume*	Rate	Nonaccrual Income	Total
12/31/02 - 12/31/01				
Interest income	\$ 4,072	\$ (4,846)	\$ (155)	\$ (929)
Interest expense	2,850	(3,745)	—	(895)
Change in net interest income	\$ 1,223	\$ (1,102)	\$ (155)	\$ (34)
12/31/01 - 12/31/00				
Interest income	\$ 3,551	\$ (2,944)	\$ (63)	\$ 544
Interest expense	2,634	(2,019)	—	615
Change in net interest income	\$ 917	\$ (925)	\$ (63)	\$ (71)

* Volume variances can be the result of increased/decreased loan volume or from changes in the percentage composition of assets and liabilities between periods.

Noninterest income for the period ended December 31, 2002, increased \$604 as compared to the same period of 2001. The increase is primarily attributed to increases of patronage refunds and miscellaneous income by \$744 and \$23, respectively. The Association received \$2,051 in patronage refund from AgFirst Farm Credit Bank (the Bank) and other Farm Credit institutions, including \$216 in a special distribution from the Bank for the twelve months ended December 31, 2002. The increases referenced were offset by decreases in loan fees of \$152 and fees for financially related services of \$11.

Noninterest expense increased \$189 or 4.43 percent for the twelve months ended December 31, 2002, as compared to the same period of 2001. Operating expenses for the year ended December 31, 2002, totaled \$4,457, compared to \$4,268 the previous year-end. Salaries and employee benefits along with occupancy and equipment expenses each decreased by \$8. However, Insurance Fund premiums went from \$0 in 2001 to \$72 in 2002. Also contributing to the increase was a rise in other operating expenses of \$133.

The Association recorded a benefit for income taxes of \$49 for the twelve months ended December 31, 2002, as compared to a benefit of \$10 for the same period in 2001.

A key factor in the growth of net income for future years will be continued improvement in net interest and noninterest income. Our goal is to generate earnings sufficient to fund operations, adequately capitalize the Association, and achieve an adequate rate of return for our members. To meet this goal, the Association must

meet certain objectives. These objectives are to attract and maintain high quality loan volume priced at competitive rates and to manage credit risk in our entire portfolio, while efficiently meeting the credit needs of our members.

LIQUIDITY AND FUNDING SOURCES

Liquidity

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. The Association's participation in the Farmer Mac and other secondary market programs provides additional liquidity. Sufficient liquid funds have been available to meet all financial obligations.

Funding Sources

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances the funds to the Association, creating notes payable to the Bank. 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 December 31, 2002, were \$206,383 as compared to \$190,993 at December 31, 2001. The increase of 8.06 percent during the period is attributable to the increase in loan volume.

The Association had a \$2,000 line of credit outstanding with a third party as of December 31, 2002. No funds have been drawn against this line, which expires August 21, 2003.

Funds Management

The Bank and the Association manage assets and liabilities to provide a broad range of loan products and funding options, which will permit the Association to be competitive in all interest rate environments. The primary objective of the asset/liability management process is to provide stable and rising earnings, while maintaining adequate capital levels by managing exposure to credit and interest rate risks.

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers fixed, adjustable and variable rate loan products that are marginally priced according to financial market rates. Variable rate loans may be indexed to either the Prime Rate or the 90-day London Interbank Offered Rate (LIBOR). Adjustable rate mortgages are indexed to U.S. Treasury Rates. Fixed rate loans are priced based on the current cost of Farm Credit debt of similar terms to maturity.

The Association's net interest income as a percentage of average earning assets (net interest margin) was 2.71 percent on December 31, 2002, compared to 3.42 percent on December 31, 2001. The change is mainly attributed to higher loan volume but at lower interest rates.

The majority of the interest rate risk in the Association balance sheet is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control risk associated with the loan portfolio.

CAPITAL RESOURCES

Total members' equity at December 31, 2002, decreased 6.15 percent to \$29,922 from the December 31, 2001, total of \$31,883. The primary cause of the decrease was the recording of \$2,684 in accumulated other comprehensive loss related to a minimum pension liability adjustment. Refer to Note 9 in the Notes to the Consolidated Financial Statements section of this annual report for additional information.

Total capital stock and participation certificates were \$2,006 on December 31, 2002, compared to \$2,247 on December 31, 2001. This 10.73 percent decrease is attributed to the retirement of protected stock and participation certificates on loans liquidated in the normal course of business, retirement of excess stock through revolvment and new loans being capitalized at low regulatory levels.

The Association's permanent capital ratio as of December 31, 2002 was 13.53 percent compared to 15.52 percent on December 31, 2001. Farm Credit Administration (FCA) regulations require all Farm Credit institutions maintain a minimum permanent capital ratio of 7 percent. The permanent capital ratio is calculated by dividing the Association's permanent capital by a risk-adjusted asset base.

FCA regulations also require all Farm Credit institutions to maintain two other minimum capital ratios: total surplus ratio of 7 percent and core surplus ratio of 3.5 percent. The total surplus and core surplus ratios are calculated by dividing total surplus and core surplus as defined in FCA regulations by a risk-adjusted asset base. As of December 31, 2002, the Association's total surplus ratio and core surplus ratio was 12.49 percent and 10.06 percent, respectively, as compared to 14.85 percent and 12.64 percent, respectively, on December 31, 2001.

Annually, the Association establishes target capital ratios. The Association's 2002 target permanent capital ratio was 13 to 15 percent of risk-adjusted assets. The targeted total surplus and core surplus ratios for 2002 were 12.00 percent and 9.00 percent, respectively. As of December 31, 2002, the Association exceeded all target capital ratios.

Disclosure Required by Farm Credit Administration Regulations

Description of Business

Descriptions of the territory served, persons eligible to borrow, types of lending activities engaged in, financial services offered and related Farm Credit organizations are incorporated herein by reference to Note 1 to the consolidated financial statements, "Organization and Operations," included in this annual report to stockholders.

The description of significant developments that had or could have a material impact on earnings or interest rates to borrowers, acquisitions or dispositions of material assets, material changes in the manner of conducting the business, seasonal characteristics, and concentrations of assets, if any, is incorporated in "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this annual report to stockholders.

Description of Property

The following table sets forth certain information regarding the properties of the reporting entity, all of which are located in South Carolina:

<u>Location</u>	<u>Description</u>	<u>Form of Ownership</u>
2229 South Irby Street Florence	Administrative/ Branch	Owned
207 East Liberty Street Sumter	Branch	Owned
212 Main Street Conway	Branch	Owned

Legal Proceedings

Information, if any, to be disclosed in this section is incorporated herein by reference to Note 12 to the consolidated financial statements, "Commitments and Contingencies," included in this annual report to stockholders.

Description of Capital Structure

Information to be disclosed in this section is incorporated herein by reference to Note 7 to the consolidated financial statements, "Members' Equity," included in this annual report to stockholders.

Description of Liabilities

The description of liabilities, contingent liabilities and intrasystem financial assistance rights and obligations to be disclosed in this section is incorporated herein by reference to Notes 2, 6, 10 and 12 to the consolidated financial statements included in this annual report to stockholders.

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

"Management's Discussion and Analysis of Financial Condition and Results of Operations," which appears in this annual report to stockholders and is to be disclosed in this section, is incorporated herein by reference.

Senior Officers

The following represents certain information regarding the senior officers of the Association:

<u>Senior Officer</u>	<u>Position</u>
Jasper W. Shuler	President and Chief Executive Officer
Kathy S. Heustess	Chief Financial Officer
William H. Wise, Jr.	Chief Operating Officer
Richard H. Horn	Chief Credit Officer

The business experience for the past five years for senior officers is with the Farm Credit System.

The total amount of compensation earned by all senior officers, including the CEO, as a group during the years ended December 31, 2002, 2001 and 2000, is as follows:

<u>Aggregate Number of Senior Officers</u>	<u>Year</u>	<u>Annual</u>		<u>Total</u>
		<u>Salary</u>	<u>Bonus</u>	
CEO	2001	\$160,120	\$ 30,000	\$190,120
7	2002	\$668,024	—	\$668,024
7	2001	\$621,651	\$173,402	\$795,053
7	2000	\$577,552	\$ 63,854	\$641,406

In addition to a base salary, all employees with the exception of the chief executive officer are eligible for additional compensation under incentive plans. In addition to the general plan, specified employees are eligible for individual or group incentive plans. The chief executive officer is eligible for a bonus at the sole discretion of the board.

Executive management, excluding the chief executive officer, is eligible for an incentive plan based on overall company results. The general incentive plan is designed to reward excellent performance while increasing the Association's financial position and stockholder wealth. The individual and group incentive plans are specifically for account officers, credit officers, participations credit support/accounting staff, special asset manager, farm-related business coordinator and contracted accounting staff to reward them when goals in their incentive plans are exceeded.

The goals of the account officers' plan include generation of fee and farm related services income in excess of salaries with an on/off switch based on Association delinquencies. The goal of the credit officer plan is to generate fee income from loans in excess of salary with on/off switches based on credit administration, credit quality and net interest margin. The goal of the participations credit support/accounting plan is to return fee income in excess of salaries with on/off switches based on credit quality and credit administration. The goal of the special asset manager's plan is to resolve and collect nonaccrual loans with an on/off switch based on Association delinquencies. The goal of the farm related services coordinator's plan is to increase related services income over previous year's income. The goal of the contracted accounting incentive plan is to generate fee income in excess of salary and benefits for contractual accounting services performed for other associations. The general plan is paid based on a percentage of net income in excess of budgeted net income. The key factors for payment of the general plan include return on assets, credit quality, permanent capital, CIPA rating and customer satisfaction survey results. The criteria for payment of all incentive plans include: employees must be employed as of the fiscal year end, new employees with less than a full year of employment will receive a pro rata share based on the number of full months employed during the calendar year, employees who retire or die prior to year end will receive a pro rata share of the incentive, the plan will be paid based on percentage of salary, and will be paid from the Association's core earnings. The employees must have satisfactory performance and not have been on probation during the year. The payment of the incentive available to all employees is determined on a percentage basis. The executive plan has four categories that are equally weighted and payment is made on a per category basis. In addition, executive management is eligible for 10 percent of net income in excess of budget if all four categories are met. There was no payout from any of the above plans for the year ended December 2002. No material changes were made to existing plans from previous year. Bonuses are shown in the year earned, which may be different than the year of payment.

Disclosure of the total compensation earned in 2002 by any senior officer, or to any other individual included in the total whose compensation exceeds \$50,000, is available to stockholders upon request.

Directors

Directors and senior officers are reimbursed on an actual cost basis for all expenses incurred in the performance of official duties. Such expenses may include transportation, lodging, meals, tips, tolls, parking of cars, laundry, registration fees, and other expenses associated with travel on official business. A copy of the policy is available to shareholders of the Association upon request.

The aggregate amount of reimbursement for travel, subsistence and other related expenses for all directors as a group was \$27,993 for 2002, \$18,609 for 2001, and \$33,777 for 2000.

Subject to approval by the board, the Association may allow directors honoraria of \$375 for attendance at meetings, committee meetings, or special assignments. Total compensation paid to directors, as a group was \$60,000.

The following represents certain information regarding the directors of the Association, including their principal occupation and employment for the past five years:

Dale W. Player, Chairman, is a farmer and serves on the boards of AgFirst Farm Credit Bank, SC Cotton Board, and Carolina Cotton Growers Cooperative. He has been a self-employed farmer for the past five years. During 2002, he served 12 days at Association board meetings and 4 days in other official activities and was paid \$6,000. His three-year term of office began March 2001.

Harry B. DuRant, Vice Chairman, is a farmer and serves on the Laurence Manning Academy school board and the Phillip Morris Quality Advisory Committee. He has been a self-employed farmer for the past five years. During 2002, he served 12 days at Association board meetings and 9 days in other official activities and was paid \$7,875. His three-year term of office began March 2000.

DuPree Atkinson is a farmer and serves on the Clemson Advisory Committee and the Phillip Morris Advisory Committee. He has been a self-employed farmer for the past five years. During 2002, he served 12 days at Association board meetings and 9 days in other official activities and was paid \$7,875. His three-year term of office began March 2002.

Leroy W. Baxley is a farmer and serves on the Southern Cotton Growers and the National Cotton Council boards. He has been a self-employed farmer for the past five

years. During 2002, he served 12 days at Association board meetings and 6 days in other official activities and was paid \$6,750. His three-year term of office began March 2001.

Dr. Morgan B. Coker is a retired college professor and department dean. He has been retired for the past five years. During 2002, he served 12 days at Association board meetings and 9 days in other official activities and was paid \$7,875. His one-year term of office began March 2002.

W. Edwin Dargan, Jr. is a farmer and serves on the boards of SC Soybean Association, Darlington County Bank, and Darlington County Farm Service Agency. He has been a self-employed farmer for the past five years. During 2002, he served 12 days at Association board meetings and 9 days in other official activities and was paid \$7,875. His three-year term of office began March 2002.

Jimmy Poston is a farmer and serves on the boards of Florence County Soil and Water Conservation District, Quality Assurance Committee for Phillip Morris, SC Tobacco Grower's Association and the Southern States Advisory Board. He has been a self-employed farmer for the past five years. During 2002, he served 12 days at Association board meetings and 9 days in other official activities and was paid \$7,875. His three-year term of office began March 2000.

James M. Ward is a farmer and serves on the boards of Farm Service Agency Florence County Committee and Farm Service Agency Tobacco Appeals Committee. He has been a self-employed farmer for the past five years. During 2002, he served 12 days at Association board meetings and 9 days in other official activities and was paid \$7,875. His three-year term of office began March 2001.

Transactions with Senior Officers and Directors

The reporting entity's policies on loans to and transactions with its officers and directors, to be disclosed in this section are incorporated herein by reference to Note 11 to the consolidated financial statements, "Related Party Transactions," included in this annual report to stockholders.

Involvement in Certain Legal Proceedings

There were no matters which came to the attention of management or the board of directors regarding involvement of current directors or senior officers in specified legal proceedings which should be disclosed in this section.

Relationship with Independent Public Accountants

There were no material disagreements with our independent public accountants on any matter of accounting principles or financial statement disclosure during this period.

Consolidated Financial Statements

The consolidated financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated February 19, 2003, and the report of management, which appear in this annual report to stockholders are incorporated herein by reference.

Copies of the Association's quarterly reports are available upon request free of charge by calling 1-800-741-7332, or writing Kathy S. Heustess, Chief Financial Officer, Pee Dee Farm Credit, P. O. Box 13209, Florence, SC 29504.

Borrower Information Regulations

Since 1972, Farm Credit Administration (FCA) regulations have required that borrower information be held in strict confidence by Farm Credit System (FCS) institutions, their directors, officers and employees. These regulations provide Farm Credit institutions clear guidelines for protecting their borrowers' nonpublic personal information.

On November 10, 1999, the FCA Board adopted a policy that requires FCS institutions to formally inform new borrowers at loan closing of the FCA regulations on releasing borrower information and to address this information in the annual report to shareholders. The implementation of these measures ensures that new and existing borrowers are aware of the privacy protections afforded them through FCA regulations and Farm Credit System institution efforts.

Stockholder Investment

Stockholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of the District annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 503, or writing Patti Trotter, AgFirst Farm Credit Bank, P. O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained by going to AgFirst's website at www.AgFirst.com.

Report of Independent Accountants



PricewaterhouseCoopers LLP
10 Tenth Street, Suite 1400
Atlanta, GA 30309
Telephone (678) 419 1000

Report of Independent Accountants

February 19, 2003

To the Board of Directors and Stockholders
of Pee Dee Farm Credit, ACA

We have audited the accompanying consolidated balance sheets of Pee Dee Farm Credit, ACA (Association) and its subsidiaries as of December 31, 2002, 2001, and 2000, and the related consolidated statements of income, of changes in members' equity, and of cash flows for each of the three years in the period ended December 31, 2002. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Association and its subsidiaries at December 31, 2002, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

Consolidated Balance Sheets

<i>(dollars in thousands)</i>	December 31, 2002	December 31, 2001	December 31, 2000
Assets			
Cash	\$ 2	\$ 3	\$ 3
Loans	240,891	223,041	152,268
Less: allowance for loan losses	5,320	5,459	5,447
Net loans	235,571	217,582	146,821
Accrued interest receivable	2,620	2,812	3,103
Investment in other Farm Credit institutions	4,212	4,216	4,209
Premises and equipment, net	618	655	684
Other assets	2,299	2,646	2,229
Total assets	<u>\$ 245,322</u>	<u>\$ 227,914</u>	<u>\$ 157,049</u>
Liabilities			
Notes payable to AgFirst Farm Credit Bank	\$ 206,383	\$ 190,993	\$ 120,470
Accrued interest payable	679	705	726
Patronage refund payable	1,641	1,913	1,858
Other liabilities	6,697	2,420	2,625
Total liabilities	<u>215,400</u>	<u>196,031</u>	<u>125,679</u>
Commitments and contingencies			
Members' Equity			
Protected borrower equity	818	1,053	1,194
Capital stock and participation certificates	1,188	1,194	1,152
Retained earnings			
Allocated	15,735	15,124	14,577
Unallocated	14,865	14,512	14,447
Accumulated other comprehensive income (loss)	(2,684)	—	—
Total members' equity	<u>29,922</u>	<u>31,883</u>	<u>31,370</u>
Total liabilities and members' equity	<u>\$ 245,322</u>	<u>\$ 227,914</u>	<u>\$ 157,049</u>

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

Consolidated Statements of Income

<i>(dollars in thousands)</i>	For the year ended December 31,		
	2002	2001	2000
Interest Income			
Loans	\$ 15,289	\$ 16,218	\$ 15,674
Interest Expense			
Notes payable to AgFirst Farm Credit Bank	8,773	9,668	9,053
Net interest income	6,516	6,550	6,621
Provision for (reversal of) loan losses	1,150	150	—
Net interest income after provision for (reversal of) loan losses	5,366	6,400	6,621
Noninterest Income			
Loan fees	702	854	389
Fees for financially related services	239	250	199
Patronage refund from other Farm Credit institutions	2,051	1,307	942
Miscellaneous	286	263	18
Total noninterest income	3,278	2,674	1,548
Noninterest Expense			
Salaries and employee benefits	3,120	3,128	2,482
Occupancy and equipment	283	291	286
Insurance Fund premium	72	—	—
Other operating expenses	982	849	826
Total noninterest expense	4,457	4,268	3,594
Income before income taxes	4,187	4,806	4,575
Provision (benefit) for income taxes	(49)	(10)	5
Net income	\$ 4,236	\$ 4,816	\$ 4,570

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

Consolidated Statements of Changes in Members' Equity

<i>(dollars in thousands)</i>	Protected Borrower Equity	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 1999	\$ 1,341	\$ 1,156	\$ 14,016	\$ 14,346	\$ —	\$ 30,859
Net income				4,570		4,570
Protected borrower equity retired	(147)					(147)
Capital stock/participation certificates issued		95				95
Capital stock/participation certificates retired		(99)				(99)
Patronage distribution						
Cash				(1,809)		(1,809)
Qualified allocated retained earnings			2,714	(2,714)		—
Retained earnings retired			(2,122)			(2,122)
Distribution adjustment			(31)	54		23
Balance at December 31, 2000	1,194	1,152	14,577	14,447	—	31,370
Net income				4,816		4,816
Protected borrower equity retired	(141)					(141)
Capital stock/participation certificates issued		132				132
Capital stock/participation certificates retired		(90)				(90)
Patronage distribution						
Cash				(1,868)		(1,868)
Qualified allocated retained earnings			2,802	(2,802)		—
Retained earnings retired			(2,306)			(2,306)
Distribution adjustment			51	(81)		(30)
Balance at December 31, 2001	1,053	1,194	15,124	14,512	—	31,883
Comprehensive income						
Net income				4,236		4,236
Minimum pension liability					(2,684)	(2,684)
Total comprehensive income						1,552
Protected borrower equity retired	(235)					(235)
Capital stock/participation certificates issued		88				88
Capital stock/participation certificates retired		(94)				(94)
Patronage distribution						
Cash				(1,590)		(1,590)
Qualified allocated retained earnings			1,741	(1,741)		—
Nonqualified allocated retained earnings			643	(643)		—
Retained earnings retired			(1,716)			(1,716)
Distribution adjustment			(57)	91		34
Balance at December 31, 2002	\$ 818	\$ 1,188	\$ 15,735	\$ 14,865	\$ (2,684)	\$ 29,922

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

Consolidated Statements of Cash Flows

<i>(dollars in thousands)</i>	For the year ended December 31,		
	2002	2001	2000
Cash flows from operating activities:			
Net income	\$ 4,236	\$ 4,816	\$ 4,570
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation on premises and equipment	151	166	164
Provision for (reversal of) loan losses	1,150	150	—
(Gains) losses from sale of premises and equipment, net	(14)	—	—
Changes in operating assets and liabilities:			
(Increase) decrease in accrued interest receivable	192	291	44
(Increase) decrease in investment in other Farm Credit institutions	4	(7)	—
(Increase) decrease in other assets	347	(417)	(127)
Increase (decrease) in accrued interest payable	(26)	(21)	14
Increase (decrease) in other liabilities	1,593	(205)	162
Total adjustments	3,397	(43)	257
Net cash provided by (used in) operating activities	7,633	4,773	4,827
Cash flows from investing activities:			
Net (increase) decrease in loans	(19,139)	(70,911)	(2,868)
Purchase of premises and equipment, net	(114)	(137)	(132)
Proceeds from sale of premises and equipment, net	14	—	—
Net cash provided by (used in) investing activities	(19,239)	(71,048)	(3,000)
Cash flows from financing activities:			
Advances on (repayment of) notes payable to AgFirst Farm Credit Bank, net	15,390	70,523	2,341
Protected borrower equity retired	(235)	(141)	(147)
Capital stock and participation certificates issued	88	132	95
Capital stock and participation certificates retired	(94)	(90)	(99)
Patronage refunds paid	(1,828)	(1,843)	(1,895)
Retained earnings retired	(1,716)	(2,306)	(2,122)
Net cash provided by (used in) financing activities	11,605	66,275	(1,827)
Net increase (decrease) in cash	(1)	—	—
Cash, beginning of period	3	3	3
Cash, end of period	\$ 2	\$ 3	\$ 3
Supplemental schedule of non-cash investing and financing activities:			
Cash dividends or patronage distributions declared or payable	\$ 1,590	\$ 1,868	\$ 1,809
Supplemental information:			
Interest paid	\$ 8,799	\$ 9,689	\$ 9,039
Taxes paid, net	59	24	4

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)

Note 1 — Organization and Operations

A. **Organization:** Pee Dee Farm Credit, ACA (the Association) is a member-owned cooperative which provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified purposes in the counties of Abbeville, Allendale, Calhoun, Charleston, Chesterfield, Clarendon, Darlington, Dillon, Florence, Georgetown, Greenwood, Horry, Jasper, Kershaw, Lee, Lexington, Marion, Marlboro, Richland, Sumter, Union and Williamsburg in the state of South Carolina; the counties of Alachua, Collier, Columbia, Dade, DeSoto, Duval, Hendry, Hernando, Highlands, Nassau, Palm Beach and Polk in the state of Florida; the county of Evans in the state of Georgia; the counties of Anson, Columbus, Mecklenburg, Robeson, Union and Wake in the state of North Carolina; Monterey County in the state of California; Wicomico County in the state of Maryland; Genesee County in the state of New York; and Huntingdon County in the state of Pennsylvania, in cooperation with the ACAs chartered in those territories.

The Association is a lending institution of the Farm Credit System (the System) which was established by Acts of Congress and is subject to the provisions of the Farm Credit Act of 1971, as amended (the Farm Credit Act). The most recent significant amendment to the Farm Credit Act was the Agricultural Credit Act of 1987.

The nation is currently served by six Farm Credit Banks (FCBs), each of which has specific lending authorities within its chartered territory, and one Agricultural Credit Bank (ACB) which has nationwide lending authorities. Each FCB and the ACB serve one or more Production Credit Associations (PCAs) that originate and service short- and intermediate-term loans, Federal Land Credit Associations (FLCAs) that originate and service long-term real estate mortgage loans and/or Agricultural Credit Associations (ACAs) that originate both long-term and short- and intermediate-term loans. ACAs may reorganize into a parent-subsidary structure and may operate their long-term mortgage lending activities through a newly created FLCA subsidiary and their short- and intermediate-term lending activities through a newly created PCA subsidiary. PCAs, FLCAs and ACAs are collectively referred to as Associations.

Effective January 1, 2002, pursuant to a plan of restructuring approved by the Farm Credit Administration (FCA) and Association shareholders, the Association reorganized its existing organizational structure. Pursuant to this restructuring, an FLCA and a PCA were formed as wholly owned subsidiaries of the Association. The formation of these subsidiaries enables the Association to take advantage of the tax-exempt status of net income from long-term mortgage operations of the FLCA. This restructuring was accounted for as a reorganization of entities under common control similar to a pooling of interests.

Prior to the restructuring, the ACA was subject to federal and state income tax. As a result of the restructuring, long-term lending activity was separated into a wholly owned FLCA subsidiary, which is exempt from federal and state income tax. The ACA, which is the holding company, along with the wholly owned PCA subsidiary, continue to be subject to income tax.

AgFirst Farm Credit Bank (Bank) and its related Associations are collectively referred to as the "District." The Bank is responsible for supervising the activities of the Association, as well as the other associations operating within the AgFirst District. The District consists of the Bank and twenty-four ACAs, twenty-one of which have reorganized as ACA parent-subsidary structures as of December 31, 2002. Effective January 1, 2003, one additional Association will reorganize as an ACA holding company.

The Association makes short- and intermediate-term loans for agricultural production or operating purposes, and secured long-term real estate mortgage loans, with funding from the Bank.

The FCA is delegated authority by Congress to regulate the System banks and associations. The activities of the associations are examined by the FCA and certain actions by the associations are subject to the prior approval of the FCA and the supervising Bank.

The Farm Credit Act established the Farm Credit System Insurance Corporation (Insurance Corporation) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is required to be used to (1) ensure the timely payment of principal and interest on Systemwide debt obligations (Insured debt),

(2) ensure the retirement of protected borrower capital at par or stated value, and (3) for other specified purposes. The Insurance Fund is also available for discretionary uses by the Insurance Corporation of providing assistance to certain troubled System institutions and to cover the operating expenses of the Insurance Corporation. Each System bank is required to pay premiums into the Insurance Fund, based on its annual average loan principal outstanding until the monies in the Insurance Fund reach the “secure base amount,” which is defined in the Farm Credit Act as 2.0 percent of the aggregate insured obligations (Systemwide debt obligations). When the amount in the Insurance Fund exceeds the secure base amount, the Insurance Corporation is required to reduce premiums, but it still must ensure that reduced premiums are sufficient to maintain the level of the Insurance Fund at the secure base amount.

B. Operations: The Farm Credit Act sets forth the types of authorized lending activity, persons eligible to borrow, and financial services which can be offered by the Association. The Association is authorized to provide, either directly or in participation with other lenders, credit, credit commitments and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents, and farm-related businesses.

The Association may sell to any Farm Credit borrowing member, on an optional basis, credit or term life insurance appropriate to protect the loan commitment in the event of death of the debtor(s). The sale of other insurance necessary to protect a member’s farm or aquatic unit is permitted, but limited to hail and multi-peril crop insurance, and insurance necessary to protect the facilities and equipment of aquatic borrowers.

Upon request, stockholders of the Association will be provided with an AgFirst Farm Credit Bank Annual Report to Stockholders, which includes the combined financial statements of the Bank and its related Associations. The Association’s financial condition may be impacted by factors that affect the Bank. The AgFirst Annual Report discusses the material aspects of the District’s financial condition, changes in financial condition, and results of operations. In addition, the AgFirst Annual Report identifies favorable and unfavorable trends, significant events, uncertainties and the impact of activities of the Financial Assistance Corporation Assistance Board (Assistance Board) and Insurance Corporation.

The lending and financial services offered by the Bank are described in Note 1 of the District’s Annual Report to Stockholders.

Note 2 — Summary of Significant Accounting Policies

The accounting and reporting policies of the Association conform with accounting principles generally accepted in the United States (GAAP) and prevailing practices within the banking industry. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Significant estimates are discussed in these footnotes, as applicable. Actual results may differ from these estimates.

Certain amounts in prior years’ financial statements have been reclassified to conform to current consolidated financial statement presentation. Such reclassifications had no effect on net income or total members’ equity of prior years. The consolidated financial statements include the accounts of the FLCA and the PCA. All significant inter-company transactions have been eliminated in consolidation.

A. Cash: Cash, as included in the statement of cash flows, represents cash on hand and on deposit at banks.

B. Loans and Allowance for Loan Losses: Long-term real estate mortgage loans generally have maturities ranging up to 30 years. Substantially all short- and intermediate-term loans for agricultural production or operating purposes have maturities of 10 years or less.

Loans are carried at their principal amount outstanding less unearned income. Interest on loans is accrued and credited to interest income based upon the principal amount outstanding. Loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days or more (unless adequately secured and in the process of collection) or circumstances indicate that collection of principal and/or interest is in doubt. When a loan is placed in nonaccrual status, accrued interest deemed uncollectible is either reversed (if accrued in the current year) or charged against the allowance for loan losses (if accrued in prior years).

When loans are in nonaccrual status, the interest portion of payments received in cash are generally recognized as interest income if collection of the recorded investment in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it. Otherwise, loan payments are applied against the recorded investment in the loan asset. Nonaccrual loans may be transferred to accrual status when principal and interest are current, prior charge-offs have been recovered, the ability of the borrower to fulfill the contractual repayment terms is fully expected and the loan is not classified “doubtful” or “loss.”

In cases where a borrower experiences financial difficulties and the Association makes certain monetary concessions to the borrower through modifications to the contractual terms of the loan, the loan is classified as a restructured loan. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

The allowance for loan losses is maintained at a level considered adequate by management to provide for estimated losses inherent in the loan portfolio. The allowance is based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition and prior loan loss experience. Loan principal and interest, when appropriate, are charged against the allowance for loan losses when management believes collection is unlikely.

The allowance for loan losses is based upon estimates, appraisals and evaluations of loans which, by their nature, contain elements of uncertainty and imprecision. The possibility exists that changes in the economy and its impact on borrower repayment capacity will cause these estimates, appraisals and evaluations to change.

C. Investment in AgFirst Farm Credit Bank: The Association is required to maintain ownership in the Bank in the form of B and C stock. Accounting for this investment is on the cost plus allocated equities basis. Patronage refunds from the Bank are accrued as earned. The receivable for such patronage refunds is included in other assets.

D. Other Property Owned: Other property owned, consisting of real and personal property acquired through a collection action, is recorded at fair value less estimated selling costs upon acquisition. Revised estimates to the fair value less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income and expenses from operations and carrying value adjustments are included in gains (losses) on other property owned.

E. Premises and Equipment: Premises and equipment are carried at cost less accumulated depreciation. Depreciation is provided on the straight-line method over the estimated useful life. Estimated useful lives of premises and equipment are summarized as follows:

Buildings and Improvements	40 years
Furniture and Equipment	5 to 10 years
Automobiles and Trucks	3 years
Computer Equipment	3 years

Gains and losses on dispositions are reflected in current operations. Maintenance and repairs are charged to operating expense and improvements are capitalized.

F. Advanced Conditional Payments: The Association is authorized under the Farm Credit Act to accept advance payments from borrowers. To the extent the borrower's access to such advance payments is restricted, the advanced conditional payments are netted against the borrower's related loan balance. Advanced conditional payments are not insured. Interest is generally paid by the Association on such accounts.

G. Employee Benefit Plans: The employees of the Association participate in the District's defined benefit retirement plan (the Plan). The "Projected Unit Credit" actuarial method is used for financial reporting purposes and the "Entry-Age Normal Cost" method for funding purposes. As a result of the funded status at the Plan's measurement date (September 30) of the underlying Plan, the Association may record a minimum liability, an intangible asset relating to unrecognized prior service cost and other comprehensive income (loss). The adjustment to other comprehensive income (loss) would be net of deferred taxes, if significant.

The employees of the Association are eligible to participate in the District's thrift/deferred compensation plan (Thrift Plan); a percentage of employee contributions is matched by the Association. Thrift Plan costs are expensed as funded.

The Association provides certain health care and life insurance benefits to eligible retired employees. Substantially all employees may become eligible for these benefits if they reach normal retirement age while working for the Association. Expenses of \$428, \$344 and \$315 for the years ended December 31, 2002, 2001 and 2000, respectively, were classified as salaries and employee benefits.

H. Income Taxes: The Association is generally subject to federal and certain other income taxes. The Association is eligible to operate as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage refunds in the form of cash, stock or allocated surplus. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage refunds. The Association distributes patronage on the basis of book income. The Association recognizes deferred tax assets and liabilities for the expected future tax consequences of the temporary differences between the carrying amounts and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled.

Effective January 1, 2002, the Association formed a tax exempt subsidiary as described in Note 1.

I. Patronage Refund from AgFirst and Other

Financial Institutions: The Association records patronage refunds from the Bank and certain District Associations on an accrual basis.

Note 3 — Loans and Allowance for Loan Losses

A summary of loans follows:

	December 31,		
	2002	2001	2000
Long-term farm mortgage	\$ 60,396	\$ 45,947	\$ 42,271
Production and intermediate-term	125,671	120,344	83,473
Rural home	11,361	11,561	10,571
Farm related business	7,971	5,863	4,852
Processing and marketing	36,811	1,855	91
Sales contracts	352	472	649
Nonaccruals	1,828	514	505
Plus: participations purchased	55,333	60,088	9,856
Less: participations sold	(58,832)	(23,603)	—
Total	\$ 240,891	\$ 223,041	\$ 152,268

The Association's concentration of credit risk in various agricultural commodities is shown in the following table. While the amounts represent the Association's maximum potential credit risk as it relates to recorded loan principal, a substantial portion of the Association's lending activities is collateralized and the Association's exposure to credit loss associated with lending activities is reduced accordingly. An estimate of the Association's credit risk exposure is considered in the determination of the allowance for loan losses.

Total loans at December 31, 2002, 2001 and 2000 consisted of the following commodity types:

Commodity Type	December 31,		
	2002	2001	2000
Forestry	21%	17%	12%
Poultry	16	19	19
Tobacco	11	12	17
Row Crops	9	11	12
Livestock	6	8	19
Field/Grain	4	10	4
Rural Home	4	5	7
Nurseries	3	3	4
Cotton Gins	2	1	2
Other	24	14	4
Total	100%	100%	100%

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Long-term real estate loans are secured by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a

property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in the loan to value ratios in excess of the regulatory maximum.

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

The following table presents information relating to impaired loans.

	December 31,		
	2002	2001	2000
Nonaccrual:			
Current as to principal and interest	\$ 832	\$ 300	\$ 114
Past due	996	214	391
Accrual:			
Restructured	10	27	31
90 days or more past due	—	—	—
Total impaired loans	\$ 1,838	\$ 541	\$ 536

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at December 31, 2002.

The average recorded investment in impaired loans during 2002, 2001 and 2000 was \$1,647, \$739 and \$440, respectively. Impaired loans of \$46, \$1 and \$14 at December 31, 2002, 2001 and 2000, respectively, had related specific allowances for loan losses totaling \$5, \$1 and \$13, respectively. The Association recognized interest income on impaired loans of \$177 in 2002, \$334 in 2001 and \$394 in 2000.

The Association recognized interest income on nonaccrual loans in the form of cash payments totaling \$176 in 2002, \$212 in 2001 and \$394 in 2000. Interest reversed was not significant.

A summary of the changes in the allowance for loan losses follows:

	Year Ended December 31,		
	2002	2001	2000
Balance at beginning of year	\$ 5,459	\$ 5,447	\$ 5,531
Provision for (reversal of) loan losses	1,150	150	—
Loans charged off	(1,291)	(209)	(96)
Recoveries	2	71	12
Balance at end of year	\$ 5,320	\$ 5,459	\$ 5,447

To mitigate the risk of loans being placed in nonaccrual status, the Association may enter into long-term standby commitments to purchase agreements with the Federal Agricultural Mortgage Corporation (Farmer Mac). The agreements, which are effectively credit guarantees that will remain in place until the loans are paid in full, give the Association the right to sell the loans identified in the agreements to Farmer Mac in the event a delinquency of

four months occurs. Pee Dee Farm Credit has Farm Service and USDA guarantees of \$16,652 and \$12,932 as of December 31, 2002 and 2001, respectively. Further, Pee Dee Farm Credit has Farmer Mac long-term standby commitments of \$22,396 and \$15,287 at December 31, 2002 and 2001, respectively. Fees paid to Farmer Mac for such commitments totaled \$104 and \$23 for the years ended December 31, 2002 and 2001, respectively. These amounts are classified as noninterest expense.

Note 4 — Investment in AgFirst Farm Credit Bank

The Association is required to maintain ownership in the Bank of Class B and Class C stock as determined by the Bank. The Bank may require additional capital contributions to maintain its capital requirements.

Note 5 — Premises and Equipment

Premises and equipment consisted of the following:

	December 31,		
	2002	2001	2000
Land	\$ 110	\$ 110	\$ 110
Buildings and improvements	828	828	828
Furniture and equipment	819	792	785
	<u>1,757</u>	<u>1,730</u>	<u>1,723</u>
Less: accumulated depreciation	1,139	1,075	1,039
Total	<u>\$ 618</u>	<u>\$ 655</u>	<u>\$ 684</u>

Note 6 — Notes Payable to AgFirst Farm Credit Bank

The Association's indebtedness to the Bank represents borrowings by the Association to fund its loan portfolio. This indebtedness is collateralized by a pledge of substantially all of the Association's assets and the terms of the revolving lines of credit are governed by a general financing agreement. Interest rates on both variable and fixed rate notes payable are generally established loan-by-loan based on the Bank's marginal cost of funds, capital position, operating costs and return objectives. The interest rate is periodically adjusted by the Bank based upon agreement between the Bank and Association. The weighted average interest rates on the variable rate notes were 2.55 percent for LIBOR-based loans, 2.36 percent for Prime-based loans, and the weighted average remaining maturities were 3.6 years and 5.4 years, respectively, at December 31, 2002. The weighted average interest rate on the fixed rate and adjustable rate mortgage (ARM) notes payable which are match funded by the Bank was 4.97 percent and the weighted average remaining maturity was 6.0 years at December 31, 2002. The weighted average interest rate on all interest-bearing notes payable was 3.59 percent and the weighted average remaining maturity was 5.0 years at December 31, 2002.

Variable rate and fixed rate notes payable represent approximately 47.41 percent and 52.59 percent, respectively, of total notes payable at December 31, 2002.

The Bank, consistent with FCA regulations, has established limitations on the Association's ability to borrow funds based on specified factors or formulas relating primarily to credit quality and financial condition. At December 31, 2002, the Association's notes payable were within the specified limitations.

Note 7 — Members' Equity

A description of the Association's capitalization requirements, protection mechanisms, regulatory capitalization requirements and restrictions, and equities are provided below.

A. Protected Borrower Equity

Protection of certain borrower equity is provided under the Farm Credit Act which requires the Association, when retiring protected borrower equity, to retire such equity at par or stated value regardless of its book value. Protected borrower equity includes capital stock, participation certificates and allocated equities which were outstanding as of January 6, 1988, or were issued or allocated prior to October 6, 1988. If an Association is unable to retire protected borrower equity at par value or stated value, amounts required to retire this equity would be obtained from the Insurance Fund.

B. Capital Stock and Participation Certificates

In accordance with the Farm Credit Act and the Association's capitalization bylaws, each borrower is required to invest in Class C stock for agricultural loans, or participation certificates in the case of rural home and farm related business loans, as a condition of borrowing. The initial borrower investment, through either purchase or transfer, must be in an amount equal to the lesser of \$1 thousand or two percent of the amount of the loan. The Board of Directors may increase the amount of investment if necessary to meet the Association's capital needs. Loans designated for sale or sold into the Secondary Market on or after April 16, 1996 will have no voting stock or participation certificate purchase requirement if sold within 180 days following the date of designation.

The borrower acquires ownership of the capital stock or participation certificates at the time the loan is made, but usually does not make a cash investment. The aggregate par value is generally added to the principal amount of the related loan obligation. The Association retains a first lien on the stock or participation certificates owned by borrowers. Retirement of such equities will generally be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock or participation certificates.

C. Regulatory Capitalization Requirements and Restrictions

FCA’s capital adequacy regulations require the Association to achieve permanent capital of seven percent of risk-adjusted assets and off-balance-sheet commitments. Failure to meet the seven percent capital requirement can initiate certain mandatory and possibly additional discretionary actions by FCA that, if undertaken, could have a direct material effect on the Association’s financial statements. The Association is prohibited from reducing permanent capital by retiring stock or making certain other distributions to shareholders unless prescribed capital standards are met. FCA regulations also require that additional minimum standards for capital be achieved. These standards require all System institutions to achieve and maintain ratios as defined by FCA regulations. These required ratios are total surplus as a percentage of risk-adjusted assets of seven percent and of core surplus as a percentage of risk-adjusted assets of three and one-half percent. The Association’s permanent capital, total surplus and core surplus ratios at December 31, 2002 were 13.53 percent, 12.49 percent and 10.06 percent, respectively.

An FCA regulation empowers it to direct a transfer of funds or equities by one or more System institutions to another System institution under specified circumstances. The Association has not been called upon to initiate any transfers and is not aware of any proposed action under this regulation.

D. Description of Equities

The Association is authorized to issue or have outstanding Classes A and D Preferred Stock, Classes A, B and C Common Stock, Classes B and C Participation Certificates and such other classes of equity as may be provided for in amendments to the bylaws in such amounts as may be necessary to conduct the Association’s business. All stock and participation certificates have a par or face value of five dollars (\$5.00) per share.

The Association had the following shares outstanding at December 31, 2002:

Class	Protected	Shares Outstanding	
		Number	Aggregate Par Value
A Common/Nonvoting	Yes	38,709	\$ 194
B Common/Nonvoting	Yes	107,580	538
C Common/Voting	No	215,368	1,077
B Participation Certificates/Nonvoting	Yes	17,331	86
C Participation Certificates/Nonvoting	No	22,123	111
Total Capital Stock and Participation Certificates		401,111	\$ 2,006

Protected common stock and participation certificates are retired at par or face value in the normal course of business. At-risk common stock and participation certificates are retired at the sole discretion of the Board

at book value not to exceed par or face amounts, provided the minimum capital adequacy standards established by the Board are met.

Retained Earnings

The Association maintains an unallocated retained earnings account and an allocated retained earnings account. The minimum aggregate amount of these two accounts is determined by the Board. At the end of any fiscal year, if the retained earnings accounts otherwise would be less than the minimum amount determined by the Board as necessary to maintain adequate capital reserves to meet the commitments of the Association, the Association shall apply earnings for the year to the unallocated retained earnings account in such amounts as may be determined necessary by the Board. Unallocated retained earnings are maintained for each borrower to permit liquidation on a patronage basis.

The Association maintains an allocated retained earnings account consisting of earnings held and allocated to borrowers on a patronage basis. In the event of a net loss for any fiscal year, such allocated retained earnings account will be subject to full impairment in the order specified in the bylaws beginning with the most recent allocation.

The Association has a first lien and security interest on all retained earnings account allocations owned by any borrowers, and all distributions thereof, as additional collateral for their indebtedness to the Association. When the debt of a borrower is in default or is in the process of final liquidation by payment or otherwise, the Association, upon approval of the Board, may order any and all retained earnings account allocations owned by such borrower to be applied on the indebtedness.

Allocated equities shall be retired solely at the discretion of the Board; provided, however, that minimum capital standards established by the FCA and the Board are met. All nonqualified distributions are tax deductible only when redeemed.

At December 31, 2002, allocated members’ equity consisted of \$15,092 of qualified surplus and \$643 of nonqualified allocated surplus.

Patronage Distributions

Prior to the beginning of any fiscal year, the Board, by adoption of a resolution, may obligate the Association to distribute to borrowers on a patronage basis all or any portion of available net earnings for such fiscal year or for that and subsequent fiscal years. Patronage distributions are based on the proportion of the borrower’s interest to the amount of interest earned by the Association on its total loans unless another proportionate patronage basis is approved by the Board.

If the Association meets its capital adequacy standards after making the patronage distributions, the patronage distributions may be in cash, authorized stock of the Association, allocations of earnings retained in an allocated members' equity account, or any one or more of such forms of distribution. Patronage distributions of the Association's earnings may be paid on either a qualified or nonqualified basis, or a combination of both, as determined by the Board. A minimum of 20 percent of the total qualified patronage distribution to any borrower for any fiscal year shall always be paid in cash.

Dividends

The Association may declare noncumulative dividends on its capital stock and participation certificates provided the dividend rate does not exceed 20 percent of the par value of the respective capital stock and participation certificates. Such dividends may be paid solely on Classes A or D Preferred Stock, or on all classes of stock and participation certificates.

The rate of dividends paid on Class A Preferred Stock for any fiscal year may not be less than the rate of dividends paid on Classes A, B and C Common Stock or participation certificates for such year. The rate of dividends on Classes A, B and C Common Stock and participation certificates shall be at the same rate per share.

Dividends may not be declared if, after recording the liability, the Association would not meet its capital adequacy standards. No dividends were declared by the Association for any of the periods included in these financial statements.

Transfer

Classes A and D Preferred, Classes A, B and C Common Stocks, and Classes B and C Participation Certificates may be transferred to persons or entities eligible to purchase or hold such equities.

Impairment

Any net losses recorded by the Association shall first be applied against unallocated members' equity. To the extent that such losses would exceed unallocated members' equity, such losses would be applied consistent with the Association's bylaws and distributed pro rata to each share and/or unit outstanding in the class, in the following order:

1. Class C Common Stock and Class C Participation Certificates
2. Classes A and B Common Stock and Class B Participation Certificates
3. Classes A and D Preferred Stock

Liquidation

In the event of liquidation or dissolution of the Association, any assets of the Association remaining after payment or retirement of all liabilities should be distributed to the holders of the outstanding stock and participation certificates in the following order:

1. Holders of Classes A and D Preferred Stock
2. Holders of Classes A and B Common Stock and Class B Participation Certificates
3. Holders of Class C Common Stock and Class C Participation Certificates
4. Holders of allocated surplus evidenced by qualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed
5. Holders of allocated surplus evidenced by nonqualified written notices of allocation, in the order of year of issuance and pro rata by year of issuance, until the total amount of such allocated surplus has been distributed
6. Any remaining assets of the Association after such distributions shall be distributed to past and present Patrons on a patronage basis, to the extent practicable

E. Other Comprehensive Income (Loss)

The Association reports other comprehensive income (loss) in its Statement of Changes in Members' Equity. For the year ended December 31, 2002, the other comprehensive income (loss) results from a minimum pension liability adjustment of \$2,684 as a result of the funded status of the underlying plan.

Note 8 — Income Taxes

The provision (benefit) for income taxes follows:

	Year Ended December 31,		
	2002	2001	2000
Current:			
Federal	\$ (12)	\$ 87	\$ 5
State	(2)	12	2
Federal refunds related to long-term lending	—	(139)	—
	<u>(14)</u>	<u>(40)</u>	<u>7</u>
Deferred:			
Federal	(35)	27	(2)
State	—	3	—
	<u>(35)</u>	<u>30</u>	<u>(2)</u>
Total provision (benefit) for income taxes	<u>\$ (49)</u>	<u>\$ (10)</u>	<u>\$ 5</u>

In connection with the restructuring discussed in Note 1, the net deferred tax asset relating to the long-term lending activities was written off as of January 1, 2002 to reflect the change in tax status. The amount of this write-off was not significant. During 2001, the Association signed a settlement agreement with the IRS resolving the taxability of the prior years' earnings from its long-term mortgage lending activities. This settlement agreement was modeled after one used by another System ACA to reach a settlement agreement with the IRS in August 2000. As a result of this settlement, the Association recorded a tax refund of \$139, which was included as a component of the 2001 current income tax provision. In addition, the Association recorded \$70 in interest related to these refunds, which was included in Other Income in the accompanying Statements of Income. All such refunds have been received by the Association.

The provision (benefit) for income tax differs from the amount of income tax determined by applying the applicable U.S. statutory federal income tax rate to pretax income as follows:

	December 31,		
	2002	2001	2000
Federal tax at statutory rate	\$ 1,424	\$ 1,634	\$ 1,547
State tax, net	—	10	6
Patronage distributions	(1,057)	(1,588)	(1,534)
Tax-exempt FLCA earnings	(361)	—	—
Long-term lending related refunds	—	(139)	—
Deferred tax asset adjustment	(7)	—	—
Other	(48)	73	(14)
Provision (benefit) for income taxes	<u>\$ (49)</u>	<u>\$ (10)</u>	<u>\$ 5</u>

Deferred tax assets and liabilities result from the following at:

	December 31,		
	2002	2001	2000
Annual leave	\$ 6	\$ (6)	\$ 1
Postretirement benefits other than pensions	—	19	4
Depreciation (reclassified)	—	1	—
Gross deferred tax assets	<u>6</u>	<u>14</u>	<u>5</u>
Future Bank equity redemption	(4)	(30)	(6)
Pensions	(1)	(18)	(3)
Gross deferred tax liability	<u>(5)</u>	<u>(48)</u>	<u>(9)</u>
Net deferred tax asset (liability)	<u>\$ 1</u>	<u>\$ (34)</u>	<u>\$ (4)</u>

At December 31, 2002, deferred income taxes have not been provided by the Association on approximately \$0.5 million of patronage refunds received from the Bank prior to January 1, 1993. Such refunds, distributed in the form of stock, are subject to tax only upon conversion to cash. The tax liability related to future conversions is not expected to be material.

Note 9 — Employee Benefit Plans

The Association participates in a Districtwide defined benefit retirement plan. This plan is noncontributory and covers substantially all Association employees. Benefits are based on salary and years of service. The assets, liabilities and 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 the Association's salary expense as a percentage of the District's salary expense.

At December 31, 2002, the Accumulated Benefit Obligation (ABO) of the District's defined benefit plan exceeded the fair value of plan assets. In accordance with the provisions of SFAS No. 87, "Employers' Accounting for Pensions", (SFAS No. 87), the recognition of a minimum liability in the amount of the excess of the ABO over the fair value of plan assets is required. At December 31, 2002, the Association's allocated amount of minimum liability of \$1,467 was recognized. In conjunction with the recognition of the minimum liability, a reduction in Other Comprehensive Income of \$2,684 was recorded. The impact on deferred taxes was not significant.

The Association also participates in a districtwide Thrift Plan. The Thrift Plan requires the Association to match 50 percent of employee optional contributions up to a maximum employee contribution of 6 percent of total compensation.

The District sponsors a plan providing certain benefits (primarily health care) to its retirees. Certain Association charges related to this plan are an allocation of District charges based on the Association's proportional share of the plan liability.

The following is a table of retirement and postretirement benefits expenses (credits):

	2002	2001	2000
Pension	\$ 311	\$ 2	\$ 25
Thrift/deferred compensation	54	66	52
Other Postretirement benefits	<u>428</u>	<u>344</u>	<u>315</u>
Total	<u>\$ 793</u>	<u>\$ 412</u>	<u>\$ 392</u>

Note 10 — Intra-System Financial Assistance

The Farm Credit System Financial Assistance Corporation (Financial Assistance Corporation) was established in 1988 primarily to provide capital to institutions of the System experiencing financial difficulty. Such assistance was funded through the Financial Assistance Corporation's issuance of \$1.261 billion of 15-year U.S. Treasury-guaranteed debt. The interest rates on these issuances range from 8.80 percent to 9.45 percent. The repayment of this debt and related interest is the responsibility of System banks.

Each System bank may be required to pay premiums into the Insurance Fund based on its annual average loan principal outstanding. The Bank, in turn, may also assess the Association for insurance premiums based on the average principal outstanding of accrual and nonaccrual loans of the Association for each year. At December 31, 2002, the assets in the Insurance Fund aggregated \$1.839 billion. However, due to the authorized uses of the Insurance Fund, there is no assurance that such assets will be available or sufficient to ensure the payment of principal of, or interest on, insured debt securities in the event of a default by any System bank having primary liability thereon.

Note 11 — Related Party Transactions

In the ordinary course of business, the Association enters into loan transactions with officers and directors of the Association, their immediate families and other organizations with which such persons may be associated. Such loans are subject to special approval requirements contained in the FCA regulations and are made on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated borrowers.

Total loans to such persons at December 31, 2002 amounted to \$2,600. During 2002, \$1,813 of new loans were made and repayments totaled \$1,724. In the opinion of management, none of these loans outstanding at December 31, 2002 involved more than a normal risk of collectibility.

Note 12 — Commitments and Contingencies

The Association has various commitments outstanding and contingent liabilities as discussed elsewhere in these Notes to the Consolidated Financial Statements.

Note 13 — Financial Instruments with Off-Balance-Sheet Risk

In the normal course of business, the Association may participate in credit related financial instruments with off-balance-sheet risk to satisfy the financing needs of their borrowers. These financial instruments include commitments to extend credit and standby letters of credit.

Standby letters of credit are unconditional commitments issued by the Association to guarantee the performance of a customer to a third party. As of December 31, 2002, the Association had \$5,621 outstanding in such guarantees, predominantly with terms of one year or less.

At December 31, 2002, \$50,562 of commitments to extend credit were outstanding. Since many of these commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. However, these financial instruments have

off-balance-sheet credit risk because their amounts are not reflected on the Consolidated Balance Sheet until funded or drawn upon. The credit risk associated with issuing commitments and letters of credit is substantially the same as that involved in extending loans to borrowers and the same credit policies are applied by management. Upon fully funding a commitment, the credit risk amounts are equal to the contract amounts, assuming that borrowers fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower.

Note 14 — Disclosures About Fair Value Of Financial Instruments

The following table presents the carrying amounts and fair values of the Association's financial instruments at December 31, 2002, 2001 and 2000. The fair value of a financial instrument is generally defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

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

The estimated fair values of the Association's financial instruments are as follows:

	December 31, 2002		December 31, 2001	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash	\$ 2	\$ 2	\$ 3	\$ 3
Loans	\$ 240,891	\$ 245,814	\$ 223,041	\$ 223,747
Allowance for loan losses	5,320	—	5,459	—
Loans, net	<u>\$ 235,571</u>	<u>\$ 245,814</u>	<u>\$ 217,582</u>	<u>\$ 223,747</u>
Financial liabilities:				
Notes payable to AgFirst Farm Credit Bank	\$ 206,383	\$ 208,418	\$ 190,993	\$ 191,188
December 31, 2000				
	Carrying Amount	Estimated Fair Value		
Financial assets:				
Cash	\$ 3	\$ 3		
Loans	\$ 152,268	\$ 154,834		
Allowance for loan losses	5,447	—		
Loans, net	<u>\$ 146,821</u>	<u>\$ 154,834</u>		
Financial liabilities:				
Notes payable to AgFirst Farm Credit Bank	\$ 120,470	\$ 122,062		

A description of the methods and assumptions used to estimate the fair value of each class of the Association's financial instruments for which it is practicable to estimate that value follows:

- A. **Cash:** The carrying value is a reasonable estimate of fair value.
- B. **Loans:** Because no active market exists for the Association's loans, fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans would be made to borrowers with similar credit risk. As the discount rates are based on the Bank's loan rates, as well as management estimates, management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale.

For purposes of determining fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics based upon repricing and credit risk. Expected future cash flows and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

Fair value of loans in a nonaccrual status is estimated to be the carrying amount less specific reserves.

The carrying value of accrued interest approximates its fair value.

- C. **Investment in AgFirst Farm Credit Bank:** Estimating the fair value of the Association's investment in the Bank is not practicable because the stock is not traded. As described in Note 4, the net investment is a requirement of borrowing from the Bank and is carried at cost plus allocated equities in the accompanying balance sheet. The Association owns 2.11 percent of the issued stock of the Bank as of December 31, 2002 net of any reciprocal investment. As of that date, the Bank's assets totaled \$14.7 billion and shareholders' equity totaled \$757 million. The Bank's earnings were \$194 million during 2002.

In addition, the Association has an investment of \$202 related to other Farm Credit institutions.

- D. **Notes Payable to AgFirst Farm Credit Bank:** The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the notes payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

- E. **Commitments to Extend Credit and Standby Letters of Credit:** The estimated market value of off-balance-sheet commitments is nominal since the committed rate approximates current rates offered for commitments with similar rate and maturity characteristics and since the related credit risk is not significant.

Note 15 — Quarterly Financial Information (Unaudited)

Quarterly results of operations for the years ended December 31, 2002, 2001 and 2000 follow:

	2002				
	First	Second	Third	Fourth	Total
Net interest income	\$ 1,561	\$ 1,646	\$ 1,716	\$ 1,593	\$ 6,516
Provision for (reversal of) loan losses	—	250	750	150	1,150
Noninterest income (expense), net	(298)	(433)	(425)	26	(1,130)
Net income (loss)	\$ 1,263	\$ 963	\$ 541	\$ 1,469	\$ 4,236

	2001				
	First	Second	Third	Fourth	Total
Net interest income	\$ 1,610	\$ 1,691	\$ 1,692	\$ 1,557	\$ 6,550
Provision for (reversal of) loan losses	—	—	—	150	150
Noninterest income (expense), net	(398)	(427)	(554)	(205)	(1,584)
Net income (loss)	\$ 1,212	\$ 1,264	\$ 1,138	\$ 1,202	\$ 4,816

	2000				
	First	Second	Third	Fourth	Total
Net interest income	\$ 1,627	\$ 1,652	\$ 1,794	\$ 1,548	\$ 6,621
Provision for (reversal of) loan losses	—	—	—	—	—
Noninterest income (expense), net	(439)	(519)	(549)	(544)	(2,051)
Net income (loss)	\$ 1,188	\$ 1,133	\$ 1,245	\$ 1,004	\$ 4,570