

# **FIRST QUARTER 2006**

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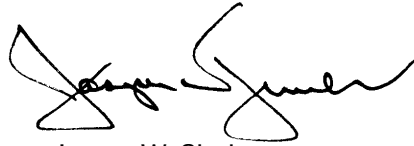
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Jasper W. Shuler  
Chief Executive Officer



Dale W. Player  
Chairman of the Board

April 28, 2006

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

*(dollars in thousands)*

The following commentary reviews the financial condition and results of operations of Pee Dee Farm Credit ACA, (Association) for the period ended March 31, 2006. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2005 Annual Report of the Association.

## LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio is diversified over a range of agricultural commodities in our region, including tobacco, poultry, swine and forestry. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm income in the area, somewhat impacts the level of dependency on a given commodity. Approximately one third of the portfolio has significant outside income to diversify dependence on agriculture, consisting of lifestyle loans and loans to less than full-time farmers with retirement income, salaried income and non-agricultural business income. Further, approximately twenty-two percent of the assets carry federal guarantees as a risk management tool.

The gross loan volume of the Association as of March 31, 2006, was \$290,416, an increase of \$3,042 as compared to \$287,374 at December 31, 2005. Net loans outstanding at March 31, 2006, were \$289,666 as compared to \$286,363 at December 31, 2005. The Association has investment securities that are classified as held to maturity in the amount of \$10,882 at March 31, 2006 compared to \$12,538 at December 31, 2005. The Association has entered into commitments to acquire Successor-in-Interest Contracts (SIIC), beginning in the fourth quarter of 2005. As of March 31, 2006, the Association had \$120,102 in other investments for SIIC, compared to \$73,189 at December 31, 2005. Net loans and investments accounted for 97.15 percent of total assets at March 31, 2006, as compared to 96.23 percent of total assets at December 31, 2005.

The increase in gross and net loan volume during the reporting period is attributed primarily to the seasonal lending upswing. The Association continues to review and engage in participation opportunities, as well as customer opportunities within the territory.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level, however, and credit administration remains satisfactory. Nonaccrual loans increased from \$263 at December 31, 2005, to \$334 at March 31, 2006. Several loans including both farm and home loans became more than ninety days delinquent during the quarter and were moved to nonaccrual status.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at March 31, 2006, was \$750, compared to \$1,011 at December 31, 2005, and was considered by management to be adequate to cover possible losses. The Association recognized a reversal of loan losses of \$211 during the period ending March 31, 2006.

## Geographic Distribution of Loans by State at March 31, 2006:

	<u>Percentage</u>
South Carolina	63.37%
Alaska	.09
Arizona	.28
Arkansas	.08
California	1.08
Colorado	.28
Florida	12.53
Georgia	12.30
Kentucky	.20
Maine	.02
Maryland	.05
New Jersey	.15
New York	.20
North Carolina	3.83
Tennessee	.99
Texas	3.34
Virginia	.13
Washington	.68
Wisconsin	.40
	<u>100.00%</u>

## Distribution of Loans by Loan Type at March 31, 2006:

	<u>Percentage</u>	
Agricultural Production:		
Cash grains	2.01%	
Tobacco	10.23	
Livestock	6.53	
Cotton	3.81	
Poultry	10.85	
General row crops	1.36	
Forestry	7.96	
Other commodities	1.32	
		44.07%
Agricultural real estate mortgage	20.70	
Aquatics	.09	
Rural home	3.33	
Notes receivable sales contracts/PMMs	1.27	
Basic processing	15.74	
Farm-related business	2.99	
Nonaccruals	.11	
Participations purchased	60.85	
Participations sold	(49.15)	
		<u>100.00%</u>

## RESULTS OF OPERATIONS

### *For the three months ended March 31, 2006*

Net income for the three months ended March 31, 2006, totaled \$1,941, as compared to \$1,480 for the same period in 2005. Net interest income increased \$183, for the three months ended March 31, 2006, as compared to the same period in 2005. Increased loan and investment volume along with rising interest rates, are the primary reasons for the increase in net interest income.

At March 31, 2006, interest income on accruing loans increased \$1,484 compared to \$3,765 at March 31, 2005. Nonaccrual income was \$22 for the three months ended March 31, 2006, as compared to \$149 for the same period in 2005. Interest income on investment securities decreased to \$178 from the March 31, 2005 amount of \$183. Interest income was \$1,628 on other investments (SIIC) for the three months ended March 31, 2006, while there was not any during the same period in 2005. Interest expense increased \$2,797 for the three months ended March 31, 2006, as compared to the comparable period of 2005. This was a result of increased volume and rising interest rates.

Noninterest income for the three months ended March 31, 2006, totaled \$1,227, as compared to \$874 for the same period of 2005, an increase of \$353. The increase is primarily the result of increased patronage income, loan fees, and other income. Noninterest expense for the three months ended March 31, 2006, increased \$297 compared to the same period of 2005. Increases in salaries and employee benefits, other operating expenses and insurance fund premiums were the main causes for the increase.

## FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (the Bank) through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at March 31, 2006, was \$381,703 as compared to \$334,915 at December 31, 2005. The increase during the period is primarily attributed to increased loan and investment volume and interest rates.

## CAPITAL RESOURCES

Total members' equity at March 31, 2006, increased to \$43,557 from the December 31, 2005, total of \$41,666. The increase is primarily attributed to the increase in retained earnings in excess of the reduction of capital stock, participation certificates and revolved equities.

Total capital stock and participation certificates were \$1,645 on March 31, 2006, compared to \$1,693 on December 31, 2005. This decrease is attributed to the retirement of protected stock and participation certificates on loans liquidated in the normal course of business, new loans being capitalized at new lower regulatory levels, and the annual retirement of B stock.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of March 31, 2006, the Association's total surplus ratio and core surplus ratio were 14.40 percent and 11.51 percent, respectively, and the permanent capital ratio was 14.86 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

**NOTE:** Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 378, or writing Jay Wise, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, [www.agfirst.com](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-741-7332, writing Joan Boice, Corporate Secretary, Pee Dee Farm Credit, ACA, P.O. Box 13209, Florence, SC 29504, or accessing the website, [www.peedeefarmcredit.com](http://www.peedeefarmcredit.com). The Association prepares a quarterly report within 45 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

*Pee Dee Farm Credit, ACA*  
**Consolidated Balance Sheets**

<i>(dollars in thousands)</i>	<b>March 31, 2006</b> <i>(unaudited)</i>	<b>December 31, 2005</b> <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 158	\$ —
Investment securities, held to maturity	10,882	12,538
Loans	290,416	287,374
Less: allowance for loan losses	750	1,011
Net loans	289,666	286,363
Other investments	120,102	73,189
Accrued interest receivable	3,703	3,687
Investment in other Farm Credit institutions	4,123	4,080
Premises and equipment, net	409	444
Other property owned	—	49
Prepaid retirement expense	2,983	3,082
Due from AgFirst Farm Credit Bank	—	2,859
Other assets	959	390
Total assets	<u>\$ 432,985</u>	<u>\$ 386,681</u>
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 381,703	\$ 334,915
Accrued interest payable	1,805	1,383
Patronage refund payable	153	1,975
Other liabilities	5,767	6,742
Total liabilities	<u>389,428</u>	<u>345,015</u>
Commitments and contingencies		
<b>Members' Equity</b>		
Protected borrower equity	468	522
Capital stock and participation certificates	1,177	1,171
Retained earnings		
Allocated	23,543	23,977
Unallocated	18,369	15,996
Total members' equity	<u>43,557</u>	<u>41,666</u>
Total liabilities and members' equity	<u>\$ 432,985</u>	<u>\$ 386,681</u>

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

*Pee Dee Farm Credit, ACA*

# Consolidated Statements of Income

*(unaudited)*

<i>(dollars in thousands)</i>	<b>For the three months ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Interest Income</b>		
Loans	\$ 5,271	\$ 3,914
Investment securities	178	183
Other	1,628	—
	7,077	4,097
<b>Interest Expense</b>		
Notes payable to AgFirst Farm Credit Bank	5,051	2,254
Net interest income	2,026	1,843
Provision for (reversal of allowance for) loan losses	(211)	—
	2,237	1,843
<b>Noninterest Income</b>		
Loan fees	328	308
Fees for financially related services	7	9
Equity in earnings of other Farm Credit institutions	783	475
Gains (losses) on other property owned, net	1	—
Other noninterest income	108	82
	1,227	874
<b>Noninterest Expense</b>		
Salaries and employee benefits	880	800
Occupancy and equipment	86	83
Insurance Fund premium	99	24
Other operating expenses	457	318
	1,522	1,225
Income before income taxes	1,942	1,492
Provision (benefit) for income taxes	1	12
	1,941	1,480
Net income	\$ 1,941	\$ 1,480

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

*Pee Dee Farm Credit, ACA*

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

*(dollars in thousands)*

	<b>Protected Borrower Capital</b>	<b>Capital Stock and Participation Certificates</b>	<b>Retained Earnings</b>		<b>Total Members' Equity</b>
			<b>Allocated</b>	<b>Unallocated</b>	
Balance at December 31, 2004	\$ 584	\$ 1,172	\$ 22,225	\$ 15,133	\$ 39,114
Net income				1,480	1,480
Protected borrower equity retired	(49)				(49)
Capital stock/participation certificates issued		48			48
Capital stock/participation certificates retired		(27)			(27)
Retained earnings retired			(7)		(7)
Distribution adjustment			234	(254)	(20)
Balance at March 31, 2005	<u>\$ 535</u>	<u>\$ 1,193</u>	<u>\$ 22,452</u>	<u>\$ 16,359</u>	<u>\$ 40,539</u>
Balance at December 31, 2005	\$ 522	\$ 1,171	\$ 23,977	\$ 15,996	\$ 41,666
Net income				1,941	1,941
Protected borrower equity retired	(54)				(54)
Capital stock/participation certificates issued		35			35
Capital stock/participation certificates retired		(29)			(29)
Distribution adjustment			(434)	432	(2)
Balance at March 31, 2006	<u>\$ 468</u>	<u>\$ 1,177</u>	<u>\$ 23,543</u>	<u>\$ 18,369</u>	<u>\$ 43,557</u>

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

# Notes to the Consolidated Financial Statements

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

## NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

A description of the organization and operations of Pee Dee Farm Credit, ACA (the Association), the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2005, are contained in the 2005 Annual Report to Shareholders. These unaudited first quarter 2006 consolidated financial statements should be read in conjunction with the 2005 Annual Report to Shareholders.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles. The results for the three months ended March 31, 2006, are not necessarily indicative of the results to be expected for the year ending December 31, 2006.

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

The Association maintains an allowance for loan losses in accordance with generally accepted accounting principles. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of March 31, 2006, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

*Investment Securities:* The Association, as permitted under the FCA regulations, holds investments for purposes of maintaining a liquidity reserve, managing short-term surplus funds and managing interest rate risk. The Association's investments are classified as held to maturity and accordingly have been reported at amortized cost. Purchased premiums and discounts are amortized or accreted using the effective interest method over the term of the respective security.

The Association reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered an impairment, is temporary or permanent. In the event of permanent impairment, the cost basis of the investment would be written down to its fair value, and the realized loss would be included in current earnings.

## NOTE 2 – ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses follows:

Balance at 12-31-04	\$ 1,000
(Reversal of) provision for loan losses	—
Recoveries, net of loans charged off	<u>2</u>
Balance at 3-31-05	<u>\$ 1,002</u>
Balance at 12-31-05	\$ 1,011
(Reversal of) provision for loan losses	(211)
Loans (charged off), net of recoveries	<u>(50)</u>
Balance at 3-31-06	<u>\$ 750</u>

## NOTE 3 – EMPLOYEE BENEFIT PLANS

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

The following is a table of retirement and postretirement benefit expense for the three months ended March 31, 2006:

	<b>For the three months ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
Pension	\$ 99	\$ 97
Thrift/deferred compensation	19	14
Other postretirement benefits	<u>70</u>	<u>119</u>
Total	<u>\$ 188</u>	<u>\$ 230</u>

As of March 31, 2006, no contributions have been made to the pension plan for 2006. Actuarial projections as of the last plan measurement date (September 30, 2005) did not anticipate any contributions for 2006; however, market conditions could impact discount rates and return on plan assets which could change this expectation, making contributions necessary before the next plan measurement date.