

# **SECOND QUARTER 2008**

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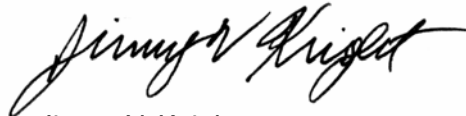
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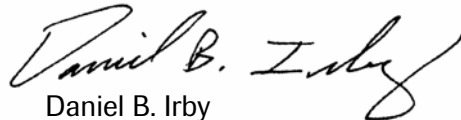
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Jimmy V. Knight  
Chief Executive Officer



Daniel B. Irby  
Chief Financial Officer



Walter S. Farr  
Chairman of the Board

July 24, 2008

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

*(dollars in thousands)*

The following commentary reviews the financial condition and results of operations of Farm Credit of Southwest Florida, ACA (the Association) for the period ended June 30, 2008. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2007 Annual Report of the Association.

## **LOAN PORTFOLIO**

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

The gross loan volume of the Association as of June 30, 2008, was \$179,508, a decrease of \$78,737 as compared to \$258,245 at December 31, 2007. Net loans outstanding at June 30, 2008, were \$177,212 as compared to \$258,013 at December 31, 2007. Net loans accounted for 72.52 percent of total assets at June 30, 2008, as compared to 80.65 percent of total assets at December 31, 2007. The decrease in gross and net loan volume during the reporting period is largely attributed to the sale of loan assets through the AgFirst Farm Credit Bank Capitalization Participation Pool (CPP).

The Association maintains an allowance for loan losses at a level considered adequate to provide for probable and estimable credit losses within the loan portfolio. The Association increases the allowance by providing a provision for loan losses in the income statement. Loan losses are recorded against and serve to decrease the allowance when management determines that any portion of a loan is uncollectible. Any subsequent recoveries are added to the allowance. Managements' evaluations consider factors which include, among many other things, loan loss experience, portfolio quality, loan portfolio composition, current agricultural production conditions, and general economic conditions. The allowance for loan losses at June 30, 2008 was \$2,296 compared to \$232 at December 31, 2007, and was

considered by management to be adequate to cover probable losses.

## **RESULTS OF OPERATIONS**

### ***For the three and six months ended June 30, 2008***

Net loss for the three months ended June 30, 2008, totaled \$(458), as compared to net income of \$2,142 for the same period in 2007. Net interest income decreased \$628 for the three months ended June 30, 2008, as compared to the same period in 2007. Net interest income after provision for loan losses decreased \$1,811 or 120.49 percent as compared to the same period in 2007.

Net income for the six months ended June 30, 2008, totaled \$1,093, as compared to \$3,949 for the same period in 2007. Net interest income decreased \$689 for the six months ended June 30, 2008, as compared to the same period in 2007. Net interest income after provision for loan losses decreased \$2,791 or 89.37 percent as compared to the same period in 2007.

For both the three and six month periods, net interest income decreased primarily due to the sale of loan assets through the CPP. The sold loans generate income in the form of patronage. Net interest income after provision for loan losses decreased for both the three and six month periods primarily due to specific loss reserves established for loans placed on nonaccrual in 2008.

Non-interest income for the three months ended June 30, 2008, totaled \$1,276, as compared to \$2,273 for the same period of 2007, a decrease of \$997. Non-interest expense for the three months ended June 30, 2008, decreased \$208 compared to the same period of 2007.

Non-interest income for the six months ended June 30, 2008, totaled \$3,881, as compared to \$4,201 for the same period of 2007, a decrease of \$320. Non-interest expense for the six months ended June 30, 2008, decreased \$232 compared to the same period of 2007.

The decrease in non-interest income for both the three and six month periods is primarily due to decreased accrued earnings for non-CPP patronage from other Farm Credit Institutions and AgFirst Farm Credit Bank. The decrease in non-interest expense for both the three and six month

periods is primarily due to decreased incentive compensation costs and the changes made in payment schedules for controllable operating costs associated with the normal course of business.

## FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (the Bank) through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The Bank advances funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at June 30, 2008, was \$193,147 as compared to \$260,052 at December 31, 2007. The decrease is associated with the sale of loan assets through the CPP.

## CAPITAL RESOURCES

Total members' equity at June 30, 2008, decreased to \$46,985 from the December 31, 2007, total of \$51,569. The decrease is primarily due to the revolvment of surplus back to members.

Total capital stock and participation certificates were \$882 on June 30, 2008, compared to \$937 on December 31, 2007. The decrease is attributed to lower loan volume allowing capital stock and participation certificates to be retired.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2008, the Association's total surplus ratio and core surplus ratio were 17.04 percent and 11.44 percent, respectively, and the permanent capital ratio was 17.34 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

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**NOTE:** Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank (AgFirst). 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 Stephen Gilbert, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst 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 1-800-307-5677 ext. 141, or writing Lori Langfang, Controller, Farm Credit of Southwest Florida, ACA 330 N. Brevard Ave 34266, or accessing the website, [www.farmcreditswfl.com](http://www.farmcreditswfl.com). The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

*Farm Credit of Southwest Florida, ACA*  
**Consolidated Balance Sheets**

<i>(dollars in thousands)</i>	<b>June 30, 2008</b> <i>(unaudited)</i>	<b>December 31, 2007</b> <i>(audited)</i>
<b>Assets</b>		
Cash	\$ —	\$ 64
Investment securities:		
Held to maturity (fair value of \$40,162 and \$36,599 respectively)	40,496	36,958
Total investment securities	40,496	36,958
Loans	179,508	258,245
Less: allowance for loan losses	2,296	232
Net loans	177,212	258,013
Accrued interest receivable	1,590	2,617
Investment in other Farm Credit institutions	16,723	11,166
Premises and equipment, net	1,057	1,072
Due from AgFirst Farm Credit Bank	2,575	5,247
Other assets	4,711	4,768
Total assets	\$ 244,364	\$ 319,905
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 193,147	\$ 260,052
Accrued interest payable	619	1,274
Patronage refund payable	37	2,646
Other liabilities	3,576	4,364
Total liabilities	197,379	268,336
Commitments and contingencies		
<b>Members' Equity</b>		
Protected borrower equity	340	356
Capital stock and participation certificates	542	581
Retained earnings		
Allocated	21,337	26,030
Unallocated	24,961	24,827
Accumulated other comprehensive income (loss)	(195)	(225)
Total members' equity	46,985	51,569
Total liabilities and members' equity	\$ 244,364	\$ 319,905

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

*Farm Credit of Southwest Florida, ACA*  
**Consolidated Statements of Operations**

*(unaudited)*

<i>(dollars in thousands)</i>	<b>For the three months ended June 30,</b>		<b>For the six months ended June 30,</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
<b>Interest Income</b>				
Investment securities	\$ 327	\$ 455	\$ 810	\$ 874
Loans	2,452	4,387	5,633	8,753
Total interest income	2,779	4,842	6,443	9,627
<b>Interest Expense</b>				
Notes payable to AgFirst Farm Credit Bank	1,921	3,356	4,062	6,557
Net interest income	858	1,486	2,381	3,070
Provision for (reversal of allowance for) loan losses	1,166	(17)	2,049	(53)
Net interest income after provision for (reversal of allowance for) loan losses	(308)	1,503	332	3,123
<b>Noninterest Income</b>				
Loan fees	155	81	400	261
Equity in earnings of other Farm Credit institutions	1,099	2,054	3,422	3,751
Gains (losses) on other property owned, net	1	2	3	3
Other noninterest income	21	136	56	186
Total noninterest income	1,276	2,273	3,881	4,201
<b>Noninterest Expense</b>				
Salaries and employee benefits	890	1,016	1,980	2,074
Occupancy and equipment	89	92	188	200
Insurance Fund premium	61	82	125	160
Other operating expenses	386	444	825	916
Total noninterest expense	1,426	1,634	3,118	3,350
Income (loss) before income taxes	(458)	2,142	1,095	3,974
Provision (benefit) for income taxes	—	—	2	25
Net income (loss)	\$ (458)	\$ 2,142	\$ 1,093	\$ 3,949

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

*Farm Credit of Southwest Florida, ACA*

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

*(dollars in thousands)*

	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2006	\$ 508	\$ 601	\$ 25,779	\$ 24,871	\$ —	\$ 51,759
Net income				3,949		3,949
Protected borrower equity retired	(9)					(9)
Capital stock/participation certificates issued/(retired), net		(61)				(61)
Patronage distribution						
Cash				(350)		(350)
Allocated retained earnings			261	(261)		—
Nonqualified allocated retained earnings			1,135	(1,135)		—
Retained earnings retired			(5,300)			(5,300)
Patronage distribution adjustment			(11)	18		7
Balance at June 30, 2007	\$ 499	\$ 540	\$ 21,864	\$ 27,092	\$ —	\$ 49,995
Balance at December 31, 2007	\$ 356	\$ 581	\$ 26,030	\$ 24,827	\$ (225)	\$ 51,569
Net income				1,093		1,093
Protected borrower equity retired	(16)					(16)
Capital stock/participation certificates issued/(retired), net		(39)				(39)
Retained earnings retired			(5,513)			(5,513)
Patronage distribution adjustment			820	(939)		(119)
Employee benefit plans adjustments				(20)	30	10
Balance at June 30, 2008	\$ 340	\$ 542	\$ 21,337	\$ 24,961	\$ (195)	\$ 46,985

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

*Farm Credit of Southwest Florida, ACA*

# Notes to the Consolidated Financial Statements

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

**NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

The accompanying financial statements include the accounts of Farm Credit of Southwest Florida, ACA (the Association). A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2007, are contained in the 2007 Annual Report to Shareholders. These unaudited second quarter 2008 consolidated financial statements should be read in conjunction with the 2007 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 (GAAP) and prevailing practices within the banking industry. The results for the six months ended June 30, 2008, are not necessarily indicative of the results to be expected for the year ending December 31, 2008.

Certain amounts in the prior period's consolidated financial statements may have been reclassified to conform to the current period's 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 GAAP. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of June 30, 2008, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

In December 2007, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141R, "Business Combinations" (SFAS 141R). SFAS 141R requires business combinations to be accounted for under the acquisition method of accounting (previously called the purchase method). The acquisition method requires (a) identifying the acquirer, (b) determining the acquisition date, (c) recognizing and measuring the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree, at their acquisition date fair values, and (d) recognizing and measuring goodwill or a gain from a bargain purchase. SFAS 141R should be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first

annual reporting period beginning on or after December 15, 2008. Early application is prohibited. The Association is still evaluating the provisions of SFAS 141R, but believes that its adoption will significantly impact its accounting for combinations/acquisitions that may occur in 2009 and beyond.

**NOTE 2 – ALLOWANCE FOR LOAN LOSSES**

An analysis of the allowance for loan losses follows:

	<b>For the six months ended June 30,</b>	
	<b>2008</b>	<b>2007</b>
Balance at beginning of period	\$ 232	\$ 187
Provision for (reversal of) loan losses	2,049	(53)
Loans (charged off), net of recoveries	15	14
Balance at end of period	<u>\$ 2,296</u>	<u>\$ 148</u>

**NOTE 3 – EMPLOYEE BENEFIT PLANS**

The following is a table of retirement and other postretirement benefit expenses for the Association:

	<b>For the six months ended June 30,</b>	
	<b>2008</b>	<b>2007</b>
Pension	\$ 147	\$ 160
401(k)	42	38
Other postretirement benefits	37	37
Total	<u>\$ 226</u>	<u>\$ 235</u>

The following is a table of retirement and other postretirement benefit contributions for the Association:

	<b>Actual YTD Through 6/30/08</b>	<b>Projected Contributions For Remainder of 2008</b>	<b>Projected Total Contributions 2008</b>
Pension	\$ -	\$ -	\$ -
Other postretirement benefits	21	31	52
Total	<u>\$ 21</u>	<u>\$ 31</u>	<u>\$ 52</u>

Market conditions could impact discount rates and return on plan assets which could change the above contribution projections by making additional contributions necessary before the next plan measurement date.

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In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans (SFAS 158)*, which required the recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. The balance sheet recognition provisions of SFAS 158 were adopted at December 31, 2007 by the Association.

SFAS 158 also requires that employers measure the benefit obligation and plan assets as of the fiscal year end for fiscal years ending after December 15, 2008. In fiscal 2007 and earlier, a September 30 measurement date was used for pension and other postretirement benefit plans. The Standard provides two approaches for an employer to transition to a fiscal year end measurement date. The approach applied by the Association allows for the use of the measurements determined for the prior year end. Under this alternative, pension and other postretirement benefit expense measured for the three-month period October 1, 2007 to December 31, 2007 (determined using the September 30, 2007 measurement date) is reflected as an adjustment to beginning 2008 unallocated retained earnings. As a result, the Association decreased unallocated retained earnings and increased the pension liability by \$20 thousand.

Upon adoption, SFAS 158 further required the determination of the fair value of plan assets and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of accumulated other comprehensive income (AOCI). These amounts are subsequently recognized as components of net periodic benefit costs over time. For the first six months of 2008, \$30 thousand has been recognized as a credit to accumulated other comprehensive income and a debit to pension expense to reflect the amortization of the components previously recognized in AOCI.

Further details regarding employee benefit plans and adoption of SFAS 158 are contained in the 2007 Annual Report to Shareholders.