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*Southwest Georgia Farm Credit, ACA*

# **THIRD QUARTER 2007**

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Richard S. Monson  
President/CEO



Bobby J. Brooks  
Chairman of the Board

October 25, 2007

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

*(dollars in thousands)*

The following commentary reviews the financial condition and results of operations of Southwest Georgia Farm Credit, ACA (Association) for the period ended September 30, 2007. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2006 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit committee of the Board of Directors.

## **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 peanuts, cotton, vegetables, livestock, dairy, poultry, timber, pecans, landlords and rural home loans. These major farm commodity groups represent approximately \$420,615 or 81.10 percent of the loan portfolio as of September 30, 2007. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the opportunities for non-farm income in the area, somewhat impacts the level of dependency on a given commodity.

Southwest Georgia has experienced drought weather conditions during the first part of the crop season. Peanut harvest is behind schedule due to delays in planting and is in process at this time. Despite the summer drought, peanut yields are good due to irrigation and timely rainfall. Peanut prices are the highest in years. Georgia's pecan crop is on target to be the best in years and the next few weeks will enter a critical time for water. The harvest of pecans starts in mid-October and runs through Thanksgiving.

Investment securities classed as held to maturity as of September 30, 2007 was \$36,178, an increase of \$4,172 compared to \$32,006 at December 31, 2006. The gross loan volume of the Association as of September 30, 2007, was \$452,259, a decrease of \$25,149 as compared to \$477,408 at December 31, 2006. Net loans outstanding at September 30, 2007, were \$451,739 as compared to \$476,981 at December 31, 2006, a decrease of \$25,242. Total assets at September 30, 2007 were \$604,520, compared to \$630,120 at December 31, 2006, a decrease of \$25,600. The decrease in total assets was primarily in loans because of the sale of loans into the AgFirst Capital Participation Pool. Net loans and Investments accounted for 93.47 percent of total assets at September 30, 2007, as compared to 94.17 percent of total assets at December 31, 2006.

The decrease in gross and net loan volume during the reporting period is attributed primarily to the sale of loans into the AgFirst Capital Participation pool. The short-term portfolio, which is heavily influenced by operating-type loans, normally reaches a peak between August and September and declines in the fall months as farm commodities are marketed and proceeds are applied to the operating loans.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level and credit administration remains satisfactory. The Association has a portfolio management policy and plan in place to address portfolio risk and the portfolio is monitored. Nonaccrual loans decreased from \$102 at December 31, 2006, to \$95 at September 30, 2007. This was a decrease of \$7, which was attributed to a reinstatement to accrual.

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 September 30, 2007, was \$520 compared to \$427 as of December 31, 2006 an increase of \$93 primarily because of a provision to the allowance for loan loss. The provision was due to the sale of USDA guaranteed loan volume being replaced by volume that was not guaranteed. In the calculation of the Allowance for loan loss, guaranteed loans are not considered in the FAS 5 general volume calculation. Since the loan volume was replaced by nonguaranteed volume, the FAS 5 general balance increased and caused the need for a provision to the allowance for loan loss. The allowance at September 30, 2007 was considered by management to be adequate to cover possible losses.

## **RESULTS OF OPERATIONS**

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

Net income for the three months ended September 30, 2007, totaled \$3,002, as compared to \$3,202 for the same period in 2006, a decrease of \$200. Net interest income decreased \$376, for the three months ended September 30, 2007, as compared to the same period in 2006. At September 30, 2007, interest income on loans decreased \$601 compared to September 30, 2006. At September 30, 2007, interest income on Investment securities was \$557, a decrease of \$33 compared to same period 2006. Other Interest income was \$1,068 at September 30, 2007, a decrease of \$109 compared to same period 2006. Nonaccrual income was \$41 for the three months ended September 30, 2007, an increase of \$41 from the three months ended September 2006. Interest expense decreased \$458, for the three months ended September 30, 2007, as compared to September 30, 2006. The decrease in interest income is primarily the result of decreased loan volume due to selling a significant portion of the USDA loans, and due to the sale of loans to AgFirst into the Capital Participation Pool.

Noninterest income for the three months ended September 30, 2007, totaled \$1977, as compared to \$1,601 for the same period in 2006, an increase of \$376. Noninterest expense for the three months ended September 30, 2007 totaled \$1,992, as compared to \$1,794 for the same period in 2006, an increase of \$198. A benefit for income taxes was recorded in the amount of \$20 for the three months ended compared to a benefit in the amount of \$22 for the same period in 2006, a decrease of tax benefit in the amount of \$2.

#### ***For the nine months ended September 30, 2007***

Net income for the nine months ended September 30, 2007, totaled \$8,860, as compared to \$8,938 for the same period in 2006, a decrease of \$78. This decrease is attributed to an increase in interest income on loans and investment of \$1,013, an increase in non-interest income of \$1,148 offset by an increase of interest expense of \$1,480, an increase in non-interest expense of \$662 and an increase of \$6 in income taxes. Nonaccrual income was \$41 for the nine months ended September 30, 2007 an increase of \$41 as compared to the nine months ended September 30, 2006.

Non-interest income for the nine months ended September 30, 2007, totaled \$5,624, compared to \$4,476 for the same period in 2006, an increase of \$1,148. The increase resulted from an increase of \$1,223 from equity in earnings of AgFirst Farm Credit Bank (the Bank), offset by a decrease in loan fees of \$60, a decrease in fees for financially related services of \$6, and a decrease in other noninterest income of \$9.

Non-interest expense for the nine months ended September 30, 2007 totaled \$5,832, compared to \$5,170 for the same period in 2006, an increase of \$662. The increase resulted from an increase in salaries and employee benefits of \$504, an increase in insurance premium of \$8, an increase in other operating expense of \$156, and an increase in losses on other property owned of \$7, offset by a decrease in occupancy and equipment of \$13. The Association made a provision for income taxes of \$11 for the nine months ended September 30, 2007 as compared to a provision for income taxes of \$5 in 2006, an increase of \$6 in tax expense compared to September 2006.

#### **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 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 September 30, 2007, was \$523,888 as compared to \$547,249 at December 31, 2006. The decrease during the period is primarily a result of selling a significant portion of the USDA loans, the annual SIIC tobacco payment, the sale of loans to AgFirst into the capital participation pool and payments in the normal course of business.

#### **PENSION ACCOUNTING UPDATE**

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

#### **CAPITAL RESOURCES**

Total members' equity at September 30, 2007, increased \$6,160 from the December 31, 2006, total of \$66,497. The increase is primarily attributed to year to date net income rolling into unallocated retained earnings. Total capital stock and participation certificates were \$1,507 on September 30, 2007, compared to \$1,543 on December 31, 2006.

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 September 30, 2007, the Association's total surplus ratio and core surplus ratio were 11.49 percent and 9.78 percent, respectively, and the permanent capital ratio was 11.74 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

**NOTE:** Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 316, or writing Wanda Martin, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, [www.agfirst.com](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-229-246-8032 or 1-800-844-2615, writing Belinda H. Robertson, Chief Financial Officer, Southwest Georgia Farm Credit, ACA, P. O. Box 790, Bainbridge, Georgia 39818-0790 or accessing the website, [www.swgafarmcredit.com](http://www.swgafarmcredit.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.

*Southwest Georgia Farm Credit, ACA*  
**Consolidated Balance Sheets**

<i>(dollars in thousands)</i>	<b>September 30, 2007</b> <i>(unaudited)</i>	<b>December 31, 2006</b> <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 1,476	\$ 2,885
Investment securities, held to maturity	36,178	32,006
Loans	452,259	477,408
Less: allowance for loan losses	520	427
Net loans	451,739	476,981
Other investments, held to maturity	77,108	84,426
Accrued interest receivable	11,578	10,167
Investment in other Farm Credit institutions	16,663	13,473
Premises and equipment, net	1,310	1,313
Other property owned	—	7
Prepaid retirement expense	2,625	2,891
Due from AgFirst Farm Credit Bank	4,211	5,239
Other assets	1,632	732
Total assets	\$ 604,520	\$ 630,120
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 523,888	\$ 547,249
Accrued interest payable	2,567	2,733
Patronage refund payable	19	4,009
Other liabilities	5,389	9,632
Total liabilities	531,863	563,623
Commitments and contingencies		
<b>Members' Equity</b>		
Protected borrower equity	362	402
Capital stock and participation certificates	1,145	1,141
Retained earnings		
Allocated	24,765	25,198
Unallocated	46,385	39,756
Total members' equity	72,657	66,497
Total liabilities and members' equity	\$ 604,520	\$ 630,120

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

*Southwest Georgia Farm Credit, ACA*  
**Consolidated Statements of Income**

*(unaudited)*

<i>(dollars in thousands)</i>	<b>For the three months ended September 30,</b>		<b>For the nine months ended September 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>Interest Income</b>				
Loans	\$ 9,375	\$ 9,976	\$ 28,056	\$ 27,509
Investment securities	557	590	1,540	899
Other	1,068	1,177	3,142	3,317
Total interest income	<u>11,000</u>	<u>11,743</u>	<u>32,738</u>	<u>31,725</u>
<b>Interest Expense</b>				
Notes payable to AgFirst Farm Credit Bank	7,912	8,370	23,568	22,088
Net interest income	3,088	3,373	9,170	9,637
Provision for (reversal of allowance for) loan losses	91	—	91	—
Net interest income after provision for (reversal of allowance for) loan losses	<u>2,997</u>	<u>3,373</u>	<u>9,079</u>	<u>9,637</u>
<b>Noninterest Income</b>				
Loan fees	326	328	884	944
Fees for financially related services	4	7	4	10
Equity in earnings of other Farm Credit institutions	1,625	1,216	4,601	3,378
Other noninterest income	22	50	135	144
Total noninterest income	<u>1,977</u>	<u>1,601</u>	<u>5,624</u>	<u>4,476</u>
<b>Noninterest Expense</b>				
Salaries and employee benefits	1,165	1,065	3,491	2,987
Occupancy and equipment	99	108	324	337
Insurance Fund premium	159	163	472	464
Other operating expenses	569	458	1,539	1,383
Losses on other property owned, net	—	—	6	(1)
Total noninterest expense	<u>1,992</u>	<u>1,794</u>	<u>5,832</u>	<u>5,170</u>
Income before income taxes	2,982	3,180	8,871	8,943
Provision (benefit) for income taxes	(20)	(22)	11	5
Net income	<u>\$ 3,002</u>	<u>\$ 3,202</u>	<u>\$ 8,860</u>	<u>\$ 8,938</u>

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

*Southwest Georgia Farm Credit, ACA*

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

*(dollars in thousands)*

	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings		Total Members' Equity
			Allocated	Unallocated	
Balance at December 31, 2005	\$ 481	\$ 1,125	\$ 24,744	\$ 35,137	\$ 61,487
Net income				8,938	8,938
Protected borrower equity retired	(78)				(78)
Capital stock/participation certificates issued		120			120
Capital stock/participation certificates retired		(104)			(104)
Retained earnings retired			(4,097)		(4,097)
Distribution adjustment			79	(532)	(453)
Balance at September 30, 2006	\$ 403	\$ 1,141	\$ 20,726	\$ 43,543	\$ 65,813
Balance at December 31, 2006	\$ 402	\$ 1,141	\$ 25,198	\$ 39,756	\$ 66,497
Net income				8,860	8,860
Protected borrower equity retired	(40)				(40)
Capital stock/participation certificates issued		106			106
Capital stock/participation certificates retired		(102)			(102)
Retained earnings retired			(2,811)		(2,811)
Distribution adjustment			2,378	(2,231)	147
Balance at September 30, 2007	\$ 362	\$ 1,145	\$ 24,765	\$ 46,385	\$ 72,657

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

Southwest Georgia Farm Credit, ACA

# 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 Southwest Georgia 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, 2006, are contained in the 2006 Annual Report to Shareholders. These unaudited third quarter 2007 consolidated financial statements should be read in conjunction with the 2006 Annual Report to Shareholders.

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

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

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

The Association maintains an allowance for loan losses in accordance with generally accepted accounting principles. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of September 30, 2007, 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:

	<b>For the nine months ended September 30,</b>	
	<b>2007</b>	<b>2006</b>
Balance at beginning of period	\$ 427	\$ 844
Provision for (reversal of) loan losses	91	–
Recoveries, net of loans charged off	2	–
Balance at end of period	<u>\$ 520</u>	<u>\$ 844</u>

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**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:

	<b>For the nine months ended September 30,</b>	
	<b><u>2007</u></b>	<b><u>2006</u></b>
Pension	\$ 266	\$ 291
Thrift/deferred compensation	91	65
Other postretirement benefits	94	92
Total	<b><u>\$ 451</u></b>	<b><u>\$ 448</u></b>

As of September 30, 2007, no contributions have been made to the pension plan for 2007. The Association does not anticipate making additional contributions for the remainder of 2007.