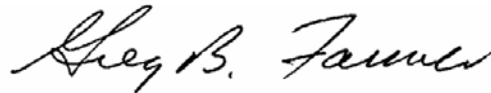


# **THIRD QUARTER 2007**

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Greg B. Farmer  
Chief Executive Officer



Clarke E. Fox  
Chairman of the Board

October 26, 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 *Colonial 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 including livestock operations such as beef cattle, horses, poultry, swine, and dairy farms and various field crops such as soybeans, peanuts, tobacco, cotton, and corn. Other predominant commodities in the portfolio are timber and rural home loans. 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 September 30, 2007, was \$638,980, an increase of \$24,298, as compared to \$614,682 at December 31, 2006. Net loans outstanding at September 30, 2007, were \$636,361 as compared to \$611,954 at December 31, 2006. Net loans accounted for 95.67 percent of total assets at September 30, 2007, as compared to 95.21 percent of total assets at December 31, 2006. The increase in gross and net loan volume during the reporting period is attributed primarily to the normal seasonal disbursement of farm 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, however, and credit administration remains satisfactory. Nonaccrual loans increased from \$1,191 at December 31, 2006, to \$1,321 at September 30, 2007. This increase is primarily the result of delinquencies on two accounts.

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 \$2,619 compared to \$2,728 at December 31, 2006, and was considered by management to be adequate to cover probable losses.

## **RESULTS OF OPERATIONS**

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

Net income for the three months ended September 30, 2007, totaled \$3,536, as compared to \$2,809 for the same period in 2006. Net interest income increased \$59 for the three months ended September 30, 2007, as compared to the same period in 2006. Higher volume and a higher return on the Association's free cash investment are the primary reasons for this increase in net interest income.

Noninterest income for the three months ended September 30, 2007, totaled \$1,927, as compared to \$1,323 for the same period of 2006, an increase of \$604. The increase is the result of interest income of \$605 received on state income tax refunds and an increase in patronage of \$39 offset by a decrease in loan fees of \$25, financially related service fees of \$8, gains from the sale of rural home loans of \$5, and other noninterest income of \$2. Noninterest expense for the three months ended September 30, 2007, decreased \$249 compared to the same period of 2006. This decrease is the result of a decrease in salaries and benefits of \$231 and other operating expenses of \$52 offset by an increase in occupancy and equipment of \$25 and FCSIC insurance premium of \$9.

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

Net income for the nine months ended September 30, 2007, totaled \$10,202, as compared to \$8,414 for the same period in 2006. At September 30, 2007, net interest income increased by \$587 or 4.59 percent compared to September 30, 2006. Interest income on loans increased by \$3,141 and interest expense increased by \$2,554. This change in net interest income is the result of higher volume and a higher return on the Association's free cash investment.

Nonaccrual income was \$16 for the nine months ended September 30, 2007, as compared to \$77 for the same period in 2006. The Association recorded a provision for loan losses of \$70 for the nine months ended September 30, 2007, and a provision for loan losses of \$6 for the same period in 2006.

Noninterest income for the nine months ended September 30, 2007, totaled \$4,761, as compared to \$3,956 for the same period of 2006, an increase of \$805. The increase is the result of interest income of \$643 received on state income tax refunds, an increase in patronage of \$155, an increase in other noninterest income of \$32, and an increase in gains from the sale of rural home loans of \$6 offset by a decrease in loan fees of \$29 and financially related service fees of \$2. Noninterest expense for the nine months ended September 30, 2007, decreased \$321 compared to the same period of 2006. The decrease in noninterest expense is attributable to a decrease in salaries and benefits of \$203 and other operating expense of \$186 offset by an increase in FCSIC insurance premium of \$36 and occupancy and equipment of \$32.

### **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 September 30, 2007, was \$535,439 as compared to \$514,861 at December 31, 2006.

### **CAPITAL RESOURCES**

Total members' equity at September 30, 2007, increased to \$121,552 from the December 31, 2006, total of \$111,729. The increase is attributed to current year's earnings less net retirements of member stock.

Total capital stock and participation certificates were \$5,502 on September 30, 2007, compared to \$5,728 on December 31, 2006. This decrease is attributed to the retirement of inactive Class C 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 September 30, 2007, the Association's total surplus ratio and core surplus ratio were 15.98 percent and 15.98 percent, respectively, and the permanent capital ratio was 16.82 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 1-804-746-1252, or writing Terri E. Branch, Executive Vice President and Chief Financial Officer, Colonial Farm Credit, ACA, P.O. Box 727, Mechanicsville, VA 23111, or accessing the website, [www.colonialfarmcredit.com](http://www.colonialfarmcredit.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.

*Colonial 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	\$ 217	\$ 208
Loans	638,980	614,682
Less: allowance for loan losses	2,619	2,728
Net loans	636,361	611,954
Other investments, held to maturity	2,144	1,990
Accrued interest receivable	8,801	6,742
Investment in other Farm Credit institutions	8,491	8,491
Premises and equipment, net	2,406	2,531
Prepaid retirement expense	3,188	3,683
Due from AgFirst Farm Credit Bank	2,909	4,481
Other assets	612	2,683
Total assets	<u>\$ 665,129</u>	<u>\$ 642,763</u>
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 535,439	\$ 514,861
Accrued interest payable	2,557	2,389
Patronage refund payable	139	6,459
Other liabilities	5,442	7,325
Total liabilities	<u>543,577</u>	<u>531,034</u>
Commitments and contingencies		
<b>Members' Equity</b>		
Capital stock and participation certificates	5,502	5,728
Retained earnings		
Unallocated	116,050	106,001
Total members' equity	<u>121,552</u>	<u>111,729</u>
Total liabilities and members' equity	<u>\$ 665,129</u>	<u>\$ 642,763</u>

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

*Colonial 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	\$ 12,189	\$ 11,449	\$ 35,415	\$ 32,321
Other	35	28	100	53
Total interest income	12,224	11,477	35,515	32,374
<b>Interest Expense</b>				
Notes payable to AgFirst Farm Credit Bank	7,728	7,040	22,134	19,580
Net interest income	4,496	4,437	13,381	12,794
Provision for (reversal of allowance for) loan losses	177	3	70	6
Net interest income after provision for (reversal of allowance for) loan losses	4,319	4,434	13,311	12,788
<b>Noninterest Income</b>				
Loan fees	121	146	425	454
Fees for financially related services	29	37	64	66
Equity in earnings of other Farm Credit institutions	1,003	964	2,909	2,754
Gains (losses) on other property owned, net	3	3	10	10
Gains (losses) on sale of rural home loans	134	139	499	493
Other noninterest income	637	34	854	179
Total noninterest income	1,927	1,323	4,761	3,956
<b>Noninterest Expense</b>				
Salaries and employee benefits	1,760	1,991	5,286	5,489
Occupancy and equipment	201	176	588	556
Insurance Fund premium	235	226	689	653
Other operating expenses	503	555	1,446	1,632
Total noninterest expense	2,699	2,948	8,009	8,330
Income before income taxes	3,547	2,809	10,063	8,414
Provision (benefit) for income taxes	11	—	(139)	—
Net income	\$ 3,536	\$ 2,809	\$ 10,202	\$ 8,414

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

*Colonial Farm Credit, ACA*

# Consolidated Statements of Changes in Members' Equity

*(unaudited)*

*(dollars in thousands)*

	<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, 2005	\$ 6,921	\$ 3,135	\$ 98,491	\$ 108,547
Net income			8,414	8,414
Capital stock/participation certificates issued	369			369
Capital stock/participation certificates retired	(1,574)			(1,574)
Patronage distribution				
Cash			(4,459)	(4,459)
Retained earnings retired		(225)		(225)
Distribution adjustment		—	(63)	(63)
Balance at September 30, 2006	<u>\$ 5,716</u>	<u>\$ 2,910</u>	<u>\$ 102,383</u>	<u>\$ 111,009</u>
Balance at December 31, 2006	\$ 5,728	\$ —	\$ 106,001	\$ 111,729
Net income			10,202	10,202
Capital stock/participation certificates issued	377			377
Capital stock/participation certificates retired	(603)			(603)
Distribution adjustment		—	(153)	(153)
Balance at September 30, 2007	<u>\$ 5,502</u>	<u>\$ —</u>	<u>\$ 116,050</u>	<u>\$ 121,552</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 Colonial 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.

## 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	\$ 2,728	\$ 2,726
Provision for (reversal of) loan losses	70	6
Loans (charged off), net of recoveries	(179)	(9)
Balance at end of period	<u>\$ 2,619</u>	<u>\$ 2,723</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 a Districtwide Thrift Plan.

The Association sponsors a plan providing certain benefits (primarily health care) to its retirees. The following table sets forth the components of net periodic benefit costs of the other postretirement benefits plan:

	<b>For the nine months ended September 30,</b>	
	<b><u>2007</u></b>	<b><u>2006</u></b>
Service cost	\$ 65	\$ 83
Interest cost	181	165
Amortization of prior service cost	(32)	(32)
Recognized net actuarial (gain) loss	112	128
Net periodic benefit cost	<b><u>\$ 326</u></b>	<b><u>\$ 344</u></b>

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	\$ 505	\$ 613
Thrift/deferred compensation	147	135
Other postretirement benefits	326	344
Total	<b><u>\$ 978</u></b>	<b><u>\$ 1,092</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.