First South Farm Credit, ACA

FIRST QUARTER 2005

Stephen L. Rochelle
Chief Executive Officer

Paul Clark
Chairman of the Board

April 29, 2005

First South Farm Credit, ACA

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 First South Farm Credit, ACA (Association) for the period ended March 31, 2005. These comments should be read in conjunction with the accompanying financial statements, notes to the financial statements and the 2004 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. The Association's loan portfolio is diversified over a range of agricultural commodities in our region, including poultry, cotton, livestock, 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.

The gross loan volume of the Association as of March 31, 2005, was $894,958, an increase of $5,882 as compared to $889,076 at December 31, 2004. Net loans outstanding at March 31, 2005, were $889,731 as compared to $883,887 at December 31, 2004. Net loans accounted for 91.08 percent of total assets at March 31, 2005, as compared to 89.68 percent of total assets at December 31, 2004.

The increase in gross and net loan volume during the reporting period is primarily attributed to participation loans purchased from other Farm Credit System institutions.

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 $3,311 at December 31, 2004, to $3,424 at March 31, 2005. As of March 31, 2005, there were no loans that were over 90 days past due. 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, 2005, was $5,227 compared to $5,189 at December 31, 2004, and was considered by management to be adequate to cover possible losses. As discussed in the 2004 Annual Report, the Association recorded a loan loss reversal of $14,809 in the fourth quarter of 2004 that resulted in a decrease in the allowance for loan losses. See the 2004 Annual Report of the Association for further information concerning the allowance for loan losses.

RESULTS OF OPERATIONS

For the three months ended March 31, 2005

Net income for the three months ended March 31, 2005, totaled $3,998, as compared to $2,661 for the same period in 2004. Net interest income increased $846 for the three months ended March 31, 2005, as compared to the same period in 2004. The increase in net interest income was primarily the result of an increase in average accruing loans outstanding of 11.20 percent for the three months ending March 31, 2005, compared to the same period of 2004.

At March 31, 2005, interest income on accruing loans increased $2,349 compared to March 31, 2004. Nonaccrual income was $29 for the three months ended March 31, 2005, as compared to $55 for the same period in 2004, a decrease of $26. Interest expense increased $1,477 for the three months ended March 31, 2005, as compared to the comparable period in 2004. Noninterest income for the three months ended March 31, 2005, totaled $2,205 as compared to $1,950 for the same period of 2004, an increase of $255. Noninterest expense for the three months ended March 31, 2005, decreased $154 compared to the same period of 2004. Provision for income taxes decreased $82 for the three months ended March 31, 2005, as compared to the same period in 2004.

The Association did not record a provision for loan losses for the three months ended March 31, 2005, or for the same period in 2004.

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, 2005, was $747,271 as compared to $759,497 at December 31, 2004. The decrease during the period is primarily attributed to cash patronage received from the Bank and net income for the three months ending March 31, 2005.

CAPITAL RESOURCES

Total members' equity at March 31, 2005, decreased to $200,261 from the December 31, 2004, total of $202,663. The decrease is primarily attributed to the retirement of allocated retained earnings of $6,534, partially offset by net income of $3,998, and an increase in capital stock and participation certificates of $202.

Total capital stock and participation certificates were $63,704 on March 31, 2005, compared to $63,502 on December 31, 2004. This increase is attributed to the issuance of member stock associated with the increase in loan volume.

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, 2005, the Association's total surplus ratio and core surplus ratio were 14.16 percent and 9.72 percent, respectively, and the permanent capital ratio was 15.58 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.

First South Farm Credit, ACA

Consolidated Balance Sheets

(dollars in thousands)	March 31, 2005	December 31, 2004
	(unaudited)	
Assets		
Cash	$ 4,257	$ 10,375
Loans	894,958	889,076
Less: allowance for loan losses	5,227	5,189
Net loans	889,731	883,887
Accrued interest receivable	9,183	9,504
Investment in other Farm Credit institutions	61,513	61,513
Premises and equipment, net	3,590	3,897
Other property owned	15	739
Other assets	8,539	15,641
Total assets	$ 976,828	$ 985,556
Liabilities		
Notes payable to AgFirst Farm Credit Bank	$ 747,271	$ 759,497
Accrued interest payable	2,353	2,253
Patronage refund payable	4	3,105
Postretirement benefits other than pensions	11,271	11,204
Other liabilities	15,668	6,834
Total liabilities	776,567	782,893
Commitments and contingencies		
Members' Equity		
Protected borrower equity	142	142
Capital stock and participation certificates	63,562	63,360
Retained earnings		
Allocated	51,684	58,064
Unallocated	84,873	81,097
Total members' equity	200,261	202,663
Total liabilities and members' equity	$ 976,828	$ 985,556

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

First South Farm Credit, ACA

Consolidated Statements of Income

(unaudited)

(dollars in thousands)	For the three months ended March 31, 2005	2004
Interest Income		
Loans	$ 13,224	$ 10,901
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	6,613	5,134
Other	–	2
Total interest expense	6,613	5,136
Net interest income	6,611	5,765
Provision for (reversal of) loan losses	–	–
Net interest income after provision for (reversal of) loan losses	6,611	5,765
Noninterest Income		
Loan fees	647	571
Fees for financially related services	6	17
Equity in earnings of other Farm Credit institutions	1,415	1,273
Gains (losses) on other property owned, net	31	(3)
Other noninterest income	106	92
Total noninterest income	2,205	1,950
Noninterest Expense		
Salaries and employee benefits	3,432	3,437
Occupancy and equipment	242	266
Insurance Fund premium	80	192
Other operating expenses	985	998
Total noninterest expense	4,739	4,893
Income before income taxes	4,077	2,822
Provision (benefit) for income taxes	79	161
Net income	$ 3,998	$ 2,661

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

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Total Members' Equity
Balance at December 31, 2003	$ 147	$ 62,952	$ 52,081	$ 66,805	$ 181,985
Net income				2,661	2,661
Protected borrower equity retired	(5)				(5)
Capital stock/participation certificates issued		431			431
Capital stock/participation certificates retired		(427)			(427)
Retained earnings retired			(1)		(1)
Distribution adjustment			(139)	184	45
Balance at March 31, 2004	$ 142	$ 62,956	$ 51,941	$ 69,650	$ 184,689
Balance at December 31, 2004	$ 142	$ 63,360	$ 58,064	$ 81,097	$ 202,663
Net income				3,998	3,998
Capital stock/participation certificates issued		442			442
Capital stock/participation certificates retired		(240)			(240)
Retained earnings retired			(6,534)		(6,534)
Distribution adjustment			154	(222)	(68)
Balance at March 31, 2005	$ 142	$ 63,562	$ 51,684	$ 84,873	$ 200,261

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 First South 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, 2004, are contained in the 2004 Annual Report to Stockholders. These unaudited first quarter 2005 consolidated financial statements should be read in conjunction with the 2004 Annual Report to Stockholders.

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, 2005, are not necessarily indicative of the results to be expected for the year ending December 31, 2005.

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, 2005, 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:

Balance at 12-31-03	$ 20,630
(Reversal of) provision for loan losses	–
Loans (charged off), net of recoveries	(17)
Balance at 3-31-04	$ 20,613
Balance at 12-31-04	$ 5,189
(Reversal of) provision for loan losses	–
Recoveries, net of loans charged off	38
Balance at 3-31-05	$ 5,227

As discussed in the 2004 Annual Report, the Association recorded a loan loss reversal of $14,809 in the fourth quarter of 2004 that resulted in a decrease in the allowance for loan losses.

NOTE 3 – EMPLOYEE BENEFIT PLANS

The Association's employees participate in a defined benefit retirement plan. This plan is noncontributory and covers substantially all employees of the Association.

The following is a table of the components of net periodic benefit (income) cost for the defined benefit retirement plan for the three months ended March 31, 2005:

	For the three months ended March 31,	
	2005	2004
Service cost	$ 310	$ 289
Interest cost	570	558
Expected return on plan assets	(631)	(586)
Amortization of net (gain) loss	(85)	(84)
Amortization of prior service cost	36	66
Recognized net actuarial (gain) loss	189	221
Net periodic benefit (income) cost	$ 389	$ 464

As of March 31, 2005, no contributions have been made to the pension plan for 2005. The total employer contribution expected for 2005 is $830.

The Association also participates in Districtwide thrift and other postretirement benefit plans. The other postretirement benefit plan provides certain benefits (primarily health care) to its retirees.

The following is a table of retirement and postretirement benefit expense for the three months ended March 31, 2005:

	For the three months ended March 31,	
	2005	2004
Pension	$ 389	$ 464
Thrift/deferred compensation	56	52
Other postretirement benefits	209	290
Total	$ 654	$ 806