First South Farm Credit, ACA

THIRD QUARTER 2005

Stephen L. Rochelle
Chief Executive Officer

Paul Clark
Chairman of the Board

October 28, 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 September 30, 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 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 reduces the level of dependency on any single commodity.

The gross loan volume of the Association as of September 30, 2005, was $1,102,146, an increase of $213,070, as compared to $889,076 at December 31, 2004. Net loans outstanding at September 30, 2005, were $1,096,681 as compared to $883,887 at December 31, 2004. Net loans accounted for 91.50 percent of total assets at September 30, 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 attributable to seasonal lending. The short-term portfolio is heavily influenced by operating-type loans that normally peak in September and rapidly decline in the fall and winter months when farm commodities are marketed.

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. Nonaccrual loans decreased from $3,311 at December 31, 2004, to $2,185 at September 30, 2005. This decrease is primarily the result of liquidation, normal payouts, and upgrading to performing 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 September 30, 2005, was $5,465 compared to $5,189 at December 31, 2004, and was considered by management to be adequate to cover probable losses.

RESULTS OF OPERATIONS

For the three months ended September 30, 2005

Net income for the three months ended September 30, 2005, totaled $5,333, as compared to $4,607 for the same period in 2004. Net interest income increased $1,367 for the three months ended June 30, 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 14.03 percent for the three months ending September 30, 2005, compared to the same period of 2004.

Noninterest income for the three months ended September 30, 2005, totaled $2,358, as compared to $2,056 for the same period of 2004, an increase of $302. The increase is primarily the result of an increase in loan fees of $77, an increase in equity in earnings of AgFirst Farm Credit Bank (the Bank) of $223, an increase in gains on other property owned of $2, and an increase in other noninterest income of $3, partially offset by a decrease in fees for financially related services of $3. Noninterest expense for the three months ended September 30, 2005, increased $293 compared to the same period of 2004. The primary reasons for the increase in noninterest expense were an increase in occupancy and equipment expense of $24, an increase in the Insurance Fund premium of $251, and an increase in other operating expenses of $36, partially offset by a decrease in salaries and benefits expense of $18.

The Association recorded a provision for loan loss of $305 for the three months ended September 30, 2005, compared to no provision for the same period in 2004. Provision for income taxes was $44 for the three months ended September 30, 2005, compared to a credit of $301 for the same period in 2004.

For the nine months ended September 30, 2005

Net income for the nine months ended September 30, 2005, totaled $13,974, as compared to $10,455 for the same period in 2004. At September 30, 2005, net interest income increased by $3,275 or 17.28 percent compared to June 30, 2004. Interest income on loans increased by $10,547 and interest expense increased by $7,272. This change in net interest income is primarily the result of an increase in average accruing loans outstanding of 12.17 percent for the nine months ending September 30, 2005, compared to the same period of 2004.

Nonaccrual income was $152 for the nine months ended September 30, 2005, as compared to $121 for the same period in 2004. The Association recorded a provision for loan loss of $305 for the nine months ended September 30, 2005, compared to no provision for the same period in 2004. 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 significant decrease in the allowance for loan losses. Please refer to the 2004 Annual Report of the Association for a more detailed explanation of this change in accounting estimate.

Noninterest income for the nine months ended September 30, 2005, totaled $6,819, as compared to $5,979 for the same period of 2004, an increase of $840. The increase is primarily the result of an increase in loan fees of $199, an increase in equity in earnings of the Bank of $524, an increase in gains on other property owned of $141, and an increase in other noninterest income of $15, partially offset by a decrease in fees for financially related services of $39. Noninterest expense for the nine months ended September 30, 2005, increased $185 compared to the same period of 2004. The primary reasons for the increase in noninterest expense were an increase in the Insurance Fund premium of $28 and an increase in other operating expenses of $217, partially offset by a decrease in salaries and benefits expense of $47 and a decrease in occupancy and equipment expense of $13.

Provision for income taxes for the nine months ended September 30, 2005, was $56 compared to a credit of $50 for the same period in 2004.

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 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, 2005, was $968,833 as compared to $759,497 at December 31, 2004.

CAPITAL RESOURCES

Total members' equity at September 30, 2005, increased to $210,559 from the December 31, 2004, total of $202,663. The increase is primarily attributed to net income of $13,974 and an increase in capital stock and participation certificates of $559, partially offset by the retirement of allocated earnings of $6,576.

Total capital stock and participation certificates were $64,061 on September 30, 2005, compared to $63,502 on December 31, 2004. This increase is attributed to the issuance of member stock associated with the increase in gross loan volume at September 30, 2005, compared to December 31, 2004.

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, 2005, the Association's total surplus ratio and core surplus ratio were 11.85 percent and 9.92 percent, respectively, and the permanent capital ratio was 13.06 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.

STOCKHOLDER INVESTMENT

Stockholder 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*. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-955-1722, writing Bryan Applewhite, Chief Financial Officer, First South Farm Credit, ACA, P. O. Box 6008, Ridgeland, MS 39158-6008, or accessing the website, *www.firstsouthfarmcredit.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.

First South Farm Credit, ACA

Consolidated Balance Sheets

(dollars in thousands)	September 30, 2005	December 31, 2004
	(unaudited)	*(audited)*
Assets		
Cash	$ 6,236	$ 10,375
Loans	1,102,146	889,076
Less: allowance for loan losses	5,465	5,189
Net loans	1,096,681	883,887
Accrued interest receivable	16,462	9,504
Investment in other Farm Credit institutions	61,513	61,513
Premises and equipment, net	4,055	3,897
Other property owned	5	739
Other assets	13,624	15,641
Total assets	$ 1,198,576	$ 985,556
Liabilities		
Notes payable to AgFirst Farm Credit Bank	$ 968,833	$ 759,497
Accrued interest payable	3,388	2,253
Patronage refund payable	4	3,105
Postretirement benefits other than pensions	11,399	11,204
Other liabilities	4,393	6,834
Total liabilities	988,017	782,893
Commitments and contingencies		
Members' Equity		
Protected borrower equity	140	142
Capital stock and participation certificates	63,921	63,360
Retained earnings		
Allocated	51,643	58,064
Unallocated	94,855	81,097
Total members' equity	210,559	202,663
Total liabilities and members' equity	$ 1,198,576	$ 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 September 30, 2005	For the three months ended September 30, 2004	For the nine months ended September 30, 2005	For the nine months ended September 30, 2004
Interest Income				
Loans	$ 18,205	$ 13,385	$ 46,535	$ 35,988
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	9,869	6,415	24,306	17,030
Other	–	1	–	4
Total interest expense	9,869	6,416	24,306	17,034
Net interest income	8,336	6,969	22,229	18,954
Provision for (reversal of) loan losses	305	–	305	–
Net interest income after provision for (reversal of) loan losses	8,031	6,969	21,924	18,954
Noninterest Income				
Loan fees	456	379	1,678	1,479
Fees for financially related services	104	107	245	284
Equity in earnings of other Farm Credit institutions	1,791	1,568	4,746	4,222
Gains (losses) on other property owned, net	2	–	39	(102)
Other noninterest income	5	2	111	96
Total noninterest income	2,358	2,056	6,819	5,979
Noninterest Expense				
Salaries and employee benefits	3,443	3,461	10,277	10,324
Occupancy and equipment	286	262	783	796
Insurance Fund premium	170	(81)	341	313
Other operating expenses	1,113	1,077	3,312	3,095
Total noninterest expense	5,012	4,719	14,713	14,528
Income before income taxes	5,377	4,306	14,030	10,405
Provision (benefit) for income taxes	44	(301)	56	(50)
Net income	$ 5,333	$ 4,607	$ 13,974	$ 10,455

The accompanying notes are an integral 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				10,455	10,455
Protected borrower equity retired	(5)				(5)
Capital stock/participation certificates issued		1,220			1,220
Capital stock/participation certificates retired		(950)			(950)
Retained earnings retired			(7,004)		(7,004)
Distribution adjustment			(161)	235	74
Balance at September 30, 2004	$ 142	$ 63,222	$ 44,916	$ 77,495	$ 185,775
Balance at December 31, 2004	$ 142	$ 63,360	$ 58,064	$ 81,097	$ 202,663
Net income				13,974	13,974
Protected borrower equity retired	(2)				(2)
Capital stock/participation certificates issued		1,372			1,372
Capital stock/participation certificates retired		(811)			(811)
Retained earnings retired			(6,576)		(6,576)
Distribution adjustment			155	(216)	(61)
Balance at September 30, 2005	$ 140	$ 63,921	$ 51,643	$ 94,855	$ 210,559

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 Shareholders. These unaudited third quarter 2005 consolidated financial statements should be read in conjunction with the 2004 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 nine months ended September 30, 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 September 30, 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	(676)
Balance at 9-30-04	$ 19,954
Balance at 12-31-04	$ 5,189
(Reversal of) provision for loan losses	305
Loans (charged off), net of recoveries	(29)
Balance at 9-30-05	$ 5,465

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 nine months ended September 30, 2005:

	For the nine months ended September 30,	
	2005	**2004**
Service cost	$ 929	$ 866
Interest cost	1,711	1,674
Expected return on plan assets	(1,892)	(1,757)
Amortization of net (gain) loss	(254)	(254)
Amortization of prior service cost	107	198
Recognized net actuarial (gain) loss	567	664
Other	–	5
Net periodic benefit (income) cost	$ 1,168	$ 1,396

The Association had previously anticipated making a contribution of $830 to the defined benefit retirement plan during 2005 based upon actuarial projections as of the last plan measurement date (September 30, 2004). However, due to market conditions affecting discount rates and return on plan assets, current actuarial projections indicated that a higher contribution was needed to meet the expected accumulated benefit obligation at September 30, 2005. During the third quarter of 2005, the Association contributed $2,500 to the defined benefit retirement plan. The Association does not anticipate making additional contributions for the remainder of 2005.

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 nine months ended September 30, 2005:

	For the nine months ended September 30,	
	2005	**2004**
Pension	$1,168	$1,396
Thrift/deferred compensation	178	168
Other postretirement benefits	626	870
Total	$1,972	$2,434