# Central Texas Farm Credit, ACA

# 2018
# Quarterly Report
# First Quarter

## For the Quarter Ended March 31, 2018

**REPORT OF MANAGEMENT**

The undersigned certify that we have reviewed this report, that it has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate and complete to the best of our knowledge and belief.

Boyd J. Chambers

Boyd J. Chambers, Chief Executive Officer and President

*May 7, 2018*

Robby A. Halfmann, Chairman, Board of Directors

*May 7, 2018*

Keith Prater

Keith Prater, Chief Financial Officer

*May 7, 2018*

# CENTRAL TEXAS FARM CREDIT, ACA
# MANAGEMENT'S DISCUSSION AND ANALYSIS

The following commentary reviews the financial performance of the Central Texas Farm Credit, ACA (Agricultural Credit Association), referred to as the Association, for the quarter ended March 31, 2018. These comments should be read in conjunction with the accompanying consolidated financial statements and the December 31, 2017 Annual Report to Stockholders.

The Association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial institutions established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association's audit committee.

**Significant Events:**

*2018*

In March 2018, a patronage refund of $6,300,000 was distributed to the Association's borrowers. The patronage refund was declared by the board of directors in December 2017, and the amount was based on the Association's 2017 operating results.

*2017*

In December 2017, the Association received a direct loan patronage of $1,531,794 from the Farm Credit Bank of Texas (Bank), representing 39 basis points on the average daily balance of the Association's direct loan with the Bank. During 2017, the Association received $166,872 in patronage payments from the Bank, based on the Association's stock investment in the Bank. Also, the Association received a capital markets patronage of $49,651 from the Bank, representing 75 basis points on the Association's average balance of participations in the Bank's patronage pool program.

In March 2017, a patronage refund of $6,000,000 was distributed to the Association's borrowers. The patronage refund was declared by the board of directors in December 2016, and the amount was based on the Association's 2016 operating results.

*2016*

In December 2016, the Association received a direct loan patronage of $1,592,290 from the Farm Credit Bank of Texas (Bank), representing 41 basis points on the average daily balance of the Association's direct loan with the Bank. During 2016, the Association also received $128,071 in patronage payments from the Bank, based on the Association's stock investment in the Bank. In addition, the Association received a capital markets patronage of $54,450 from the Bank, representing 75 basis points on the Association's average balance of participations in the Bank's patronage pool program.

In September 2016, the Association completed construction of a new headquarters building located in the city of Early, which is included in premises and equipment on the consolidated balance sheet.

In March 2016, a patronage refund of $5,600,000 was distributed to the Association's borrowers. The patronage refund was declared by the board of directors in December 2015, and the amount was based on the Association's 2015 operating results.

*2015*

In December 2015, the Association received a direct loan patronage of $1,448,584 from the Bank, representing 42 basis points on the average daily balance of the Association's direct loan with the Bank. During 2015, the Association received $112,767 in patronage payments from the Bank, based on the Association's stock investment in the Bank.

In March 2015, a patronage refund of $5,200,000 was distributed to the Association's borrowers. The patronage refund was declared by the board of directors in December 2014, and the amount was based on the Association's 2014 operating results.

**Loan Portfolio:**

Total loans outstanding at March 31, 2018, including nonaccrual loans and sales contracts, were $488,931,127 compared to $496,045,375 at December 31, 2017, reflecting a decrease of 1.4 percent. Nonaccrual loans as a percentage of total loans outstanding were 1.0 percent at March 31, 2018, compared to 0.9 percent at December 31, 2017.

The Association recorded $52,508 in recoveries and $17,992 in charge-offs for the quarter ended March 31, 2018, however, no recoveries or charge offs were recorded for the same period of 2017. The Association's allowance for loan losses was 0.3 percent of total loans outstanding as of both March 31, 2018, and December 31, 2017.

Currently, the Association has $4,984,165 in nonaccrual loans. These loans, which include a capital markets loan in the amount of $1,499,985 that was downgraded to nonaccrual in first quarter of 2018, are included in the Association's core loan portfolio. There have been no material changes in the Association's core portfolio's borrower profile, geographic distribution, commodity concentration or asset quality.

*Problem Loans*

*2018*

During the first quarter of 2018, the Association recorded a charge-off in the amount of $17,992.

A recovery of $52,508 was recorded due to a payoff on a nonaccrual loan in the first quarter of 2018.

During the first quarter of 2018, a capital markets loan was downgraded to nonaccrual and a specific allowance of $438,893 was recorded to provision expense.

*2017*

The Association did not have any reportable problem loan activity in 2017.

*2016*

During the third quarter of 2016, a nonaccrual loan in the amount of $198,666 was foreclosed on. The property was sold during the quarter and the Association was paid in full.

During the third quarter of 2016, three production and intermediate term loans to a borrower were downgraded to Substandard Non-Accrual and a subsequent charge-off of $1,029,171 was recognized.

After the sale of acquired property in 2013, a balance of $129,075 was held in acquired property to represent funds still owed to the Association. During the third quarter of 2016 that amount was charged off as the collection of those funds was no longer expected.

*2015*

During the first quarter of 2015, a nonaccrual loan in the amount of $85,486 was foreclosed on, and the collateral was then acquired by the Association. The property was sold during the second quarter of 2015 and a gain of $4,109 was recognized.

*Territory Conditions*

The local economy in our chartered territory is relatively strong. Real estate prices are stable and land sales have continued to increase despite sagging ag-related commodities and petroleum prices and the lost income for those connected to those industries. The majority of the Association's new loans made during the past number of years have been to absentee landowners with diverse income sources looking for a place for a small agricultural operation or recreational use. As a result, the Association has a diversified portfolio that is not heavily dependent on agricultural income. Even those borrowers who are primarily agricultural producers typically have outside income from a spouse's employment, part-time jobs, investments, etc. The above is reflected in the Association's sound credit quality and small number of delinquencies.

According to an April USDA report, 65% of the state had slipped into an abnormally dry or moderate drought condition, generally affecting southern and western counties in the Association's territory. However, pastures in many areas are improving with much needed spring rains in most parts of our territory.

The USDA report "Texas Crop Progress and Condition" for the last week of March 2018, reported 11 percent of cotton acres were planted. They also reported farmers are hesitant to plant cotton this year due to drought conditions. Cotton planting and field preparations are ongoing in the Low Plains and Edwards Plateau. Corn acres planted was 55% with 26% emerged and 42% of sorghum was planted. Winter wheat and oats headed at 11% and 26%, respectively.

Cattle markets were steady to lower with trading and demand at a moderate level. Steer and heifer calves and yearlings were weak to $1.00 lower. Slaughter cows and bulls, stock cows, and pairs were all steady. By the end of the first quarter the market had found some stability and was pushing higher thanks to continued exports to Japan. Argentina reports a decrease of one million head due to drought conditions which will negatively affect future Argentinian beef exports to other countries. Chines tariffs on bee imports is expected to have minimal impact since this is a small percentage of U.S. exports. The USDA report in "Cattle on Feed" dated March 1, 2018 that cattle and calves, in Texas feedlots with capacities exceeding 1,000 head, totaled 11.7 million, an increase of 9%, year over year. The USDA "Milk Production" report released March 20, 2018, Texas milk production in February totaled almost 1 billion, a 5.5% increase compared to the first quarter of 2017. The increase in milk production is partially due to the addition of 16,000 head.

Most of our borrowers continue to do well right now, but many remain cautious due to weakened commodity markets. Management realize the impact the current commodity environment could potentially have on borrowers. We feel our portfolio is managed very well as operating loans are reviewed at least annually and, in some cases, more often. It is our belief that the PD ratings accurately reflect the risk level of the portfolio and no impairment pool for any specific commodity is necessary at this time.

**Risk Exposure:**

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned. The following table illustrates the association's components and trends of high-risk assets.

| | **March 31, 2018** | | December 31, 2017 | |
|---|---|---|---|---|
| | **Amount** | **%** | Amount | % |
| Nonaccrual | **$ 4,984,165** | **99.3%** | $ 4,294,741 | 100.0% |
| 90 days past due and still accruing interest | **36,134** | **0.7%** | - | 0.0% |
| Total | **$ 5,020,299** | **100.0%** | $ 4,294,741 | 100.0% |

Nonaccrual loans increased by a net amount of $725,558. This was due to a capital markets relationship in the amount of $1,499,985 being downgraded to nonaccrual, offset by a payoff of a nonaccrual loan in the core portfolio.

**Results of Operations:**

The Association had net income of $2,648,304 for the quarter ended March 31, 2018, as compared to net income of $2,217,138 for the same period in 2017, reflecting an increase of 19.5 percent. Net interest income was $3,711,393 for the quarter ended March 31, 2018, compared to $3,621,450 for the same period in 2017.

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| | Three months ended: | | | |
|---|---|---|---|---|
| | **March 31, 2018** | | March 31, 2017 | |
| | **Average Balance** | **Interest** | Average Balance | Interest |
| Loans | **$ 492,128,961** | **$ 6,053,332** | $ 487,943,955 | $ 5,558,411 |
| Interest-bearing liabilities | **390,152,556** | **2,341,939** | 389,467,075 | 1,936,961 |
| Impact of capital | **$ 101,976,405** | | $ 98,476,880 | |
| Net interest income | | **$ 3,711,393** | | $ 3,621,450 |

| | **2018 Average Yield** | 2017 Average Yield |
|---|---|---|
| Yield on loans | **4.99%** | 4.62% |
| Cost of interest-bearing liabilities | **2.43%** | 2.02% |
| Interest rate spread | **2.56%** | 2.60% |
| Net interest income as a percentage of average earning assets | **3.06%** | 3.01% |

| | Three months ended: March 31, 2018 vs. March 31, 2017 | | |
|---|---|---|---|
| | Increase (decrease) due to | | |
| | **Volume** | **Rate** | **Total** |
| Interest income - loans | **$ 47,674** | **$ 447,247** | **$ 494,921** |
| Interest expense | **3,409** | **401,569** | **404,978** |
| Net interest income | **$ 44,265** | **$ 45,678** | **$ 89,943** |

Interest income for the three months ended March 31, 2018, increased by $494,921, or 8.9 percent, from the same period of 2017, primarily due to increases in yields on earning assets and an increase in average loan volume. Interest expense for the three months ended March 31, 2018, increased by $404,978, or 20.9 percent, from the same period of 2017 due to an increase in interest rates. Average loan volume for the first quarter of 2018 was $492,128,961, compared to $487,943,955 in the first quarter of 2017. The average net interest rate spread on the loan portfolio for the first quarter of 2018 was 2.56 percent, compared to 2.60 percent in the first quarter of 2017.

The Association's return on average assets for the three months ended March 31, 2018, was 2.30 percent compared to 1.78 percent for the same period in 2017. The Association's return on average equity for the three months ended March 31, 2018, was 10.76 percent, compared to 8.56 percent for the same period in 2017.

**Liquidity and Funding Sources:**

The Association secures the majority of its lendable funds from the Farm Credit Bank of Texas (the Bank), which obtains its funds through the issuance of System-wide obligations and with lendable equity. The following schedule summarizes the Association's borrowings.

| | | **March 31, 2018** | | December 31, 2017 |
|---|---|---|---|---|
| Note payable to the Bank | **$** | **387,721,199** | $ | 394,242,092 |
| Accrued interest on note payable | | **817,982** | | 779,048 |
| Total | **$** | **388,539,181** | $ | 395,021,140 |

The Association operates under a general financing agreement (GFA) with the Bank. The current GFA is effective through September 30, 2018. The primary source of liquidity and funding for the Association is a direct loan from the Bank. The outstanding balance of $387,721,199 as of March 31, 2018, is recorded as a liability on the Association's balance sheet. The note carried a weighted average interest rate of 2.50 percent at March 31, 2018. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by the general financing agreement. The decrease in note payable to the Bank and related accrued interest payable since December 31, 2017, is due to the Association's decrease in total assets. The Association's own funds, which represent the amount of the Association's loan portfolio funded by the Association's equity, were $99,519,900 at March 31, 2018. The maximum amount the Association may borrow from the Bank as of March 31, 2018, was $491,734,157 as defined by the general financing agreement. The indebtedness continues in effect until the expiration date of the general financing agreement, which is September 30, 2018, unless sooner terminated by the Bank upon the occurrence of an event of default, or by the Association, in the event of a breach of this agreement by the Bank, upon giving the Bank 30 calendar days' prior written notice, or in all other circumstances, upon giving the Bank 120 days' prior written notice.

The liquidity policy of the Association is to manage cash balances, to maximize debt reduction and to increase accrual loan volume. This policy will continue to be pursued during 2018. As borrower payments are received, they are applied to the Association's note payable to the Bank.

The Association will continue to fund its operations through direct borrowings from the Bank, capital surplus from prior years and borrower stock. It is management's opinion that funds available to the Association are sufficient to fund its operations for the coming year.

**Capital Resources:**

The Association's capital position increased by $2,623,170 at March 31, 2018, compared to December 31, 2017. The Association's debt as a percentage of members' equity was 3.60:1 as of March 31, 2018, compared to 3.78:1 as of December 31, 2017.

Farm Credit Administration regulations require us to maintain minimums for various regulatory capital ratios. New regulations became effective January 1, 2017, which replaced the previously required core surplus and total surplus ratios with common equity tier 1, tier 1 capital, and total capital risk-based capital ratios. The new regulations also added tier 1 leverage and unallocated retained earnings and equivalents (UREE) ratios. The permanent capital ratio continues to remain in effect, with some modifications to align with the new regulations. As of March 31, 2018, the Association exceeded all regulatory capital requirements.

**Significant Recent Accounting Pronouncements:**

In February 2018, the Financial Accounting Standards Board (FASB) issued guidance entitled "Income Statement — Reporting Comprehensive Income — Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This guidance allows for the reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the recently issued tax legislation, Tax Cuts and Jobs Act (TCJA) that lowered the federal corporate tax rate from 35% to 21%. The amount of the reclassification shall include the effect of the change in the tax rate on gross deferred tax amounts and related valuation allowances at the date of enactment of the TCJA related to items remaining in accumulated other comprehensive income. The guidance becomes effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

In March 2017, the FASB issued guidance entitled "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Cost." The guidance requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. Other components are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition but did change the classification of certain items in the results of operations.

In August 2016, the FASB issued guidance entitled "Classification of Certain Cash Receipts and Cash Payments." The guidance addresses specific cash flow issues with the objective of reducing the diversity in the classification of these cash flows. Included in the cash flow issues are debt prepayment or debt extinguishment costs and settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations but did change the classification of certain items in the statement of cash flows.

In June 2016, the FASB issued guidance entitled "Measurement of Credit Losses on Financial Instruments." The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange Commission filers this guidance becomes effective for interim and annual periods beginning after December 15, 2020, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. This guidance becomes effective for interim and annual periods beginning after December 15, 2018, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In January 2016, the FASB issued guidance entitled "Recognition and Measurement of Financial Assets and Liabilities." The guidance affects, among other things, the presentation and disclosure requirements for financial instruments. For public entities, the guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations but did impact the Association's fair value disclosures.

In May 2014, the FASB issued guidance entitled, "Revenue from Contracts with Customers." The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. In this regard, a majority of our contracts would be excluded from the scope of this new guidance. In August 2015, the FASB issued an update that defers this guidance by one year, which results in the new revenue standard becoming effective for interim and annual reporting periods beginning after December 15, 2017. The Association has determined that the effect of the adoption is not material to its financial condition or results of operations and will not change its current recognition practices.

**Regulatory Matters:**

On March 10, 2016, the Farm Credit Association approved a final rule to modify the regulatory capital requirements for System banks and associations. The stated objectives of the proposed rule are as follows:

- To modernize capital requirements while ensuring that the institutions continue to hold sufficient regulatory capital to fulfill their mission as a government-sponsored enterprise,
- To ensure that the System's capital requirements are comparable to the Basel III framework and the standardized approach that the federal banking regulatory agencies have adopted, but also to ensure that the rules recognize the cooperative structure and the organization of the System,
- To make system regulatory capital requirements more transparent, and
- To meet the requirements of section 939A of the Dodd-Frank Act.

**Relationship With the Farm Credit Bank of Texas:**

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the 2017 Annual Report of Central Texas Farm Credit, ACA more fully describe the Association's relationship with the Bank.

The Texas Farm Credit District's (District) annual and quarterly stockholder reports, as well as those of the Bank, are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9204. Copies of the District's quarterly and annual stockholder reports also can be requested by e-mail at *fcb@farmcreditbank.com*. The annual and quarterly stockholder reports for the Bank and the District are also available on its website at *www.farmcreditbank.com.*

The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Central Texas Farm Credit, ACA, 1026 Early Boulevard, Early, Texas, 76802, or calling (325) 643-5563. The annual and quarterly stockholder reports for the association are also available on its website at *wwww.centraltexasfarmcredit.com.* Copies of the Association's quarterly stockholder reports can also be requested by e-mailing *Keith.Prater@farmcreditbank.com.*

**CENTRAL TEXAS FARM CREDIT, ACA**

**CONSOLIDATED BALANCE SHEET**

| | March 31, 2018 (unaudited) | December 31, 2017 |
|---|---|---|
| **ASSETS** | | |
| Cash | **$ 11,112** | $ 9,872 |
| Loans | **488,931,127** | 496,045,375 |
| Less: allowance for loan losses | **1,357,630** | 1,288,981 |
| Net loans | **487,573,497** | 494,756,394 |
| Accrued interest receivable | **4,932,808** | 4,896,672 |
| Investment in and receivable from the Farm Credit Bank of Texas: | | |
| Capital stock | **7,846,940** | 7,846,940 |
| Other | **587** | 1,175,607 |
| Premises and equipment, net | **3,729,544** | 3,747,632 |
| Other assets | **892,399** | 225,878 |
| Total assets | **$ 504,986,887** | $ 512,658,995 |
| **LIABILITIES** | | |
| Note payable to the Farm Credit Bank of Texas | **$ 387,721,199** | $ 394,242,092 |
| Accrued interest payable | **817,982** | 779,048 |
| Drafts outstanding | **25,693** | 6,343 |
| Dividends payable | **-** | 6,300,000 |
| Other liabilities | **6,535,343** | 4,068,012 |
| Total liabilities | **395,100,217** | 405,395,495 |
| **MEMBERS' EQUITY** | | |
| Capital stock and participation certificates | **2,277,470** | 2,305,685 |
| Unallocated retained earnings | **107,993,085** | 105,344,781 |
| Accumulated other comprehensive loss | **(383,885)** | (386,966) |
| Total members' equity | **109,886,670** | 107,263,500 |
| Total liabilities and members' equity | **$ 504,986,887** | $ 512,658,995 |

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

## CENTRAL TEXAS FARM CREDIT, ACA

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(unaudited)

| | Quarter Ended March 31, | |
|---|---|---|
| | **2018** | 2017 |
| **INTEREST INCOME** | | |
| Loans | **$ 6,053,332** | $ 5,558,411 |
| **INTEREST EXPENSE** | | |
| Note payable to the Farm Credit Bank of Texas | **2,341,939** | 1,936,961 |
| Net interest income | **3,711,393** | 3,621,450 |
| **PROVISION FOR LOAN LOSSES** | **71,069** | 157,949 |
| Net interest income after provision for loan losses | **3,640,324** | 3,463,501 |
| **NONINTEREST INCOME** | | |
| Income from the Farm Credit Bank of Texas: | | |
| Patronage income | **351,405** | 330,220 |
| Loan fees | **31,942** | 31,120 |
| Financially related services income | **3,147** | 2,773 |
| Other noninterest income | **285,566** | 2,268 |
| Total noninterest income | **672,060** | 366,381 |
| **NONINTEREST EXPENSES** | | |
| Salaries and employee benefits | **982,643** | 969,385 |
| Directors' expense | **30,606** | 39,382 |
| Purchased services | **64,462** | 46,340 |
| Travel | **41,158** | 37,559 |
| Occupancy and equipment | **95,391** | 89,747 |
| Communications | **27,975** | 27,615 |
| Advertising | **58,079** | 43,498 |
| Public and member relations | **103,251** | 88,706 |
| Supervisory and exam expense | **54,715** | 52,062 |
| Insurance Fund premiums | **148,984** | 136,042 |
| Other noninterest expense | **56,816** | 82,408 |
| Total noninterest expenses | **1,664,080** | 1,612,744 |
| **NET INCOME** | **2,648,304** | 2,217,138 |
| Other comprehensive income: | | |
| Change in postretirement benefit plans | **3,081** | (3,695) |
| **COMPREHENSIVE INCOME** | **$ 2,651,385** | $ 2,213,443 |

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

**CENTRAL TEXAS FARM CREDIT, ACA**

**CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY**
(unaudited)

| | Capital Stock/ Participation Certificates | Unallocated Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Total Members' Equity |
|---|---|---|---|---|
| Balance at December 31, 2016 | $ 2,283,345 | $ 101,740,850 | $ (188,571) | $ 103,835,624 |
| Comprehensive income | - | 2,217,138 | (3,695) | 2,213,443 |
| Capital stock/participation certificates and allocated retained earnings issued | 92,355 | - | - | 92,355 |
| Capital stock/participation certificates and allocated retained earnings retired | (65,635) | - | - | (65,635) |
| Balance at March 31, 2017 | $ 2,310,065 | $ 103,957,988 | $ (192,266) | $ 106,075,787 |
| | | | | |
| Balance at December 31, 2017 | $ 2,305,685 | $ 105,344,781 | $ (386,966) | $ 107,263,500 |
| Comprehensive income | - | 2,648,304 | 3,081 | 2,651,385 |
| Capital stock/participation certificates and allocated retained earnings issued | 65,945 | - | - | 65,945 |
| Capital stock/participation certificates and allocated retained earnings retired | (94,160) | - | - | (94,160) |
| **Balance at March 31, 2018** | **$ 2,277,470** | **$ 107,993,085** | **$ (383,885)** | **$ 109,886,670** |

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

## CENTRAL TEXAS FARM CREDIT, ACA
## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

## NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

The Central Texas Farm Credit, ACA, (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Brown, Callahan, Coke, Coleman, Comanche, Concho, Haskell, Irion, Jones, Knox, McCulloch, Menard, Mills, Reagan, San Saba, Sterling, and Tom Green. The Association is a lending institution of the Farm Credit System (System), which was established by Acts of Congress to meet the needs of American agriculture.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2017, as contained in the 2017 Annual Report to Stockholders.

In the opinion of management, 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), except for the inclusion of a statement of cash flows. GAAP require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements. These interim financial statements should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2017, as contained in the 2017 Annual Report to Stockholders. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ending December 31, 2018. Descriptions of the significant accounting policies are included in the 2017 Annual Report to Stockholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform with GAAP and prevailing practices within the banking industry.

In February 2018, the Financial Accounting Standards Board (FASB) issued guidance entitled "Income Statement — Reporting Comprehensive Income — Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This guidance allows for the reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the recently issued tax legislation, Tax Cuts and Jobs Act (TCJA) that lowered the federal corporate tax rate from 35% to 21%. The amount of the reclassification shall include the effect of the change in the tax rate on gross deferred tax amounts and related valuation allowances at the date of enactment of the TCJA related to items remaining in accumulated other comprehensive income. The guidance becomes effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Association is evaluating the impact of adoption on the Association's financial condition and its results of operations.

In March 2017, the FASB issued guidance entitled "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Cost." The guidance requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. Other components are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition but did change the classification of certain items in the results of operations.

In August 2016, the FASB issued guidance entitled "Classification of Certain Cash Receipts and Cash Payments." The guidance addresses specific cash flow issues with the objective of reducing the diversity in the classification of these cash flows. Included in the cash flow issues are debt prepayment or debt extinguishment costs and settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations but did change the classification of certain items in the statement of cash flows.

In June 2016, FASB issued guidance entitled "Measurement of Credit Losses on Financial Instruments." The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange Commission filers this guidance becomes effective for interim and annual periods beginning after December 15, 2020, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. This guidance becomes effective for interim and annual periods beginning after December 15, 2018, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In January 2016, the FASB issued guidance entitled "Recognition and Measurement of Financial Assets and Liabilities." This guidance affects, among other things, the presentation and disclosure requirements for financial instruments. For public entities, the guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost. This guidance becomes effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations but did impact the Association's fair value disclosures.

In May 2014, the FASB issued guidance entitled, "Revenue from Contracts with Customers." The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. In August 2015, the FASB issued an update that defers this guidance by one year, which results in the new revenue standard becoming effective for interim and annual reporting periods beginning after December 15, 2017. The Association has determined that the effect of the adoption is not material to its financial condition or results of operations and will not change its current recognition practices.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management's estimates. The results for the quarter ended March 31, 2018, are not necessarily indicative of the results to be expected for the year ended December 31, 2018. Certain amounts in the prior period's financial statements have been reclassified to conform to current financial statement presentation.

## NOTE 2 — LOANS AND ALLOWANCE FOR LOAN LOSSES:

A summary of loans follows:

| Loan Type | **March 31, 2018 Amount** | December 31, 2017 Amount |
|---|---|---|
| Production agriculture: | | |
| Real estate mortgage | **$ 340,523,060** | $ 346,406,190 |
| Production and intermediate term | **64,041,325** | 67,896,084 |
| Agribusiness: | | |
| Processing and marketing | **42,364,341** | 41,149,234 |
| Farm-related business | **14,478,781** | 13,902,709 |
| Loans to cooperatives | **3,911,411** | 3,346,691 |
| Communication | **11,246,489** | 10,566,486 |
| Energy | **11,156,258** | 11,426,977 |
| Rural residential real estate | **1,171,565** | 1,313,107 |
| Water and waste water | **37,897** | 37,897 |
| Total | **$ 488,931,127** | $ 496,045,375 |

The Association purchases or sells participation interests with other parties in order to diversify risk, manage loan volume and comply with Farm Credit Administration regulations. The following table presents information regarding the balances of participations purchased and sold at March 31, 2018:

| | Other Farm Credit Institutions | | Non-Farm Credit Institutions | | Total | |
|---|---|---|---|---|---|---|
| | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold | Participations Purchased | Participations Sold |
| Agribusiness | $ 47,495,571 | $ - | $ - | $ - | $ 47,495,571 | $ - |
| Communication | 11,246,489 | - | - | - | 11,246,489 | - |
| Energy | 11,156,258 | - | - | - | 11,156,258 | - |
| Real estate mortgage | 9,950,868 | 12,433,629 | - | - | 9,950,868 | 12,433,629 |
| Production and intermediate term | 9,362,818 | 4,548,816 | - | - | 9,362,818 | 4,548,816 |
| Total | $ 89,212,004 | $ 16,982,445 | $ - | $ - | $ 89,212,004 | $ 16,982,445 |

The Association is authorized under the Farm Credit Act to accept "advance conditional payments" (ACPs) from borrowers. To the extent the borrower's access to such ACPs is restricted and the legal right of setoff exists, the ACPs are netted against the borrower's related loan balance. Unrestricted advance conditional payments are included in other liabilities. ACPs are insured, and interest is generally paid by the Association on such balances. There were no ACPs at March 31, 2018, and December 31, 2017, respectively.

Nonperforming assets (including related accrued interest) and related credit quality statistics are as follows:

| | | March 31, 2018 | December 31, 2017 |
|---|---|---|---|
| **Nonaccrual loans:** | | | |
| Production and intermediate term | | **1,841,386** | 1,988,401 |
| Real estate mortgage | **$** | **1,642,794** | $ 2,306,340 |
| Energy | | **1,499,985** | - |
| Total nonaccrual loans | | **4,984,165** | 4,294,741 |
| | | | |
| Total nonperforming assets | **$** | **4,984,165** | $ 4,294,741 |

One credit quality indicator utilized by the association is the Farm Credit Administration Uniform Loan Classification System that categorizes loans into five categories. The categories are defined as follows:

- Acceptable – assets are expected to be fully collectible and represent the highest quality;
- Other assets especially mentioned (OAEM) – assets are currently collectible but exhibit some potential weakness;
- Substandard – assets exhibit some serious weakness in repayment capacity, equity and/or collateral pledged on the loan;
- Doubtful – assets exhibit similar weaknesses to substandard assets; however, doubtful assets have additional weaknesses in existing factors, conditions and values that make collection in full highly questionable; and
- Loss – assets are considered uncollectible.

The following table shows loans and related accrued interest as a percentage of total loans and related accrued interest receivable by loan type as of:

| | **March 31, 2018** | December 31, 2017 |
|---|---|---|
| Real estate mortgage | | |
| Acceptable | **98.0** % | 98.0 % |
| OAEM | **0.8** | 0.7 |
| Substandard/doubtful | **1.2** | 1.3 |
| | **100.0** | 100.0 |
| Production and intermediate term | | |
| Acceptable | **88.1** | 87.0 |
| OAEM | **8.5** | 8.6 |
| Substandard/doubtful | **3.4** | 4.4 |
| | **100.0** | 100.0 |
| Agribusiness | | |
| Acceptable | **95.3** | 95.1 |
| OAEM | **4.7** | 4.9 |
| Substandard/doubtful | **-** | - |
| | **100.0** | 100.0 |
| Energy and water/waste water | | |
| Acceptable | **77.8** | 78.0 |
| OAEM | **8.9** | 9.0 |
| Substandard/doubtful | **13.3** | 13.0 |
| | **100.0** | 100.0 |
| Communication | | |
| Acceptable | **100.0** | 100.0 |
| OAEM | **-** | - |
| Substandard/doubtful | **-** | - |
| | **100.0** | 100.0 |
| Rural residential real estate | | |
| Acceptable | **100.0** | 100.0 |
| OAEM | **-** | - |
| Substandard/doubtful | **-** | - |
| | **100.0** | 100.0 |
| Total loans | | |
| Acceptable | **95.9** | 95.7 |
| OAEM | **2.5** | 2.5 |
| Substandard/doubtful | **1.6** | 1.8 |
| | **100.0** % | 100.0 % |

The following tables provide an age analysis of past due loans (including accrued interest) as of:

| **March 31, 2018** | **30-89 Days Past Due** | **90 Days or More Past Due** | **Total Past Due** | **Not Past Due or Less Than 30 Days Past Due** | **Total Loans** | **Recorded Investment >90 Days and Accruing** |
|---|---|---|---|---|---|---|
| **Real estate mortgage** | **$ 2,068,755** | **$ -** | **$ 2,068,755** | **$ 342,308,018** | **$ 344,376,773** | **$ -** |
| **Production and intermediate term** | **108,492** | **36,134** | **144,626** | **64,804,959** | **64,949,585** | **-** |
| **Processing and marketing** | **-** | **-** | **-** | **42,435,717** | **42,435,717** | **-** |
| **Farm-related business** | **-** | **-** | **-** | **14,533,589** | **14,533,589** | **-** |
| **Communication** | **-** | **-** | **-** | **11,262,240** | **11,262,240** | **-** |
| **Energy and Water/Waste Water** | **39,962** | **-** | **39,962** | **11,175,498** | **11,215,460** | **-** |
| **Loans to cooperatives** | **-** | **-** | **-** | **3,914,900** | **3,914,900** | **-** |
| **Rural residential real estate** | **-** | **-** | **-** | **1,175,671** | **1,175,671** | **-** |
| **Total** | **$ 2,217,209** | **$ 36,134** | **$ 2,253,343** | **$ 491,610,592** | **$ 493,863,935** | **$ -** |

| December 31, 2017 | 30-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Not Past Due or Less Than 30 Days Past Due | Total Loans | Recorded Investment >90 Days and Accruing |
|---|---|---|---|---|---|---|
| Real estate mortgage | $ 1,010,918 | $ 857,450 | $ 1,868,368 | $ 348,456,355 | $ 350,324,723 | $ - |
| Production and intermediate term | 848,986 | - | 848,986 | 67,869,247 | 68,718,233 | - |
| Loans to cooperatives | - | - | - | 3,347,965 | 3,347,965 | - |
| Processing and marketing | - | - | - | 41,205,238 | 41,205,238 | - |
| Farm-related business | - | - | - | 13,955,998 | 13,955,998 | - |
| Communication | - | - | - | 10,590,656 | 10,590,656 | - |
| Energy | - | - | - | 11,442,153 | 11,442,153 | - |
| Water and waste water | - | - | - | 39,425 | 39,425 | - |
| Rural residential real estate | - | - | - | 1,317,656 | 1,317,656 | - |
| Total | $ 1,859,904 | $ 857,450 | $ 2,717,354 | $ 498,224,693 | $ 500,942,047 | $ - |

Note: The recorded investment in the receivable is the face amount increased or decreased by applicable accrued interest and unamortized premium, discount, finance charges or acquisition costs, and may also reflect a previous direct write-down of the investment.

A restructuring of a debt constitutes a troubled debt restructuring if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Troubled debt restructurings are undertaken in order to improve the likelihood of recovery on the loan and may include, but are not limited to, forgiveness of principal or interest, interest rate reductions that are lower than the current market rate for new debt with similar risk, or significant term or payment extensions.

As of March 31, 2018, the Association had no trouble debt restructured loans. In structuring where principal is forgiven, the amount of forgiveness is immediately charged off. In restructurings where accrued interest is forgiven, the interest is reversed (if current year interest) or charged off (if prior year interest).

The predominant form of concession granted for troubled debt restructuring is extension of the term. Other types of modifications include principal or accrued interest reductions, interest rate decreases, and delayed payments, among others. At times, these terms might be offset with incremental payments, collateral or new borrower guarantees, in which case we assess all of the modified terms to determine if the overall modification qualifies as a troubled debt restructuring.

Additional impaired loan information is as follows:

| | March 31, 2018 | | | December 31, 2017 | | |
|---|---|---|---|---|---|---|
| | Recorded Investment | Unpaid Principal Balance[a] | Related Allowance | Recorded Investment | Unpaid Principal Balance[a] | Related Allowance |
| Impaired loans with a related allowance for credit losses: | | | | | | |
| Real estate mortgage | $ - | $ - | $ - | $ - | $ - | $ - |
| Production and intermediate term | - | - | - | - | - | - |
| Energy and water/waste water | 1,499,985 | 1,499,985 | 438,893 | - | - | - |
| Total | $ 1,499,985 | $ 1,499,985 | $438,893 | $ - | $ - | $ - |
| Impaired loans with no related allowance for credit losses: | | | | | | |
| Real estate mortgage | 1,642,794 | 1,642,902 | - | 2,306,340 | 2,358,956 | $ - |
| Production and intermediate term | $ 1,841,386 | $ 2,889,251 | $ - | $ 1,988,401 | $ 3,018,275 | - |
| Energy and water/waste water | - | - | - | - | - | - |
| Total | $ 3,484,180 | $ 4,532,153 | $ - | $ 4,294,741 | $ 5,377,231 | $ - |
| Total impaired loans: | | | | | | |
| Real estate mortgage | $ 1,841,386 | $ 2,889,251 | $ - | $ 1,988,401 | $ 3,018,275 | $ - |
| Production and intermediate term | 1,642,794 | 1,642,902 | - | 2,306,340 | 2,358,956 | - |
| Energy and water/waste water | 1,499,985 | 1,499,985 | 438,893 | - | - | - |
| Total | $ 4,984,165 | $ 6,032,138 | $438,893 | $ 4,294,741 | $ 5,377,231 | $ - |

[a] Unpaid principal balance represents the recorded principal balance of the loan.

| | For the Quarter & Year Ended March 31, 2018 | | For the Quarter & Year Ended March 31, 2017 | |
|---|---|---|---|---|
| | Average Impaired Loans | Interest Income Recognized | Average Impaired Loans | Interest Income Recognized |
| Impaired loans with a related allowance for credit losses: | | | | |
| Real estate mortgage | $ - | $ - | $ - | $ - |
| Production and intermediate term | - | - | - | - |
| Energy and water/waste water | 95,808 | 235 | - | - |
| Total | $ 95,808 | $ 235 | $ - | $ - |
| Impaired loans with no related allowance for credit losses: | | | | |
| Real estate mortgage | 1,576,209 | 1,667 | 3,411,913 | 24,096 |
| Production and intermediate term | $1,933,983 | $ 366 | $1,362,992 | $ - |
| Energy and water/waste water | - | - | - | - |
| Total | $3,510,192 | $ 2,033 | $4,774,905 | $ 24,096 |
| Total impaired loans: | | | | |
| Real estate mortgage | $1,576,209 | $ 1,667 | $3,411,913 | $ 24,096 |
| Production and intermediate term | 1,933,983 | 366 | 1,362,992 | - |
| Energy and water/waste water | 95,808 | 235 | - | - |
| Total | $3,606,000 | $ 2,268 | $4,774,905 | $ 24,096 |

A summary of changes in the allowance for loan losses and period end recorded investment in loans is as follows:

| | Real Estate Mortgage | Production and Intermediate Term | Agribusiness | Communications | Energy and Water/Waste Water | Rural Residential Real Estate | Total |
|---|---|---|---|---|---|---|---|
| **Allowance for Credit Losses:** | | | | | | | |
| Balance at December 31, 2017 | $ 252,274 | $ 414,969 | $ 256,914 | $ 51,606 | $ 312,302 | $ 916 | $ 1,288,981 |
| Charge-offs | - | (17,992) | - | - | - | - | (17,992) |
| Recoveries | 52,508 | - | - | - | - | - | 52,508 |
| Provision for loan losses | (67,336) | (32,891) | (5,489) | (2,462) | 179,476 | (229) | 71,070 |
| Adjustment due to merger | - | - | - | - | - | - | - |
| Other | 4 | (23,575) | 10,447 | 237 | (24,301) | 251 | (36,937) |
| Balance at March 31, 2018 | $ 237,450 | $ 340,511 | $ 261,873 | $ 49,381 | $ 467,477 | $ 938 | $ 1,357,630 |
| Ending Balance: | | | | | | | |
| Individually evaluated for impairment | $ - | $ - | $ - | $ - | $ 387,185 | $ - | $ 387,185 |
| Collectively evaluated for impairment | 237,450 | 340,511 | 261,873 | 49,381 | 80,292 | 938 | 970,445 |
| Balance at March 31, 2018 | $ 237,450 | $ 340,511 | $ 261,873 | $ 49,381 | $ 467,477 | $ 938 | $ 1,357,630 |
| Balance at December 31, 2016 | $ 197,602 | $ 337,170 | $ 246,053 | $ 110,077 | $ 176,128 | $ 371 | $ 1,067,401 |
| Charge-offs | - | - | - | - | - | - | - |
| Recoveries | - | - | - | - | - | - | - |
| Provision for loan losses | 11,714 | (3,861) | (10,088) | (25,525) | 185,725 | (16) | 157,949 |
| Other | (72) | (7,556) | 19,482 | 3,444 | (24,822) | 30 | (9,494) |
| Balance at March 31, 2017 | $ 209,244 | $ 325,753 | $ 255,447 | $ 87,996 | $ 337,031 | $ 385 | $ 1,215,856 |
| Ending Balance: | | | | | | | |
| Individually evaluated for impairment | $ - | $ - | $ - | $ - | $ - | $ - | $ - |
| Collectively evaluated for impairment | 209,244 | 325,753 | 255,447 | 87,996 | 337,031 | 385 | 1,215,856 |
| Balance at March 31, 2017 | $ 209,244 | $ 325,753 | $ 255,447 | $ 87,996 | $ 337,031 | $ 385 | $ 1,215,856 |

| | Real Estate Mortgage | Production and Intermediate Term | Agribusiness | Communications | Energy and Water/Waste Water | Rural Residential Real Estate | Total |
|---|---|---|---|---|---|---|---|
| **Recorded Investments in Loans Outstanding:** | | | | | | | |
| Ending Balance at March 31, 2018 | $344,376,773 | $ 64,949,585 | $ 60,884,206 | $ 11,262,240 | $ 11,215,460 | $1,175,671 | $493,863,935 |
| Individually evaluated for impairment | $ 1,642,794 | $ 1,841,386 | $ - | $ - | $ 1,499,990 | $ - | $ 4,984,170 |
| Collectively evaluated for impairment | $342,733,979 | $ 63,108,199 | $ 60,884,206 | $ 11,262,240 | $ 9,715,470 | $1,175,671 | $488,879,765 |
| Ending Balance at March 31, 2017 | $341,821,243 | $ 62,418,358 | $ 61,172,350 | $ 13,342,119 | $ 12,145,369 | $1,006,798 | $491,906,237 |
| Individually evaluated for impairment | $ 3,438,848 | $ 1,354,174 | $ - | $ - | $ - | $ - | $ 4,793,022 |
| Collectively evaluated for impairment | $338,382,395 | $ 61,064,184 | $ 61,172,350 | $ 13,342,119 | $ 12,145,369 | $1,006,798 | $487,113,215 |

## NOTE 3 — CAPITAL:

The Association’s board of directors has established a Capital Adequacy Plan (Plan) that includes the capital targets that are necessary to achieve the institution's capital adequacy goals as well as the minimum permanent capital standards. The Plan monitors projected dividends, equity retirements and other actions that may decrease the Association’s permanent capital. In addition to factors that must be considered in meeting the minimum standards, the board of directors also monitors the following factors: capability of management; quality of operating policies, procedures and internal controls; quality and quantity of earnings; asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan and lease portfolios; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the Association's goals and objectives with the board.

### Regulatory Capitalization Requirements

| Risk-adjusted: | **Regulatory Minimums** | **Conservation Buffer** | **Total** | **As of March 31, 2018** | **As of December 31, 2017** |
|---|---|---|---|---|---|
| Common equity tier 1 ratio | 4.50% | 2.50% | 7.00% | 18.94% | 19.12% |
| Tier 1 capital ratio | 6.00% | 2.50% | 8.50% | 18.94% | 19.12% |
| Total capital ratio | 8.00% | 2.50% | 10.50% | 19.21% | 19.38% |
| Permanent capital ratio | 7.00% | 0.00% | 7.00% | 18.98% | 19.16% |
| Non-risk-adjusted: | | | | | |
| Tier 1 leverage ratio | 4.00% | 1.00% | 5.00% | 20.17% | 20.41% |
| UREE leverage ratio | 1.50% | 0.00% | 1.50% | 21.27% | 21.50% |

| March 31, 2018 | Common equity tier 1 ratio | Tier 1 capital ratio | Total capital ratio | Permanent capital ratio |
|---|---|---|---|---|
| **Numerator:** | | | | |
| **Unallocated retained earnings** | **106,538,508** | **106,538,508** | **106,538,508** | **106,538,508** |
| **Common Cooperative Equities:** | | | | |
| **Statutory minimum purchased borrower stock** | **2,291,695** | **2,291,695** | **2,291,695** | **2,291,695** |
| **Allowance for loan losses and reserve for credit losses subject to certain limitations** | | | **1,459,216** | |
| **Regulatory Adjustments and Deductions:** | | | | |
| **Amount of allocated investments in other System institutions** | **(7,842,884)** | **(7,842,884)** | **(7,842,884)** | **(7,842,884)** |
| | **100,987,319** | **100,987,319** | **102,446,535** | **100,987,319** |
| **Denominator:** | | | | |
| **Risk-adjusted assets excluding allowance** | **541,067,234** | **541,067,234** | **541,067,234** | **541,067,234** |
| **Regulatory Adjustments and Deductions:** | | | | |
| **Regulatory deductions included in total capital** | **(7,842,884)** | **(7,842,884)** | **(7,842,884)** | **(7,842,884)** |
| **Allowance for loan losses** | | | | **(1,278,527)** |
| | **533,224,350** | **533,224,350** | **533,224,350** | **531,945,823** |

| December 31, 2017 | Common equity tier 1 ratio | Tier 1 capital ratio | Total capital ratio | Permanent capital ratio |
|---|---|---|---|---|
| Numerator: | | | | |
| Unallocated retained earnings | 108,236,057 | 108,236,057 | 108,236,057 | 108,236,057 |
| Common Cooperative Equities: | | | | |
| Statutory minimum purchased borrower stock | 2,302,209 | 2,302,209 | 2,302,209 | 2,302,209 |
| Allowance for loan losses and reserve for credit losses subject to certain limitations | | | 1,414,277 | |
| Regulatory Adjustments and Deductions: | | | | |
| Amount of allocated investments in other System institutions | (7,756,689) | (7,756,689) | (7,756,689) | (7,756,689) |
| | 102,781,577 | 102,781,577 | 104,195,854 | 102,781,577 |
| Denominator: | | | | |
| Risk-adjusted assets excluding allowance | 545,402,827 | 545,402,827 | 545,402,827 | 545,402,827 |
| Regulatory Adjustments and Deductions: | | | | |
| Regulatory deductions included in total capital | (7,756,689) | (7,756,689) | (7,756,689) | (7,756,689) |
| Allowance for loan losses | | | | (1,197,041) |
| | 537,646,138 | 537,646,138 | 537,646,138 | 536,449,097 |

| | **March 31, 2018** | | December 31, 2017 | |
|---|---|---|---|---|
| | **Tier 1 leverage ratio** | **UREE leverage ratio** | Tier 1 leverage ratio | UREE leverage ratio |
| **Numerator:** | | | | |
| **Unallocated retained earnings** | **106,538,508** | **106,538,508** | 108,236,057 | 108,236,057 |
| **Common Cooperative Equities:** | | | | |
| **Statutory minimum purchased borrower stock** | **2,291,695** | **-** | 2,302,209 | - |
| **Regulatory Adjustments and Deductions:** | | | | |
| **Amount of allocated investments in other System institutions** | **(7,842,884)** | **-** | (7,756,689) | - |
| | **100,987,319** | **106,538,508** | 102,781,577 | 108,236,057 |
| **Denominator:** | | | | |
| **Total Assets** | **510,782,544** | **510,782,544** | 514,409,011 | 514,409,011 |
| **Regulatory Adjustments and Deductions:** | | | | |
| **Regulatory deductions included in tier 1 capital** | **(10,010,245)** | **(10,010,245)** | (10,933,168) | (10,933,168) |
| | **500,772,299** | **500,772,299** | 503,475,843 | 503,475,843 |

An additional component of equity is accumulated other comprehensive income, which is reported net of taxes, is as follows:

| **March 31, 2018** | **Net of Tax** |
|---|---|
| **Nonpension postretirement benefits** | **$ (383,885)** |
| **Total** | **$ (383,885)** |

| March 31, 2017 | Net of Tax |
|---|---|
| Nonpension postretirement benefits | $ (192,266) |
| Total | $ (192,266) |

The Association's accumulated other comprehensive loss relates entirely to its nonpension other postretirement benefits. Amortization of prior service credits and of actuarial loss are reflected in "Salaries and employee benefits" in the Consolidated Statement of Comprehensive Income. The following table summarizes the changes in accumulated other comprehensive income (loss) for the three months ended March 31:

| | **2018** | 2017 |
|---|---|---|
| Accumulated other comprehensive loss at January 1 | **$(386,966)** | $(188,571) |
| Amortization of prior service credits included in salaries and employee benefits | **(3,375)** | (4,497) |
| Amortization of actuarial loss included in salaries and employee benefits | **6,456** | 802 |
| Other comprehensive income (loss), net of tax | **3,081** | (3,695) |
| Accumulated other comprehensive loss at March 31 | **$ (383,885)** | $ (192,266) |

## NOTE 4 — INCOME TAXES:

Central Texas Farm Credit, ACA conducts its business activities through two wholly-owned subsidiaries. Long-term mortgage lending activities are conducted through a wholly-owned FLCA subsidiary which is exempt from federal and state income tax. Short- and intermediate-term lending activities are conducted through a wholly-owned PCA subsidiary. The PCA subsidiary and the ACA holding company are subject to income tax. Central Texas Farm Credit, ACA operates as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, Central Texas Farm Credit, ACA can exclude from taxable income amounts distributed as qualified patronage dividends in the form of cash, stock or allocated retained earnings. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage dividends. Deferred taxes are recorded at the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. A valuation allowance is provided against deferred tax assets to the extent that it is more likely than not (more than 50 percent probability), based on management's estimate, that they will not be realized. The Association's valuation allowance was $711,255 as of the quarter ended March 31, 2018 for no available tax benefit as of that point in time.

## NOTE 5 — FAIR VALUE MEASUREMENTS:

FASB guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability. See Note 13 of the 2017 Annual Report to Stockholders for a more complete description.

There were no assets and liabilities measured at fair value on a nonrecurring basis as of March 31, 2018, or at December 31, 2017.

## Valuation Techniques

As more fully discussed in Note 2 to the 2017 Annual Report to Stockholders, authoritative guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Association's assets and liabilities. For a more complete description, see Notes to the 2017 Annual Report to Stockholders.

*Loans Evaluated for Impairment*

For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon the underlying real estate collateral since the loans were collateral-dependent. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, a majority of these loans have fair value measurements that fall within Level 3 of the fair value hierarchy. When the value of the real estate, less estimated costs to sell, is less than the principal balance of the loan, a specific reserve is established. The fair value of these loans would fall under Level 2 of the hierarchy if the process uses independent appraisals and other market-based information.

*Other Property Owned*

Other property owned is generally classified as Level 3 of the fair value hierarchy. The process for measuring the fair value of the other property owned involves the use of independent appraisals and other market-based information. Costs to sell represent transaction costs and are not included as a component of the asset's fair value. As a result, these fair value measurements fall within Level 3 of the hierarchy.

*Cash*

For cash, the carrying amount is a reasonable estimate of fair value.

*Loans*

Fair value is estimated by discounting the expected future cash flows using the Association's current interest rates at which similar loans would be made to borrowers with similar credit risk. The discount rates are based on the Association's current loan originate rates as well as management's estimates of credit risk. Management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale and could be less.

For purposes of estimating fair value of accruing loans, the loan portfolio is segregated into pools of loans with homogeneous characteristics. Expected future cash flows, primarily based on contractual terms, and interest rates reflecting appropriate credit risk are separately determined for each individual pool.

The fair value of loans in nonaccrual status that are current as to principal and interest is estimated as described above, with appropriately higher interest rates which reflect the uncertainty of continued cash flows. For collateral-dependent impaired loans, it is assumed that collection will result only from the disposition of the underlying collateral.

## NOTE 6 — EMPLOYEE BENEFIT PLANS:

The following table summarizes the components of net periodic benefit costs of nonpension other postretirement employee benefits for the three months ended March 31:

| | Other Benefits | |
|---|---|---|
| | **2018** | 2017 |
| Service cost | **$ 13,031** | $ 12,891 |
| Interest cost | **22,588** | 22,621 |
| Amortization of prior service credits | **(3,375)** | (4,497) |
| Amortization of net actuarial loss | **3,081** | 802 |
| Net periodic benefit cost | **$ 35,325** | $ 31,817 |

The Association's liability for the unfunded accumulated obligation for these benefits at March 31, 2018, was $2,299,894 and is included in "Other Liabilities" in the balance sheet.

The components of net periodic benefit cost other than the service cost component are included in the line item "other components of net periodic postretirement benefit cost" in the income statement.

The structure of the District's defined benefit pension plan is characterized as multiemployer since the assets, liabilities and cost of the plan are not segregated or separately accounted for by participating employers (bank and associations). The Association recognizes its amortized annual contributions to the plan as an expense. As of March 31, 2018, $107,477 of contributions have been made. The Association presently anticipates contributing an additional $322,431 to fund the defined benefit plan in 2018, for a total of $429,908.

## NOTE 7 — COMMITMENTS AND CONTINGENT LIABILITIES:

The Association is involved in various legal proceedings in the normal course of business. In the opinion of legal counsel and management, there are no legal proceedings at this time that are likely to materially affect the association.

## NOTE 8 — SUBSEQUENT EVENTS:

The association has evaluated subsequent events through May 7, 2018, which is the date the financial statements were issued. There are no other significant events requiring disclosure as of May 7, 2018.