MOMENTUM

2004 ANNUAL REPORT
FARM CREDIT BANK OF TEXAS

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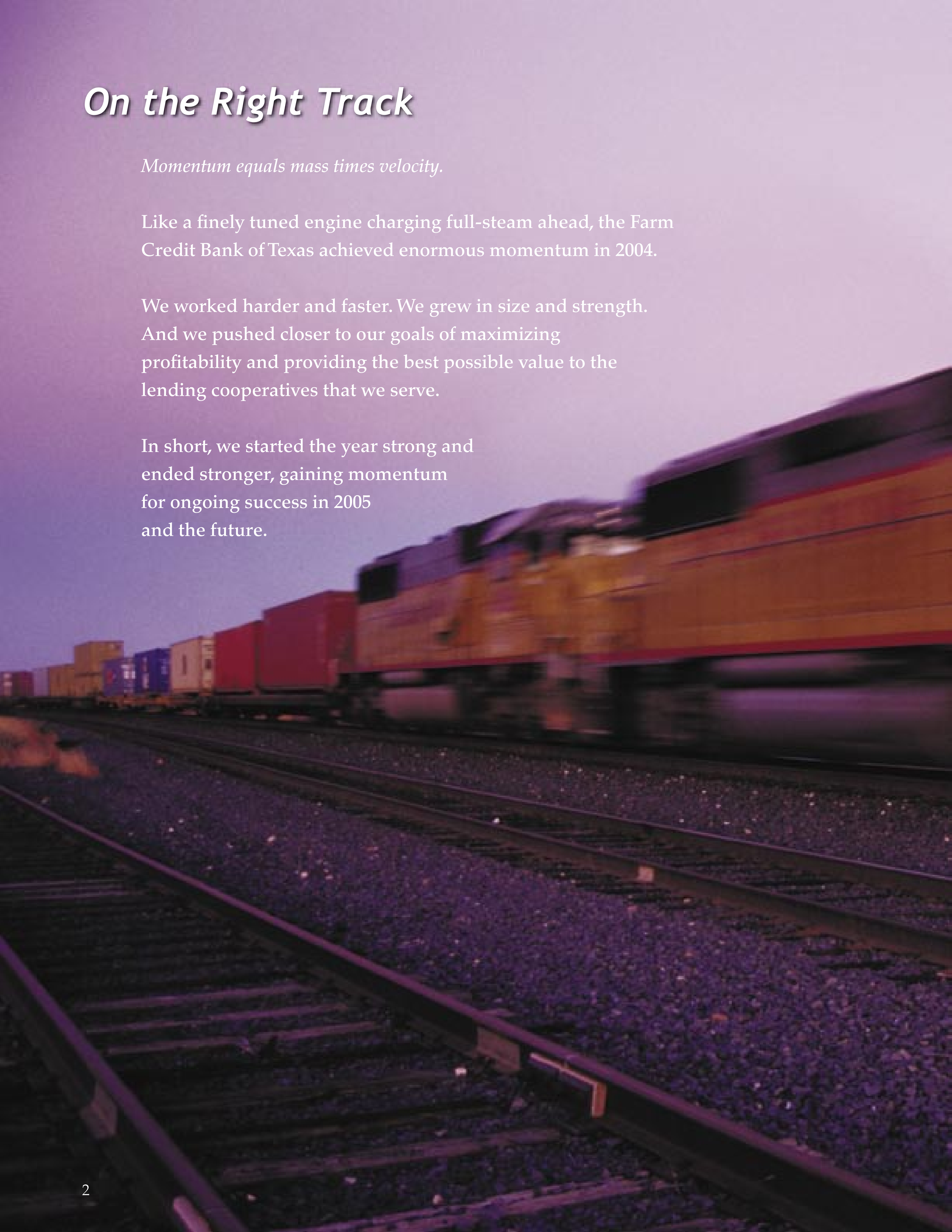
MOMENTUM



On the Right Track

Momentum equals mass times velocity.

Like a finely tuned engine charging full-steam ahead, the Farm Credit Bank of Texas achieved enormous momentum in 2004.

We worked harder and faster. We grew in size and strength. And we pushed closer to our goals of maximizing profitability and providing the best possible value to the lending cooperatives that we serve.

In short, we started the year strong and ended stronger, gaining momentum for ongoing success in 2005 and the future.

MOMENTUM

Breaking Records

Looking back at last year, we can be proud of our many achievements.

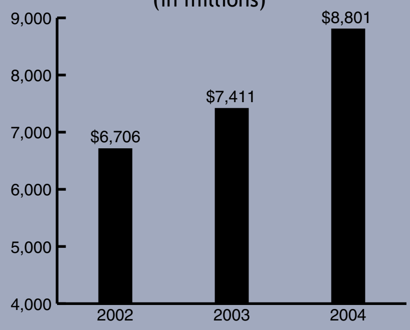
As one of the oldest and strongest sources of credit and financial services for rural America, the Farm Credit Bank of Texas has enjoyed many successful years. But 2004 was exceptional. We exceeded expectations and set new records in the key areas of growth, profitability and stockholder value.

Our interest-earning assets increased from the previous year by nearly 19 percent, and net interest income climbed at a rate of almost 34 percent. It is particularly noteworthy that we were able to increase our profitability and sustain almost-perfect credit quality while growing our loan portfolio.

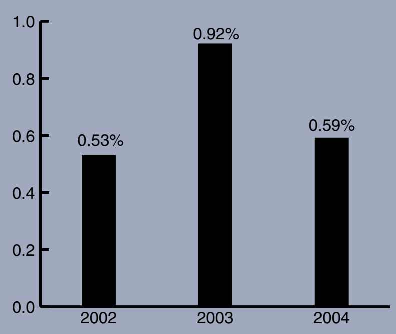
As a cooperative, the Farm Credit Bank of Texas believes the most important measure of success, however, is the value we provide to our affiliated lending cooperatives. That is why we were delighted to double the level of patronage dividend we paid out in 2004 over what we distributed in 2003.

It is a pleasure to report such strong financial results, which were achieved through the hard work and dedication of our Bank staff, working together with the Associations in the Tenth Farm Credit District. We appreciate the support of our Association borrowers and the trusted partnership we share with them. We look forward to setting new records together in the future.

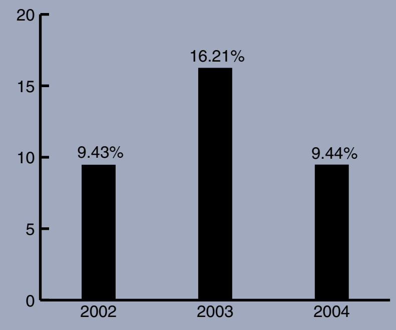
Total Assets Outstanding at Year-End
(in millions)



Return on Average Assets for the Year



Return on Average Equity for the Year



Financial Highlights

For the Year *(in thousands)*	**2004**	2003	2002
Net interest income	**$ 66,662**	$ 49,826	$ 45,091
Negative provision (provision) for loan losses	**7,878**	(340)	2,902
Noninterest (expense) income, net	**(27,558)**	15,338	(15,526)
Net income	**46,982**	64,824	32,467
Rate of return on:			
Average assets	**0.59%**	0.92%	0.53%
Average shareholders' equity	**9.44**	16.21	9.43
Cash patronage paid	**$ 16,775**	$ 49,144	$ 3,615

At Year-End *(in millions)*			
Total loans	**$ 6,918**	$ 5,835	$ 5,827
Total assets	**8,801**	7,411	6,706
Total liabilities	**8,300**	6,933	6,337
Total shareholders' equity	**501**	478	369
Permanent capital ratio	**19.82%**	23.71%	18.06%
Total surplus ratio	**16.55**	19.15	14.01
Core surplus ratio	**11.51**	14.44	12.56
Net collateral ratio	**105.69**	106.62	105.32

Farm Credit Bank of Texas
Board of Directors

(left to right)

Jimmy Dodson

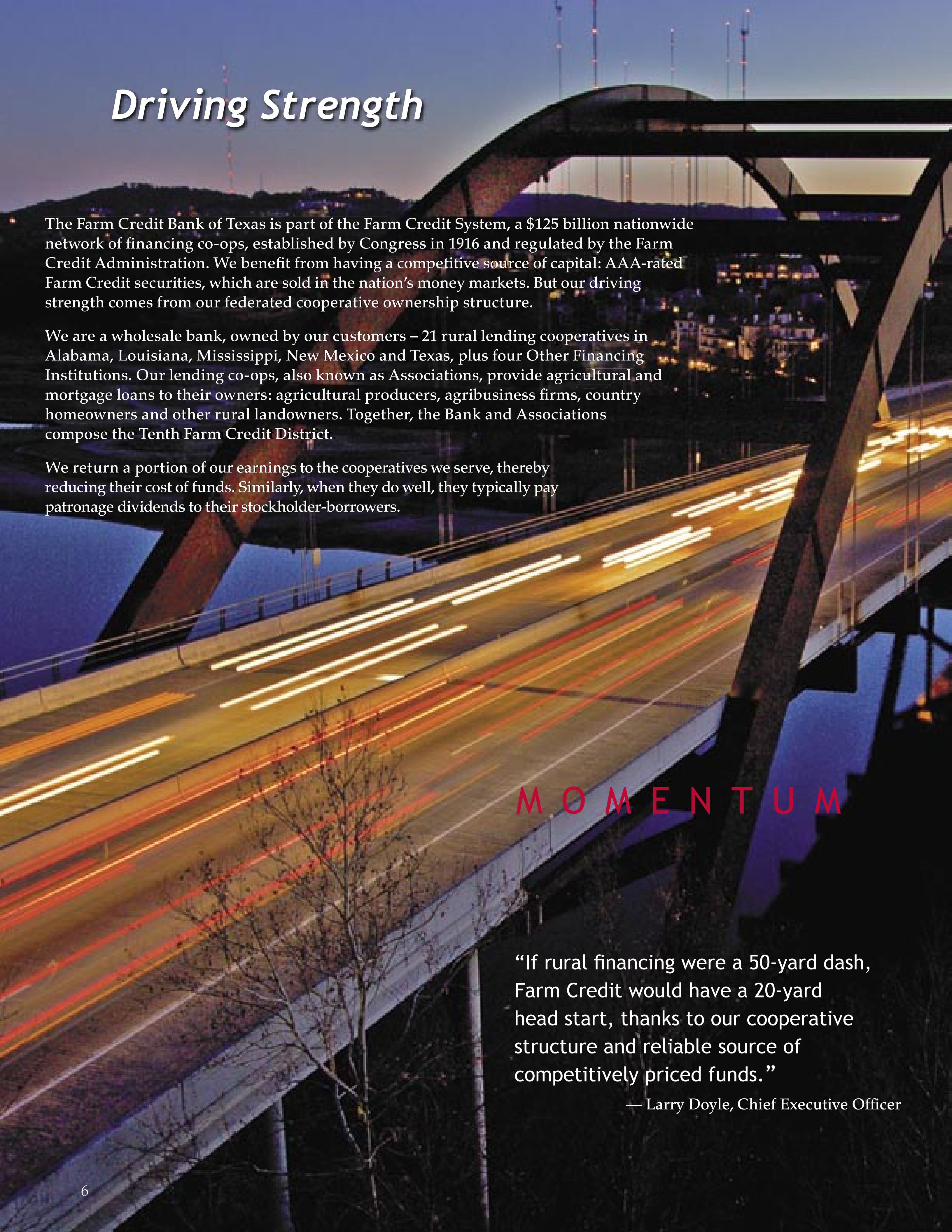
Kenneth Andrews

Jon "Mike" Garnett
Vice Chairman

Joe Crawford

Ralph W. "Buddy" Cortese
Chairman

William Staats



Driving Strength

The Farm Credit Bank of Texas is part of the Farm Credit System, a $125 billion nationwide network of financing co-ops, established by Congress in 1916 and regulated by the Farm Credit Administration. We benefit from having a competitive source of capital: AAA-rated Farm Credit securities, which are sold in the nation's money markets. But our driving strength comes from our federated cooperative ownership structure.

We are a wholesale bank, owned by our customers – 21 rural lending cooperatives in Alabama, Louisiana, Mississippi, New Mexico and Texas, plus four Other Financing Institutions. Our lending co-ops, also known as Associations, provide agricultural and mortgage loans to their owners: agricultural producers, agribusiness firms, country homeowners and other rural landowners. Together, the Bank and Associations compose the Tenth Farm Credit District.

We return a portion of our earnings to the cooperatives we serve, thereby reducing their cost of funds. Similarly, when they do well, they typically pay patronage dividends to their stockholder-borrowers.

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"If rural financing were a 50-yard dash, Farm Credit would have a 20-yard head start, thanks to our cooperative structure and reliable source of competitively priced funds."

— Larry Doyle, Chief Executive Officer

Farm Credit Bank of Texas
Senior Management Team

Larry Doyle, *Chief Executive Officer* (left)
Tom Hill, *Senior Vice President, Chief Financial Officer, Chief Operations Officer* (center)
Steve Fowlkes, *Senior Vice President, Chief Credit Officer*

Energized by the Challenge

In 2003, the Farm Credit Bank of Texas launched an aggressive five-year plan focused on increasing our profitability. The ultimate goal of this plan is to reduce our reliance on Association direct-note income and neutralize our Associations' cost of borrowing.

Energized by the challenge of implementing this new business model, we concentrated our efforts last year in three strategic areas: growing capital and increasing earnings; providing competitive, customer-responsive products and services to our Associations; and streamlining operations.

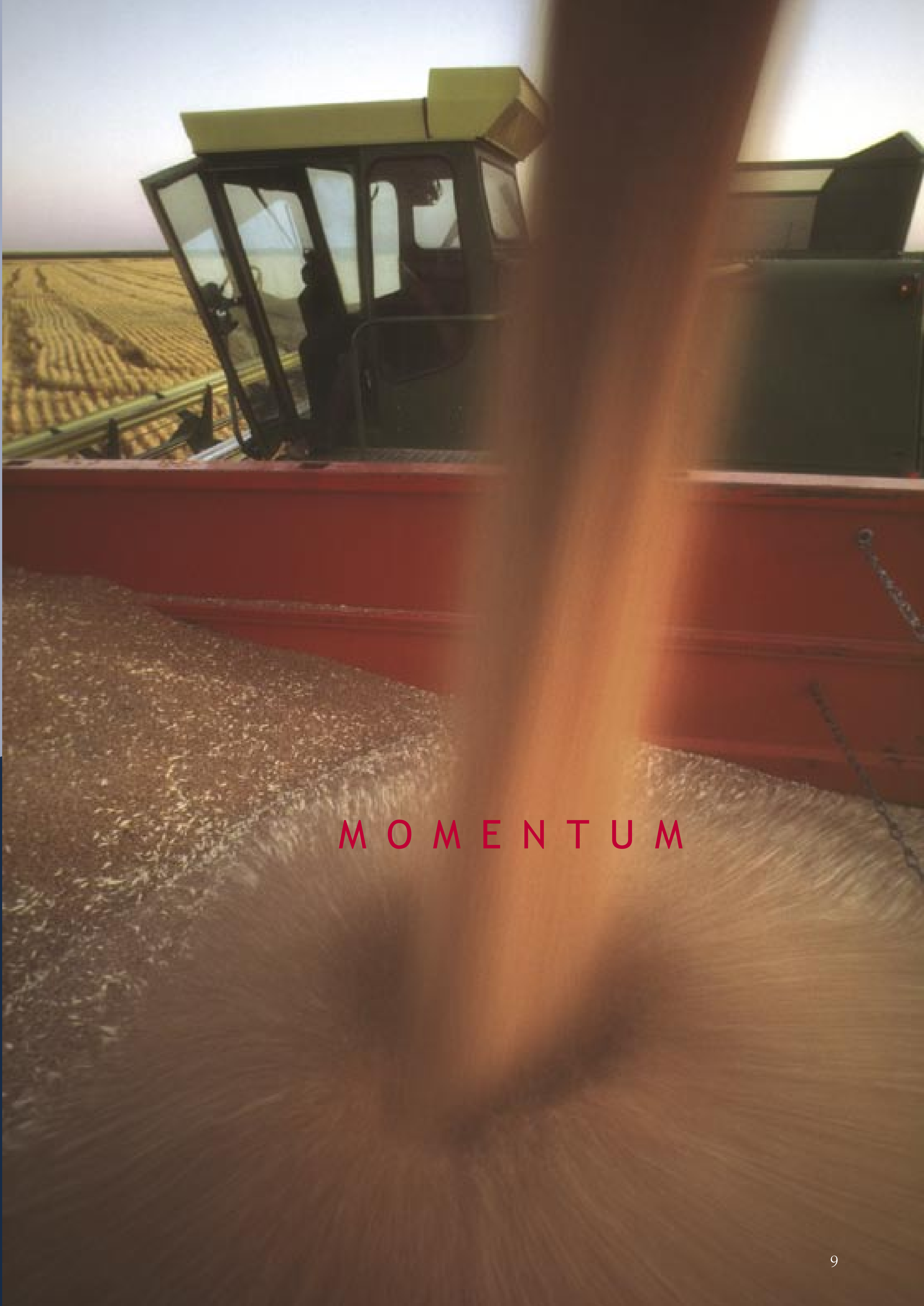
Growing Capital and Earnings

Our strategy for building capital is to turn the Bank into an earnings engine that will generate strong returns from investments and participation loans. Last year we started the engine, and this year we shifted it into overdrive, with the following results:

- Net income totaled $47 million in 2004, compared with $64.8 million the previous year. Absent revenue from a one-time minerals sale reported in 2003, net income would have reflected a $12.7 million, or 36.9 percent, increase from 2003 to 2004.
- Interest-earning assets totaled $8.8 billion at year-end 2004, an 18.6 percent increase from a year earlier.
- Net interest income for 2004 was $66.7 million, compared to $49.8 million in 2003, an increase of 33.8 percent.
- Loan volume of $6.9 billion at December 31, 2004, was up 18.6 percent from year-end 2003. One-third of this growth came from participation loans with other lenders, while nearly two-thirds resulted from Association direct borrowings.
- Participation loan volume increased to $752.5 million at December 31, 2004, from $395.4 million a year earlier.
- The quality of the Bank's portfolio remained exceptionally high, with acceptable credit quality of 99.59 percent at year-end.
- Our investment portfolio expanded by $295 million in 2004, and continues to be diversified into the highest credit-quality instruments.
- We established lending agreements with two additional Other Financing Institutions.
- Through our Capital Markets Group, we forged new relationships with other lenders, identified new agribusiness lending opportunities and participated in a number of large-loan transactions outside of our District.

As a result of these achievements, in December we paid our affiliated Associations 20 basis points on their average direct borrowings from the Bank—double the level of patronage paid on direct borrowings in 2003.

At the heart of all we do is our mission —
to enable our members to be the lender of choice
to agriculture and rural America by providing them
with value-added funds and services.



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Building Strength and Value

Improved Products and Operations

As a partner to our affiliated Associations, the Farm Credit Bank of Texas provides custom-designed products and services that offer time- and cost-savings and improve credit delivery. In 2004, we launched several new loan products and cash management products for Association use, and implemented a new risk-rating model.

To support both the Bank and our Associations across five states, we continued to upgrade the District's information network and security systems and automated our manual reporting processes. We also conducted the most comprehensive credit-training curriculum for Association loan officers in the Bank's history.

In May, the Farm Credit Bank of Texas relocated to new headquarters in West Austin, a cost-saving move that freed up capital for revenue generation. We expect to realize additional savings under a new strategic alliance with AgFirst Farm Credit Bank to share benefits and payroll programs.

We also have a strong financial alliance with CoBank, the primary lender to cooperatives in the Farm Credit System. Through the CoBank alliance, we strengthened and further diversified our balance sheet in 2004. In return, their alliance with us helped them provide improved capacity and patronage benefits for some of their member cooperatives. Both alliances prove the value of mutually beneficial relationships within the Farm Credit family.

Redefining Our Credit Culture

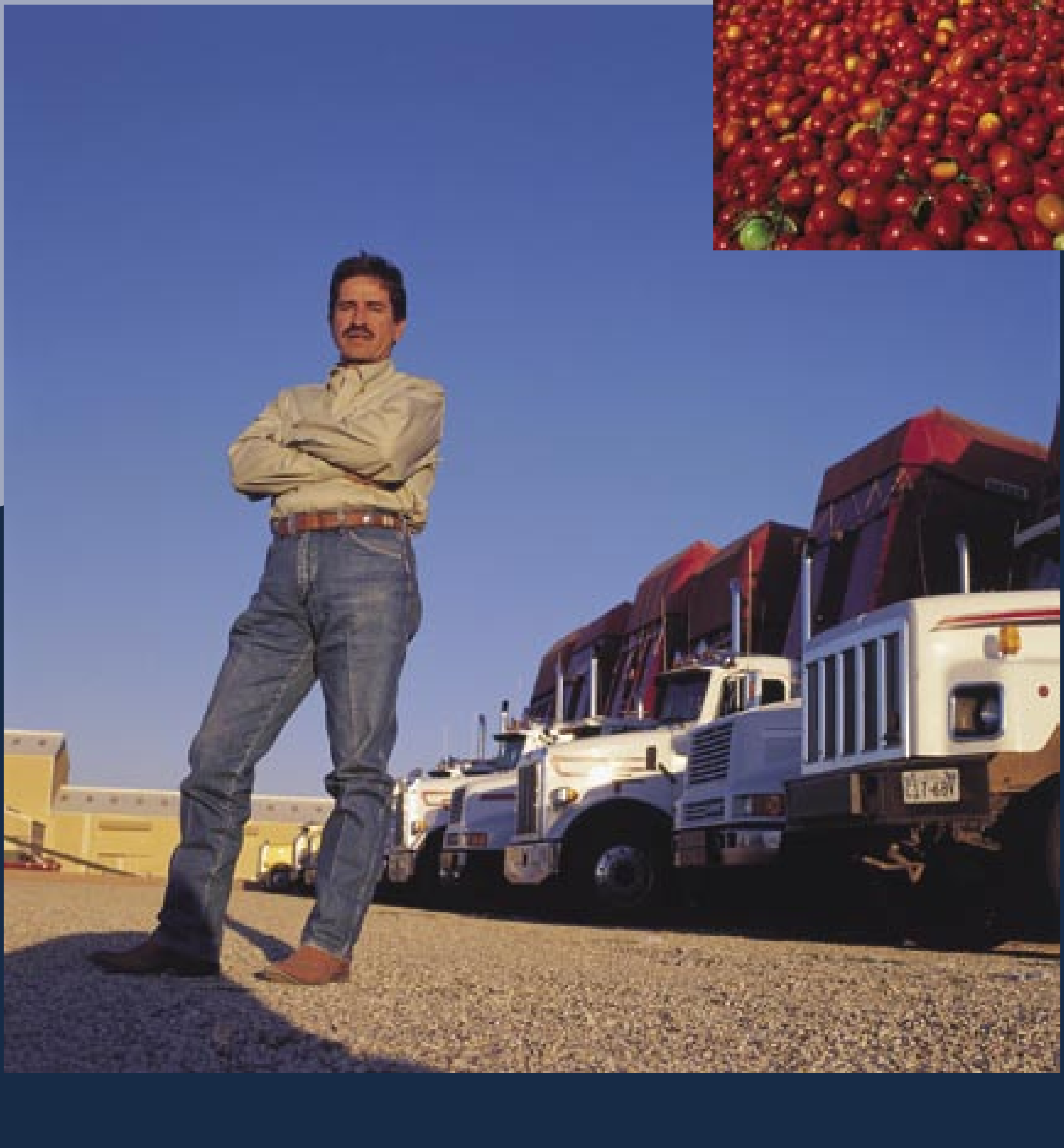
Accomplishments like these would not have happened, however, without a dramatic change in the Bank's credit culture. Beginning in 2003 and continuing in 2004, we transitioned the Bank's lending culture to support Association growth, moving away from a supervisory role and becoming an arm's-length partner with our customers. Today, our Associations can count on us to help them open doors and close deals.

Through our Direct Lending Group, a team of skilled Farm Credit veterans, we are helping our Associations aggressively attack their local markets by providing credit expertise and market development assistance. If they need help with pricing, packaging and structuring loans, we are available as a resource. If they require a partner on loans that exceed their lending authorities, they can turn to the Bank.

Meanwhile, our Capital Markets Group is leading the effort to turn the District into an earnings producer for our Associations by partnering with other lenders on large agribusiness loans. Through this group of highly experienced capital markets officers, we provide capital and liquidity for national and multinational food and agribusiness firms, rural utilities and rural communications companies.

Last year, the Farm Credit Bank of Texas enjoyed lending relationships with 38 financial institutions. Alliances like these enable us to offer financial solutions for even our largest customers.

We transitioned the Bank's lending culture to support Association growth. Today, our Associations can count on us to help them open doors and close deals.



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Moving Ahead

The Tenth Farm Credit District lending territory is a fertile agribusiness financing market, rich in diverse commodities, research talent and business know-how. As we grow our earnings engine in 2005, we will continue to work with our Associations to pursue a larger share of this marketplace and to build our reputation as a dominant agribusiness lender in the capital markets arena.

Last year, we increased our portfolio of purchased participation loans from $395.4 million at December 31, 2003, to $752.5 million at year-end 2004. This 90 percent increase in participation loans in 2004 set the stage for further achievement in the coming year.

Our commitment is to build on the momentum of our outstanding 2004 performance, and to deliver even greater value to our District Associations in the future.

This 90 percent increase in participation loans in 2004 set the stage for further achievement in the coming year.

REPORT OF MANAGEMENT

The financial statements of the Farm Credit Bank of Texas are prepared by management, which is responsible for their integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The financial statements have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances, except as noted. Other financial information included in this annual report is consistent with that in the financial statements.

To meet its responsibility for reliable financial information, management depends on the Bank's accounting and internal control systems, which have been designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions are properly authorized and recorded. The systems have been designed to recognize that the cost of controls must be related to the benefits derived. To monitor compliance, the internal audit staff of the Farm Credit Bank of Texas audits the accounting records, reviews accounting systems and internal controls, and recommends improvements as appropriate. The financial statements are audited by PricewaterhouseCoopers LLP (PwC), independent auditors, who also conduct a review of internal accounting controls to establish a basis for reliance thereon in determining the nature, extent and timing of the audit tests applied in the examination of the financial statements. In addition, the Bank is examined annually by the Farm Credit Administration.

The audit committee of the board of directors has overall responsibility for the Bank's system of internal controls and financial reporting. The audit committee meets periodically with management and PwC and reviews the results of audits and the examinations referred to previously. The audit committee also reviews with PwC the matters required to be discussed by Statement on Auditing Standards No. 61, "Communication with Audit Committees." The audit committee is composed of the entire board of directors of the Bank and held five meetings in 2004. In the opinion of management, the financial statements are true and correct and fairly state the financial position of the Farm Credit Bank of Texas at December 31, 2004, 2003, and 2002.

Ralph W. Cortese
Chairman of the Board

Larry R. Doyle
Chief Executive Officer

Thomas W. Hill
Chief Financial Officer

March 4, 2005

FIVE-YEAR SUMMARY OF SELECTED FINANCIAL DATA

Farm Credit Bank of Texas

(dollars in thousands)	**2004**	2003	2002	2001	2000
Balance Sheet Data					
Cash, federal funds sold and overnight investments	**$ 51,114**	$ 28,265	$ 61,859	$ 48,804	$ 13,630
Investment securities	**1,787,706**	1,518,102	785,071	503,978	551,124
Loans	**6,918,236**	5,834,929	5,826,951	5,111,193	4,421,612
Less allowance for loan losses	**239**	9,834	9,695	13,643	12,189
Net loans	**6,917,997**	5,825,095	5,817,256	5,097,550	4,409,423
Other property owned, net	**—**	529	2,615	373	373
Other assets	**44,388**	38,833	39,225	48,679	57,288
Total assets	**$ 8,801,205**	$ 7,410,824	$ 6,706,026	$ 5,699,384	$ 5,031,838
Obligations with maturities of one year or less	**$ 4,058,078**	$ 2,487,260	$ 3,751,585	$ 3,911,788	$ 3,468,011
Obligations with maturities greater than one year	**4,241,696**	4,445,935	2,585,463	1,461,130	1,262,924
Total liabilities	**8,299,774**	6,933,195	6,337,048	5,372,918	4,730,935
Preferred stock, net	**98,644**	98,644	—	—	—
Capital stock and participation certificates	**118,323**	109,787	109,896	93,938	77,918
Retained earnings	**292,022**	273,647	257,884	231,659	222,412
Accumulated other comprehensive (loss) income	**(7,558)**	(4,449)	1,198	869	573
Total shareholders' equity	**501,431**	477,629	368,978	326,466	300,903
Total liabilities and shareholders' equity	**$ 8,801,205**	$ 7,410,824	$ 6,706,026	$ 5,699,384	$ 5,031,838
Statement of Income Data					
Net interest income	**$ 66,662**	$ 49,826	$ 45,091	$ 36,427	$ 53,816
Negative provision (provision) for loan losses	**7,878**	(340)	2,902	(1,439)	(19,191)
Noninterest (expense) income, net	**(27,558)**	15,338	(15,526)	(10,110)	7,189
Net income	**$ 46,982**	$ 64,824	$ 32,467	$ 24,878	$ 41,814
Key Financial Ratios (unaudited)					
Rate of return on:					
Average assets	**0.59%**	0.92%	0.53%	0.48%	0.87%
Average shareholders' equity	**9.44%**	16.21%	9.43%	7.96%	12.68%
Net interest income to average earning assets	**0.85%**	0.71%	0.74%	0.70%	1.14%
Net charge-offs to average loans	**0.03%**	—	0.02%	—	0.49%
Total shareholders' equity to total assets	**5.70%**	6.45%	5.50%	5.73%	5.98%
Debt to shareholders' equity (:1)	**16.55**	14.52	17.17	16.46	15.72
Allowance for loan losses to total loans	**—**	0.17%	0.17%	0.27%	0.28%
Permanent capital ratio	**19.82%**	23.71%	18.06%	18.10%	19.18%
Total surplus ratio	**16.55%**	19.15%	14.01%	14.01%	14.40%
Core surplus ratio	**11.51%**	14.44%	12.56%	12.82%	13.63%
Net collateral ratio	**105.69%**	106.62%	105.32%	105.33%	105.21%
Net Income Distributions					
Patronage distributions declared					
Cash	**$ 16,775**	$ 49,144	$ 3,615	$ 3,102	$ 25,322
Allocated retained earnings	**14**	1,645	928	—	—

MANAGEMENT'S DISCUSSION & ANALYSIS

(dollars in thousands, except as otherwise noted)

The following commentary provides a discussion and analysis of the financial position and the results of operations of the Farm Credit Bank of Texas (the Bank or FCBT) for the years ended December 31, 2004, 2003 and 2002. The commentary should be read in conjunction with the accompanying financial statements, notes to the financial statements (Notes) and additional sections of this annual report.

The Bank is part of the Tenth Farm Credit District (District), which is part of the federally chartered Farm Credit System (System). The Bank provides funding to District Associations and certain Other Financing Institutions, which, in turn, provide credit to their borrowers/shareholders. As of December 31, 2004, the Bank served 8 Federal Land Credit Associations (FLCAs), 13 Agricultural Credit Associations (ACAs) and certain Other Financing Institutions (OFIs). FLCAs and ACAs are collectively referred to as Associations. See Note 1, "Organization and Operations," for an expanded description of the structure and operations of the Bank.

Financial Highlights

- Net interest income for the year ended December 31, 2004, was $66.7 million, a 33.8 percent increase over the year ended December 31, 2003.
- Net income totaled $47.0 million for the year ended December 31, 2004, a decrease of 27.5 percent compared to 2003. (Net income of $64.8 million for 2003 included a one-time gain of $30.5 million from the sale of the Bank's mineral interest holdings.)
- Outstanding loan volume of $6.9 billion at December 31, 2004, increased by $1.1 billion, or 18.6 percent, from $5.8 billion at December 31, 2003.
- Total assets of $8.8 billion at December 31, 2004, increased by $1.4 billion, or 18.8 percent, from $7.4 billion at December 31, 2003.
- Return on average assets and return on average shareholders' equity for the year ended December 31, 2004, were 0.59 and 9.44 percent, respectively, compared to 0.92 and 16.21 percent, respectively, for 2003.
- Patronage distributions declared and retained earnings allocated totaled $16.8 million in 2004, compared to $50.8 million in 2003. (The 2003 distributions included patronage of $37.6 million related to the Bank's gain on the sale of its mineral interest holdings and income from mineral operations.)

Projects Completed in 2004

- The Bank refined its allowance for loan loss (allowance) methodology, resulting in a negative provision of $7.9 million for the year ended December 31, 2004.
- The Bank adopted a single-employer plan to administer non-pension retirement benefits. In the single-employer plan, the Bank no longer has joint- and several-liability for non-pension postretirement benefits obligations with District Associations. The adoption resulted in the recognition of $7.8 million of expense to record the accumulated liability for the Bank's obligation for these benefits.

- Enhanced cash management products for District borrowers, *GFX* and *AgriLine*, were implemented in 2004. *GFX* is an application which automates wire-transfer activities. *AgriLine* provides an Association borrower with the ability to write checks on their line of credit.
- The Bank entered into a strategic alliance with AgFirst Farm Credit Bank, another System bank, for the use of their payroll and human resources system, as well as their capital markets loan accounting system. This alliance will result in favorable costs and new services for the entire District.
- The Bank implemented a 14-point credit classification system, thereby expanding and improving District entities' risk-management practices.

Strategic Initiatives for 2005

- **Reporting of loan types** – The Bank recently expanded the loan types within its loan system to allow better disclosure and analysis for credit risk profiling.
- **Economic capital model** – The Bank is continuing to assess and analyze loan performance data elements that will support an economic capital model based on the Basel II Capital Accord.
- **Strategic alliances** – The Bank will continue to pursue strategic alliances in certain operational areas with other System banks to create economies of scale.
- **Business continuity plan** – Testing and evaluation of the Bank's business continuity plan are scheduled events for 2005.

Risk Management

The major risks to which the Bank is exposed are:

- **Credit risk** – Credit risk is the risk of loss due to borrower or counterparty default. Credit risk related to borrowers is the possibility of default on the part of borrowers and is discussed in the "Financial Condition" section of this Management's Discussion and Analysis (MD&A), in Note 4, "Loans and Allowance for Loan Losses" and in Note 13, "Financial Instruments With Off-Balance-Sheet Risk." Credit risk related to counterparties is the possibility of default on the part of a counterparty on a derivative financial instrument that has a positive fair value, and is discussed in the "Asset/Liability Management" section of the MD&A and in Note 15, "Derivative Instruments and Hedging Activity."
- **Interest rate risk and liquidity risk** – Interest rate risk is the exposure of the Bank's financial condition to adverse movements in interest rates. Liquidity risk is the risk that the Bank would be unable to fund increases in assets and meet obligations as they become due. These risks are discussed in the "Asset/Liability Management" section of the MD&A and in Note 15, "Derivative Instruments and Hedging Activity."
- **Operational and business risks** – Operational and business risks relate to the risk of loss resulting from inadequate or failed processes or systems, human factors or external events. The Bank maintains and monitors a business continuity plan which includes safeguards and alternatives in the event of failures or damage that might affect its critical functions or systems infrastructure.

RESULTS OF OPERATIONS

Net Income

The Bank's net income of $46,982 for the year ended December 31, 2004, reflects a decrease of 27.5 percent from 2003, while 2003 net income of $64,824 increased by 99.7 percent from 2002. The 2003 results included the recognition of a one-time gain of $30.5 million on the sale of the Bank's mineral interest rights holdings. The return on average assets decreased to 0.59 percent for the year ended December 31, 2004, from 0.92 percent reported for the year ended December 31, 2003. The 2003 results included the Bank's sale of its mineral rights holdings, resulting in a one-time gain on the sale of $30.5 million. The return on average assets was 0.53 percent for the year ended December 31, 2002. Major components of the changes in net income for the referenced periods are outlined in the following table and discussion:

	2004 vs. 2003	2003 vs. 2002
Net income (prior period)	$ 64,824	$ 32,467
Increase (decrease) due to:		
Interest income	35,222	(19,369)
Interest expense	(18,386)	24,104
Net interest income	16,836	4,735
Provision for loan losses	8,218	(3,242)
Gain on sale of mineral rights	(30,494)	30,494
Noninterest income	(3,993)	4,430
Noninterest expense	(8,409)	(4,060)
Total change in net income	(17,842)	32,357
Net income	$ 46,982	$ 64,824

Interest Income

Total interest income for the year ended December 31, 2004, was $224,528, an increase of $35,222, or 18.6 percent, compared to 2003. This increase is primarily attributable to the combination of an increase in average earnings assets and the effect of an increase in the average yield on these assets.

Total interest income for 2003 was $189,306, a decrease of $19,369, or 9.3 percent, from 2002. This decrease was primarily attributable to the effects of the decreasing rate environment during 2003, offset by an increase in average earning assets.

The following table illustrates the impact that volume and yield changes had on interest income over these periods:

	Year Ended December 31, 2004 vs. 2003	Year Ended December 31, 2003 vs. 2002
Increase in average earning assets	$ 829,251	$ 918,694
Average yield (prior year)	2.69%	3.42%
Interest income variance attributed to change in volume	22,307	31,419
Average earning assets (current year)	7,857,254	7,028,003
Increase (decrease) in average yield	0.17%	(0.73%)
Interest income variance attributed to change in yield	12,915	(50,788)
Net change in interest income	$ 35,222	$ (19,369)

Interest Expense

Total interest expense for the year ended December 31, 2004, was $157,866, an increase of $18,386, or 13.2 percent, compared to the same period of 2003. The increase in interest expense for 2004 was primarily attributable to the increase in average interest-bearing liabilities and only slightly to the increase in interest rates.

Total interest expense for 2003 was $139,480, a decrease of $24,104, or 14.7 percent, from 2002. This decrease in interest expense was primarily attributable to declining interest rates, partially offset by an increase in average interest-bearing liabilities.

The following table illustrates the impact that volume and rate changes had on interest expense over these periods:

	Year Ended December 31, 2004 vs. 2003	Year Ended December 31, 2003 vs. 2002
Increase in average interest-bearing liabilities	$ 723,853	$ 871,227
Average rate (prior year)	2.10%	2.84%
Interest expense variance attributed to change in volume	15,201	24,743
Average interest-bearing liabilities (current year)	7,352,080	6,628,227
Increase (decrease) in average rate	0.05%	(0.74%)
Interest expense variance attributed to change in rate	3,185	(48,847)
Net change in interest expense	$ 18,386	$ (24,104)

Net Interest Income

Net interest income increased by $16,836 from 2003 to 2004. The increase was due to an $829,251 increase in average interest-earning assets and a 12-basis-point increase in the interest rate spread, which is the difference between the average rate received on interest-earning assets and the average rate paid on interest-bearing debt. The increase in the yield on investments was attributable to a reallocation into higher yield term securities as the portfolio size was increased to enhance both liquidity and earnings. Factors responsible for these changes are illustrated in the table, "Analysis of Net Interest Income."

Net interest income in 2003 was $4,735 greater than 2002. This increase was primarily due to a $918,694 increase in average interest-earning assets and a slight increase in the interest rate spread.

ANALYSIS OF NET INTEREST INCOME

	2004		2003		2002	
	Average Balance	**Interest**	Average Balance	Interest	Average Balance	Interest
Loans	**$ 6,242,127**	**$ 175,907**	$ 5,897,185	$ 165,037	$ 5,488,761	$ 194,135
Investments	**1,615,127**	**48,621**	1,130,818	24,269	620,548	14,540
Total earning assets	**7,857,254**	**224,528**	7,028,003	189,306	6,109,309	208,675
Interest-bearing liabilities	**7,352,080**	**157,866**	6,628,227	139,480	5,757,000	163,584
Impact of capital	**$ 505,174**		$ 399,776		$ 352,309	
NET INTEREST INCOME		**$ 66,662**		$ 49,826		$ 45,091

	2004 Average Yield	2003 Average Yield	2002 Average Yield
Yield on loans	**2.82%**	2.80%	3.54%
Yield on investments	**3.01%**	2.15%	2.34%
Yield on earning assets	**2.86%**	2.69%	3.42%
Cost of interest-bearing liabilities	**2.15%**	2.10%	2.84%
Interest rate spread	**0.71%**	0.59%	0.58%
Impact of capital	**0.14%**	0.12%	0.16%
Net interest income/average earning assets	**0.85%**	0.71%	0.74%

Provision for Loan Losses

In 2004, the Bank refined its allowance for loan loss methodology, as further described in the "Allowance for Loan Losses" section of this MD&A. The new methodology resulted in a $7.9 million negative provision for loan losses for 2004. This negative provision is a decrease of $8.2 million from the $340 provision of 2003. The provision for loan losses for 2003 increased by $3,242 from 2002. This increase is attributable to a negative provision of $3,332 in 2002 related to the sale of a nonaccrual loan to another System bank.

Noninterest Income

Noninterest income for the year ended December 31, 2004, was $15,301, a decrease of $34,487, or 69.3 percent, compared to 2003. The decrease is attributable to decreased ordinary mineral income of $4,994 and the gain of $30,494 on the sale of its mineral rights holdings in late 2003. The mineral rights had been retained on foreclosed properties when the surface rights were sold prior to the amendment of the Farm Credit Act in 1987 and they were recorded at zero value on the balance sheet. Ordinary mineral income from these mineral rights was included in "Miscellaneous income, net" in 2003 and 2002, and totaled $4,994 and $3,775, respectively.

The decline in fees for services to Associations of $1.9 million from 2003 to 2004 was the result of the continuing transition of certain services to the Associations to further develop an arm's-length relationship between the Bank and the Associations it serves.

In 2004, the Bank recorded a gain on the sale of investment securities of $420 associated with the sale of $85 million of asset-backed securities and collateralized mortgage obligations.

Noninterest income totaled $49,788 for 2003, an increase of $34,924 from 2002. The increase was attributable to the Bank's gain of $30,494 on the sale of its mineral rights holdings in late 2003 and to an increase of $1,220 in annual mineral income for the year, as described above. In addition, a loss of $2,919 was realized on sales of investment securities during 2002.

Noninterest Expenses

Noninterest expenses totaled $42,859 for 2004, reflecting an increase of $8,409, or 24.4 percent, over 2003. This increase was primarily due to a $6,045 increase in salaries and employee benefits, an increase of $3,904 in other operating expenses, and an increase of $863 in occupancy and equipment expense, offset by a decrease of $2,403 in intra-System financial assistance expense. The increase in salaries and employee benefits was attributable to the recording of $7.8 million in a cumulative, actuarially calculated liability for non-pension retirement benefits in 2004, resulting from a change in methodology followed by the Bank, as described below, offset by a decline in salaries of $518, a decline in pension and retirement expense of $793 and a decline in medical insurance premiums of $303. The increase in other operating expenses of $3,904 was primarily attributable to nonrecurring costs of $1,949 incurred during 2004 related to the sale of the Bank's old headquarters building, to an increase in professional fees and services of $1,210, and to an increase of $816 in fees and assessments from the Farm Credit Banks Funding Corporation (Funding Corporation), offset by an increase in the gains on sale of other property owned of $404. The increase in professional fees and services was primarily related to $612 in consulting fees related to initiatives and projects in progress, $430 in fees to another System bank for the use of their capital markets loan accounting system and their payroll and human resources system. Occupancy and equipment expense increased as a result of the cost of leasing new corporate office space in addition to costs associated with occupancy of the old headquarters building for the first six months of 2004. The decline in intra-System financial assistance expense is due to the maturity in July 2003 of three of the five remaining outstanding Financial Assistance Corporation (FAC) debt issuances.

In 2003 and 2002, the Bank participated in the District's multi-employer health and welfare benefit plan, through which it provided substantially all employees with postretirement health care and life insurance benefits. Neither the assets, liabilities nor cost of the multi-employer plan were segregated or separately accounted for by the participating entities. Costs were recognized only to the extent of contributions to the plan. In 2004, the Bank adopted a single-employer plan to administer non-pension postretirement benefits. Under the new plan, the Bank will no longer be jointly and severally liable with any other employers. The implementation of this new plan occurred in December 2004 and resulted in the recording of an expense and liability of $7.8 million, reflecting the unfunded accumulated benefit obligation for its retirees and employees, in accordance with Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions."

Noninterest expenses for the year ended December 31, 2003, totaled $34,450, an increase of $4,060 over the same period of 2002. The increase was primarily due to an increase of $2,242 in salaries and employee benefits, an increase of $664 in assessments from the Farm Credit Banks Funding Corporation (Funding Corporation), an increase of $448 in occupancy and equipment expense, and a $340 increase in premiums to the Farm Credit System Insurance Corporation (FCSIC).

FINANCIAL CONDITION

Loans

The Bank's loan portfolio consists of direct notes receivable from District Associations, loan participations purchased, loans to qualifying financial institutions serving agriculture and other loans. See Note 1, "Organization and Operations," and Note 4, "Loans and Allowance for Loan Losses," for further discussions.

Gross loan volume of $6.918 billion at December 31, 2004, reflected an increase of $1.083 billion, or 18.6 percent, from December 31, 2003. The increase in loan volume was attributable to the retail loan growth at the Associations, which are primarily funded through Association borrowings payable (direct notes) to the Bank. In addition, the Bank participations purchased increased by $357 million, or 90.3 percent, in 2004 as compared to 2003.

The loan volume balance of $5.835 billion at December 31, 2003, reflected an increase of $8 million, or 0.1 percent, from the $5.827 billion balance at December 31, 2002. This slight increase is net of the effect of the Bank's sale of $300 million in participations in its direct notes receivable from District Associations to another System bank.

The following table presents each loan category as a percentage of the total loan portfolio:

	December 31,		
	2004	2003	2002
Direct notes receivable from District Associations	**87.3%**	91.5%	92.9%
Participations purchased	**10.9**	7.7	6.3
Other loans	**1.8**	0.8	0.8
Total	**100.0%**	100.0%	100.0%

Bank credit quality has remained strong during the past three years, with the majority of Association and OFI direct notes rated acceptable during this period. Credit quality for all loans other than direct notes to Associations and OFIs was 95.4, 96.0 and 93.2 percent acceptable at December 31, 2004, 2003 and 2002, respectively.

The Bank is continuing its initiative to increase the volume in its participations portfolio, as evidenced by the increase in participations purchased during 2004. In November 2003, the Bank sold, at par, $300 million of participations in five of its direct notes receivable from Associations to another System bank. The purpose of the sale was to diversify the credit exposure of the Bank by providing capital for liquidity and expansion of the capital markets loan participations portfolio. On February 1, 2005, the Bank sold an additional $100 million in direct note participations to the same System bank.

Association Direct Notes

As the table illustrates, 87.3 percent of the Bank's loan portfolio consisted of direct notes from Associations at December 31, 2004. Terms of loans to Associations are specified in a separate general financing agreement between each Association and the Bank, and all assets of each Association secure the direct notes to the Bank. Each Association is a federally chartered instrumentality of the United States and is regulated by the Farm Credit Administration (FCA). See Note 1, "Organization and Operations," for further discussion of the Farm Credit System.

The credit exposure of the Bank's loans to Associations, which are evidenced by direct notes with full recourse, is dependent on the Associations' creditworthiness and the ability of their borrowers to repay loans made to them. The credit risk to the Bank is mitigated by diversity in the Associations' loan portfolios in terms of underlying collateral and income sources, geography and range of individual loan amounts. In addition, the risk-bearing capacities of the Associations are assessed quarterly by the Bank. Each Association maintains an allowance for loan losses determined by its management and is capitalized to serve its unique market area. Associations are subject to FCA regulations concerning minimum capital, loan underwriting and portfolio management, and are audited annually by independent accountants.

Despite a sluggish general economy, District Associations have experienced significant loan growth over the last three years. The District's loan growth is attributed to the competitive pricing inherent in the Farm Credit System's cooperative structure, continued solid demand for real estate in most areas of the District, increased marketing and customer service efforts undertaken by the Associations, and increased activity in loan participations. During 2004, the District Associations made significant use of loan participation activity as a means of diversifying their existing portfolios. Loan growth in the Associations is funded substantially by, and therefore results in, Association direct note growth at the Bank.

Government support of agriculture, the availability of off-farm income sources and utilization of guarantees have helped to diminish the effects of adverse economic conditions for the District's Associations.

The diversity of commodities underlying the District's credit portfolio is reflected in the following table:

	Percentage of Portfolio		
Commodity Group	**2004**	2003	2002
Livestock	**41%**	41%	42%
Crops	**16**	17	19
Timber	**11**	12	11
Cotton	**8**	10	10
Poultry	**5**	6	5
Dairy	**2**	2	2
Rural home	**1**	2	2
Other	**16**	10	9
Total	**100%**	100%	100%

While the Bank and District Associations have a significant number of loans to cattle producers, nearly half of these loans are not dependent on agricultural income for repayment, and the majority are collateralized by real estate. Livestock operations, including fed cattle stockers and cow-calf operations, represented approximately 41% percent of the District's loan portfolio at year-end. In spite of restrictions on importing U.S. beef by most countries due to the December 2003 discovery of bovine spongiform encephalopathy (BSE or "mad cow disease"), demand has remained strong. Prices for beef and dairy cows, as well as replacement heifers, have remained high. Feedlot performance has been marked by reduced slaughter weight because of the strong demand for beef and near-record prices which have caused cattle to be marketed sooner than usual.

Fed cattle supplies remain tight and may result in continued pressure to slaughter earlier in order to meet demand, as was the case at the end of 2003. Although pasture conditions were above average in 2004 and growing conditions resulted in abundant corn, wheat, soy and hay for feeding purposes, most ranchers are faced with pressure to sell at the beneficial current prices.

Although all sectors of the cattle industry have been profitable during 2004 and appear optimistic in the near future, the ultimate impact of the BSE discovery and access to foreign markets is not yet apparent. The USDA forecasts for 2005 assume a continuation of policies currently in effect, including a recently announced minimal-risk rule. The rule will set forth factors to be considered when listing a region as one of minimal risk, as well as requirements for risk-mitigating measures. The only minimal-risk region currently is Canada, which has accumulated an increasing inventory of cattle in the last two years.

District Associations serve all or part of five states. The following table illustrates the geographic dispersion of direct notes receivable from District Associations, by state:

	December 31,		
	2004	2003	2002
Texas	**71%**	74%	71%
Alabama	**10**	9	10
Mississippi	**9**	8	9
Louisiana	**8**	8	9
New Mexico	**2**	1	1
Total	**100%**	100%	100%

Direct notes from the Associations in Texas represent the majority of the Bank's direct notes from all District Associations. However, these notes are collateralized by a diverse loan portfolio, both in terms of geography and underlying commodities, which helps to mitigate the concentration risk often associated with one state or locale. Associations in each state have commodity diversification that is being augmented by increased purchases of loan participations.

Loans $5,000 or greater in size (which generally represent corporate agribusiness) make up approximately 9.8 percent of the District's loan volume outstanding. Approximately 69.8 percent of District loans outstanding are made up of loans of $1,000 or less, and loans less than $250 make up approximately 42.0 percent of outstanding loan volume.

Credit quality at the District's Associations at December 31, 2004, 2003 and 2002 remained strong, with greater than 96 percent acceptable for each of the three year-ends. Association non-earning assets as a percentage of total loans at December 31, 2004, was 0.5 percent, compared to 0.9 percent and 0.7 percent at December 31, 2003 and 2002, respectively.

High-Risk Assets

The following table discloses the components of the Bank's high-risk assets at December 31,

	2004	2003	2002
Nonaccrual loans	**$ 2,325**	$ 10,322	$ 4,789
Formally restructured loans	**618**	633	937
Loans past due 90 days or more and still accruing interest	**206**	—	—
Other property owned, net	—	529	2,615
Total	**$ 3,149**	$ 11,484	$ 8,341

High-risk assets decreased by $8,335, or 72.58 percent, from $11,484 at December 31, 2003, to $3,149 at December 31, 2004. The decrease of $7,997 in nonaccrual loans is attributed to the sale of a nonaccrual participation of $4,883, the reclassification of a $1,716 participation loan to accrual status, and repayments on nonaccrual loans. In addition, other property owned, net, decreased due to the sale during 2004 of properties which had been acquired through foreclosure. At December 31, 2004, $1,726, or 74.2 percent, of loans classified as nonaccrual were current as to principal and interest, compared to $9,921 (96.1 percent) and $2,555 (53.4 percent) at December 31, 2003 and 2002, respectively.

Allowance for Loan Losses

During 2004, the Bank completed a study to further refine its allowance for loan losses methodologies, taking into account recently issued guidance by the FCA, the System's regulator, as well as the Securities and Exchange Commission (SEC) and Federal Financial Institutions Examination Council guidelines. As a result of these studies and the resulting refinements in methodologies, during the fourth quarter of 2004 the Bank recorded a $7.9 million reversal of its allowance for loan losses.

The Bank's allowance for loan losses methodologies were adjusted and revised in the late 1980s to take into account the credit losses experienced in the mid-to-late 1980s, as a result of unusually adverse economic factors affecting American agriculture. Given the long cyclical nature of the agricultural economy, loss factors utilized to determine the allowance for loan losses subsequent to 1989 continued to reflect, to some extent, the loss history of the mid-to-late 1980s, which resulted in conservative estimates of the allowance for loan losses. The Bank's allowance for loan losses methodology utilized throughout the period was in accordance with generally accepted accounting principles and was consistently applied.

While conservative in estimating the allowance for loan losses, the methodology used resulted in annual provisions for loan losses over the periods that reflected changes in credit quality and loss experience. Accordingly, the reserves provided in the mid-to-late 1980s have, in effect, remained part of the allowance for loan losses. The Bank's allowance for loan losses methodology has consistently adhered to proper accounting policies under the regulatory supervision of the FCA in its role as a "safety and soundness" regulator. It was the FCA's view that the allowance for loan losses should include, among other considerations, an assessment of probable losses, historical loss experience and economic conditions.

In April 2004, the FCA issued an "Informational Memorandum" to System institutions regarding the criteria and methodologies that would be used in evaluating the adequacy of a System institution's allowance for loan losses. The FCA endorsed the direction provided by other bank regulators and the SEC and indicated that the conceptual framework addressed in their guidance would be included as part of their examination process.

The refinement in methodology resulted in calculated allowances for loan losses that were significantly less than the previously recorded balances due to revised loss factors that are more indicative of actual loss experience in recent years and current borrower analysis. The factors considered in determining the revised levels of allowance for loan losses were generally based on recent historical charge-off experience adjusted for relevant environmental factors. The Bank considered the following when adjusting the historical charge-offs experience:

- changes in credit risk classifications,
- changes in collateral values,
- changes in risk concentrations,
- changes in weather-related conditions, and
- changes in economic conditions.

While the reversals had a significant impact on 2004 results of operations and the previously recorded allowance for loan losses, the refinement in methodology is not expected to have a significant impact on comparative results of operations in future periods. Additionally, the refinement in methodology did not have a significant impact on the level of the risk-bearing capacity of the Bank, generally referred to as "risk funds" (capital plus the allowance for loan losses), which totaled $501.7 million at December 31, 2004 (7.3 percent of Bank loans), as compared with $487.5 million at December 31, 2003 (8.4 percent of Bank loans).

The allowance for loan losses at December 31, 2004, was $239, compared to $9,834 and $9,695 at December 31, 2003 and 2002, respectively. Because analysis indicates that an allowance on the Association direct notes is not warranted, the entire balance of the allowance for loan losses at December 31, 2004, reflects reserves for risks identified in the Bank's participations and other loans portfolios.

The following table provides an analysis of key statistics related to the allowance for loan losses at December 31,

	2004	2003	2002
Allowance for loan losses as a percentage of:			
Average loans	**—%**	0.17%	0.18%
Loans at year-end			
Total loans	**—**	0.17	0.17
Participations	**0.03**	2.19	2.64
Nonaccrual loans	**10.28**	95.27	202.44
Total high-risk loans	**7.59**	89.77	169.32
Net charge-offs to average loans	**0.03**	—	0.02
(Negative provision) provision expense to average loans	**(0.13)**	0.01	(0.05)

The activity in the allowance for loan losses is discussed further in Note 4, "Loans and Allowance for Loan Losses."

Liquidity and Funding Sources

FCBT's liquidity management objectives are to provide a reliable source of funding for borrowers, meet maturing debt obligations and fund operations in a cost-effective manner. The Bank maintains an investment portfolio comprising primarily high-quality liquid securities. The composition of the Bank's investment portfolio provides a stable source of operating funds, and the high-quality nature of the portfolio ensures that the portfolio can quickly be converted to cash without significant risk of loss.

The Bank's liquidity policy states that the Bank will maintain cash and marketable investment securities equal to a minimum of 90 days of maturing debt obligations. Implementation of this policy in 2003 required restructuring the Bank's debt portfolio and increasing the investment portfolio. A significant portion of short-term debt was replaced by a combination of long-term, floating-rate notes and term debt hedged with interest rate swaps to support the repricing characteristics of the Bank's variable rate loan portfolio. This strategy is part of the Bank's active participation in the System guideline to reduce the System's reliance on the short-term (one year or less) debt markets.

As of December 31, 2004, the Bank's investment portfolio consisted of the following:

	Amount	Percent of Total
Mortgage-backed securities	$ 1,583,435	86%
Money market instruments	140,738	8
Corporate debt	30,007	2
Asset-backed securities	33,526	2
Total investment securities	1,787,706	98
Overnight investments	47,500	2
Total	$ 1,835,206	100%

In the fourth quarter of 2004, the Bank realized a gain of $420 on the sale of mortgage-backed securities with a book value of $85,225.

In the fourth quarter of 2002, the Bank realized a loss of $2,919 on the sale of an asset-backed security, collateralized by credit card receivables, that had been downgraded from an "Aaa" to an "Aa" credit rating. FCA regulations require divestiture of securities when their credit rating falls below anything less than "the highest rating from a Nationally Recognized Statistical Rating Organization."

The Bank's primary source of funds is Systemwide debt securities issued through the Federal Farm Credit Banks Funding Corporation. This funding is readily available to the Bank due to the System's high credit quality and standing in the capital markets. The types and characteristics of securities are described in Note 7, "Bonds and Notes." As a condition of the Bank's participation in the issuance of Systemwide debt securities, the Bank is required by regulation to maintain specified eligible assets as collateral in an amount equal to or greater than the total amount of bonds and notes outstanding for which the Bank is liable. At December 31, 2004, the Bank had excess collateral of $501 million. Management expects the Bank to maintain sufficient collateral to permit its continued participation in Systemwide debt issuances in the foreseeable future.

The following tables provide a summary of the debt obligations of the Bank (dollars in millions):

	December 31, 2004	2003	2002
Bonds and term notes outstanding	**$ 7,500**	$ 6,657	$ 5,512
Average effective interest rate	**2.89%**	2.04%	2.58%
Average remaining life (years)	**1.6**	1.8	1.6
Discount notes outstanding	**$ 733**	$ 230	$ 773
Average effective interest rates	**1.96%**	0.82%	1.44%
Average remaining life (days)	**20**	19	68

	For the years ended December 31, 2004	2003	2002
Average interest-bearing liabilities outstanding	**$ 7,352**	$ 6,628	$ 5,757
Average interest rates on interest-bearing liabilities	**2.15%**	2.10%	2.84%

The Bank had no commercial bank lines of credit in use at December 31, 2004.

ASSET/LIABILITY MANAGEMENT

The Bank's asset/liability management process establishes controls for determining the composition of interest-rate-sensitive assets and liabilities. The Bank is able to direct the balance sheet structure by using various product offerings, debt issuance strategies and hedging transactions. Management's objective is to maintain adequate and stable net interest income in any interest rate environment.

FCBT maintains a loan pricing perspective that offering rates should be based on competitive market rates of interest. The District Associations offer a wide variety of products, including a one-month variable, and fixed-rate terms ranging from three to 30 years. The interest rates on these loans are directly related to the Bank's cost-to-issue debt in the capital markets. In addition, the Associations offer loan products in which the interest rates are tied to the Prime or LIBOR indices. Amortization terms for all loans are primarily in the range of one to 30 years.

The Bank offers an array of loan programs to Associations that are designed to meet the needs of Associations' borrowers. These loan programs have flexible repayment terms, including fixed and level principal payments, and a wide choice of payment frequencies, such as monthly, quarterly, semi-annual and annual payments. Additionally, the Bank offers a choice of early prepayment options to meet customer needs.

FCBT uses high-level complex modeling tools to manage and measure the risk characteristics of its earning assets and liabilities, including gap and simulation analyses. The following interest rate gap analysis sets forth the Bank's interest-earning assets and interest-bearing liabilities outstanding as of December 31, 2004, which are expected to mature or reprice in each of the future time periods shown:

INTEREST RATE GAP ANALYSIS

as of December 31, 2004

	Interest-Sensitive Period						
	One Month or Less	Over One Through Six Months	Over Six Through Twelve Months	**Total Twelve Months or Less**	Over One Year but Less Than Five Years	Over Five Years and Non-Rate-Sensitive	**Total**
Interest-Earning Assets							
Total loans	$ 4,754,975	$ 493,773	$ 300,349	**$ 5,549,097**	$ 1,132,699	$ 236,440	**$ 6,918,236**
Total investments	472,149	99,502	115,274	**686,925**	850,844	297,437	**1,835,206**
Total interest-earning assets	5,227,124	593,275	415,623	**6,236,022**	1,983,543	533,877	**8,753,442**
Interest-Bearing Liabilities							
Total interest-bearing funds*	5,417,533	514,000	345,000	**6,276,533**	1,736,000	220,000	**8,232,533**
Excess of interest-earning assets over interest-bearing liabilities	—	—	—	—	—	520,909	**520,909**
Total interest-bearing liabilities	5,417,533	514,000	345,000	**6,276,533**	1,736,000	740,909	**$ 8,753,442**
Interest rate sensitivity gap	$ (190,409)	$ 79,275	$ 70,623	**$ (40,511)**	$ 247,543	$ (207,032)	
Cumulative interest rate sensitivity gap	$ (190,409)	$ (111,134)	$ (40,511)	**$ (40,511)**	$ 207,032		

* The impact of interest rate swaps is included with interest-bearing funds.

The amount of assets or liabilities shown, which reprice or mature during the time period, were determined based on the earlier of repricing date, contractual maturity or anticipated loan prepayments. Additionally, adjustments have been made to reflect the characteristics of callable debt instruments and the impact of derivative transactions. The "interest rate sensitivity gap" line reflects the mismatch, or gap, in the maturity or repricing of interest-rate-sensitive assets and liabilities. A gap position can be either positive or negative. A positive gap indicates that a greater volume of assets than liabilities reprices or matures in a given time period, and conversely, a negative gap indicates that a greater volume of liabilities than assets reprices or matures in a given time period. On a 12-month cumulative basis, the Bank has a negative gap position, indicating that the Bank has an exposure to increasing interest rates. This occurs when maturing or repricing debt is replaced by debt with higher cost, while corresponding income on interest-earning assets increases more slowly due to the lag in their maturity or repricing cycle.

To more appropriately reflect the cash flow and repricing characteristics of the Bank's balance sheet, an estimate of expected prepayments on loans is reflected in the maturities of the loans in the earning assets section of the gap analysis. Changes in market interest rates will affect the volume of prepayments on loans. Correspondingly, adjustments have been made to reflect the characteristics of callable debt instruments and the effect derivative financial instruments have on the repricing structure of the Bank's balance sheet.

Interest rate risk exposure is measured by simulation modeling, which calculates the Bank's expected net interest income based upon projections of interest-rate-sensitive assets and liabilities, derivative financial instruments and interest rate scenarios. The Bank monitors its financial exposure to instantaneous and parallel changes in interest rates of 200 basis points up or down over a rolling 12-month period. Per FCA regulations, when the current 3-month Treasury bill interest rate is less than 4 percent, both the minus 400 and minus 200 basis point scenarios should be replaced with a downward shock equal to one-half of the 3-month Treasury bill rate. The Bank's policy guideline for the maximum negative impact to the Bank's net interest income is 16 percent. The Bank manages its interest rate risk exposure well within this guideline. As of December 31, 2004, projected annual District net interest income of the existing interest-earning assets and interest-bearing liabilities would decrease by $4,548, or 5.9 percent, if interest rates were to increase by 200 basis points, and would increase by $8,922, or 11.6 percent, if interest rates were to decrease by 111 basis points.

Utilizing simulation analysis, the Bank projects net interest income and market value of equity (the market value of assets net of the market value of liabilities) under multiple interest rate scenarios. The following tables set forth FCBT's projected annual net interest income and market value of equity for interest rate movements as prescribed by policy as of December 31, 2004, based on the Bank's interest-earning assets and interest-bearing liabilities at December 31, 2004:

Net Interest Income

Scenario	Net Interest Income	% Change
400 BP Shock	$ 66,116	(14.4)%
200 BP Shock	72,688	(5.9)
0 BP	77,236	—
- 111 BP Shock	86,158	11.6

Market Value of Equity

Scenario	Assets	Liabilities	Equity	% Change
Book value	$ 8,801,205	$ 8,299,774	$ 501,431	11.1%
+ 200 BP Shock	8,569,810	8,203,282	366,528	(18.8)
0 BP Shock	8,770,394	8,318,931	451,463	—
- 111 BP Shock	8,861,682	8,371,600	490,082	8.6

The Bank uses derivative financial instruments, consisting primarily of interest rate swaps, to manage its interest rate risk and liquidity position. Interest rate swaps for asset/liability management purposes are used to change the repricing characteristics of liabilities to match the repricing characteristics of the assets they support, thereby creating synthetic floating-rate debt. In 2004, the Bank entered into two cash flow hedges as a part of an overall strategy to shorten the repricing characteristics of its fixed-rate debt. The Bank does not hold, and is restricted by policy from holding, derivative financial instruments for trading purposes and is not a party to leveraged derivative transactions.

At December 31, 2004, the Bank had interest rate swaps outstanding with a notional amount of $1.8 billion and a negative fair value of $9.4 million and cash flow hedges with a notional amount of $95 million and a positive fair value of $1.3 million. To the extent that its derivatives have a negative fair value, the Bank has a payable on the instrument, and the counterparty is exposed to the credit risk of the Bank. To the extent that its derivatives have a positive fair value, the Bank has a receivable on the instrument and is therefore exposed to credit risk from the counterparty. To manage this credit risk, the Bank diversifies counterparties and monitors the credit ratings of all counterparties with whom they transact. The Bank's activity in derivative financial instruments for 2004 is summarized in the table below:

Activity in Derivative Financial Instruments
(Notional Amounts)

(in millions)	Receive Fixed; Pay Floating
Balance, December 31, 2003	$ 1,670
Additions	1,080
Maturities/calls	(475)
Terminations	(350)
Balance, December 31, 2004	**$ 1,925**

Capital

Total shareholders' equity at December 31, 2004, was $501,431, compared to $477,629 and $368,978 at December 31, 2003 and 2002, respectively. The increases are due primarily to the issuance of preferred stock and increases in retained earnings.

On November 7, 2003, FCBT issued 100,000 shares of $1,000 Cumulative Perpetual Preferred Stock for net proceeds of $98.6 million, after expenses associated with the offering. The dividend rate is 7.561 percent, payable semi-annually to December 15, 2013, after which dividends are payable quarterly at a rate equal to 3-month LIBOR plus 445.75 bps. The preferred stock qualifies as capital and is reflected as a separate line item in the Bank's balance sheet. The issuance of the preferred stock was a part of the Bank's plan to fund the expansion of its loan portfolio with higher earning participations, which will contribute to a reduction in the cost of funds for the District's Associations. The Bank paid out dividends totaling $7,561 on the preferred stock on June 15 and December 15, 2004.

The Bank paid out cash patronage totaling $16.8 million during 2004, including $12.0 million paid on average direct note volumes, $1.9 million in patronage on certain participations and $2.9 million in interest credit patronage, based on each Association's and OFI's stock investment in the Bank.

Accumulated other comprehensive loss increased $3.1 million, or 70.0 percent, to $7.5 million at December 31, 2004, from $4.4 million at December 31, 2003, due to an increase of $4.4 million in unrealized net losses on the Bank's investments, partially offset by an increase of $1.3 million in unrealized gains on the Bank's cash flow hedges. The increases in unrealized net losses on investments were primarily due to the effect of rising market interest rates on fixed-rate mortgage-backed securities in the Bank's investment portfolio. The $1.3 million increase in unrealized gains on cash flow hedges represents the increase in their fair value since their inception early in 2004.

Capital adequacy is evaluated using various ratios for which the FCA has established regulatory minimums. The following table reflects the Bank's capital ratios at December 31,

	2004	2003	2002	Regulatory Minimum
Permanent capital ratio	**19.82%**	23.71%	18.06%	7.00%
Total surplus ratio	**16.55**	19.15	14.01	7.00
Core surplus ratio	**11.51**	14.44	12.56	3.50
Collateral ratio	**105.69**	106.62	105.32	103.00

For additional information about the Bank's capital, see Note 8, "Shareholders' Equity."

OTHER

Contractual Interbank Performance Agreement

All banks in the System, the Federal Farm Credit Banks Funding Corporation and the FAC participate in the Contractual Interbank Performance Agreement (CIPA). The objective of the CIPA is to encourage districts to achieve and/or maintain higher levels of financial condition and performance by subjecting them to a scoring process based on district profitability, asset quality and capital adequacy, with penalties for weak liquidity and excessive interest rate risk. The District's composite CIPA score is in compliance with agreed-upon CIPA standards and is expected to remain so during 2005.

Regulatory and Other Matters

Effective January 1, 2004, two of the District's FLCAs merged. Effective July 1, 2004, one of the District FLCAs restructured to form an ACA parent company structure with operating FLCA and PCA subsidiaries. As of December 31, 2004, the Associations totaled 21, with 13 ACAs and 8 FLCAs. During 2004 the Bank entered into funding relationships with two new OFIs; at December 31, 2004, the Bank had agreements with four OFIs.

Any statements contained in this Management's Discussion and Analysis that are not historical facts are forward-looking statements that involve risks and uncertainties. Such forward-looking statements include, but are not limited to, the impact of economic conditions (both generally and more specifically in the markets in which the District operates), the impact of competition for the District's customers from other providers of financial services, the impact of government legislation or regulation, and other risks detailed in this annual report.

REPORT OF INDEPENDENT AUDITORS

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
300 West 6th Street
Suite 1800
Austin TX 78701
Telephone (512) 477 1300
Facsimile (512) 477 8681

Report of Independent Auditors

To the Board of Directors and Shareholders
of the Farm Credit Bank of Texas:

In our opinion, the accompanying balance sheets and the related statements of income, changes in shareholders' equity and of cash flows present fairly, in all material respects, the financial position of the Farm Credit Bank of Texas (Bank) at December 31, 2004, 2003 and 2002, and the results of its operations, changes in shareholders' equity and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

March 4, 2005

BALANCE SHEETS

Farm Credit Bank of Texas

(in thousands)	2004	December 31, 2003	2002
Assets			
Cash	**$ 3,614**	$ 6,465	$ 7,890
Federal funds sold and overnight investments	**47,500**	21,800	53,969
Investment securities	**1,787,706**	1,518,102	785,071
Loans	**6,918,236**	5,834,929	5,826,951
Less allowance for loan losses	**239**	9,834	9,695
Net loans	**6,917,997**	5,825,095	5,817,256
Accrued interest receivable	**26,032**	19,194	19,066
Other property owned, net	**—**	529	2,615
Premises and equipment, net	**2,416**	957	929
Other assets	**15,940**	18,682	19,230
Total assets	**$ 8,801,205**	$ 7,410,824	$ 6,706,026
Liabilities and shareholders' equity			
Liabilities			
Bonds and notes, net	**$ 8,232,533**	$ 6,886,738	$ 6,284,567
Accrued interest payable	**36,850**	32,700	38,329
Intra-System financial assistance payable	**—**	280	4,334
Other liabilities	**30,391**	13,477	9,818
Total liabilities	**8,299,774**	6,933,195	6,337,048
Commitments and contingencies (Note 12)			
Shareholders' equity			
Preferred stock, net	**98,644**	98,644	—
Capital stock	**118,323**	109,787	109,896
Allocated retained earnings	**9,980**	14,237	11,711
Unallocated retained earnings	**282,042**	259,410	246,173
Accumulated other comprehensive (loss) income	**(7,558)**	(4,449)	1,198
Total shareholders' equity	**501,431**	477,629	368,978
Total liabilities and shareholders' equity	**$ 8,801,205**	$ 7,410,824	$ 6,706,026

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

STATEMENTS OF INCOME

Farm Credit Bank of Texas

(in thousands)	2004	Year Ended December 31, 2003	2002
Interest Income			
Investment securities and other	**$ 48,621**	$ 24,269	$ 14,540
Loans	**175,907**	165,037	194,135
Total interest income	**224,528**	189,306	208,675
Interest Expense			
Bonds and notes	**157,818**	139,447	163,555
Notes payable and other	**48**	33	29
Total interest expense	**157,866**	139,480	163,584
Net Interest Income	**66,662**	49,826	45,091
(Negative provision) provision for loan losses	**(7,878)**	340	(2,902)
Net interest income after provision for loan losses	**74,540**	49,486	47,993
Noninterest Income			
Fees for services to Associations	**8,744**	10,624	11,065
Fees for loan-related services	**3,817**	3,071	2,446
Gain on sale of mineral rights	**—**	30,494	—
Gain (loss) from sale of investment securities	**420**	—	(2,919)
Miscellaneous income, net	**2,320**	5,599	4,272
Total noninterest income	**15,301**	49,788	14,864
Noninterest Expenses			
Salaries and employee benefits	**24,688**	18,643	16,401
Occupancy and equipment	**4,557**	3,694	3,246
Intra-System financial assistance expenses	**398**	2,801	3,206
Other operating expenses	**13,216**	9,312	7,537
Total noninterest expenses	**42,859**	34,450	30,390
Net Income	**$ 46,982**	$ 64,824	$ 32,467

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

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Farm Credit Bank of Texas

(in thousands)	Preferred Stock	Capital Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at December 31, 2001	$ —	$ 93,938	$ 13,410	$ 218,249	$ 869	$ 326,466
Comprehensive income						
Net income	—	—	—	32,467	—	32,467
Unrealized net gains on investment securities	—	—	—	—	329	329
Total comprehensive income	—	—	—	32,467	329	32,796
Capital stock issued	—	17,726	—	—	—	17,726
Capital stock and allocated retained earnings retired	—	(1,768)	(2,627)	—	—	(4,395)
Patronage						
Cash	—	—	—	(3,615)	—	(3,615)
Shareholders' equity	—	—	928	(928)	—	—
Balance at December 31, 2002	—	109,896	11,711	246,173	1,198	368,978
Comprehensive income						
Net income	—	—	—	64,824	—	64,824
Unrealized net losses on investment securities	—	—	—	—	(5,647)	(5,647)
Total comprehensive income	—	—	—	64,824	(5,647)	59,177
Preferred stock issued, net of expenses	98,644	—	—	—	—	98,644
Capital stock issued	—	6,638	953	—	—	7,591
Capital stock and allocated retained earnings retired	—	(6,747)	(72)	—	—	(6,819)
Cash dividends – preferred stock	—	—	—	(798)	—	(798)
Patronage						
Cash	—	—	—	(49,144)	—	(49,144)
Shareholders' equity	—	—	1,645	(1,645)	—	—
Balance at December 31, 2003	98,644	109,787	14,237	259,410	(4,449)	477,629
Comprehensive income						
Net income	—	—	—	46,982	—	46,982
Unrealized net losses on investment securities	—	—	—	—	(4,418)	(4,418)
Unrealized net gains on cash flow derivatives	—	—	—	—	1,309	1,309
Total comprehensive income	—	—	—	46,982	(3,109)	43,873
Capital stock issued	—	9,122	—	—	—	9,122
Capital stock and allocated retained earnings retired	—	(586)	(4,271)	—	—	(4,857)
Cash dividends – preferred stock	—	—	—	(7,561)	—	(7,561)
Patronage						
Cash	—	—	—	(16,775)	—	(16,775)
Shareholders' equity	—	—	14	(14)	—	—
Balance at December 31, 2004	**$ 98,644**	**$ 118,323**	**$ 9,980**	**$ 282,042**	**$ (7,558)**	**$ 501,431**

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

STATEMENTS OF CASH FLOWS

Farm Credit Bank of Texas

(in thousands)	Year Ended December 31, 2004	2003	2002
Cash Flows From Operating Activities			
Net income	**$ 46,982**	$ 64,824	$ 32,467
Reconciliation of net income to net cash provided by operating activities			
(Negative provision) provision for loan losses	**(7,878)**	340	(2,902)
Provision for losses on other property owned	**39**	132	171
Depreciation on premises and equipment	**655**	456	1,168
Accretion of net discount on loans	**(210)**	—	—
Amortization and accretion on debt instruments	**3,913**	(7,006)	16,910
Accretion of net (premium) on investments	**(3,466)**	(7,663)	(491)
(Gains) losses on sales of investment securities	**(420)**	—	2,919
Gain on sales of mineral rights	**—**	(30,494)	—
Gains on sales of other property owned, net	**(511)**	(409)	(36)
Loss on sales of premises and equipment	**14**	20	220
(Increase) decrease in accrued interest receivable	**(6,838)**	(128)	3,678
Increase in other assets, net	**(3,501)**	(2,519)	(605)
Increase (decrease) in accrued interest payable	**4,150**	(5,629)	(5,064)
Decrease in intra-System financial assistance payable	**(280)**	(4,054)	(405)
Increase in other liabilities, net	**7,103**	3,659	2,593
Net cash provided by operating activities	**39,752**	11,529	50,623
Cash Flows From Investing Activities			
Net (increase) decrease in federal funds sold and securities purchased under resale agreements	**(25,700)**	32,169	(14,969)
Investment securities			
Purchases	**(2,938,373)**	(7,713,178)	(4,738,052)
Proceeds from maturities, calls and prepayments	**2,582,672**	6,982,163	4,432,751
Proceeds from sales	**85,565**	—	22,109
Increase in loans, net	**(1,084,814)**	(8,179)	(719,212)
Proceeds from sales of mineral rights, net	**—**	30,494	—
Proceeds from sales of other property owned, net	**1,001**	2,363	31
Proceeds from sales of premises and equipment	**71**	68	15,962
Expenditures for premises and equipment	**(2,199)**	(572)	(640)
Net cash used in investing activities	**(1,381,777)**	(674,672)	(1,002,020)
Cash Flows From Financing Activities			
Bonds and notes issued	**92,451,402**	32,134,277	23,012,741
Bonds and notes retired	**(91,092,157)**	(31,522,033)	(22,072,974)
Preferred stock issued, net of expenses	**—**	98,644	—
Capital stock issued	**9,122**	7,591	17,726
Capital stock retired and allocated retained earnings distributed	**(4,857)**	(6,819)	(4,395)
Cash dividends on preferred stock	**(7,561)**	(798)	—
Cash patronage distributions paid	**(16,775)**	(49,144)	(3,615)
Net cash provided by financing activities	**1,339,174**	661,718	949,483
Net decrease in cash	**(2,851)**	(1,425)	(1,914)
Cash at beginning of year	**6,465**	7,890	9,804
Cash at End of Year	**$ 3,614**	$ 6,465	$ 7,890
Supplemental Schedule of Noncash Investing and Financing Activities			
Financed sales of other property owned	**$ —**	$ —	$ 40
Loans transferred to other property owned	**—**	—	2,448
Unrealized net (loss) gain on investment securities	**(4,418)**	(5,647)	329
Supplemental Schedule of Noncash Changes in Fair Value Related to Hedging Activities			
(Decrease) increase in bonds and notes	**$ (17,363)**	$ (3,067)	$ 11,676
Supplemental Disclosure of Cash Flow Information			
Interest paid	**$ 142,774**	$ 147,640	$ 156,801

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

NOTES TO FINANCIAL STATEMENTS

Farm Credit Bank of Texas

(dollars in thousands, except per share amounts and as otherwise noted)

Note 1 — Organization and Operations

A. Organization:

The Farm Credit Bank of Texas (FCBT or Bank) is one of the banks of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations established by acts of Congress. The System is currently subject to the provisions of the Farm Credit Act of 1971, as amended (Farm Credit Act).

The United States is served by four Farm Credit Banks (FCBs), each of which has specific lending authority within its chartered territory, and one Agricultural Credit Bank (ACB), which has nationwide lending authority for lending to cooperatives. The ACB also has the lending authorities of an FCB within its chartered territories. The Bank is chartered to serve the states of Alabama, Louisiana, Mississippi, New Mexico and Texas.

Each FCB and the ACB serve one or more Federal Land Credit Associations (FLCAs) and/or Agricultural Credit Associations (ACAs). The District's 8 FLCAs, 13 ACA parent Associations, each containing two wholly-owned subsidiaries (an FLCA and a Production Credit Association [PCA]), certain Other Financing Institutions (OFIs), and the Bank's preferred stockholders jointly owned the Bank at December 31, 2004. FLCAs and ACAs collectively are referred to as Associations. The Bank and its related Associations collectively are referred to as the Tenth Farm Credit District (District).

Each FCB and the ACB are responsible for supervising certain activities of the Associations within their districts. The FCBs and/or Associations make loans to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. Funds for the FCBs and the ACB are principally raised through the sale of consolidated Systemwide bonds and notes to the public, through the Federal Farm Credit Banks Funding Corporation (Funding Corporation).

The Farm Credit Administration (FCA) is delegated authority by Congress to regulate the Bank and Associations. The activities of the Bank and Associations are examined by the FCA, and certain actions by these entities are subject to the FCA's prior approval.

B. Operations:

The Farm Credit Act sets forth the types of authorized lending activities and financial services which can be offered by the Bank and defines the eligible borrowers which it may serve.

The Bank lends primarily to the District Associations in the form of revolving lines of credit (direct notes) to fund the Associations' loan portfolios. These direct notes are collateralized by a pledge of substantially all of each Association's assets. The terms of the revolving direct notes are governed by a general financing agreement between the Bank and each Association. Each advance is structured so that the principal cash flow, repricing characteristics and underlying index (if any) of the advance match those of the assets being funded. By match-funding the Association loans, the interest rate risk is effectively transferred to the Bank. Advances are also made to fund general operating expenses of the Associations. FLCAs borrow money from the Bank and, in turn, originate and service long-term real estate and agribusiness loans to their members. ACAs borrow from the Bank and in turn originate and service long-term mortgage loans through the FLCA subsidiary and short- and intermediate-term loans through the PCA subsidiary. An Association's indebtedness to the Bank, under a general financing agreement between the Bank and the Association, represents demand borrowings by the Association to fund the majority, but not all, of its loan advances to Association members/borrowers.

In addition to providing loan funds to District Associations, the Bank also provides banking and support services to them, such as accounting, information systems and marketing. The fees charged by the Bank for these services are included in the Bank's noninterest income.

The Bank is also authorized to provide, in participation with other lenders, credit, credit commitments and related services to eligible borrowers. Eligible borrowers include farmers, ranchers, producers or harvesters of aquatic products, rural residents and farm-related businesses. The Bank may also lend to qualifying financial institutions engaged in lending to eligible borrowers.

The Bank, in conjunction with other banks in the System, jointly owns several service organizations which were created to provide a variety of services for the System. The Bank has ownership interests in the following service organizations:

- Funding Corporation — provides for the issuance, marketing and processing of Systemwide debt securities using a network of investment dealers and dealer banks. The Funding Corporation also provides financial management and reporting services.
- Farm Credit System Building Association — leases premises and equipment to the FCA, as required by the Farm Credit Act.
- Farm Credit System Association Captive Insurance Company — as a reciprocal insurer, provides insurance services to its member organizations.

These ownership interests are accounted for using the cost method. In addition, the Farm Credit Council acts as a full-service, federated trade association which represents the System before Congress, the Executive branch and others, and provides support services to System institutions on a fee basis.

The Farm Credit Act also established the Farm Credit System Insurance Corporation (FCSIC) to administer the Farm Credit Insurance Fund (Insurance Fund). The Insurance Fund is used (1) to ensure the timely payment of principal and interest on Systemwide debt obligations, (2) to ensure the retirement of protected borrower capital at par or stated value, and (3) for other specified purposes. The Insurance Fund also is available for the permissible uses of providing assistance to certain troubled and insured System institutions and for covering the operating expenses of the FCSIC.

Each System bank is insured and is required to pay premiums to the Insurance Fund until the monies in the Insurance Fund reach the "secure base amount," which is defined in the Farm Credit Act as 2.0 percent of the System's aggregate insured obligations (Systemwide debt obligations). When the amount in the Insurance Fund exceeds the secure base amount, the FCSIC is required to reduce premiums, but it still must ensure that reduced premiums are sufficient to maintain the level of the Insurance Fund at the secure base amount. Premiums are based on the average principal outstanding of accrual and nonaccrual loans of the District for the year. At December 31, 2004, the assets in the Insurance Fund were approximately $2 billion; however, due to the other authorized uses of the Insurance Fund, there is no assurance that any available amount in the Insurance Fund will be sufficient to ensure the timely payment of principal or interest on an insured debt obligation in the event of a default by any System bank having primary liability thereon. Assets of the Insurance Fund will be used to repay, upon maturity, the Financial Assistance Corporation (FAC) debt issued to fund the purchase of $374 million of preferred stock issued by the former Federal Land Bank of Jackson (FLB of Jackson), to the extent that funds of the FAC Trust Fund (Trust Fund) are not sufficient for such purposes. As of December 31, 2004, available funds in the Trust Fund amounted to $78.1 million.

Note 2 — Summary of Significant Accounting Policies

The accounting and reporting policies of the Bank conform to accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of financial statements in conformity with GAAP requires the management of the Bank to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant estimates are discussed in these notes as applicable.

The accompanying financial statements include the accounts of the Bank and reflect the investments in and allocated earnings of the service organizations in which the Bank has partial ownership interests. The multi-employer structure of certain retirement and benefit plans of the District results in the recording of these plans only in the combined financial statements of the District.

A. Cash:

Cash, as included in the financial statements, represents cash on hand and on deposit at banks.

B. Investment Securities:

The Bank, as permitted under FCA regulations, holds eligible investments for the purposes of maintaining a liquidity reserve, managing short-term surplus funds and managing interest rate risk.

The Bank's investments are to be held for an indefinite time period and, accordingly, have been classified as available for sale at December 31, 2004, 2003 and 2002. These investments are reported at fair value, and unrealized holding gains and losses are netted and reported as a separate component of shareholders' equity in the balance sheet. Purchased premiums and discounts are amortized or accreted using a constant yield method (which is not materially different from the effective interest method) over the term of the respective issues. Realized gains and losses are determined using the specific identification method and are recognized in current operations.

The Bank reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered an impairment, is temporary or permanent. In the event of permanent impairment, the cost basis of the investment would be written down to its fair value, and the realized loss would be included in current earnings.

C. Loans and Allowance for Loan Losses:

Loans are carried at their principal amount outstanding less any unearned income or unamortized discount. Interest on loans is accrued and credited to interest income based on the daily principal amount outstanding. Funds which are held by the Bank on behalf of the borrowers, where legal right of setoff exists and which can be used to reduce outstanding loan balances at the Bank's discretion, are netted against loans in the balance sheet.

Loans are generally placed in nonaccrual status when principal or interest is delinquent for 90 days (unless adequately secured and in the process of collection) or circumstances indicate that full collection of principal and interest is in doubt. In accordance with FCA regulations, all loans 180 days or more past due are considered nonaccrual. When a loan is placed in nonaccrual status, accrued interest deemed uncollectible is either reversed (if current year interest) or charged against the allowance for loan losses (if prior year interest).

Payments received on nonaccrual loans are generally applied to the recorded investment in the loan asset. If collection of the recorded investment in the loan is fully expected and the loan does not have a remaining unrecovered prior charge-off associated with it, payments are recognized as interest income. Nonaccrual loans may be returned to accrual status when contractual principal and interest are current, prior charge-offs have been recovered, the ability of the borrower to fulfill the contractual repayment terms is fully expected and the loan is not classified "doubtful" or "loss." If previously unrecognized interest income exists upon reinstatement of a nonaccrual loan to accrual status, interest income will only be recognized upon receipt of cash payments applied to the loan.

In cases where a borrower experiences financial difficulties and the Bank makes certain monetary concessions to the borrower through modifications to the contractual terms of the loan, the loan is classified as a restructured loan. If the borrower's ability to meet the revised payment schedule is uncertain, the loan is classified as a nonaccrual loan.

Statement of Financial Accounting Standards (SFAS) No. 91, "Accounting for Nonrefundable Fees and Costs Associated With Originating and Acquiring Loans and Initial Direct Costs of Leases," requires loan origination fees and direct loan origination costs, if material, to be capitalized and the net fee or cost to be amortized over the life of the related loan as an adjustment to yield. SFAS No. 91 has not been implemented because the effects were not material to the financial position or results of operations for any year presented.

The allowance for loan losses is a valuation account used to reasonably estimate loan and lease losses as of the financial statement date. Determining the appropriate allowance for loan losses balance involves significant judgment about when a loss has been incurred and the amount of that loss. The determination of the allowance for loan losses is based on management's current judgments about the credit quality of its loan portfolio. A specific allowance may be established for impaired loans under SFAS No. 114. Impairment of these loans is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as practically expedient, at the loan's observable market price or fair value of the collateral if the loan is collateral dependent. See Note 4 for a discussion on the refinement of the allowance for loan losses methodologies.

The allowance for loan losses is maintained at a level considered adequate by management to provide for probable and estimable losses inherent in the loan portfolio. The allowance is increased through provisions for loan losses and loan recoveries and is decreased through reversals of provisions for loan losses and loan charge-offs.

The level of allowance for loan losses is generally based on recent charge-off experience adjusted for relevant environmental factors. The Bank considers the following factors when adjusting the historical charge-offs experience:

- Changes in credit risk classifications,
- Changes in collateral values,
- Changes in risk concentrations,
- Changes in weather-related conditions, and
- Changes in economic conditions.

D. Other Property Owned:

Other property owned, consisting of real and personal property acquired through foreclosure or other collection action, is recorded at fair value, based on appraisal, less estimated selling costs upon acquisition. Revised estimates to the fair value, established by appraisal, less cost to sell are reported as adjustments to the carrying amount of the asset, provided that such adjusted value is not in excess of the carrying amount at acquisition. Income and expenses from operations and carrying value adjustments are included in miscellaneous income.

E. Premises and Equipment:

Premises and equipment are carried at cost less accumulated depreciation. Depreciation expense is calculated using the straight-line method over the estimated useful lives of 40 years for buildings and improvements, three to 10 years for furniture, equipment and certain leasehold improvements, and three to four years for automobiles. Computer software and hardware are amortized over three years. Gains and losses on dispositions are reflected currently. Maintenance and repairs are charged to operating expense, and improvements are capitalized and amortized over the remaining useful life of the asset.

F. Other Assets and Other Liabilities:

Direct expenses incurred in issuing debt are deferred and amortized using the straight-line method (which is not materially different from the effective interest method) over the term of related indebtedness.

In connection with past foreclosure and sale proceedings, the Bank retained certain mineral interests in land from which it received revenues from lease bonuses, rentals and royalties. These intangible assets were recorded at nominal or no value in the balance sheet. Income received from mineral and royalty holdings, net of related property taxes, in 2003 and 2002 was $4,994 and $3,775, respectively, and is included in miscellaneous income in the statement of income. These mineral interests were sold in November 2003 for proceeds of $30.5 million, which is included in "gains on sale of mineral rights." Of this gain, $29.6 million was paid out as patronage to the District Associations in 2003.

The Bank 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 not insured, and interest is generally paid by the Bank on such balances. There were no significant balances of ACPs at December 31, 2004, 2003 and 2002.

Derivative financial instruments are included on the balance sheet at fair value, as either other assets or other liabilities.

G. Employee Benefit Plans:

The employees of the Bank participate in one of two districtwide retirement plans and are eligible to participate in the Thrift Plus Plan of the District. Additionally, certain qualified individuals in the Bank may participate in a separate, supplemental pension plan. Within the Thrift Plus Plan, a certain percentage of employee contributions is matched by the Bank and Associations. Thrift Plus Plan costs are expensed as incurred.

The structure of the District's defined benefit plan (DB plan) is characterized as multi-employer, since neither the assets, liabilities nor cost of the plan is segregated or separately accounted for by participating employers (Bank and Associations). No portion of any surplus assets is available to any participating employer, nor is any participating employer required to pay for plan liabilities upon withdrawal from the plan. As a result, participating employers of the plan only recognize as cost the required contributions for the period and a liability for any unpaid contributions required for the period of their financial statements. Plan obligations, assets and the components of annual benefit expenses are recorded and reported upon combination only. The Bank records current contributions to the DB Plan as an expense in the current year.

The Bank provides certain health care and life insurance benefits to eligible retired employees. No Bank employees hired on or after January 1, 2004, will be eligible for these health care and life insurance benefits upon retirement.

H. Income Taxes:

The Bank is exempt from federal and certain other income taxes as provided in the Farm Credit Act.

I. Derivative Instruments and Hedging Activity:

The Bank is party to derivative financial instruments, consisting of interest rate swaps, which are principally used to manage interest rate risk on assets, liabilities and anticipated transactions. Derivatives are recorded on the balance sheet as assets and liabilities, measured at fair value.

In accordance with SFAS No. 133, for fair-value hedge transactions which hedge changes in the fair value of assets, liabilities or firm commitments, changes in the fair value of the derivative will generally be offset by changes in the hedged item's fair value. For cash flow hedges, which hedge the exposure to variability in expected future cash flows, changes in the fair value of the derivative will generally be offset by an entry to accumulated other comprehensive income in shareholders' equity. The Bank formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives designated as fair value hedges to specific liabilities on the balance sheet. The Bank uses interest rate swaps whose critical terms match the corresponding hedged item, thereby qualifying for short-cut treatment under the provisions of SFAS No. 133, and are presumed to be highly effective in offsetting changes in the fair value. The Bank would discontinue hedge accounting prospectively if it was determined that a hedge has not been or is not expected to be effective as a hedge. In the event that hedge accounting were discontinued and the derivative remained outstanding, the Bank would carry the derivative at its fair value on the balance sheet, recognizing changes in fair value in current period earnings.

J. Recent Accounting Developments:

The Emerging Issues Task Force (EITF) of the Financial Accounting Standards Board (FASB) issued EITF No. 03-01, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," in 2003 and modified it in 2004 to effectively codify the provisions of SEC Staff Accounting Bulletin No. 59 and require additional disclosures. The disclosure requirements are effective for annual reporting periods ending after June 15, 2004. In September 2004, the FASB delayed the expense recognition provisions of EITF No. 03-01 pending further guidance: however, the disclosure requirements remain effective and have been adopted. The FASB has proposed that immaterial impairments not be recognized. Larger impairments would need to be closely analyzed to determine if the Bank has both the ability and the intent to hold the investment securities until they recover their value.

Note 3 — Investment Securities

A summary of the amortized cost and estimated fair value of investment securities at December 31, 2004, 2003 and 2002, follows:

	December 31, 2004				
	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Weighted Average Yield**
Commercial paper and other	**$ 170,744**	**$ 7**	**$ (6)**	**$ 170,745**	**2.33%**
Collateralized mortgage obligations	**1,592,344**	**1,019**	**(9,928)**	**1,583,435**	**3.58**
Asset-backed securities	**33,485**	**41**	**—**	**33,526**	**2.69**
Total	**$ 1,796,573**	**$ 1,067**	**$ (9,934)**	**$ 1,787,706**	**3.42%**

	December 31, 2003				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Commercial paper and other	$ 290,331	$ 56	$ (6)	$ 290,381	1.16%
Collateralized mortgage obligations	1,196,072	2,586	(7,225)	1,191,433	3.17
Asset-backed securities	36,148	144	(4)	36,288	1.36
Total	$ 1,522,551	$ 2,786	$ (7,235)	$ 1,518,102	2.72%

	December 31, 2002				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Commercial paper and other	$ 407,839	$ —	$ (49)	$ 407,790	1.63%
Collateralized mortgage obligations	307,459	1,233	—	308,692	3.20
Asset-backed securities	68,575	14	—	68,589	1.68
Total	$ 783,873	$ 1,247	$ (49)	$ 785,071	2.25%

A summary of expected maturity, amortized cost, estimated fair value and weighted average yield of investment securities at December 31, 2004, follows:

	Amortized Cost	Fair Value	Weighted Average Yield
Due in one year or less	$ 170,744	$ 170,745	2.33%
Due after one year through five years	—	—	—
Due after five years through ten years	144,417	144,126	3.88
Due after ten years	1,481,412	1,472,835	3.54
Total securities	$ 1,796,573	$ 1,787,706	3.42%

Collateralized mortgage obligations (CMOs) have stated contractual maturities in excess of 15 years. However, the security structure of the CMOs is designed to produce a relatively short-term life. At December 31, 2004, the CMO portfolio had a weighted average remaining life of approximately two years.

Proceeds and related gains and losses on sales of investment securities follow:

	Year Ended December 31,		
	2004	2003	2002
Proceeds on sales	**$ 85,565**	$ —	$ 22,109
Realized gains (losses)	**420**	—	(2,919)

The net realized gain (loss) is included in the statements of income as part of total noninterest income.

The following table shows the fair value and gross unrealized losses for investments in a loss position aggregated by investment category, and the length of time the securities have been in a continuous unrealized position at December 31, 2004. The continuous loss position is based on the date the impairment occurred. The unrealized losses on these investments resulted from interest rate volatility and are not credit related. The Bank has both the ability and the intent to recover substantially all of our cost in these investments.

(in thousands)	**Less Than 12 Months**		**Greater Than 12 Months**	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Mortgage-backed securities	$ 1,137,837	$ 8,387	$ 93,551	$ 1,541
Commercial paper	90,738	6	—	—
Total	$ 1,228,575	$ 8,393	$ 93,551	$ 1,541

Note 4 — Loans and Allowance for Loan Losses

Loans comprised the following categories at December 31:

	2004	2003	2002
Direct notes receivable from District Associations	**$ 6,036,906**	$ 5,341,875	$ 5,411,885
Participations purchased	**752,549**	395,419	296,989
Other loans	**128,781**	97,635	118,077
Total loans	**$ 6,918,236**	$ 5,834,929	$ 5,826,951

A substantial portion of the Bank's loan portfolio consists of direct notes receivable from District Associations. As described in Note 1, "Organization and Operations," these notes are used by the Associations to fund their loan portfolios and therefore the Bank's implicit concentration of credit risk in various agricultural commodities approximates that of the District as a whole. Loan concentrations are considered to exist when there are amounts loaned to borrowers engaged in similar activities, which could cause them to be similarly impacted by economic or other conditions. The percentages below represent the District portfolio's diversification of credit risk as it relates to recorded loan principal. A substantial portion of the Associations' lending activities is collateralized and the Associations' exposure to credit loss associated with lending activities is reduced accordingly. An estimate of the Bank's credit risk exposure is considered in the Bank's allowance for loan losses.

The District's concentration of credit risk in various agricultural commodities is shown in the following table at December 31:

Commodity	**2004**	2003	2002
Livestock	**41%**	41%	42%
Crops	**16**	17	19
Timber	**11**	12	11
Cotton	**8**	10	10
Poultry	**5**	6	5
Dairy	**2**	2	2
Rural home	**1**	2	2
Other	**16**	10	9
Total	**100%**	100%	100%

Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms of the loans. Interest income recognized and cash payments received on nonaccrual impaired loans are applied in a similar manner as for nonaccrual loans, as described in Note 2,"Summary of Significant Accounting Policies."

The following table presents information concerning nonaccrual loans, accruing restructured loans and accruing loans 90 days or more past due, collectively referred to as "impaired loans." Restructured loans are loans whose terms have been modified and on which concessions have been granted because of borrower financial difficulties. The Bank's impaired loans consisted of participations purchased and other loans; no direct notes to District Associations were impaired at December 31, 2004, 2003 and 2002.

	December 31,		
	2004	2003	2002
Nonaccrual loans			
Current as to principal and interest	**$ 1,726**	$ 9,921	$ 2,555
Past due	**599**	401	2,234
Total nonaccrual loans	**2,325**	10,322	4,789
Impaired accrual loans			
Restructured accrual loans	**618**	633	937
Accrual loans 90 days or more past due	**206**	—	—
Total impaired accrual loans	**824**	633	937
Total impaired loans	**$ 3,149**	$ 10,955	$ 5,726
Average impaired loans	**$ 8,929**	$ 6,865	$ 10,293

Interest income is recognized and cash payments are applied on nonaccrual impaired loans as described in Note 2. The following table presents interest income recognized on impaired loans for the years ended December 31:

	2004	2003	2002
Interest income recognized on nonaccrual loans	**$ 1,325**	$ 378	$ 2,914
Interest income on impaired accrual loans	**114**	81	136
Interest income recognized on impaired loans	**$ 1,439**	$ 459	$ 3,050

The following table presents information concerning impaired loans as of December 31:

	2004	2003	2002
With related specific allowance	$ 1,286	$ 638	$ 2,247
With no related specific allowance	1,863	10,317	3,479
Total impaired loans	$ 3,149	$ 10,955	$ 5,726
Allowance on impaired loans	$ 239	$ 291	$ 599

Interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans were as follows at December 31:

	2004	2003
Interest income which would have been recognized under the original loan terms	$ 1,994	$ 1,004
Less: interest income recognized	1,439	459
Foregone interest income	$ 555	$ 545

Refinement of the Allowance for Loan Losses Methodology

During 2004, the Bank conducted studies to further refine its allowance for loan losses methodology, taking into account recently issued guidance by the FCA, the System's regulator, as well as the Securities and Exchange Commission (SEC) and Federal Financial Institutions Examination Council guidelines.

The Bank's allowance for loan losses methodology was adjusted and revised in the late 1980s to take into account credit losses in that period. Given the long cyclical nature of the agricultural economy, loss factors utilized to determine the allowance for loan losses subsequent to 1989 continued to reflect, to some extent, the loss history of the mid-to-late 1980s, which resulted in conservative estimates of the allowance for loan losses. The Bank allowance for loan losses methodology utilized throughout the period was in accordance with generally accepted accounting principles and was consistently applied.

While conservative in estimating the allowance for loan losses, the methodology used resulted in annual provisions for loan losses over the periods that reflected changes in credit quality and loss experience. Accordingly, the reserves provided in the mid-to-late 1980s have, in effect, remained part of the allowance for loan losses. The Bank's allowance for loan losses methodology has consistently adhered to proper accounting policies, under the regulatory supervision of the FCA in its role as a "safety and soundness" regulator. It was the FCA's view that the allowance for loan losses should include, among others, an assessment of probable losses, historical loss experience and economic conditions.

In April 2004, the FCA issued an "Informational Memorandum" to System institutions regarding the criteria and methodologies that would be used in evaluating the adequacy of a System institution's allowance for loan losses. The FCA endorsed the direction provided by other bank regulators and the SEC and indicated that the conceptual framework addressed in this guidance would be included as part of their examination process.

During the fourth quarter of 2004, the Bank completed its study and refined its methodology to be in compliance with the guidance discussed in the previous paragraph. The refinement in methodology resulted in a calculated allowance for loan losses that was significantly less than the previously recorded balance due to revised loss factors that are more indicative of actual loss experience in recent years and current borrower analysis.

While the $7.9 million reversal had a significant impact on 2004 results of operations and the previously recorded allowance for loan losses, the refinement in methodology is not expected to have a significant impact on comparative results of operations in future periods. Additionally, the refinement in methodology did not have a significant impact on the level of the risk-bearing capacity of the Bank, generally referred to as "risk funds" (capital plus the allowance for loan losses), which totaled $502 million at December 31, 2004, or 7.25 percent of Bank loans, as compared with $487 million at December 31, 2003, or 8.35 percent of Bank loans.

A summary of changes in the allowance for loan losses follows:

	December 31, 2004	2003	2002
Balance at beginning of year	$ 9,834	$ 9,695	$ 13,643
Provision (negative provision) for loan losses	—	340	(2,902)
Nonrecurring negative provision for loan losses	(7,878)	—	—
Loans charged off	(5,725)	(201)	(1,046)
Recoveries	4,008	—	—
Balance at end of year	$ 239	$ 9,834	$ 9,695

To mitigate risk of loan losses, District Associations have entered into long-term standby commitments to purchase agreements with the Federal Agricultural Mortgage Corporation ("Farmer Mac") through an arrangement with the Bank. The agreements, which are effectively credit guarantees that will remain in place until the loans are paid in full, give the Associations the right to sell the loans identified in the agreements to the Bank, who can, in turn, sell them to Farmer Mac in the event of default, subject to certain conditions. The balance of loans under long-term standby commitments to purchase was $95.5 million at December 31, 2004. Fees paid to Farmer Mac for such commitments are paid by the Associations.

In November 2003 the Bank sold, at par, $300 million of participations in five of its direct notes with District Associations to another System bank. The purpose of the sale was to diversify the credit exposure of the Bank by allowing the acquisition of mortgage-type investment securities and interests in other capital market loan participations.

Note 5 — Premises and Equipment

Premises and equipment comprised the following at:

	December 31, 2004	2003	2002
Buildings and leasehold improvements	$ 929	$ 22	$ —
Furniture and equipment	9,170	10,098	10,665
	10,099	10,120	10,665
Accumulated depreciation	(7,683)	(9,163)	(9,736)
Total	$ 2,416	$ 957	$ 929

In November 2002, the Bank sold its headquarters building and related land, with a net book value of $16,145, for net proceeds of $16,321.

On September 30, 2003, the Bank entered into a lease for approximately 102,500 square feet of office space to house its headquarters facility. The lease was effective September 30, 2003, and its term is from September 1, 2003, to August 31, 2013. Under the terms of the lease, the Bank was obligated to pay base rental or its share of basic costs during the first 12 months of the lease. Thereafter, the Bank will pay annual base rental ranging from $11 per square foot in the second year to $19 per square foot in the tenth year. The Bank moved to the new facilities during the second quarter of 2004.

Following is a schedule of the minimum lease payments on the lease:

	Minimum Lease Payments
2005	$ 1,161
2006	1,264
2007	1,366
2008	1,503
2009	1,674
Subsequent years	6,899
Total minimum lease payments	$ 13,867

Note 6 — Other Assets and Other Liabilities

Other assets comprised the following at December 31:

	2004	2003	2002
Accounts receivable	**$ 8,137**	$ 2,809	$ 3,182
Unamortized debt issue costs	**3,181**	2,743	1,874
Fair value of derivatives	**2,469**	8,711	10,988
Land investment	**—**	793	793
Other, net	**2,153**	3,626	2,393
Total	**$ 15,940**	$ 18,682	$ 19,230

Other liabilities comprised the following at December 31:

	2004	2003	2002
Fair value of derivatives	**$ 10,601**	$ 790	$ —
Obligation for non-pension postretirement benefits	**9,634**	2,034	2,230
Accounts payable	**2,784**	2,024	500
Notes payable	**1,903**	3,112	2,432
Supplemental pension	**1,766**	2,296	1,649
Mortgage life additional reserve	**1,757**	1,912	1,887
FCSIC premium payable	**315**	510	170
Other, net	**1,631**	799	950
Total	**$ 30,391**	$ 13,477	$ 9,818

Note 7 — Bonds and Notes

The System, unlike commercial banks and other depository institutions, obtains funds for its lending operations primarily from the sale of Systemwide debt securities issued by the banks through the Funding Corporation. Certain conditions must be met before the Bank can participate in the issuance of Systemwide debt securities. The Bank is required by the Farm Credit Act and FCA regulations to maintain specified eligible assets at least equal in value to the total amount of debt obligations outstanding for which it is primarily liable as a condition for participation in the issuance of Systemwide debt. This requirement does not provide holders of Systemwide debt securities, or bank and other bonds, with a security interest in any assets of the banks. In general, each bank determines its participation in each issue of Systemwide debt securities based on its funding and operating requirements, subject to the availability of eligible assets as described above and subject to Funding Corporation determinations and FCA approval. At December 31, 2004, the Bank had such specified eligible assets totaling $8.8 billion and obligations and accrued interest payable totaling $8.3 billion, resulting in excess eligible assets of $501.0 million.

In 1994, the System banks and the Funding Corporation entered into the Market Access Agreement (MAA), which established criteria and procedures for the banks to provide certain information to the Funding Corporation and, under certain circumstances, for restricting or prohibiting an individual bank's participation in Systemwide debt issuances, thereby reducing other System banks' exposure to statutory joint and several liability. At December 31, 2004, the Bank was, and currently remains, in compliance with the conditions and requirements of the MAA.

Each issuance of Systemwide debt securities ranks equally, in accordance with the FCA regulations, with other unsecured Systemwide debt securities. Systemwide debt securities are not issued under an indenture and no trustee is provided with respect to these securities. Systemwide debt securities are not subject to acceleration prior to maturity upon the occurrence of any default or similar event.

The Bank's participation in Systemwide debt securities at December 31, 2004, follows *(dollars in millions)*:

	Systemwide							
	Bonds		Medium-Term Notes		Discount Notes		Total	
Year of Maturity	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate
2005	$ 3,157.1	2.45%	$ 100.8	5.70%	$ 732.9	1.96%	$ 3,990.8	2.44%
2006	2,564.8	2.45	72.3	5.91	—	—	2,637.1	2.54
2007	669.6	3.32	—	—	—	—	669.6	3.32
2008	344.7	4.17	20.0	5.57	—	—	364.7	4.25
2009	230.0	4.32	—	—	—	—	230.0	4.32
Subsequent years	340.3	5.58	—	—	—	—	340.3	5.58
Total	$ 7,306.5	2.81%	$ 193.1	5.77%	$ 732.9	1.96%	$ 8,232.5	2.80%

In the preceding table, the weighted average effective rate reflects the effects of interest rate swaps used to manage the interest rate risk on the bonds and notes issued by the Bank. The Bank's interest rate swap strategy is discussed more fully in Note 2, "Summary of Significant Accounting Policies" and Note 15, "Derivative Instruments and Hedging Activity."

Systemwide bonds, medium-term notes, master notes, discount notes (Systemwide debt securities) and bank bonds are the joint and several obligations of all System banks. Discount notes are issued with maturities ranging from one to 365 days. The average maturity of discount notes at December 31, 2004, was 20 days.

The Bank's Systemwide debt includes callable debt, consisting of the following at December 31, 2004 *(dollars in thousands)*:

Year of Maturity	Amount	Range of First Call Dates
2005	$ 80,000	1/1/2005
2006	435,000	1/1/2005–6/15/2005
2007	485,000	1/1/2005–11/12/2005
2008	210,000	1/1/2005–10/29/2005
2009	175,000	1/1/2005–3/16/2005
Subsequent years	135,000	1/1/2005–3/21/2005
Total	$ 1,520,000	1/1/2005–11/12/2005

Callable debt may be called on the first call date and, generally, everyday thereafter with seven days' notice.

As described in Note 1, "Organization and Operations," the Insurance Fund is available to ensure the timely payment of principal and interest on bank bonds and Systemwide debt securities (insured debt) of insured System banks to the extent net assets are available in the Insurance Fund. All other liabilities in the combined financial statements are uninsured.

The Bank had no outstanding commercial bank lines of credit at December 31, 2004.

Note 8 — Shareholders' Equity

Descriptions of the Bank's equities, capitalization requirements and regulatory capitalization requirements and restrictions are provided below.

A. Description of Bank Equities:

On November 7, 2003, the Bank issued 100,000 shares of $1,000 Cumulative Perpetual Preferred Stock for net proceeds of $98,644, after expenses of $1,356 associated with the offering. The dividend rate is 7.561 percent, payable semi-annually to December 15, 2013, after which dividends are payable quarterly at a rate equal to 3-month London Interbank Offered Rate (LIBOR) plus 445.75 basis points. For regulatory purposes, the preferred stock is treated as equity. It is not mandatorily redeemable. Dividends on preferred stock are recorded as declared. The preferred stock ranks, as to dividends and other distributions (including patronage) upon liquidation, dissolution or winding up, prior to all other classes and series of equity securities of the Bank. On June 15 and December 15, 2004, preferred stock dividends totaling $7,561 were paid. At December 31, 2004, accumulated dividends on the preferred stock totaled $357.

According to the Bank's bylaws, the minimum and maximum stock investments required of the ACAs and FLCAs are 2 percent (or one thousand dollars, whichever is greater) and 5 percent, respectively, of each Association's average borrowings from the Bank. The investments in the Bank are required to be in the form of Class A voting common stock (with a par value of $5 per share) and allocated retained earnings. The current investment required of the Associations is 2 percent of their average borrowings from the Bank. There were 23,500 shares, 21,856 shares and 21,878 shares of Class A voting common stock issued and outstanding at December 31, 2004, 2003 and 2002, respectively.

The Bank requires OFIs to make cash purchases of Class A nonvoting common stock (with a par value of $5 per share) in the Bank based on a minimum and maximum of 2 percent (or one thousand dollars, whichever is greater) and 5 percent, respectively, of the OFIs' average borrowings from the Bank. The Bank has a first lien on these equities for the repayment of any indebtedness to the Bank. There were 164 shares, 102 shares and 102 shares of Class A nonvoting common stock issued and outstanding at December 31, 2004, 2003 and 2002, respectively.

Allocated retained earnings of $9,980 at December 31, 2004, consisted of $9,966 of patronage refunds allocated to certain PCAs prior to January 1, 1993, and $14 allocated for the payment of patronage on a loan participated with another System bank. The $9,966 in patronage refunds is used to satisfy all or part of the 2 percent Bank stock requirement by certain of the PCAs, all of which are now subsidiaries of ACA parent companies. Bank management's intent is to permanently invest these undistributed earnings in the Bank and to indefinitely postpone their conversion to cash.

Allocated retained earnings of $14,237 at December 31, 2003, consisted of $2,573 allocated to certain participating Associations from earnings generated by the Bank's participation loans and $11,664 of patronage refunds allocated to certain PCAs as previously described.

Allocated retained earnings of $11,711 at December 31, 2002, consisted of $928 allocated to certain participating Associations from earnings generated by the Bank's participation loans and $10,783 of patronage refunds allocated to certain PCAs, as previously described.

At December 31, investment in the Bank included the following investment in capital stock and allocated retained earnings:

	2004	2003	2002
Class A voting common stock - Associations	**$ 117,501**	$ 109,278	$ 109,388
Class A nonvoting common stock – Other Financing Institutions	**822**	509	508
Total common stock	**118,323**	109,787	109,896
Preferred stock	**98,644**	98,644	—
Allocated retained earnings			
Associations	**9,966**	14,237	11,711
Other entities	**14**	—	—
Total allocated retained earnings	**9,980**	14,237	11,711
Total capital stock and allocated retained earnings	**$ 226,947**	$ 222,668	$ 121,607

Patronage may be paid to the holders of Class A voting common stock and allocated retained earnings of the Bank, as the board of directors may determine by resolution, subject to the capitalization requirements defined by the FCA. During 2004, $16,775 in cash patronages were paid to District Associations, OFIs and other entities, compared to $49,144 in 2003 and $3,615 in 2002.

B. Regulatory Capitalization Requirements and Restrictions:

FCA's capital adequacy regulations require the Bank to achieve and maintain, at minimum, permanent capital of 7 percent of risk-adjusted assets and off-balance-sheet commitments. The Farm Credit Act has defined permanent capital to include all capital except stock and other equities that may be retired upon the repayment of the holder's loan or otherwise at the option of the holder, or is otherwise not at risk. Risk-adjusted assets have been defined by regulations as the balance sheet assets and off-balance-sheet commitments adjusted by various percentages ranging from 0 to 100 percent, depending on the level of risk inherent in the various types of assets. The Bank is prohibited from reducing permanent capital by retiring stock or by making certain other distributions to stockholders unless the minimum permanent capital standard is met.

The Bank is required by FCA regulations to achieve and maintain net collateral of at least 103 percent of total liabilities. Net collateral consists of loans, real or personal property acquired in connection with loans, marketable investments, cash and cash equivalents.

The following table reflects the Bank's capital ratios at December 31:

	2004	2003	2002	Regulatory Minimum
Permanent capital ratio	**19.82%**	23.71%	18.06%	7.00%
Total surplus ratio	**16.55**	19.15	14.01	7.00
Core surplus ratio	**11.51**	14.44	12.56	3.50
Collateral ratio	**105.69**	106.62	105.32	103.00

Note 9 — Employee Benefit Plans

Employees of the Bank participate in either the District's defined benefit retirement plan (DB plan) or a District defined contribution plan (DC plan) and are eligible to participate in the District's Thrift Plus Plan.

The structure of the District's DB plan is characterized as multi-employer, since neither the assets, liabilities nor cost of any plan is segregated or separately accounted for by participating employers (Bank and Associations). No portion of any surplus assets is available to any participating employer, nor is any participating employer required to pay for plan liabilities upon withdrawal from the plan. As a result, participating employers of the plan only recognize as cost the required contributions for the period and a liability for any unpaid contributions required for the period of their financial statements. Plan obligations, assets and the components of annual benefit expenses are recorded and reported upon combination only. The Bank records current contributions to the DB plan as an expense in the current year.

The DB plan is noncontributory and benefits are based on salary and years of service. The "projected unit credit" actuarial method is used for both financial reporting and funding purposes. District employers have the option of providing enhanced retirement benefits, under certain conditions, within the DB plan in 1998 and beyond, to facilitate reorganization and/or restructuring. Additionally, certain qualified individuals in the Bank may participate in a separate, defined benefit supplemental pension plan. The Bank accrues the cost and liability of the supplemental pension plan as incurred, and not as contributions are required. Actuarial information regarding the DB and supplemental pension plan accumulated benefit obligations and plan assets are calculated for the District as a whole and is presented in the District's Annual Report to Stockholders. The actuarial present value of vested and nonvested accumulated benefit obligations exceeded the net assets of both plans as a whole as of December 31, 2004.

Participants in the DC plan generally include employees who elected to transfer from the DB plan prior to January 1, 1996, and all employees hired on or after January 1, 1996. DC plan participants direct the placement of their employers' contributions (4.0 percent of eligible compensation during 2004) made on their behalf into various investment alternatives.

The District also participates in a districtwide Thrift Plus Plan, which offers a 401(k) pre-tax and after-tax compensation deferral feature (401(k) plan). During 2002, the 401(k) plan required the Bank and Associations to match 50 percent of employee contributions up to a maximum employee contribution of 6 percent of eligible compensation. In 2003, the employers made contribution enhancements to the Thrift Plus Plan employer contributions. Beginning January 1, 2003, employers matched 100 percent of employee contributions for the first 3 percent of eligible compensation and then matched 50 percent of employee contributions on the next 2 percent of eligible compensation, for a maximum employer contribution of 4 percent of eligible compensation.

The following table presents the Bank's retirement expenses for the years ended:

	2004	2003	2002
Pension	**$ 2,196**	$ 3,018	$ 1,052
Thrift plan	**411**	383	277
Total	**$ 2,607**	$ 3,401	$ 1,329

The Bank provides certain health care and life insurance benefits to eligible retired employees. No Bank employees hired on or after January 1, 2004, will be eligible for these health care and life insurance benefits upon retirement.

Until 2004, the Bank participated in the District's multi-employer health and welfare plan, through which it provided substantially all employees with postretirement health care and life insurance benefits. Neither the assets, liabilities nor cost of the multi-employer plan were segregated or separately accounted for by participating entities. Costs were recognized only to the extent of contributions to the plan. In December 2004, the Bank adopted a new single-employer plan to provide the same benefits to its retirees, employees and directors. Under the new plan, the Bank will no longer be jointly and severally liable with any other employers. As such, the Bank has recorded a liability at December 31, 2004, of $9,634, which reflects the unfunded accumulated benefit obligation for its retirees and employees.

The following tables reflect the benefit obligation, cost and actuarial assumptions for the Bank's other postretirement benefits:

Liabilities and Assets

Accumulated postretirement benefit obligation, December 31, 2004	$ (9,869)
Fair value of plan assets	287
Funded status of plan	(9,582)
Unrecognized net transition obligation	—
Unrecognized prior service cost	(952)
Unrecognized net loss (gain)	813
Fourth quarter contributions	87
Accrued postretirement benefit cost	$ (9,634)

Weighted-Average Assumptions Used to Determine Obligations at Year-End

Measurement date	September 30, 2004
Discount rate	6.00%
Health care cost trend rate assumed for next year (pre-/post-65)	11.00% / 11.50%
Ultimate health care cost trend rate (pre-/post-65)	5.00% / 5.50%
Year that the rate reaches the ultimate trend rate	2012

At December 31, 2004, the Bank had an accrued benefit liability of $9,634 on its balance sheet. The total net postretirement benefit cost for 2004 was $7,755, and the Bank's employer contributions for 2004 totaled $432.

The September 30, 2004, valuation reflects the impact of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003. For Medicare-eligible participants receiving actuarially equivalent drug benefits, the plan's management has estimated that the expected per capita claims cost will be reduced by 13 percent beginning in 2006 due to a government reimbursement of 28 percent of prescription drug benefits. Actuarial equivalence with the government benefit was determined based on the employer-subsidized benefits for each individual under the current retiree cost sharing provisions.

Note 10 — Intra-System Financial Assistance

The FAC was established in 1988 primarily to provide capital to institutions of the System experiencing financial difficulty. Such assistance was funded through the FAC's issuance of $1.26 billion of 15-year U.S. Treasury–guaranteed debt. The interest rates on these issuances ranged from 8.80 percent to 9.45 percent. The proceeds from the debt offerings were used to fund existing intra-System financial assistance payables ($417 million), to purchase preferred stock from certain troubled System banks ($808 million), and for other purposes ($36 million).

Pursuant to the Farm Credit Act, the U.S. Treasury paid the interest on $844 million of the FAC bonds for the first five years of the respective terms of such bonds. The payment of interest on this debt is allocated between the U.S. Treasury and System banks during the second five years. As the result of growth of the System's surplus, the allocation provisions of the Farm Credit Act required that the banks pay 100 percent of the interest beginning in 1999. The Farm Credit Act and supplemental agreements dictate how the banks will repay the principal and fund the interest of each type of issuance. With the exception of the assistance provided through the purchase of preferred stock, repayment of the FAC debt obligations will be allocated to all System banks, and annual expense accruals and funding assessments are generally allocated based on each bank's proportion of System loan volume over various time periods.

Financial assistance was provided by the FAC to five System banks through its purchase of preferred stock of those institutions. Through 1994, four System banks redeemed their preferred stock in the amount of $419 million through the transfer of assets to the FAC. The FLB of Jackson, whose charter was canceled in January 1995, received $374 million of financial assistance for which the related preferred stock has not been redeemed.

All interest advanced by the U.S. Treasury must be repaid by System banks in 2005. System banks record their share of the liability based upon each bank's proportionate share of average accruing retail loan volume. To fund the repayment obligation, annual annuity-type payments are made by each bank to the FAC in an amount designed to accumulate, in total, including earnings thereon, the total amount of each bank's ultimate obligation.

The FAC assumed certain payables previously accrued by the Bank under the System's Capital Preservation Agreements and funded payment of such accruals by the issuance of 15-year U.S. Treasury–guaranteed debt. Under the Farm Credit Act, the System banks were required to fund the bonds upon maturity. Although GAAP required recognition in the financial statements of the Bank's liability to the FAC, the Farm Credit Act states that for all financial reporting purposes, this obligation should not be considered a liability of any System bank until the maturity of such debt. The obligation was paid in July 2003. The Bank's unrecorded liability and related unrecorded reduction in retained earnings at December 31, 2002, was estimated to be $1.2 million. There was a statutorily mandated repayment plan, which effectively spread the financial assistance payments and expenses over a number of years and, accordingly, gradually reduced the effect of the unrecorded liability.

The Bank's financial assistance expense totaled $0.4 million, $2.8 million and $3.2 million for the years ended December 31, 2004, 2003 and 2002, respectively. The liability for financial assistance totaled $280 and $4,334 at December 31, 2003 and 2002, respectively. At December 31, 2004, the Bank had a receivable for $459, which is included in other assets.

Note 11 — Related Party Transactions

As discussed in Note 1, "Organization and Operations," the Bank lends funds to the District Associations and OFIs to fund their loan portfolios. Interest income recognized on direct notes receivable from District Associations and OFIs was $147,728, $142,909 and $168,437 for 2004, 2003 and 2002, respectively. Further disclosure regarding these related party transactions is found in Note 4, "Loans and Allowance for Loan Losses," and Note 8, "Shareholders' Equity."

In addition to providing loan funds to District Associations, the Bank also provides banking and support services to them, such as accounting, information systems, marketing and other services. Income derived by the Bank from these activities was $8,744, $10,624 and $11,065 for 2004, 2003 and 2002, respectively, and was included in the Bank's noninterest income.

Note 12 — Commitments and Contingencies

In the normal course of business, the Bank has various outstanding commitments and contingent liabilities as discussed elsewhere in these notes.

The Bank is primarily liable for its portion of Systemwide debt obligations. Additionally, the Bank is jointly and severally liable for the consolidated Systemwide bonds and notes of other System banks. The total Bank and consolidated Systemwide debt obligations of the System at December 31, 2004, were approximately $99.1 billion.

Other actions are pending against the Bank in which claims for monetary damages are asserted. Upon the basis of current information, management and legal counsel are of the opinion that the ultimate liability, if any resulting therefrom, will not be material in relation to the financial position or results of operations of the Bank.

Note 13 — Financial Instruments With Off-Balance-Sheet Risk

The Bank may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of its borrowers and to manage its exposure to interest rate risk. In the normal course of business, various commitments are made to customers, including commitments to extend credit and standby letters of credit, which represent credit-related financial instruments with off-balance-sheet risk.

At any time, the Bank has outstanding a significant number of commitments to extend credit. The Bank also provides standby letters of credit to guarantee the performance of customers to third parties. Commitments to extend credit are agreements to lend to a borrower as long as there is not a violation of any condition established in the contract. Commitments and letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. Credit-related financial instruments have off-balance-sheet credit risk, because only origination fees (if any) are recognized in the balance sheet (as other liabilities) for these instruments until the commitments are fulfilled or expire. Since many of the commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. The Bank's commitments to extend credit totaled $706.5 million, $107.2 million and $45.4 million at December 31, 2004, 2003 and 2002, respectively.

The credit risk involved in issuing commitments and letters of credit is essentially the same as that involved in extending loans to customers, and the same credit policies are applied by management. In the event of funding, the credit risk amounts are equal to the contract amounts, assuming that counterparties fail completely to meet their obligations and the collateral or other security is of no value. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the counterparty.

Note 14 — Disclosure About the Fair Value of Financial Instruments

The following table presents the carrying amounts and estimated fair values of the Bank's financial instruments at December 31, 2004, 2003 and 2002. The fair value of a financial instrument is generally defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Quoted market prices are generally not available for System financial instruments. Accordingly, fair values are based on judgments regarding anticipated cash flows, future expected loss experience, discount rates, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates involve uncertainties and matters of judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The estimated fair values of the Bank's financial instruments follow:

	December 31, 2004		December 31, 2003		December 31, 2002	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets						
Cash, federal funds sold, securities purchased under resale agreements and investment securities	**$ 1,838,820**	**$ 1,838,820**	$ 1,546,367	$ 1,546,367	$ 846,930	$ 846,930
Loans	**6,918,236**	**6,864,564**	5,834,929	5,835,743	5,826,951	5,866,556
Allowance for loan losses	**(239)**	**—**	(9,834)	—	(9,695)	—
Loans, net	**6,917,997**	**6,864,564**	5,825,095	5,835,743	5,817,256	5,866,556
Derivative assets	**2,469**	**2,469**	8,711	8,711	10,988	10,988
Financial liabilities						
Bonds and notes	**8,241,974**	**8,274,094**	6,878,817	6,937,980	6,273,579	6,385,910
Fair value adjustment of derivatives	**(9,441)**	**(9,441)**	7,921	7,921	10,988	10,988
Total bonds and notes	**8,232,533**	**8,264,653**	6,886,738	6,945,901	6,284,567	6,396,898
Financial assistance related liabilities*	**—**	**—**	280	748	4,334	5,472
Derivative liabilities	**10,601**	**10,601**	790	790	—	—

* These amounts exclude the assumption of Third Quarter 1986 Capital Preservation Agreement obligations with carrying amounts of $1.2 million and $1.6 million and estimated fair values of $2.7 million and $3.9 million at December 31, 2002 and 2001, respectively. The obligation was paid in July 2003.

A description of the methods and assumptions used to estimate the fair value of each class of the District's financial instruments for which it is practicable to estimate that value follows:

A. **Cash:**

The carrying value is a reasonable estimate of fair value.

B. **Federal Funds Sold, Securities Purchased Under Resale Agreements, and Investment Securities:**

Fair value is based upon currently quoted market prices.

C. **Loans:**

Because no active market exists for the District's loans, fair value is estimated by discounting the expected future cash flows using the District's current interest rates at which similar loans would be made to borrowers with similar credit risk. As the discount rates are based on the District's loan rates as well as on management estimates, management has no basis to determine whether the fair values presented would be indicative of the value negotiated in an actual sale.

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

Fair value of loans in a nonaccrual status which are current as to principal and interest is estimated as described above, with appropriately higher discount rates to reflect the uncertainty of continued cash flows. For noncurrent nonaccrual loans, it is assumed that collection will result only from the disposition of the underlying collateral. Fair value of these loans is estimated to equal the aggregate net realizable value of the underlying collateral, discounted at an interest rate that appropriately reflects the uncertainty of the expected future cash flows over the average disposal period.

D. **Bonds and Notes:**

Systemwide bonds and notes are not regularly traded; thus, quoted market prices are not available. Fair value of these instruments is estimated by discounting expected future cash flows based on the quoted market price of similar-maturity Treasury notes, assuming a constant estimated yield spread relationship between Systemwide bonds and notes and comparable Treasury notes.

E. **Obligations to FAC:**

Fair value of these obligations is determined by discounting the cumulative expected future cash outflows of all of the obligations using a discount rate commensurate with bonds having a similar maturity.

F. **Commitments to Extend Credit:**

Fees on commitments to extend credit are not normally assessed; hence, there is no fair value to be assigned to these commitments until they are funded.

Note 15 — Derivative Instruments and Hedging Activity

The Bank maintains an overall interest rate risk-management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest rate volatility. The Bank's goal is to manage interest rate sensitivity by modifying the repricing or maturity characteristics of certain balance sheet liabilities so that the net interest margin is not adversely affected by movements in interest rates. As a result of interest rate fluctuations, hedged fixed-rate liabilities will appreciate or depreciate in market value. The effect of this unrealized appreciation or depreciation is expected to be substantially offset by the Bank's gains or losses on the derivative instruments that are linked to these hedged liabilities. Another result of interest rate fluctuations is that the interest expense of hedged variable-rate liabilities will increase or decrease. The effect of this variability in earnings is expected to be substantially offset by the Bank's gains and losses on the derivative instruments that are linked to these hedged liabilities. The Bank considers its strategic use of derivatives to be a prudent method of managing interest rate sensitivity, as it prevents earnings from being exposed to undue risk posed by changes in interest rates.

The Bank enters into derivatives, particularly interest rate swaps, primarily to lower interest rate risk. Interest rate swaps allow the Bank to raise long-term borrowings at fixed rates and swap them into floating rates that are lower than those available to the Bank if floating-rate borrowings were made directly. Under interest rate swap arrangements, the Bank agrees with other parties to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating-rate index.

The Bank's interest-earning assets (principally loans and investments) tend to be medium-term floating-rate instruments, while the related interest-bearing liabilities tend to be short- or medium-term fixed-rate obligations. Given this asset-liability mismatch, interest rate swaps in which the Bank pays the floating rate and receives the fixed rate (receive fixed swaps) are used to reduce the impact of market fluctuations on the Bank's net interest income.

In addition to interest rate swaps, in 2004 the Bank entered into two cash flow hedges, with a total notional amount of $95 million, as a part of an overall strategy to shorten the repricing characteristics of fixed-rate debt.

By using derivative instruments, the Bank exposes itself to credit and market risk. If a counterparty fails to fulfill its performance obligations under a derivative contract, the Bank's credit risk will equal the fair value gain of the derivative. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes the Bank, thus creating a repayment risk for the Bank. When the fair value of the derivative contract is negative, the Bank owes the counterparty and, therefore, assumes no repayment risk.

To minimize the risk of credit losses, the Bank deals with counterparties that have an investment grade or better credit rating from a major rating agency, and also monitors the credit standing of, and levels of exposure to, individual counterparties. At December 31, 2004, the Bank had credit exposure totaling $1.8 million with two counterparties. The Bank does not anticipate nonperformance by either of these counterparties. The Bank typically enters into master agreements that contain netting provisions. These provisions allow the Bank to require the net settlement of covered contracts with the same counterparty in the event of default by the counterparty on one or more contracts.

The credit exposure represents the exposure to credit loss on derivative instruments, which is estimated by calculating the cost, on a present value basis, to replace all outstanding derivative contracts in a gain position.

The table below presents the credit ratings of counterparties to whom the Bank has credit exposure:

($ in millions)	Remaining Years to Maturity: Less Than 1 Year	1 to 5 Years	Over 5 Years	Total	Maturity Distribution Netting	Exposure	Collateral Held	Exposure Net of Collateral
Standard & Poors Credit Rating								
A-	$ —	$ .68	$ 1.08	$ 1.76	$ —	$ 1.76	$ —	$ 1.76

The Bank's derivative activities are monitored by its Asset-Liability Management Committee (ALCO) as part of the ALCO's oversight of the Bank's asset/liability and treasury functions. The ALCO is responsible for approving hedging strategies that are developed through its analysis of data derived from financial simulation models and other internal and industry sources. The resulting hedging strategies are then incorporated into the Bank's overall interest rate risk-management strategies. The Bank enters into interest rate swaps classified as fair value hedges primarily to convert a portion of its non-prepayable fixed-rate long-term debt to floating-rate debt.

The table below provides information about derivative financial instruments and other financial instruments that are sensitive to changes in interest rates, including debt obligations and interest rate swaps. The debt information below presents the principal cash flows and related weighted average interest rates by expected maturity dates. The derivative information below represents the notional amounts and weighted average interest rates by expected maturity dates.

December 31, 2004 ($ in millions)	Maturities of 2004 Derivative Products and Other Financial Instruments: **2005**	2006	2007	2008	2009	Subsequent Years	Total	Fair Value
Total debt obligations:								
Fixed rate	**$ 2,316**	$ 1,162	$ 670	$ 365	$ 230	$ 340	$ 5,083	$ 5,115
Weighted average interest rate	**1.94%**	2.90%	3.32%	4.24%	4.32%	5.58%	2.86%	
Variable rate	**$ 1,675**	$ 1,475	$ —	$ —	$ —	$ —	$ 3,150	$ 3,150
Weighted average interest rate	**2.28%**	2.27%	—	—	—	—	2.27%	
Total debt obligations	**$ 3,991**	$ 2,637	$ 670	$ 365	$ 230	$ 340	$ 8,233	$ 8,265
Weighted average interest rate	**2.08%**	2.55%	3.32%	4.24%	4.32%	5.58%	2.63%	
Derivative instruments:								
Receive fixed swaps								
Notional value	**$ 970**	$ 525	$ 165	$ 75	$ —	$ 95	$ 1,830	$ (9)
Weighted average receive rate	**2.06%**	2.80%	3.35%	3.47%	—	4.63%	2.58%	
Weighted average pay rate	**2.36%**	2.24%	2.25%	2.19%	—	2.41%	2.31%	
Pay fixed swaps								
Notional value	**$ —**	$ 95	$ —	$ —	$ —	$ —	$ 95	$ 1
Weighted average receive rate	—	2.41%	—	—	—	—	2.41%	
Weighted average pay rate	—	2.32%	—	—	—	—	2.32%	

Note 16 — Selected Quarterly Financial Information (Unaudited)

Quarterly results of operations are shown below for the years ended December 31:

	2004				
	First	**Second**	**Third**	**Fourth**	**Total**
Net interest income	**$ 15,326**	**$ 16,684**	**$ 16,161**	**$ 18,491**	**$ 66,662**
Nonrecurring negative provision for loan losses	**—**	**—**	**—**	**(7,878)**	**(7,878)**
Noninterest expense, net	**5,932**	**6,427**	**3,474**	**11,327**	**27,160**
FAC expense	**101**	**91**	**78**	**128**	**398**
Net income	**$ 9,293**	**$ 10,166**	**$ 12,609**	**$ 14,914**	**$ 46,982**

	2003				
	First	Second	Third	Fourth	Total
Net interest income	$ 12,245	$ 12,682	$ 12,232	$ 12,667	$ 49,826
Provision for loan losses	340	—	—	—	340
Noninterest expense (income), net	3,682	1,987	2,733	(26,541)	(18,139)
FAC expense	1,163	1,695	80	(137)	2,801
Net income	$ 7,060	$ 9,000	$ 9,419	$ 39,345	$ 64,824

	2002				
	First	Second	Third	Fourth	Total
Net interest income	$ 9,546	$ 10,774	$ 11,588	$ 13,130	$ 45,038
Provision for loan losses	190	203	1,216	(4,511)	(2,902)
Noninterest expense, net	3,559	1,349	1,505	5,854	12,267
FAC expense	580	844	848	934	3,206
Net income	$ 5,217	$ 8,378	$ 8,019	$ 10,853	$ 32,467

As discussed in Note 2,"Summary of Significant Accounting Policies," the Bank's mineral interests were sold in November 2003 for proceeds of $30.5 million, which is included in "Noninterest expense, net."

Note 17 — Combined Association Financial Data (Unaudited)

Condensed financial information for the combined District Associations follows. All significant transactions and balances between the Associations are eliminated in combination. The multi-employer structure of the District's DB plan results in the recording of this plan only in the District's combined financial statements.

	December 31,		
Balance Sheet Data	**2004**	2003	2002
Cash	**$ 40,555**	$ 40,952	$ 43,476
Loans	**7,568,736**	6,789,215	6,393,934
Less allowance for loan losses	**10,378**	166,652	159,045
Net loans	**7,558,358**	6,622,563	6,234,889
Accrued interest receivable	**95,747**	84,323	93,503
Other property owned, net	**5,184**	5,528	3,577
Other assets	**181,656**	159,623	159,773
Total assets	**$ 7,881,500**	$ 6,912,989	$ 6,535,218
Bonds and notes	**$ 6,336,917**	$ 5,641,875	$ 5,411,885
Other liabilities	**147,434**	96,573	79,528
Total liabilities	**6,484,351**	5,738,448	5,491,413
Capital stock and participation certificates	**92,103**	104,657	106,237
Retained earnings	**1,305,046**	1,069,884	937,568
Total shareholders' equity	**1,397,149**	1,174,541	1,043,805
Total liabilities and shareholders' equity	**$ 7,881,500**	$ 6,912,989	$ 6,535,218

	Year Ended December 31,		
Statement of Income Data	**2004**	2003	2002
Interest income	**$ 387,570**	$ 355,600	$ 356,059
Interest expense	**152,932**	143,328	167,120
Net interest income	**234,638**	212,272	188,939
(Negative provision) provision for loan losses	**(151,953)**	10,883	13,836
Net interest income after provision for loan losses	**386,591**	201,389	175,103
Noninterest income	**43,152**	69,329	24,124
Intra-System financial assistance expense	**3,406**	3,993	4,148
Other expense	**147,635**	109,416	95,939
Provision (negative provision) for income taxes	**1,768**	324	(724)
Net income	**$ 276,934**	$ 156,985	$ 99,864

DISCLOSURE INFORMATION AND INDEX

Disclosures Required by Farm Credit Administration Regulations

Description of Business

The Farm Credit Bank of Texas (FCBT or Bank) is one of the banks of the Farm Credit System (System), a nationwide system of cooperatively owned banks and associations established by acts of Congress. The Bank provides credit and credit-related services to or for the benefit of the Agricultural Credit Associations (ACAs) and the Federal Land Credit Associations (FLCAs) of the Tenth Farm Credit District (District) in the states of Alabama, Louisiana, Mississippi, New Mexico and Texas. The District's FLCAs and ACA parent associations, which contain two wholly-owned FLCA and Production Credit Association (PCA) subsidiaries, are collectively referred to as Associations. A further description of territory served, entities eligible to borrow, types of lending activities engaged in, financial services offered and related Farm Credit organizations required to be disclosed in this section are incorporated herein by reference to Note 1, "Organization and Operations," to the accompanying financial statements.

The description of significant developments that had or could have a material impact on results of operations or interest rates to borrowers, acquisitions or dispositions of material assets, material changes in the manner of conducting business, seasonal characteristics and concentrations of assets, if any, required to be disclosed in this section is incorporated herein by reference to "Management's Discussion and Analysis" of the Bank included in this annual report to stockholders.

Directors and Senior Officers

The following represents certain information regarding the directors and senior officers of the Bank as of February 1, 2005:

DIRECTORS

Ralph W. Cortese joined the board in 1995, and his current term expires December 31, 2007. Cortese has served as chairman since 2000. Prior to joining the Bank board, Cortese was chairman of the PCA of Eastern New Mexico Board of Directors. Early in his career, he was vice president of Roswell PCA. He is a farmer and rancher from Fort Sumner, New Mexico. In 2001, he joined the American Land Foundation Board. He is a member of the Bank's Audit Committee. In June 2003, he was appointed to the Farmer Mac board.

Jon M. Garnett began his first term on the board in 1999 and his current term expires December 31, 2007. He has served as board vice chairman since 2000. Prior to joining the Bank board, he was chairman of the Panhandle-Plains Federal Land Bank Association (FLBA) Board of Directors. In January 2003, he joined the national Farm Credit Council Board of Directors as a Tenth District representative. He also serves on the Bank's Audit Committee and the State Technical Committee for the Natural Resources Conservation Service. Garnett farms, feeds stocker cattle, and operates a custom haying and baling business near Spearman, Texas.

C. Kenneth Andrews began service on the board in 1994, and is currently elected to a three-year term that expires December 31, 2005. He was manager of the former FLBA of Madisonville for 17 years and later served on the board of directors of the FLBA of Bryan. The Madisonville, Texas, rancher is chairman of the Tenth District Farm Credit Council and has represented the District on the national Farm Credit Council Board of Directors since 1996. He also serves on the Bank's Audit Committee.

Joe R. Crawford began his first term on the board in 1998 and is currently elected to a three-year term that expires December 31, 2006. Previously, he was a member of the FLBA of North Alabama Board of Directors. He also served on the Tenth District FLBA Legislative Advisory Committee. Currently, he is the Tenth District's representative on the board of directors of the Federal Farm Credit Banks Funding Corporation and is a member of the Bank's Audit Committee. Crawford, who lives near Baileyton, Alabama, has owned and operated a cattle business since 1968.

James F. Dodson joined the board of directors in January 2003, elected to a three-year term that will expire December 31, 2005. He is a past chairman of the Texas AgFinance, FCS Board of Directors and a former member of the Tenth Farm Credit District Stockholders' Advisory Committee. He currently serves on the Tenth District Farm Credit Council board and on the Bank's Audit Committee. Dodson grows cotton and milo and operates a seed sales business with his family in Robstown, Texas. He is on the board of Cotton Incorporated and holds other national farm leadership positions.

William F. Staats joined the board in 1997, and his current term will expire December 31, 2005. Staats is Louisiana Bankers Association Chair Emeritus of Banking and Professor Emeritus, Department of Finance, at Louisiana State University, where he held the Hermann Moyse Jr. Distinguished Professorship. Previously, he was vice president and corporate secretary of the Federal Reserve Bank of Philadelphia. Staats also serves on the boards of the Money Management International Education Foundation, Money Management International and SevenOaks Capital Associates, LLC. He is chairman of the Bank's Audit Committee.

SENIOR OFFICERS

Name and Title	Time in Position	Experience — Past Five Years
Larry R. Doyle, *Chief Executive Officer*	1.5 years	Executive Vice President and Chief Operating Officer, AgFirst Farm Credit Bank
Thomas W. Hill, *Senior Vice President, Chief Financial Officer, Chief Operations Officer*	10 years 1 year	Senior Vice President, Chief Financial Officer, FCBT
Steven H. Fowlkes, *Senior Vice President, Chief Credit Officer*	7 years 1 year	Senior management and management positions, FCBT
David N. Clinton, *Senior Vice President, Chief Information Officer*	6 years	Senior management position, FCBT
William E. Zimmerman, *Senior Vice President, Corporate Affairs, General Counsel and Corporate Secretary*	17 years	Senior Vice President, Corporate Affairs, General Counsel and Corporate Secretary, FCBT

Compensation of Directors and Senior Officers

Directors of the Bank are compensated for service on the Bank's board. Compensation for 2004 was paid at the rate of $2,196 per month, the maximum allowed under the Farm Credit Administration's (FCA) "Annual Adjustment of Maximum Director Compensation for 2004." In addition to days served at board meetings, directors may serve additional days on other official assignments, and under exceptional circumstances the board may approve additional compensation, not to exceed 30 percent of the annual maximum. Information for each director for the year ended December 31, 2004, is provided below:

Board Member	Days Served at Board Meetings	Days Served on Other Official Assignments	Total Compensation Paid
Ralph W. Cortese	36.5	13.5	$ 31,858
Jon M. Garnett	29.0	37.5	34,265
C. Kenneth Andrews	32.0	37.5	34,265
Joe R. Crawford	30.0	17.5	30,858
James F. Dodson	29.0	13.0	28,358
William F. Staats	31.5	15.5	31,858
			$ 191,462

The following table summarizes the compensation paid to all senior officers of the bank during 2004, 2003 and 2002:

Summary Compensation Table

Name of Individual or Group	Year	Annual Salary (a)	Annual Bonus (b)	Other (c)	Total
Larry R. Doyle, Chief Executive Officer	2004	$ 440,000	$ 100,000	$ —	$ 540,000
Larry R. Doyle, Chief Executive Officer	2003	316,666	—	92,400	409,066
Arnold Henson, Chief Executive Officer, retired	2003	51,667	55,000	64,099	170,766
Arnold Henson, Chief Executive Officer	2002	310,000	50,000	—	360,000
Aggregate number of senior officers: (includes Chief Executive Officer)					
6	2004	1,396,992	298,247	—	1,695,239
8	2003	1,362,683	201,513	255,095	1,819,291
6	2002	1,116,775	168,451	—	1,285,226

(a) Gross salary
(b) Incentive pay
(c) Other includes relocation benefits, retirement gifts and unused annual leave paid in conjunction with retirement.

Disclosure of the compensation paid during 2004 to any senior officer included in the table above is available and will be disclosed to stockholders of the institution and stockholders of the District's Associations upon written request.

Directors and senior officers are reimbursed for reasonable travel, subsistence and other related expenses while conducting Bank business. The aggregate amount of expenses reimbursed to directors in 2004, 2003 and 2002 totaled $91,473, $71,001 and $47,407, respectively. A copy of FCBT's travel policy is available to shareholders upon request.

Bank employees, including senior officers, can earn compensation above base salary through an annual success-sharing incentive plan, which the FCBT adopted during 2001. The plan is based upon the achievement of predetermined Bank performance standards, which are approved by the board of directors annually.

Description of Property

In November of 2002, the Bank sold the District headquarters building and 8.4 acres of land on which it was situated on the northeast side of Austin, Texas. As a part of the sale agreement, the Bank leased space in the building until June 2004. On September 30, 2003, the Bank entered into a lease for approximately 102,500 square feet of office space to house its headquarters facility. The lease was effective September 30, 2003, and the term is from September 1, 2003 to August 31, 2013. The Bank moved into the new facilities during May of 2004. The Bank's investment in property is further detailed in Note 5, "Premises and Equipment," to the accompanying financial statements.

Legal Proceedings

There are no legal proceedings pending against the Bank and Associations, the outcome of which, in the opinion of legal counsel and management, would materially affect the financial position of the Bank and Associations. Note 12, "Commitments and Contingencies," to the accompanying financial statements outlines the Bank's position with regard to possible contingencies at December 31, 2004.

Description of Capital Structure

The Bank and Associations are authorized to issue and retire certain classes of capital stock and retained earnings in the management of their capital structures. Details of the capital structures are described in Note 8, "Shareholders' Equity," to the accompanying financial statements, and in the "Management's Discussion and Analysis" of the District included in this annual report to stockholders.

Description of Liabilities

The Bank's debt outstanding is described in Note 7, "Bonds and Notes," to the accompanying financial statements. The Bank's contingent liabilities and intra-System financial assistance rights and obligations are described in Note 12, "Commitments and Contingencies," and Note 10, "Intra-System Financial Assistance," to the accompanying financial statements.

Selected Financial Data

The selected financial data for the five years ended December 31, 2004, required to be disclosed, is incorporated herein by reference to the "Five-Year Summary of Selected Combined Financial Data" included in this annual report to stockholders.

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

"Management's Discussion and Analysis," which precedes the financial statements in this annual report, is incorporated herein by reference.

Transactions With Senior Officers and Directors

The Bank does not have lending authority to make loans to individual borrowers, and so has no loans to or transactions with its officers and directors.

Relationship With Public Accountants

There were no changes in independent public accountants since the prior annual report to stockholders, and there were no material disagreements with our independent public accountants on any matter of accounting principles or financial statement disclosure during this period.

Financial Statements

The financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated March 4, 2005, and the report of management in this annual report to stockholders, are incorporated herein by reference.

The Bank's and the District's annual and quarterly reports 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 can be requested by e-mailing *fcb@farmcreditbank.com*. The District's quarterly reports are available approximately 45 days after the end of each fiscal quarter. The District's quarterly and annual stockholder reports also are available on its Web site at *www.farmcreditbank.com*.