The lender who can get you there

2006 ANNUAL REPORT

FARM CREDIT BANK OF TEXAS

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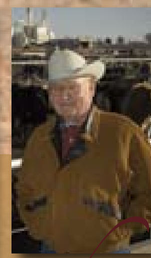
  

The lender who can get you there

Since 1916, Farm Credit Bank of Texas has focused on putting our customers first and helping them achieve their goals. Whether we are providing competitive, market-priced funds, cutting-edge products and enhanced services for the lending co-ops that own the bank, or participating with them in large agribusiness loans, we are equipping them to better serve their customers in rural America.

Farm Credit Bank of Texas is a lending partner who cares about our customers' success. As the customers on the following pages attest, Farm Credit is the lender who can get you there.

On the Texas High Plains, where the horizon runs straight and the evening sky explodes in hues of pink and purple and orange, Paul Engler runs the largest privately owned cattle-feeding business in the world, feeding nearly 1 million head of cattle a year.

Engler co-founded Cactus Feeders in 1975 with a single feedyard. Since then, the company has grown into a model of cattle-feeding efficiency, innovative marketing and proper cattle handling. Today, the business includes 10 feedyards — seven in West Texas and three in Kansas — with a one-time capacity of 520,000 head of cattle.

The Amarillo-based company also owns and operates three ranches in Texas and New Mexico, where it maintains 1,000 mother cows and more than 20,000 stocker calves on 140,000 acres of farmland and pasture. Together, these operations generate gross revenues of $750 million annually.

"In an operation of this scale, the daily cash-flow is enormous, so it's important that our lender understands our business and has the funding capacity and cash management products we need to be successful," says Engler.

Those factors figured prominently in Cactus Feeders' decision in 2006 to form a banking relationship with the Farm Credit Bank of Texas and affiliated Farm Credit lending co-ops.

Nearly one-third owned by its 500-plus employees, Cactus Feeders also appreciates Farm Credit's cooperative business model of rewarding its customer-owners.

"Farm Credit pays patronage dividends to their borrowers, which returns money to the rural economy. By doing business with Farm Credit and sharing in their earnings, we all come out stronger in the end," Engler says.

In more than 50 years of buying and selling cattle, he has seen Farm Credit stick with producers through tough times. "I remember the economic debacle and the humanitarian disasters that accompanied the Great Depression, when commercial banks were known more for foreclosing on farm and ranch properties than for making loans to rebuild U.S. agriculture. Thankfully, the Farm Credit System was set up to furnish the necessary credit to farmers and ranchers and, in so doing, saved American agriculture," Engler says. "Cactus Feeders is therefore proud to be a Farm Credit customer."

CACTUS FEEDERS
Proud to Be a Customer

PAUL ENGLER

SOCIAL LEARNING

While Lipan, Texas, businessman Bill McKay was closing a ranch loan with his local Farm Credit cooperative in early 2006, he mentioned that he was seeking financing for three rural schools for at-risk teenagers.

In the past, Farm Credit would not have been able to help McKay. However, Farm Credit Bank of Texas had recently adopted a resolution to use its regulatory authorities to invest in rural projects that it could not finance through traditional loans.

As luck would have it, the schools fit the criteria for the bank's new Rural America Bond Program: They are located in rural communities with low per capita income; they provide jobs for scores of rural residents; and they contribute to the economic vitality of the rural areas in which they are located.

In October, Farm Credit Bank of Texas partnered with McKay's local Farm Credit lender to purchase bonds totaling $5.5 million from Social Learning Environment, Inc., a non-profit entity that McKay has managed since 1979.

Social Learning Environment operates residential treatment centers and schools for 12- to 18-year-olds who have educational, emotional and/or behavioral challenges. The company has facilities near Fort Davis, Texas, and Valmora, N.M., established in 1976 and 1994, respectively. It employs 120 local residents at each location. A third school will be built near Missoula, Mont., in 2007, creating over 100 more rural jobs. All three schools are located at least 25 miles outside a rural town and within reasonable proximity of a university, so that they can provide more value to rural America.

"Not many lenders are interested in financing nonprofit schools in rural areas. Thanks to Farm Credit's Rural America Bond Program, however, we will be able to contribute to the economies where the schools are located while making a difference in the lives of a great many young people," says McKay.

ENVIRONMENT, INC.

Supporting the Rural Economy

BILL McKAY

From the edge of Capote Farms

in Texas' Lower Rio Grande Valley, you can hear the roar of 18-wheelers, heading to and from the nearby Pharr International Bridge.

For the most part, the trucks are loaded with materials bound for American-owned assembly and manufacturing plants in Reynosa, Mexico — plants that choose to have their raw materials and components delivered daily from Texas.

Some old-timers around Pharr might find the traffic a nuisance — but not the Dyer family, longtime owners of Capote Farms, a cotton, vegetable, sugarcane and citrus operation that fronts the Rio Grande.

Recognizing a demand for distribution facilities close to the bridge, they decided to take advantage of the international commerce by establishing a new enterprise — an industrial park for U.S. companies doing business in Mexico.

"While agriculture will continue to be at the heart of Capote Farms, the warehouse provides an opportunity to diversify and contribute to local economic growth," explains Phil Dyer, one of Malcolm and Mary Agnes Dyer's four children.

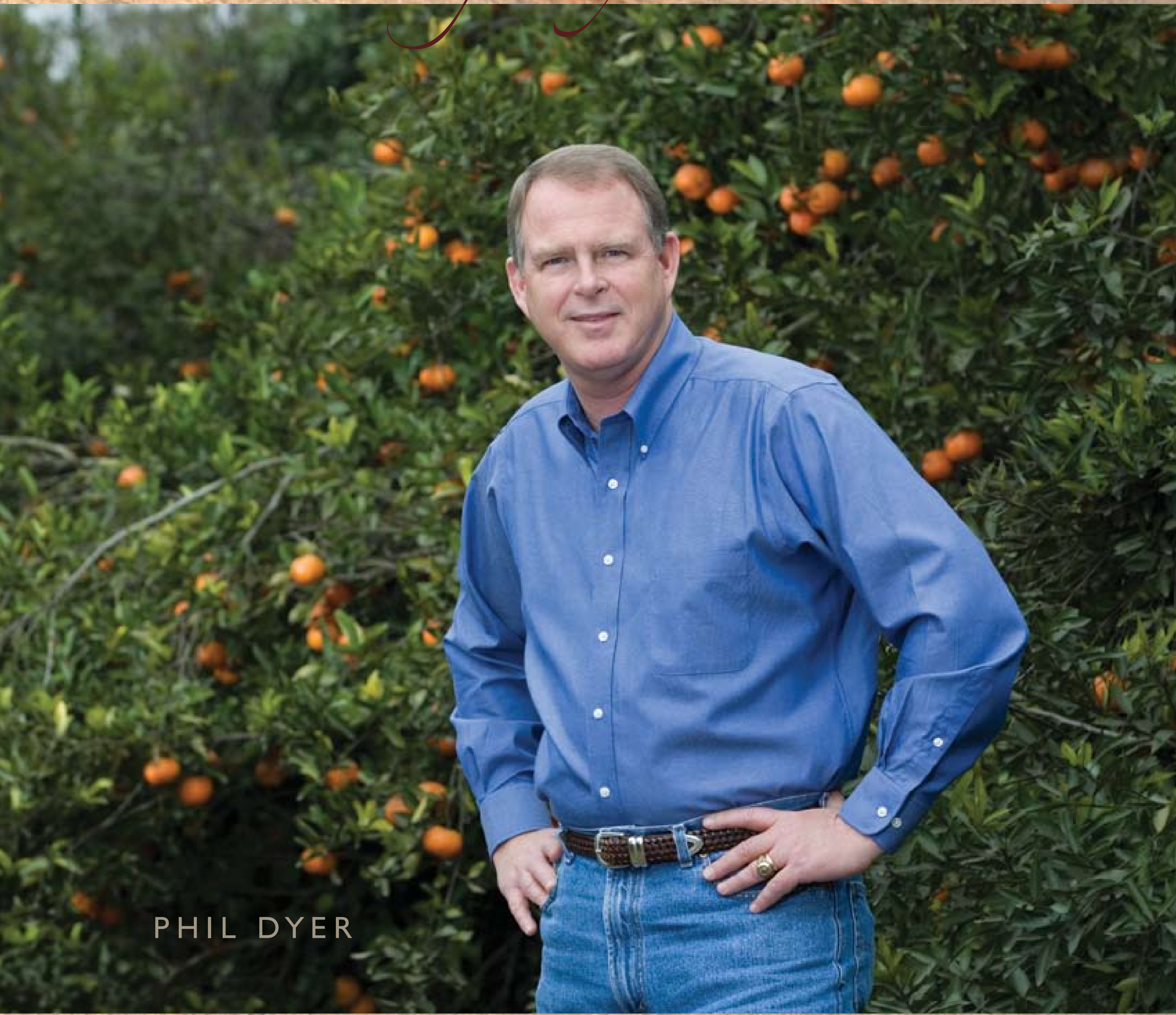
The steps involved in launching the project — market research, working with zoning boards, hiring contractors and so forth — have been long and sometimes complicated.

In the end, it has been well worth the effort with the financing from Farm Credit.

The project was eligible for Farm Credit financing because Capote Farms' primary relationship with Farm Credit was, and continues to be, agricultural loans. With a loan package assembled by their local Farm Credit association and Farm Credit Bank of Texas, construction of the new warehouses got under way in 2006. Tenants, including at least one Fortune 500 company, began occupying leased space in early 2007.

"Farm Credit has supported our family's goals over the past 35 years, and we are grateful to Farm Credit for financing this latest venture," says Dyer. "It is reassuring to have a financing partner who wants to help us realize our dreams."

CAPOTE FARMS
Branching Beyond the Farm



PHIL DYER

Farm Credit Bank of Texas
BOARD OF DIRECTORS

Elizabeth G. "Betty" Flores

(Seated) Ralph W. "Buddy" Cortese
Chairman

Jimmy Dodson

William Staats

Joe Crawford

(Seated) Jon "Mike" Garnett
Vice Chairman

THE COOPERATIVE DIFFERENCE

Kenneth Andrews

What sets Farm Credit Bank of Texas apart from other lenders are our cooperative structure and cooperative business model.

The bank is a wholesale lender that provides funding to our stockholders — 20 rural lending cooperatives in Alabama, Louisiana, Mississippi, New Mexico and Texas, and four Other Financing Institutions. We also share our earnings with them, thus reducing their cost of funds. In turn, the lending co-ops provide agricultural and rural real estate financing to their borrower-stockholders — farmers, ranchers, agribusiness firms, country homeowners and other rural landowners. And when they do well, they typically pay patronage to their customers, effectively reducing the cost of borrowing.

As part of the Farm Credit System, a $163-billion nationwide network of rural financing cooperatives established by Congress in 1916, Farm Credit Bank of Texas has a competitive source of funds — AAA-rated Farm Credit securities, which are sold in the nation's money markets. This funding source and our cooperative business model offer distinct advantages that allow us to outperform our competitors.

Farm Credit Bank of Texas

SENIOR MANAGEMENT TEAM

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

In 2006, Farm Credit Bank of Texas celebrated 90 years of financing agriculture and rural America, and we are proud to report that it was one of the most successful years in our long history. Strong growth and a record direct-note patronage distribution highlighted our financial results.

Net income was up 12.8 percent over 2005, and year-end loan volume increased 18.5 percent from the previous year. Credit quality remained extremely strong for the third consecutive year. Once again, the bank exceeded our regulator's minimum requirements for permanent capital, core surplus, total surplus and net collateral ratio.

For a cooperative, however, the most significant measure of success is the level of earnings we share with our owners. In 2006, the bank declared $37 million, or 57 percent, of its net income in patronage. In turn, our 20 affiliated associations and Other Financing Institutions declared a record $120.5 million in patronage to their customers.

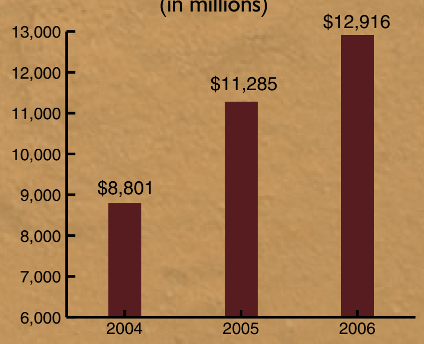
FINANCIAL HIGHLIGHTS

For the Year *(in thousands)*	**2006**	2005	2004
Net interest income	**$ 90,342**	$ 75,960	$ 66,662
(Provision) negative provision for loan losses	**(2,578)**	344	7,878
Noninterest (expense) income, net	**(22,770)**	(18,688)	(27,558)
Net income	**64,994**	57,616	46,982
Rate of return on:			
Average assets	**0.53%**	0.60%	0.59%
Average shareholders' equity	**10.07**	10.57	9.44
Cash patronage declared	**$ 37,043**	$ 28,713	$ 16,775

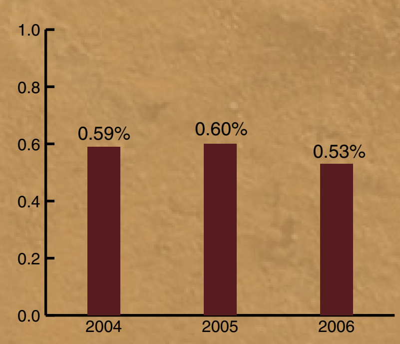
At Year End *(in millions)*			
Total loans	**$ 10,055**	$ 8,482	$ 6,918
Total assets	**12,916**	11,285	8,801
Total liabilities	**12,252**	10,661	8,300
Total shareholders' equity	**664**	624	501
Permanent capital ratio	**13.67%**	17.36%	19.82%
Total surplus ratio	**11.61**	14.97	16.55
Core surplus ratio	**6.93**	8.82	11.51
Net collateral ratio	**105.35**	105.90	105.69

Total Assets Outstanding at Year End

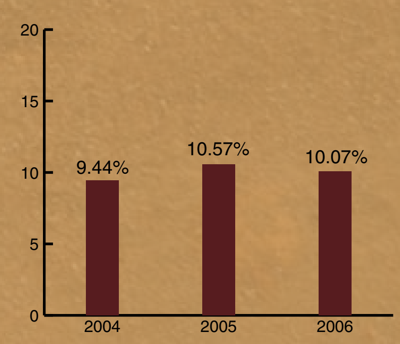
(in millions)



Return on Average Assets for the Year



Return on Average Equity for the Year



2006 Accomplishments

For Farm Credit Bank of Texas, 2006 was a year full of accomplishments and notable achievements. Most important, 2006 will be remembered as the year in which we delivered on our promise to our association stockholders to provide them with their lowest cost of funds ever. We succeeded in reducing the net cost of funds loaned to associations from 29 basis points in 2004 to just 5 basis points in 2006, a rate comparable to the implied marginal cost of funds. This achieved a goal set out in the bank's five-year plan adopted in 2003.

Entering 2006, we set high expectations and made firm commitments to accomplish all of the key initiatives in our annual strategic plan. By year end, we had met these goals.

- To diversify the bank's credit exposure and manage capital, we sold an additional $1 billion in direct notes to CoBank, resulting in a total of $1.4 billion of direct notes sold.
- Through alliances with other financial institutions, including Wachovia Bank and Chase Bank, we offered new cash management products, notably a sweep product and a remote deposit product.
- We continued to grow our balance sheet in 2006. Serviced direct-note loan volume with associations increased by 24 percent, or $1.8 billion, in 2006, while our capital markets participations portfolio increased by 61.4 percent to total $2.1 billion at year end.
- Automated tools were made available to associations to distribute their patronage to their stockholders following beneficial cooperative principles.
- We piloted Customer Relationship Management tools that will increase the district's ability to better manage business relationships.
- We gained regulatory approval of a Rural America Bond Program, through which the bank and Tenth District associations can use their authorities to invest in rural enterprises and communities, thereby enhancing life in rural America.
- The bank launched a branding initiative that will leverage Farm Credit's strong presence in rural America for the benefit of all Tenth District associations.
- We further implemented the bank's diversity program through recruitment efforts and staff training for both bank and association personnel, as well as through corporate sponsorships and scholarships.

The Year Ahead

In 2007, the Farm Credit Bank of Texas will complete the final year of a five-year business plan to increase profitability, become more competitive and provide greater value to our stockholders. As we enter the homestretch of this ambitious course, we can be proud of our accomplishments to date, having met or exceeded all of our target goals on schedule.

The race is not over, however. This year, we will strive to be even more competitive and provide even greater value to our stockholders, as we continue to manage capital, increase earnings, serve our customers and enhance operational standards.

The bank will continue to build on its ongoing commitment to provide our association stockholders with competitive support services and business tools in 2007. One of our top priorities in this area is to select a new market-fresh loan accounting system that will keep our associations competitive and innovative in the banking industry.

In recent years, the profile of rural America has changed considerably. Full-time farmers and ranchers are becoming fewer; small towns are losing infrastructure; and yet more and more people are moving to the country. These changing demographics are driving several of the bank's 2007 initiatives.

We have made a commitment to help sustain and develop rural communities. Working in partnership with our associations, we plan to use the new Rural America Bond Program in 2007 as a tool to help meet the growing financing and capital needs of agriculture and rural America.

We will also continue to work with other Farm Credit System lenders to support the ever-changing needs of our rural marketplace through modest and incremental changes in the System's legislative and regulatory authorities.

Recognizing the rich cultural and ethnic diversity within the population of the Tenth Farm Credit District, we will focus on serving our increasingly diverse marketplace. This includes assembling a top-notch staff that represents a mix of ideas, backgrounds and skill sets so that diversity becomes an intrinsic part of our business culture.

Indeed, employees are our greatest asset and must be credited for their hard work in achieving the bank's outstanding 2006 financial results. In the coming year we will continue to invest in our staff through a new professional development program that recognizes the leadership potential of each bank employee.

As we begin 2007, we are focused on staying competitive and improving the bank's earnings through participation and investment earnings so that we can increase patronage dividends to our stockholders. Ultimately, our goal is to drive down the cost of funds for farmers, ranchers and other Farm Credit customers and improve the use of the capital they have invested in our Tenth District financing cooperatives.

At Farm Credit Bank of Texas, customers come first, and in 2007, as always, we remain committed to their success.

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.

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, 2006, 2005 and 2004. The independent auditors have direct access to the board, which is composed solely of directors who are not officers or employees of the bank. The undersigned certify that the Farm Credit Bank of Texas' Annual Report has been prepared in accordance with applicable statutory or regulatory requirements and that the information contained herein is true, accurate and complete to the best of our knowledge and belief.

Ralph W. Cortese
Chairman of the Board

Larry R. Doyle
Chief Executive Officer

Thomas W. Hill
Chief Financial Officer

March 1, 2007

FIVE-YEAR SUMMARY OF SELECTED FINANCIAL DATA

Farm Credit Bank of Texas

(dollars in thousands)	2006	2005	2004	2003*	2002
Balance Sheet Data					
Cash, federal funds sold and overnight investments	$ 103,394	$ 46,836	$ 51,114	$ 28,265	$ 61,859
Investment securities	2,672,242	2,697,876	1,787,706	1,518,102	785,071
Loans	10,055,428	8,481,501	6,918,236	5,834,929	5,826,951
Less allowance for loan losses	142	142	239	9,834	9,695
Net loans	10,055,286	8,481,359	6,917,997	5,825,095	5,817,256
Other property owned, net	—	—	—	529	2,615
Other assets	84,838	58,717	44,388	38,833	39,225
Total assets	$ 12,915,760	$ 11,284,788	$ 8,801,205	$ 7,410,824	$ 6,706,026
Obligations with maturities of one year or less	$ 4,835,886	$ 5,371,770	$ 4,058,078	$ 2,487,260	$ 3,751,585
Obligations with maturities greater than one year	7,415,653	5,288,711	4,241,696	4,445,935	2,585,463
Total liabilities	12,251,539	10,660,481	8,299,774	6,933,195	6,337,048
Preferred stock, net	200,000	200,000	100,000	100,000	—
Capital stock	161,421	135,390	118,323	109,787	109,896
Retained earnings	324,270	315,047	290,666	272,291	257,884
Accumulated other comprehensive (loss) income	(21,470)	(26,130)	(7,558)	(4,449)	1,198
Total shareholders' equity	664,221	624,307	501,431	477,629	368,978
Total liabilities and shareholders' equity	$ 12,915,760	$ 11,284,788	$ 8,801,205	$ 7,410,824	$ 6,706,026
Statement of Income Data					
Net interest income	$ 90,341	$ 75,960	$ 66,662	$ 49,826	$ 45,091
(Provision) negative provision for loan losses	(2,578)	344	7,878	(340)	2,902
Noninterest (expense) income, net	(22,769)	(18,688)	(27,558)	15,338	(15,526)
Net income	$ 64,994	$ 57,616	$ 46,982	$ 64,824	$ 32,467
Financial Ratios (unaudited)					
Rate of return on:					
Average assets	0.53%	0.60%	0.59%	0.92%	0.53%
Average shareholders' equity	10.07%	10.57%	9.44%	16.21%	9.43%
Net interest income to average earning assets	0.74%	0.80%	0.85%	0.71%	0.74%
Net charge-offs to average loans	0.03%	—	0.03%	—	0.02%
Total shareholders' equity to total assets	5.14%	5.53%	5.70%	6.45%	5.50%
Debt to shareholders' equity (:1)	18.44	17.08	16.55	14.52	17.17
Allowance for loan losses to total loans	—	—	—	0.17%	0.17%
Permanent capital ratio	13.67%	17.36%	19.82%	23.71%	18.06%
Total surplus ratio	11.61%	14.97%	16.55%	19.15%	14.01%
Core surplus ratio	6.93%	8.82%	11.51%	14.44%	12.56%
Net collateral ratio	105.35%	105.90%	105.69%	106.62%	105.32%
Net Income Distributions					
Net income distributions declared					
Preferred stock dividends	$ 15,122	$ 11,342	$ 7,561	$ 798	$ —
Patronage distributions declared					
Cash	$ 37,043	$ 28,713	$ 16,775	$ 49,144	$ 3,615
Allocated earnings	1,058	837	14	1,645	928

* 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 mineral interests were sold in November 2003. Net income and certain profitability ratios for 2003 were affected by the one-time gain of $30.5 million from the sale of mineral interests in that year.

Management's Discussion &

(DOLLARS IN THOUSANDS, EXCEPT AS OTHERWISE NOTED)

The following commentary is 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, 2006, 2005 and 2004. 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 accompanying financial statements were prepared under the oversight of the bank's audit committee.

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, which, in turn, provide credit to their borrowers/shareholders. As of December 31, 2006, the bank served six Federal Land Credit Associations (FLCAs), 14 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.

Forward-Looking Information

This annual information statement contains forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," "will," or other variations of these terms are intended to identify the forward-looking statements. These statements are based on assumptions and analyses made in light of experience and other historical trends, current conditions, and expected future developments. However, actual results and developments may differ materially from our expectations and predictions due to a number of risks and uncertainties, many of which are beyond our control. These risks and uncertainties include, but are not limited to:

- political, legal, regulatory and economic conditions and developments in the United States and abroad;
- economic fluctuations in the agricultural, rural utility, international and farm-related business sectors;
- weather-related, disease and other adverse climatic or biological conditions that periodically occur that impact agricultural productivity and income;
- changes in United States government support of the agricultural industry; and
- actions taken by the Federal Reserve System in implementing monetary policy.

Critical Accounting Policies

The financial statements are reported in conformity with accounting principles generally accepted in the United States of America. Our significant accounting policies are critical to the understanding of our results of operations and financial position because some accounting policies require us to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. We consider these policies critical because management has to make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 2 , "Summary of Significant Accounting Policies," of the accompanying financial statements. The following is a summary of certain critical policies.

- Allowance for loan losses — The allowance for loan losses is management's best estimate of the amount of probable losses existing in and inherent in our loan portfolio. The allowance for loan losses is increased through provisions for loan losses and loan recoveries and is decreased through loan loss reversals and loan charge-offs. The allowance for loan losses is determined based on a periodic evaluation of the loan portfolio, which generally considers recent historical charge-off experience adjusted for relevant factors. These factors include types of loans, credit quality, specific industry conditions, general economic and political conditions, and changes in the character, composition and performance of the portfolio, among other factors.

Analysis

Significant individual loans are evaluated based on the borrower's overall financial condition, resources and payment record; the prospects for support from any financially responsible guarantor; and, if appropriate, the estimated net realizable value of any collateral. The allowance for loan losses attributable to these loans is established by a process that estimates the probable loss inherent in the loans, taking into account various historical and projected factors, internal risk ratings, regulatory oversight, and geographic, industry and other factors.

Changes in the factors considered by management in the evaluation of losses in the loan portfolios could result in a change in the allowance for loan losses and could have a direct impact on the provision for loan losses and the results of operations.

- Valuation methodologies — Management applies various valuation methodologies to assets and liabilities that often involve a significant degree of judgment, particularly when liquid markets do not exist for the particular items being valued. Quoted market prices are referred to when estimating fair values for certain assets for which an observable liquid market exists, such as most investment securities. Management utilizes significant estimates and assumptions to value items for which an observable liquid market does not exist. Examples of these items include impaired loans, pension and other postretirement benefit obligations, and certain derivative and other financial instruments. These valuations require the use of various assumptions, including, among others, discount rates, rates of return on assets, repayment rates, cash flows, default rates, costs of servicing and liquidation values. The use of different assumptions could produce significantly different results, which could have material positive or negative effects on the bank's results of operations.
- Pensions — The bank and its related associations participate in the district's defined benefit (DB) retirement plan. The plan is noncontributory and benefits are based on salary and years of service. In addition, the bank and its related associations also participate in defined contribution retirement savings plans. Pension expense for all plans is recorded as part of salaries and employee benefits. The structure of the district's DB plan is characterized as multiemployer, 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.

Financial Highlights

- The aggregate principal amount of loans outstanding at December 31, 2006, was $10.1 billion, compared to $8.5 billion at December 31, 2005, and $6.9 billion at December 31, 2004, reflecting increases of 18.5 and 45.3 percent over December 31, 2005 and 2004, respectively.
- The bank's investment portfolio at December 31, 2006, totaled $2.8 billion, compared to $2.7 billion at December 31, 2005, and $1.8 billion at December 31, 2004, reflecting increases of 0.8 and 50.5 percent over December 31, 2005 and 2004, respectively.
- Net income totaled $65.0 million for the year ended December 31, 2006, an increase of 12.8 percent compared to 2005.
- Net interest income for the year ended December 31, 2006, was $90.3 million, an 18.9 percent increase over the year ended December 31, 2005.
- Return on average assets and return on average shareholders' equity for the year ended December 31, 2006, were 0.53 and 10.07 percent, respectively, compared to 0.60 and 10.57 percent for 2005, respectively.
- Approximately $1.0 billion of participations in four of the bank's direct notes with the district associations were sold, at par, to another System bank in 2006.
- Patronage distributions declared and earnings allocated totaled $38.1 million in 2006, compared to $29.5 million in 2005.

RESULTS OF OPERATIONS

Net Income

The bank's net income of $64,994 for the year ended December 31, 2006, reflects an increase of 12.8 percent over 2005, while 2005 income of $57,616 increased by 22.6 percent from 2004. The return on average assets was 0.53 percent for the year ended December 31, 2006, down from 0.60 percent reported for the year ended December 31, 2005. The return on average assets was 0.59 percent for the year ended December 31, 2004. Changes in the major components of net income for the referenced periods are outlined in the following table and discussion.

	2006 vs. 2005	2005 vs. 2004
Net income (prior period)	$ 57,616	$ 46,982
Increase (decrease) due to:		
Interest income	260,331	167,698
Interest expense	(245,950)	(158,400)
Net interest income	14,381	9,298
Provision for loan losses	(2,922)	(7,534)
Noninterest income	1,352	1,614
Noninterest expense	(5,433)	7,256
Total change in net income	7,378	10,634
Net income	$ 64,994	$ 57,616

Discussion of the changes in components of net income is included in the following narrative.

Interest Income

Total interest income for the year ended December 31, 2006, was $652,557, an increase of $260,331, or 66.4 percent, compared to 2006. Total interest income for 2005 was $392,226, an increase of $167,698, or 74.7 percent, from 2004. These increases were primarily attributable to the effect of the increasing interest rate environment that prevailed during 2006 and 2005, combined with increases 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, 2006 vs. 2005	Year Ended December 31, 2005 vs. 2004
Increase in average earning assets	$ 2,639,656	$ 1,678,915
Average yield (prior year)	4.11%	2.86%
Interest income variance attributed to change in volume	108,490	48,017
Average earning assets (current year)	12,175,825	9,536,169
Increase in average yield	1.25%	1.25%
Interest income variance attributed to change in yield	151,841	119,681
Net change in interest income	$ 260,331	$ 167,698

Interest Expense

Total interest expense for the year ended December 31, 2006, was $562,216, an increase of $245,950, or 77.8 percent, compared to the same period of 2005. Total interest expense for 2005 was $316,266, an increase of $158,400, or 100.3 percent, from 2004. These increases were primarily attributable to the effect of the increasing interest rate environment that prevailed during 2006 and 2005, combined with increases 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, 2006 vs. 2005	Year Ended December 31, 2005 vs. 2004
Increase in average interest-bearing liabilities	$ 2,503,437	$ 1,626,313
Average rate (prior year)	3.52%	2.15%
Interest expense variance attributed to change in volume	88,121	34,966
Average interest-bearing liabilities (current year)	11,481,830	8,978,393
Increase in average rate	1.38%	1.37%
Interest expense variance attributed to change in rate	157,829	123,434
Net change in interest expense	$ 245,950	$ 158,400

Net Interest Income

Net interest income, the excess of interest income over interest expense, increased by $14,382 from 2005 to 2006, and increased by $9,298 from 2004 to 2005. The increase in 2006 was due to a $2.6 billion increase in average interest-earning assets offset by a 13 basis point decrease in the interest rate spread. Interest rate spread is the difference between the average rate received on interest-earning assets and the average rate paid on interest-bearing debt. The decrease in the interest rate spread is due to several factors. Competitive pricing on the bank's participation loan portfolio has compressed the interest rate spread on those loans. The bank has also issued longer-term debt in order to manage its interest rate risk profile. In addition, the bank has increased its investment portfolio to enhance liquidity, although at lower spreads than its other earning assets. The bank has also passed on the increasing benefit of its lendable equity in a rising-rate environment in its pricing on direct notes to district associations and OFIs.

Net interest income in 2005 was $9,298 greater than 2004. The increase in 2005 was due to a $1.68 billion increase in average interest-earning assets offset by a 12 basis point decrease in the interest rate spread. The decrease in the interest rate spread is due to several factors. Competitive pricing on the bank's participation loan portfolio compressed the interest rate spread on those loans. The bank also issued longer-term debt in order to manage its interest rate risk profile. In addition, the bank increased its investment portfolio to enhance liquidity albeit at lower spreads.

The impact of capital on net interest income increased by 7 basis points in 2006 and in 2005. These increases were due to the effects of the increasing interest rate environment during these periods.

ANALYSIS OF NET INTEREST INCOME

	2006		2005		2004	
	Avg. Balance	**Interest**	Avg. Balance	Interest	Avg. Balance	Interest
Loans	**$ 9,246,083**	**$ 511,297**	$ 7,501,731	$ 315,491	$ 6,242,127	$ 175,907
Investments	**2,929,742**	**141,260**	2,034,438	76,735	1,615,127	48,621
Total earning assets	**12,175,825**	**652,557**	9,536,169	392,226	7,857,254	224,528
Interest-bearing liabilities	**11,481,830**	**562,216**	8,978,393	316,266	7,352,080	157,866
Impact of capital	**$ 693,995**		$ 557,776		$ 505,174	
Net Interest Income		**$ 90,341**		$ 75,960		$ 66,662

	2006	2005	2004
	Average Yield	Average Yield	Average Yield
Yield on loans	**5.53%**	4.21%	2.82%
Yield on investments	**4.82%**	3.77%	3.01%
Yield on earning assets	**5.36%**	4.11%	2.86%
Cost of interest-bearing liabilities	**4.90%**	3.52%	2.15%
Interest rate spread	**0.46%**	0.59%	0.71%
Impact of capital	**0.28%**	0.21%	0.14%
Net interest income/average earning assets	**0.74%**	0.80%	0.85%

Provision for Loan Losses

In 2006, the bank recorded a $2,578 provision for loan losses, which was an increase of $2,922 from the negative provision for loan losses of $344 recorded in 2005. The increase resulted from a loss of $2.8 million related to a loan participated with a district association, offset by recoveries on other loans. The negative provision for 2005 was a $7,534 decrease from the $7,878 negative provision for loan losses recorded in 2004. In 2004, the bank refined its allowance for loan loss methodologies, as further described in the "Allowance for Loan Losses" section of this MD&A. The allowance at December 31, 2006, was considered adequate by management to absorb probable losses inherent to its loan portfolio.

Noninterest Income

Noninterest income for the year ended December 31, 2006, was $17,847, an increase of $1,352, or 8.2 percent, compared to 2005. The increase is primarily attributable to a $907 gain on the sale of investment securities, a $610 gain on the bank's share of the sale of part of 0.75 acres and development rights in McLean, Virginia, by the Farm Credit System Building Association, and an increase of $237 in services billed to district associations, partially offset by a $337 decrease in loan-related fee income.

Noninterest income totaled $16,495 for 2005, an increase of $1,614, or 10.8 percent, from 2004. The increase is primarily attributable to an increase of $2,176 in loan-related fees, partially offset by a $420 decrease in gains on sales of investments and a $125 decrease in fees for services performed for district associations.

Noninterest Expenses

Noninterest expenses totaled $40,616 for 2006, an increase of $5,433, or 15.4 percent, from 2005. This increase was primarily due to a $2,309 increase in salaries and employee benefits, a $1,969 increase in premiums to the Farm Credit System Insurance Corporation (FCSIC or Insurance Fund), a $605 increase in occupancy and equipment expenses, and $1,330 increase in other operating expenses. The effect of these increases was offset by a $761 decrease in intra-System financial assistance, and a $19 increase in net gains on other property owned.

The increase in salaries and employee benefits was due to a $1.7 million increase in compensation and related payroll taxes and to an $890 increase in retirement and pension expenses, partially offset by a $284 decrease in other employee benefits. Increases in compensation and related payroll taxes were primarily related to an increase in compensation rates and a slight increase in number of the bank's employees. The increase in retirement and pension expenses was primarily related to an increase in contributions to the district's defined benefit pension plan. The decrease in other employee benefits was attributable to changes in coverage of post-retirement plans designed to control costs for those benefits.

Insurance Fund premiums increased due to an increase in the premium rates charged by the FCSIC and to increases in the volume of loans on which those premiums are based.

The increase in other operating expenses included an $826 increase in advertising and member relations expenses, a $292 increase in travel-related expenses, a $271 increase in communications expenses, a $224 increase in supervisory and examination expenses, and a $191 increase in fees paid on participation loans.

Intra-System financial assistance decreased due to the maturity and retirement of all remaining debt issuances during 2005.

Noninterest expenses for 2005 totaled $35,183, a decrease of $7,256, or 17.1 percent, over 2004. This decrease was primarily due to a $6,815 decrease in salaries and employee benefits, a $612 decrease in occupancy and equipment expenses, and a $192 decrease in other operating expenses. The effect of these decreases was offset by a $363 increase in intra-System financial assistance. The decrease 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, which resulted from a change in methodology followed by the bank, and a decrease in pension and retirement expenses of $305, offset by an increase in compensation and related payroll taxes of $754 and an increase in employee medical and other benefits of $491. Occupancy and equipment declined as a result of the cost, in 2004, 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 decrease in other operating expenses was primarily due to nonrecurring costs of $1,949 incurred during 2004 related to the sale of the bank's old headquarters building and a decrease of $629 in assessments from the Farm Credit Banks Funding Corporation (Funding Corporation), significantly offset by a $1.1 million increase in professional and contract services, a $489 decrease in net gains on other property owned, a $263 increase in premiums paid to the FCSIC, a $102 increase in travel expenses, and an $86 increase in advertising and member relations. The increase in professional fees and services was primarily related to services related to district compliance with System governance and controls initiatives as well as to another System bank for the use of their capital markets loan accounting system and their payroll and human resources system. Premiums to the intra-System financial assistance expense for 2005 included the maturity and retirement of the last of the remaining issuances of debt obligations at the end of the second quarter of 2005. All existing issuances of intra-System financial assistance have matured and been extinguished.

Operating expense (salaries and employee benefits, occupancy and equipment, Insurance Fund premiums and other operating expenses) statistics are set forth below for each of the three years ended December 31,

	2006	2005	2004
Excess of net interest income over operating expense	**$ 49,677**	$41,509	$24,104
Operating expense as a percentage of net interest income	**45.0%**	45.4%	63.8%
Operating expense as a percentage of net interest income and noninterest income	**37.6**	37.3	52.2
Operating expense as a percentage of average loans	**0.44**	0.46	0.68
Operating expense as a percentage of average earning assets	**0.33**	0.36	0.54

The bank's operating expense statistics reflect the effects of dramatic growth in the earning assets and is due primarily to the growth in the loan portfolio and, to a lesser extent, to the increase in the bank's operating expenses. The bank's net interest income has increased 18.9 percent and 13.9 percent for the years ended December 31, 2006 and 2005, respectively, while operating expenses increased 18.0 percent in 2006 and decreased 19.1 percent in 2005. Operating expense for 2004 included the $7.8 million liability for non-pension postretirement benefits.

CORPORATE RISK PROFILE

Overview

The bank is in the business of making agricultural and other loans that requires us to take certain risks in exchange for compensation for the risks undertaken. Management of risks inherent in our business is essential for our current and long-term financial performance. Our goal is to mitigate risk, where appropriate, and to properly and effectively identify, measure, price, monitor and report risks in our business activities.

The major types of risk to which we have exposure are:

- **structural risk** — risk inherent in our business and related to our structure (an interdependent network of lending institutions),
- **credit risk** — risk of loss arising from an obligor's failure to meet the terms of its contract or failure to perform as agreed,
- **interest rate risk** — risk that changes in interest rates may adversely affect our operating results and financial condition,
- **liquidity risk** — risk of loss arising from the inability to meet obligations when they come due without incurring unacceptable losses,
- **operational risk** — risk of loss resulting from inadequate or failed internal processes or systems, errors by employees or external events, and
- **political risk** — risk of loss of support for the System and agriculture by the federal and state governments.

Structural Risk Management

Structural risk results from the fact that the bank, along with its related associations, is part of the Farm Credit System (System), which is comprised of banks and associations that are cooperatively owned, directly or indirectly, by their borrowers. While System institutions are financially and operationally interdependent, this structure at times requires action by consensus or contractual agreement. Further, there is structural risk in that only the banks are jointly and severally liable for the payments of Systemwide debt securities. Although capital at the association level reduces a bank's credit exposure with respect to its direct loans to its affiliated associations, this capital may not be available to support the payment of principal and interest on Systemwide debt securities.

In order to mitigate this risk, we utilize two integrated contractual agreements — the Amended and Restated Contractual Interbank Performance Agreement, or CIPA, and the Amended and Restated Market Access Agreement, or MAA. Under provisions of the CIPA, a score is calculated that measures the financial condition and performance of each district using various ratios that take into account the district's and bank's capital, asset quality, earnings, interest-rate risk and liquidity. Based on these measures, the CIPA establishes an agreed-upon standard of financial condition and performance that each district must achieve and maintain.

Periodically, the ratios in the CIPA model are reviewed, with the assistance of an independent party, to take into consideration current performance standards in the financial services industry. In connection with the most recent review, effective January 1, 2005, certain ratios were revised to better reflect improved financial condition and performance in the financial services industry. In addition, the agreed-upon financial condition and performance standard was revised to conform to the trigger points in the MAA. The CIPA also establishes economic incentives whereby monetary penalties are applied if the performance standard is not met. These penalties will occur at the same point at which a bank would be required to provide additional monitoring information under the MAA.

The MAA establishes criteria and procedures for the banks, which are jointly and severally liable for the payment of Systemwide debt securities, that provide operational oversight and control over a bank's access to System funding if the creditworthiness of the bank declines below certain agreed-upon levels. The MAA promotes the identification and resolution of individual bank financial problems in a timely manner and discharges the Funding Corporation's statutory responsibility for determining conditions of participation for each bank's participation in each issuance of Systemwide debt securities.

Under the MAA, if certain financial criteria are not met, a bank may be placed in one of three categories, each of which imposes certain requirements and/or restrictions on the affected bank. The criteria under the MAA are the CIPA scores, the net collateral ratio and the permanent capital ratio of a bank. The bank net collateral ratio is net collateral (primarily earning assets) divided by total liabilities, and the bank permanent capital ratio is primarily the bank's common and preferred stock and surplus divided by risk-adjusted assets. The criteria for the net collateral ratio and the permanent capital ratio are:

	Net Collateral Ratio	Permanent Capital Ratio
Category I	<104%	<8.0%
Category II	<103%	<7.0%
Category III	<102%	<5.0%

The categories are progressively more restrictive: a "Category I" bank is subject to additional monitoring and reporting requirements; a "Category II" bank's ability to participate in issuances of Systemwide debt securities may be curtailed; and a "Category III" bank may not be permitted to participate in issuances of Systemwide debt securities.

During the three years ended and as of December 31, 2006, all banks met the agreed-upon standard of financial condition and performance required by the CIPA and none of the banks were placed in any of the three categories designated for banks failing to meet the MAA's specified financial criteria.

Credit Risk Management

Credit risk arises from the potential inability of an obligor to meet its repayment obligation and exists in our outstanding loans, letters of credit, unfunded loan commitments, investment portfolio and derivative counterparty credit exposures. We manage credit risk associated with our retail lending activities through an assessment of the credit risk profile of an individual borrower. We set our own underwriting standards and lending policies, approved by the board of directors, that provides direction to loan officers. Underwriting standards include, among other things, an evaluation of:

- **character** — borrower integrity and credit history,
- **capacity** — repayment capacity of the borrower based on cash flows from operations or other sources of income,
- **collateral** — protects the lender in the event of default and represents a potential secondary source of loan repayment,
- **capital** — ability of the operation to survive unanticipated risks, and
- **conditions** — intended use of the loan funds.

The retail credit risk management process begins with an analysis of the borrower's credit history, repayment capacity and financial position. Repayment capacity focuses on the borrower's ability to repay the loan based on cash flows from operations or other sources of income, including non-farm income. Real estate mortgage loans must be secured by first liens on the real estate (collateral). As required by Farm Credit Administration regulations, each institution that makes loans on a secured basis must have collateral evaluation policies and procedures. Real estate mortgage loans may be made only in amounts up to 85 percent of the original appraised value of the property taken as security or up to 97 percent of the appraised value if guaranteed by a state, federal or other governmental agency. The actual loan to appraised value when loans are made is generally lower than the statutory maximum percentage. Appraisals are required for loans of more than $250,000. In addition, each loan is assigned a credit risk rating based on the underwriting standards. This credit risk rating process incorporates objective and subjective criteria to identify inherent strengths and weaknesses and risks in a particular relationship.

This credit risk rating process uses a two-dimensional loan rating structure, incorporating a 14-point risk-rating scale to identify and track the probability of borrower default and a separate scale addressing loss given default. The loan rating structure calculates estimates of loss through two components, borrower risk and transaction risk. Borrower risk is the risk of loss driven by factors intrinsic to the borrower. The transaction risk or facility risk is related to the structure of a credit (tenor, terms and collateral). This 14-point scale provides for nine "acceptable" categories, one "other assets especially mentioned" category, two "substandard" categories, one "doubtful" category and one "loss" category.

By buying and selling loans or interests in loans to or from other institutions within the System or outside the System, we limit our exposure to either a borrower or commodity concentration. This also allows us to manage growth and capital, and to improve geographic diversification.

Portfolio credit risk is also evaluated with the goal of managing the concentration of credit risk. Concentration risk is reviewed and measured by industry, product, geography and customer limits.

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 $10.055 billion at December 31, 2006, reflected an increase of $1.574 billion, or 18.5 percent, from December 31, 2005. The balance of $8.482 billion at December 31, 2005, reflected an increase of $1.564 billion, or 22.6 percent, from the $6.918 billion balance at December 31, 2004.

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

	December 31,		
	2006	2005	2004
Direct notes receivable from district associations and OFIs	**78.6%**	84.1%	88.3%
Participations purchased	**21.1**	15.5	10.9
Other loans	**0.3**	0.4	0.8
Total	**100.0%**	100.0%	100.0%

Bank credit quality has remained strong during the past three years, with all association and OFI direct notes rated (under the Farm Credit Administration's Uniform Loan Classification System) as "acceptable" or "other assets especially mentioned" during this period. Credit quality for all loans other than direct notes to associations and OFIs classified as "acceptable" or "other assets especially mentioned" as a percentage of total loans and accrued interest receivable was 98.9, 98.5 and 98.6 percent at December 31, 2006, 2005 and 2004, respectively.

While loan participations purchased made up only 21.1 percent of the bank's total loans at December 31, 2006, the bank has continued its initiative to increase the size of its participations portfolio. To this end, in 2006, the bank sold, at par, an additional $1.0 billion of participations in four of its direct notes receivable from associations to another System bank, for a total of $1.4 billion. The purpose of the sales was to diversify the credit exposure of the bank by providing capital for liquidity and expansion of the capital markets loan participations portfolio.

Association Direct Notes

As the preceding table illustrates, 78.6 percent of the bank's portfolio consisted of direct notes from associations and OFIs at December 31, 2006. 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 annually by the bank and are currently deemed adequate to absorb most interest-related shocks. 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.

District associations have experienced significant loan growth over the last three years. The district's loan growth is attributed to increased focus on market share and opportunities within the territory, competitive pricing offered by the bank and associations, increased marketing and customer service efforts by the associations, and continued activity in loan participations with district and outside entities. 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	**2006**	2005	2004
Livestock	**38%**	40%	41%
Crops	**13**	15	16
Timber	**12**	13	11
Cotton	**5**	7	8
Poultry	**4**	4	5
Dairy	**4**	2	2
Rural home	**1**	1	1
Other	**23**	18	16
Total	**100%**	100%	100%

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,		
	2006	2005	2004
Texas	**70%**	73%	71%
Alabama	**11**	10	10
Louisiana	**9**	8	8
Mississippi	**8**	8	9
New Mexico	**2**	1	2
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 18.7 percent of the district's loan volume outstanding. Approximately 55.3 percent of district loans outstanding are made up of loans of $1,000 or less, and loans less than $250 make up approximately 30.8 percent of outstanding loan volume.

Credit quality at the district's associations at December 31, 2006, 2005 and 2004 remained strong, with greater than 97 percent classified as "acceptable" or "other assets especially mentioned" as a percentage of total loans for each of the three year-ends. Association non-earning assets as a percentage of total loans at December 31, 2006, were 0.4 percent, compared to 0.4 percent and 0.5 percent at December 31, 2005 and 2004, respectively.

High-Risk Assets

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

	2006	2005	2004
Nonaccrual loans	**$ 3,713**	$ 3,542	$ 2,325
Formally restructured loans	**885**	908	618
Loans past due 90 days or more and still accruing interest	**—**	147	206
Total	**$ 4,598**	$ 4,597	$ 3,149

High-risk assets increased by $1 from December 31, 2005, to $4,598 at December 31, 2006. The increase in nonaccrual loans is attributable to the addition during 2006 of $1.3 million in one participation loan, offset by repayments and reductions on other nonaccrual loans. At December 31, 2006, $3,671, or 98.9 percent, of loans classified as nonaccrual were current as to principal and interest, compared to $3,416 (96.4 percent) and $1,726 (74.2 percent) at December 31, 2005 and 2004, respectively.

Allowance for Loan Losses

The allowance for loan losses at December 31, 2006, was $142, compared to $142 and $239 at December 31, 2005 and 2004, respectively. Because analysis indicates that an allowance on the association direct notes is not warranted, the entire balance of the allowance for loan losses reflects reserves for risks identified in the bank's participations and other loan portfolios.

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

	2006	2005	2004
Allowance for loan losses as a percentage of:			
Average loans	**<0.01%**	<0.01%	<0.01%
Loans at year end			
Total loans	**<0.01**	<0.01	<0.01
Participations	**<0.01**	0.01	0.03
Nonaccrual loans	**3.82**	4.01	10.28
Total high-risk loans	**3.09**	3.09	7.59
Net charge-offs to average loans	**0.03**	<0.01	0.03
Provision (negative provision) expense to average loans	**0.03**	<0.01	(0.13)

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

Interest Rate Risk Management

Asset/liability management is the bank's process for directing and controlling the composition, level and flow of funds related to the district's interest-rate-sensitive assets and liabilities. Management's objective is to generate adequate and stable net interest income in a changing interest rate environment.

The bank uses a variety of techniques to manage the district's financial exposure to changes in market interest rates. These include monitoring the difference in the maturities or repricing cycles of interest-rate-sensitive assets and liabilities; monitoring the change in the market value of interest-rate-sensitive assets and liabilities under various interest rate scenarios; and simulating changes in net interest income under various interest rate scenarios.

The interest rate risk inherent in a district association's loan portfolio is substantially mitigated through its funding relationship with the bank. The bank manages interest rate risk through its direct loan pricing and asset/liability management process. Under the Farm Credit Act of 1971, as amended, a district association is obligated to borrow only from the bank unless the bank approves borrowing from other funding sources. 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 of its loan advances to association members.

The bank's net interest income is determined by the difference between income earned on loans and investments and the interest expense paid on funding sources, typically Systemwide bonds, medium-term notes and discount notes. The bank's level of net interest income is affected by both changes in market interest rates and timing differences in the maturities or repricing cycles of interest-rate-sensitive assets and liabilities. Depending upon the direction and magnitude of changes in market interest rates, the bank's net interest income may be affected either positively or negatively by the mismatch in the maturity or the repricing cycle of interest-rate-sensitive assets and liabilities.

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 manage the balance sheet composition by using various debt issuance strategies and hedging transactions to match its asset structure. Management's objective is to maintain adequate and stable net interest income in any interest rate environment.

FCBT maintains a loan pricing perspective that loan rates should be based on competitive market rates of interest. The district associations offer a wide variety of products, including LIBOR- and prime-indexed variable-rate loans and loans with 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.

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 wide 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, 2006, which are expected to mature or reprice in each of the future time periods shown:

INTEREST RATE GAP ANALYSIS

as of December 31, 2006

	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	$ 4,229,714	$ 1,324,370	$ 645,323	**$ 6,199,407**	$ 2,784,458	$ 1,071,563	**$ 10,055,428**
Total investments	1,006,435	182,376	188,838	**1,377,649**	1,138,340	245,483	**2,761,472**
Total interest-earning assets	5,236,149	1,506,746	834,161	**7,577,056**	3,922,798	1,317,046	**12,816,900**
Interest-Bearing Liabilities							
Total interest-bearing funds*	5,562,782	685,000	465,000	**6,712,782**	3,638,000	1,770,001	**12,120,783**
Excess of interest-earning assets over interest-bearing liabilities	—	—	—	**—**	—	696,117	**696,117**
Total interest-bearing liabilities	5,562,782	685,000	465,000	**6,712,782**	3,638,000	2,466,118	**$ 12,816,900**
Interest rate sensitivity gap	$ (326,663)	$ 821,746	$ 369,161	**$ 864,274**	$ 284,798	$ (1,149,072)	
Cumulative interest rate sensitivity gap	$ (326,633)	$ 495,113	$ 864,274	**$ 864,274**	$ 1,149,072		

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

The amount of assets or liabilities shown in each of the time periods was 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 positive gap position, indicating that the bank has an exposure to decreasing interest rates. This would occur when income on interest-earning assets decreases due to their maturing or repricing cycle sooner than maturing or repricing debt is replaced with debt at a lower cost. The cumulative gap, which is a static measure, does not take into consideration the options available to the bank in order to manage this exposure, specifically the ability to exercise options on callable debt and replace it with lower-priced debt. These options are considered when projecting the effects of interest rate changes on net income and on the market value of equity in the following tables.

To reflect the expected cash flow and repricing characteristics of the bank's balance sheet, an estimate of expected prepayments on loans is used to adjust 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 multiple interest rate scenarios. The bank's policy guideline for the maximum negative impact to the bank's net interest income is 16 percent for a 200 basis point change in interest rates. The bank manages its interest rate risk exposure well within this guideline. As of December 31, 2006, projected annual net interest income of the existing interest-earning assets and interest-bearing liabilities would increase by $2,685, or 2.5 percent, if interest rates were to increase by 200 basis points, and would increase by $31,516, or 29.4 percent, if interest rates were to decrease by 200 basis points. Favorable results in an interest rate decrease scenario are basically provided by the effects of the call options on debt mentioned previously.

Utilizing simulation analysis, the bank projects net interest income and market value of equity 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, 2006, based on the bank's interest-earning assets and interest-bearing liabilities at December 31, 2006.

Net Interest Income

Scenario	Net Interest Income	% Change
400 BP Shock	$ 107,706	0.37%
200 BP Shock	109,997	2.50
0 BP	107,312	—
- 200 BP Shock	138,828	29.37

Market Value of Equity

Scenario	Assets	Liabilities	Equity	% Change
Book value	$ 12,915,760	$12,251,539	$ 664,221	21.95%
+ 200 BP Shock	12,362,188	11,888,151	474,037	(12.97)
0 BP Shock	12,790,940	12,246,273	544,667	—
- 200 BP Shock	13,068,477	12,512,885	555,592	2.01

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. 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, 2006, the bank had fair value hedges outstanding with a notional amount of $440 million and a negative fair value of $3.5 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 in the bank's transactions and monitors the credit ratings of all counterparties with whom it transacts. The bank's activity in derivative financial instruments for 2006 is summarized in the table below:

Activity in Derivative Financial Instruments
(Notional Amounts)

(in millions)	
Balance, December 31, 2005	$ 977
Additions	175
Maturities/calls	(702)
Terminations	(10)
Balance, December 31, 2006	**$ 440**

Liquidity Risk Management

The bank's liquidity risk management practices ensure the district's ability to meet its financial obligations. These obligations include the repayment of Systemwide debt securities as they mature, the ability to fund new and existing loan and other funding commitments, and the ability to fund operations in a cost-effective manner. A primary objective of liquidity risk management is to plan for unanticipated changes in the capital markets.

Funding Sources

Our primary source of liquidity is the ability to issue Systemwide debt securities, which are the general unsecured joint and several obligations of the System banks. We continually raise funds to support our mission to provide credit and related services to the rural and agricultural sectors, repay maturing Systemwide debt securities, and meet other obligations. As a government-sponsored enterprise, we have had access to the nation's and world's capital markets. This access has provided us with a dependable source of competitively priced debt that is critical to support our mission of providing funding to the rural and agricultural sectors. Moody's Investors Service and Standard & Poor's rate the System's long-term debt as Aaa and AAA, and our short-term debt as P-1 and A-1+. These rating agencies base their ratings on many quantitative and qualitative factors, including the System's government-sponsored enterprise status. Material changes to the factors considered could result in a different debt rating. However, as a result of the System's financial performance, credit quality and standing in the capital markets, we anticipate continued access to funding necessary to support System needs. The U.S. government does not guarantee, directly or indirectly, Systemwide debt securities.

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, 2006, the bank had excess collateral of $666.8 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:

	December 31,		
(dollars in millions)	**2006**	2005	2004
Bonds and term notes outstanding	**$ 11,354**	$ 9,155	$ 7,500
Average effective interest rate	**5.04%**	4.13%	2.89%
Average remaining life (years)	**2.7**	1.8	1.6
Discount notes outstanding	**$ 767**	$ 1,408	$ 733
Average effective interest rates	**5.23%**	4.11%	1.96%
Average remaining life (days)	**29**	35	20

	For the years ended December 31,		
	2006	2005	2004
Average interest-bearing liabilities outstanding	**$ 11,482**	$ 8,978	$ 7,352
Average interest rates on interest-bearing liabilities	**4.90%**	3.52%	2.15%

The bank had no commercial bank lines of credit in use at December 31, 2006.

Liquidity Standard

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 securities provide a stable source of income for the bank, and their high quality ensures the portfolio can quickly be converted to cash should the need arise.

The System banks have jointly developed and adopted a common minimum liquidity standard (standard). This standard is designed to maintain and assure adequate liquidity to meet the business and financial needs of each bank and the System. The standard requires each bank to maintain a minimum of 90 days of liquidity on a continuous basis, assuming no access to the capital markets. The number of days of liquidity is calculated by comparing maturing Systemwide debt securities and other bonds with the total amount of cash, investments and other liquid assets maintained by the bank. For purposes of calculating liquidity, liquid assets are subject to discounts that reflect potential exposure to adverse market value changes that might be recognized upon liquidation or sale. At December 31, 2006, the bank had 151 days of liquidity coverage, as compared with 138 days at December 31, 2005.

Investments

As permitted under FCA regulations, a bank is authorized to hold eligible investments (including federal funds) for the purposes of maintaining a diverse source of liquidity, profitably managing short-term surplus funds, and managing interest rate risk. During 2005, the FCA approved a rule that increased the amount of eligible investments a bank is authorized to hold to an amount not to exceed 35 percent of loans outstanding from the previous percentage of 30 percent. FCA regulations also permit an association to hold eligible investments with the approval of its affiliated bank.

In addition, the System has initiated mission-related investment programs, approved by the FCA, whereby banks and associations may make investments that further the System's mission to serve rural America. These investments are not included in the banks' liquidity calculations and are not covered by the limitations discussed above. Mortgage-backed securities issued by the Federal Agricultural Mortgage Corporation ("Farmer Mac") are also excluded from the limitation and the banks' liquidity calculations.

FCA regulations also define eligible investments by specifying credit rating criteria, final maturity limit and percentage of investment portfolio limit for each investment type. Generally, the banks' investments must be highly rated by a Nationally Recognized Statistical Rating Organization, such as Moody's Investors Service or Standard & Poor's. A bank must dispose of an investment that becomes ineligible within six months, unless the FCA grants permission to divest the instrument over a longer period of time.

As of December 31, 2006, the bank's investment portfolio consisted of the following:

	Amount	**Percent of Total**
Mortgage-backed securities	$ 1,921,980	70%
Asset-backed securities	384,035	14
Corporate debt	234,878	8
Money market instruments	131,349	5
Total investment securities	2,672,242	97
Overnight investments	89,229	3
Total	$ 2,761,471	100%

Capital Adequacy

Total shareholders' equity at December 31, 2006, was $664,221, compared to $624,307 and $501,431 at December 31, 2005 and 2004, respectively. The increase during 2006 was due primarily to net income of $65.0 million, $26.0 million in capital stock issued and $4.7 million in increases to accumulated other comprehensive income, offset by patronage of $37.0 million, dividends paid on preferred stock totaling $15.1 million, and the retirement of $3.6 million of allocated retained earnings. The bank's $37.0 million in declared patronage included $24.7 million in direct loan patronage, $5.6 million patronage on certain participations and $6.9 million patronage based on the associations' and OFIs' stock investment in the bank.

Accumulated other comprehensive loss decreased $4.7 million, or 17.8 percent, to $21.5 million at December 31, 2006, from $26.1 million at December 31, 2005, due to a reduction of $5.7 million in unrealized net losses on the bank's investments and a decrease of $1.0 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 $1.0 million decrease of unrealized gains on cash flow hedges is the result of the maturity of those hedges during 2006. At December 31, 2006, the bank held no cash flow hedges.

In 2006, the bank sold an additional $1.0 billion of participations in four of its direct notes receivable from district associations to another System bank. The purpose of these sales was to diversify the credit exposure of the bank by providing capital for liquidity and expansion of the capital markets loan participation portfolio.

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,

	2006	2005	2004	Regulatory Minimum
Permanent capital ratio	**13.67%**	17.36%	19.82%	7.00%
Total surplus ratio	**11.61**	14.97	16.55	7.00
Core surplus ratio	**6.93**	8.82	11.51	3.50
Collateral ratio	**105.35**	105.90	105.69	103.00

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

Operational Risk Management

Operational risk is the risk of loss resulting from inadequate or failed processes or systems, human factors or external events, including the execution of unauthorized transactions by employees, errors relating to transaction processing and technology, breaches of the internal control system and the risk of fraud by employees or persons outside the System. The board of directors is required, by regulation, to adopt an internal control policy that provides adequate direction to the institution in establishing effective control over and accountability for operations, programs and resources. The policy must include, at a minimum, the following items:

- direction to management that assigns responsibility for the internal control function to an officer of the institution,
- adoption of internal audit and control procedures,
- direction for the operation of a program to review and assess its assets,
- adoption of loan, loan-related assets and appraisal review standards, including standards for scope of review selection and standards for work papers and supporting documentation,
- adoption of asset quality classification standards,
- adoption of standards for assessing credit administration, including the appraisal of collateral, and
- adoption of standards for the training required to initiate a program.

In general, we address operational risk through the organization's internal framework under the supervision of the internal auditors. Exposure to operational risk is typically identified with the assistance of senior management, and internal audit plans are developed with higher risk areas receiving more review.

Political Risk Management

We, as part of the System, are an instrumentality of the federal government and are intended to further governmental policy concerning the extension of credit to or for the benefit of agricultural and rural America. The System and its borrowers may be significantly affected by federal legislation that affects the System directly, such as changes to the Farm Credit Act, or indirectly, such as agricultural appropriations bills. Political risk to the System is the risk of loss of support for the System or agriculture by the U.S. government.

We manage political risk by actively supporting The Farm Credit Council, which is a full-service, federal trade association representing the System before Congress, the Executive Branch and others. The council provides the mechanism for "grassroots" involvement in the development of System positions and policies with respect to federal legislation and government actions that impact the System. Additionally, we take an active role in representing the individual interests of System institutions and their borrowers before Congress. In addition to The Farm Credit Council, each district has its own council, which is a member of The Farm Credit Council. The district councils represent the interests of their members on a local and state level, as well as on a federal level.

Regulatory Matters

During the year ended December 31, 2006, the FCA took no enforcement actions against the bank or its related associations, and there were no enforcement actions in effect for the bank or its related associations at December 31, 2006.

Report of Audit Committee

The Audit Committee (committee) is composed of the entire board of directors of the Farm Credit Bank of Texas (bank). The committee oversees the scope of the bank's system of internal controls and procedures, and the adequacy of management's action with respect to recommendations arising from those internal control activities. The committee's approved responsibilities are described more fully in the Audit Committee Charter, which is available on request or on the bank's Web site at www.farmcreditbank.com. In 2006, six committee meetings were held. At the first of their meetings, the committee approved the appointment of PricewaterhouseCoopers LLP (PwC) independent auditors for 2006.

Management is responsible for the bank's internal controls and for the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America. PwC is responsible for performing an independent audit of the bank's financial statements in accordance with auditing standards generally accepted in the United States of America and to issue a report thereon. The committee's responsibilities include monitoring and overseeing these processes.

In this context, the committee reviewed and discussed the bank's audited financial statements for the year ended December 31, 2006 (Audited Financial Statements) with management and PwC. The committee also reviewed with PwC the matters required to be discussed by Statement on Auditing Standards No. 61, as amended (Communications With Audit Committees), and both PwC and the bank's internal auditors directly provided reports on significant matters to the Committee.

The committee discussed with appropriate representatives of PwC the firm's independence from the bank. The committee also reviewed the non-audit services provided by PwC and concluded that these services were not incompatible with maintaining the independent accountant's independence. Furthermore, throughout 2006 the committee has discussed with management and PwC such other matters and received such assurances from them as the committee deemed appropriate.

William F. Staats, Chairman
James F. Dodson, Vice Chairman
C. Kenneth Andrews
Ralph W. Cortese
Joe R. Crawford
Elizabeth G. Flores
Jon M. Garnett

Audit Committee Members

March 1, 2007

Report of Independent Auditors

PRICEWATERHOUSECOOPERS

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

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, of 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, 2006, 2005 and 2004, and the results of its operations 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 1, 2007

BALANCE SHEETS

Farm Credit Bank of Texas

(in thousands)	**2006**	December 31, 2005	2004
Assets			
Cash	**$ 14,165**	$ 4,392	$ 3,614
Federal funds sold and overnight investments	**89,229**	42,444	47,500
Investment securities	**2,672,242**	2,697,876	1,787,706
Loans	**10,055,428**	8,481,501	6,918,236
Less allowance for loan losses	**142**	142	239
Net loans	**10,055,286**	8,481,359	6,917,997
Accrued interest receivable	**63,967**	43,994	26,032
Premises and equipment, net	**2,286**	2,489	2,416
Other assets	**18,585**	12,234	15,940
Total assets	**$ 12,915,760**	$ 11,284,788	$ 8,801,205
Liabilities and Shareholders' Equity			
Liabilities			
Bonds and notes, net	**$ 12,120,783**	$ 10,563,278	$ 8,232,533
Accrued interest payable	**96,550**	60,113	36,850
Other liabilities	**34,206**	37,090	30,391
Total liabilities	**12,251,539**	10,660,481	8,299,774
Commitments and contingencies (Note 12)			
Shareholders' Equity			
Preferred stock	**200,000**	200,000	100,000
Capital stock	**161,421**	135,390	118,323
Allocated retained earnings	**6,194**	8,742	9,980
Unallocated retained earnings	**318,076**	306,305	280,686
Accumulated other comprehensive loss	**(21,470)**	(26,130)	(7,558)
Total shareholders' equity	**664,221**	624,307	501,431
Total liabilities and shareholders' equity	**$ 12,915,760**	$ 11,284,788	$ 8,801,205

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

STATEMENTS OF INCOME

Farm Credit Bank of Texas

(*in thousands*)	Year Ended December 31, 2006	2005	2004
Interest Income			
Investment securities and other	**$ 141,260**	$ 76,735	$ 48,621
Loans	**511,297**	315,491	175,907
Total interest income	**652,557**	392,226	224,528
Interest Expense			
Bonds and notes	**562,211**	316,201	157,818
Notes payable and other	**5**	65	48
Total interest expense	**562,216**	316,266	157,866
Net Interest Income	**90,341**	75,960	66,662
Provision (negative provision) for loan losses	**2,578**	(344)	(7,878)
Net interest income after provision for loan losses	**87,763**	76,304	74,540
Noninterest Income			
Fees for services to associations	**8,856**	8,619	8,744
Fees for loan-related services	**5,656**	5,993	3,817
Gain from sale of investment securities	**907**	—	420
Miscellaneous income, net	**2,428**	1,883	1,900
Total noninterest income	**17,847**	16,495	14,881
Noninterest Expenses			
Salaries and employee benefits	**20,182**	17,873	24,688
Occupancy and equipment	**4,550**	3,945	4,557
Insurance Fund premiums	**2,548**	579	315
Gains on other property owned	**(48)**	(29)	(517)
Intra-System financial assistance expenses	**—**	761	398
Other operating expenses	**13,384**	12,054	12,998
Total noninterest expenses	**40,616**	35,183	42,439
Net Income	**$ 64,994**	$ 57,616	$ 46,982

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	Retained Earnings Allocated	Retained Earnings Unallocated	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at December 31, 2003	$ 100,000	$ 109,787	$ 14,237	$ 258,054	$ (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 hedge 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	100,000	118,323	9,980	280,686	(7,558)	501,431
Comprehensive income						
Net income	—	—	—	57,616	—	57,616
Unrealized net losses on investment securities	—	—	—	—	(18,310)	(18,310)
Unrealized net losses on cash flow hedge derivatives	—	—	—	—	(262)	(262)
Total comprehensive income	—	—	—	57,616	(18,572)	39,044
Preferred stock issued	100,000	—	—	—	—	100,000
Premium received on preferred stock net of issuance costs	—	—	—	6,773	—	6,773
Capital stock issued	—	17,170	—	—	—	17,170
Capital stock and allocated retained earnings retired	—	(103)	(2,075)	—	—	(2,178)
Cash dividends – preferred stock	—	—	—	(9,220)	—	(9,220)
Patronage						
Cash	—	—	—	(28,713)	—	(28,713)
Shareholders' equity	—	—	837	(837)	—	—
Balance at December 31, 2005	200,000	135,390	8,742	306,305	(26,130)	624,307
Comprehensive income						
Net income	—	—	—	64,994	—	64,994
Net change in unrealized net losses on investment securities	—	—	—	—	5,707	5,707
Net change in unrealized net gains on cash flow hedge derivatives	—	—	—	—	(1,047)	(1,047)
Total comprehensive income	—	—	—	64,994	4,660	69,654
Capital stock issued	—	26,031	—	—	—	26,031
Capital stock and allocated retained earnings retired	—	—	(3,606)	—	—	(3,606)
Cash dividends – preferred stock	—	—	—	(15,122)	—	(15,122)
Patronage						
Cash	—	—	—	(37,043)	—	(37,043)
Shareholders' equity	—	—	1,058	(1,058)	—	—
Balance at December 31, 2006	**$ 200,000**	**$ 161,421**	**$ 6,194**	**$ 318,076**	**$ (21,470)**	**$ 664,221**

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, 2006	2005	2004
Cash Flows From Operating Activities			
Net income	**$ 64,994**	$ 57,616	$ 46,982
Reconciliation of net income to net cash provided by operating activities			
Provision (negative provision) for loan losses	**2,578**	(344)	(7,878)
Provision for losses on other property owned	**—**	—	39
Depreciation on premises and equipment	**793**	645	655
Accretion of net discount on loans	**(187)**	(372)	(210)
Amortization and accretion on debt instruments	**(660)**	7,776	(4,404)
Accretion of net (discount) premium on investments	**3,626**	7,009	(3,466)
Gain on sale of investment securities	**(907)**	—	(420)
(Gains) losses on sales of other property owned, net	**(48)**	36	(511)
Loss from sales of premises and equipment	**12**	5	14
Increase in accrued interest receivable	**(19,973)**	(17,962)	(6,838)
(Increase) decrease in other assets, net	**(5,640)**	862	(9,743)
Increase in accrued interest payable	**36,437**	23,263	4,150
Decrease in intra-System financial assistance payable	**—**	—	(280)
Increase (decrease) in other liabilities, net	**3,040**	1,428	(2,708)
Net cash provided by operating activities	**84,065**	79,962	15,382
Cash Flows From Investing Activities			
Net (increase) decrease in federal funds sold and securities purchased under resale agreements	**(46,785)**	5,056	(25,700)
Investment securities			
Purchases	**(6,666,471)**	(4,653,111)	(2,938,373)
Proceeds from maturities, calls and prepayments	**6,587,280**	3,717,622	2,582,672
Proceeds from sales	**107,814**	—	85,565
Increase in loans, net	**(2,576,270)**	(1,662,682)	(1,084,814)
Proceeds from sale of loans	**1,000,000**	100,000	—
Proceeds from sales of other property owned, net	**—**	—	1,001
Proceeds from sales of premises and equipment	**59**	190	71
Expenditures for premises and equipment	**(661)**	(913)	(2,199)
Net cash used in investing activities	**(1,595,034)**	(2,493,838)	(1,381,777)
Cash Flows From Financing Activities			
Bonds and notes issued	**28,809,507**	24,454,370	92,467,455
Bonds and notes retired	**(27,261,180)**	(22,126,945)	(91,083,840)
Preferred stock issued, net of expenses	**—**	106,773	—
Capital stock issued	**26,031**	17,170	9,122
Capital stock retired and allocated retained earnings distributed	**(3,606)**	(2,178)	(4,857)
Cash dividends on preferred stock	**(15,122)**	(9,220)	(7,561)
Cash patronage distributions paid	**(34,888)**	(25,316)	(16,775)
Net cash provided by financing activities	**1,520,742**	2,414,654	1,363,544
Net increase (decrease) in cash	**9,773**	778	(2,851)
Cash at beginning of year	**4,392**	3,614	6,465
Cash at End of Year	**$ 14,165**	$ 4,392	$ 3,614
Supplemental Schedule of Noncash Investing and Financing Activities			
Net decrease (increase) in unrealized losses on investment securities	**$ 5,707**	$ (18,310)	$ (4,418)
Declared participations patronage payable	**5,551**	3,396	35
Supplemental Schedule of Noncash Changes in Fair Value Related to Hedging Activities			
Increase (decrease) in bonds and notes	**$ 9,837**	$ (2,097)	$ (17,363)
Supplemental Disclosure of Cash Flow Information			
Interest paid	**$ 525,779**	$ 297,389	$ 142,774

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 six FLCAs, 14 ACA parent associations, each containing two wholly-owned subsidiaries (an FLCA and a Production Credit Association [PCA]), certain Other Financing Institutions (OFIs), and preferred stockholders jointly owned the bank at December 31, 2006. 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. The OFIs borrow from the bank and in turn originate and service short- and intermediate term loans to their members. 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 or Insurance Fund) 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, 2006, the assets in the Insurance Fund were approximately $2.3 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.

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, 2006, 2005 and 2004. 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 other than temporary. In the event of other-than-temporary impairment, the cost basis of the investment would be written down to its fair value, and the loss would be included in current earnings. The bank may also hold additional investments in accordance with mission-related investment programs, approved by the Farm Credit Administration.

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.

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms of the loan. Impaired loans include nonaccrual loans, restructured loans, and loans past due 90 days or more and still accruing interest. A loan is considered contractually past due when any principal repayment or interest payment required by the loan instrument is not received on or before the due date. A loan shall remain contractually past due until it is formally restructured or until the entire amount past due, including principal, accrued interest and penalty interest incurred as the result of past due status, is collected or otherwise discharged in full.

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. The bank capitalizes origination fees in excess of $50 thousand and amortizes them over the lives of the related loans on a straight-line basis.

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.

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.

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, 2006, 2005 and 2004.

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

G. Employee Benefit Plans:

Substantially all employees of the bank participate in one of two districtwide retirement plans (a defined benefit plan and a defined contribution plan) and are eligible to participate in the 401(k) plan of the district. Additionally, certain qualified individuals in the bank may participate in a separate, supplemental pension plan. Within the plan, a certain percentage of employee contributions is matched by the bank. The 401(k) 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, "Accounting for Derivative Instruments and Hedging Activities," as amended, 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 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. Recently Issued Accounting Pronouncements:

In February 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 155, "Accounting for Certain Hybrid Financial Instruments – an amendment to FASB Statements 133 and 140." The primary objectives of this statement with respect to Statement 133 are 1) to simplify accounting for certain hybrid financial instruments by permitting fair value measurement and 2) eliminate the interim guidance in Statement 133 Implementation Issue D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets," which provides that beneficial interests are not subject to the provisions of Statement 133. The primary objective with respect to Statement 140 is to eliminate a restriction on the passive derivative instruments that a qualifying special-purpose entity may hold. This guidance is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The impact of adoption of the standard is not expected to have a material impact on the bank's financial position or results of operations.

On September 30, 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans." The standard requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in that funded status in the year in which the changes occur through comprehensive income. The standard is effective for employers with publicly traded securities for the fiscal year ending after December 15, 2006, and for employers without publicly traded securities for the fiscal year ending after June 15, 2007. The bank will be required to implement the standard for the year ended December 31, 2007. In addition, this standard requires that the funded status of a plan be measured as of the date of the year-end financial statements. Currently, the bank uses a measurement date of September 30. The requirement to measure the funded status as of the fiscal year-end is effective for fiscal years ending after December 15, 2008. The bank is currently evaluating the impact of implementing this standard. It is anticipated that the impact from the implementation of this standard will have no impact on the income statement and, based on the current funded status of the defined benefit plans, it is not expected to have a material or significant impact on the balance sheet.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, Fair Value Option for Financial Assets and Financial Liabilities. The standard permits entities to choose on an instrument-by-instrument basis, at specified election dates, to measure eligible items at fair value (the "fair value option"). Unrealized gains and losses on items for which the fair value option has been elected shall be reported in earnings at each subsequent reporting date. Up-front costs and fees related to items for which the fair value option is elected shall be recognized in earnings as incurred and not deferred. This standard is effective for financial statements issued for fiscal years beginning after November 15, 2007.

K. Statements of Cash Flows

In 2006 the bank revised its cash flow statement reporting for the presentation of cash flows associated with discount notes. Prior years' cash flow statements were adjusted to conform to the current year presentation. For 2005, this change reduced cash provided by operations by $22,103 and increased cash flows provided by financing activities by $22,103. For 2004, this change reduced cash provided by operations by $8,317 and increased cash flows provided by financing activities by $8,317.

Note 3 — Investment Securities

A summary of the amortized cost and estimated fair value of investment securities at December 31, 2006, 2005 and 2004, follows.

	December 31, 2006				
	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Weighted Average Yield**
Commercial paper and other	**$ 366,173**	**$ 83**	**$ (29)**	**$ 366,227**	**5.36%**
Collateralized mortgage obligations	**1,943,842**	**1,341**	**(23,203)**	**1,921,980**	**4.86**
Asset-backed securities	**383,697**	**406**	**(68)**	**384,035**	**5.60**
Total	**$ 2,693,712**	**$ 1,830**	**$(23,300)**	**$ 2,672,242**	**5.04%**

	December 31, 2005				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
Commercial paper and other	$ 550,981	$ —	$ (67)	$ 550,914	4.35%
Collateralized mortgage obligations	1,749,796	702	(27,835)	1,722,663	4.31
Asset-backed securities	424,276	118	(95)	424,299	4.62
Total	$ 2,725,053	$ 820	$(27,997)	$ 2,697,876	4.37%

	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%

A summary of contractual maturity, amortized cost, estimated fair value and weighted average yield of investment securities at December 31, 2006, follows:

	Amortized Cost	Fair Value	Weighted Average Yield
Due in one year or less	$ 276,173	$ 276,150	5.33%
Due after one year through five years	119,967	120,049	5.50
Due after five years through ten years	387,129	381,333	4.78
Due after 10 years	1,910,443	1,894,710	5.01
Total securities	$ 2,693,712	$ 2,672,242	5.04%

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, 2006, 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,		
	2006	2005	2004
Proceeds on sales	**$ 107,814**	$ —	$ 85,565
Realized gains	**907**	—	420

The net realized gain 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, 2006. 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	$ 349,048	$ (1,345)	$ 1,066,870	$ (21,858)
Commercial paper	174,795	(29)	—	—
Asset-backed securities	7,337	(1)	10,911	(67)
Total	$ 531,180	$ (1,375)	$ 1,077,781	$ (21,925)

Note 4 — Loans and Allowance for Loan Losses

Loans comprised the following categories at December 31:

	2006	2005	2004
Direct notes receivable from district associations and OFIs	**$ 7,905,292**	$ 7,128,339	$ 6,110,098
Participations purchased	**2,121,173**	1,314,500	752,549
Other loans	**28,963**	38,662	55,589
Total loans	**$ 10,055,428**	$ 8,481,501	$ 6,918,236

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	**2006**	2005	2004
Livestock	**38%**	40%	41%
Crops	**13**	15	16
Timber	**12**	13	11
Cotton	**5**	7	8
Poultry	**4**	4	5
Dairy	**4**	2	2
Rural home	**1**	1	1
Other	**23**	18	16
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, 2006, 2005 and 2004.

	December 31,		
	2006	2005	2004
Nonaccrual loans			
Current as to principal and interest	**$ 3,671**	$ 3,416	$ 1,726
Past due	**42**	126	599
Total nonaccrual loans	**3,713**	3,542	2,325
Impaired accrual loans			
Restructured accrual loans	**885**	908	618
Accrual loans 90 days or more past due	**—**	147	206
Total impaired accrual loans	**885**	1,055	824
Total impaired loans	**$ 4,598**	$ 4,597	$ 3,149
Average impaired loans	**$ 4,907**	$ 4,887	$ 8,929

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

	2006	2005	2004
Interest income recognized on nonaccrual loans	$ 1,054	$ 635	$ 1,325
Interest income on impaired accrual loans	138	84	114
Interest income recognized on impaired loans	$ 1,192	$ 719	$ 1,439

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

	2006	2005	2004
With related specific allowance	$ 2,016	$ 3,137	$ 1,286
With no related specific allowance	2,582	1,460	1,863
Total impaired loans	$ 4,598	$ 4,597	$ 3,149
Allowance on impaired loans	$ 142	$ 142	$ 239

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:

	2006	2005	2004
Interest income which would have been recognized under the original loan terms	$ 1,658	$ 1,103	$ 1,994
Less: interest income recognized	1,192	719	1,439
Foregone interest income	$ 466	$ 384	$ 555

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 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 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.

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

	December 31,		
	2006	2005	2004
Balance at beginning of year	$ 142	$ 239	$ 9,834
Provision (negative provision) for loan losses	2,578	(344)	—
Nonrecurring negative provision for loan losses	—	—	(7,878)
Loans charged off	(2,834)	—	(5,725)
Recoveries	256	247	4,008
Balance at end of year	$ 142	$ 142	$ 239

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 $256.7 million at December 31, 2006. Fees paid to Farmer Mac for such commitments are paid by the associations.

In 2006, the bank sold an additional $1.0 billion of participations in four of its direct notes receivable from district associations to another System bank for a total of $1.4 billion. The purpose of these sales was to diversify the credit exposure of the bank by providing capital for liquidity and expansion of the capital markets loan participations portfolio.

Note 5 — Premises and Equipment

Premises and equipment comprised the following at:

	December 31,		
	2006	2005	2004
Leasehold improvements	$ 937	$ 929	$ 929
Furniture and equipment	6,235	7,244	9,170
	7,172	8,173	10,099
Accumulated depreciation	(4,886)	(5,684)	(7,683)
Total	$ 2,286	$ 2,489	$ 2,416

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. Annual lease expenses for the new facility were $2.5 million, $2.3 million and $2.7 million for 2006, 2005 and 2004, respectively.

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

	Minimum Lease Payments
2007	$ 1,366
2008	1,503
2009	1,674
2010	1,776
2011	1,879
Subsequent years	3,244
Total minimum lease payments	$ 11,442

Note 6 — Other Assets and Other Liabilities

Other assets comprised the following at December 31:

	2006	2005	2004
Unamortized debt issue costs	**$ 7,318**	$ 4,316	$ 3,181
Accounts receivable	**3,551**	4,130	8,137
Investment in other System bank	**2,362**	—	—
Fair value of derivatives	**1,758**	1,047	2,469
Other, net	**3,596**	2,741	2,153
Total	**$ 18,585**	$ 12,234	$ 15,940

Other liabilities comprised the following at December 31:

	2006	2005	2004
Obligation for non-pension postretirement benefits	**$ 9,773**	$ 9,864	$ 9,634
Patronage payable	**5,551**	3,396	35
Supplemental pension	**3,701**	2,593	1,766
Fair value of derivatives	**3,459**	11,538	10,601
Accounts payable	**3,373**	3,727	2,784
FCSIC premium payable	**2,548**	579	315
Mortgage life additional reserve	**2,049**	1,749	1,757
Accrued building lease payable	**1,619**	1,410	1,098
Notes payable	**—**	1,142	1,903
Other, net	**2,133**	1,092	498
Total	**$ 34,206**	$ 37,090	$ 30,391

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, 2006, the bank had such specified eligible assets totaling $12.9 billion and obligations and accrued interest payable totaling $12.2 billion, resulting in excess eligible assets of $666.8 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, 2006, the bank was, and currently remains, in compliance with the conditions and requirements of the System banks' and the Funding Corporation's 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, 2006, 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
2007	$ 3,938.2	4.81%	$ —	—%	$ 766.9	5.23%	$ 4,705.1	4.88%
2008	2,878.2	4.95	20.0	5.56	—	—	2,898.2	4.95
2009	1,178.3	4.87	—	—	—	—	1,178.3	4.87
2010	894.5	5.14	—	—	—	—	894.5	5.14
2011	676.1	5.41	—	—	—	—	676.1	5.41
Subsequent years	1,768.6	5.64	—	—	—	—	1,768.6	5.64
Total	$ 11,333.9	5.04%	$ 20.0	5.56%	$ 766.9	5.23%	$ 12,120.8	5.05%

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, 2006, was 29 days.

The bank's Systemwide debt includes callable debt, consisting of the following at December 31, 2006 *(dollars in thousands)*:

Year of Maturity	Amount	Range of First Call Dates
2007	$ 430,000	1/1/2007
2008	595,000	1/1/2007-4/29/2007
2009	590,000	1/1/2007-12/28/2007
2010	560,000	1/1/2007-8/4/2008
2011	520,000	1/1/2007-12/29/2008
Subsequent years	1,250,000	1/1/2007-11/7/2011
Total	$ 3,945,000	1/1/2007-11/7/2011

Callable debt may be called on the first call date and, generally, every day 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 financial statements are uninsured.

The bank had no outstanding commercial bank lines of credit at December 31, 2006.

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. On September 26, 2005, the bank issued an additional 100,000 shares of Cumulative Perpetual Preferred Stock with the same terms. For regulatory purposes, the preferred stock is treated as equity, and 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. In 2006, preferred stock dividends of $15,122 were declared and paid. At December 31, 2006, accumulated dividends on the preferred stock totaled $672.

According to the bank's bylaws, the minimum and maximum stock investments that the bank may require 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 31,912 shares, 26,754 shares and 23,500 shares of Class A voting common stock issued and outstanding at December 31, 2006, 2005 and 2004, 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 373 shares, 324 shares and 164 shares of Class A nonvoting common stock issued and outstanding at December 31, 2006, 2005 and 2004, respectively.

Allocated retained earnings of $6,194 at December 31, 2006, consisted of $4,286 of patronage refunds allocated to certain PCAs, and $1,908 allocated for the payment of patronage on loans participated with another System bank. The $4,286 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.

Allocated retained earnings of $8,742 at December 31, 2005, consisted of $7,892 of patronage refunds allocated to certain PCAs, and $850 allocated for the payment of patronage on loans participated with another System bank.

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.

At December 31, the associations' investment in the bank included the following investment in common stock and allocated retained earnings:

	2006	2005	2004
Class A voting common stock – Associations	**$ 159,558**	$ 133,772	$ 117,501
Class A nonvoting common stock – Other Financing Institutions	**1,863**	1,618	822
Total common stock	**161,421**	135,390	118,323
Preferred stock	**200,000**	200,000	100,000
Allocated retained earnings			
Associations	**4,286**	7,892	9,966
Other entities	**1,908**	850	14
Total allocated retained earnings	**6,194**	8,742	9,980
Total capital stock and allocated retained earnings	**$ 367,615**	$ 344,132	$ 228,303

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 2006, $37,043 in cash patronages was declared to district associations, OFIs and other entities, compared to $28,713 in 2005 and $16,775 in 2004.

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:

	2006	2005	2004	Regulatory Minimum
Permanent capital ratio	**13.67%**	17.36%	19.82%	7.00%
Total surplus ratio	**11.61**	14.97	16.55	7.00
Core surplus ratio	**6.93**	8.82	11.51	3.50
Collateral ratio	**105.35**	105.90	105.69	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 401(k) plan.

The structure of the district's DB plan is characterized as multiemployer, 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 is 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, 2006.

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 2006) made on their behalf into various investment alternatives.

The district also participates in a districtwide 401(k) plan, which offers a pre-tax and after-tax compensation deferral feature. In 2003, the employers made contribution enhancements to employer contributions under the plan. 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. Effective January 1, 2006, the districtwide 401(k) plan was merged with the AgFirst Farm Credit Employee Thrift Plan. The new plan is known as the AgFirst/FCBT 401(k) Benefit Plan.

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

	2006	2005	2004
Pension	**$ 2,744**	$ 1,897	$ 2,196
401(k) plan	**449**	406	411
Total	**$ 3,193**	$ 2,303	$ 2,607

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	2006	2005	2004
Accumulated postretirement benefit obligation, December 31	**$ (6,580)**	$ (7,374)	$ (9,869)
Fair value of plan assets	**—**	—	287
Funded status of plan	**(6,580)**	(7,374)	(9,582)
Unrecognized net transition obligation	**—**	—	—
Unrecognized prior service cost	**(2,927)**	(3,212)	(952)
Unrecognized net loss (gain)	**(343)**	683	813
Fourth quarter contributions	**77**	39	87
Accrued postretirement benefit cost	**$ (9,773)**	$ (9,864)	$ (9,634)
Amounts Recognized in the Balance Sheets			
Accrued benefit liability	**$ (9,773)**	$ (9,864)	$ (9,634)
Contribution and benefit payments			
Employer contributions	**$ 310**	$ 528	$ 432
Participant contributions	**124**	197	
Benefits paid	**434**	955	

Weighted-Average Assumptions Used to Determine Obligations at Year End	2006	2005	2004
Measurement date	**September 30**	September 30	September 30
Discount rate	**6.00%**	5.25%	6.00%
Health care cost trend rate assumed for next year – medical (pre-/post-65)	**9.0%/6.75%**	9.5%/7.0%	11.0%/11.50%
Health care cost trend rate assumed for next year – Rx (pre-/post-65)	**13.00%**	13.5%/13.5%	11.0%/11.50%
Ultimate health care cost trend rate (pre-/post-65)	**4.75%**	4.75%/4.75%	5.00%/5.50%
Year that the rate reaches the ultimate trend rate	**2016**	2016	2012
Total Cost			
Service cost	**$ 220**	$ 286	
Interest cost	**378**	577	
Expected return on plan assets	**—**	(2)	
Amortization of:			
Unrecognized prior service cost	**(339)**	(153)	
Unrecognized net (gain) loss	**(2)**	2	
Accrued postretirement benefit cost	**$ 257**	710	

Expected Future Cash Flows	
Expected Benefit Payments (net of employee contribution):	
Fiscal 2007	**$ 359**
Fiscal 2008	**378**
Fiscal 2009	**401**
Fiscal 2010	**415**
Fiscal 2011	**431**
Fiscal 2012-2016	**2,385**
Expected Contributions:	
Fiscal 2006	**359**

At December 31, 2006, the bank had an accrued benefit liability of $9,773 on its balance sheet. The total net postretirement benefit cost for 2006 was $257, and the bank's employer contributions for 2006 totaled $310.

The September 30, 2006, valuation reflects the increase in the discount rate used to determine benefit obligations from 5.25 percent to 6.00 percent.

Note 10 — Intra-System Financial Assistance

The Farm Credit Act provided for capital assistance to System institutions experiencing severe financial stress through the issuance, prior to October 1, 1992, by the Financial Assistance Corporation of U.S. Treasury–guaranteed 15-year bonds, of which $1.261 billion in principal amount was originally issued. The last remaining Financial Assistance Corporation bonds matured and were repaid on June 10, 2005.

Pursuant to the Farm Credit Act, the U.S. Treasury paid $440 million, on behalf of the System, in interest costs on $844 million of the Financial Assistance Corporation bonds issued for purposes other than funding Capital Preservation Agreement accruals. The banks had irrevocably set aside funds, including interest earned, that totaled the $440 million needed to repay the interest advanced by the U.S. Treasury. On June 10, 2005, the banks repaid the U.S. Treasury the interest advanced. As provided in the Farm Credit Act, the Financial Assistance Corporation was dissolved effective December 31, 2006.

Note 11 — Related Party Transactions

As discussed in Note 1, "Organization and Operations," the bank lends funds to the district associations to fund their loan portfolios. Interest income recognized on direct notes receivable from district associations was $395,822, $255,902 and $147,728 for 2006, 2005 and 2004, respectively. Further disclosure regarding these related party transactions is found in Note 4, "Loans and Allowances 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, loan processing, marketing and other services. Income derived by the bank from these activities was $8,856, $8,619 and $8,744 for 2006, 2005 and 2004, 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, 2006, were approximately $133.6 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 $1.358 billion, $1.175 billion and $706.5 million at December 31, 2006, 2005 and 2004, respectively. At December 31, 2006, the bank had $95.0 million in outstanding standby letters of credit, issued primarily in conjunction with participation loans. The letters of credit are generally issued for terms up to one year or are annually renewable. The $1.1 million fair value of these obligations at December 31, 2006, is based on the fees for the unexpired period remaining and is included in other liabilities.

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, 2006, 2005 and 2004. 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, 2006		December 31, 2005		December 31, 2004	
	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	**$ 2,775,636**	**$ 2,775,636**	$ 2,744,712	$ 2,744,712	$ 1,838,820	$ 1,838,820
Loans	**10,055,428**	**9,935,881**	8,481,501	8,390,165	6,918,236	6,864,564
Allowance for loan losses	**(142)**	**—**	(142)	—	(239)	—
Loans, net	**10,055,286**	**9,935,881**	8,481,359	8,390,165	6,917,997	6,864,564
Derivative assets	**1,758**	**1,758**	1,047	1,047	2,469	2,469
Financial liabilities						
Bonds and notes	**12,124,242**	**12,121,813**	10,574,816	10,578,272	8,241,974	8,274,094
Fair value adjustment of derivatives	**(3,459)**	**(3,459)**	(11,538)	(11,538)	(9,441)	(9,441)
Total bonds and notes	**12,120,783**	**12,118,354**	10,563,278	10,566,734	8,232,533	8,264,653
Financial assistance–related liabilities	**—**	**—**	—	—	—	—
Derivative liabilities	**3,459**	**3,459**	11,538	11,538	10,601	10,601

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. Obligation 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. Derivative Assets and Liabilities:

The fair value of derivative financial instruments is the estimated amount that a bank would receive or pay to replace the instruments at the reporting date, considering the current interest rate environment and the current creditworthiness of the counterparties. Where such quoted market prices do not exist, these values are generally provided by sources outside the respective bank or by internal market valuation models.

G. 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. Fair value hedges 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 fair value hedge 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. At December 31, 2006, the bank had fair value hedges with a total notional amount of $440 million.

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, fair value hedges 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 2004 the bank entered into two cash flow hedges, with a total notional amount of $95 million, which hedge the exposure to variability in expected future cash flows that matured in 2006.

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, 2006, the bank had credit exposure totaling $1.70 million with one counterparty. The bank does not anticipate nonperformance by this counterparty. 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 bank held no cash flow hedging instruments at December 31, 2006.

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	Remaining Years to Maturity: 1 to 5 Years	Total	Maturity Distribution Netting	Exposure	Collateral Held	Exposure Net of Collateral
Standard & Poors Credit Rating							
A+	$ —	$ 1.70	$ 1.70	$ —	$ 1.70	$ —	$ 1.70

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 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, 2006 *($ in millions)*	Maturities of 2006 Derivative Products and Other Financial Instruments: 2007	2008	2009	2010	2011	Subsequent Years	Total	Fair Value
Total debt obligations:								
Fixed rate	$ 1,880	$ 1,148	$ 1,178	$ 895	$ 676	$ 1,769	$ 7,546	$ 7,543
Weighted average interest rate	4.38%	4.56%	4.87%	5.14%	5.41%	5.64%	4.06%	
Variable rate	$ 2,825	$ 1,750	$ —	$ —	$ —	$ —	$ 4,575	$ 4,575
Weighted average interest rate	5.43%	5.21%	—	—	—	—	4.28%	
Total debt obligations	$ 4,705	$ 2,898	$ 1,178	$ 895	$ 676	$ 1,769	$ 12,121	$ 12,118
Weighted average interest rate	4.88%	4.95%	4.87%	5.14%	5.41%	5.64%	4.13%	
Derivative instruments:								
Receive fixed swaps								
Notional value	$ 165	$ 100	$ 125	$ —	$ 50	$ —	$ 440	$ (2)
Weighted average receive rate	3.35%	3.83%	5.05%	—	5.50%	—	4.18%	
Weighted average pay rate	5.19%	5.18%	5.19%	—	5.19%	—	5.19%	

Note 16 — Selected Quarterly Financial Information (Unaudited)

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

	2006				
	First	**Second**	**Third**	**Fourth**	**Total**
Net interest income	**$ 22,446**	**$ 22,115**	**$ 22,231**	**$ 23,549**	**$ 90,341**
Provision for loan losses	**—**	**2,578**	**—**	**—**	**2,578**
Noninterest expense, net	**6,734**	**5,594**	**4,269**	**6,172**	**22,769**
Net income	**$ 15,712**	**$ 13,943**	**$ 17,962**	**$ 17,377**	**$ 64,994**

	2005				
	First	Second	Third	Fourth	Total
Net interest income	$ 18,539	$ 18,759	$ 18,516	$ 20,146	$ 75,960
Negative provision for loan losses	(96)	(248)	—	—	(344)
Noninterest expense, net	5,795	4,032	3,754	4,346	17,927
FAC expense	218	(5)	548	—	761
Net income	$ 12,622	$ 14,980	$ 14,214	$ 15,800	$ 57,616

	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

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 certain of the district's retirement and benefit plans results in the recording of these plans only in the district's combined financial statements.

	December 31,		
Balance Sheet Data	**2006**	2005	2004
Cash	**$ 46,005**	$ 47,455	$ 40,555
Loans	**10,665,377**	8,774,807	7,568,736
Less allowance for loan losses	**13,827**	9,391	10,378
Net loans	**10,651,550**	8,765,416	7,558,358
Accrued interest receivable	**176,583**	129,467	95,747
Other property owned, net	**2,020**	3,902	5,184
Other assets	**211,927**	186,512	181,656
Total assets	**$11,088,085**	$ 9,132,752	$ 7,881,500
Bonds and notes	**$ 9,214,287**	$ 7,430,075	$ 6,336,917
Other liabilities	**235,617**	191,082	147,434
Total liabilities	**9,449,904**	7,621,157	6,484,351
Capital stock and participation certificates	**60,771**	75,593	92,103
Retained earnings	**1,577,410**	1,436,002	1,305,046
Total shareholders' equity	**1,638,181**	1,511,595	1,397,149
Total liabilities and shareholders' equity	**$11,088,085**	$ 9,132,752	$ 7,881,500

	Year Ended December 31,		
Statement of Income Data	**2006**	2005	2004
Interest income	**$ 724,454**	$ 530,067	$ 387,570
Interest expense	**428,281**	268,222	152,932
Net interest income	**296,173**	261,845	234,638
Provision (negative provision) for loan losses	**6,778**	1,428	(151,953)
Net interest income after provision for loan losses	**289,395**	260,417	386,591
Noninterest income	**66,257**	53,594	43,152
Intra-System financial assistance expense	**—**	1,144	3,406
Other expense	**144,261**	126,546	147,635
(Benefit from) provision for income taxes	**(228)**	639	1,768
Net income	**$ 211,619**	$ 185,682	$ 276,934

Disclosure Information and Index

DISCLOSURES REQUIRED BY FARM CREDIT ADMINISTRATION REGULATIONS

Description of Business

The Farm Credit Bank of Texas (FCBT or bank), Agricultural Credit Associations (ACAs) and the Federal Land Credit Associations (FLCAs) of the Tenth Farm Credit District (district) are member-owned cooperatives which provide credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes in the states of Alabama, Louisiana, Mississippi, New Mexico and Texas. The district's ACA parent associations, which each contain wholly-owned FLCA and Production Credit Association (PCA) subsidiaries, and FLCAs are collectively referred to as associations. A further description of territory served, persons 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 combined 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 are incorporated herein by reference to "Management's Discussion and Analysis" of the district included in this annual report to stockholders.

Directors and Senior Officers

The following represents certain information regarding the district directors and senior officers of the bank as of February 16, 2007:

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 and is chairman of the Compensation 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 Panhandle-Plains Land Bank, FLCA Board of Directors. In January 2003, he joined the national Farm Credit Council Board of Directors as a Tenth District representative. He is also a member of the bank's Audit Committee and the State Technical Committee for the Natural Resources Conservation Service, and is the vice chairman of the Compensation Committee. 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 his current term expires December 31, 2008. 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 a member of the Tenth District Farm Credit Council and represented the district on the national Farm Credit Council Board of Directors from 1996 to 2005. He also serves on the bank's Audit and Compensation committees.

Joe R. Crawford began his first term on the board in 1998, and his current term expires December 31, 2009. 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. He is a director on the board of the Federal Farm Credit Banks Funding Corporation and is a member of the bank's Audit and Compensation committees. 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, and his current term will expire December 31, 2008. 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 is chairman of the Tenth District Farm Credit Council board, is vice chairman of the bank's Audit Committee and serves on the bank's Compensation Committee. Dodson grows cotton and milo and operates a seed sales business with his family in Robstown, Texas. He is the president of Dodson Farms, Inc., Dodson Ag, Inc. and Chapman Ranch Gin Cooperative; the owner of Jimmy Dodson Farms; a trustee of Evelyn Kathryn Dodson Testamentary Trust; a partner in Weber Greene, Ltd; and a managing partner in Weber Station LLC. He holds other national farm leadership positions in the National Cotton Council of America, South Texas Cotton and Grain Association, and American Cotton Producers.

Elizabeth G. Flores joined the board in August 2006, and her current term expires December 31, 2009. She was mayor of Laredo, Texas, where she resides, from 1998 to June 2006. Previously, she was senior vice president of Laredo National Bank. She is a partner with a ranching and real estate limited partnership, E.G. Ranch, Ltd. Flores also is a member of the bank's Audit and Compensation committees.

William F. Staats joined the board in 1997, and his current term will expire December 31, 2008. 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, SevenOaks Capital Associates, LLC and Platinum Healthcare Staffing, Inc. He is a member of the Farm Credit System Audit Committee, is chairman of the bank's Audit Committee, serves on the bank's Compensation Committee, and is the bank's designated financial expert.

Compensation of Directors

Directors of the bank are compensated for service on the bank's board. Compensation for 2006 was paid at the rate of $3,812 per month. 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, 2006, is provided below:

Board Member	Days Served at Board Meetings	Days Served on Other Official Assignments	Total Compensation Paid
Ralph W. Cortese	30.0	25.0	$ 48,740
Jon M. Garnett	29.0	29.0	47,740
C. Kenneth Andrews	30.5	20.5	47,740
Joe R. Crawford	30.0	25.5	45,740
James F. Dodson	26.5	22.0	48,740
Elizabeth G. Flores	11.0	12.0	19,058
William F. Staats	25.5	17.5	51,740
			$ 309,498

SENIOR OFFICERS

Name and Title	Time in Position	Experience — Past Five Years
Larry R. Doyle, *Chief Executive Officer*	3.5 years	Executive Vice President and Chief Operating Officer, AgFirst Farm Credit Bank
Thomas W. Hill, *Senior Vice President, Chief Financial Officer,* *Chief Operations Officer*	12 years 3 years	Senior Vice President, Chief Financial Officer, FCBT
Steven H. Fowlkes, *Senior Vice President,* *Chief Credit Officer*	9 years 3 years	Senior management and management positions, FCBT
David N. Clinton, *Senior Vice President,* *Chief Information Officer*	8 years	Senior management position, FCBT
William E. Zimmerman, *Senior Vice President, Corporate Affairs,* *General Counsel and Corporate Secretary*	19 years	Senior Vice President, Corporate Affairs, General Counsel and Corporate Secretary, FCBT

Compensation Discussion and Analysis – Chief Executive Officer (CEO)

Overview

A primary objective of the Farm Credit Bank of Texas is to attract, develop and retain senior officers who are proficient in the implementation of the bank's strategic objectives, operational activities and delivery of performance results that maximize the principles of a cooperative organization. The philosophy of the bank's compensation program centers on the performance and contributions of its employees while maintaining salaries and benefits which position the bank to be competitive in the financial services marketplace. The board of directors, through its Compensation Committee, annually considers the appropriate mix of market-based base salary and benefits with variable incentive compensation that will provide incentives and rewards for the current year accomplishments of the bank's strategic business plan and financial objectives. With data derived from an independent third-party compensation consultant, the bank's board annually reviews competitive market salary data of competition in the financial services area to make sure that base salaries and incentive plan structures are in line with market-comparable positions with similarly situated financial institutions. This study provides the basis for actions by the board of directors to approve the compensation level and incentive plan structure of the bank's chief executive officer annually. The bank's compensation program encompasses two primary elements: base salary and an annual Success Sharing Plan incentive.

CEO Compensation Table and Policy

The percentage of base salary that is utilized to calculate the CEO's non-equity incentive compensation paid in 2006 was increased to a higher percentage of his base salary, while making no adjustments to the base salary amount. The incentive calculation percentage has changed to put more total compensation "at risk" based on the performance of the bank. There are no long-term incentive plans, deferred compensation arrangements or retention plans in place for the CEO. Payment of the incentive is made in the first 90 days of the subsequent calendar year following the close of the year.

The following table summarizes the compensation paid to the chief executive officer of the bank during 2006, 2005 and 2004:

Summary Compensation Table

		Annual			
Name of Chief Executive Officer	Year	Salary (a)	Non-Equity Incentive Plan Compensation (b)	Other (c)	Total
Larry R. Doyle	2006	$ 440,017	$ 238,000	$ 20,362	$ 698,379
Larry R. Doyle	2005	440,017	176,000	17,016	633,033
Larry R. Doyle	2004	440,000	100,000	13,605	553,605

(a) Gross salary
(b) Incentive pay
(c) Other includes contributions to 401(k) and defined contribution plans, automobile benefits and premiums paid for life insurance.

Pension Benefits Table

The following table presents a summary of the total annual benefits provided from the pension plans applicable to the CEO:

	Years of Service				
Remuneration	25	30	35	40	45
$ 300,000	$ 154,844	$ 185,812	$ 216,781	$ 247,750	$ 278,718
400,000	208,594	250,312	292,031	333,750	375,468
500,000	262,344	314,812	367,281	419,750	472,218
600,000	316,094	379,312	442,531	505,750	568,968
700,000	369,844	443,812	517,781	591,750	665,718

Pension Benefits Table Narrative Disclosure

The CEO participates in the Farm Credit Bank of Texas Pension Plan (qualified plan) and in a supplemental plan which restores benefits otherwise restricted by limits in the qualified plan. Compensation, as defined in the plans, includes the sum of wages, incentives and deferrals to the 401(k) and flexible spending account plans, but excludes accrued annual leave that may be paid in cash at the time of termination, retirement or transfer of employment, severance payments, retention bonuses, taxable fringe benefits and any other payments. Pension benefits are based on the average of monthly compensation over the 60 consecutive months that produce the highest average out of the last 120 months of employment (FAC60). The benefit formula is the sum of 1.65 percent of FAC60 plus 0.50 percent of FAC60 in excess of Social Security Covered Compensation times years of service. The estimated annual benefits illustrated assume retirement at age 65 with benefits payable as a 50 percent joint and survivor annuity with a spouse two years younger. The CEO had 31 years of credited service as of December 31, 2006. There is an offset amount from another Farm Credit System institution for the CEO.

Employment Agreement

The CEO was employed by the bank under the terms and conditions of an "employment at will" agreement and is not bound by the terms of a contract for any duration of time. The agreement provides for a minimum compensation level, consisting of base salary and incentive compensation. The CEO will receive a set severance amount if terminated for any reason other than cause and will receive a guarantee of bridging of time and service to satisfy the pension rule of 85 (combination of age and years of service) if such termination should occur before the CEO reaches the rule of 85 for pension benefits.

Compensation of Other Senior Officers

The following table summarizes the compensation paid to all other senior officers of the bank during 2006, 2005 and 2004:

Summary Compensation Table

		Annual			
Name of Individual or Group	Year	Salary (a)	Non-Equity Incentive Plan Compensation (b)	Other (c)	Total
Aggregate number of senior officers: (excludes Chief Executive Officer)					
5	2006	$ 1,072,241	$ 254,265	$ 105,873	$ 1,432,379
5	2005	1,023,365	209,108	109,543	1,342,016
5	2004	956,992	198,247	100,694	1,255,933

(a) Gross salary
(b) Incentive pay
(c) Other includes contributions to 401(k) and defined contribution plans, automobile benefits and premiums paid for life insurance.

Disclosure of the compensation paid during 2006 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 2006, 2005 and 2004 totaled $123,258, $120,436 and $91,473, 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 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

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.

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 combined financial statements outlines the bank's position with regard to possible contingencies at December 31, 2006.

Description of Capital Structure

The bank is authorized to issue and retire certain classes of capital stock and retained earnings in the management of its 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" 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, 2006, 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 policies on loans to and transactions with its officers and directors, required to be disclosed in this section, are incorporated herein by reference to Note 11, "Related Party Transactions," to the accompanying financial statements.

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 1, 2007, and the report of management in this annual report to stockholders, are incorporated herein by reference.

The Tenth Farm Credit 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.

Credit and Services to Young, Beginning and Small Farmers and Ranchers and Producers or Harvesters of Aquatic Products (YBS)

In line with our mission, we have policies and programs for making credit available to young, beginning and small farmers and ranchers.

The definitions for YBS, as prescribed by FCA regulations, are provided below.

Young Farmer or Rancher – A farmer, rancher or producer or harvester of aquatic products who was age 35 or younger as of the date the loan was originally made.

Beginning Farmer or Rancher – A farmer, rancher or producer or harvester of aquatic products who had 10 years or less of experience at farming, ranching or producing or harvesting aquatic products as of the date the loan was originally made.

Small Farmer or Rancher – A farmer, rancher or producer or harvester of aquatic products who normally generated less than $250,000 in annual gross sales of agricultural or aquatic products at the date the loan was originally made.

For the purposes of YBS, the term "loan" means an extension of, or a commitment to extend, credit authorized under the Farm Credit Act, whether it results from direct negotiations between a lender and a borrower or is purchased from, or discounted for, another lender, including participation interests. A farmer/rancher may be included in multiple categories as they are included in each category in which the definition is met.

The bank and associations' efforts to respond to the credit and related needs of YBS borrowers are evidenced by the following table:

($ in thousands)	At December 31, 2006 Number of Loans	Volume
Total loans and commitments	72,636	$ 15,371,473
Loans and commitments to young farmers and ranchers	13,435	$ 1,680,036
Percent of loans and commitments to young farmers and ranchers	18.5%	10.9%
Loans and commitments to beginning farmers and ranchers	32,765	$ 5,835,493
Percent of loans and commitments to beginning farmers and ranchers	45.1%	38.0%

The following table summarizes information regarding new loans to young and beginning farmers and ranchers:

($ in thousands)	For the Year Ended December 31, 2006 Number of Loans	Volume
Total new loans and commitments	18,827	$ 7,120,869
New loans and commitments to young farmers and ranchers	3,409	$ 643,198
Percent of new loans and commitments to young farmers and ranchers	18.1%	9.0%
New loans and commitments to beginning farmers and ranchers	8,155	$ 2,391,049
Percent of new loans and commitments to beginning farmers and ranchers	43.3%	33.6%

The following table summarizes information regarding loans to small farmers and ranchers:

	At December 31, 2006				
	Annual Gross Sales				
($ in thousands)	$50 Thousand or Less	$50 to $100 Thousand	$100 to $250 Thousand	Over $250 Thousand	Total
Total number of loans and commitments	23,519	18,793	18,075	12,249	72,636
Number of loans and commitments to small farmers and ranchers	16,897	14,139	13,256	6,363	50,655
Percent of loans and commitments to small farmers and ranchers	71.8%	75.2%	73.3%	51.9%	69.7%
Total loans and commitments volume	$ 455,852	$ 1,062,271	$ 2,365,777	$ 11,487,573	$ 15,371,473
Total loans and commitments to small farmers and ranchers volume	$ 346,703	$ 816,814	$ 1,808,321	$ 3,925,391	$ 6,897,229
Percent of loans and commitments volume to small farmers and ranchers	76.1%	76.9%	76.4%	34.2%	44.9%

The following table summarizes information regarding new loans made to small farmers and ranchers:

	For the Year Ended December 31, 2006				
	Annual Gross Sales				
($ in thousands)	$50 Thousand or Less	$50 to $100 Thousand	$100 to $250 Thousand	Over $250 Thousand	Total
Total number of new loans and commitments	6,031	3,717	4,604	4,475	18,827
Number of new loans and commitments to small farmers and ranchers	4,240	2,924	3,433	1,959	12,556
Percent of new loans and commitments to small farmers and ranchers	70.3%	78.7%	74.6%	43.8%	66.7%
Total new loans and commitments volume	$ 133,202	$ 273,998	$ 757,780	$ 5,955,889	$ 7,120,869
Total new loans and commitments to small farmers and ranchers volume	$ 107,009	$ 213,933	$ 554,814	$ 1,708,779	$ 2,584,535
Percent of loan and commitment volume to small farmers and ranchers	80.3%	78.1%	73.2%	28.7%	36.3%