STRENGTH THROUGH DIVERSITY

2007 ANNUAL REPORT
TENTH FARM CREDIT DISTRICT

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STRENGTH THROUGH **DIVERSITY**

The significant growth achieved in the Tenth District last year contributed to our **STRENGTH**. But it is not the whole story. The growth occurred THROUGH several markets, and that portfolio **DIVERSITY** also plays a role in keeping us strong.

TENTH FARM CREDIT DISTRICT

ALABAMA • LOUISIANA • MISSISSIPPI • NEW MEXICO • TEXAS

If you drive from one end of our five-state district to the other end, you will notice richness and diversity in the geography, people and agricultural activities that make up the Tenth Farm Credit District. From chilies to chickens, pecan trees to pine, no other area of the country offers as much variety.

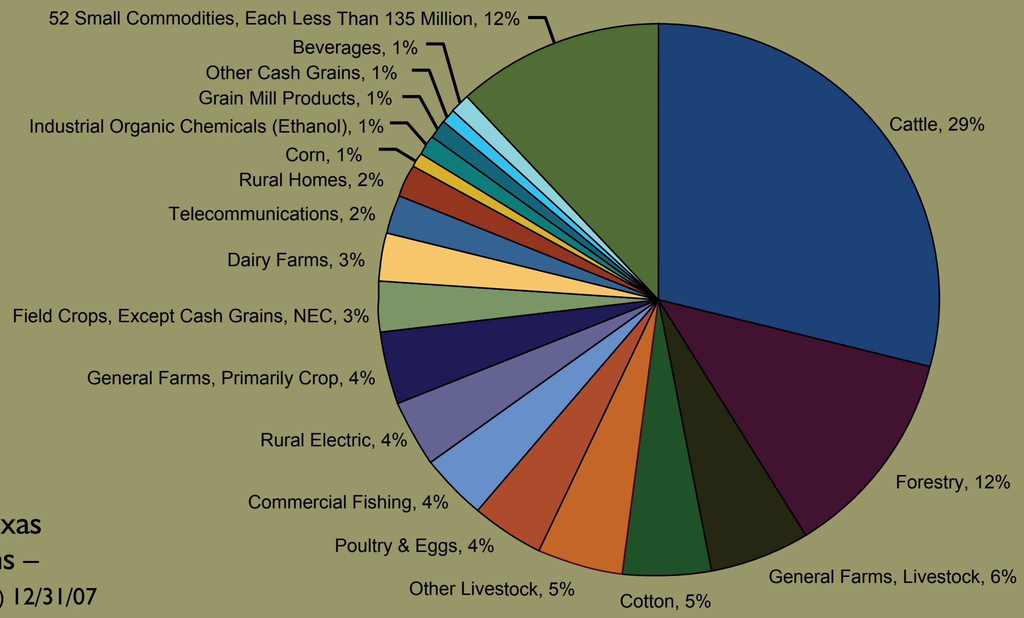
The diversity becomes obvious first in the terrain, which ranges from mountains to valleys, grasslands to forests. With such diverse geography, it is no wonder that an abundance of agricultural products are produced here. It is our intent to be the lender of choice for the agribusinesses that are thriving throughout our district. That includes participating with other lenders on large, complex loans to multimillion-dollar operations, as well as creating specialized lending programs to support young, beginning and small farmers and ranchers who are just getting started.

Another unique aspect of our district is the people who live here. They represent not only different backgrounds and ethnicities, but also a broad set of interests and talents. We are proud to serve such unique individuals and look forward to broadening our reach with products and services that will help even more people.

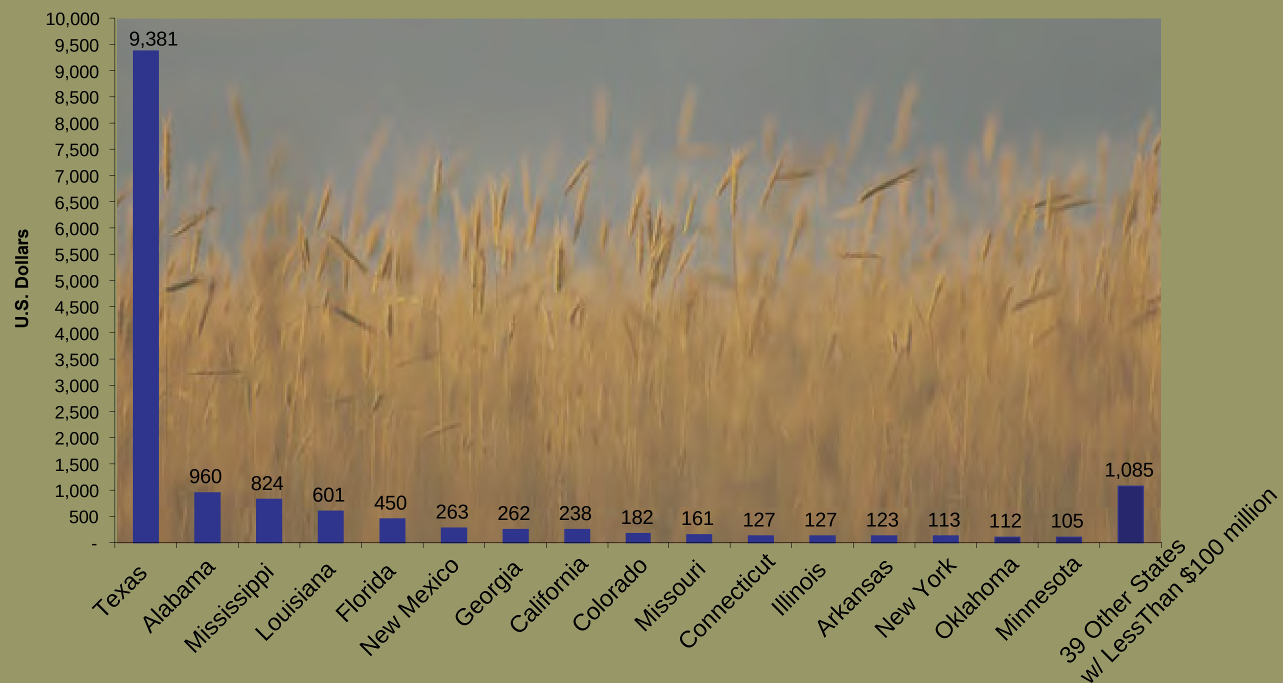
In addition, we are proud of the diverse activities that our associations sponsor and our employees support. From sponsorship of agricultural youth programs like 4-H and FFA to involvement in community activities such as food drives and fun runs, we are investing in our communities and in the future of agriculture in our areas.

"We are blessed in where we live and work. No other area of the country

Farm Credit Bank of Texas and District Associations – Loans by Commodity 12/31/07



Farm Credit Bank of Texas and District Associations – Loans by State (in millions) 12/31/07



has as much rich agricultural diversity as our five states." – Larry Doyle

BOARD OF DIRECTORS
FARM CREDIT BANK OF TEXAS

Kenneth Andrews	(Seated) Ralph W. "Buddy" Cortese Chairman	Joe Crawford	Jimmy Dodson	Elizabeth G. "Betty" Flores	(Seated) Jon "Mike" Garnett Vice Chairman	William Staats

Commitment to Rural America

Since the Farm Credit System was established by Congress in 1916, our mission has been to support agricultural producers and rural communities. We have never wavered in that commitment and are proud to serve our rural territory today with outstanding products and services, as well as investing in our communities through volunteerism, scholarships and sponsorships. In 2007, we also continued to look for opportunities to invest in rural America through the Rural America Bond Program that was approved in 2006.

Focus on Our Stockholders

As cooperatives, the lending associations in the Tenth District have one objective: to operate in the best interest of their borrowers, the stockholders who own their organizations. For example, each association shares its earnings with its borrower-stockholders through its respective patronage program. Patronage distributions continue to increase each year, which reflects our ongoing commitment to our borrowers.

The district has also worked to develop new products and services to meet the diverse financial needs of our customers. As we continue to investigate those needs, we will work to fully serve the various interests of each and every borrower. We also will focus more attention on our internal controls and credit review functions to safeguard credit quality while we grow our associations.

Emphasis on Cooperative Structure

The cooperative structure of Farm Credit associations sets them apart from other lenders. The cooperative philosophy translates into our daily activities, from our patronage programs to the extensive training provided for our board members through the Director Development Program. In addition, we strive to maintain effective communication with our stockholders and transparency in our financial reporting.

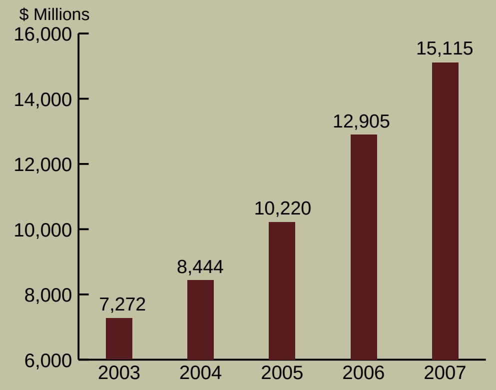
2007 FINANCIAL HIGHLIGHTS

The district's net income for the year ended December 31, 2007, was $242.5 million, reflecting a $2.4 million increase over the net income reported in 2006. Credit quality remains strong at 98.8 percent acceptable at year end, compared to 98.9 percent at December 31, 2006.

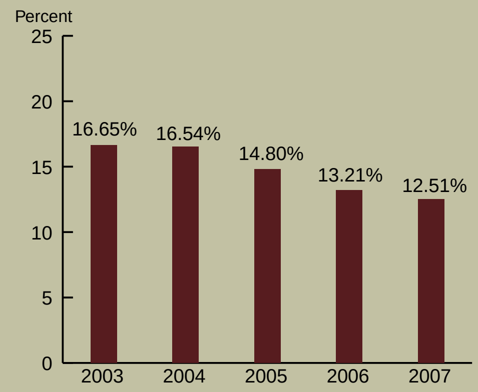
Gross loan volume increased to $15.11 billion, adding another $2.20 billion, or 17.1 percent, to the $12.91 billion reported at December 31, 2006. This is the fourth year in a row that the district has reported double-digit growth.

Tenth District associations continued to share earnings with their borrowers through patronage programs. Patronage distributions declared totaled $133.7 million in 2007, compared to $124.8 and $56.4 million in 2006 and 2005, respectively.

Total Loans Outstanding at Year End



Total Members' Equity to Total Assets at Year End

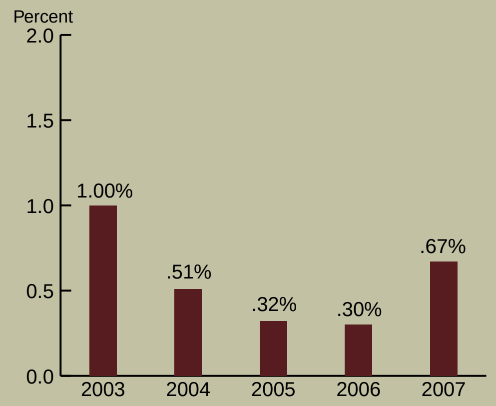


2007 KEY FINANCIAL HIGHLIGHTS

(Dollars in Thousands)

Total Loans	$15,114,537
Total Assets	$17,996,497
Net Income	$242,540
Return on Average Assets	1.44%
Return on Average Members' Equity	10.86%

Nonaccrual Loans and Other Property Owned to Total Loans and Other Property Owned at Year End



MESSAGE TO STOCKHOLDERS

With a gross loan volume exceeding $15 billion, the Tenth District has reached record size. We have experienced double-digit growth consistently over the last four years. This significant growth is primarily the result of our lending staff that has worked hard to capture more market share in our territory, and effectively participated loans with other lenders to fund more large loans.

Our increased lending activities have proved beneficial for our borrower-stockholders. Today, our associations offer additional products and services that can further meet the needs of each and every borrower. Also, patronage dividends and allocated equities continue to increase, which lowers borrowers' effective interest rates. Last year, Tenth District associations paid a record $133.7 million to their customers through various patronage programs.

Along with our loan volume growth, our net income of $242.5 million edged past the $240.1 million in net income we brought in last year, and our credit quality remained high at 98.8 percent of loans acceptable.

While we are pleased to report on our positive results, we also recognize that with growth comes increased responsibility. As we move forward, we will keep the benefit of our stockholders in mind, balancing potential growth against risk to protect their investment in our cooperative associations. We will focus extensively on credit analysis and review, and strengthen our internal control structures.

We will also continue our commitment to serve our customers well by offering enhanced products, market pricing and increased patronage. Plus, we will step up our marketing efforts to help potential customers find out about the benefits of doing business with Farm Credit and to educate our customers about all of the loan products available to them. We hope to fully serve each of our customers, offering them the best products at competitive prices, topped off with a patronage benefit.

When we provide each customer with a positive lending experience, we fuel our long-term growth potential. Satisfied customers will return, and will refer friends and family to us. We owe our success to our stockholders, and we remain committed to their best interest.

Larry R. Doyle
Chief Executive Officer
Farm Credit Bank of Texas

REPORT OF MANAGEMENT

The Farm Credit Bank of Texas and the Tenth Farm Credit District Associations

The accompanying combined financial statements of the Farm Credit Bank of Texas (bank) and Tenth Farm Credit District (district) associations are prepared by management, which is responsible for their integrity and objectivity, including amounts that must necessarily be based on judgments and estimates. The combined financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America appropriate in the circumstances. The combined financial statements, in the opinion of management, present fairly the financial condition of the district. Other financial information included in the annual report is consistent with that in the combined financial statements.

To meet its responsibility for reliable financial information, management depends on the 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 must be reasonable in relation to the benefits derived. To monitor compliance, financial operations audits are performed. The combined financial statements are audited by PricewaterhouseCoopers LLP (PwC) independent auditors, who also conduct a review of internal controls to the extent necessary to comply with auditing standards generally accepted in the United States of America. The Farm Credit Bank of Texas and district associations are also examined by the Farm Credit Administration.

In the opinion of management, the combined financial statements are true and correct and fairly state the financial position of the bank and district at December 31, 2007, 2006 and 2005. The independent auditors have direct access to the board, which is composed solely of directors who are not officers or employees of the bank or district associations.

The undersigned certify that we have reviewed the December 31, 2007, annual report of the Farm Credit Bank of Texas and district associations, that the report has been prepared in accordance with all applicable statutory or regulatory requirements, and that the information included 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

February 29, 2008

Five-Year Summary of Selected Combined Financial Data

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

(dollars in thousands)	**2007**	2006	2005	2004*	2003
Balance Sheet Data					
Cash, federal funds sold and securities purchased under resale agreements	**$ 181,205**	$ 149,399	$ 94,291	$ 91,669	$ 69,217
Investment securities	**2,410,999**	2,672,242	2,697,876	1,787,706	1,518,102
Loans	**15,114,537**	12,905,321	10,219,596	8,444,347	7,272,314
Less allowance for loan losses	**24,495**	13,969	9,533	10,617	173,980
Net loans	**15,090,042**	12,891,352	10,210,063	8,433,730	7,098,334
Other property owned, net	**1,817**	2,020	3,902	5,184	6,057
Other assets	**312,434**	272,054	206,088	180,650	150,498
Total assets	**$ 17,996,497**	$ 15,987,067	$ 13,212,220	$ 10,498,939	$ 8,842,208
Obligations with maturities of one year or less	**$ 7,751,462**	$ 6,458,754	$ 5,968,414	$ 4,521,114	$ 2,924,218
Obligations with maturities greater than one year	**7,994,374**	7,415,653	5,288,711	4,241,696	4,445,935
Total liabilities	**15,745,836**	13,874,407	11,257,125	8,762,810	7,370,153
Preferred stock	**202,754**	203,565	203,569	103,963	103,998
Capital stock and participation certificates	**62,489**	59,068	73,642	88,962	101,168
Allocated retained earnings	**133,423**	83,705	32,327	32,662	35,328
Unallocated retained earnings	**1,886,488**	1,792,723	1,692,534	1,531,503	1,236,010
Accumulated other comprehensive loss	**(34,493)**	(26,401)	(46,977)	(20,961)	(4,449)
Total members' equity	**2,250,661**	2,112,660	1,955,095	1,736,129	1,472,055
Total liabilities and members' equity	**$ 17,996,497**	$ 15,987,067	$ 13,212,220	$ 10,498,939	$ 8,842,208
Statement of Income Data					
Net interest income	**$ 432,381**	$ 386,246	$ 340,472	$ 304,136	$ 265,051
(Provision) negative provision for loan losses	**(43,131)**	(9,356)	(1,084)	157,325	(11,602)
Noninterest expense, net	**(146,569)**	(137,000)	(118,872)	(117,177)	(84,509)
(Provision for) benefit from income taxes	**(141)**	228	(639)	(1,768)	(324)
Net income	**$ 242,540**	$ 240,118	$ 219,877	$ 342,516	$ 168,616
Key Financial Ratios (unaudited)					
Net income to:					
Average assets	**1.44%**	1.66%	1.92%	3.66%	2.07%
Average members' equity	**10.86**	11.69	11.80	21.89	12.53
Net interest income to average earning assets	**2.61**	2.72	3.04	3.26	3.29
Net charge-offs (recoveries) to average loans	**0.23**	0.04	0.02	0.08	0.05
Total members' equity to total assets	**12.51**	13.21	14.80	16.54	16.65
Allowance for loan losses to total loans	**0.16**	0.11	0.09	0.13	2.39
Regulatory permanent capital ratio (bank only)	**13.43**	13.67	17.36	19.82	23.71
Total surplus ratio (bank only)	**11.15**	11.61	14.97	16.55	19.15
Core surplus ratio (bank only)	**6.70**	6.93	8.82	11.51	14.44
Net collateral ratio (bank only)	**105.18**	105.35	105.90	105.69	105.62
Other (unaudited)					
Net income distributions declared					
Preferred stock dividends	**$ 15,122**	$ 15,122	$ 11,342	$ 7,561	$ 798
Patronage distributions					
Cash	**76,253**	70,479	49,964	37,946	22,649
Allocated earnings	**57,400**	54,328	6,435	1,886	4,143

*As discussed more fully in the following pages, net income and certain profitability ratios for 2004 were affected by the nonrecurring negative provision for loan losses of $157.7 million.

Combined Average Balances and Net Interest Earnings

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS
(unaudited)
December 31,

	2007			2006			2005		
(dollars in thousands)	**Average Balance**	**Interest**	**Average Rate**	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Assets									
Investment securities, federal funds sold and securities purchased under resale agreements	**$ 2,598,854**	**$ 131,768**	**5.07%**	$ 2,929,742	$ 141,260	4.82%	$ 2,034,438	$ 76,735	3.77%
Loans	**13,940,105**	**1,053,629**	**7.56**	11,272,884	845,135	7.50	9,170,084	595,995	6.50
Total interest-earning assets	**16,538,959**	**1,185,397**	**7.17**	14,202,626	986,395	6.95	11,204,522	672,730	6.00
Cash	**33,110**			32,709			22,907		
Accrued interest receivable	**238,632**			191,322			140,233		
Allowance for loan losses	**(21,122)**			(11,285)			(10,368)		
Other noninterest-earning assets	**103,376**			90,355			90,310		
Total average assets	**$ 16,892,955**			$ 14,505,727			$ 11,447,604		
Liabilities and Members' Equity									
Bonds and medium-term notes, net	**$ 11,718,042**	**$ 608,067**	**5.19%**	$ 10,343,964	$ 506,346	4.90%	$ 8,181,609	$ 290,312	3.55%
Discount notes, net, and other	**2,618,740**	**144,949**	**5.54**	1,788,304	93,803	5.25	1,188,291	41,946	3.53
Total interest-bearing liabilities	**14,336,782**	**753,016**	**5.25**	12,132,268	600,149	4.95	9,369,900	332,258	3.55
Noninterest-bearing liabilities	**323,042**			319,585			213,853		
Total liabilities	**14,659,824**			12,451,853			9,583,753		
Members' equity and retained earnings	**2,233,131**			2,053,874			1,863,851		
Total average liabilities and members' equity	**$ 16,892,955**			$ 14,505,727			$ 11,447,604		
Net interest rate spread		**$ 432,381**	**1.92%**		$ 386,246	2.00%		$ 340,472	2.45%
Net interest margin			**2.61%**			2.72%			3.04%

Management's Discussion and Analysis

(dollars in thousands, except as noted)

The following commentary provides a discussion and analysis of the combined financial position and results of operations of the Farm Credit Bank of Texas (bank), the Federal Land Credit Associations (FLCAs) and the Agricultural Credit Associations (ACAs) of the Tenth Farm Credit District (district). FLCAs and ACAs collectively are referred to as "associations." The commentary should be read in conjunction with the accompanying combined financial statements, notes to the combined financial statements (notes) and additional sections of this report. The accompanying combined financial statements were prepared under the oversight of the bank's Audit Committee.

The district, which serves Texas, Alabama, Mississippi, Louisiana and portions of New Mexico, is part of the federally chartered Farm Credit System (System). The bank provides funding to the associations, which, in turn, provide credit to their borrower-shareholders. As of December 31, 2007, the district comprised the bank, six FLCAs and 14 ACAs. The bank also had funding relationships with five Other Financing Institutions (OFIs).

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 combined 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 combined 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.

  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 or district's results of operations.

- Pensions – The bank and its related associations participate in defined benefit retirement plans. These plans are non-contributory, 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. Pension expense is determined by actuarial valuations based on certain assumptions, including expected long-term rate of return on plan assets and discount rate. The expected return on plan assets for the year is calculated based on the composition of assets at the beginning of the year and the expected long-term rate of return on that portfolio of assets. The discount rate is used to determine the present value of our future benefit obligations. We selected the discount rate by reference to Hewitt's corporate bond index, actuarial analyses and industry norms.

Financial Highlights

- ❖ The aggregate principal amount of loans outstanding at December 31, 2007, was $15.11 billion, compared to $12.91 billion at December 31, 2006, and $10.22 billion at December 31, 2005, reflecting increases of 17.0 and 47.8 percent over December 31, 2006 and 2005, respectively.
- ❖ Net income totaled $242.5 million for the year ended December 31, 2007, compared to $240.1 million for 2006 and $219.9 million for 2005, reflecting an increase of 1.0 percent from 2006 and an increase of 10.3 percent over 2005.
- ❖ Net interest income for the year ended December 31, 2007, was $432.4 million compared to $386.2 million for 2006 and $340.5 million for 2005, reflecting 11.9 and 27.0 percent increases over the years ended December 31, 2006 and 2005, respectively.
- ❖ Return on average assets and return on average members' equity for the year ended December 31, 2007, were 1.44 and 10.86 percent, respectively, compared to 1.66 and 11.69 percent for 2006 and 1.92 and 11.80 percent for 2005, respectively.
- ❖ Patronage distributions declared totaled $133.7 million in 2007, compared to $124.8 and $56.4 million in 2006 and 2005, respectively.
- ❖ In 2007, the bank sold $1.3 billion of participations in district direct notes receivable to another System bank. In 2006, the bank sold $1.0 billion of these participations. Cumulative sales of the participations in direct notes total $2.7 billion at December 31, 2007. These transactions enhance the composition of the bank's capital and liquidity position in order to facilitate the district's diversification and opportunities for growth.

RESULTS OF OPERATIONS

Net Income

The district's net income of $242.5 million for the year ended December 31, 2007, reflected an increase of 1.0 percent from net income of $240.1 million for the year ended December 31, 2006, and an increase of 10.3 percent from net income of $219.9 million for 2005. The return on average assets decreased to 1.44 percent for the year ended December 31, 2007, from 1.66 percent reported for the year ended December 31, 2006. This decrease was due primarily to an increase of $33.8 million in the district's provision for loan losses, discussed more fully in the "Loan Portfolio" section of this discussion, and to the effects of a 16.5 percent expansion in the district's earning assets and the decrease in the interest rate spread on those earning assets, discussed more fully in the following "Net Interest Income" section.

Changes in Components of Net Income

	2007 vs. 2006	2006 vs. 2005
Net income, prior period	$ 240,118	$ 219,877
Interest income	199,002	313,665
Interest expense	(152,867)	(267,891)
Net interest income	46,135	45,774
Provision for loan losses	(33,775)	(8,272)
Noninterest income	3,498	3,277
Noninterest expense	(13,067)	(21,405)
Provision for income taxes	(369)	867
Total increase in net income	2,422	20,241
Net income	$ 242,540	$ 240,118

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, 2007, was $1.2 billion, an increase of $199.0 million, or 20.2 percent, compared to 2006. This increase was due to an increase in average interest-earning assets, and to a lesser extent, an increase in the interest rates on earning assets.

Total interest income for 2006 was $986.4 million, an increase of $313.7 million, or 46.6 percent, from 2005. This increase was due to an increase in interest rates and to an increase in average interest-earning assets.

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

	Year Ended December 31,	
	2007 vs. 2006	2006 vs. 2005
Increase in average earning assets	$ 2,336,333	$ 2,998,104
Average yield, prior year	6.95%	6.00%
Interest income variance attributed to change in volume	162,375	179,886
Average earning assets, current year	16,538,959	14,202,626
Increase in average yield	0.22%	0.95%
Interest income variance attributed to change in yield	36,627	133,779
Net change in interest income	$ 199,002	$ 313,665

Interest Expense

Total interest expense for the year ended December 31, 2007, was $753.0 million, an increase of $152.9 million, or 25.5 percent, from the prior year. Total interest expense for the year ended December 31, 2006, was $600.1 million, an increase of $267.9 million, or 80.6 percent, from 2005. The increase for 2007 over 2006 was due primarily to an increase in interest-bearing liabilities, and to a lesser extent, to an increase in the average rate on that debt. The increase from 2006 over 2005 was due mainly to increases in average rate and, to a lesser extent, an increase in 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, 2007 vs. 2006	Year Ended December 31, 2006 vs. 2005
Increase in average interest-bearing liabilities	$ 2,204,514	$ 2,762,368
Average rate, prior year	4.95%	3.55%
Interest expense variance attributed to change in volume	109,123	98,064
Average interest-bearing liabilities, current year	14,336,782	12,132,268
Increase in average rate	0.30%	1.40%
Interest expense variance attributed to change in rate	43,744	169,827
Net change in interest expense	$ 152,867	$ 267,891

Analysis of Operating Margin to Average Earning Assets

	For the Years Ended December 31, 2007	2006	2005
Net interest margin	**2.61%**	2.72%	3.04%
Operating expense	**1.04**	1.11	1.21
Operating margin	**1.57%**	1.61%	1.83%

Net Interest Income

Net interest income increased by $46.1 million, or 11.9 percent, from 2006 to 2007 and increased by $45.8 million, or 13.4 percent, from 2005 to 2006. Factors responsible for these changes are illustrated in Figure 1.

Net interest income for 2007 increased from 2006 due to an increase in average-earning assets, partially offset by an 8-basis-point decrease in the interest rate spread, which is the difference between the average rate received on interest-earning assets and the average rate paid on interest-bearing debt. The increase in earning assets was due primarily to loan growth at the district's associations, and, to a lesser extent, to growth in the bank's loan participation portfolio. The bank's investment portfolio was reduced as the bank shifted more of its earning assets to the loan portfolio. Also, during 2007 the bank called $2.535 billion in debt, replacing it with debt that had more favorable terms, which should continue to benefit the interest rate spread in 2008. The decrease in the interest rate spread was due primarily to a combination of competitive market forces and the changes in the composition of the district's earning assets. Loan pricing spreads at the associations have narrowed as they compete more aggressively with commercial banks and other lenders for a larger market share. Competitive conditions at the time of an association loan's repricing may affect interest rate spreads. Market competition has also reduced interest rate spreads on participation loans. Although the interest rate spread on association loans has been compressed, they continue to be the highest yielding of the district's earning assets.

Net interest income for 2006 increased from 2005 due to an increase in the district's earning assets, partially offset by a 45-basis-point decrease in the interest rate spread.

Noninterest Income

Noninterest income of $24.8 million reflected an increase of $3.5 million, or 16.4 percent, from 2006 to 2007. The increase was due to a $3.7 million increase in patronage from another System bank and the $1.2 million write-off in the fourth quarter of 2006 of patronage receivable from the Funding Corporation, offset by an $825 decrease in loan prepayment fees, a decrease of $364 in gains on sales of investments and a $287 adjustment decreasing the bank's gain recognized on the bank's portion of property sold by the Farm Credit System Building Association during 2006.

Noninterest income for 2006 of $21.3 million reflected an increase of $3.3 million, or 18.2 percent, from 2005 to 2006. The increase is mainly attributable to a $1.2 million increase in loan-related fee income and a $1.9 million increase in other gains, including a $907 gain on the sale of investments in 2006.

Provision for Loan Losses

The provision for loan losses for 2007 was $43.1 million, reflecting an increase of $33.7 million from the $9.4 million provision

Figure 1

Analysis of Net Interest Income

	2007 Avg. Balance	2007 Interest	2006 Avg. Balance	2006 Interest	2005 Avg. Balance	2005 Interest
Loans	**$ 13,940,105**	**$ 1,053,629**	$ 11,272,884	$ 845,135	$ 9,170,084	$ 595,995
Investments	**2,598,854**	**131,768**	2,929,742	141,260	2,034,438	76,735
Total earning assets	**16,538,959**	**1,185,397**	14,202,626	986,395	11,204,522	672,730
Interest-bearing liabilities	**14,336,782**	**753,016**	12,132,268	600,149	9,369,900	332,258
Impact of capital	**$ 2,202,177**		$ 2,070,358		$ 1,834,622	
NET INTEREST INCOME		**$ 432,381**		$ 386,246		$ 340,472

	2007 Average Yield	2006 Average Yield	2005 Average Yield
Yield on loans	**7.56%**	7.50%	6.50%
Yield on investments	**5.07**	4.82	3.77
Yield on earning assets	**7.17**	6.95	6.00
Cost of interest-bearing liabilities	**5.25**	4.95	3.55
Interest rate spread	**1.92**	2.00	2.45
Impact of capital	**0.69**	0.72	0.59
Net interest income/average earning assets	**2.61**	2.72	3.04

recorded in 2006. The increase is due primarily to the provisions by associations related to the participation loans to one borrower. For more information on these participation loans, see the "Loan Portfolio" section of this discussion.

Noninterest Expenses

Noninterest expenses for 2007 totaled $171.4 million, increasing $13.1 million, or 8.3 percent, from 2006. The increase was primarily due to an increase of $4.8 million in premiums to the Farm Credit System Insurance Corporation (FCSIC or Insurance Fund), an increase of $3.6 million in salaries and employment benefits, an increase of $3.8 million in other operating expenses, and an increase of $1.0 in occupancy and equipment expense. The $4.8 million increase in premiums paid to the FCSIC was primarily due to volume increases on the loans on which premiums are assessed. The $3.6 million increase in salaries and employee benefits was due primarily to a $7.9 million increase in compensation and related payroll taxes, a $1.2 million increase in pension and retirement expenses, and an $861 increase in other benefits, substantially offset by a $6.4 million increase in capitalization of salaries and benefits in accordance with FAS 91. Compensation and payroll-related taxes increased due to increases in compensation rates and in the number of employees at district associations and at the bank. The $3.8 million increase in other operating expenses was primarily due to a $2.3 million increase in professional and contract services (including an $894 increase in legal fees, primarily related to the participation loans to the borrower described in the High-Risk Assets section), a $594 increase in advertising and member relations expenses, a $415 increase in supervisory and examination expenses, a $357 increase in travel expenses, a $322 increase in training expenses, and a $305 increase in directors' expenses.

Noninterest expenses for 2006 totaled $158.3 million, increasing $21.4 million, or 15.6 percent, from 2005. The increase was primarily due to an increase of $11.7 million in premiums to the Insurance Fund, an increase of $5.8 million in salaries and employment benefits, an increase of $4.7 million in other operating expenses, partially offset by a $1.9 million decrease in intra-System financial assistance expense. Premiums to the Insurance Fund rose as a result of increased premium rates effective in 2006 compared with 2005 and increased loan volume to which the rates are applied. Salaries and employment benefits for 2006 increased due to a $5.9 million increase in compensation and related payroll taxes and a $1.1 million increase in pension and retirement expenses, offset by a $1.2 million decrease in other benefits. Compensation and payroll-related taxes increased primarily due to increases in compensation rates and increases in the number of employees at the district's associations from 2005 to 2006. Other benefits decreased due to the effects of changes in coverage of postretirement plans sponsored by district employers in an effort to control costs for these benefits. The increase in other operating expenses included a $2.2 million increase in advertising and member relations expenses, an $884 increase in travel-related expenses, an $803 increase in property and casualty insurance, and a $692 increase in expenses related to directors' compensation and travel. Intra-System financial assistance expenses decreased due to the maturity and retirement of the last of the remaining issuances of debt obligations at the end of the second quarter of 2005.

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,

	2007	2006	2005
Excess of net interest income over operating expense	**$ 261,023**	$ 228,017	$ 205,418
Operating expense as a percentage of net interest income	**39.6%**	41.0%	39.7%
Operating expense as a percentage of net interest income and noninterest income	**37.5**	38.8	37.7
Operating expense as a percentage of average loans	**1.23**	1.40	1.47
Operating expense as a percentage of average earning assets	**1.04**	1.11	1.21

The district's operating expense statistics for 2007 reflect the district's growth in net interest income, which outpaced increases in operating expenses, and also the growth in the district's earning assets. In 2006, the increase in operating expenses was greater than the growth of net interest income. Net interest income has increased 11.9 percent and 13.4 percent for the years ended December 31, 2007 and 2006, respectively, while operating expenses increased at the rates of 8.3 percent and 17.2 percent, respectively, for the same periods.

CORPORATE RISK PROFILE

Overview

The district 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 and its related associations are 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 Federal Farm Credit Banks Funding Corporation's (Funding Corporation) 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, 2007, 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.

Loan Portfolio

The loan portfolio consists only of retail loans. Bank loans to its affiliated associations have been eliminated in the combined financial statements. Gross loan volume of $15.11 billion at December 31, 2007, reflected an increase of $2.20 billion, or 17.0 percent, from the $12.91 billion loan portfolio balance at December 31, 2006. Loans, net of the allowance for loan losses, represented 83.8 percent, 80.6 percent and 77.3 percent of total assets as of December 31, 2007, 2006 and 2005, respectively.

Agricultural real estate mortgage loans totaled $10.15 billion at December 31, 2007, an increase of $1.14 billion, or 12.7 percent, from 2006, and currently comprise approximately 67.2 percent of the district's loan portfolio. Commercial loans for agricultural production, processing and marketing totaled $3.34 billion, an increase of $706.5 million, or 26.9 percent, from 2006, and represented 22.1 percent of the loan portfolio at December 31, 2007. All other loans, including energy loans, communications loans, farm-related business loans, rural home loans and loans to OFIs, increased by $358.5 million to $1.63 billion. The composition of the district's loan portfolio by category may be found in Note 4, "Loans and Allowance for Loan Losses." The primary factors contributing to the growth in the district's loan volume included an increased focus on market share and loan growth opportunities within the territory; competitive pricing; increased marketing and customer service efforts by the associations; and growth in loan participations.

The bank and district associations review the credit quality of the loan portfolio as a part of their credit risk practices, using the classifications of the Uniform Classification System which is used by all System institutions. The classifications are defined as follows:

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

The following table discloses the credit quality of the district's loan portfolio at December 31,

	2007	2006	2005
Acceptable	**97.2 %**	97.1%	96.5%
Special mention	**1.6**	1.8	1.9
Substandard	**1.2**	1.1	1.6
Total	**100.0%**	100.0%	100.0%

During 2007, overall credit quality remained strong. Loans classified (under the Farm Credit Administration's Uniform Loan Classification System) as "acceptable" or "other assets especially mentioned" as a percentage of total loans and accrued interest receivable were 98.8 percent at December 31, 2007, compared to 98.9 percent at December 31, 2006, and 98.4 percent at December 31, 2005.

Twelve associations in the district, along with two other Farm Credit associations, participated in a loan to one borrower with the original funded balance of $68.5 million. The district's associations held $56.3 million of this original balance. During 2007, the loan was deemed to be nonaccrual due to its significant undercollateralized position and a credit default. The lead lending association in the district has pursued collection efforts and liquidated a part of the collateral, which was applied towards the outstanding balance of all participants. Five of the associations in the district repurchased the participation interests in the loan held by the two other Farm Credit associations as well as the other seven associations in the district. As of December 31, 2007, the district associations have recorded net charge-offs of approximately $28.9 million and specific reserves remaining of approximately $1.46 million. The loan has a remaining book balance of $10.7 million at December 31, 2007. The bank does not have a participation interest in this loan.

High-Risk Assets

Total high-risk assets have increased by $78.8 million, or 170.6 percent, from $46.2 million at December 31, 2006, to $125.0 million at December 31, 2007. The increase is primarily attributable to a $63.9 million increase in nonaccrual loans which includes the addition of participations held by district associations as well as $23.8 million in two loans held by the bank. These loans are highly collateralized and, where appropriate, provisions for loan losses have been recorded. The increase in loans past due 90 days or more and still accruing interest was due primarily to one $10.0 million participation loan. This loan is well secured, and full collection of principal and interest is expected.

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

(in millions)	**2007**	2006	2005
Nonaccrual loans	**$ 100.1**	$ 36.2	$ 29.1
Formally restructured loans	**6.2**	7.2	7.1
Loans past due 90 days or more and still accruing interest	**16.9**	0.8	2.7
Other property owned, net	**1.8**	2.0	3.9
Total	**$ 125.0**	$ 46.2	$ 42.8

At December 31, 2007, $79.5 million, or 79.4 percent, of loans classified as nonaccrual were current as to principal and interest, compared to $24.5 million, or 67.8 percent, of nonaccrual loans at December 31, 2006, and $19.5 million, or 67.1 percent, at December 31, 2005.

Figures 2, 3 and 4 provide analyses of the relationships of nonaccrual loans and high-risk assets to total loans and members' equity at December 31, 2007, 2006 and 2005.

Allowance and Provision for Loan Losses

At December 31, 2007, the allowance for loan losses was $24.5 million, or 0.16 percent of total loans outstanding, compared to $14.0 million (0.11 percent) and $9.5 million (0.09 percent) at December 31, 2006 and 2005, respectively. Net charge-offs of $32.6 million, $4.9 million and $2.2 million were recorded in 2007, 2006 and 2005, respectively. The district's net provision for loan losses of $43.1 million for 2007 reflected an increase of $33.7 million, or 358.5 percent, from the $9.4 million provision recorded for 2006, due primarily to provision related to the participation loan described in the "Provision for Loan Losses" section of this discussion. The allowance for loan losses for the district represents the aggregate of each entity's individual evaluation of its allowance for loan losses requirements. Although aggregated in the combined financial statements, the allowance for loan losses of each entity is particular to that institution and is not available to absorb losses realized by other institutions. The allowance for loan losses at each period end was considered by management to be adequate to absorb probable losses existing in and inherent to its loan portfolio. Management's evaluations consider factors including loan loss experience, portfolio quality, loan portfolio composition, current agricultural production conditions and economic conditions.

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

	2007	2006	2005
Allowance for loan losses as a percentage of:			
Average loans	**0.2%**	0.1%	00.1%
Loans at year end			
Total loans	**0.2**	0.1%	0.1
Nonaccrual loans	**24.5**	38.6	32.8
Total impaired loans	**19.9**	31.6	24.5
Net charge-offs to average loans	**0.2**	<0.1	<0.1
Provision expense to average loans	**0.3**	0.1	<0.1

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 district'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 district'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 district'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 rate sensitivity gap analysis in Figure 5 sets forth a static measurement of the district's volume of interest-rate-sensitive assets and liabilities outstanding as of December 31, 2007, which are projected to mature or reprice in each of the future time periods shown. The "interest rate sensitivity gap" line reflects the mismatch, or gap, in

Figure 2

Nonaccrual Loans
as a Percentage of Total Loans
at Year End

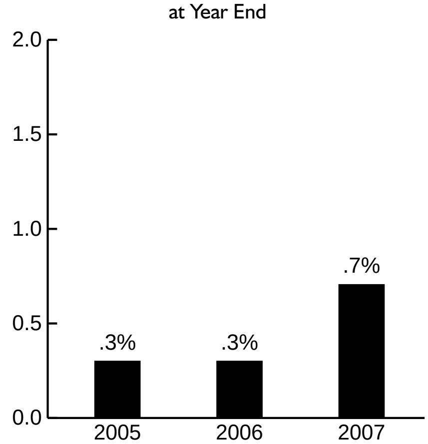


Figure 3

High-Risk Assets
as a Percentage of Total Members' Equity
at Year End

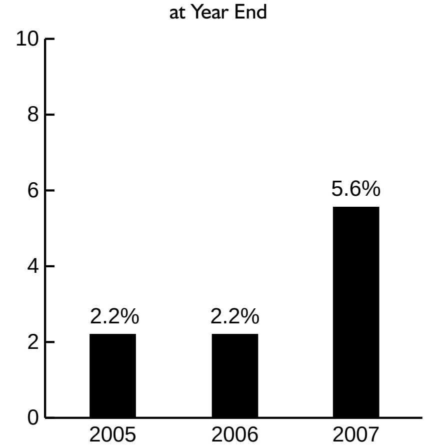


Figure 4

High-Risk Assets
as a Percentage of Total Loans and
Other Property Owned at Year End

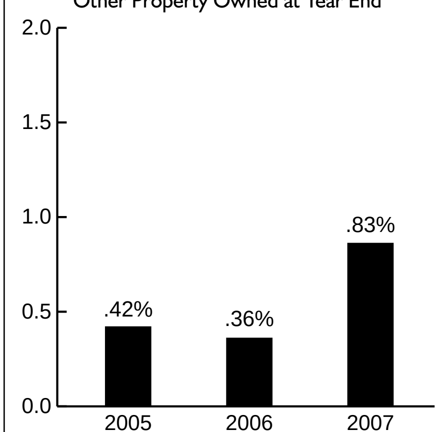


Figure 5

Interest Rate Gap Analysis
as of December 31, 2007

	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**
Earning Assets							
Total loans	$ 6,504,745	$ 1,674,007	$ 1,135,487	**$ 9,314,239**	$ 4,204,471	$ 1,595,827	**$ 15,114,537**
Total investments	856,471	229,936	243,082	**1,329,489**	1,083,353	123,659	**2,536,501**
Total earning assets	7,361,216	1,903,943	1,378,569	**10,643,728**	5,287,824	1,719,486	**17,651,038**
Interest-Bearing Liabilities							
Total interest-bearing funds*	6,182,787	810,000	1,185,000	**8,177,787**	6,298,000	860,500	**15,336,287**
Excess of earning assets over interest-bearing liabilities	—	—	—	**—**	—	2,314,751	**2,314,751**
Total interest-bearing liabilities	6,182,787	810,000	1,185,000	**8,177,787**	6,298,000	3,175,251	**$ 17,651,038**
Interest rate sensitivity gap	$ 1,178,429	$ 1,093,943	$ 193,569	**$ 2,465,941**	$ (1,010,176)	$ (1,455,765)	
Cumulative interest rate sensitivity gap	$ 1,178,429	$ 2,272,372	$ 2,465,941	**$ 2,465,941**	$ 1,455,765		

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

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 district has a positive gap position, indicating that the district has an exposure to declining interest rates. This occurs when maturing or repricing interest-rate-sensitive assets are replaced by loans and investments earning lower market interest rates, while corresponding funding costs decrease more slowly due to the lag in their maturity or repricing cycle.

To more appropriately reflect the cash flow and repricing characteristics of the district's balance sheet, an estimate of expected prepayments on loans is reflected in the maturities of the loans in the earning assets section of Figure 5. 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 district's balance sheet.

The bank uses derivative financial instruments to manage the district's 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. 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, 2007, the bank had three fair value interest rate swap contracts with a total notional amount of $175 million. The fair value swap contracts had a net fair value of $5.8 million, which is reflected in bonds and notes, net. In addition, the bank had six cash flow interest rate swaps with a total notional amount of $750 million; these cash flow hedges had a net positive fair value of $1.0 million at December 31, 2007. 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. Figure 6 summarizes the bank's activity in derivative financial instruments for 2007.

Interest rate risk exposure is measured by simulation modeling, which calculates the district'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 the district's financial exposure to instantaneous and parallel changes in interest rates of 200 basis points up or down over a rolling 12-month period. As of December 31, 2007, projected district net interest income would increase by $41.5 million, or 9.4 percent, if interest rates were to increase by 200 basis points, and would increase by $9.8 million, or 2.2 percent, if interest rates were to decrease by 200 basis points. In general, the bank's ability to exercise call options on debt benefit the district in the event of decreasing interest rates. In a rising interest rate scenario, the benefit of rate increases on association loans and the bank's participation loans would outpace the increase in the cost of debt.

Liquidity Risk Management

The district'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

Figure 6

Activity in Derivative Financial Instruments
(Notional Amounts)

(in millions)	
Balance, December 31, 2006	$ 440
Additions	1,225
Maturities/calls	(165)
Terminations	(575)
Balance, December 31, 2007	**$ 925**

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 following tables provide a summary of the debt obligations of the district *(dollars in millions)*:

	December 31,		
	2007	2006	2005
Bonds and term notes outstanding	**$ 11,464**	$ 11,354	$ 9,155
Average effective interest rate	**4.98%**	5.04%	4.13%
Average life (years)	**3.2**	2.7	1.8
Discount notes outstanding	**$ 1,160**	$ 767	$ 1,408
Average effective interest rate	**4.10%**	5.23%	4.11%
Average life (days)	**39**	29	35
Notes payable to other System banks	**$ 2,700**	$ 1,400	$ 400
Average effective interest rate	**5.74%**	5.84%	4.81%
Average life (years)	**1.0 or less**	1.0 or less	1.0 or less

	For the years ended December 31,		
	2007	2006	2005
Average interest-bearing liabilities outstanding	**$ 14,337**	$ 12,132	$ 9,370
Average interest rates on interest-bearing liabilities	**5.25%**	4.95%	3.55%

Liquidity Standard

The banks have jointly developed and adopted a Common Minimum Liquidity 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 that 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, 2007, the bank had 121 days of liquidity coverage, as compared with 151 days at December 31, 2006. The decrease in the number of days of liquidity is due to a shift in the bank's earning assets from investments to loans for capital management purposes.

In 2007, the bank sold an additional $1.3 billion of participations in six 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 and to achieve the bank's capital management goals.

The district had no commercial bank lines of credit in use at December 31, 2007.

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 Farm Credit Administration (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. Farm Credit Administration regulations also permit an association to hold eligible investments with the approval of its affiliated bank.

Farm Credit Administration 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 develop and submit to the FCA a divestiture plan that includes disposal of an asset that becomes ineligible.

The following table discloses the district's holdings in federal funds and investment securities at December 31,

	2007	2006	2005
Mortgage-backed securities	**$ 1,801,734**	$ 1,921,980	$ 1,722,663
Money market instruments	**219,475**	131,349	550,914
Asset-backed securities	**210,950**	384,035	424,299
Corporate debt	**178,840**	234,878	—
Federal funds	**125,502**	89,229	42,444
Total available investments	**$ 2,536,501**	$ 2,761,471	$ 2,740,320

At December 31, 2007, the bank's investment portfolio included $187.0 million of asset-backed securities supported by first lien home equity mortgages. In view of the recent economic conditions and volatility related to these types of securities, the bank is actively monitoring the creditworthiness of these securities, which were all rated Aaa by Moody's Investors Service or AAA by Standard & Poor's at year end. These securities are supported by various forms of credit enhancements including favorable priority of payments, overcollateralization, excess spread and insurance guarantees. Based on our evaluations, we believe these securities do not pose a significant risk of loss given the credit enhancements and relatively short weighted average lives. Since year end, one of the securities in question with a book value of $4.9 million and a fair value of $4.0 million was downgraded by Moody's Investors Service from Aaa to A3 and by Standard & Poor's from AAA to A. As a result of these rating

Figure 7

Members' Equity
as a Percentage of Net Loans
at Year End

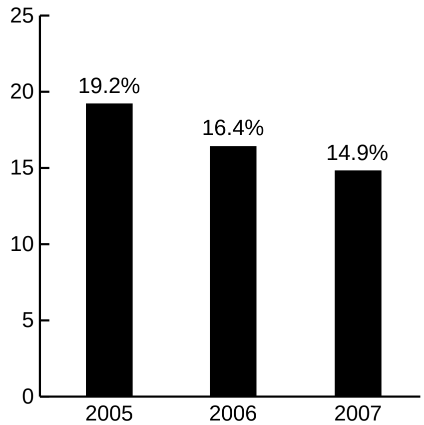


Figure 8

Members' Equity
as a Percentage of Total Assets
at Year End

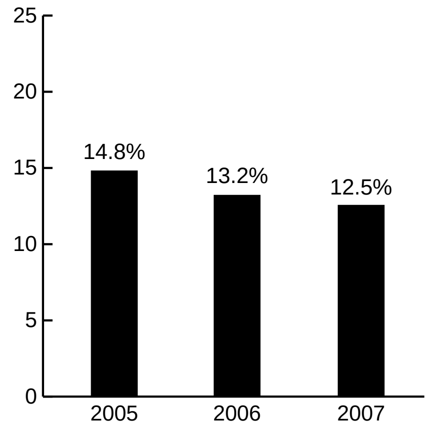
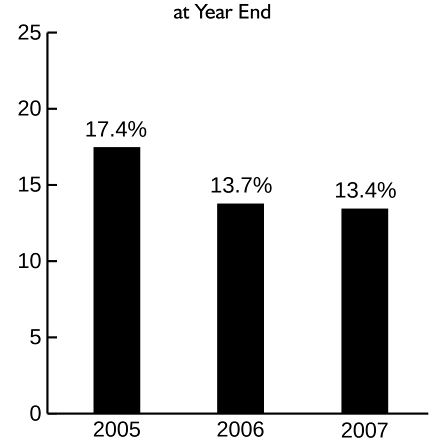


Figure 9

Regulatory Permanent
Capital Ratio (bank)
at Year End



actions, the bank is in the process of developing a plan of divestiture to comply with regulatory policy.

The composition and characteristics of the district's investment securities are described in Note 3, "Investment Securities."

Capital Adequacy

In November 2003, the bank issued 100,000 shares of $1,000 Cumulative Perpetual Preferred Stock for net proceeds of $98.6 million. The preferred stock is treated as equity and is not mandatorily redeemable. The preferred stock was issued for general corporate purposes. In September 2005, an additional 100,000 shares of $1,000 Cumulative Perpetual Preferred Stock was issued for net proceeds of $108.9 million, which included $2.1 million in accrued dividends payable. Net proceeds from the additional issue were used to enhance the composition of the bank's capital and liquidity position; to support the bank's loan growth; to provide a base for further growth and service opportunities to our members and to rural America; and for general corporate purposes.

Borrower equity purchases required by association capitalization bylaws (see Note 8, "Members' Equity"), combined with a history of growth in retained earnings at district institutions, have resulted in district institutions being able to maintain strong capital positions. The $2.25 billion capital position of the district at December 31, 2007, reflects an increase of 6.6 percent over the December 31, 2006, capital position of $2.11 billion. This increase is attributable to the $242.5 million of net income earned in 2007; issuances of capital stock, participation certificates and allocated retained earnings of $12.9 million; a decrease in net unrealized losses on investments of $16.5 million; an increase of net unrealized gains in cash flow derivatives of $1.0 million, offset by dividend and patronage distributions of $91.4 million; an adjustment to accumulated other comprehensive income of $30.6 million resulting from the adoption of Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" (SFAS 158); and retirements of capital stock, participation certificates and allocated retained earnings of $18.0 million.

The return on average members' equity for the year ended December 31, 2007, was 10.9 percent, compared to 11.7 percent and 11.8 percent reported for the years ended December 31, 2006 and 2005, respectively.

On December 31, 2007, the bank and its related associations adopted SFAS 158, which requires the recognition of a plan's over-funded or under-funded status as an asset or liability with an offsetting adjustment to accumulated other comprehensive income, net of tax. SFAS 158 requires the determination of the fair values of a plan's assets at year end, and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of accumulated other comprehensive losses, net of tax. The net charge against the district's accumulated other comprehensive loss resulting from the adoption of SFAS 158 was $30.6 million. These amounts were previously netted against the plans' funded status in the district's combined statement of condition pursuant to the provisions of SFAS 87. These amounts will be subsequently recognized as components of net periodic benefit costs. Further, actuarial gains and losses that arise in subsequent periods that are not initially recognized as a component of net periodic benefit cost will be recognized as a component of accumulated other comprehensive income, net of tax. Those amounts will subsequently be recognized as a component of net periodic benefit cost as they are amortized during future periods.

FCA regulations require System institutions to compute a total surplus ratio, a core surplus ratio and a net collateral ratio (bank only), and maintain at least the minimum standard for each ratio. In those instances where an entity may not be in compliance, the regulations require the entity to submit a corrective plan to the FCA designed to move the institution into compliance. As of December 31, 2007, the bank and all district associations were in compliance with the regulations. Note 8, "Members' Equity," outlines the ranges of capital ratios for the bank and district associations. The bank's permanent capital ratio of 13.43 percent at December 31, 2007, is considered adequate, in accordance with the capital plan adopted by the bank's board of directors. An analysis of the trend in the district's capital ratios is presented in Figures 7, 8 and 9.

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.

Association Structural Changes

As of December 31, 2007 and 2006, there were 14 ACAs and six FLCAs, totaling 20 associations within the district. As of December 31, 2005, there were 13 ACAs and eight FLCAs, totaling 21 associations within the district. During 2006, two of the district's ACAs merged and two FLCAs restructured to form ACA parent structures with operating FLCA and Production Credit Association subsidiaries.

Regulatory Matters

During the year ended December 31, 2007, the Farm Credit Administration 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, 2007.

In September 2007, the Farm Credit Administration issued a final rule and a direct final rule amending the priority of claims regulations. The final rule amended the priority of claims regulations to give the same subrogation rights to a bank that makes a joint and several liability payment under a written agreement as the bank has under a statutory joint and several call. The Farm Credit Administration must approve the written agreement. The direct final rule amended the priority of claims regulations to clarify that subordinated claims are to be paid after the claims of general creditors are paid in full.

On October 31, 2007, the Farm Credit Administration published an advanced notice of public rule-making in the Federal Register with respect to the consideration of possible modifications to the Farm Credit Administration's risk-based capital rules for Farm Credit System institutions that are similar to the standardized approach delineated in the Basel II Framework. The Farm Credit Administration is seeking comments to facilitate the development of a proposed rule that would enhance their regulatory capital framework and more closely align minimum capital requirements with risks taken by System institutions. Comments on the advanced notice of public rule-making are due no later than March 31, 2008. The System is in the process of developing a comment letter to provide to the Farm Credit Administration on the advanced notice of public rule-making.

The current farm bill is scheduled to expire on March 15, 2008. In July 2007, the House of Representatives passed its version of a new farm bill. The Senate passed its version in December 2007. The measure is now in a conference committee, where the differences between the two versions will be worked out among conferees. A consolidated version will then be sent to the President for his consideration. Under both versions, payments to farmers under the commodity programs, i.e., direct and countercyclical payments and loan deficiency payments, would be reduced by varying degrees over the next 10 years. However, the specific provisions of the final farm bill may increase payments for certain commodities, or increase them in certain years and reduce them in others. This farm bill is also expected to revise certain income payment limitations.

Both the House of Representatives and the Senate versions contain provisions that would expand certain authorities of the Farm Credit System Insurance Corporation. The proposed changes generally would authorize the Insurance Corporation to collect higher levels of premiums and expand the base upon which premiums are charged. Premiums of up to 20 basis points could be charged against insured debt adjusted for government-guaranteed loans and up to an additional 10 basis points could be charged for any loan volume that is nonaccrual or investments that are other-than-temporarily impaired. Currently, premiums of up to 15 basis points may be charged on accruing loans and up to 25 basis points for nonaccrual loans.

Report of Audit Committee

The Farm Credit Bank of Texas and the Tenth Farm Credit District Associations

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 district'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 2007, four committee meetings were held. At the first of their meetings, the committee approved the appointment of PricewaterhouseCoopers LLP (PwC) as independent auditors for 2007.

Management is responsible for the district's internal controls and 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 district'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 district's audited financial statements for the year ended December 31, 2007 (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 district'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 district. 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 2007 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
Joe R. Crawford, Vice Chairman
Ralph W. Cortese
Jon M. Garnett
C. Kenneth Andrews
James F. Dodson
Elizabeth G. Flores

Audit Committee Members

February 29, 2008

PRICEWATERHOUSECOOPERS

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

Report of Independent Auditors

To the Board of Directors and Shareholders
of the Farm Credit Bank of Texas and
the Tenth Farm Credit District Associations

In our opinion, the accompanying combined balance sheets and the related combined statements of income, of changes in members' equity and of cash flows present fairly, in all material respects, the financial position of the Farm Credit Bank of Texas (bank) and the Tenth Farm Credit District associations (district) at December 31, 2007, 2006 and 2005, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These combined financial statements are the responsibility of the district's management. Our responsibility is to express an opinion on these combined 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 combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined 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

February 29, 2008

Combined Financial Statements

Combined Balance Sheets

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

	December 31,		
(dollars in thousands)	**2007**	2006	2005
Assets			
Cash	**$ 55,703**	$ 60,170	$ 51,847
Federal funds sold and securities purchased under resale agreements	**125,502**	89,229	42,444
Investment securities	**2,410,999**	2,672,242	2,697,876
Loans	**15,114,537**	12,905,321	10,219,596
Less allowance for loan losses	**24,495**	13,969	9,533
Net loans	**15,090,042**	12,891,352	10,210,063
Accrued interest receivable	**228,212**	204,603	146,769
Other property owned, net	**1,817**	2,020	3,902
Premises and equipment, net	**42,599**	40,635	37,982
Other assets	**41,623**	26,816	21,337
Total assets	**$ 17,996,497**	$ 15,987,067	$ 13,212,220
Liabilities and members' equity			
Liabilities			
Bonds and notes, net	**$ 15,324,015**	$ 13,520,784	$ 10,963,278
Accrued interest payable	**122,459**	102,585	61,718
Patronage distributions payable	**63,899**	60,073	42,676
Other liabilities	**235,463**	190,965	189,453
Total liabilities	**15,745,836**	13,874,407	11,257,125
Commitments and contingencies (Note 12)			
Members' equity			
Preferred stock	**202,754**	203,565	203,569
Common stock and participation certificates	**62,489**	59,068	73,642
Allocated retained earnings	**133,423**	83,705	32,327
Unallocated retained earnings	**1,886,488**	1,792,723	1,692,534
Accumulated other comprehensive loss	**(34,493)**	(26,401)	(46,977)
Total members' equity	**2,250,661**	2,112,660	1,955,095
Total liabilities and members' equity	**$ 17,996,497**	$ 15,987,067	$ 13,212,220

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

Combined Statements of Income

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

	Year Ended December 31,		
(dollars in thousands)	**2007**	2006	2005
Investment securities, federal funds sold and securities purchased under resale agreements	**$ 131,768**	$ 141,260	$ 76,735
Loans	**1,053,629**	845,135	595,995
Total interest income	**1,185,397**	986,395	672,730
Bonds and notes	**653,972**	562,211	316,201
Notes payable and other	**99,044**	37,938	16,057
Total interest expense	**753,016**	600,149	332,258
Net interest income	**432,381**	386,246	340,472
Provision for loan losses	**43,131**	9,356	1,084
Net interest income after provision for loan losses	**389,250**	376,890	339,388
Fees for loan-related services	**14,429**	15,255	14,028
Gain from sale of investment securities	**503**	907	—
Miscellaneous income, net	**9,888**	5,160	4,017
Total noninterest income	**24,820**	21,322	18,045
Salaries and employee benefits	**88,489**	84,936	79,133
Occupancy and equipment expense	**12,394**	11,422	10,524
Insurance Fund premiums	**21,092**	16,328	4,587
Losses (gains) on other property owned, net	**31**	93	(42)
Intra-System financial assistance expenses	**—**	—	1,905
Other operating expenses	**49,383**	45,543	40,810
Total noninterest expense	**171,389**	158,322	136,917
Income before income taxes	**242,681**	239,890	220,516
Provision for (benefit from) income taxes	**141**	(228)	639
Net income	**$ 242,540**	$ 240,118	$ 219,877

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

Combined Statements of Changes in Members' Equity

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

(dollars in thousands)	Preferred Stock	Common Stock and Participation Certificates	Retained Earnings Allocated	Retained Earnings Unallocated	Retained Earnings Total	Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
Balance at December 31, 2004	$ 103,963	$ 88,962	$ 32,662	$ 1,531,503	$ 1,564,165	$ (20,961)	$ 1,736,129
Comprehensive income							
Net income	—	—	—	219,877	219,877	—	219,877
Unrealized net losses on investment securities	—	—	—	—	—	(18,310)	(18,310)
Unrealized net losses on cash flow hedge derivatives	—	—	—	—	—	(262)	(262)
Minimum pension liability adjustment	—	—	—	—	—	(7,444)	(7,444)
Total comprehensive income	—	—	—	219,877	219,877	(26,016)	193,861
Preferred stock issued	100,000	—	—	—	—	—	100,000
Premium received on preferred stock net of issuance costs	—	—	—	6,773	6,773	—	6,773
Capital stock/participation certificates issued	—	23,983	—	—	—	—	23,983
Capital stock/participation certificates and allocated retained earnings retired	(394)	(39,303)	(6,770)	—	(6,770)	—	(46,467)
Cash dividends on preferred stock	—	—	—	(9,220)	(9,220)	—	(9,220)
Patronage distributions							
Cash	—	—	—	(49,964)	(49,964)	—	(49,964)
Members' equity	—	—	6,435	(6,435)	—	—	—
Balance at December 31, 2005	203,569	73,642	32,327	1,692,534	1,724,861	(46,977)	1,955,095
Comprehensive income							
Net income	—	—	—	240,118	240,118	—	240,118
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)
Minimum pension liability adjustment	—	—	—	—	—	15,916	15,916
Total comprehensive income	—	—	—	240,118	240,118	20,576	260,694
Capital stock/participation certificates issued	—	22,878	—	—	—	—	22,878
Capital stock/participation certificates and allocated retained earnings retired	(4)	(37,452)	(2,950)	—	(2,950)	—	(40,406)
Cash dividends on preferred stock	—	—	—	(15,122)	(15,122)	—	(15,122)
Patronage distributions							
Cash	—	—	—	(70,479)	(70,479)	—	(70,479)
Members' equity	—	—	54,328	(54,328)	—	—	—
Balance at December 31, 2006	203,565	59,068	83,705	1,792,723	1,876,428	(26,401)	2,112,660
Comprehensive income							
Net income	—	—	—	242,540	242,540	—	242,540
Net change in unrealized net losses on investment securities	—	—	—	—	—	16,513	16,513
Net change in unrealized gains on cash flow hedge derivatives	—	—	—	—	—	1,047	1,047
Minimum pension liability adjustment	—	—	—	—	—	4,931	4,931
Total comprehensive income	—	—	—	242,540	242,540	22,491	265,031
Adjustment to initially apply SFAS 158	—	—	—	—	—	(30,583)	(30,583)
Capital stock/participation certificates issued	—	12,926	—	—	—	—	12,926
Capital stock/participation certificates and allocated retained earnings retired	(811)	(9,505)	(7,682)	—	(7,682)	—	(17,998)
Cash dividends on preferred stock	—	—	—	(15,122)	(15,122)	—	(15,122)
Patronage distributions							
Cash	—	—	—	(76,253)	(76,253)	—	(76,253)
Members' equity	—	—	57,400	(57,400)	—	—	—
Balance at December 31, 2007	**$ 202,754**	**$ 62,489**	**$ 133,423**	**$1,886,488**	**$2,019,911**	**$ (34,493)**	**$ 2,250,661**

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

Combined Statements of Cash Flows

FARM CREDIT BANK OF TEXAS AND DISTRICT ASSOCIATIONS

(dollars in thousands)	Year Ended December 31, 2007	2006	2005
Operating Activities			
Net income	**$ 242,540**	$ 240,118	$ 219,877
Reconciliation of net income to net cash provided by operating activities			
Provision for loan losses	**43,131**	9,356	1,084
Provision (negative provision) for losses on other property owned	**133**	249	(46)
Depreciation and amortization on premises and equipment	**5,375**	5,029	4,625
Accretion of net discount on loans	**(1,876)**	(344)	(3,434)
Amortization and accretion on debt instruments	**(1,759)**	(660)	7,776
Accretion of net (discount) premium on investments	**(3,004)**	3,626	7,009
Gains on sale of investment securities	**(503)**	(907)	—
Losses (gains) on sales of other property owned, net	**34**	256	(14)
Gains on sales of premises and equipment	**(1,978)**	(6,422)	(4,217)
Increase in accrued interest receivable	**(23,609)**	(57,834)	(40,560)
(Increase) decrease in other assets, net	**(9,615)**	(4,768)	15,277
Increase in accrued interest payable	**19,874**	40,867	24,167
Decrease in intra-System financial assistance payable	**—**	—	(77)
Increase in other liabilities, net	**13,716**	16,836	24,142
Net cash provided by operating activities	**282,459**	245,402	255,609
Investing Activities			
Net (increase) decrease in federal funds sold and securities purchased under resale agreements	**(36,273)**	(46,785)	5,056
Investment securities available for sale:			
Purchases	**(3,971,804)**	(6,666,471)	(4,653,111)
Proceeds from maturities, calls and prepayments	**4,159,943**	6,587,280	3,717,622
Proceeds from sales	**93,123**	107,814	—
Increase in loans, net	**(2,239,909)**	(2,688,924)	(1,772,641)
Proceeds from sale of loans	**1,300,000**	1,000,000	100,000
Proceeds from sales of premises and equipment	**4,255**	4,033	6,471
Expenditures for premises and equipment	**(9,616)**	(5,293)	(9,878)
Net cash used in investing activities	**(700,281)**	(1,708,346)	(2,606,481)
Financing Activities			
Bonds and notes issued	**31,248,805**	28,809,507	24,454,370
Bonds and notes retired	**(30,751,324)**	(27,261,180)	(22,126,945)
Increase (decrease) in advanced conditional payments	**8,495**	8,440	6,020
Preferred stock issued, net of expenses	**—**	—	106,773
Capital stock and participation certificates issued	**12,926**	22,878	23,983
Capital stock and participation certificates retired and allocated retained earnings distributed	**(17,998)**	(40,406)	(46,467)
Cash dividends on preferred stock	**(15,122)**	(15,122)	(9,220)
Cash dividends and patronage distributions paid	**(72,427)**	(52,850)	(49,964)
Net cash provided by financing activities	**413,355**	1,471,267	2,358,550
Net (decrease) increase in cash	**(4,467)**	8,323	7,678
Cash at beginning of year	**60,170**	51,847	44,169
Cash at end of year	**$ 55,703**	$ 60,170	$ 51,847
Supplemental Schedule of Noncash Investing and Financing Activities			
Financed sales of other property owned	**$ 4,079**	$ 2,575	$ 3,618
Loans transferred to other property owned	**4,043**	4,464	2,276
Net decrease (increase) in unrealized losses on investment securities	**21,444**	5,708	(18,310)
Patronage distributions payable	**63,899**	60,073	42,676
Supplemental Schedule of Noncash Changes in Fair Value Related to Hedging Activities			
Increase (decrease) in bonds and notes	**$ 7,510**	$ 9,837	$ (2,097)
Supplemental Information			
Cash paid during the year for:			
Interest	**$ 733,142**	$ 559,282	$ 297,009
Income taxes	**315**	203	448

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

Notes to Combined Financial Statements

Farm Credit Bank of Texas and District Associations
(dollars in thousands, except per share amounts and as noted)

Note 1 — Organization and Operations

A. Organization:

The Farm Credit Bank of Texas (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 lending authorities of an FCB within its chartered territories. The bank is chartered to service the states of Alabama, Louisiana, Mississippi, New Mexico and Texas.

Each FCB and the ACB serve one or more Agricultural Credit Associations (ACAs) and/or Federal Land Credit Associations (FLCAs). The bank and its related associations collectively are referred to as the Tenth Farm Credit District (district). 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, 2007. FLCAs and ACAs collectively are referred to as associations.

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 borrower-stockholders for qualified agricultural purposes. District associations borrow the majority of funds from their related bank. The FCBs and the ACB obtain a substantial majority of their funds for lending operations through the sale of consolidated Systemwide bonds and notes to the public, but also obtain a portion of their funds from internally generated earnings and from the issuance of common and preferred stock and, to a lesser extent, from the issuance of subordinated debt.

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 the associations and defines the eligible borrowers which they may serve. The associations are authorized to provide, or participate with other lenders to provide, credit, credit commitments and related services to eligible borrowers. Eligible borrowers are defined as (a) bona fide farmers and ranchers and producers or harvesters of aquatic products, (b) persons furnishing to farmers and ranchers services directly related to their on-farm operating needs, (c) owners of rural homes, (d) rural residents and (e) farm-related businesses. The bank also may lend to any national bank, state bank, trust company, agricultural credit corporation, incorporated livestock loan company, savings institution, credit union or any association of agricultural producers (aggregately referred to as OFIs) engaged in the making of loans to farmers and ranchers, and any corporation engaged in the making of loans to producers or harvesters of aquatic products.

The associations also serve as intermediaries in offering credit life and multi-peril crop insurance and financial management services to their borrowers.

FCA regulations require borrower information be held in strict confidence by Farm Credit institutions, their directors, officers and employees. Directors and employees of the Farm Credit institutions are prohibited, except under specified circumstances, from disclosing nonpublic personal information about members.

FLCAs borrow funds from the bank and in turn originate and service long-term real estate mortgage loans made to their members. The OFIs borrow from the bank and, in turn, originate and service short- and intermediate-term loans for their members. The ACAs borrow from the bank and in turn may originate and service both long-term real estate mortgage and short- and intermediate-term loans to their members. ACAs may form a parent-subsidiary structure and may operate their long-term mortgage activities through an FLCA subsidiary and their short- and intermediate-term lending activities through a PCA subsidiary. In the states of Alabama and Mississippi, the bank may discount or purchase from FLCAs long-term real estate mortgage loans. In the states of Louisiana, New Mexico and Texas, the bank may discount or purchase from FLCAs and ACAs long-term real estate mortgage loans and, from ACAs, short- and intermediate-term loans.

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:

- Federal Farm Credit Banks Funding Corporation (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.

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 two percent of the 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. The premium is based on the average principal outstanding of accrual and nonaccrual loans of the district for the year. At December 31, 2007, the assets in the Insurance Fund were approximately $2.6 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 combined bank and associations conform to accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry. The preparation of combined financial statements in conformity with GAAP requires the managements of the bank and associations to make estimates and assumptions that affect the amounts reported in the combined financial statements and accompanying notes. Significant estimates are discussed in these notes as applicable. Certain amounts in prior years' combined financial statements have been reclassified to conform to the current year's presentation.

The accompanying combined financial statements include the accounts of the bank and associations, and reflect the investments in and allocated earnings of the service organizations in which the bank has partial ownership interests. All significant transactions and balances between the bank and associations have been eliminated in combination. The multi-employer structure of the district's defined benefit retirement plan results in the recording of the plan upon combination only.

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, 2007, 2006 and 2005. These investments are reported at fair value, and unrealized holding gains and losses are netted and reported as a separate component of members' equity in the combined balance sheets. Purchased premiums and discounts are amortized or accreted using the 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 and associations may also hold additional investments in accordance with mission-related investment programs, approved by the FCA.

C. Loans and Allowance for Loan Losses:

Long-term real estate mortgage loans generally have maturities ranging from five to 40 years. Substantially all short-term and intermediate-term loans are made for agricultural production or operating purposes and have maturities of 10 years or less.

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 district on behalf of the borrowers, where legal right of setoff exists, and which can be used to reduce outstanding loan balances at the district's discretion, are netted against loans in the combined balance sheets.

Loan origination fee income and salary and benefits expenses attributable to loans originated are deferred and amortized over the life of the related loans as an adjustment to yield.

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 or association 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.

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 based on a periodic evaluation of the loan portfolio by management in which numerous factors are considered, including economic conditions, loan portfolio composition and prior loan loss experience. The allowance for loan losses encompasses various judgments, evaluations and appraisals with respect to the loans and their underlying security that, by their nature, contain elements of uncertainty and imprecision. Changes in the agricultural economy and their impact on borrower repayment capacity will cause these various judgments, evaluations and appraisals to change over time. Accordingly, actual circumstances could vary significantly from the institutions' expectations and predictions of those circumstances. Managements consider the following factors in determining and supporting the levels of allowances for loan losses: the concentration of lending in agriculture, combined with uncertainties associated with farmland values, commodity prices, exports, government assistance programs, regional economic effects and weather-related influences. The allowance is increased through provisions for loan losses and loan recoveries and is decreased through reversals of provisions for loan losses and loan charge-offs. The level of allowance for loan losses is generally based on recent charge-off experience adjusted for relevant environmental factors.

The 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.

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 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 losses (gains) on other property owned, net.

E. Premises and Equipment:

Premises and equipment are carried at cost less accumulated depreciation. Land is carried at cost. 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 and associations are 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. ACPs which are held by the district but cannot be used to reduce outstanding loan balances, except at the direction of the borrower, are classified as other liabilities in the combined balance sheets. ACPs are not insured, and interest is generally paid by the associations on such balances. The total outstanding gross balances of advance conditional payments, both netted against loans and classified as other liabilities, at December 31, 2007, 2006 and 2005 were $309.0 million, $286.4 million and $248.1 million, respectively.

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 and associations participate in one of two districtwide retirement plans 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 401(k) plan, a certain percentage of employee contributions is matched by the bank and associations. The 401(k) plan costs are expensed as incurred.

As more fully described in Note 10, "Employee Benefit Plans," these plans are accounted for and reported in accordance with SFAS No. 87, "Employers' Accounting for Pensions," SFAS No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits," SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," SFAS No. 132, "Employers' Disclosures About Pensions and Other Postretirement Benefits," and SFAS No. 158, "Employers' Accounting for Defined Benefit Pension Plans and Other Postretirement Benefits." The bank and all but one association provide certain health care and life insurance benefits to eligible retired employees and directors. District employees' eligibility for these benefits upon retirement is dependent on conditions set by each district employer.

The structure of the district's defined benefit plan is characterized as multi-employer, since neither the assets, liabilities nor cost of any plan is segregated or separately accounted for by participating employers (bank and associations). No portion of any surplus assets is available to any participating employer, nor is any participating employer required to pay for plan liabilities upon withdrawal from the plans. As a result, participating employers of the plans 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. The majority of plan obligations, assets and the components of annual benefit expenses are recorded and reported upon combination only.

H. Income Taxes:

The bank, FLCAs and FLCA subsidiaries of ACA parent companies are exempt from federal and certain other income taxes as provided in the Farm Credit Act. The ACAs and their PCA subsidiaries provide for federal and certain other income taxes.

Certain ACAs operate as cooperatives which qualify for tax treatment under Subchapter T of the Internal Revenue Code. These ACAs and their PCA subsidiaries can exclude from taxable income amounts distributed as qualified patronage distributions to borrowers in the form of cash, stock or allocated retained earnings. Provisions for income taxes for these ACAs are made only on the earnings not distributed as qualified patronage distributions. Certain ACAs distribute patronage on the basis of taxable income. In this method, deferred income taxes are provided on the taxable income of ACAs on the basis of a proportionate share of the tax effect of temporary differences not allocated in patronage form. Other ACAs distribute patronage on the basis of book income. In this method, deferred taxes are recorded on the tax effect of all temporary differences based on the assumption that such temporary differences are retained by the institution and will therefore impact future tax payments. For all ACAs, a valuation allowance is provided for the deferred tax assets to the extent that it is more likely than not (over 50 percent probability), based on management's estimate, that they will not be realized. The consideration of valuation allowances involves various estimates and assumptions as to future taxable earnings, including the effects of our expected patronage program, which reduces taxable earnings.

As of December 31, 2007, deferred income taxes have not been provided by the ACAs and their PCA subsidiaries on $34.3 million of pre-1993 patronage distributions from the bank because management's intent is to (1) permanently invest these and other undistributed earnings in the bank, thereby indefinitely postponing their conversion to cash, or (2) pass through any distributions related to pre-1993 earnings to borrowers through qualified patronage allocations. No deferred taxes have been provided on the bank's post-1994 unallocated earnings. The bank currently has no plans to distribute unallocated bank earnings and does not contemplate circumstances which, if distributions were made, would result in income taxes being paid at the association level.

I. Derivative Instruments and Hedging Activity:

The bank is party to derivative financial instruments and cash flow hedges, consisting of interest rate swaps, which are principally used to manage interest rate risk on assets, liabilities and firm commitments. Derivatives are recorded on the balance sheet as assets and liabilities at fair value.

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 are reflected in accumulated other comprehensive income. 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, "Accounting for Derivative Instruments and Hedging Activities," and are presumed to be highly effective in offsetting changes in the fair value. The bank would discontinue hedge accounting prospectively when the bank determines that a derivative 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 July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes — an Interpretation of FASB Statement No. 109" (FIN 48 or interpretation) that was effective for fiscal years beginning after December 15, 2006. FIN 48 clarifies how an enterprise should recognize, measure, present and disclose in its financial statements uncertain tax positions that the enterprise has taken or expects to take on a tax return. Under the interpretation, the financial statements reflect expected future tax consequences of income tax positions presuming the relevant taxing authority's full knowledge of the position and all relevant facts, but without considering time values. FIN 48 is applicable to all uncertain positions for taxes accounted for under FASB Statement No. 109. The bank and its related associations adopted FIN 48 on January 1, 2007, and determined that interest and penalties would be classified as a component of income taxes.

There were no uncertain positions for income taxes or corresponding cumulative adjustment to beginning surplus at January 1, 2007. No district associations recorded uncertain tax positions during 2007.

The tax years that remain open for federal and major state income tax jurisdictions are 2005 and forward.

On September 30, 2006, the FASB 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 other comprehensive income. The standard further requires the determination of the fair value of plan assets at year end and recognition of actuarial gains and losses, prior service costs or credits, and transition assets and obligations as a component of other comprehensive income. The bank and its related associations adopted the standard on December 31, 2007. The adoption of this standard increased accumulated other comprehensive losses by approximately $30.6 million in 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 and its related associations use 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.

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 financial assets and liabilities and certain other items at fair value (the "fair value option"). Unrealized gains and losses on items for which the fair value option has been elected must 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 became effective as of January 1, 2008. The bank and its related associations have not made any elections under the fair value option, thus there is no impact from the adoption of the standard.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements." This statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. As a result, there is now a common definition of fair value to be used throughout generally accepted accounting principles. The FASB believes that the new standard will make the measurement of fair value more consistent and comparable, and will improve disclosures about those measures. This statement clarifies that the term fair value is intended to mean a market-based measure, not an entity-specific measure. In measuring fair value for a financial statement item, the statement sets forth a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The highest priority is given to quoted prices in active markets and the lowest priority to unobservable inputs. Additional disclosure requirements will be required for the lowest priority level. The statement became effective as of January 1, 2008. During 2007, the FASB became aware of numerous implementation issues as companies worked to adopt SFAS No. 157. Accordingly, the FASB agreed in November 2007 to propose a one-year deferral of the effective date for nonfinancial assets and liabilities that are recognized or disclosed at fair value on a nonrecurring basis. The FASB is expected to approve the proposed deferral in early 2008.

Note 3 — Investment Securities

A summary of the amortized cost and estimated fair value of investment securities available for sale at December 31, 2007, 2006 and 2005, follows.

	December 31, 2007				
	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Weighted Average Yield**
Commercial paper and other	**$ 399,265**	**$ 14**	**$ (964)**	**$ 398,315**	**4.60%**
Collateralized mortgage obligations	**1,798,988**	**10,921**	**(8,175)**	**1,801,734**	**4.99**
Asset-backed securities	**217,703**	**—**	**(6,753)**	**210,950**	**5.13**
Total	**$2,415,956**	**$10,935**	**$(15,892)**	**$2,410,999**	**4.93%**

	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%

A summary of contractual maturity, amortized cost, estimated fair value and weighted average yield of investment securities at December 31, 2007, follows:

	Amortized Cost	**Fair Value**	**Weighted Average Yield**
Due in one year or less	$ 319,265	$ 319,278	4.59%
Due after one year through five years	130,098	129,341	4.88
Due after five years through 10 years	428,577	428,704	4.80
Due after 10 years	1,538,016	1,533,676	5.06
Total	$ 2,415,956	$ 2,410,999	4.93%

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, 2007, the CMO portfolio had a weighted average remaining life of approximately two years.

At December 31, 2007, the bank's investment portfolio included $187.0 million of asset-backed securities supported by first lien home equity mortgages. In view of the recent economic conditions and volatility related to these types of securities, the bank is actively monitoring the creditworthiness of these securities, which were all rated Aaa by Moody's Investors Service or AAA by Standard & Poor's at year end. These securities are supported by various forms of credit enhancements including favorable priority of payments, overcollateralization, excess spread and insurance guarantees. Based on our evaluations, we believe these securities do not pose a significant risk of loss given the credit enhancements and relatively short weighted average lives. Since year end, one of the securities in question with a book value of $4.9 million and a fair value of $4.0 million was downgraded by Moody's Investors Service from Aaa to A3 and by Standard & Poor's from AAA to A. As a result of these rating actions, the bank is in the process of developing a plan of divestiture to comply with regulatory policy.

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

	Year Ended December 31,		
	2007	2006	2005
Proceeds on sales	**$ 93,123**	$ 107,814	$ —
Realized gains	**503**	907	—

The net realized gain and loss is included on the combined 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, 2007. The continuous loss position is based on the date the impairment occurred. An investment is considered impaired if its fair value is less than its cost. The impairments of these investments are considered temporary. The ratings of all of the investments meet all applicable regulatory standards and their current loss positions result solely from interest rate fluctuations and not from any deterioration of investment quality. The bank has the ability and the intent to hold these investments for a period of time sufficient to collect all amounts due according to the contractual terms of the investments, obtaining a full recovery of the cost of the investment.

	Less Than 12 Months		Greater Than 12 Months	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Asset-backed securities	$ 205,229	$ (6,640)	$ 5,721	$ (112)
Collateralized mortgage obligations	144,875	(1,373)	661,128	(6,802)
Commercial paper	98,996	(964)	—	—
Total	$ 449,100	$ (8,977)	$ 666,849	$ (6,914)

Note 4 — Loans and Allowance for Loan Losses

Loans comprised the following categories at December 31:

	2007	2006	2005
Real estate mortgage	**$ 10,149,685**	$ 9,005,408	$ 7,543,357
Production and intermediate term	**2,115,224**	1,685,374	1,209,962
Agribusiness			
Loans to cooperatives	**184,229**	53,988	33,868
Processing and marketing	**1,220,876**	944,258	609,909
Farm-related business	**277,912**	226,473	149,622
Communication	**306,351**	378,728	206,084
Energy	**524,175**	348,020	242,146
Water and waste disposal	**50,098**	28,372	997
Rural home	**151,583**	130,091	116,832
Mission-related	**28,055**	5,391	—
International	**979**	1,056	1,035
Loans to other financial institutions	**100,328**	90,059	91,998
Lease receivables	**5,042**	8,103	13,786
Total	**$ 15,114,537**	$ 12,905,321	$ 10,219,596

The FCA approved a program that allows the bank and its associations to purchase investments in debt instruments called "Rural America Bonds." This program is intended to help meet the growing financing needs of agriculture and rural America, improve the income and economic well-being of American farmers and ranchers, and enhance the economic vibrancy of rural areas that support agriculture. Loans related to this initiative are included in "mission-related" loans in the above table.

A significant source of liquidity for the district is the repayments and maturities of loans. The following table presents the contractual maturity distribution of loans by type at December 31, 2007, and indicates that approximately 52 percent of loans had maturities of one year or less.

	Due in One Year or Less	Due After One Through Five Years	Due After Five Years	Total
Real estate mortgage	$ 4,008,419	$ 2,682,132	$ 3,459,134	$10,149,685
Production and intermediate term	1,856,838	200,995	57,391	2,115,224
Agribusiness				
Loans to cooperatives	141,995	28,619	13,615	184,229
Processing and marketing	965,577	141,405	113,894	1,220,876
Farm-related business	199,279	48,914	29,719	277,912
Communication	280,648	23,869	1,834	306,351
Energy	321,544	51,854	150,777	524,175
Water and waste disposal	2,420	11,089	36,589	50,098
Rural home	46,407	45,133	60,043	151,583
Mission-related	18,509	2,076	7,470	28,055
International	74	376	529	979
Loans to other financial institutions	79,307	3,144	17,877	100,328
Lease receivables	2,736	2,272	34	5,042
Total	$ 7,923,753	$ 3,241,878	$ 3,948,906	$15,114,537

The district's concentration of credit risk in various agricultural commodities is shown in the following table at December 31 (*dollars in millions*):

	2007		2006		2005	
Commodity	**Amount**	**%**	Amount	%	Amount	%
Livestock	**$ 6,000**	**40%**	$ 4,966	38%	$ 4,037	40%
Crops	**2,095**	**14**	1,692	13	1,530	15
Timber	**1,819**	**12**	1,597	12	1,285	13
Cotton	**774**	**5**	662	5	698	7
Poultry	**575**	**4**	467	4	423	4
Dairy	**476**	**3**	453	4	248	2
Rural home	**152**	**1**	130	1	117	1
Other	**3,224**	**21**	2,938	23	1,882	18
Total	**$ 15,115**	**100%**	$ 12,905	100%	$ 10,220	100%

While the amounts in the table above represent the maximum potential credit risk as it relates to recorded loan principal, a substantial portion of the district's lending activities is collateralized, and, accordingly, the actual credit risk associated with lending activities is considerably less than the recorded loan principal. An estimate of actual credit risk is considered in the combined financial statements in the allowance for loan losses.

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. Restructured loans are loans whose terms have been modified and on which concessions have been granted because of borrower financial difficulties.

	December 31, 2007	2006	2005
Nonaccrual loans			
Current as to principal and interest	**$ 79,501**	$ 24,529	$ 19,513
Past due	**20,618**	11,665	9,581
Total nonaccrual loans	**100,119**	36,194	29,094
Accrual loans			
Restructured	**6,191**	7,218	7,111
90 days or more past due	**16,852**	750	2,719
Total impaired accrual loans	**23,043**	7,968	9,830
Total impaired loans	**$ 123,162**	$ 44,162	$ 38,924
Average impaired loans	**$ 73,680**	$ 45,541	$ 43,991

There were $5.3 million in commitments to lend additional funds to borrowers whose loans were classified as nonaccrual or restructured at December 31, 2007.

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:

	2007	2006	2005
Interest income recognized on nonaccrual loans	**$ 1,515**	$ 1,976	$ 2,034
Interest income on impaired accrual loans	**1,353**	984	773
Interest income recognized on impaired loans	**$ 2,868**	$ 2,960	$ 2,807

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

	2007	2006	2005
With related specific allowance	**$ 51,588**	$ 12,544	$ 9,730
With no related specific allowance	**71,574**	31,618	29,194
Total impaired loans	**$ 123,162**	$ 44,162	$ 38,924
Allowance on impaired loans	**$ 10,376**	$ 4,047	$ 2,159

Interest income on nonaccrual and accruing restructured loans that would have been recognized under the original terms of the loans during 2007 were as follows:

	2007	2006	2005
Interest income which would have been recognized under the original loan terms	**$ 15,086**	$ 7,238	$ 7,144
Less: Interest income recognized	**2,868**	2,960	2,807
Foregone interest income	**$ 12,218**	$ 4,278	$ 4,337

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

	December 31, 2007	2006	2005
Balance at beginning of year	**$ 13,969**	$ 9,533	$ 10,617
Charge-offs:			
Real estate mortgage	**30,017**	873	263
Production and intermediate term	**2,868**	732	2,244
Agribusiness	**—**	4,285	1,220
Farm-related business	**127**	—	—
Energy	**—**	—	—
Rural home	**22**	—	—
Lease receivables	**—**	—	—
Total charge-offs	**33,034**	5,890	3,727
Recoveries:			
Real estate mortgage	**—**	—	24
Production and intermediate term	**142**	393	1,187
Agribusiness	**—**	577	348
Farm-related business	**287**	—	—
Energy	**—**	—	—
Rural home	**—**	—	—
Lease receivables	**—**	—	—
Total recoveries	**429**	970	1,559
Net charge-offs	**(32,605)**	(4,920)	(2,168)
Provision for loan losses	**43,131**	9,356	1,084
Nonrecurring negative provision for loan losses	**—**	—	—
Balance at end of year	**$ 24,495**	$ 13,969	$ 9,533
Ratio of net charge-offs during the period to average loans outstanding during the period	0.23%	0.04%	0.02%

The following table presents a breakdown of the allowance for loan losses at December 31 (*dollars in thousands*):

	2007		2006		2005	
	Amount	**%**	Amount	%	Amount	%
Real estate mortgage	**$ 18,847**	**77%**	$ 10,748	77%	$ 7,549	79%
Production and intermediate term	**3,315**	**13**	1,843	13	1,135	12
Agribusiness	**1,689**	**7**	943	7	548	6
Communication	**153**	**1**	158	1	101	1
Energy	**196**	**1**	101	1	67	1
Water and waste disposal	**—**	**—**	—	—	1	—
Rural home	**285**	**1**	169	1	125	1
International	**2**	**—**	1	—	1	—
Lease receivables	**8**	**—**	6	—	6	—
Total	**$ 24,495**	**100%**	$ 13,969	100%	$ 9,533	100%

Twelve associations in the district, along with two other Farm Credit associations, participated in a loan to one borrower with the original funded balance of $68.5 million. The district's associations held $56.3 million of this original balance. During 2007, the loan was deemed to be nonaccrual due to its significant undercollateralized position and a credit default. The lead lending association in the district has pursued collection efforts and liquidated a part of the collateral, which was applied towards the outstanding balance of all participants. Five of the associations in the district repurchased the participation interests in the loan held by the two other Farm Credit associations as well as the other seven associations in the district. As of December 31, 2007, the district associations have recorded net charge-offs of approximately $28.9 million and specific reserves remaining of approximately $1.46 million. The loan has a remaining book balance of $10.7 million at December 31, 2007. The bank does not have a participation interest in this loan.

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 Farmer Mac in the event of default, subject to certain conditions. The balance of loans under long-term standby commitments to purchase was $450.9 million at December 31, 2007. Fees paid to Farmer Mac for such commitments totaled $1.3 million for the year ended December 31, 2007, and are classified as noninterest expense.

In 2007, the bank sold an additional $1.3 billion of participations in six of its direct notes receivable from district associations to another System bank for a total of $2.7 billion. The purpose of these sales was to diversify the credit exposure of the bank and to satisfy the bank's capital management goals.

Note 5 — Premises and Equipment

Premises and equipment comprised the following at:

	December 31,		
	2007	2006	2005
Land	**$ 9,798**	$ 9,050	$ 8,937
Buildings and improvements	**33,942**	32,687	29,707
Furniture and equipment	**30,650**	28,724	28,990
	74,390	70,461	67,634
Accumulated depreciation	**(31,791)**	(29,826)	(29,652)
Total	**$ 42,599**	$ 40,635	$ 37,982

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 $2.9 million, $2.5 million, and $2.3 million for 2007, 2006, and 2005, respectively.

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

	Minimum Lease Payments
2008	$ 1,503
2009	1,674
2010	1,776
2011	1,879
2012	1,947
Subsequent year	1,297
Total minimum lease payments	$ 10,076

Note 6 — Other Assets and Other Liabilities

Other assets comprised the following at December 31:

	2007	2006	2005
Accounts receivable	**$ 20,838**	**$** 12,310	**$** 9,418
Unamortized debt issue costs	**9,628**	7,318	4,316
Fair value of derivatives	**7,034**	1,758	1,047
Deferred tax assets	**2,079**	2,299	2,490
Intangible assets related to pensions	**—**	1,278	1,522
Land investment	**—**	141	179
Other, net	**2,044**	1,712	2,365
Total	**$ 41,623**	$ 26,816	$ 21,337

Other liabilities comprised the following at December 31:

	2007	2006	2005
Pension liability	$ **72,052**	$ 23,536	$ 19,662
Advance conditional payments	**51,503**	43,008	34,568
Postretirement benefits	**36,547**	49,950	49,332
Bank draft payable	**25,615**	26,624	26,893
Accounts payable	**24,785**	18,302	11,275
FCSIC premium payable	**20,691**	16,240	4,540
Additional minimum pension liability	**—**	6,209	22,639
Deferred tax liabilities	**611**	958	1,603
Notes payable	**—**	—	1,142
Income taxes payable	**602**	248	472
Fair value of derivatives	**178**	3,459	11,538
Other, net	**2,879**	2,431	5,789
Total	$ **235,463**	$ 190,965	$ 189,453

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, 2007, the bank had such specified eligible assets totaling $13.4 billion and obligations and accrued interest payable totaling $12.7 billion, resulting in excess eligible assets of $705.8 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, 2007, the bank was, and currently remains, in compliance with the conditions and requirements of the MAA.

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

The bank's participation in Systemwide debt securities follows (*dollars in millions*):

	Systemwide						Notes Payable to Other System Bank		Total	
	Bonds		Medium-Term Notes		Discount Notes					
Year of Maturity	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate
2008	$ 3,449.8	4.74%	$ 20.0	5.56%	$ 1,159.8	4.10%	$ 2,700.0	5.74%	$ 7,329.6	5.01%
2009	2,169.2	4.69	—	—	—	—	—	—	2,169.2	4.69
2010	1,538.1	4.82	—	—	—	—	—	—	1,538.1	4.82
2011	887.6	5.02	—	—	—	—	—	—	887.6	5.02
2012	775.2	5.16	—	—	—	—	—	—	775.2	5.16
Subsequent years	2,624.3	5.57	—	—	—	—	—	—	2,624.3	5.57
Total	$ 11,444.2	5.04%	$ 20.0	5.56%	$ 1,159.8	4.10%	$ 2,700.0	5.74%	$ 15,324.0	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, 2007, was 39 days.

The bank's Systemwide debt includes callable debt, consisting of the following at December 31, 2006:

Year of Maturity	Amount	Range of First Call Dates
2008	$ 380,000	1/1/2008
2009	290,000	1/1/2008 – 3/28/2008
2010	655,000	1/1/2008 – 11/26/2008
2011	585,000	1/1/2008 – 9/14/2009
2012	635,000	1/1/2008 – 12/27/2010
Subsequent Years	1,850,000	1/1/2008 – 11/7/2011
Total	$ 4,395,000	1/1/2008 – 11/7/2011

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

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

In 2007, the bank sold an additional $1.3 billion of participations in six of its direct notes receivable from district associations to another System bank for a total of $2.7 billion. Accordingly, this $2.7 billion is included as a liability in "bonds and notes, net" on the district's balance sheet.

The bank had no outstanding commercial bank lines of credit at December 31, 2007.

Note 8 — Members' Equity

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

A. Capitalization Requirements:

As a condition of borrowing, in accordance with the Farm Credit Act, each borrower is required to invest in common stock (in the case of mortgage or agricultural loans) or participation certificates (in the case of rural residence or farm-related business loans) of their respective association. Capitalization bylaws of the associations establish minimum and maximum stock purchase requirements for borrowers. The initial investment requirement of the associations ranges from the statutory minimum of $1,000 to 2 percent of the loan amount. The capitalization bylaws also limit the capital contributions that an institution can require from its borrowers to 10 percent of defined borrowings for associations. If necessary, each association's board of directors may modify, within the range defined in their bylaws, the capitalization requirements to meet the association's capital needs.

A borrower obtaining a mortgage or agricultural loan purchases voting common stock which entitles the holder to a single vote, regardless of the number of shares held in the respective association. Within two years after a borrower's loan is repaid in full, any voting common stock held by the borrower will be converted to nonvoting common stock. A borrower obtaining a rural residence or farm-related business loan purchases participation certificates which provide no voting rights to their owner.

Each class of nonvoting stock must approve, as a class, the adoption of future revisions of capitalization bylaws if the class of stock is affected by a change in the preference provided for in the proposed capitalization bylaws.

Capitalization bylaws for each association provide for the amount of voting common stock or participation certificates that are required to be purchased by a borrower as a percentage of the loan obtained. The borrower acquires ownership of the common stock or participation certificates at the time the loan is made, but usually does not make a cash investment; the aggregate par value is added to the principal amount of the related loan obligation. The bank and the associations have a first lien on the stock or participation certificates owned by borrowers. Retirement of such equities will be at the lower of par or book value, and repayment of a loan does not automatically result in retirement of the corresponding stock or participation certificates.

B. Regulatory Capitalization Requirements and Restrictions:

FCA's capital adequacy regulations require the bank and associations 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 and associations are 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's permanent capital ratio at December 31, 2007, was 13.43 percent and exceeded FCA standards. All associations currently meet the minimum capital standard established by FCA regulations. All associations are able to retire stock or distribute earnings in accordance with the Farm Credit Act and FCA regulatory restrictions. Management knows of no reasons why the bank and associations would be prohibited from retiring stock or from making patronage distributions during 2008.

The following table sets forth the ranges of capital standards for the district at December 31, 2007:

	Permanent Capital Ratio Ranges %	Core Surplus Ratio Ranges %	Total Surplus Ratio Ranges %
Bank	13.43	6.70	11.15
FLCAs	12.84 – 16.32	12.50 – 15.62	12.50 – 15.62
ACAs	10.71 – 18.00	9.65 – 17.33	10.56 – 17.33
Regulatory minimum standard	7.00	3.50	7.00

The bank is required by FCA regulations to achieve and maintain net collateral of 103 percent of total liabilities. Net collateral consists of loans, real or personal property acquired in connection with loans, marketable investments, and cash and cash equivalents. At December 31, 2007, the bank's net collateral ratio was 105.18 percent.

C. Description of Associations' Equities:

The following is a summary of the associations' stock and participation certificates outstanding:

Stock and Participation Certificates	Par Value	Number of Shares at December 31, 2007	2006	2005
Stock				
Common – voting (eligible for dividends, convertible)	$ 5.00	**11,647,412**	11,016,476	13,880,028
Common – nonvoting (eligible for dividends, convertible)	$ 5.00	**93,083**	88,565	101,421
Preferred – nonvoting (eligible for dividends, nonconvertible)	$ 5.00	**550,840**	713,056	713,769
Participation certificates – nonvoting (eligible for dividends, convertible)	$ 5.00	**370,682**	344,044	431,332

The preferred stock noted above is nonvoting stock. It is issued by one association as evidence of borrowers' claims to allocated retained earnings of a specific year. The preferred stock may be retired at the sole discretion of the association's board of directors.

In the event of the liquidation or dissolution of an association, any assets of the association remaining after payment or retirement of all liabilities shall be distributed to stockholders in the following order:

First, holders of preferred stock at par value, if any;

Second, ratably to holders of all classes of common stock and participation certificates at par value or face amount;

Third, ratably to the holders of allocated retained earnings on the basis of oldest allocations first;

Fourth, ratably to the holders of nonqualified written notices of allocation on the basis of the oldest allocations first;

Then, the remainder of assets ratably to all holders of common stock and participation certificates, in proportion to the aggregate patronage of each such holder to the total patronage of all holders.

ACA bylaws provide for operation as cooperatives which qualify for tax treatment under Subchapter T of the Internal Revenue Code. Under cooperative operations, earnings of the ACA may be distributed to borrowers. Patronage distributions are generally in the form of allocated retained earnings and cash. At least 20 percent of the total patronage distribution must be paid in cash. Amounts not distributed are retained as unallocated retained earnings.

D. Description of Bank Equities:

According to the bank's bylaws, the minimum and maximum stock investments required of the ACAs and FLCAs are 2 percent (or one thousand dollars, whichever is greater) and 5 percent, respectively, of each association's average borrowings from the bank. The investments in the bank are required to be in the form of Class A voting common stock. These intercompany balances and transactions are eliminated in combination.

The bank requires OFIs to make cash purchases of common nonvoting stock in the bank based on the OFI's average borrowings from the bank. The bank has a first lien on these equities for the repayment of any indebtedness to the bank. At December 31, 2007, the bank had $1.98 million of common stock outstanding to OFIs at a par value of $5.00 per share.

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 preferred stock was issued to provide capital for general corporate purposes. On September 26, 2005, an additional 100,000 shares was issued for net proceeds of $108,894, including $2,121 of accrued dividends payable and after expenses of $1,687 associated with the offering. Net proceeds from the additional issue were to enhance the composition of the bank's capital and liquidity, to support the bank's loan growth, to provide a base for further growth and service opportunities to our members and to rural America, and for general corporate purposes. The dividend rate on the Cumulative Perpetual Preferred Stock is 7.561 percent, payable semi-annually to December 31, 2013, after which dividends are payable quarterly at a rate equal to 3-month

London Interbank Offered Rate (LIBOR) plus 445.75 basis points. For regulatory purposes, the preferred stock is treated as equity, and is not mandatorily redeemable. Dividends on the stock are reported as declared. Preferred stock dividends totaling $15,122 were paid during 2007.

Note 9 — Income Taxes

The information that follows relates only to the district's ACAs, as the bank and FLCAs are exempt from federal and other income taxes.

The provision for (benefit from) income taxes follows for years ended December 31:

	2007	2006	2005
Current			
Federal	$ 262	$ 209	$ 383
State	6	18	42
Total current	268	227	425
Deferred			
Federal	(75)	(415)	286
State	(52)	(40)	(72)
Total deferred	(127)	(455)	214
Total provision for (benefit from) income taxes	$ 141	$ (228)	$ 639

The provision for (benefit from) income tax differs from the amount of income tax determined by applying the statutory federal income tax rate to pretax income as a result of the following differences for years ended December 31:

	2007	2006	2005
Federal tax at statutory rate	$ 60,407	$ 54,371	$ 42,150
State tax, net	—	20	42
Effect of nontaxable entities	(56,265)	(50,244)	(38,099)
Patronage distributions	(4,302)	(6,830)	(4,222)
Capital download to associations	(351)	(727)	(1,912)
Other, net	652	3,182	2,680
Total provision for (benefit from) income taxes	$ 141	$ (228)	$ 639

Deferred tax assets and liabilities comprised the following elements at December 31:

	2007	2006	2005
Allowance for loan losses	$ 3,685	$ 2,912	$ 1,936
Allowance for acquired property	—	—	120
Postretirement benefits	3,490	4,334	2,290
Other	3,256	2,596	742
Gross deferred tax assets	10,431	9,842	5,088
Less valuation allowance	(8,357)	(7,543)	(2,598)
Adjusted gross deferred tax assets	2,074	2,299	2,490
FCBT stock redemption	(508)	(859)	(1,586)
Other	(98)	(99)	(18)
Gross deferred tax liabilities	(606)	(958)	(1,604)
Net deferred tax assets	$ 1,468	$ 1,341	$ 886

The bank and its related associations adopted the provisions of the Financial Accounting Standards Board Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," on January 1, 2007. There were no uncertain tax positions and related liabilities for unrecognized tax benefits recorded at Januuary 1, 2007, or December 31, 2007, as a result of adoption of this interpretation. Any penalties and interest related to income taxes would be accounted for as an adjustment to income tax expense.

Note 10 — Employee Benefit Plans

Employees of the bank and district associations participate in either the defined benefit retirement plan (DB plan) or a defined contribution plan (DC plan) and are eligible to participate in the district's 401(k) plan.

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. Under SFAS No. 88, pension plan termination benefits recognized resulting from employees who qualified for an early retirement option under a retention plan totaled $320, $103 and $87 during the years ended December 31, 2007, 2006 and 2005, respectively. Additionally, certain qualified individuals in the bank may participate in a separate, non-qualified defined benefit supplemental pension plan.

Participants in the DC plan generally include employees who elected to transfer from the DB plan prior to January 1, 1996, and 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. Employer contributions to the DC plan were $3.4 million, $3.1 million and $2.8 million for the years ended December 31, 2007, 2006 and 2005, respectively.

The district also participates in a 401(k) plan, which offers a pre-tax and after-tax compensation deferral feature. Employers match 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. Employer contributions were $2.8 million, $2.5 million and $2.2 million for the years ended December 31, 2007, 2006 and 2005, respectively. 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 Farm Credit Benefits Alliance 401(k) Plan.

The bank and associations also provide certain health care and life insurance benefits to eligible retired employees, beneficiaries and directors (retiree medical plan). District employees' eligibility for these benefits upon retirement is dependent on conditions set by their district employer.

On December 31, 2007, the bank and its related associations adopted SFAS 158, which requires the recognition of a plan's over-funded or under-funded status as an asset or liability with an offsetting adjustment to accumulated other comprehensive income, net of tax. SFAS 158 requires the determination of the fair values of a plan's assets at year end and recognition of actuarial gains and losses, prior service costs or credits, and transition assets or obligations as a component of accumulated other comprehensive income, net of tax. These amounts were previously netted against the plans' funded status in the district combined statement of condition pursuant to the provisions of SFAS 87. These amounts will be subsequently recognized as components of net periodic benefit costs. Further, actuarial gains and losses that arise in subsequent periods that are not initially recognized as a component of net periodic benefit cost will be recognized as a component of accumulated other comprehensive income, net of tax. Those amounts will subsequently be recognized as a component of net periodic benefit cost as they are amortized during future periods.

The effects of the adoption of SFAS 158 on elements in the balance sheet are reflected in the following table:

	Before Adoption of SFAS 158	Adjustments	After Adoption of SFAS 158
Other assets	$ 42,054	$ (431)	$ 41,623
Total assets	17,996,928	(431)	17,996,497
Other liabilities	205,311	30,152	235,463
Total liabilities	15,715,684	30,152	15,745,836
Accumulated other comprehensive loss	(3,910)	(30,583)	(34,493)
Total members' equity	2,281,244	(30,583)	2,250,661
Total liabilities and members' equity	17,996,928	(431)	17,996,497

The following table reflects the benefit obligation, cost and actuarial assumptions for the district's pension and other postretirement benefit plans:

	Pension Benefits			Other Postretirement Benefits		
	2007	2006	2005	**2007**	2006	2005
Accumulated benefit obligation, end of year	**$ 190,594**	$ 182,784	$ 182,569			
Change in projected benefit obligation						
Projected benefit obligation, beginning of year	**$ 230,244**	$ 221,954	$ 189,425	**$ 38,489**	$ 38,730	$ 48,500
Service cost	**5,209**	5,304	4,778	**1,235**	1,404	1,851
Interest cost	**13,549**	11,441	11,154	**2,271**	2,004	2,868
Plan participants' contributions	**—**	—	—	**365**	346	636
Plan amendments	**—**	3,337	—	**—**	411	(13,434)
Special termination benefits	**320**	103	87	**—**	—	—
Actuarial loss (gain)	**1,424**	(4,148)	24,058	**(3,969)**	(3,047)	796
Benefits paid	**(8,740)**	(7,747)	(7,548)	**(1,580)**	(1,359)	(2,487)
Projected benefit obligation, end of year	**$ 242,006**	$ 230,244	$ 221,954	**$ 36,811**	$ 38,489	$ 38,730
Change in plan assets						
Plan assets at fair value, beginning of year	**$ 152,936**	$ 141,851	$ 124,093	**$ —**	$ —	$ 288
Actual return on plan assets	**19,206**	11,745	18,428	**—**	—	(58)
Company contributions	**6,552**	7,087	6,878	**1,215**	1,013	1,621
Plan participants' contributions	**—**	—	—	**365**	346	636
Benefits paid	**(8,740)**	(7,747)	(7,548)	**(1,580)**	(1,359)	(2,487)
Plan assets at fair value, end of year	**$ 169,954**	$ 152,936	$ 141,851	**$ —**	$ —	$ —
Reconciliation of funded status						
Funded status	**$ (72,052)**	$ (77,308)	$ (80,103)	**$ (36,811)**	$ (38,489)	$ (38,730)
Unrecognized prior service cost	**N/A**	4,593	2,306	**N/A**	(16,438)	(18,769)
Unrecognized net loss (gain)	**N/A**	49,313	58,048	**N/A**	4,729	8,038
Contributions between measurement date and fiscal year end	**—**	103	87	**264**	248	129
Net pension asset/(liability) at end of year	**$ (72,052)**	$ (23,299)	$ (19,662)	**$ (36,547)**	$ (49,950)	$ (49,332)
Amounts recognized consist of:						
Accrued benefit cost	**$ (72,052)**	$ (23,299)	$ (19,662)	**$ (36,547)**	$ (49,950)	$ (49,332)
Minimum pension liability adjustment	**—**	(6,446)	(22,369)	**—**	—	—
Intangible asset	**—**	1,515	1,522	**—**	—	—
Deferred income tax assets	**—**	—	—	**(431)**	—	—
Accumulated other comprehensive income	**44,056**	4,931	20,847	**(13,474)**	—	—
Amounts recognized in accumulated other comprehensive income						
Additional minimum pension liability adjustment	**$ —**	$ 1,853	$ 20,847	**$ —**	$ —	$ —
Net actuarial loss (gain)	**40,608**	N/A	N/A	**667**	N/A	N/A
Prior service cost (credit)	**3,448**	N/A	N/A	**(14,141)**	N/A	N/A
Total	**$ 44,056**	$ 1,853	$ 20,847	**$ (13,474)**	$ —	$ —

A funding policy adopted in 2007 establishes contribution requirements for the district's DB plan if plan assets are less than the accumulated benefit obligation at year end. The policy calls for contributions equal to the value of the additional benefits expected to be earned by employees during the year plus a payment on the shortfall between the accumulated benefit obligation and the plan assets. The additional payments for any shortfall are intended to fund the shortfall over seven years.

The following table discloses the excess of the DB plan's accumulated benefit obligation over its plan assets at December 31,

District DB plan assets at fair value	**$ 169,954**	$ 152,936	$ 141,851
Accumulated benefit obligation of district DB plan	**185,918**	179,083	181,375
Funding shortfall	**$ (15,964)**	$ (26,147)	$ (39,524)

In accordance with this policy, a contribution of $14.9 million was made to the DB plan in January 2008. The supplemental (nonqualified) pension plan is not funded. The projected benefit obligation and accumulated benefit obligation for the supplemental pension plan at December 31, 2007, were $8,644 and $4,676, respectively.

	Pension Benefits			Other Postretirement Benefits		
	2007	2006	2005	**2007**	2006	2005
Net periodic benefit cost						
Service cost	**$ 5,209**	$ 5,304	$ 4,778	**$ 1,235**	$ 1,404	$ 1,851
Interest cost	**13,549**	11,441	11,154	**2,271**	2,004	2,868
Expected return on plan assets	**(12,249)**	(11,443)	(9,916)	**—**	—	(2)
Amortization of:						
Prior service cost	**1,144**	1,050	1,090	**(1,844)**	(1,919)	(886)
Net actuarial loss (gain)	**3,171**	4,286	2,931	**71**	262	198
Net periodic benefit cost	**$ 10,824**	$ 10,638	$ 10,037	**$ 1,733**	$ 1,751	$ 4,029
Special termination benefits	**320**	103	87	**—**	—	—
Total benefit cost	**$ 11,144**	$ 10,741	$ 10,124	**$ 1,733**	$ 1,751	$ 4,029
Weighted-average assumptions used to determine benefit obligation as of December 31						
Measurement date	**9/30/2007**	9/30/2006	9/30/2005	**9/30/2007**	9/30/2006	9/30/2005
Discount rate	**6.50%**	6.00%	5.25%	**6.50%**	6.00%	5.25%
Rate of compensation increase	**8% in 2008 down to 4% in 2012**	9% in 2007 down to 4% in 2012	4.50%			
Health care cost trend rate assumed for next year (pre/post-65) – medical				**8.5%/6.5%**	9.0%/6.75%	9.5%/7.0%
Health care cost trend rate assumed for next year (pre/post-65) – prescriptions				**12.00%**	13.00%	13.50%
Ultimate health care cost trend rate				**4.75%**	4.75%	4.75%
Year that the rate reaches the ultimate trend rate				**2016**	2016	2016
Weighted-average assumptions used to determine net periodic pension cost for year ended December 31						
Measurement date	**9/30/2006**	9/30/2005	9/30/2004	**9/30/2006**	9/30/2005	9/30/2004
Discount rate	**6.00%**	5.25%	6.00%	**6.00%**	5.25%	6.00%
Expected return on plan assets	**8.00%**	8.00%	8.00%	**N/A**	N/A	N/A
Rate of compensation increase	**8% in 2008 down to 4% in 2012**	4.50%	4.50%			
Health care cost trend rate assumed for next year (pre/post-65) – medical				**9.0%/6.75%**	9.5%/7.0%	11.0%/11.5%
Health care cost trend rate assumed for next year (pre/post-65) – prescriptions				**13.00%**	13.50%	11.0%/11.5%
Ultimate health care cost trend rate				**4.75%**	4.75%	5.00%/5.50%
Year that the rate reaches the ultimate trend rate				**2016**	2016	2012
Effect of change in assumed heath care cost trend rates						
Effect on total service cost and interest cost components						
One-percentage point increase				**$ 629,573**		
One-percentage point decrease				**$ (495,452)**		
Effect on year-end postretirement benefit obligation						
One-percentage point increase				**$ 5,891,560**		
One-percentage point decrease				**$ (4,717,994)**		
Expected Future Cash Flow Information						
Expected Benefit Payments						
Fiscal 2008	**$ 8,982**			**$ 1,344**		
Fiscal 2009	**10,809**			**1,506**		
Fiscal 2010	**11,984**			**1,696**		
Fiscal 2011	**13,104**			**1,874**		
Fiscal 2012	**14,639**			**2,051**		
Fiscal 2013 – 2017	**94,165**			**12,919**		
Expected Contributions						
Fiscal 2008	**$ 15,437**			**$ 1,344**		

Note 11 — Related Party Transactions

In the ordinary course of business, the bank and associations have entered into loan transactions with directors, officers and other employees of the bank or associations and other organizations with which such persons may be associated. Total loans to such persons at December 31, 2007, amounted to $160.4 million. In the opinion of management, such loans outstanding to directors, officers and other employees at December 31, 2007, did not involve more than a normal risk of collectibility and were subject to approval requirements contained in FCA regulations and were made on the same terms, including interest rates, amortization schedules and collateral, as those prevailing at the time for comparable transactions with unrelated borrowers. Disclosures on individual associations' officers and directors are found in the associations' individual annual reports.

Note 12 — Commitments and Contingencies

In the normal course of business, the bank and associations have various outstanding commitments and contingent liabilities as discussed elsewhere in these notes. For a discussion of commitments to extend credit and standby letters of credit issued, see Note 13, "Financial Instruments With Off-Balance-Sheet Risk."

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, 2007, were approximately $154.4 billion.

As of December 31, 2007, a district association was party to three lawsuits involving a lending matter with a borrower group. The borrower group has filed counterclaims against the district association. In early February 2008, all other participants in the lending matter and the respective district banks of the involved associations were named as counter-defendants in the lawsuit. Management and legal counsel of the bank and associations believe that the association's claims are supported by facts and applicable law and have a reasonable chance of success, and at the same time believe that the claims of the borrower group are without merit and the association will likely be successful in its defense against such claims. In addition, other actions incurred in the ordinary course of business are pending against the bank and association 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 from the lawsuit mentioned and other pending actions will not be material in relation to the financial position, results of operations or cash flows of the bank and associations.

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

The bank and associations may participate in financial instruments with off-balance-sheet risk to satisfy the financing needs of their borrowers and to manage their 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 and associations have outstanding a significant number of commitments to extend credit. The bank and associations also provide 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 combined balance sheets (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 district's commitments to extend credit totaled $3.076 billion, $2.871 billion and $2.267 billion at December 31, 2007, 2006 and 2005, respectively. At December 31, 2007, the district had $210.5 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 fair value of these obligations is $2.1 million, based on the fees for the unexpired period remaining.

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 district's financial instruments at December 31, 2007, 2006 and 2005. 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 debt instruments. Accordingly, fair values on those instruments 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 district's financial instruments follow:

	December 31, 2007		December 31, 2006		December 31, 2005	
	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	**$ 2,592,204**	**$ 2,592,204**	$ 2,821,641	$ 2,821,641	$ 2,792,167	$ 2,792,167
Loans	**15,114,537**	**15,041,574**	12,905,321	12,706,284	10,219,596	10,016,888
Allowance for loan losses	**(24,495)**	**—**	(13,969)	—	(9,533)	—
Loans, net	**15,090,042**	**15,041,574**	12,891,352	12,706,284	10,210,063	10,016,888
Derivative assets	**7,034**	**7,034**	1,758	1,758	1,047	1,047
Financial liabilities						
Bonds and notes	**15,324,193**	**15,439,340**	13,524,243	13,521,813	10,974,816	10,978,323
Fair value adjustment of derivatives	**(178)**	**(178)**	(3,459)	(3,459)	(11,538)	(11,538)
Total bonds and notes	**15,324,015**	**15,439,162**	13,520,784	13,518,354	10,963,278	10,966,785
Derivative liabilities	**178**	**178**	3,459	3,459	11,538	11,538

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, Federal Funds Sold, and Securities Purchased Under Resale Agreements:

The carrying value is a reasonable estimate of fair value.

B. 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 bank's and/or the associations' 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 which appropriately reflects the uncertainty of the expected future cash flows over the average disposal period. Where the net realizable value of the collateral exceeds the legal obligation for a particular loan, the legal obligation is generally used in place of net realizable value.

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 new issues of Systemwide bonds with similar-maturity terms.

E. 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.

F. Commitments to Extend Credit:

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

Note 15 — Derivative Instruments and Hedging Activity

The bank maintains an overall interest rate risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest rate volatility. The bank's goal is to manage interest rate sensitivity by modifying the repricing or maturity characteristics of certain balance sheet liabilities so that the net interest margin is not adversely affected by movements in interest rates. As a result of interest rate fluctuations, hedged fixed-rate liabilities will appreciate or depreciate in market value. The effect of this unrealized appreciation or depreciation is expected to be substantially offset by the district'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 fair value and cash flow 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, 2007, the bank had three fair value hedges with a total notional amount of $175 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.

At December 31, 2007, the bank had six cash flow hedges, with a total notional amount of $750 million, which hedge the exposure to variability in expected future cash flows.

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, 2007, the bank had credit exposure totaling $7.36 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 table below presents the credit ratings of counterparties to whom the bank has credit exposure:

	Remaining Years to Maturity						
(dollars in millions)	Less Than One Year	One to Five Years	Total	Maturity Distribution Netting	Exposure	Collateral Held	Exposure Net of Collateral
Standard & Poor's Credit Rating							
A+	0.71	0.76	1.47	—	7.36	—	7.36

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 district's overall interest rate risk-management strategies. The bank enters into interest rate swaps classified as fair value hedges primarily to convert a portion of its non-prepayable fixed-rate long-term debt to floating-rate debt.

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

December 31, 2007 *(dollars in millions)*	Maturities of 2007 Derivative Products and Other Financial Instruments: 2008	2009	2010	2011	2012	Subsequent Years	Total	Fair Value
Total debt obligations:								
Fixed rate	$ 2,380	$ 1,444	$ 1,538	$ 888	$ 775	$ 2,624	$ 9,649	$ 9,764
Weighted average interest rate	4.39%	4.65%	4.82%	5.02%	5.16%	5.57%	4.94%	
Variable rate	$ 4,950	$ 725	$ —	$ —	$ —	$ —	$ 5,675	$ 5,675
Weighted average interest rate	5.31%	4.76%	—	—	—	—	5.24%	
Total debt obligations	$ 7,330	$ 2,169	$ 1,538	$ 888	$ 775	$ 2,624	$ 15,324	$ 15,439
Weighted average interest rate	5.01%	4.69%	4.82%	5.02%	5.16%	5.57%	5.05%	
Derivative instruments:								
Receive fixed swaps								
Notional value	$ 25	$ —	$ —	$ —	$ —	$ 150	$ 175	$ 6
Weighted average receive rate	3.53%	—	—	—	—	4.95%	4.75%	
Weighted average pay rate	4.72%	—	—	—	—	3.81%	3.94%	
Pay fixed swaps								
Notional value	$ 300	$ 450	$ —	$ —	$ —	$ —	$ 750	$ 1
Weighted average receive rate	4.19%	3.94%	—	—	—	—	4.04%	
Weighted average pay rate	4.09%	3.91%	—	—	—	—	3.98%	

Note 16 — Selected Quarterly Financial Information (Unaudited)

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

	2007 First	Second	Third	Fourth	Total
Net interest income	**$ 105,570**	**$ 106,186**	**$ 110,290**	**$ 110,335**	**$ 432,381**
Provision for loan losses	**1,242**	**25,778**	**8,333**	**7,778**	**43,131**
Noninterest expense, net	**37,275**	**36,107**	**35,794**	**37,534**	**146,710**
Net income	**$ 67,053**	**$ 44,301**	**$ 66,163**	**$ 65,023**	**$ 242,540**

	2006 First	Second	Third	Fourth	Total
Net interest income	$ 92,571	$ 93,777	$ 97,464	$ 102,434	$ 386,246
Provision for loan losses	973	3,931	1,677	2,775	9,356
Noninterest expense, net	35,029	31,302	32,050	38,391	136,772
Net income	$ 56,569	$ 58,544	$ 63,737	$ 61,268	$ 240,118

	2005 First	Second	Third	Fourth	Total
Net interest income	$ 81,300	$ 82,382	$ 85,179	$ 91,611	$ 340,472
Provision for loan losses	(449)	(83)	883	733	1,084
Noninterest expense, net	30,651	26,000	26,632	34,323	117,606
FAC expense	906	668	331	—	1,905
Net income	$ 50,192	$ 55,797	$ 57,333	$ 56,555	$ 219,877

Note 17 — Bank-Only Financial Data

Condensed financial information for the bank follows. All significant transactions and balances between the bank and associations are eliminated in combination. The multi-employer structure of the district's defined benefit plan results in the recording of this plan only upon combination.

	December 31,		
Balance Sheet Data	**2007**	2006	2005
Cash, federal funds sold and securities purchased under resale agreements	**$ 142,102**	$ 103,394	$ 46,836
Investment securities	**2,410,999**	2,672,242	2,697,876
Loans			
To associations	**8,058,130**	7,815,233	7,036,341
To others	**2,807,861**	2,240,195	1,445,160
Less allowance for loan losses	**1,065**	142	142
Net loans	**10,864,926**	10,055,286	8,481,359
Accrued interest receivable	**66,789**	63,967	43,994
Other assets	**35,962**	20,871	14,723
Total assets	**$ 13,520,778**	$ 12,915,760	$ 11,284,788
Bonds and notes	**$ 12,624,015**	$ 12,120,783	$ 10,563,278
Other liabilities	**168,162**	130,756	97,203
Total liabilities	**12,792,177**	12,251,539	10,660,481
Preferred stock	**200,000**	200,000	200,000
Capital stock	**198,864**	161,421	135,390
Retained earnings	**334,394**	324,270	315,047
Accumulated other comprehensive loss	**(4,657)**	(21,470)	(26,130)
Total members' equity	**728,601**	664,221	624,307
Total liabilities and members' equity	**$ 13,520,778**	$ 12,915,760	$ 11,284,788

	Year Ended December 31,		
Statement of Income Data	**2007**	2006	2005
Interest income	**$ 753,541**	$ 652,557	$ 392,226
Interest expense	**653,976**	562,216	316,266
Net interest income	**99,565**	90,341	75,960
Provision (negative provision) for loan losses	**1,043**	2,578	(344)
Net interest income after provision for loan losses	**98,522**	87,763	76,304
Noninterest income	**22,116**	17,847	16,495
Intra-System financial assistance expense	**—**	—	761
Other expense	**46,634**	40,616	34,422
Net income	**$ 74,004**	$ 64,994	$ 57,616

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 borrower-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 29, 2008:

DIRECTORS

Ralph W. Cortese joined the board in 1995, and his current term expires December 31, 2010. 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 and Compensation committees. In June 2003, he was appointed to the Farmer Mac Board. He is also a member of the Texas Agricultural Cooperative Council board of directors.

Jon M. Garnett began his first term on the board in 1999, and his current term expires December 31, 2010. 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 and is a member of the Farm Credit Council Board of Directors' legislative committee. 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 chairman of the bank's Compensation Committee. Garnett raises grain and forage crops and runs stocker cattle 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. Vice chairman of the bank's Audit Committee, Crawford also serves on the bank's Compensation Committee. He is a director on the board and an audit committee member of the Federal Farm Credit Banks Funding Corporation. He is also a member and past president of the Alabama Cattlemen's Association and a member of the National Cattlemen's Beef Association, the Alabama Farm Bureau and the Alabama Farmers Federation. 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 and serves on the bank's Audit and Compensation committees. 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. and Dodson Ag, Inc.; the owner of Jimmy Dodson Farms; a partner in Weber Greene, Ltd; and managing partner in Weber Station LLC. In addition, Dodson serves on the boards of Gulf Coast Cooperative and South Texas Cotton and Grain Association, and holds leadership positions in the National Cotton Council of America 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 and Leadership America 2008.

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. He is also a member of the Texas Lutheran University board of regents.

Compensation of Directors

Directors of the bank are compensated in cash for service on the bank's board. Compensation for 2007 was paid at the rate of $48,815 per year, payable at $4,068 per month. In addition to days served at board meetings, directors may serve additional days on other official assignments, and under exceptional circumstances where extraordinary time and effort are involved, the board may approve additional compensation, not to exceed 30 percent of the annual maximum allowable by FCA regulations. The board approved additional compensation in the amount of $5,000 during 2007 as noted below. No director received non-cash compensation exceeding $5,000 in 2007. Total cash compensation paid to all directors as a group during 2007 was $346,705. Information for each director for the year ended December 31, 2007, is provided below:

Board Member	Days Served at Board Meetings*	Days Served on Other Official Assignments**	Total Compensation Paid
Ralph W. Cortese	26.5	21.5	$ 48,815
Jon M. Garnett	26.5	25.5	48,815
C. Kenneth Andrews	26.5	19.5	48,815
Joe R. Crawford	26.5	20.5	48,815
James F. Dodson	24.0	25.0	48,815
Elizabeth G. Flores***	26.5	37.5	53,815
William F. Staats	26.5	19.5	48,815
			$ 346,705

* Includes travel time, but does not include time required to prepare for board meetings.

** Includes Audit Committee meetings, Compensation Committee meetings, special assignments, training and travel time.

*** During 2007, additional compensation of $3,000 was paid to Ms. Flores for travel time and efforts rendered for serving as a panelist on the topic of diversity at a leadership event for Farm Credit System directors sponsored by Farm Credit Council Services. Also in 2007, additional compensation of $2,000 was paid to Ms. Flores for the travel time and efforts for her participation as a panelist at a conference sponsored by the bank for two organizations, National Society of Hispanic MBAs and National Black MBA Association. Both conferences promoted the bank's ongoing commitment to diversity and supported the bank's initiative on diversity as outlined in the bank's business plan.

Directors are reimbursed for reasonable travel, subsistence and other related expenses while conducting bank business. The aggregate amount of expenses reimbursed to directors in 2007, 2006 and 2005 totaled $149,254, $123,258, and $120,436, respectively. The increase in expenses in 2007 as compared to previous years was primarily due to the addition of a board member in late 2006. A copy of FCBT's travel policy is available to shareholders upon request.

SENIOR OFFICERS

Name and Title	Time in Position	Experience — Past Five Years
Larry R. Doyle, *Chief Executive Officer*	4.5 years	Executive Vice President and Chief Operating Officer, AgFirst Farm Credit Bank
Thomas W. Hill, *Senior Vice President, Chief Financial Officer, Chief Operations Officer*	13 years 4 years	Senior Vice President, Chief Financial Officer, FCBT
Steven H. Fowlkes, *Senior Vice President, Chief Credit Officer*	10 years 4 years	Senior management and management positions, FCBT
William E. Zimmerman, *Senior Vice President, Corporate Affairs, General Counsel and Corporate Secretary*	20 years Retired January 2008	Senior Vice President, Corporate Affairs, General Counsel and Corporate Secretary, FCBT
Kyle Pankonien, *Vice President, Corporate Affairs, General Counsel and Corporate Secretary*	Appointed January 2008	Vice President, Corporate Affairs, Deputy General Counsel, FCBT

Compensation Discussion and Analysis – Senior Officers

Overview

The board of directors of the Farm Credit Bank of Texas, through its Compensation Committee, has pursued a compensation philosophy for the bank that promotes leadership in the adoption and administration of a comprehensive compensation program so that:

- Competent senior officers can be attracted, developed and retained for the delivery of performance that will result in the attainment of the bank's strategic business plan;
- Operational activities that produce bank efficiencies and produce financial results that maximize the principles of a cooperative organization will be rewarded;
- Consistent application of compensation programs will link compensation to bank performance and levels of accountability for the achievement of the bank's strategies and programs; and,
- Market-based base salaries, benefits and bonus compensation will position the bank to be a competitive employer in the financial services marketplace.

The Compensation Committee annually reviews the appropriate mix of salaries, benefits and bonus arrangements and approves these programs for senior officers of the bank. With data derived from an independent third-party compensation consultant, the Compensation Committee considers market salary data of competition in the financial services sector to ensure that base salaries and bonus plan structures are in line with market-comparable positions with similarly situated financial institutions. This study provides the basis for actions by the Compensation Committee to approve the compensation level and bonus plan structure of the bank's chief executive officer (CEO) annually, plus review and approve other compensation programs for the other senior officers of the bank. The bank's compensation program encompasses four primary elements: (1) base salary, (2) discretionary bonus compensation, (3) bank-paid retirement benefits and (4) secondary benefits such as an executive physical program, annual leave, bank-paid life insurance and bank-provided vehicles.

CEO Compensation Table and Policy

The base salary amount of the CEO was $440,017 for 2007. The amount of the non-equity discretionary bonus compensation is higher than the base salary amount for 2007, which in essence has put more of the CEO's total compensation "at risk" based on the performance of the bank. The Compensation Committee considers the year-end results of certain financial key performance indicators, such as return on assets, return on equity, collateral ratio, credit quality ratios, growth in total and net assets, and net income, along with accomplishments of the bank in attaining strategic plan operational objectives as the bases for determining a discretionary bonus for the CEO. Included in the process for awarding base and bonus compensation for the CEO is the committee's annual appraisal assessment of the CEO's performance in areas such as Farm Credit System and Farm Credit Administration relationships; alliances with other financial institutions; and coordination of bank board, stockholder and association relations. There are no long-term bonus plans, deferred compensation arrangements or retention plans in place for the CEO. Payments of bonus awards for the CEO are 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 2007, 2006, and 2005. Amounts reflected for bonus compensation are presented in the year the compensation is earned.

Summary Compensation Table

		Annual					
Name of Chief Executive Officer	Year	Salary (a)	Bonus (b)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (c)	Deferred/Perquisites (d)	Other (e)	Total
Larry R. Doyle	**2007**	**$ 440,017**	**$ 560,000**	**$ 1,884,534**	**$ 22,017**	**—**	**$ 2,906,568**
Larry R. Doyle	2006	440,017	440,000	N/A	20,362	—	900,379
Larry R. Doyle	2005	440,017	238,000	N/A	17,016	—	695,033

(a) Gross salary

(b) Bonus

(c) Disclosure of change in pension value reflected only for year 2007. "N/A" represents information not available for prior years, 2006 and 2005. Change in the actuarial present value of the accumulated benefit under all defined benefit and actuarial pension plans (including supplement plans) from the pension measurement date used for financial statement reporting purposes with respect to the audited financial statements for the prior completed fiscal year to the pension measurement date used for financial statement reporting purposes with respect to the audited financial statements for the covered fiscal year.

(d) Deferred/Perquisites include contributions to 401(k) and defined contribution plans, automobile benefits and premiums paid for life insurance.

(e) Other — no amounts paid in years presented.

Pension Benefits Table

The following table presents a summary of the total annual benefit provided from the pension plans applicable to the CEO for the year ended December 31, 2007:

Name	Plan Name	Number of Years Credited Service	Present Value of Accumulated Benefit	Payments During 2007
Larry R. Doyle, FCB of Texas	Farm Credit Bank of Texas Pension Plan	33.583	$ 823,761	$ —
	Supplemental Pension Plan for Farm Credit Bank of Texas	33.583	$ 5,867,225	$ —

Pension Benefits Table Narrative Disclosure

The CEO participates in the Farm Credit Bank of Texas Pension Plan (qualified plan) and in the Farm Credit Bank of Texas Supplemental Pension Plan (nonqualified plan). The supplemental plan restores benefits to participants who otherwise would be restricted by Internal Revenue Code limits that are in the qualified plan. Compensation, as defined in the plans, includes the sum of wages, bonus compensation and deferrals to the 401(k) and flexible spending account plans, but excludes annual leave that may be paid in cash at the time of termination or transfer of employment, severance payments, retention bonuses, taxable fringe benefits and any other payments. Pension benefits are based on the average of monthly eligible compensation over the 60 consecutive months that produces 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 CEO had 33.583 years of credited service as of December 31, 2007. There is an offset amount from another Farm Credit System institution for the CEO. The present values of the accumulated benefits are calculated assuming retirement had occurred at the measurement date used for financial statement reporting purposes with retirement at age 55. The pension plan benefits are payable in the form of a 50 percent joint and survivor annuity with a spouse two years younger. Benefits from the supplemental plan are payable as a lump sum value with a gross-up for income taxes because the benefit is fully taxable to the recipient upon distribution from the plan.

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 bonus compensation. The CEO will receive a set severance amount if terminated for any reason other than cause.

Compensation of Other Senior Officers

The following table summarizes the compensation paid to the five highest paid officers of the bank during 2007, 2006, and 2005. (Amounts reflected for bonus compensation are presented in the year the compensation is earned.)

Summary Compensation Table

Name of Individual or Group	Year	Annual Salary (a)	Annual Bonus (b)	Annual Deferred/Perquisites (c)	Annual Other (d)	Total
Aggregate of five highest paid officers: (excludes Chief Executive Officer)						
5	**2007**	**$ 1,118,743**	**$ 404,825**	**$ 115,711**	**—**	**$ 1,639,279**
5	2006	1,072,241	371,960	105,873	—	1,550,074
5	2005	1,023,365	254,265	109,543	—	1,387,173

(a) Gross salary

(b) Bonus

(c) Deferred/Perquisites include contributions to 401(k) and defined contribution plans, automobile benefits and premiums paid for life insurance.

(d) Other — no amounts paid in years presented.

Other senior officers of the bank are not eligible for any deferred compensation or long-term incentive plans, but can participate in a retention plan, at the discretion and approval of the bank board's Compensation Committee. Senior officers, other than the CEO, participate in a bank discretionary bonus program, whose terms and conditions are detailed in writing as a Success Sharing Plan, with awards annually approved by the board's Compensation Committee. Payments of bonus awards for the senior officers are made in the first 90 days of the subsequent calendar year following the close of the year.

Disclosure of the compensation paid during 2007 to any senior officer or officer included in the table is available and will be disclosed to shareholders of the institution and stockholders of the district's associations upon written request.

Senior officers are reimbursed for reasonable travel, subsistence and other related expenses while conducting bank business. A copy of the bank's travel policy is available to shareholders upon request.

Bank employees can earn compensation above base salary through an annual Success Sharing Plan, which the bank adopted in 2001. The plan is based upon the achievement of bank performance standards, which are approved by the board's Compensation Committee 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. The district associations own 17 headquarter locations and lease three. There are 121 owned and 71 leased association branch locations. The bank's and associations' investment in property is further detailed in Note 5, "Premises and Equipment," to the accompanying combined financial statements.

Legal Proceedings

There were no matters that came to the attention of the board of directors or management regarding the involvement of current directors or senior officers in specified legal proceedings which are required to be disclosed.

As of December 31, 2007, a district association was party to three lawsuits involving a lending matter with a borrower group. The borrower group has filed counterclaims against the district association. In early February 2008, all other participants in the lending matter and the respective district banks of the involved associations were named as counter-defendants in the lawsuit. Management and legal counsel of the bank and associations believe that the association's claims are supported by facts and applicable law and have a reasonable chance of success, and at the same time believe that the claims of the borrower group are without merit and the association will likely be successful in its defense against such claims. Upon the basis of current information, management and legal counsel are of the opinion that the ultimate liability, if any, resulting from the lawsuit mentioned and other pending actions will not be material in relation to the financial position, results of operations or cash flows of the bank and associations. Note 12, "Commitments and Contingencies," to the accompanying combined financial statements outlines the bank and association's position with regard to possible contingencies at December 31, 2007.

Description of Capital Structure

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

Description of Liabilities

The bank's debt outstanding is described in Note 7, "Bonds and Notes," to the accompanying financial statements. The bank's contingent liabilities are described in Note 12, "Commitments and Contingencies," to the accompanying financial statements.

Selected Financial Data

The selected financial data for the five years ended December 31, 2007, 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 district's 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 combined financial statements.

Relationship With Public Accountants

The district's auditors were PricewaterhouseCoopers LLP. 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.

During 2007, district entities paid their independent public accountants $1.1 million for audit services and $79,873 for tax services. There were no other non-audit services provided by the independent public accountants.

Financial Statements

The financial statements, together with the report thereon of PricewaterhouseCoopers LLP dated February 29, 2008, 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 annual report will be posted on the bank's Web site (at www.farmcreditbank.com), within 75 calendar days of the end of the district fiscal year. This posting coincides with an electronic version of the report being provided to its regulator, the Farm Credit Administration. Within 90 calendar days of the end of the district fiscal year, a copy of the district's annual report will be provided to its stockholders.

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:

	At December 31, 2007	
(dollars in thousands)	Number of Loans	Volume
Total loans and commitments	76,544	$ 17,953,844
Loans and commitments to young farmers and ranchers	14,147	$ 1,880,813
Percent of loans and commitments to young farmers and ranchers	18.5%	10.5%
Loans and commitments to beginning farmers and ranchers	35,641	$ 6,920,735
Percent of loans and commitments to beginning farmers and ranchers	46.6%	38.8%

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

	For the Year Ended December 31, 2007	
(dollars in thousands)	Number of Loans	Volume
Total new loans and commitments	19,533	$ 7,492,169
New loans and commitments to young farmers and ranchers	3,493	$ 721,249
Percent of new loans and commitments to young farmers and ranchers	17.9%	9.6%
New loans and commitments to beginning farmers and ranchers	8,653	$ 2,548,149
Percent of new loans and commitments to beginning farmers and ranchers	44.3%	34.0%

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

	At December 31, 2007				
	Annual Gross Sales				
(dollars in thousands)	$50 Thousand or Less	$50 to $100 Thousand	$100 to $250 Thousand	Over $250 Thousand	Total
Total number of loans and commitments	23,490	19,297	19,797	13,960	76,544
Number of loans and commitments to small farmers and ranchers	16,669	14,752	14,690	7,470	53,581
Percent of loans and commitments to small farmers and ranchers	71.0%	76.4%	74.2%	53.5%	70.0%
Total loans and commitments volume	$ 483,349	$ 1,101,113	$ 2,617,259	$ 13,752,123	$ 17,953,844
Total loans and commitments to small farmers and ranchers volume	$ 348,850	$ 861,750	$ 1,971,784	$ 4,851,371	$ 8,033,755
Percent of loans and commitments volume to small farmers and ranchers	72.2%	78.3%	75.3%	35.3%	44.7%

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

	For the Year Ended December 31, 2007				
	Annual Gross Sales				
(dollars 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	5,912	3,900	4,923	4,798	19,533
Number of new loans and commitments to small farmers and ranchers	4,248	3,006	3,576	2,184	13,014
Percent of new loans and commitments to small farmers and ranchers	71.9%	77.1%	72.6%	45.5%	66.6%
Total new loans and commitments volume	$ 140,031	$ 287,696	$ 811,162	$ 6,253,280	$ 7,492,169
Total new loans and commitments to small farmers and ranchers volume	$ 109,432	$ 221,802	$ 582,614	$ 1,982,299	$ 2,896,147
Percent of loan and commitment volume to small farmers and ranchers	78.1%	77.1%	71.8%	31.7%	38.7%

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