

# QUARTERLY REPORT



September 30, 2020



# FARM CREDIT EAST

## Management's Discussion and Analysis

The following commentary is a review of the financial condition and results of operations of Farm Credit East, ACA (the Association) for the nine month period ended September 30, 2020. This commentary should be read in conjunction with the accompanying unaudited consolidated financial statements and notes included in this report, as well as the 2019 Annual Report. Dollar amounts are in thousands unless otherwise noted.

The accompanying financial statements were prepared under the oversight of the Audit Committee.

### Business Overview

Farm Credit East is a lending institution of the Farm Credit System (the System). The System is a federally chartered network of borrower-owned lending institutions composed of cooperatives and related service organizations. We are a mission-based lender with authority to make loans and provide related financial services to eligible borrowers for qualified agricultural purposes. As a cooperative, the Association is owned by the members it serves. The territory served extends across a diverse agricultural region covering the entire states of Connecticut, Maine, Massachusetts, New Jersey and Rhode Island, six counties of New Hampshire and all of New York except two counties. The Association makes short and intermediate term loans for agricultural production and long term real estate mortgage loans. Our success begins with our extensive agricultural experience and knowledge of the market.

Farm Credit East's annual and quarterly reports to stockholders are available on the Association's website, **Farmcrediteast.com** or can be obtained free of charge by calling the Association's main office at 860-741-4380. Annual reports are available 75 days after year end and quarterly reports are available 40 days after each calendar quarter end. The financial condition and results of operations of CoBank, ACB (Bank), materially affect the risk associated with stockholder investments in Farm Credit East, ACA. To obtain a free copy of the CoBank Annual Report to Stockholders, please contact us at one of our offices or by accessing **CoBank.com**.

### Results of Operations

The COVID-19 pandemic has affected nearly every aspect of the economy, including the agriculture, forest products and commercial fishing industries. Although the impacts on customers, thus far, have been less than anticipated, and some customers have achieved strong earnings year to date, other customers are facing operational or financial challenges because of the pandemic. In either case, the ongoing impacts of the pandemic have created an uncertain outlook for many businesses. Farm Credit East will continue to be a reliable source of credit and high value financial services and work with customers negatively impacted by COVID-19 on a case by case basis. Farm Credit East also partnered with a third party vendor to provide customers access to Paycheck Protection Program (PPP) loans administered by the Small Business Association (SBA). Staff has provided technical assistance to borrowers applying to the program as well as helping them prepare for the forgiveness process. See **Business Outlook** section on page 9 for additional discussion on COVID-19.

Farm Credit East posted strong financial results for the nine month period ended September 30, 2020. Net income was \$152.6 million for the nine months ended September 30, 2020, an increase of \$11.2 million (7.9%) as compared with the same period in 2019. Our strong earnings primarily reflect higher net interest income, higher noninterest income and no provision for loan losses offset by higher operating expenses.

The following table reflects key performance results (*\$ in millions*).

For the nine months ended September 30	2020	2019
Net income	\$ 152.6	\$ 141.4
Net interest income	\$ 175.5	\$ 169.8
Net interest margin	3.04%	3.21%
Return on average assets	2.48%	2.55%
Return on average members equity	12.62%	12.44%

The following table provides detail of changes in the significant components of net income (*\$ in millions*).

<b>For the nine months ended September 30</b>	<b>2020 versus 2019</b>	<b>2019 versus 2018</b>
Increase in net interest income	\$ 5.7	\$ 16.2
Decrease (increase) in provision for loan losses	5.0	(2.5)
Increase (decrease) in noninterest income	5.9	(6.5)
Increase in noninterest expenses	(5.1)	(2.0)
Increase in provision for income taxes	(0.3)	(0.2)
<b>Total increase in net income</b>	<b>\$ 11.2</b>	<b>\$ 5.0</b>

### **Net Interest Income**

Net interest income was \$175.5 million for the nine months ended September 30, 2020, a \$5.7 million increase over the same period in 2019. The increase in net interest income was primarily driven by higher average loan volume and earnings from the Association's hedging position of its equity.

Information regarding the average daily balances and average rates earned and paid on our portfolio are presented in the following table:

<b>As of September 30</b>	<b>2020</b>	<b>2019</b>
Net interest income	\$ 175,527	\$ 169,843
Average balances:		
Average interest earning loans	\$ 7,724,807	\$ 7,076,638
Average interest bearing liabilities	\$ 6,339,169	\$ 5,786,269
Average yields and rates:		
Interest earning loan yield	4.11%	5.47%
Rate paid on interest bearing liabilities	1.66%	2.76%
Interest rate spread	2.45%	2.71%
Net interest margin (interest income as a percentage of average interest earning loans)	3.04%	3.21%

The Association's average loan rate was 4.11% as of September 30, 2020, down from 5.47% as of September 30, 2019. Average cost of debt funding also decreased from 2.76% in 2019 to 1.66% in 2020. Interest income and cost of debt are both lower due to decreases in publicized short-term rates which decreases both Farm Credit East's and our customer's cost of borrowing. The average interest rate spread over cost of funding decreased twenty six basis points year over year from 2.71% to 2.45%. The decrease in spread was due to the Association strategically lowering margins slightly within its loan portfolio.

### **Noninterest income**

Noninterest income was \$55.6 million for the nine months ended September 30, 2020, a \$5.9 million increase over the same period in 2019 mainly due to significantly higher loan fees and slightly higher patronage income offset by lower financially related services. Included in noninterest income is \$1.6 million in refunds received for a portion of excess Insurance Fund premiums paid in prior years, essentially unchanged from 2019. These refunds are nonrecurring items and represents the Association's portion of the excess in the System-wide Insurance Fund above the required minimum secure base amount.

Patronage income from CoBank is a significant part of the Association's noninterest income. Patronage income is based on the average balance of the Association's note payable to CoBank. For the nine month period ended September 30, 2020, CoBank patronage income totaled \$17.1 million, compared to \$17.4 million in 2019. The patronage rate paid by CoBank on the Association's note payable is 36 basis points in 2020 and was 40 basis points in 2019.

The Association also receives patronage income from CoBank and other Farm Credit entities that purchased interest in loans originated by the Association. For the nine months ended September 30, 2020 this revenue totaled \$7.6 million compared to \$6.2 million in 2019.

Noninterest income also includes fees for financial services, loan fees, compensation on participation loans and other noninterest income. These other noninterest income sources totaled \$29.3 million for the nine months ended September 30, 2020, an increase of \$4.9 million compared to 2019. Financial services fee income is the largest component with \$19.3 million in revenue for the nine months ended September 30, 2020, a decrease of \$0.9 million compared to 2019, partially the result of the Internal Revenue Service tax extension filing deadline being pushed back to October 15, 2020. Loan fees increased \$5.7 million to \$7.6 million for the nine months ended September 30, 2020. This increase is primarily a result of fee income received from new lending activity and conversion loan fees associated with changes to customer fixed rate contracts.

### ***Noninterest expense***

Total noninterest expenses totaled \$77.3 million for the nine months ended September 30, 2020, an increase of \$5.1 million, or 7.0%, from \$72.3 million over the same period last year.

Salaries and employee benefits is the primary component of noninterest expense and totaled \$49.3 million, for the nine months ended September 30, 2020 an increase of \$5.1 million from \$44.2 million compared to the same period a year ago. The increase is a result of higher retirement plan expenses, slightly higher staffing levels and normal merit and incentive compensation increases.

Insurance Fund premiums were \$3.9 million for the nine months ended September 30, 2020, a \$0.3 million increase compared to the same period a year ago. Insurance Fund premium rates are set by the Farm Credit System Insurance Corporation and were eight basis points of adjusted insured debt obligations for the first six months of 2020 and increased to eleven basis points July 1, 2020 compared to nine basis points in 2019.

Noninterest expenses also include fees paid to our technology service provider, occupancy and equipment expense and other operating expenses and totaled \$24.1 million for the nine months ended September 30, 2020, \$0.4 million decrease compared to the same period a year ago. The decrease is primarily related to lower travel and meeting expenses offset by higher information technology services for new software and digital initiatives.

### ***Provision for Income Taxes***

The provision for income taxes totaled \$1.2 million for the nine months ended September 30, 2020 and was \$0.4 million for the period ended September 30, 2019. The Association's effective tax rate is significantly less than the applicable federal and state tax statutory income tax rates primarily due to tax deductible patronage distributions and our tax exempt business activities.

### ***Patronage Distributions***

The Association has a patronage program that allows it to distribute its available net earnings to its stockholders. The patronage program consists of a qualified cash distribution and a non-qualified distribution.

An anticipated patronage distribution payable to members of \$57.2 million was accrued during the first nine months of 2020. In June, Farm Credit East's Board of Directors approved a \$30.0 million advance cash payment on 2020's patronage dividends which was distributed to eligible customers in late July. This distribution is intended to provide customers additional liquidity and cash flow in light of the impact COVID-19 has had on Northeast agriculture.

At December 31, 2019, liabilities included a \$70.0 million patronage distribution payable to members, which has since been distributed in cash. Additionally, in 2019 a special cash patronage dividend of \$25.0 million was paid in October.

**Loan Portfolio**

Loans outstanding were \$7.9 billion at September 30, 2020 an increase of \$443.6 million, or 6.0% from the December 31, 2019 balance of \$7.4 billion. Compared to September 30, 2019 loan volume grew 8.5%. The combined period to period growth was driven by our branch-based farm loan portfolio which grew \$72.0 million, or 1.5%, as strong demand for agricultural products benefited our producers. Our residential country living mortgage program grew \$133.7 million, or 15.7%, as reasonably strong demand continued in our Local Service Area (LSA) for this product and our capital markets group grew \$400.4 million, or 25.7% due to increased capital market activity resulting in our ability to purchase additional loan participations.

While we make loans and provide financially related services to qualified borrowers in agricultural and rural sectors and to certain related entities, our loan portfolio is diversified by loan participations purchased and sold, geographic locations served, commodities financed and loan size.

The Association purchases loan volume from other System and non-System entities to diversify risk related to existing commodities financed within our geographic area served, resulting in additional income for the ACA. In addition, we sell a portion of certain large loans to other System and non-System entities to reduce risk and comply with internal lending limits we have established. Our volume of participations purchased and sold as of September 30 are reflected in the following table.

<b>As of September 30</b>	<b>2020</b>	<b>2019</b>
Purchased loans	\$ 1,679,159	\$ 1,363,178
Sold loans	\$ 1,032,358	\$ 1,013,115

Loans are originated and serviced within the LSA in New York, New Jersey, Maine and throughout Southern New England. The geographic distribution of loans follows. As previously mentioned, we purchase loans outside our territory – which are included in other states in the following table.

<b>As of September 30</b>	<b>2020</b>	<b>2019</b>
New York	45%	48%
New Jersey	11	11
Maine	8	8
Connecticut	7	4
Massachusetts	6	6
Rhode Island, New Hampshire and other states	23	23
Total	100%	100%

The following table shows the primary agricultural commodities produced by our borrowers based on the Standard Industrial Classification System (SIC) published by the federal government. This system is used to assign commodity or industry categories based on the primary business of the customer. A primary business category is assigned when the commodity or industry accounts for 50% or more of the total value of sales for a business; however, a large percentage of agricultural operations typically includes more than one commodity.

<b>As of September 30</b>	<b>2020</b>	<b>2019</b>
Dairy	20.0%	21.6%
Timber	10.5	10.3
Processing & Marketing	10.2	10.0
Cash Field	10.0	9.5
Livestock	8.8	9.3
Fruit	8.7	9.0
Aquatic	4.4	4.4
Farm Services	3.8	3.6
Utilities	3.8	2.2
Potato	3.6	3.0
Vegetables	3.6	3.8
Nursery	2.7	3.1
Greenhouse	2.5	2.7
All Other	7.4	7.5
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>

### **High Risk Assets**

Nonperforming loan volume is comprised of nonaccrual loans, accruing restructured loans, and loans 90 days past due still accruing interest and are referred to as impaired loans. Nonaccrual loans represent all loans where there is a reasonable doubt as to collection of principal and/or interest. High Risk assets consist of impaired loans and other property owned. The following table summarizes high risk assets and delinquency information:

<b>As of</b>	<b>September 30, 2020</b>	<b>December 31, 2019</b>
Nonaccrual loans	\$ 41,141	\$ 39,901
Accruing loans 90 days or more past due	2,596	2,734
Accruing restructured loans	586	347
<b>Total impaired loans</b>	<b>\$ 44,323</b>	<b>\$ 42,982</b>
Other property owned	1,502	1,657
<b>Total high risk assets</b>	<b>\$ 45,825</b>	<b>\$ 44,639</b>
Impaired loans to total loans	0.56%	0.58%
High risk assets to total loans	0.58%	0.60%
Nonaccrual loans to total loans	0.52%	0.54%
Delinquencies as a % of total performing loans	0.34%	0.39%

The \$1.3 million increase in impaired loans was primarily due to challenges impacting a small number of loans to farm related businesses and part-time farmers. In general, the Association is adequately secured on much of the \$41.1 million in nonaccrual loan volume at September 30, 2020. However, the Association has established specific loan loss allowances of \$4.7 million in relation to \$15.5 million of the nonaccrual portfolio.

Other property owned is comprised of real or personal property that has been acquired through collections or deed in lieu of foreclosure. Other property owned totaled \$1.5 million at September 30, 2020, a \$0.2 million decrease from December 31, 2019. During the first nine months, the Association acquired one property and sold two properties. The Association is actively marketing all other property owned assets and intends to dispose of all properties in an orderly and timely fashion.

For additional loan type information, see Note 2 to these consolidated financial statements “Loans, Loan Quality and Allowance for Credit Losses”.

**Credit Quality Conditions and Measurements in the Loan Portfolio**

We review the credit quality of the loan portfolio on an on-going basis as part of our risk management practices. Each loan is classified according to the Uniform Classification System (UCS) which is used by all System institutions. The following table presents statistics based on UCS classified as a percent of total loans and related accrued interest.

<b>As of September 30</b>	<b>2020</b>	<b>2019</b>
Acceptable	92.12%	91.60%
Special mention	4.26	4.22
Substandard/doubtful	3.62	4.18
Total	100.00%	100.00%

Over the last twelve months, loans classified acceptable increased by 0.5% of total loans while loans classified as special mention remained essentially unchanged. Adversely classified loans (“substandard”, “doubtful” and “loss”) decreased by 0.6% of total loans from a year ago. While overall loan quality measures remain strong at September 30, 2020, we do expect some deterioration during the fourth quarter of 2020 and into 2021 as there is uncertainty around the magnitude and duration of business disruptions related to COVID-19 and its impact on the economy.

**Credit Risk Management**

Credit risk arises from the inability of an obligor to meet its repayment obligation and exists in our outstanding loans, unfunded loan commitments and letters of credit. We manage credit risk associated with our lending activities through an assessment of the credit risk profile of each individual borrower based on an analysis of the borrower’s credit history, repayment capacity, financial position and collateral. Repayment capacity focuses on the borrower’s ability to repay the loan based on cash flows from operations or other sources of income. The Association also manages credit risk by establishing limits for single borrower hold positions and industry concentrations based on underlying risks. The geographic and commodity diversity in the loan portfolio, coupled with disciplined underwriting reduces the potential for significant credit losses.

To further manage portfolio risk, the Association is a Preferred Lender under the USDA’s Farm Service Agency guarantee program and as of September 30, 2020 has guarantees totaling \$277.4 million. In addition, the Association has loan guarantees with State agencies totaling \$15.6 million. The Association also participates in the Farmer Mac Long Term Standby Commitment to Purchase Program and as of September 30, 2020, commitments totaling \$7.9 million were in this program.

**Provision for Loan Losses and Allowance for Credit Losses**

We monitor our loan portfolio on a regular basis to determine if any increase through provision for loan losses or decrease through a loan loss reversal in our allowance for loan losses is warranted based on our assessment of the probable and estimable losses inherent in our loan portfolio. The allowance for loan losses covers the funded portion of loans outstanding, while the reserve for unfunded commitments covers losses on unfunded lending commitments.

As a result of overall stable credit quality, Farm Credit East did not record a provision for loan losses for the nine months ended September 30, 2020 compared to a \$5.0 million provision recognized at September 30, 2019.

Information regarding comparative allowance coverage, as a percentage of key loan categories, are presented in the following table:

As of September 30	2020	2019
Components:		
Allowance for loan losses	\$ 71,164	\$ 84,633
Reserve for unfunded commitments	19,341	9,231
Allowance for credit losses (ACL)	\$ 90,505	\$ 93,864
ACL as a percentage of:		
Total loans	1.15%	1.29%
Nonaccrual loans	219.99%	193.45%
Impaired loans	204.19%	180.75%

For further discussion regarding the allowance for loan losses, refer to Note 2 to the consolidated financial statements “Loans, Loan Quality and Allowance for Credit Losses”.

### Liquidity and Funding Sources

The Association’s primary source of funding is CoBank. Funds are obtained through borrowing on a revolving line of credit governed by a General Financing Agreement. At September 30, 2020 the Association’s note payable to CoBank totaled \$6.4 billion.

The line of credit available to the Association is formula-driven based on Association loan volume and credit quality. Because of the funding relationship with CoBank, the Association does not maintain large balances in cash or other liquid investments. Substantially all of the Association’s assets are pledged as security to CoBank. The Association is in full compliance with its financing agreement with CoBank and has capacity under the agreement to borrow funds needed to meet anticipated loan demand.

### Members’ Equity

In conjunction with its annual financial planning process, the Association’s Board of Directors reviews and approves a Capitalization Plan. The objective of the plan is to build and maintain adequate capital for continued financial viability and to provide for growth necessary to meet customer needs.

Members’ equity, which is available as loanable funds, was \$1.7 billion at September 30, 2020 and consisted of capital stock and participation certificates of \$15.9 million, additional paid in capital of \$229.2 million, unallocated retained earnings of \$1.4 billion, and accumulated other comprehensive loss of (\$32.5) million.

### Capital Plan and Regulatory Requirements

The Board of Directors establishes a formal capital adequacy plan that addresses capital goals in relation to risks. The capital adequacy plan assesses the capital level necessary for financial viability and to provide for growth. Our plan is updated annually and approved as part of the Association’s annual Business Plan.

As shown in the following table, our capital and leverage ratios exceeded regulatory minimums. If these capital standards are not met, the FCA can impose restrictions, including limiting our ability to pay patronage distributions and retire equities.

As of September 30	2020	2019	FCA Minimum with Buffer
Common Equity Tier 1 Capital Ratio (CET1)	17.46%	18.01%	7.00%
Tier 1 Capital Ratio	17.46%	18.01%	8.50%
Total Regulatory Capital Ratio (TRC)	18.58%	19.18%	10.50%
Tier 1 Leverage Ratio	18.37%	18.92%	5.00%
UREE Leverage Ratio	20.19%	20.73%	1.50%
Permanent Capital	17.62%	18.20%	7.00%

For additional information on the New Capital Regulations, see Note 3 to these consolidated financial statements “Members’ Equity”.



### **Critical Accounting Estimates**

The financial statements are reported in conformity with accounting principles generally accepted in the United States of America. The Association's significant accounting policies are critical to the understanding of the results of operations and financial position because some accounting policies require management to make complex or subjective judgments and estimates that may affect the value of certain assets or liabilities. Management considers these policies critical because it has to make judgments about matters that are inherently uncertain. For a complete discussion of significant accounting policies, see Note 1 to the consolidated financial statements "Organization and Significant Accounting Policies".

### **Business Outlook**

After the COVID-19 pandemic evolved from a global public health crisis into a global economic crisis in the late first quarter and into the second quarter, the Federal government as well as state and local governments responded with unprecedented actions to slow the spread of the virus. In addition, Congress passed several major relief bills providing fiscal stimulus and support for individuals and businesses while the Federal Reserve deployed a full range of emergency monetary stimulus tools to ensure the financial system continued to function.

The third quarter saw some return to normalcy in the economy including those sectors served by Farm Credit East. No additional major relief programs were passed by Congress in the third quarter and some of the benefits from earlier measures were allowed to expire. Many agricultural producers have benefited from payments under the Commodity Food Assistance Program (CFAP) and a second round of payments, CFAP-2, was announced in September that should provide additional assistance to specialty crop producers.

Despite the major disruptions due to COVID-19 in many of the industries Farm Credit East serves, our customers have showed remarkable resilience in adjusting operations and many sectors, particularly dairy, greenhouse, nursery and agricultural retail have showed improved conditions through the end of the third quarter. Additionally, many industries modified supply chains or made other changes to adapt to market conditions, resulting in better-than-expected prices and markets for many Northeast producers. While the Association's year to date results have been better than expected, there are still many unknowns surrounding the pandemic, and thereby, the Association's business outlook continues to be uncertain. In addition, much of Farm Credit East's territory experienced dry conditions during the growing season which negatively impacted the production of many crops and feed supplies.

During the third quarter as the number of COVID-19 cases in Farm Credit East's states declined, the Association began to resume some operations that had been suspended including visiting customer businesses, having some employees return to offices and allowing customer office visits by appointment. Our limited re-opening has complied with state and local guidelines and enforced appropriate safeguards such as social distancing and required face coverings to protect the health and safety of our employees and customers. Farm Credit East continues to monitor developments in the states it serves and in accordance with state and local guidelines and adjusts business practices accordingly.

Early in the fourth quarter, some parts of the Northeast are seeing a resurgence of the virus. Depending on the continued federal, state and local response, the improving market conditions in the second and third quarters may not persist and could result in more widespread distress for customers. The financial distress that is being experienced by our customers could have an adverse impact on Farm Credit East in the event customers are unable to fulfill their obligations to the Association.

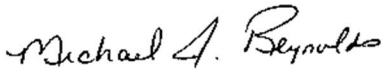
Farm Credit East's dedicated staff and strong financial condition will allow the Association to continue to meet customers' credit and financial service needs. Our Board of Directors and executive team are prepared for a resurgence of the pandemic in our region and a potential reversal of the second and third quarter's improving economic conditions.

### **Forward-Looking Statements**

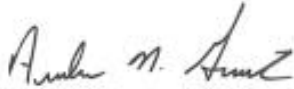
Certain information included in this report contains forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. Words such as “believes,” “could,” “estimates,” “anticipates,” “may,” “should,” “will,” or other variations of these terms or similar expressions are intended to identify forward-looking statements. These statements are based on assumptions and analyses made in light of experience, 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 fluctuations in the economy, the relative strengths and weaknesses in the agricultural credit sectors and in the real estate market, and the actions taken by the Federal Reserve in implementing monetary policy.

**Certification**

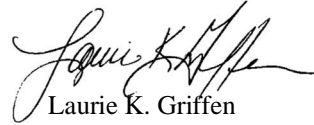
The undersigned certify that they have reviewed this report and it has been prepared in accordance with all applicable statutory and regulatory requirements and that the information contained herein is true, accurate and complete to the best of their knowledge and belief. There were no material changes in the internal control over financial reporting during the nine months ended September 30, 2020.



Michael J. Reynolds  
Chief Executive Officer



Andrew N. Grant  
Chief Financial Officer



Laurie K. Griffen  
Chair of the Board

Dated: November 5, 2020

**CONSOLIDATED BALANCE SHEETS**  
*(unaudited and dollars in thousands)*

	September 30, 2020	December 31, 2019
<b>ASSETS</b>		
Loans	\$ 7,878,567	\$ 7,434,982
Less: Allowance for loan losses	71,164	84,234
Net loans	7,807,403	7,350,748
Cash	11,148	21,481
Accrued interest receivable	23,633	28,489
Investment in CoBank, ACB	251,358	250,266
Premises and equipment, net	25,889	26,771
Other property owned	1,502	1,657
Other assets	78,599	69,571
<b>Total Assets</b>	<b>\$ 8,199,532</b>	<b>\$ 7,748,983</b>
<b>LIABILITIES</b>		
Notes payable to CoBank, ACB	\$ 6,423,891	\$ 6,036,193
Patronage distributions payable	27,150	70,000
Accrued interest payable	6,837	11,936
Reserve for unfunded commitments	19,341	9,125
Other liabilities	68,685	77,421
<b>Total Liabilities</b>	<b>6,545,904</b>	<b>6,204,675</b>
<b>MEMBERS' EQUITY</b>		
Capital stock and participation certificates	15,861	15,499
Additional paid-in capital	229,198	229,198
Unallocated retained earnings	1,441,079	1,345,666
Accumulated other comprehensive loss	(32,510)	(46,055)
<b>Total Members' Equity</b>	<b>1,653,628</b>	<b>1,544,308</b>
<b>Total Liabilities and Members' Equity</b>	<b>\$ 8,199,532</b>	<b>\$ 7,748,983</b>

The accompanying notes are an integral part of these statements.

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(unaudited and dollars in thousands)

	For the three months ended September 30,		For the nine months ended September 30,	
	2020	2019	2020	2019
<b>INTEREST INCOME</b>				
Loans	\$ 74,907	\$ 98,476	\$ 244,342	\$ 292,488
Other	128	203	358	515
Total interest income	75,035	98,679	244,700	293,003
<b>INTEREST EXPENSE</b>				
Notes payable to CoBank, ACB	17,078	39,638	69,158	123,148
Other	8	5	15	12
Total interest expense	17,086	39,643	69,173	123,160
Net interest income	57,949	59,036	175,527	169,843
Provision for loan losses	-	5,000	-	5,000
Net interest income after provision for loan losses	57,949	54,036	175,527	164,843
<b>NONINTEREST INCOME</b>				
Patronage income	7,891	7,201	24,675	23,605
Financially related services income	5,903	5,744	19,251	20,111
Compensation on participation loans, net	758	839	2,392	2,418
Loan fees	2,911	854	7,637	1,893
Other income	3	4	1,604	1,654
Total noninterest income	17,466	14,642	55,559	49,681
<b>NONINTEREST EXPENSE</b>				
Salaries and employee benefits	17,035	14,592	49,263	44,160
Occupancy and equipment	1,152	1,133	3,224	3,236
Insurance Fund premiums	1,605	1,206	3,934	3,603
Information technology services	3,339	3,173	11,526	9,716
Other operating expenses	1,720	3,150	9,389	11,563
Total noninterest expenses	24,851	23,254	77,336	72,278
Income before income taxes	50,564	45,424	153,750	142,246
Provision for income taxes	395	180	1,187	838
<b>Net Income</b>	<b>50,169</b>	<b>45,244</b>	<b>152,563</b>	<b>141,408</b>
<b>OTHER COMPREHENSIVE INCOME (LOSS)</b>				
Net change in cash flow hedge	(4,756)	1,237	13,525	15,951
Net change in retirement plan liabilities	-	-	20	5
Other Comprehensive Income (loss)	(4,756)	1,237	13,545	15,956
<b>Comprehensive Income</b>	<b>\$ 45,413</b>	<b>\$ 46,481</b>	<b>\$ 166,108</b>	<b>\$ 157,364</b>

The accompanying notes are an integral part of these statements.

## CONSOLIDATED STATEMENTS OF CHANGES IN MEMBERS' EQUITY

*(unaudited and dollars in thousands)*

	Capital Stock and Participation Certificates	Additional Paid-in- Capital	Unallocated Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Total Members' Equity
<b>Balance at December 31, 2018</b>	\$ 15,079	\$ 229,198	\$ 1,255,417	\$ (45,753)	\$ 1,453,941
Cumulative effect of adjustment from change in accounting principle	-	-	(944)	944	-
<b>Balance at December 31, 2018, as adjusted</b>	\$ 15,079	\$ 229,198	\$ 1,254,473	\$ (44,809)	\$ 1,453,941
Comprehensive income (loss)	-	-	141,408	15,956	157,364
Capital stock and participation certificates issued	990	-	-	-	990
Capital stock and participation certificates retired	(750)	-	-	-	(750)
Patronage Distribution	-	-	(71,670)	-	(71,670)
<b>Balance at September 30, 2019</b>	\$ 15,319	\$ 229,198	\$ 1,324,211	\$ (28,853)	\$ 1,539,875
<b>Balance at December 31, 2019</b>	\$ 15,499	\$ 229,198	\$ 1,345,666	\$ (46,055)	\$ 1,544,308
Comprehensive income (loss)	-	-	152,563	13,545	166,108
Capital stock and participation certificates issued	1,130	-	-	-	1,130
Capital stock and participation certificates retired	(768)	-	-	-	(768)
Patronage Distribution	-	-	(57,150)	-	(57,150)
<b>Balance at September 30, 2020</b>	\$ 15,861	\$ 229,198	\$ 1,441,079	\$ (32,510)	\$ 1,653,628

The accompanying notes are an integral part of these statements.

## Notes to Consolidated Financial Statements *(unaudited and dollars in thousands except as noted)*

### **NOTE 1 – Organization and Significant Accounting Policies**

Farm Credit East, ACA (the Association or ACA) and its subsidiaries are part of the Farm Credit System. A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2019, are contained in the 2019 Annual Report to Stockholders. These unaudited third quarter 2020 financial statements should be read in conjunction with the 2019 Annual Report to Stockholders.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements and should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2019 as contained in the 2019 Annual Report to Stockholders.

In the opinion of management, the unaudited financial information is complete and reflects all adjustments, consisting of normal recurring adjustments, necessary for a fair statement of results for the interim periods. The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statement and accompanying notes. Actual results could differ from those estimates. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year ended December 31, 2020. Descriptions of the significant accounting policies are included in the 2019 Annual Report to Stockholders. In the opinion of management, these policies and the presentation of the interim financial condition and results of operations conform to GAAP and prevailing practices within the banking industry.

### **Recently Adopted or Issued Accounting Pronouncements**

In March 2020, the Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act”), which provides relief from certain requirements under GAAP, was signed into law. Section 4013 of the CARES Act gives entities temporary relief from the accounting and disclosure requirements for troubled debt restructurings (TDRs) and if certain criteria are met these loan modifications may not need to be classified as TDRs. System entities have adopted this relief for qualifying loan modifications.

In March 2020, the Financial Accounting Standards Board (FASB) issued guidance entitled “Facilitation of the Effects of Reference Rate Reform on Financial Reporting.” The guidance provides optional expedients and exceptions for applying GAAP to contracts, hedging relationships and other transactions affected by reference rate reform. The guidance simplifies the accounting evaluation of contract modifications that replace a reference rate affected by reference rate reform and contemporaneous modifications of other contracts related to the replacement of the reference rate. With respect to hedge accounting, the guidance allows amendment of formal designation and documentation of hedging relationships in certain circumstances as a result of reference rate reform and provides additional expedients for different types of hedges, if certain criteria are met. The optional amendments are effective as of March 12, 2020, through December 31, 2022. The Association is evaluating the impact of adoption on the institution’s financial condition and its results of operations.

In December 2019, the FASB issued guidance entitled “Simplifying the Accounting for Income Taxes.” This guidance eliminates certain intra period tax allocations, foreign deferred tax recognition and interim period tax calculations. In addition, the guidance simplifies disclosure regarding capital and franchise taxes, the allocation of goodwill in business combinations, subsidiary financial statements and other disclosures. The new guidance is intended to eliminate and/or simplify certain aspects of income tax accounting that are complex or that require significant judgment in application or presentation. The guidance becomes effective for fiscal years beginning after December 15, 2021. Early adoption of the guidance is permitted and the Association adopted this guidance on January 1, 2020. The adoption of this guidance did not impact the Association’s financial condition, its results of operations or financial statement disclosures; nor will

the guidance impact the presentation of taxes for prior periods in the 2020 interim or year-end financial statements.

In August 2018, the FASB issued guidance entitled “Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Cost.” The guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by this guidance. This guidance became effective for interim and annual periods beginning after December 15, 2019. The guidance also requires an entity (customer) to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. It further specifies where to present expense and payments in the financial statements. The guidance is to be applied on a retrospective or prospective basis to all implementation costs incurred after the date of adoption. The adoption of this guidance did not impact the Association’s financial condition, its results of operations or financial statement disclosures.

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Defined Benefit Plans.” The guidance modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. This guidance becomes effective for fiscal years ended after December 15, 2020. Early adoption is permitted. The guidance is to be applied on a retrospective basis for all periods. The adoption of this guidance will not impact the Association’s financial condition or its results of operations, but will impact the employee benefit plan disclosures.

In August 2018, the FASB issued guidance entitled “Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement.” The guidance modifies the requirements on fair value measurements by removing, modifying or adding to the disclosures. This guidance become effective for interim and annual periods beginning after December 15, 2019. Early adoption was permitted and an entity was permitted to early adopt any removal or modified disclosures and delay adoption of the additional disclosures until their effective date. The Association early adopted the removal and modified disclosures during the fourth quarter of 2018. The adoption of this guidance did not impact the Association’s financial condition, its results of operations or financial statement disclosures.

In June 2016, the FASB issued guidance entitled “Measurement of Credit Losses on Financial Instruments.” The guidance replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. In November 2019, the FASB approved deferral of the effective date for certain entities for this guidance by two years, which will result in the new credit loss standard becoming effective for interim and annual reporting periods beginning after December 15, 2022. The Association qualifies for the delay in the adoption date. The Association continues to evaluate the impact of adoption on its financial condition, its results of operations and financial statement disclosures.



## NOTE 2 – Loans, Loan Quality and Allowance for Credit Losses

### Loans Outstanding

Loans outstanding by loan type are shown below.

As of	September 30, 2020		December 31, 2019	
Real estate mortgage	\$ 3,476,888	44.1%	\$ 3,299,720	44.4%
Production and intermediate term	2,651,866	33.7	2,683,757	36.1
Agribusiness	1,364,391	17.3	1,214,220	16.3
Rural infrastructure	302,675	3.8	154,304	2.1
Rural residential real estate	57,411	0.7	56,916	0.8
Other	25,336	0.4	26,065	0.3
Total Loans	\$ 7,878,567	100.0%	\$ 7,434,982	100.0%

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock as well as receivables. Long-term real estate loans are secured by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85% (97% if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in the loan to value ratios in excess of the regulatory maximum.

To mitigate the risk of loan losses, the Association may enter into long-term standby commitments to purchase agreements with the Federal Agricultural Mortgage Corporation (Farmer Mac). The agreements, which are effectively credit guarantees that will remain in place until the loans are paid in full, give the Association the right to sell the loans identified in the agreements to Farmer Mac in the event of default (typically four months past due), subject to certain conditions. The balance of loans under long-term standby commitments was \$7.9 million at September 30, 2020 and \$8.8 million at December 31, 2019. Fees paid to Farmer Mac for such commitments totaled \$30 thousand for the nine months ended September 30, 2020 and \$54 thousand at September 30, 2019. These amounts are classified as noninterest expense. In addition to Farmer Mac, the Association has credit enhancements with federal and state government agencies totaling \$293.0 million at September 30, 2020 and \$290.4 million at December 31, 2019.

### Credit Quality

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

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

The following tables show loans and related accrued interest classified, by management, under the FCA Uniform Loan Classification System as a percentage of total loans and related accrued interest receivable by loan type.

<b>As of September 30, 2020</b>	<b>Acceptable</b>	<b>OAEM</b>	<b>Substandard/ Doubtful</b>	<b>Total</b>
Real estate mortgage	40.3%	1.9%	1.9%	44.1%
Production and Intermediate term	30.7	1.8	1.2	33.7
Agribusiness	16.5	0.4	0.4	17.3
Rural infrastructure	3.6	-	0.2	3.8
Rural residential real estate	0.7	-	-	0.7
Other	0.3	0.1	-	0.4
<b>Total</b>	<b>92.1%</b>	<b>4.2%</b>	<b>3.7%</b>	<b>100.0%</b>

<b>December 31, 2019</b>	<b>Acceptable</b>	<b>OAEM</b>	<b>Substandard/ Doubtful</b>	<b>Total</b>
Real estate mortgage	40.3%	2.2%	1.9%	44.4%
Production and Intermediate term	32.9	1.8	1.4	36.1
Agribusiness	15.5	0.4	0.4	16.3
Rural infrastructure	1.8	0.2	0.1	2.1
Rural residential real estate	0.8	-	-	0.8
Other	0.3	-	-	0.3
<b>Total</b>	<b>91.6%</b>	<b>4.6%</b>	<b>3.8%</b>	<b>100.0%</b>

### Impaired Loans

Impaired loans are loans for which it is probable that all principal and interest will not be collected according to the contractual terms. Interest income recognized and payments received on nonaccrual impaired loans are applied in a similar manner as for nonaccrual loans, as described in Note 2 of the 2019 Annual Report to Stockholders.

Impaired loan information is shown in the following table. Loans past due 90 days or more and still accruing interest are adequately secured and in process of collection.

<b>As of</b>	<b>September 30, 2020</b>	<b>December 31, 2019</b>
Nonaccrual loans	\$ 41,141	\$ 39,901
Accruing loans 90 days or more past due	2,596	2,734
Accruing restructured loans	586	347
<b>Total impaired loans</b>	<b>\$ 44,323</b>	<b>\$ 42,982</b>

The following table presents information on impaired loans and related amounts in the allowance for loan losses.

<b>As of</b>	<b>September 30, 2020</b>	<b>December 31, 2019</b>
Impaired loans with related allowance	\$ 15,508	\$ 11,347
Impaired loans with no related allowance	28,815	31,635
<b>Total impaired loans</b>	<b>\$ 44,323</b>	<b>\$ 42,982</b>
<b>Total specific allowance</b>	<b>\$ 4,696</b>	<b>\$ 4,164</b>

<b>For the nine months ended September 30,</b>	<b>2020</b>	<b>2019</b>
Average impaired loans	\$ 47,193	\$ 51,947
Interest income recognized on impaired loans	\$ 4,226	\$ 449

### Commitments on Impaired loans

There were no material commitments to lend additional funds to debtors whose loans were classified as impaired at September 30, 2020.

### Loan Delinquencies

The following tables present an aging of past due loans.

As of September 30, 2020	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Accruing Loans 90 Days or More Past Due
Real estate mortgage	\$ 16,043	\$ 13,552	\$ 29,595	\$3,447,035	\$ 3,476,630	\$ 1,620
Production and intermediate term	9,146	11,784	20,930	2,630,936	2,651,866	976
Agribusiness	1,658	1,780	3,438	1,360,953	1,364,391	-
Rural infrastructure	-	-	-	302,675	302,675	-
Rural residential real estate	199	132	331	57,080	57,411	-
Other	-	-	-	25,594	25,594	-
<b>Total Loans</b>	<b>\$ 27,046</b>	<b>\$ 27,248</b>	<b>\$ 54,294</b>	<b>\$ 7,824,273</b>	<b>\$ 7,878,567</b>	<b>\$ 2,596</b>

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

December 31, 2019	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Accruing Loans 90 days or More Past Due
Real estate mortgage	\$ 20,342	\$ 11,963	\$ 32,305	\$ 3,267,415	\$ 3,299,720	\$ 1,392
Production and intermediate term	11,022	11,599	22,621	2,661,136	2,683,757	1,342
Agribusiness	1,642	154	1,796	1,212,424	1,214,220	-
Rural infrastructure	-	-	-	154,304	154,304	-
Rural residential real estate	189	144	333	56,583	56,916	-
Other	-	-	-	26,065	26,065	-
<b>Total Loans</b>	<b>\$ 33,195</b>	<b>\$ 23,860</b>	<b>\$ 57,055</b>	<b>\$ 7,377,927</b>	<b>\$ 7,434,982</b>	<b>\$ 2,734</b>

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

### Troubled Debt Restructuring

Troubled debt restructurings (TDRs) are loans in which the Association has granted a concession because the borrower is experiencing financial difficulty. Concessions may include debt forgiveness and /or interest rate reductions.

The Association had one TDR that occurred during the nine months ended September 30, 2020 and none that occurred during the nine months ended September 30, 2019. During the previous 12 months, there have been no payment defaults on TDR classified loans.

The following table provides information on outstanding loans restructured in troubled debt restructurings. These loans are included as impaired loans in the impaired loan tables.

	Loans Modified as TDRs		TDRs in Nonaccrual Status*	
	September 30, 2020	December 31, 2019	September 30, 2020	December 31, 2019
Real estate mortgage	\$ 570	\$ 350	\$ 41	\$ 61
Production and intermediate term	69	72	12	15
<b>Total</b>	<b>\$ 639</b>	<b>\$ 422</b>	<b>\$ 53</b>	<b>\$ 76</b>

\* represents the portion of loans modified as TDRs (first column) that are in nonaccrual status

### Allowance for Credit Losses

The following table presents the changes in the components of the allowance for credit losses. The allowance for credit losses includes the allowance for loan losses and the reserve for unfunded commitments.

<b>For the nine months ended September 30,</b>	<b>2020</b>	<b>2019</b>
<b>Allowance for Loan Losses</b>		
Beginning balance at January 1	\$ 84,234	\$ 78,370
Charge-offs	(3,887)	(217)
Recoveries	1,033	228
Provision for loan losses	-	5,000
Transfers from (to) Reserve for Unfunded Commitments	(10,216)	1,252
<b>Ending balance at September 30,</b>	<b>\$ 71,164</b>	<b>\$ 84,633</b>
<b>Reserve for Unfunded Commitments</b>		
Beginning balance at January 1	\$ 9,125	\$ 10,483
Transfers (to) from Allowance for Loan Losses	10,216	(1,252)
<b>Ending balance at September 30,</b>	<b>\$ 19,341</b>	<b>\$ 9,231</b>
<b>Allowance for Credit Losses</b>	<b>\$ 90,505</b>	<b>\$ 93,864</b>

### NOTE 3 – Members’ Equity

A description of the Association’s capitalization requirements, protection mechanisms, regulatory capitalization requirements and restrictions, and equities are provided below. Members’ equity is described and governed by the Association’s capitalization policies. Farm Credit East’s capitalization policies are specified in the Bylaws and in the Capitalization Plan approved by the Board of Directors. Copies of the Association’s Bylaws and Capitalization Plan are available to members at any time.

#### Capital stock and participation certificates

In accordance with the Farm Credit Act, and the Association’s capitalization Bylaws and Capitalization Plan, each Association borrower, as a condition of borrowing, is required at the time the loan is made, to invest in Class B Stock for agricultural loans or Class B Participation Certificates for country home and farm related business loans. Association Bylaws require that borrowers acquire capital stock or participation certificates, as a condition of borrowing, at least the lesser of \$1,000 or 2% of the amount of the loan, and not more than 10% of the amount of the loan. Pursuant to the Association Capitalization Plan, the Association Board has determined that Class B stock and Class B participation certificates shall be issued as follows:

For all loans (except where indicated below) Class B stock and Class B participation certificates shall be issued equal to one thousand dollars per customer as a condition of borrowing from this Association. For purposes of borrower stock, a customer is defined as the primary borrower on a loan. The intent of this policy is for each primary customer to have one thousand dollars of stock, regardless of the number of loans or balance on those loans to that customer. Stock shall be purchased at the beginning of a customer’s relationship and will not be retired until all loans to that customer are paid in full and there are no funds available for advances.

Exceptions to this policy are:

- At the time of the Farm Credit East mergers in 2010 and 2014, certain customers with less than one thousand dollars of stock were “grandfathered” at the stock level at conversion. Grandfathered customer stock will be frozen at converted levels until all loans are repaid, at which time the stock will be retired, or increased to one thousand dollars at the time of a future advance or credit action.
- Certain small borrowers (customers with total commitment less than ten thousand dollars initially) will be issued at 10% of the initial commitment, consistent with By-Law limitations.
- Certain interests in loans sold to other financial institutions.
- Loans to be sold into the secondary market

All stock and participation certificates are retired at the discretion of the Association's Board of Directors after considering the capitalization plan as well as regulatory and other requirements.

### Regulatory capitalization requirements and restrictions

The Farm Credit Administration (FCA) sets minimum regulatory capital requirements for Banks and Associations.

At September 30, 2020, the Association's capital and leverage ratios exceeded regulatory minimums as shown in the following table.

Ratio	Primary Components of Numerator	Denominator	Minimum Requirement	Minimum with Buffer	Ratios as of September 30, 2020
Common Equity Tier 1 (CET1) Capital	Unallocated retained earnings (URE), common cooperative equities (qualifying capital stock and allocated equity) <sup>1</sup>	Risk-adjusted assets	4.5%	7.0%	17.46%
Tier 1 Capital	CET1 Capital, non-cumulative perpetual preferred stock	Risk-adjusted assets	6.0%	8.5%	17.46%
Total Capital	Tier 1 Capital, allowance for loan losses <sup>2</sup> , common cooperative equities <sup>3</sup> , and term preferred stock and subordinated debt <sup>4</sup>	Risk-adjusted assets	8.0%	10.5%	18.58%
Tier 1 Leverage*	Tier 1 Capital	Total assets	4.0%	5.0%	18.37%
Unallocated Retained Earnings and URE Equivalents (UREE) Leverage	URE and URE Equivalents	Total assets	1.5%	-	20.19%
Permanent Capital	Retained earnings, common stock, non-cumulative perpetual preferred stock and subordinated debt, subject to certain limits	Risk-adjusted assets	7.0%	-	17.62%

\* Must include the regulatory minimum requirement for the URE and UREE Leverage ratio.

<sup>1</sup> Equities outstanding 7 or more years

<sup>2</sup> Capped at 1.25 % of risk-adjusted assets

<sup>3</sup> Outstanding 5 or more years, but less than 7 years

<sup>4</sup> Outstanding 5 or more years

### Patronage Distribution

In December 2019, the Board of Directors approved a patronage resolution. This resolution will allow the Association to pay a patronage refund on 2020 income provided the capital goals and earnings for the Association are achieved. The patronage program is described more fully in the 2019 Annual Report to Stockholders. Farm Credit East's Board of Directors approved a \$30.0 million advance cash payment on 2020's patronage which was distributed to eligible customers in late July.

### Accumulated Other Comprehensive Income/Loss

The Association reports accumulated other comprehensive income (loss) as a component of members' equity. Other comprehensive income refers to revenue, expenses, gains and losses that under GAAP are reported as an element of members' equity and comprehensive income but excluded from net income.

Other comprehensive income/loss results from the recognition of the retirement plans net unamortized gains and losses and prior service costs or credits of (\$54.4) million at September 30, 2020 and at December 31, 2019. Also included in accumulated other comprehensive income/loss is the unrealized holding gain or loss on cash flow derivatives of \$21.9 million and \$8.3 million at September 30, 2020 and December 31, 2019, respectively. There are no other items affecting comprehensive income or loss.

#### NOTE 4 – Fair Value Measurements

Accounting guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants in the principal or most advantageous market for the asset or liability. The fair value measurement is not an indication of liquidity. See Note 2 and Note 14 to the 2019 Annual Report to Stockholders for additional information.

#### Sensitivity to Changes in Significant Unobservable Inputs

Quoted market prices may not be available for the instruments presented below. Accordingly, fair values are based on internal models that consider judgments regarding anticipated cash flows, future expected loss experience, 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.

#### Quantitative Information about Recurring and Nonrecurring Fair Value Measurements

With regard to nonrecurring measurements for impaired loans and other property owned, it is not practicable to provide specific information on inputs as each collateral property is unique. System institutions utilize appraisals to value these loans and other property owned and take into account unobservable inputs such as income and expense, comparable sales, replacement cost and comparability adjustments.

Assets and liabilities measured at fair value on a recurring basis at period end for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
<b>September 30, 2020</b>				
Derivative assets	\$ -	\$ 21,957	\$ -	\$ 21,957
Assets held in trust	\$ 14,733	\$ -	\$ -	\$ 14,733
<b>December 31, 2019</b>				
Derivative assets	\$ -	\$ 9,208	\$ -	\$ 9,208
Assets held in trust	\$ 13,721	\$ -	\$ -	\$ 13,721
<b>Liabilities:</b>				
<b>September 30, 2020</b>				
Derivative liabilities	\$ -	\$ 55	\$ -	\$ 55
<b>December 31, 2019</b>				
Derivative liabilities	\$ -	\$ 832	\$ -	\$ 832

Assets measured at fair value on a non-recurring basis at period end for each of the fair value hierarchy values are summarized below:

	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
<b>Assets:</b>				
<b>September 30, 2020</b>				
Impaired loans	\$ -	\$ -	\$ 39,628	\$ 39,628
Other Property Owned	\$ -	\$ -	\$ 1,649	\$ 1,649
Rural Investments, LLC	\$ -	\$ -	\$ 17	\$ 17
<b>December 31, 2019</b>				
Impaired loans	\$ -	\$ -	\$ 38,817	\$ 38,817
Other Property Owned	\$ -	\$ -	\$ 1,821	\$ 1,821
Rural Investments, LLC	\$ -	\$ -	\$ 27	\$ 27

Financial assets and financial liabilities measured at carrying amounts and not measured at fair value on the Balance Sheet for each of the fair value hierarchy values are summarized below:

	September 30, 2020			December 31, 2019		
	Carrying Amount	Fair Value	Fair Value Hierarchy	Carrying Amount	Fair Value	Fair Value Hierarchy
<b>Financial assets:</b>						
Loans, net	\$ 7,807,403	\$ 7,988,786	Level 3	\$ 7,350,748	\$ 7,421,749	Level 3
Cash	\$ 11,148	\$ 11,148	Level 1	\$ 21,481	\$ 21,481	Level 1
<b>Financial liabilities:</b>						
Notes payable to ACB	\$ 6,423,891	\$ 6,567,050	Level 3	\$ 6,036,193	\$ 6,078,845	Level 3

### Valuation Techniques

As more fully discussed in Note 2 to the 2019 Annual Report to Stockholders, accounting guidance establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following represent a brief summary of the valuation techniques used for the Association's assets and liabilities.

### Cash

The carrying value of cash is a reasonable estimate of fair value.

### Assets Held in Trust

Assets held in trust funds related to deferred compensation and supplemental retirement plans and are classified within Level 1. These assets include investments that are actively traded and have quoted net asset values that are observable in the marketplace.

### Loans

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

### Other Property Owned

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

### Impaired Loans

For certain loans evaluated for impairment under FASB impairment guidance, the fair value is based upon

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

### **Notes payable to CoBank, ACB**

The notes payable are segregated into pricing pools according to the types and terms of the loans (or other assets) which they fund. Fair value of the note payable is estimated by discounting the anticipated cash flows of each pricing pool using the current rate that would be charged for additional borrowings. For purposes of this estimate it is assumed the cash flow on the notes is equal to the principal payments on the Association's loan receivables plus accrued interest on the notes payable. This assumption implies that earnings on the Association's interest margin are used to fund operating expenses and capital expenditures.

### **Rural Investments, LLC**

For these investments, the fair value is based upon the underlying loans contained in the investment. The fair value measurement process uses independent appraisals and other market-based information, but in many cases it also requires significant input based on management's knowledge of and judgment about current market conditions, specific issues relating to the collateral and other matters. As a result, these fair value measurements fall within Level 3 of the hierarchy. When the value of the collateral is less than the principal balance of the investment a loss is realized.

### **Derivatives**

Exchange-traded derivatives valued using quoted prices are classified within Level 1 of the valuation hierarchy. However, few classes of derivative contracts are listed on an exchange; thus, the Association's derivative positions are valued using internally developed models that use as their basis readily observable market parameters and are classified within Level 2 of the valuation hierarchy. Such derivatives include basic interest rate swaps. Derivatives that are valued based upon models with significant unobservable market parameters and that are normally traded less actively or have trade activity that is one way are classified within Level 3 of the valuation hierarchy. The Association does not have any derivatives classified within Level 3.

The models used to determine the fair value of derivative assets and liabilities use an income approach based on observable market inputs, primarily the LIBOR swap curve and volatility assumptions about future interest rate movements.

## **NOTE 5 – Derivative Instruments and Hedging Activities**

### **Risk Management Objectives**

The Association 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 Association's goal is to manage interest rate sensitivity by modifying the repricing or maturity characteristics of certain balance sheet assets or liabilities so that the net interest margin is not adversely affected by movements in interest rates. As a result of interest rate fluctuations the Association's interest income and interest expense of hedged variable-rate assets will increase or decrease. The effect of this variability in earnings is expected to be substantially offset by the Association's gains and losses on the derivative instruments that are linked to these hedged assets. The Association 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.

By using derivative instruments, the Association exposes itself to credit and market risk. Generally, when the fair value of a derivative contract is positive, this indicates that the counterparty owes the Association, thus creating a repayment risk for the Association. When the fair value of the derivative contract is negative, the Association owes the counterparty and, therefore, assumes no repayment risk. The



Association's derivative activities are monitored by its asset/liability committee (ALCO) as part of its oversight of asset/liability and treasury functions.

### Uses of Derivatives

The Association enters into interest rate swaps to stabilize net interest income on variable priced loan assets, to the extent they are funded with equity. Under interest rate swap arrangements, the Association agrees with other parties (CoBank) to exchange, at specified intervals, payment streams calculated on a specified notional principal amount, with at least one stream based on a specified floating rate index. The Association's interest-earning assets, to the degree they are funded with debt, are matched with similarly priced and termed liabilities. Volatility in net interest income comes from equity funded variable priced assets. To the degree that variable priced assets are funded with equity, interest rate swaps in which the Association pays the floating rate and receives the fixed rate (receive fixed swaps) are used to reduce the impact of market fluctuations on the Association's net interest income.

The notional amounts of derivatives are shown in the following table:

	September 30, 2020	December 31, 2019
Interest Rate Contracts	\$ 1,240,000	\$ 1,135,000

### Accounting for Derivative Instruments and Hedging Activities

The Association records derivatives as assets and liabilities at their fair value in the consolidated balance sheets and records changes in the fair value of a derivative in accumulated other comprehensive income (loss). The Association only enters into cash flow hedge transactions.

### Cash Flow Hedges

The Association uses "receive fixed/pay variable" interest rate swaps to hedge the risk of overall changes in the cash flows of an asset. The asset is defined as a pool of long term variable rate loans equal to the notional amount of the swaps, and not exceeding the Association's equity position. These swaps, which qualify for hedge accounting, have up to a three year term, with a pay rate indexed to the three month London Inter-Bank Offered Rate (LIBOR).

### Summary of Derivative Instruments and Hedging Activities

A summary of the impact of derivative financial instruments in the consolidated balance sheets is shown in the following table:

	Derivative Assets <sup>(1)</sup>	Derivative Liabilities <sup>(2)</sup>
<b>September 30, 2020</b>		
Interest Rate Contracts	\$ 21,957	\$ 55
<b>December 31, 2019</b>		
Interest Rate Contracts	\$ 9,208	\$ 832

<sup>(1)</sup>Derivative assets are included in other assets in the consolidated balance sheets

<sup>(2)</sup>Derivative liabilities are included in other liabilities in the consolidated balance sheets

A summary of the impact of derivative financial instruments in the consolidated statements of comprehensive income is shown in the following tables:

	Net Amount of Gain or (Loss) Recognized in Income on Derivatives <sup>(1)</sup>	
September 30	2020	2019
Interest Rate Contracts	\$ 9,773	\$ (3,935)

<sup>(1)</sup>Located in interest expense in the consolidated statements of income for each of the respective periods presented.

September 30	Amount of Gain (Loss) Recognized in Accumulated Other Comprehensive Income (Loss) on Derivatives	
	2020	2019
Interest Rate Contracts	\$ 13,526	\$ 15,951

**Counterparty Credit Risk**

The Association is exposed to credit loss in the event of nonperformance by other parties to the interest rate swap agreement. If a counterparty fails to fulfill its performance obligations under a derivative contract, the Association's credit risk will equal the fair value gain in a derivative. The Association minimizes the credit (or repayment) risk by only entering into transactions with CoBank, its funding bank and are collateralized through loan agreements. Notwithstanding collateral and netting provisions, our derivative assets and liabilities are not offset in the accompanying consolidated balance sheets.

**NOTE 6 – Subsequent Events**

The Association has evaluated subsequent events through November 5, 2020 which is the date the financial statements were issued or available to be issued. No subsequent event items met the criteria for disclosure.

### Senior Officers

Michael J. Reynolds	President and Chief Executive Officer
Paul S. Bajgier	Executive Vice President Accounting and Branch Operations and Treasurer
William S. Bathel	Executive Vice President and Chief Operating Officer
Briana S. Beebe	Executive Vice President and Human Resources Director
Janice P. Bitter	Executive Vice President and Regional Manager
John P. Caltabiano	Executive Vice President and Innovation Leader
Thomas W. Cosgrove	Executive Vice President of Knowledge Exchange, Public Relations and Marketing
Daryn J. Deveau	Executive Vice President and Risk and Technology Director
Alena C. Gfeller	Executive Vice President, Managing Counsel and Corporate Secretary
Andrew N. Grant	Executive Vice President and Chief Financial Officer
Brian K. Monckton	Executive Vice President and Regional Manager
Roger E. Murray	Executive Vice President and Chief Marketplace Officer
David H. Pugh	Executive Vice President and Regional Manager
Keith Stechschulte	Executive Vice President and Regional Manager

### Board of Directors

Laurie K. Griffen, Chair	Elected	Sod	Stillwater, NY
John P. Knopf, Vice Chair	Elected	Dairy	Canandaigua, NY
Kurt W. Alstede	Elected	Fruit & Vegetable	Chester, NJ
Michael N. Brooks	Elected	Vegetable	Elmer, NJ
Barry A. Buck	Elected	Potato	Mapleton, ME
Peter R. Call	Elected	Vegetable	Batavia, NY
Tim C. Chan	Appointed	At Large	Claremont, NH
David E. Hardie	Elected	Dairy	Lansing, NY
Philip J. Jones	Elected	Ag Retail	Shelton, CT
LouAnne F. King	Elected	Dairy	Madrid, NY
James A. Robbins II	Elected	Forestry	Searsmont, ME
Lisa P. Sellew	Elected	Nursery	Lebanon, CT
Douglas W. Shelmidine	Elected	Dairy	Adams, NY
Peter H. Triandafillou	Appointed	Customer	Orono, ME
Terry R. Zittel	Elected	Vegetables	Eden, NY



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