

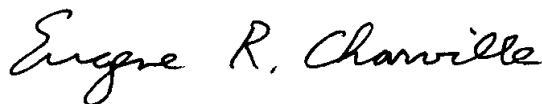
# SECOND QUARTER 2009

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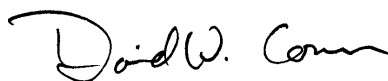
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## CERTIFICATION

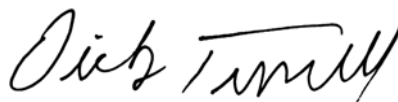
The undersigned certify that we have reviewed the June 30, 2009 quarterly report of AgCarolina Financial, ACA, that the report has been prepared under the oversight of the Audit Committee of the Board of Directors and in accordance with all applicable statutory or regulatory requirements, and that the information contained herein is true, accurate, and complete to the best of our knowledge and belief.



Eugene R. Charville  
Chief Executive Officer



David W. Corum  
Chief Financial Officer



Dick Tunnell  
Chairman of the Board

July 30, 2009

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*AgCarolina Financial, ACA*

# Report on Internal Control Over Financial Reporting

The Association's principal executives and principal financial officers, or persons performing similar functions, are responsible for establishing and maintaining adequate internal control over financial reporting for the Association's Consolidated Financial Statements. For purposes of this report, "internal control over financial reporting" is defined as a process designed by, or under the supervision of the Association's principal executives and principal financial officers, or persons performing similar functions, and effected by its Board of Directors, management and other personnel. This process provides reasonable assurance regarding the reliability of financial reporting information and the preparation of the Consolidated Financial Statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

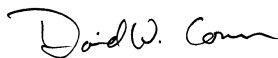
Internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Association, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial information in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures are being made only in accordance with authorizations of management and directors of the Association, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Association's assets that could have a material effect on its Consolidated Financial Statements.

The Association's management has completed an assessment of the effectiveness of internal control over financial reporting as of June 30, 2009. In making the assessment, management used the framework in *Internal Control—Integrated Framework*, promulgated by the Committee of Sponsoring Organizations of the Treadway Commission, commonly referred to as the "COSO" criteria.

Based on the assessment performed, the Association concluded that as of June 30, 2009, the internal control over financial reporting was effective based upon the COSO criteria. Additionally, based on this assessment, the Association determined that there were no material weaknesses in the internal control over financial reporting as of June 30, 2009.



Eugene R. Charville  
Chief Executive Officer



David Corum  
Chief Financial Officer

July 30, 2009

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

*(dollars in thousands)*

The following commentary reviews the financial condition and results of operations of AgCarolina Financial (Association) for the six months ended June 30, 2009. These comments should be read in conjunction with the accompanying financial statements, notes to the financial statements and the 2008 annual report of the Association.

## **LOAN PORTFOLIO**

The Association provides funds to farmers, rural homeowners, and farm-related businesses for financing of short and intermediate-term loans and long-term real estate mortgage loans. Predominant commodities in the portfolio are tobacco, cotton, forestry, and hogs, which constitute \$507,616, or 57 percent, of the loan portfolio as of June 30, 2009. Other major farm commodities include poultry, landlords, farm services, field crops, horticulture, and general livestock. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the numerous opportunities for non-farm income in the area, somewhat reduces the level of dependency on a given commodity.

The net loan volume of the Association as of June 30, 2009, was \$882,582, an increase of \$51,061 or 6.14 percent as compared to \$831,521 at December 31, 2008. Net loans accounted for 89.07 percent of total assets at June 30, 2009 as compared to 86.63 percent of total assets at December 31, 2008. The increase in net loan volume during the reporting period is primarily attributed to seasonal lending. The short-term portfolio, which is heavily influenced by operating-type loans, normally reaches a peak in August and declines in the fall and winter months as farm commodities are marketed and proceeds are applied to the operating loans.

There is an inherent risk in the extension of any type of credit. Portfolio credit quality continues to be maintained at an acceptable level, however, and credit administration remains satisfactory. Nonaccrual loans increased from \$12,058 at December 31, 2008 to \$15,082 at June 30, 2009, for an increase of 25.08 percent. The increase is due to the addition of a small number of larger accounts into nonaccruing status. Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. During the quarter the Association recognized net loan losses of \$1,167 and subsequently increased the allowance for loan losses by \$1,190 through a provision for loan losses. The allowance for loan losses at June 30, 2009 was \$7,637 as compared to \$7,618 at

December 31, 2008 and was considered by management to be adequate to cover possible losses. The ratio of the allowance for loan losses to loans at June 30, 2009 was 0.86 percent.

Other investments consists of tobacco buyout Successor-in-Interest Contracts (SIIC) which come under the FCA's Mission Related Investments. Under the SIIC, the tobacco quota holders and producers may assign their rights to receive tobacco buyout contract payments to a third party. The third party, or successor, purchases the entire contract and all related rights and obligations associated with the contract. As of June 30, 2009 the Association held tobacco buyout SIIC of \$61,917, a decrease of \$8,710 or 12.33%, as compared to \$70,627 as of December 31, 2008. The decrease is due to the receipt of the scheduled annual payment from the government during the first quarter.

## **RESULTS OF OPERATIONS**

### ***For the three months ended June 30, 2009***

Net income for the three months ended June 30, 2009 totaled \$3,220, a decrease of \$1,413, or 30.50 percent, as compared to the same period of 2008. The primary reason for the decrease in net income is due to an increase in the provision for loan losses of \$1,190, and an increase in noninterest expense over the same period in 2008. At June 30, 2009, total interest income decreased by \$2,134 compared to June 30, 2008. The decrease in interest income is primarily due to the general decrease in interest rates as compared to the same period in 2008.

Interest income from nonaccrual loans was \$26 for the three months ended June 30, 2009, a decrease of \$23 from the same period of 2008. Interest expense decreased \$2,166 for the three months ended June 30, 2009, as compared to the comparable period of 2008. The decrease in interest expense is primarily attributed to the general decline in interest rates.

Noninterest income for the three months ended June 30, 2009 totaled \$2,763 as compared to \$2,495 for the same period of 2008, an increase of \$268. The increase is primarily due to an increase in equity in earnings of other Farm Credit institutions, and from other income.

Noninterest expense for the three months ended June 30, 2009 was \$3,976, an increase of \$525 as compared to the same period of 2008. The major components of noninterest expense are salaries and employee benefits, occupancy and equipment expenses, and general operating expenses. Salaries and employee benefits totaled \$2,734 for the three months ended June 30, 2009, for an increase of \$467, or 20.60 percent, as

compared to the same period of 2008. The increase is primarily due to increased costs related to the Association's pension plan.

### **For the six months ended June 30, 2009**

Net income for the six months ended June 30, 2009 totaled \$6,871, a decrease of \$2,589, or 27.37 percent, as compared to the same period of 2008. The primary reason for the decrease in net income is due to the provision for loan losses of \$1,590. At June 30, 2009, total interest income decreased by \$4,915 compared to the same period in 2008. The decrease in interest income is due primarily to the general decrease in interest rates as compared to the same period in 2008.

Interest income from nonaccrual loans was \$97 as of June 30, 2009, a decrease of \$6 from the same period of 2008. Interest expense decreased \$4,789 for the first six months in 2009, as compared to the comparable period of 2008. The decrease in interest expense is also primarily attributed to the decrease in interest rates.

Noninterest income for the six months ended June 30, 2009 totaled \$5,846 as compared to \$5,620 for the same period of 2008, an increase of \$226. The increase is primarily due to an increase in equity in earnings of other Farm Credit institutions.

Noninterest expense for the six months ended June 30, 2009 was \$8,258, an increase of \$1,101 as compared to the same period of 2008. The major component of noninterest expense is salaries and employee benefits. Salaries and employee benefits totaled \$5,587 for the six months ended June 30, 2009, for an increase of \$1,039 or 22.85 percent, as compared to the same period of 2008. The increase is primarily due to increased costs related to the Association's pension plan.

## **LIQUIDITY AND FUNDING SOURCES**

### *Liquidity*

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with AgFirst Farm Credit Bank (Bank) and from income generated by operations. Sufficient liquid funds have been available to meet all financial obligations.

### *Funding Sources*

The principal source of funds for the Association is the borrowing relationship established with the Bank through a General Financing Agreement. The General Financing Agreement utilizes the Association's credit and fiscal performance as criteria for establishing a line of credit on which the Association may draw funds. The funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate note is utilized by the Association to fund variable rate loan advances and operating funds requirements. The fixed rate note is used specifically to fund fixed rate loan advances made by the Association. The total notes payable to the Bank at June 30, 2009 was \$832,812 as compared to \$799,323 at December 31,

2008. The 4.19 percent increase during the period is primarily attributed to seasonal lending.

The Association has no lines of credit outstanding with third parties as of June 30, 2009.

## **CAPITAL RESOURCES**

Total members' equity at June 30, 2009, increased 7.88 percent to \$143,690 from the December 31, 2008, total of \$133,194. The increase is attributed to the increase in retained earnings and capital stock. Total capital stock and participation certificates were \$15,504 on June 30, 2009, as compared to \$11,727 on December 31, 2008. The increase in capital stock resulted primarily from an increase in preferred stock. As of June 30, 2009 the Association had \$12,468 of preferred stock outstanding as compared to \$8,702 as of December 31, 2008.

Farm Credit Administration (FCA) regulations require all Farm Credit institutions to maintain minimum permanent capital, total surplus and core surplus ratios. These ratios are calculated by dividing the Association's permanent capital, total surplus and core surplus as defined in FCA regulations, by a risk-adjusted asset base. As of June 30, 2009, the Association's total surplus ratio and core surplus ratio were both 13.07 percent, and the permanent capital ratio was 14.92 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

**NOTE:** Shareholder investment in the Association could be affected by the financial condition and results of operations of AgFirst Farm Credit Bank. Copies of AgFirst's annual and quarterly reports are available upon request free of charge by calling 1-800-845-1745, ext. 378, or writing Stephen Gilbert, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, [www.agfirst.com](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-919-250-9500, writing Linda Strickland, AgCarolina Financial, ACA, P. O. Box 14789, Raleigh, NC 27620, or accessing the website, [www.agcarolina.com](http://www.agcarolina.com). The Association prepares a quarterly report within 40 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the institution.

# AgCarolina Financial, ACA

## Consolidated Balance Sheets

| <i>(dollars in thousands)</i>                | <b>June 30,<br/>2009</b><br><i>(unaudited)</i> | <b>December 31,<br/>2008</b><br><i>(audited)</i> |
|--|--|--|
| <b>Assets</b>                                |  |  |
| Cash   | \$ 138   | \$ 1,775   |
| Loans  | 890,219  | 839,139  |
| Less: allowance for loan losses              | 7,637  | 7,618  |
| Net loans                                    | 882,582  | 831,521  |
| Loans held for sale                          |  |  |
| Other investments                            | 61,917   | 70,627   |
| Accrued interest receivable                  | 11,774   | 17,371   |
| Investment in other Farm Credit institutions | 13,542   | 13,542   |
| Premises and equipment, net                  | 8,252  | 8,347  |
| Other property owned                         | 617  | 252  |
| Due from AgFirst Farm Credit Bank            | —  | 6,330  |
| Other assets                                 | 12,017   | 10,114   |
| Total assets                                 | \$ 990,839                                     | \$ 959,879                                       |
| <b>Liabilities</b>                           |  |  |
| Notes payable to AgFirst Farm Credit Bank    | \$ 832,812                                     | \$ 799,323                                       |
| Accrued interest payable                     | 2,247  | 2,736  |
| Patronage refund payable                     | 77   | 6,592  |
| Other liabilities                            | 12,013   | 18,034   |
| Total liabilities                            | 847,149  | 826,685  |
| Commitments and contingencies                |  |  |
| <b>Members' Equity</b>                       |  |  |
| Capital stock and participation certificates | 15,504   | 11,727   |
| Retained earnings                            |  |  |
| Allocated                                    | 62,060   | 61,465   |
| Unallocated                                  | 66,126   | 60,002   |
| Total members' equity                        | 143,690  | 133,194  |
| Total liabilities and members' equity        | \$ 990,839                                     | \$ 959,879                                       |

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

# AgCarolina Financial, ACA

## Consolidated Statements of Income

(unaudited)

| <i>(dollars in thousands)</i>  | For the three months<br>ended June 30, |           | For the six months<br>ended June 30, |           |
|--|--|-----------|--------------------------------------|-----------|
|  | 2009                                   | 2008      | 2009                                 | 2008      |
| <b>Interest Income</b>   |  |           |                                      |           |
| Loans  | \$ 11,522                              | \$ 13,568 | \$ 23,012                            | \$ 27,781 |
| Other  | 858                                    | 946       | 1,689                                | 1,835     |
| Total interest income  | 12,380                                 | 14,514    | 24,701                               | 29,616    |
| <b>Interest Expense</b>  |  |           |                                      |           |
| Notes payable to AgFirst Farm Credit Bank  | 6,757                                  | 8,923     | 13,828                               | 18,617    |
| Net interest income  | 5,623                                  | 5,591     | 10,873                               | 10,999    |
| Provision for (reversal of allowance for) loan losses                              | 1,190                                  | —         | 1,590                                | —         |
| Net interest income after provision for<br>(reversal of allowance for) loan losses | 4,433                                  | 5,591     | 9,283                                | 10,999    |
| <b>Noninterest Income</b>  |  |           |                                      |           |
| Loan fees  | 839                                    | 890       | 2,180                                | 2,337     |
| Fees for financially related services  | 140                                    | 62        | 271                                  | 235       |
| Equity in earnings of other Farm Credit institutions                               | 1,646                                  | 1,530     | 3,194                                | 2,925     |
| Gains (losses) on other property owned, net  | (6)                                    | —         | (2)                                  | —         |
| Gains (losses) on sale of rural home loans, net                                    | 14                                     | 17        | 18                                   | 24        |
| Other noninterest income   | 130                                    | (4)       | 185                                  | 99        |
| Total noninterest income   | 2,763                                  | 2,495     | 5,846                                | 5,620     |
| <b>Noninterest Expense</b>   |  |           |                                      |           |
| Salaries and employee benefits   | 2,734                                  | 2,267     | 5,587                                | 4,548     |
| Occupancy and equipment  | 292                                    | 253       | 562                                  | 541       |
| Insurance Fund premium   | 366                                    | 309       | 699                                  | 593       |
| Other operating expenses   | 584                                    | 622       | 1,410                                | 1,475     |
| Total noninterest expense  | 3,976                                  | 3,451     | 8,258                                | 7,157     |
| Income before income taxes   | 3,220                                  | 4,635     | 6,871                                | 9,462     |
| Provision (benefit) for income taxes   | —                                      | 2         | —                                    | 2         |
| Net income   | \$ 3,220                               | \$ 4,633  | \$ 6,871                             | \$ 9,460  |

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

AgCarolina Financial, ACA  
**Consolidated Statements of Changes in  
Members' Equity**

*(unaudited)*

| <i>(dollars in thousands)</i>                                     | Capital<br>Stock and<br>Participation<br>Certificates | Retained Earnings |             | Total<br>Members'<br>Equity |
|---|---|-------------------|-------------|-----------------------------|
|   |   | Allocated         | Unallocated |                             |
| Balance at December 31, 2007                                      | \$ 12,092   | \$ 56,644         | \$ 58,446   | \$ 127,182                  |
| Net income  |   |                   | 9,460       | 9,460                       |
| Capital stock/participation<br>certificates issued/(retired), net | 1,932   |                   |             | 1,932                       |
| Dividends declared/paid   | 203   |                   | (203)       |                             |
| Patronage distribution adjustment                                 |   | 26                | (43)        | (17)                        |
|   |   | 26                | (43)        | (17)                        |
| Balance at June 30, 2008  | \$ 14,227   | \$ 56,670         | \$ 67,660   | \$ 138,557                  |
| Balance at December 31, 2008                                      | \$ 11,727   | \$ 61,465         | \$ 60,002   | \$ 133,194                  |
| Net income  |   |                   | 6,871       | 6,871                       |
| Capital stock/participation<br>certificates issued/(retired), net | 3,622   |                   |             | 3,622                       |
| Dividends declared/paid   | 155   |                   | (155)       | —                           |
| Patronage distribution adjustment                                 |   | 595               | (592)       | 3                           |
|   |   | 595               | (592)       | 3                           |
| Balance at June 30, 2009  | \$ 15,504   | \$ 62,060         | \$ 66,126   | \$ 143,690                  |

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







