

THIRD QUARTER 2004

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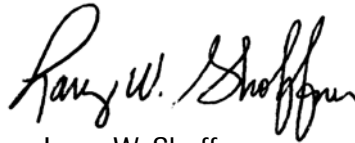
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Larry W. Shoffner
Chief Executive Officer



Bobby E. McCollum, Jr.
Chairman of the Board

October 29, 2004

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 Carolina Farm Credit, ACA (Association) for the period ended September 30, 2004. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2003 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. The Association's loan portfolio is diversified over a range of agricultural commodities in our region, including part-time farm, poultry, and rural home loans. 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, has an impact on the level of dependency on a given agricultural commodity.

The gross loan volume of the Association as of September 30, 2004, was \$1,070,909, an increase of \$18,050 as compared to \$1,052,859 at December 31, 2003. Net loans outstanding at September 30, 2004, were \$1,049,576 as compared to \$1,030,911 at December 31, 2003. Net loans accounted for 94.93 percent of total assets at September 30, 2004, as compared to 95.41 percent of total assets at December 31, 2003.

The increase in gross and net loan volume during the reporting period is attributed primarily to seasonal lending. The short-term portfolio, which is heavily influenced by operating-type loans, normally reaches a peak balance in August and rapidly declines in the fall 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 \$6,734 at December 31, 2003, to \$7,046 at September 30, 2004. This increase is primarily the result of transferring loans into nonaccrual status in excess of repayments and transfer to other property owned.

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. The allowance for loan losses at September 30, 2004, was \$21,333 compared to \$21,948 at December 31, 2003, and was considered by management to be adequate to cover possible losses.

In June, 2003, the American Institute of Certified Public Accountants' Accounting Standards Executive Committee (AcSEC) issued a proposed Statement of Position (SOP) – Allowance for Credit Losses, which was intended to clarify the methodology for estimating the allowance for credit losses and to enhance financial statement disclosures related to the allowance for credit losses. In January 2004, AcSEC abandoned its proposed SOP and announced that it would focus instead on improving financial statement disclosures regarding the allowance for loan losses.

We plan to conduct a study to further refine our methodology for calculating the allowance for loan losses taking into account generally accepted accounting principles, and applicable Farm Credit Administration requirements, as well as the Securities and Exchange Commission and Federal Financial Institutions Examination Council guidelines. The study is likely to be completed by the fourth quarter of 2004 with any appropriate reduction to the allowance for loan losses implemented at that time, which reduction may be significant.

RESULTS OF OPERATIONS

For the three months ended September 30, 2004

Net income for the three months ended September 30, 2004, totaled \$5,519, as compared to \$4,927 for the same period in 2003. Net interest income increased \$18, for the three months ended September 30, 2004, as compared to the same period in 2003.

At September 30, 2004, interest income on loans increased \$190 compared to September 30, 2003. Nonaccrual income was \$109 for the three months ended September 30, 2004, as compared to \$93 for the same period in 2003. Interest expense increased \$172 for the three months ended September 30, 2004, as compared to the comparable period of 2003.

Noninterest income for the three months ended September 30, 2004, totaled \$2,574, as compared to \$2,608 for the same period of 2003, a decrease of \$34. This decline in earnings is attributed to a decrease of \$410 in loans fees when compared to the same period in 2003. This decline was offset by an increase of \$97 in fees for financially related services, \$46 in earnings of AgFirst Farm Credit Bank, \$149 in gains on other property owned and \$84 in other noninterest income when compared to the same period in 2003.

Noninterest expense for the three months ended September 30, 2004, decreased \$350 compared to the same period of 2003. This fall in noninterest expense is attributed to a decrease of \$19 in salaries and employee benefits and \$412 in the insurance fund premium when compared to the same period in 2003. These decreases were offset by an increase of \$51 in occupancy and equipment and \$30 in other operating expenses for the same period of 2003.

The Association recorded a benefit for income taxes of \$202 for the three months ended September 30, 2004 as compared to a provision of \$56 for the same period of 2003.

For the nine months ended September 30, 2004

Net income for the nine months ended September 30, 2004, totaled \$14,624, as compared to \$15,053 for the same period in 2003. This decrease of \$429, or 2.85 percent, is attributed to changes in noninterest income. At September 30, 2004, interest income on accruing loans decreased \$1377 compared to September 30, 2003. Nonaccrual income was \$350 for the nine months ended September 30, 2004, as compared to \$269 for the same period in 2003. Interest expense decreased \$1,435 for the nine months ended September 30, 2004, as compared to the same period in 2003. This change was primarily due to a decrease in our average cost of debt.

Noninterest income for the nine months ended September 30, 2004, totaled \$7,273, as compared to \$8,612 for the same period of 2003, a decrease of \$1,339. The fall in earnings is attributed to a decrease of \$1,522 in loan fees and \$127 in other noninterest income when compared to the same period in 2003. These declines were offset by an increase of \$13 in fees for financially related services, \$174 in earnings of AgFirst Farm Credit Bank and \$123 in the gain on other property owned when compared to the same period in 2003.

Noninterest expense for the nine months ended September 30, 2004, decreased \$101 compared to the same period of 2003. The fall in noninterest expense is attributed to a decrease of \$491 in the insurance fund premium when compared to the same period in 2003. This decrease was offset by an increase of \$39 in salaries and employee benefits, \$164 in occupancy and equipment and \$187 in other operating expenses for the same period of 2003.

The Association recorded a benefit for income taxes of \$193 for the nine months ended September 30, 2004 as compared to a provision of \$58 for the same period of 2003.

FUNDING SOURCES

The principal source of funds for the Association is the borrowing relationship established with AgFirst Farm Credit Bank (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 September 30, 2004, was \$992,487 as compared to \$904,991 at December 31, 2003. The increase during the period is attributable to new borrowing by the Association for funds advanced to its borrowers.

The Association has no lines of credit outstanding with third parties as of September 30, 2004.

CAPITAL RESOURCES

Total members' equity at September 30, 2004, increased to \$148,442 from the December 31, 2003, total of \$146,286. The change in capital is attributed to net earnings for the nine months ending September 30, 2004 being in excess of the revolvment of the 1998 qualified allocated surplus, the 1993 non-qualified surplus in September of 2004 and the reduction in capital stock and participation certificates.

Total capital stock and participation certificates were \$9,804 on September 30, 2004, compared to \$9,905 on December 31, 2003. This decrease is attributable to the retirement of protected and at-risk stock and participation certificates on loans liquidated in the normal course of business and new loans being capitalized at new lower regulatory levels.

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 September 30, 2004, the Association's total surplus ratio and core surplus ratio were 14.01 percent and 10.69 percent, respectively, and the permanent capital ratio was 14.88 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.

Carolina Farm Credit, ACA
Consolidated Balance Sheets

<i>(dollars in thousands)</i>	September 30, 2004	December 31, 2003
	<i>(unaudited)</i>	
Assets		
Cash	\$ 1,653	\$ 1,353
Loans	1,070,909	1,052,859
Less: allowance for loan losses	21,333	21,948
Net loans	1,049,576	1,030,911
Accrued interest receivable	14,149	10,109
Investment in other Farm Credit institutions	14,184	14,191
Premises and equipment, net	8,873	8,778
Other property owned	1,549	369
Deferred tax asset, net	1,661	1,661
Other assets	14,024	13,172
Total assets	\$ 1,105,669	\$ 1,080,544
Liabilities		
Notes payable to AgFirst Farm Credit Bank	\$ 922,487	\$ 904,991
Accrued interest payable	3,244	3,144
Patronage refund payable	661	4,681
Postretirement benefits other than pensions	8,482	7,475
Minimum pension liability	—	5,708
Other liabilities	22,353	8,259
Total liabilities	957,227	934,258
Commitments and contingencies		
Members' Equity		
Protected borrower equity	1,015	1,288
Capital stock and participation certificates	8,789	8,617
Retained earnings		
Allocated	74,806	86,999
Unallocated	75,033	60,583
Accumulated other comprehensive income (loss)	(11,201)	(11,201)
Total members' equity	148,442	146,286
Total liabilities and members' equity	\$ 1,105,669	\$ 1,080,544

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

Carolina Farm Credit, ACA
Consolidated Statements of Income

(unaudited)

<i>(dollars in thousands)</i>	For the three months ended September 30,		For the nine months ended September 30,	
	2004	2003	2004	2003
Interest Income				
Loans	\$ 17,406	\$ 17,216	\$ 51,072	\$ 52,449
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	9,719	9,547	28,411	29,846
Net interest income	7,687	7,669	22,661	22,603
Provision for (reversal of) loan losses	—	—	—	500
Net interest income after provision for (reversal of) loan losses	7,687	7,669	22,661	22,103
Noninterest Income				
Loan fees	476	886	1,484	3,006
Fees for financially related services	235	138	446	433
Equity in earnings of other Farm Credit institutions	1,764	1,718	5,216	5,042
Gains (losses) on other property owned, net	17	(132)	—	(123)
Other noninterest income	82	(2)	127	254
Total noninterest income	2,574	2,608	7,273	8,612
Noninterest Expense				
Salaries and employee benefits	3,577	3,596	10,766	10,727
Occupancy and equipment	463	412	1,305	1,141
Insurance Fund premium	(118)	294	386	877
Other operating expenses	1,022	992	3,046	2,859
Total noninterest expense	4,944	5,294	15,503	15,604
Income before income taxes	5,317	4,983	14,431	15,111
Provision (benefit) for income taxes	(202)	56	(193)	58
Net income	\$ 5,519	\$ 4,927	\$ 14,624	\$ 15,053

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

Carolina Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)

	Protected Borrower Capital	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income	Total Members' Equity
			Allocated	Unallocated		
Balance at December 31, 2002	\$ 1,739	\$ 8,814	\$ 81,979	\$ 63,669	\$ (12,107)	\$ 144,094
Net income				15,053		15,053
Protected borrower equity retired	(420)					(420)
Capital stock/participation certificates issued		719				719
Capital stock/participation certificates retired		(552)				(552)
Retained earnings retired			(14,185)			(14,185)
Distribution adjustment			2,482	(2,672)		(190)
Balance at September 30, 2003	\$ 1,319	\$ 8,981	\$ 70,276	\$ 76,050	\$ (12,107)	\$ 144,519
Balance at December 31, 2003	\$ 1,288	\$ 8,617	\$ 86,999	\$ 60,583	\$ (11,201)	\$ 146,286
Net income				14,624		14,624
Protected borrower equity retired	(273)					(273)
Capital stock/participation certificates issued		649				649
Capital stock/participation certificates retired		(477)				(477)
Retained earnings retired			(12,310)			(12,310)
Distribution adjustment			117	(174)		(57)
Balance at September 30, 2004	\$ 1,015	\$ 8,789	\$ 74,806	\$ 75,033	\$ (11,201)	\$ 148,442

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

Notes to the Consolidated Financial Statements

(dollars in thousands, except as noted)
(unaudited)

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

A description of the organization and operations of Carolina Farm Credit, ACA (the Association), the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2003, are contained in the 2003 Annual Report to Stockholders. These unaudited third quarter 2004 consolidated financial statements should be read in conjunction with the 2003 Annual Report to Stockholders.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles. The results for the nine months ended September 30, 2004, are not necessarily indicative of the results to be expected for the year ending December 31, 2004.

Certain amounts in prior period consolidated financial statements have been reclassified to conform to current consolidated financial statement presentation. Such reclassifications had no effect on the prior period net income or total capital as previously reported.

The Association maintains an allowance for loan losses in accordance with generally accepted accounting principles. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of September 30, 2004, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

NOTE 2 – ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses follows:

Balance at 12-31-02	\$ 21,571
(Reversal of) provision for loan losses	500
Loans (charged off), net of recoveries	<u>(93)</u>
Balance at 9-30-03	<u>\$ 21,978</u>
Balance at 12-31-03	\$ 21,948
(Reversal of) provision for loan losses	–
Loans (charged off), net of recoveries	<u>(615)</u>
Balance at 9-30-04	<u>\$ 21,333</u>

NOTE 3 – EMPLOYEE BENEFIT PLANS

The Association participates in a Districtwide defined benefit retirement plan. The costs of the plan are not segregated by participating entities but are allocated among the participating entities. Pension costs are allocated by multiplying the District's net pension expense times each institution's salary expense as a percentage of the District's salary expense. The Association also participates in Districtwide Thrift and other postretirement benefit plans.

The following is a table of retirement and postretirement benefit expense for the nine months ended September 30, 2004:

	For the nine months ended September 30,	
	<u>2004</u>	<u>2003</u>
Pension	\$ 1,474	\$ 1,545
Thrift/deferred compensation	210	212
Other postretirement benefits	<u>1,470</u>	<u>1,395</u>
Total	<u>\$ 3,154</u>	<u>\$ 3,152</u>

As of September 30, 2004, the Association had contributed \$10,373 to the Districtwide defined benefit retirement plan, which was sufficient to meet its accumulated benefit obligation. The contributions eliminated the minimum pension liability with \$3,191 of the contributions being classified as prepaid retirement expense in Other Assets on the Consolidated Balance Sheets. The Association does not anticipate making additional contributions for the remainder of 2004.