

THIRD QUARTER 2005

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J. Robert Frazee
Chief Executive Officer



Robert N. Stabler
Chairman of the Board

October 28, 2005

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 MidAtlantic Farm Credit, ACA (Association) for the period ended September 30, 2005. These comments contained in this report should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2004 Annual Report of the Association.

LOAN PORTFOLIO

The Association provides funds to farmers, rural homeowners and farm-related businesses for the financing of short and intermediate-term loans and long-term real estate mortgage loans. The Association's loan portfolio covers a well diversified range of agricultural commodities, with cash grains, poultry and dairy representing the largest segments. In addition, the Association provides a significant amount of loans to lessors of agricultural real estate. Farm size varies and many of the borrowers in the region have diversified farming operations. This factor, along with the opportunities for non-farm income, impacts the level of dependency on any particular commodity.

Gross loans at September 30, 2005 totaled \$1,648,114 compared to \$1,537,010 at December 31, 2004, increasing \$111,104 or 7.2 percent during the first nine months. The Association's allowance for loan losses of \$10,421 decreased \$42 during the first nine months of 2005 resulting in net loans (gross loans less allowance for loan losses) of \$1,637,693 and \$1,526,547 at September 30, 2005 and December 31, 2004, respectively.

There is an inherent risk in the extension of any type of credit and, accordingly, the Association maintains an allowance for loan losses consistent with the risk measured in the portfolio. Credit administration remains satisfactory and the credit quality of the Association's loan portfolio has continued to improve.

Consequently, no provision for loan losses was recorded in the first nine months of 2005 that would increase the Association's allowance. The allowance for loan losses represented 0.63 percent and 0.68 percent of total loans at September 30, 2005 and December 31, 2004, respectively.

RESULTS OF OPERATIONS

For the three months ended September 30, 2005

Net income for the three months ended September 30, 2005 totaled \$9,181, an increase of \$443 compared to the three months ended September 30, 2004. Major changes in the components of net income are identified as follows:

- Net interest income increased \$1,397 for the quarter ended September 30, 2005 compared to the same period in 2004. Earnings on the Association's loanable funds credit (investable funds) increased \$896 over last year due to management's strategy of investing these funds in higher yielding notes on a portion of the funds and the increase in short-term interest rates, which favorably impacts the earnings on the variable rate investments. The remaining increase in net interest income is attributable to a \$211 increase in interest income from nonaccrual loans and to incremental earnings on an increasing loan portfolio.
- The risks identified in the Association's loan portfolio did not warrant a provision for loan losses to be recorded in either the third quarter of 2005 or 2004.
- At September 30, 2005 and 2004, the Association accrued an estimated patronage distribution of \$2,618 and \$2,436, respectively, which is based on third quarter operations only; management anticipates additional income for the fourth quarter. Since this income from AgFirst Farm Credit Bank (the Bank) is reasonably estimable

and because there is a history of these earnings, management is of the opinion that including this income in quarterly operations provides shareholders with a more accurate forecast of annualized net income.

- Noninterest Expense was \$5,089 in both the three months ended September 30, 2005 and 2004. The \$673 decrease in salaries and employee benefits for the third quarter of 2005 as compared to the same period in 2004 results primarily from the fact that an accrual for incentive based compensation in 2005 was made in the second quarter therefore reducing the amount of the accrual made in the third quarter of 2005. In 2004, no accrual was made for this same program until the third quarter. In addition, the deferral of salaries and benefits in accordance with Statement of Financial Accounting Standards No. 91 "Accounting for Non-refundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Cost of Leases," increased \$78 on a comparable quarter basis.

The FCA Insurance Corporation announced a 50 percent rate increase for the second half of 2005 as compared to rates effective for the first half of 2005. The opposite scenario occurred in the third quarter of 2004, when rates were reduced retroactive to the beginning of the year. The other variances during the quarter were principally timing related as evidenced by the following review of the nine months ended September 30, 2005 and 2004.

For the nine months ended September 30, 2005

Net income for the nine months ended September 30, 2005 totaled \$27,103 (8.8 percent) or \$2,193 more than the nine months ended September 30, 2004. Year-to-date operations for the Association simulated third quarter operations. Major changes in the components of net income are identified as follows:

- The increase in net interest income of \$4,094 is attributable to: a \$2,408 increase in Association's earnings on the loanable funds credit (investable funds) due to management's strategy of investing in higher yielding notes on a portion of the funds and the increase in short-term interest rates which favorably impacts the earnings on the variable rate investments; a \$912 increase in interest income from nonaccrual loans; and, net interest income from the increased loan portfolio.

- At the period ended September 30, 2005, the Association has accrued an estimated patronage distribution of \$7,537 as compared to \$7,165 at September 30, 2004. This accrual is based on the first nine months of the year's operations, and management anticipates additional income for the fourth quarter. Since the patronage income from the Bank is reasonably estimable and because there is a history of these earnings, management is of the opinion that including this income in quarterly operations provides shareholders with a more accurate forecast of annualized net income.
- Additional other income has been earned by the Association related to the sale of office buildings. These sales in both years were a result of management's study to determine the best site for all physical locations. There remains one former branch location to be sold this year. Proceeds from Association's property sales in both years have been redeployed in updating and modernizing Association office facilities.
- Noninterest expense increased \$232 or 1.6 percent for the first nine months of 2005 as compared to 2004, which demonstrates the Association's continued effective expense management.

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 Bank advances the funds to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sectors. The Association utilizes the variable rate note 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, 2005 were \$1,386,192 compared to \$1,286,589 at December 31, 2004. This increase during the period of \$100 million or 7.7 percent corresponds directly to the increase in the Association's loan volume offset by net cash generated from operations.

CAPITAL RESOURCES

Members' equity at September 30, 2005 totaled \$281,373 an increase of \$20,933 (8.0 percent) compared to total members' equity of \$260,440 at December 31, 2004. Net income of \$27,103 for the nine months ending September 30, 2005, net member stock issues of \$198 and net adjustments to retained earnings of \$11, offset by an estimated cash patronage distribution for the first nine months of 2005 totaling \$6,379 account for the change.

FCA regulations require all Farm Credit institutions to maintain a minimum permanent capital ratio of 7.0 percent and total surplus and core surplus ratios equal to 3.5 percent. 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, 2005, the Association's permanent capital, total surplus and core surplus ratios equaled 15.73 percent, 15.18 percent and 13.14 percent, respectively.

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 Jay Wise, 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. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-333-7950, or writing John E. Wheeler, Jr., Chief Financial Officer, MidAtlantic Farm Credit, ACA, P.O. Box 770, Westminster, MD 21158-0770, or accessing the website, www.mafc.com. The Association prepares a quarterly report within 45 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.

MidAtlantic Farm Credit, ACA

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 MidAtlantic 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, 2004, are contained in the 2004 Annual Report to Shareholders. These unaudited third quarter 2005 consolidated financial statements should be read in conjunction with the 2004 Annual Report to Shareholders.

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, 2005, are not necessarily indicative of the results to be expected for the year ending December 31, 2005.

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, 2005, 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 12-31-03	\$ 30,383
(Reversal of) provision for loan losses	—
Recoveries, net of loans charged off	<u>40</u>
Balance at 9-30-04	<u>\$ 30,423</u>
Balance at 12-31-04	\$ 10,463
(Reversal of) provision for loan losses	—
Loans (charged off), net of recoveries	<u>(42)</u>
Balance at 9-30-05	<u>\$ 10,421</u>

As discussed in the 2004 Annual Report, the Association recorded a loan loss reversal of \$20,054 in the fourth quarter of 2004 that resulted in a decrease in the allowance for loan losses.

NOTE 3 – COMMITMENTS AND CONTINGENT LIABILITIES

Actions are pending against the Association in which money damages are sought. However, on the basis of information now at hand, management and legal counsel are of the opinion that the ultimate liability, if any, resulting therefrom, would not be material in relation to the overall financial position of the Association.

NOTE 4 – 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, 2005:

	For the nine months ended September 30,	
	2005	2004
Pension	\$ 1,161	\$ 1,383
Thrift/deferred compensation	216	228
Other postretirement benefits	<u>681</u>	<u>895</u>
Total	<u>\$ 2,058</u>	<u>\$ 2,506</u>

The Association had not previously anticipated making a contribution in 2005 to the defined benefit retirement plan based upon actuarial projections as of the last plan measurement date (September 30, 2004). However, due to market conditions affecting discount rates and return on plan assets, current actuarial projections indicated that a contribution was needed to meet the expected accumulated benefit obligation at September 30, 2005. During the third quarter of 2005, the Association contributed \$2,243 to the defined benefit retirement plan. The Association does not anticipate making additional contributions for the remainder of 2005.

The Association also sponsors supplemental retirement and deferred compensation plans for certain key employees. The expenses of these plans are included in the pension and deferred compensation costs above. The Association contributed \$9 to these plans during the first nine months of 2005. The Association anticipates making additional contributions of \$3 to these supplemental retirement and deferred compensation plans during the remainder of 2005.