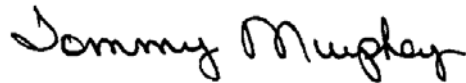
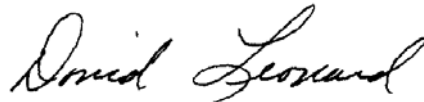


# **FIRST QUARTER 2006**

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Tommy Murphey  
Chief Executive Officer



David Leonard  
Chairman of the Board

April 28, 2006

# 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 Jackson Purchase Agricultural Credit Association (Association) for the period ended March 31, 2006. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2005 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 including corn, soybeans, poultry, and tobacco. 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 any single commodity.

The gross loan volume of the Association as of March 31, 2006, was \$227,666, a decrease of \$13,225, as compared to \$240,891 at December 31, 2005. Net loans outstanding at March 31, 2006, were \$226,509 as compared to \$239,741 at December 31, 2005. Net loans accounted for 92.37 percent of total assets at March 31, 2006, as compared to 93.25 percent of total assets at December 31, 2005. The decrease in gross and net loan volume during the reporting period is primarily attributable to seasonal paydown on production 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 decreased from \$825 at December 31, 2005, to \$709 at March 31, 2006. This decrease is primarily the result of normal collection procedures.

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 March 31, 2006, was \$1,157 compared to \$1,150 at December 31, 2005, and was considered by management to be adequate to cover probable losses.

## **RESULTS OF OPERATIONS**

### ***For the three months ended March 31, 2006***

Net income for the three months ended March 31, 2006, totaled \$916, as compared to \$945 for the same period in 2005. Net interest income increased \$43 for the three months ended March 31, 2006, as compared to the same period in 2005. This increase in net interest income is attributed primarily to interest income on our own funds and from interest income generated through the Tobacco Buyout program and marketable investments.

Noninterest income for the three months ended March 31, 2006, totaled \$535, as compared to \$425 for the same period of 2005, an increase of \$110. The increase is primarily the result of increased fee income from financially related services and loan fees, and also from an increase in equity in earnings of other Farm Credit institutions. Noninterest expense for the three months ended March 31, 2006, increased \$179 compared to the same period of 2005. The primary reasons for the increase in noninterest expense were an increase in the insurance fund premium and an increase in salaries and benefits.

Nonaccrual income was \$11 for the three months ended March 31, 2006, as compared to \$31 for the same period in 2005. The Association recorded a provision for loan loss of \$8 for the three months ended March 31, 2006, as compared to \$0 for the same period in 2005.

## **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 Bank advances funds 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 and approximately 75% of the Association's own funds. The total notes payable to the Bank at March 31, 2006, was \$201,236 compared to \$213,177 at December 31, 2005.

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## CAPITAL RESOURCES

Total members' equity at March 31, 2006, increased to \$37,212 from the December 31, 2005, total of \$36,407. The increase is primarily attributed to income generated through the first quarter.

Total capital stock and participation certificates were \$2,796 on March 31, 2006, compared to \$2,796 on December 31, 2005.

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 March 31, 2006, the Association's total surplus ratio and core surplus ratio were 14.87 percent and 13.62 percent, respectively, and the permanent capital ratio was 15.78 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.

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**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](http://www.agfirst.com). Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling (270) 247-5613, writing Malinda Scoggins, Administrative Services Manager, Jackson Purchase ACA, P. O. Box 309, Mayfield, KY 42066, or accessing the website, [www.jacksonpurchaseaca.com](http://www.jacksonpurchaseaca.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.

*Jackson Purchase Agricultural Credit Association*  
**Consolidated Balance Sheets**

<i>(dollars in thousands)</i>	<b>March 31, 2006</b> <i>(unaudited)</i>	<b>December 31, 2005</b> <i>(audited)</i>
<b>Assets</b>		
Cash	\$ 2,340	\$ 4,287
Investment securities, held to maturity	4,959	—
Loans	227,666	240,891
Less: allowance for loan losses	1,157	1,150
Net loans	226,509	239,741
Other investments	1,860	1,571
Accrued interest receivable	3,810	4,114
Investment in other Farm Credit institutions	3,449	3,450
Premises and equipment, net	1,268	1,174
Prepaid retirement expense	356	410
Due from AgFirst Farm Credit Bank	—	2,070
Other assets	656	290
Total assets	<u>\$ 245,207</u>	<u>\$ 257,107</u>
<b>Liabilities</b>		
Notes payable to AgFirst Farm Credit Bank	\$ 201,236	\$ 213,177
Accrued interest payable	913	918
Patronage refund payable	21	1,700
Other liabilities	5,825	4,905
Total liabilities	<u>207,995</u>	<u>220,700</u>
Commitments and contingencies		
<b>Members' Equity</b>		
Capital stock and participation certificates	2,796	2,796
Retained earnings		
Allocated	11,117	11,226
Unallocated	23,299	22,385
Total members' equity	<u>37,212</u>	<u>36,407</u>
Total liabilities and members' equity	<u>\$ 245,207</u>	<u>\$ 257,107</u>

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

*Jackson Purchase Agricultural Association*  
**Consolidated Statements of Income**

*(unaudited)*

<i>(dollars in thousands)</i>	<b>For the three months ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
<b>Interest Income</b>		
Loans	\$ 4,047	\$ 3,174
Investment securities	31	—
Other	27	—
	4,105	3,174
Total Interest Income		
<b>Interest Expense</b>		
Notes payable to AgFirst Farm Credit Bank	2,639	1,774
Other	23	—
	2,662	1,774
Total interest expense		
Net interest income	1,443	1,400
Provision for (reversal of allowance for) loan losses	8	—
	1,435	1,400
Net interest income after provision for (reversal of allowance for) loan losses		
<b>Noninterest Income</b>		
Loan fees	97	38
Fees for financially related services	45	33
Equity in earnings of other Farm Credit institutions	370	323
Other noninterest income	23	31
	535	425
Total noninterest income		
<b>Noninterest Expense</b>		
Salaries and employee benefits	688	595
Occupancy and equipment	71	62
Insurance Fund premium	76	19
Other operating expenses	218	198
	1,053	874
Total noninterest expense		
Income before income taxes	917	951
Provision (benefit) for income taxes	1	6
	916	945
Net income	\$ 916	\$ 945

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

*Jackson Purchase Agricultural Credit Association*  
**Consolidated Statements of Changes in  
Members' Equity**

*(unaudited)*

*(dollars in thousands)*

	<b>Capital Stock and Participation Certificates</b>	<b>Retained Earnings</b>		<b>Total Members' Equity</b>
		<b>Allocated</b>	<b>Unallocated</b>	
Balance at December 31, 2004	\$ 2,763	\$ 9,444	\$ 21,852	\$ 34,059
Net income			945	945
Capital stock/participation certificates issued	63			63
Capital stock/participation certificates retired	(70)			(70)
Distribution adjustment		(99)	148	49
Balance at March 31, 2005	<u>\$ 2,756</u>	<u>\$ 9,345</u>	<u>\$ 22,945</u>	<u>\$ 35,046</u>
Balance at December 31, 2005	\$ 2,796	\$ 11,226	\$ 22,385	\$ 36,407
Net income			916	916
Capital stock/participation certificates issued	50			50
Capital stock/participation certificates retired	(50)			(50)
Distribution adjustment		(109)	(2)	(111)
Balance at March 31, 2006	<u>\$ 2,796</u>	<u>\$ 11,117</u>	<u>\$ 23,299</u>	<u>\$ 37,212</u>

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

Jackson Purchase Agricultural Credit Association

# 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 Jackson Purchase Agricultural Credit Association (the Association), the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2005, are contained in the 2005 Annual Report to Shareholders. These unaudited first quarter 2006 consolidated financial statements should be read in conjunction with the 2005 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 three months ended March 31, 2006, are not necessarily indicative of the results to be expected for the year ending December 31, 2006.

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 March 31, 2006, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

*Investment Securities:* The Association, as permitted under the FCA regulations, holds investments for purposes of maintaining a liquidity reserve, managing short-term surplus funds and managing interest rate risk. The Association's investments are classified as held to maturity and accordingly have been reported at amortized cost. Purchased premiums and discounts are amortized or accreted over a five year term of the respective security.

The Association reviews all investments that are in a loss position in order to determine whether the unrealized loss, which is considered an impairment, is temporary or permanent. In the event of permanent impairment, the cost basis of the investment would be written down to its fair value, and the realized loss would be included in current earnings.

## NOTE 2 – ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses follows:

Balance at 12-31-04	\$ 1,200
(Reversal of) provision for loan losses	–
Loans (charged off), net of recoveries	<u>(55)</u>
Balance at 3-31-05	<u>\$ 1,145</u>
Balance at 12-31-05	\$ 1,150
(Reversal of) provision for loan losses	8
Loans (charged off), net of recoveries	<u>(1)</u>
Balance at 3-31-06	<u>\$ 1,157</u>

## NOTE 3 – EMPLOYEE BENEFIT PLANS

The Association participates in a defined benefit retirement plan with three other District associations. Pension costs were determined by an actuary on a separate entity basis.

The following is a table of the components of net periodic benefit (income) cost for the defined benefit retirement plan for the three months ended March 31, 2006:

	<b>For the three months ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
Service cost	\$ 50	\$ 43
Interest cost	59	55
Expected return on plan assets	(79)	(72)
Amortization of prior service cost	12	9
Recognized net actuarial (gain) loss	12	10
Net periodic benefit (income) cost	<u>\$ 54</u>	<u>\$ 45</u>

As of March 31, 2006, no contributions have been made to the pension plan for 2006. Actuarial projections as of the last plan measurement date (September 30, 2005) did not anticipate any contributions for 2006; however, market conditions could impact discount rates and return on plan assets which could change this expectation, making contributions necessary before the next plan measurement date.

The Association also participates in Districtwide thrift and other postretirement benefit plans. The other postretirement benefit plan provides certain benefits (primarily health care) to its retirees.

The following is a table of retirement and postretirement benefit expense for the three months ended March 31, 2006:

	<b>For the three months ended March 31,</b>	
	<b>2006</b>	<b>2005</b>
Pension	\$ 54	\$ 45
Thrift/deferred compensation	26	27
Other postretirement benefits	(2)	(1)
Total	<u>\$ 78</u>	<u>\$ 71</u>