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**Second Quarter 2018  
Report to Shareholders**

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**Farm Credit West**

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## Management's Discussion and Analysis

The following commentary is a review of the consolidated financial condition and results of operations of Farm Credit West, ACA and its subsidiaries (Farm Credit West). These comments should be read in conjunction with the unaudited second quarter 2018 consolidated financial statements and related notes included in this report, as well as the 2017 Annual Report to Shareholders. Shareholders may obtain copies of the Quarterly or Annual Report to Shareholders free of charge by calling our corporate headquarters at 916-780-1166, by writing to Farm Credit West, 3755 Atherton Road, Rocklin, CA 95765, or by accessing our website at [www.farmcreditwest.com](http://www.farmcreditwest.com). The financial condition and results of operations of CoBank, ACB (CoBank), our funding bank, materially affect the risk associated with shareholder investments in Farm Credit West. Shareholders of Farm Credit West may obtain copies of CoBank's Quarterly or Annual Report to Shareholders free of charge by calling 916-780-1166, by writing to Farm Credit West, 3755 Atherton Road, CA, 95765, or by accessing CoBank's website at [www.cobank.com](http://www.cobank.com).

### Loan and Lease Volume

Loan and lease volume (net of sold loan and lease participations) was \$9.6 billion at June 30, 2018, a decrease of \$67.9 million since December 31, 2017. The decrease was primarily due to a \$107.0 million decrease in production and intermediate-term loan volume, partially offset by a \$30.4 million and a \$10.5 million increase in agribusiness and rural infrastructure loan volumes, respectively.

In addition to the \$9.6 billion of loan and lease volume reported on our balance sheet at June 30, 2018, we serviced loans and leases totaling \$2.7 billion for other institutions.

### Portfolio Quality

As shown in the following table, our loan quality statistics declined by 1% during the first six months of 2018 due to an increase in substandard loan volume.

	June 30, 2018	December 31, 2017	December 31, 2016
Nonadversely classified	94.9%	95.9%	96.3%
Adversely classified	5.1%	4.1%	3.7%

Uncertainty around global trade activity could have a negative impact on some industries we finance. The tree nut and dairy industries are very dependent on an export market and these issues can potentially cause some stress to these borrowers including the potential for the implementation by foreign trade partners of tariffs. It is uncertain whether \$12 billion in aid to support agricultural producers, announced in July 2018, will have a favorable impact on our borrowers.

Tree nuts, which include almonds, pistachios, walnuts and pecans, represent the largest commodity concentration in the Association's loan portfolio. The price of tree nuts remained generally stable in 2017, resulting in most customers remaining profitable. The borrowers in this segment of our loan portfolio are expected to remain profitable throughout 2018.

The Arizona and California dairy industry continues to face economic challenges as a result of global production coupled with existing high inventories of dairy products, other than butter, exceeding current demand. This down cycle is anticipated to continue into the remainder of 2018 and is a concern as many of our dairy customers are operating at or below breakeven levels.

After five years of drought in California, heavy precipitation, including record snowpack, during the 2016-2017 rain season resulted in the drought designation for California being lifted. Due to the rainfall and snowpack accumulation that occurred in early spring of the 2017-2018 rain season, reservoirs continue to be maintained at encouraging levels. An additional consideration surrounding California water availability is the unknown long term impacts of the Sustainable Groundwater Management Act of 2014 (SGMA). The required reduction in groundwater usage under SGMA is expected to impact land values, and in some cases may require fallowing acreage.

The State of California's election results to legalize the production of marijuana poses customer relationship challenges for us. The cultivation of marijuana for any purpose is a federal offense. As a federally chartered entity, it remains illegal for Farm Credit West to be associated with marijuana production in any form and therefore cannot loan to any customer that is involved directly or indirectly with marijuana production. Additionally, this creates uncertainty as to the value of greenhouses that could potentially be used for marijuana production.

### Nonearning Assets

Nonearning assets (nonaccrual loan volume plus other property owned) totaled \$146.2 million at June 30, 2018, an increase of \$28.8 million from December 31, 2017. The increase was primarily due to transfers into nonaccrual of \$39.1 million during the first six months, partially offset by year-to-date net repayments on nonaccrual loans that totaled \$9.6 million.

### Allowance for Loan Losses

Our allowance for loan losses totaled \$72.5 million (0.74% of loan principal and interest) at June 30, 2018, an increase of \$7.6 million since December 31, 2017. The increase is due in part to increasing loss exposure as a result of risk rating downgrades and collateral revaluations on certain loans that

## Management's Discussion and Analysis

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resulted in a higher risk profile. The allowance is our best estimate of the amount of probable losses existing in, and inherent in, our loan portfolio as of the balance sheet date. We determine the allowance based on a regular evaluation of the loan portfolio, which generally considers recent historic charge-off experience adjusted for relevant factors. At June 30, 2018, recoveries totaled \$0.3 million, as compared to net recoveries of \$0.1 million during the same period in 2017. Additionally, provision expense of \$7.3 million was recognized in the first six months of 2018 as compared to \$4.8 million for the same period in 2017.

### Credit Risk Management

To help manage and diversify credit risk, our credit risk management framework includes selling loan participation interests, limiting our "hold" positions to amounts below the legal lending limits, and prudently establishing lending limits at the borrower level based on asset quality. Additionally, we securitize loans and obtain credit guarantees. Our loan securitizations include the exchange of mortgage loans for Federal Agricultural Mortgage Corporation (Farmer Mac) guaranteed mortgage-backed securities, which are reported as investment securities on the accompanying consolidated balance sheet.

### Net Income

Net income for the six months ended June 30, 2018 was \$122.8 million with an annualized rate of return on average assets (ROA) of 2.40%. Net income for the first six months of 2017 was \$110.1 million with an ROA of 2.23%. Following are the key changes in net income for the same period year-over-year:

- ❖ Total noninterest income increased by \$8.6 million to \$40.6 million during the first six months of 2018 compared to the same period last year. The increase was primarily due to a distribution of \$6.1 million from the Farm Credit System Insurance Corporation (FCSIC) that represented our allocated portion of the excess amount in the System's Insurance Fund above the secure base amount. No such distribution was made in 2017.

Additionally, loan related fees and patronage from CoBank and other Farm Credit associations increased by \$0.8 million and \$1.4 million, respectively.

- ❖ Net interest income increased by \$7.0 million to \$133.6 million during the first six months of 2018 compared to the same period last year. The increase was mainly due to \$4.4 million and \$2.9 million in favorable interest rate and volume variances respectively, offset by \$0.2 million less of nonaccrual interest income recognized.

Offsetting the positive net income variances were:

- ❖ Provision for loan losses increased by \$2.5 million to \$7.3 million during the first six months of 2018 compared to the same period last year.
- ❖ Total noninterest expense increased by \$0.5 million to \$44.1 million during the first six months of 2018 compared to the same period in 2017. Increases in salaries and benefits of \$1.3 million, information and technology services of \$0.4 million and occupancy and equipment of \$0.4 million were partially offset by a \$2.1 million reduction in 2018 FCSIC premiums over the prior year period.

### Preferred Stock

Our preferred stock program is a means of adding value to the customer relationship. This program enables customers to provide us with capital needed to support our growth and the customer is paid an attractive dividend on their investment. While \$500.0 million is authorized for issuance, Farm Credit West maintains an internal issuance limit of \$425.0 million based on regulatory and capital management considerations. The preferred stock balance at June 30, 2018 was \$399.3 million, a decrease of \$0.3 million from December 31, 2017 due to normal redemptions. The per annum dividend rate during the second quarter of 2018 was 2.15%, an increase of 0.05% over the first quarter of 2018.

### Future Payment Funds

At June 30, 2018, the customer-owned future payment funds increased by \$36.6 million to \$464.5 million compared to \$427.9 million at December 31, 2017. The current economic cycle has enabled many of our customers to maintain high levels of liquid assets. Future payment funds represent voluntary advance conditional payments and are an interest-bearing funding source for the Association. The per annum dividend rate during the second quarter of 2018 was 1.50%, an increase of 0.10% over the first quarter of 2018.

### Capital Regulations

In 2016 the Farm Credit Administration (FCA), our regulator, adopted final rules (the Capital Regulations) relating to regulatory capital requirements for the Farm Credit System (System) banks and associations. The Capital Regulations took effect January 1, 2017.

The Capital Regulations, among other things, replaced core surplus and total surplus requirements with common equity tier 1 (CET1), tier 1 and total capital risk-based capital ratio requirements. The Capital Regulations also added a tier 1 leverage ratio for all System institutions, which replaced the net collateral ratio for System banks. In addition, the Capital Regulations established a capital conservation buffer and a leverage buffer; enhanced the sensitivity of risk weightings; and, for System banks only, required additional public disclosures.

## Management's Discussion and Analysis

The Capital Regulations set the following minimum risk-based requirements:

- ❖ A CET1 capital ratio of 4.5 percent;
- ❖ A tier 1 capital ratio (CET1 capital plus additional tier 1 capital) of 6 percent; and
- ❖ A total capital ratio (tier 1 plus tier 2) of 8 percent.

The Capital Regulations also set a minimum tier 1 leverage ratio (tier 1 capital divided by total assets) of 4 percent, of which at least 1.5 percent must consist of unallocated retained earnings (URE) and URE equivalents, which are nonqualified allocated equities with certain characteristics of URE.

The Capital Regulations established a capital cushion through a capital conservation buffer of 2.5 percent above the risk based CET1, tier 1 and total capital requirements. In addition, the Capital Regulations established a leverage capital cushion through a leverage buffer of 1 percent above the tier 1 leverage ratio requirement. If capital ratios fall below the regulatory minimum plus the buffer, capital distributions (dividend payments and cash patronage payments) and discretionary senior executive bonuses are restricted or prohibited without prior FCA approval. The Capital Regulations allowed a three-year phase-in of the capital conservation buffer beginning January 1, 2017. There is no phase-in of the leverage buffer.

### Amounts of Capital and Capital Adequacy

In the past six months, total members' equity increased \$118.3 million to \$2.2 billion primarily due to net income of \$122.8 million, partially offset by decreases of \$4.1 million in preferred stock dividends and \$0.3 million in preferred stock.

As shown in the following table, Farm Credit West has substantially exceeded each regulatory minimum capital requirement for all periods presented.

Type of capital as % of risk-weighted assets	<i>For the quarter ended</i>			Regulatory Minimum including Buffer
	<b>June 30, 2018</b>	Dec. 31, 2017	Dec. 31, 2016	
Common Equity Tier 1	<b>13.76%</b>	13.33%		7.00%
Tier 1	<b>13.76%</b>	13.33%		8.50%
Total regulatory capital	<b>14.41%</b>	13.95%		10.50%
Tier 1 leverage <sup>(1)</sup>	<b>14.97%</b>	14.37%		5.00%
Minimum URE leverage <sup>(1)</sup>	<b>16.72%</b>	15.99%		1.50%
Permanent capital <sup>(2)</sup>	<b>17.61%</b>	17.37%	17.55%	7.00%
Total surplus			13.49%	7.00%
Core surplus			13.49%	3.50%

(1) Ratio is a % of total assets.

(2) Beginning in 2017, the calculation for risk-weighted assets for permanent capital was adjusted to align with the new capital regulations, impacting the comparability to prior period percentages.

### Forward-Looking Information

This discussion contains forward looking statements. These statements are not guarantees of future performance as future operations involve certain risks, uncertainties, and assumptions that are difficult to predict. Words such as "anticipates," "believes," "could," "estimates," "may," "should," or "will" are intended to identify forward-looking statements. These statements are based on management's assumptions and analyses made in light of experience and other 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. Readers are cautioned not to place undue reliance on these forward-looking statements. We will not update any forward-looking statements to reflect events or circumstances arising after they are made.

## Management's Discussion and Analysis

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### Certification

The undersigned certify that this report has been prepared under the oversight of the Farm Credit West Audit Committee, that it is presented 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, and we have reviewed this report.



Joseph C. Airos  
Chairman of the Board of Directors



Mark D. Littlefield  
President and Chief Executive Officer



Jean L. Koenck  
Executive Vice President – Chief Financial Officer

August 6, 2018

Farm Credit West, ACA  
**Consolidated Balance Sheet**

<i>(in thousands)</i>	<b>June 30, 2018 (unaudited)</b>	December 31, 2017
<b>Assets</b>		
Loans and leases	\$ 9,631,480	\$ 9,699,371
Less: allowance for loan and lease losses	(72,500)	(64,900)
Net loans and leases	<u>9,558,980</u>	<u>9,634,471</u>
Cash	—	827
Accrued interest receivable	101,668	78,793
Investment securities — available-for-sale	61,556	70,648
Investment securities — held-to-maturity	17,720	20,890
Investment in CoBank	318,170	315,570
Other property owned	4,365	5,085
Premises and equipment, net	43,820	42,154
Accrued patronage receivable from CoBank	21,610	43,683
Other assets	47,650	55,250
<b>Total assets</b>	<u><u>\$ 10,175,539</u></u>	<u><u>\$ 10,267,371</u></u>
<b>Liabilities</b>		
Note payable to CoBank	\$ 7,443,422	\$ 7,598,740
Future payment funds	464,480	427,927
Accrued interest payable	11,816	11,182
Patronage distribution payable	—	82,700
Unfunded disbursements	3,456	—
Other liabilities	54,367	67,111
<b>Total liabilities</b>	<u><u>7,977,541</u></u>	<u><u>8,187,660</u></u>
<b>Members' Equity</b>		
Preferred stock	399,345	399,667
Capital stock and participation certificates	5,117	5,200
Unallocated retained earnings	1,664,431	1,545,742
Additional Paid-in-Capital	133,312	133,312
Accumulated other comprehensive loss	(4,207)	(4,210)
<b>Total members' equity</b>	<u><u>2,197,998</u></u>	<u><u>2,079,711</u></u>
<b>Total liabilities and members' equity</b>	<u><u>\$ 10,175,539</u></u>	<u><u>\$ 10,267,371</u></u>

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

Farm Credit West, ACA  
**Consolidated Statement of Comprehensive Income**

<i>(unaudited and in thousands)</i>	For the three months ended June 30		For the six months ended June 30	
	2018	2017	2018	2017
<b>Interest Income</b>				
Loans and leases	\$ 109,869	\$ 94,203	\$ 214,830	\$ 183,739
Investment securities	956	1,089	1,927	2,187
<b>Total interest income</b>	<b>110,825</b>	<b>95,292</b>	<b>216,757</b>	<b>185,926</b>
<b>Interest Expense</b>				
Note payable to CoBank	42,738	30,641	80,092	57,102
Future payment funds	1,555	1,179	3,068	2,209
<b>Total interest expense</b>	<b>44,293</b>	<b>31,820</b>	<b>83,160</b>	<b>59,311</b>
<b>Net interest income</b>	<b>66,532</b>	<b>63,472</b>	<b>133,597</b>	<b>126,615</b>
Provision for loan losses	(5,254)	(3,775)	(7,338)	(4,802)
<b>Net interest income after provision for loan losses</b>	<b>61,278</b>	<b>59,697</b>	<b>126,259</b>	<b>121,813</b>
<b>Noninterest Income</b>				
Patronage income	11,863	11,339	27,244	25,827
Farm Credit Insurance Fund distribution	—	—	6,115	—
Loan and other fees	2,428	2,095	4,973	4,214
Loan servicing income	310	408	649	837
Other noninterest income	986	607	1,646	1,100
<b>Total noninterest income</b>	<b>15,587</b>	<b>14,449</b>	<b>40,627</b>	<b>31,978</b>
<b>Noninterest Expense</b>				
Salaries and employee benefits	12,785	11,981	25,636	24,352
Information technology services	2,802	2,521	5,338	4,908
Occupancy and equipment	1,381	1,138	2,827	2,394
Farm Credit Insurance Fund premiums	1,556	2,638	3,162	5,301
FCA Supervisory and examination expense	613	574	1,227	1,148
Other operating expense	2,751	2,587	5,899	5,525
Gain on other property owned, net	(3)	(14)	—	(16)
<b>Total noninterest expense</b>	<b>21,885</b>	<b>21,425</b>	<b>44,089</b>	<b>43,612</b>
<b>Income before income taxes</b>	<b>54,980</b>	<b>52,721</b>	<b>122,797</b>	<b>110,179</b>
Benefit from (provision for) income taxes	57	30	4	(70)
<b>Net income</b>	<b>\$ 55,037</b>	<b>\$ 52,751</b>	<b>\$ 122,801</b>	<b>\$ 110,109</b>
<b>Other Comprehensive Income</b>				
Change in unrealized gain on investment securities - available-for-sale	(534)	(238)	(412)	(322)
Change in unrealized actuarial losses in Pension Restoration Plan	208	242	415	484
<b>Total comprehensive income</b>	<b>\$ 54,711</b>	<b>\$ 52,755</b>	<b>\$ 122,804</b>	<b>\$ 110,271</b>

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

Farm Credit West, ACA

**Consolidated Statement of Changes in Members' Equity**

<i>(unaudited and in thousands)</i>	Preferred Stock	Capital Stock and Participation Certificates	Unallocated Retained Earnings	Additional Paid-in Capital	Accumulated Other Comprehensive Income (loss)	Total Members' Equity
<b>Balance at December 31, 2016</b>	\$ 384,119	\$ 5,200	\$ 1,416,252	\$ 133,312	\$ (3,369)	\$ 1,935,514
Comprehensive income			110,109		162	110,271
Preferred stock issued	84,115					84,115
Preferred stock retired	(71,422)					(71,422)
Capital stock and participation certificates issued		166				166
Capital stock and participation certificates retired		(195)				(195)
Preferred stock dividends declared and paid	3,845		(3,845)			—
<b>Balance at June 30, 2017</b>	<u>\$ 400,657</u>	<u>\$ 5,171</u>	<u>\$ 1,522,516</u>	<u>\$ 133,312</u>	<u>\$ (3,207)</u>	<u>\$ 2,058,449</u>
<b>Balance at December 31, 2017</b>	<b>\$ 399,667</b>	<b>\$ 5,200</b>	<b>\$ 1,545,742</b>	<b>\$ 133,312</b>	<b>\$ (4,210)</b>	<b>\$ 2,079,711</b>
Comprehensive income			122,801		3	122,804
Preferred stock issued	101,018					101,018
Preferred stock retired	(105,452)					(105,452)
Capital stock and participation certificates issued		170				170
Capital stock and participation certificates retired		(253)				(253)
Preferred stock dividends declared and paid	4,112		(4,112)			—
<b>Balance at June 30, 2018</b>	<u>\$ 399,345</u>	<u>\$ 5,117</u>	<u>\$ 1,664,431</u>	<u>\$ 133,312</u>	<u>\$ (4,207)</u>	<u>\$ 2,197,998</u>

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

## Notes to Consolidated Financial Statements

### Note 1 – Organization and Operations

A description of the organization and operations of Farm Credit West, ACA and its subsidiaries (Farm Credit West), significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2017, are contained in the 2017 Farm Credit West Annual Report to Shareholders. These unaudited second quarter 2018 financial statements should be read in conjunction with the 2017 Annual Report to Shareholders.

The accompanying financial statements contain all adjustments necessary for a fair presentation of the Association's interim financial condition and results of operations. Farm Credit West's accounting and reporting policies conform to accounting principles generally accepted in the United States of America (GAAP) and prevailing practices within the banking industry.

In February 2018, the Financial Accounting Standards Board (FASB) issued guidance entitled "Income Statement — Reporting Comprehensive Income — Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." This guidance allows for the reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the recently issued tax legislation, Tax Cuts and Jobs Act (TCJA) that lowered the federal corporate tax rate from 35% to 21%. The amount of the reclassification shall include the effect of the change in the tax rate on gross deferred tax amounts and related valuation allowances at the date of enactment of the TCJA related to items remaining in accumulated other comprehensive income. The guidance becomes effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Association has early adopted this standard with no impact to its financial condition and results of operations.

In March 2017, the FASB issued guidance entitled "Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Cost." The guidance requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. Other components are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. This guidance became effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition nor the results of operations as it did not have a material impact on the classification of items.

In August 2016, the FASB issued guidance entitled "Classification of Certain Cash Receipts and Cash Payments." The guidance addresses specific cash flow issues

with the objective of reducing the diversity in the classification of these cash flows. Included in the cash flow issues are debt prepayment or debt extinguishment costs and settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing. This guidance became effective for interim and annual periods beginning after December 15, 2017. The adoption of this guidance did not impact the Association's financial condition or its results of operations.

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 determine credit loss estimates. Credit losses relating to available-for-sale securities would also be recorded through an allowance for credit losses. For public business entities that are not U.S. Securities and Exchange Commission filers, this guidance becomes effective for interim and annual periods beginning after December 15, 2020, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In February 2016, the FASB issued guidance entitled "Leases." The guidance requires the recognition by lessees of lease assets and lease liabilities on the balance sheet for the rights and obligations created by those leases. Leases with lease terms of more than 12 months are impacted by this guidance. This guidance becomes effective for interim and annual periods beginning after December 15, 2018, with early application permitted. The Association is evaluating the impact of adoption on its financial condition and results of operations.

In January 2016, the FASB issued guidance entitled "Recognition and Measurement of Financial Assets and Liabilities." The guidance affects, among other things, the presentation and disclosure requirements for financial instruments. For public entities, the guidance eliminates the requirement to disclose the methods and significant assumptions used to estimate the fair value of financial instruments carried at amortized cost. This guidance became effective for interim and annual periods beginning after December 15, 2017. The Association early adopted this guidance in 2015 and the adoption of this guidance did not impact the Association's financial condition or its results of operations but did impact the fair value disclosures.

In May 2014, the FASB issued guidance entitled, "Revenue from Contracts with Customers." The guidance governs revenue recognition from contracts with customers and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services, and sets

## Notes to Consolidated Financial Statements

forth the requirement for new and enhanced disclosures. Financial instruments and other contractual rights within the scope of other guidance issued by the FASB are excluded from the scope of this new revenue recognition guidance. The Association adopted the new standard effective January 1, 2018, using the modified retrospective approach. As the majority of the Association's revenues are not subject to the new guidance, the adoption did not have a material impact on the financial position, results of operations, equity or cash flows.

### Note 2 – Loans and Allowance for Loan Losses

A summary of loan principal outstanding follows.

<i>(in thousands)</i>	June 30, 2018	December 31, 2017
Real estate mortgage loans	\$ 5,872,836	\$ 5,865,394
Production and intermediate-term loans	1,737,862	1,844,903
Agribusiness loans	1,533,216	1,502,847
Direct financing leases	204,033	213,238
Rural infrastructure loans	283,436	272,890
Rural residential loans	97	99
Total loans	<u>\$ 9,631,480</u>	<u>\$ 9,699,371</u>

At June 30, 2018 Farm Credit West had \$3.0 billion in unused commitments to extend credit and \$33.6 million in stand by letters of credit.

An analysis of changes in the allowance for loan losses is shown in the table below.

<i>For the six months ended June 30, (in thousands)</i>	2018	2017
Balance at beginning of year	\$ 64,900	\$ 55,600
Provision for loan losses	7,338	4,802
Charge-offs	—	(14)
Recoveries	262	112
Balance at June 30,	<u>\$ 72,500</u>	<u>\$ 60,500</u>

The following table summarizes the allowance for loan losses as collectively or individually evaluated for impairment.

<i>(in thousands)</i>	June 30, 2018	December 31, 2017
Individually evaluated for impairment	\$ 23,634	\$ 19,174
Collectively evaluated for impairment	48,866	45,726
Total allowance	<u>\$ 72,500</u>	<u>\$ 64,900</u>

Farm Credit West purchases and sells loan participations with other parties in order to diversify risk and manage loan volume. The following tables present information regarding participations purchased and sold. Participations purchased volume includes loan syndications where Farm Credit West is a lending member.

<i>June 30, 2018 (in thousands)</i>	Participations Purchased		
	Farm Credit Institutions	Non-Farm Credit Institutions	Total
Real estate mortgage	\$ 468,177	\$ 2,307	\$ 470,484
Agribusiness	717,074	85,275	802,349
Rural infrastructure loans	283,436	—	283,436
Total participations purchased	<u>\$ 1,468,687</u>	<u>\$ 87,582</u>	<u>\$ 1,556,269</u>

<i>June 30, 2018 (in thousands)</i>	Participations Sold		
	Farm Credit Institutions	Non-Farm Credit Institutions	Total
Real estate mortgage	\$ 1,524,998	\$ 2,098	\$ 1,527,096
Production and intermediate-term	456,371	—	456,371
Agribusiness	213,379	—	213,379
Direct financing leases	199,900	—	199,900
Total participations sold	<u>\$ 2,394,648</u>	<u>\$ 2,098</u>	<u>\$ 2,396,746</u>

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms. They include nonaccrual loans, accruing restructured loans and loans past due 90 days or more and still accruing interest.

The following table presents allowance information concerning impaired loans.

<i>(in thousands)</i>	June 30, 2018	December 31, 2017
Impaired loans with related allowance	\$ 46,368	\$ 33,729
Impaired loans with no related allowance	104,080	82,193
Total impaired loans	<u>\$ 150,448</u>	<u>\$ 115,922</u>
Allowance on impaired loans	<u>\$ 23,634</u>	<u>\$ 19,174</u>

## Notes to Consolidated Financial Statements

The following table presents average impaired loans and interest income recognized on impaired loans.

<i>For the six months ended June 30, (in thousands)</i>	<b>2018</b>	2017
Average impaired loans	<b>\$ 117,062</b>	\$ 147,107
Interest income recognized on impaired loans	<b>\$ 856</b>	\$ 1,344

Nonperforming assets (including related accrued interest) and related credit quality statistics are as follows:

<i>(in thousands)</i>	<b>June 30, 2018</b>	December 31, 2017
Nonaccrual loans	<b>\$ 141,806</b>	\$ 112,284
Accrual restructured	<b>6,516</b>	—
Accrual loans 90 days or more past due	<b>2,126</b>	3,638
Total impaired loans	<b>150,448</b>	115,922
Other property owned	<b>4,365</b>	5,085
Total impaired assets	<b>\$ 154,813</b>	\$ 121,007

A restructuring of a loan constitutes a troubled debt restructuring (TDR) if, for economic or legal reasons related to the debtor's financial difficulties, the Association grants a concession to the debtor that it would not otherwise consider. During the first six months of 2018, three loan restructurings were deemed a TDR. The pre and post modification outstanding recorded investment on these production and intermediate term TDR's was \$6.1 million at the time of restructure.

There were no TDRs that occurred within the previous 12 months respectively, for which there was a subsequent payment default during the six months ended June 30, 2018 or at December 31, 2017.

TDRs outstanding totaled \$11.1 million at June 30, 2018, \$4.6 million of which were in nonaccrual status. At December 31, 2017, TDR's outstanding totaled \$4.5 million, all of which were in nonaccrual status.

Additional commitments to lend to borrowers whose loans have been modified in a TDR were \$1.2 million at June 30, 2018 and \$0.5 million at December 31, 2017.

The following tables provide an age analysis of past due loans including interest.

<i>Principal and interest June 30, 2018 (in thousands)</i>	Not Past Due or Less Than 30 Days Past Due	Total Past Due	Total Loans
Real estate mortgage	<b>\$5,896,715</b>	\$ 52,355	<b>\$5,949,070</b>
Production and intermediate-term	<b>1,710,538</b>	41,524	<b>1,752,062</b>
Agribusiness	<b>1,534,339</b>	8,355	<b>1,542,694</b>
Direct financing leases	<b>201,817</b>	2,217	<b>204,034</b>
Rural infrastructure loans	<b>283,976</b>	—	<b>283,976</b>
Rural residential real loans	<b>97</b>	—	<b>97</b>
Total loans	<b>\$9,627,482</b>	<b>\$ 104,451</b>	<b>\$9,731,933</b>

<i>Principal and interest June 30, 2018 (in thousands)</i>	30-89 Days Past Due	90 Days or More Past Due	Total Past Due
Real estate mortgage	<b>\$ 8,339</b>	\$ 44,016	<b>\$ 52,355</b>
Production and intermediate-term	<b>11,651</b>	29,873	<b>41,524</b>
Agribusiness	<b>275</b>	8,080	<b>8,355</b>
Direct financing leases	<b>—</b>	2,217	<b>2,217</b>
Total loans	<b>\$ 20,265</b>	<b>\$ 84,186</b>	<b>\$ 104,451</b>

<i>Principal and interest December 31, 2017 (in thousands)</i>	Not Past Due or Less Than 30 Days Past Due	Total Past Due	Total Loans
Real estate mortgage	\$5,885,032	\$ 35,863	\$5,920,895
Production and intermediate-term	1,834,590	23,688	1,858,278
Agribusiness	1,500,464	9,668	1,510,132
Direct financing leases	212,561	677	213,238
Rural infrastructure loans	273,442	—	273,442
Rural residential loans	99	—	99
Total loans	<b>\$9,706,188</b>	<b>\$ 69,896</b>	<b>\$9,776,084</b>

<i>Principal and interest December 31, 2017 (in thousands)</i>	30-89 Days Past Due	90 Days or More Past Due	Total Past Due
Real estate mortgage	\$ 5,777	\$ 30,086	\$ 35,863
Production and intermediate-term	5,277	18,411	23,688
Agribusiness	—	9,668	9,668
Direct financing leases	662	15	677
Total loans	<b>\$ 11,716</b>	<b>\$ 58,180</b>	<b>\$ 69,896</b>

## Notes to Consolidated Financial Statements

### Note 3 – Investment Securities

The following is a summary of Farmer Mac agricultural mortgage-backed securities held by Farm Credit West.

<i>(dollars in thousands)</i>	Mortgage-Backed Securities — Available-for-Sale				Weighted Average Yield
	Amortized Cost	Gross Gains	Unrealized Losses	Fair Value	
<b>June 30, 2018</b>	<b>\$ 61,155</b>	<b>\$ 401</b>	<b>\$ —</b>	<b>\$ 61,556</b>	<b>4.79%</b>
December 31, 2017	69,835	813	—	70,648	4.52%

<i>(dollars in thousands)</i>	Mortgage-Backed Securities — Held-to-Maturity				Weighted Average Yield
	Amortized Cost	Gross Gains	Unrealized Losses	Fair Value	
<b>June 30, 2018</b>	<b>\$ 17,720</b>	<b>\$ 178</b>	<b>\$ —</b>	<b>\$ 17,898</b>	<b>4.66%</b>
December 31, 2017	20,890	292	—	21,182	4.33%

Substantially all mortgage-backed securities have contractual maturities in excess of ten years. However, expected and actual maturities for mortgage-backed securities will typically be shorter than contractual maturity due to scheduled and unscheduled payment activity affecting the loans underlying such securities.

None of Farm Credit West's investment securities are in an unrealized loss position at June 30, 2018. Accordingly, no investment security impairment has been recorded.

### Note 4 – Members' Equity

#### Preferred Stock

Farm Credit West is authorized to issue 500 million shares of class H preferred stock but had an internal issuance limit set at 425 million shares at June 30, 2018. Purchases may be made by individuals or entities that hold, at the time of their purchase of preferred stock, legal title to, or beneficial interest in, shares of any class of Farm Credit West common stock or participation certificates. Preferred stock is unprotected and "at-risk." Retirement of preferred stock upon the holder's request is at the sole discretion of the Farm Credit West Board consistent with Farm Credit West Bylaws. Retirements of preferred stock may also require approval by FCA.

The preferred stock dividend rate is a per annum rate which is subject to change each calendar month. For any particular month, the dividend rate shall not exceed 8% nor be less than the federal funds rate. The preferred stock dividend rate was 2.10% during the first quarter of 2018, and 2.15% during the second quarter of 2018. This is an increase from 2.0% at December 2017.

### Common Stock

Farm Credit West issues the following classes of common stock: class C common stock, class F participation certificates, and under certain circumstances, nonvoting class A common stock. Such equities are unprotected and "at-risk." At-risk equities can only be retired: 1) with the express approval of the Farm Credit West Board of Directors, and only if the capitalization requirements described below have been met; or 2) by Farm Credit West's president when consistent with authority delegated by the Board. At June 30, 2018, the required common investment was \$1 thousand per voting stockholder. Customers with multiple loans satisfy their equity ownership requirement with a single \$1 thousand cash investment.

At June 30, 2018, Farm Credit West had 906,793 shares of class C capital stock at a par value of \$5 per share, and 116,663 shares of class F capital stock were outstanding at a part value of \$5 per share.

#### Capital Adequacy

On March 10, 2016, the FCA Board approved a final rule to modify the regulatory capital requirements for System Banks and Associations. The final rule replaced core surplus and total surplus requirements with common equity tier 1, tier 1 and total capital risk-based capital ratio requirements. The final rule also replaced the net collateral ratio for banks with a tier 1 leverage ratio that is required for both Banks and associations. The permanent capital ratio continues to remain in effect with the final rule. The effective date of the new capital requirements was January 1, 2017.

Beginning in 2017, and in accordance with the effective date of the new capital requirements, Farm Credit West replaced the total and core surplus ratios with the new regulatory required ratios.

## Notes to Consolidated Financial Statements

As shown in the following table, Farm Credit West has substantially exceeded each regulatory minimum capital requirement for all periods presented.

Type of capital as % of risk-weighted assets	<i>For the quarter ended</i>			Regulatory Minimum including Buffer
	<b>June 30, 2018</b>	Dec. 31, 2017	Dec. 31, 2016	
Common Equity Tier 1	<b>13.76%</b>	13.33%		7.00%
Tier 1	<b>13.76%</b>	13.33%		8.50%
Total regulatory capital	<b>14.41%</b>	13.95%		10.50%
Tier 1 leverage <sup>(1)</sup>	<b>14.97%</b>	14.37%		5.00%
Minimum URE leverage <sup>(1)</sup>	<b>16.72%</b>	15.99%		1.50%
Permanent capital <sup>(2)</sup>	<b>17.61%</b>	17.37%	17.55%	7.00%
Total surplus			13.49%	7.00%
Core surplus			13.49%	3.50%

(1) Ratio is a % of total assets.

(2) Beginning in 2017, the calculation for risk-weighted assets for permanent capital was adjusted to align with the new capital regulations, impacting the comparability to prior period percentages.

### Accumulated Other Comprehensive Loss

The following tables present the activity in the accumulated other comprehensive loss, net of tax, by component.

<i>(in thousands)</i>	Unrealized	Unrecognized	Accumulated Other Comprehensive Gain (Loss)
	Gains on Investments Available for Sale	Cost in Pension and Other Plans	
Balance at December 31, 2017	\$ 813	\$ (5,023)	\$ (4,210)
Other comprehensive income (loss) before reclassifications	(412)	415	3
Net current period comprehensive change	(412)	415	3
Balance at June 30, 2018	<u>\$ 401</u>	<u>\$ (4,608)</u>	<u>\$ (4,207)</u>

<i>(in thousands)</i>	Unrealized	Unrecognized	Accumulated Other Comprehensive Gain (Loss)
	Gains on Investments Available for Sale	Cost in Pension and Other Plans	
Balance at December 31, 2016	\$ 1,604	\$ (4,973)	\$ (3,369)
Other comprehensive income (loss) before reclassifications	(322)	484	162
Net current period comprehensive change	(322)	484	162
Balance at June 30, 2017	<u>\$ 1,282</u>	<u>\$ (4,489)</u>	<u>\$ (3,207)</u>

### Note 5 – Fair Value Measurements

FASB 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. For additional information, see Note 2 to the 2017 Annual Report to Shareholders – Summary of Significant Accounting Policies.

Assets measured at fair value on a recurring basis are summarized below. There were no other assets and no liabilities measured at fair value on a recurring basis for the periods presented.

<i>(in thousands)</i>	Fair Value Measurement Using			Total Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Assets held in trusts for nonqualified benefit plans				
<b>June 30, 2018</b>	\$ 1,159			\$ 1,159
December 31, 2017	\$ 1,555			\$ 1,555
Investment securities – available-for-sale				
<b>June 30, 2018</b>		\$ 61,556		\$ 61,556
December 31, 2017		\$ 70,648		\$ 70,648

## Notes to Consolidated Financial Statements

The table below represents a reconciliation of Farm Credit West's investment securities – available-for-sale measured at fair value on a recurring basis.

<i>(in thousands)</i>	Fair Value Measurement Using Significant Unobservable Inputs (Level 3) Investment securities – available-for-sale	
	2018	2017
	Balance at beginning of year	\$ 70,648
Unrealized (losses) gains included in other comprehensive (loss) income	(412)	(322)
Settlements	(8,680)	(9,570)
Balance at June 30,	<u>\$ 61,556</u>	<u>\$ 76,990</u>

<i>(in thousands)</i>	Fair Value Measurement Using Significant Unobservable Inputs (Level 3) Investment securities – available-for-sale	
	2018	2017
	Balance at March 31,	\$ 66,190
Unrealized (losses) gains included in other comprehensive (loss) income	(534)	(238)
Settlements	(4,100)	(4,921)
Balance at June 30,	<u>\$ 61,556</u>	<u>\$ 76,990</u>

Assets measured at fair value on a non-recurring basis are summarized in the following table. There were no other assets and no liabilities measured at fair value on a non-recurring basis for the periods presented.

<i>(in thousands)</i>	Fair Value Measurement Using Significant Unobservable Inputs (Level 3)	Total Fair Value
Assets:		
Nonaccrual loans, net of related specific allowance		
<b>June 30, 2018</b>	\$ 22,734	\$ 22,734
December 31, 2017	14,555	14,555
Other property owned, appraised value		
<b>June 30, 2018</b>	\$ 5,478	\$ 5,478
December 31, 2017	6,232	6,232

### Valuation Techniques

As more fully discussed in Note 2 to the 2017 Annual Report to Shareholders, the FASB established 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 represents a brief summary of the valuation technique used by Farm Credit West for assets and liabilities subject to fair value measurement.

**Assets held in Trust:** Assets held in trust for nonqualified benefit plans are related to supplemental retirement plans and are generally classified under Level 1 and 2. These trust assets held by Farm Credit West include cash, money market funds and mutual funds that have quoted market prices in an active market and are therefore classified within Level 1.

**Investment Securities:** Where quoted prices are available in an active market, available-for-sale securities would be classified as Level 1. If quoted prices are not available in an active market, the fair value of securities are estimated using pricing models, quoted prices for similar securities received from pricing services or discounted cash flows. Generally, these securities would be classified as Level 2. This would include U.S. Treasury, U.S. agency and certain mortgage-backed and asset-backed securities. Where there is limited activity or less transparency around inputs to the valuation, the securities are classified as Level 3. Securities classified as Level 3 include Farm Credit West's mortgage-backed securities issued by the Federal Agricultural Mortgage Corporation.

Farm Credit West's held-to-maturity investment securities are carried at amortized cost and, as such, are not included here.

**Loans Evaluated for Impairment:** For nonaccrual loans evaluated for impairment under FASB impairment guidance, the fair value was based on the underlying real estate collateral for collateral-dependent loans. At June 30, 2018, substantially all of the Association's impaired loans that are recorded at fair value are secured by real estate. The fair value measurement process uses appraisals performed by independent licensed appraisers 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, certain of these loans have fair value measurements that fall within Level 3 of the fair value 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 and loans are reported at fair value.

**Other Property Owned:** The process for measuring the fair value of 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.

## Notes to Consolidated Financial Statements

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### Note 6 – Income Taxes

Farm Credit West, ACA conducts its business activities through its subsidiaries. Long-term mortgage lending activities are conducted through the Farm Credit West, FLCA and Southwest, FLCA subsidiaries which are exempt from federal and state income tax. Short- and intermediate-term lending activities are conducted through the Farm Credit West, PCA subsidiary and Southwest, PCA subsidiary. As with the PCA subsidiaries, the Farm Credit West, ACA and Southwest, ACA holding companies are subject to income tax. Farm Credit West operates as a cooperative that qualifies for tax treatment under Subchapter T of the Internal Revenue Code. Accordingly, under specified conditions, Farm Credit West can exclude from taxable income amounts distributed as qualified patronage dividends in the form of cash, stock, or allocated retained earnings. Provisions for income taxes are made only on those taxable earnings that will not be distributed as qualified patronage dividends.

The Tax Cuts and Jobs Act of 2017 (TCJA) was enacted in late 2017 which among other things lowered the federal corporate tax rate from 35 percent to 21 percent beginning in 2018. In accordance with GAAP, the change to the lower corporate tax rate led to a revaluation of deferred tax liabilities and deferred tax assets in the period of enactment (2017).

### Note 7 – Subsequent Events

The Association has evaluated subsequent events through August 6, 2018, which is the date the financial statements were issued. No subsequent event items met the criteria for disclosure.