

FIRST QUARTER 2004

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Chief Executive Officer



W. W. Sanford, III
Chairman of the Board

April 29, 2004

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

(dollars in thousands)

The following commentary reviews the consolidated financial condition and results of operations of Farm Credit of the Virginias, ACA (Association) for the period ended March 31, 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 livestock, timber, poultry and field crops. 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 impacts the level of dependency on a given commodity.

As of March 31, 2004, the gross loan volume of the Association was \$1,082,671. This was an increase of \$13,534, or 1.27 percent as compared to \$1,069,137 at December 31, 2003. The demand in loans has slowed compared to the same period last year, as interest rates have remained steady. Net loans outstanding at March 31, 2004, were \$1,059,369 as compared to \$1,045,835 at December 31, 2003. Net loans were 97.39 percent of total assets at March 31, 2004.

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 slightly from \$7,955 at December 31, 2003, to \$8,082 at March 31, 2004. The increase was primarily the result of several of the loans being downgraded to nonaccrual status.

Association management maintains an allowance for loan losses in an amount considered sufficient to absorb possible losses in the loan portfolio based on current and expected future conditions. The allowance for loan losses at March 31, 2004, was \$23,302. This amount was unchanged from 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

Net income for the three months ended March 31, 2004, totaled \$4,557, as compared to \$3,977 for the same period in 2003, an increase of \$580 or 14.58 percent. The increase in net income was primarily due to an increase in net interest income and lower provision for loan losses.

Net interest income increased \$269, or 4.70 percent, for the three months ended March 31, 2004, as compared to the same period in 2003. The increase in net interest income was mainly due to the increase in loan volume when compared to same quarter last year.

Noninterest income for the three months ended March 31, 2004, totaled \$2,100, as compared to \$2,185 for the same period of 2003, a decrease of \$85. The decrease was due primarily to lower loan fee income on loans sold into the secondary mortgage market. The Association experienced a decrease in the number of loans originated and sold into the secondary mortgage market during the first quarter of 2004 as compared to 2003. In 2003, as interest rates fell during the first half of the year, the Association experienced a high level of home mortgage activity. Customers took advantage of the low interest rates to refinance existing home mortgages or purchase new homes. As interest rates have leveled off, the level of activity, especially mortgage refinancing, has declined. The decrease in loan fee income was offset to some extent by a gain on the sale of the Abingdon branch office and increase in equity earnings of AgFirst Farm Credit Bank (Bank).

Operating expenses for the three months ended March 31, 2004 totaled \$3,497. This was a decrease of \$18 compared to the same period of 2003. After experiencing large increases in employee benefits expenses and insurance fund premium expense over the past two years, the Association for 2004 should experience little or no increase in these expenses during 2004. As result, operating expenses for the first quarter of 2004 actually decreased when compared to the same period last year.

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 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 March 31, 2004, was \$907,263 as compared to \$890,426 at December 31, 2003. The increase during the period is primarily attributed to the increase in loan volume.

CAPITAL RESOURCES

Total members' equity at March 31, 2004 totaled \$156,451, an increase of \$4,941, as compared to \$151,510 at December 31, 2003. The increase in members' equity was primarily attributed to earnings.

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, 2004, the Association's total surplus ratio and core surplus ratio were 12.03 percent and 10.04 percent, respectively, and the permanent capital ratio was 13.92 percent. All three ratios were well above the minimum regulatory ratios of 7.00 percent for permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

Farm Credit of the Virginias, ACA
Consolidated Balance Sheets

<i>(dollars in thousands)</i>	March 31, 2004	December 31, 2003
	<i>(unaudited)</i>	
Assets		
Cash	\$ 24	\$ 32
Loans	1,082,671	1,069,137
Less: allowance for loan losses	23,302	23,302
Net loans	1,059,369	1,045,835
Accrued interest receivable	7,825	6,180
Investment in AgFirst Farm Credit Bank	13,981	13,981
Premises and equipment, net	3,749	3,756
Other property owned	—	85
Deferred tax asset, net	21	21
Other assets	2,843	8,002
Total assets	\$ 1,087,812	\$ 1,077,892
Liabilities		
Notes payable to AgFirst Farm Credit Bank	\$ 907,263	\$ 890,426
Accrued interest payable	3,764	3,734
Patronage refund payable	128	8,098
Postretirement benefits other than pensions	5,043	4,870
Minimum pension liability	4,072	3,769
Other liabilities	11,091	15,485
Total liabilities	931,361	926,382
Commitments and contingencies		
Members' Equity		
Capital stock and participation certificates	19,598	19,735
Retained earnings		
Allocated	58,610	58,345
Unallocated	83,540	78,727
Accumulated other comprehensive income (loss)	(5,297)	(5,297)
Total members' equity	156,451	151,510
Total liabilities and members' equity	\$ 1,087,812	\$ 1,077,892

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

Farm Credit of the Virginias, ACA
Consolidated Statements of Income
(unaudited)

<i>(dollars in thousands)</i>	For the three months ended March 31,	
	2004	2003
Interest Income		
Loans	\$ 15,812	\$ 16,037
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	9,822	10,316
Net interest income	5,990	5,721
Provision for (reversal of) loan losses		514
Net interest income after provision for (reversal of) loan losses	5,990	5,207
Noninterest Income		
Loan fees	165	475
Fees for financially related services	11	14
Equity in earnings of AgFirst Farm Credit Bank	1,681	1,591
Other noninterest income	243	105
Total noninterest income	2,100	2,185
Noninterest Expense		
Salaries and employee benefits	2,364	2,412
Occupancy and equipment	247	220
Insurance Fund premium	267	309
Other operating expenses	619	574
Total noninterest expense	3,497	3,515
Income before income taxes	4,593	3,877
Provision (benefit) for income taxes	36	(100)
Net income	\$ 4,557	\$ 3,977

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

Farm Credit of the Virginias, ACA
**Consolidated Statements of Changes in
Members' Equity**

(unaudited)

<i>(dollars in thousands)</i>	Capital Stock and Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income	Total Members' Equity
		Allocated	Unallocated		
Balance at December 31, 2002	\$ 20,469	\$ 57,904	\$ 78,146	\$ (5,861)	\$ 150,658
Net income			3,977		3,977
Capital stock/participation certificates issued	278				278
Capital stock/participation certificates retired	(569)				(569)
Retained earnings retired		(89)			(89)
Distribution adjustment		34	(69)		(35)
Balance at March 31, 2003	\$ 20,178	\$ 57,849	\$ 82,054	\$ (5,861)	\$ 154,220
Balance at December 31, 2003	\$ 19,735	\$ 58,345	\$ 78,727	\$ (5,297)	\$ 151,510
Net income			4,557		4,557
Capital stock/participation certificates issued	230				230
Capital stock/participation certificates retired	(367)				(367)
Retained earnings retired		(33)			(33)
Distribution adjustment		298	256		554
Balance at March 31, 2004	\$ 19,598	\$ 58,610	\$ 83,540	\$ (5,297)	\$ 156,451

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

Farm Credit of the Virginias, 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 Farm Credit of the Virginias, 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 first 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 three months ended March 31, 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 March 31, 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	\$ 24,505
(Reversal of) provision for loan losses	514
Loans (charged off), net of recoveries	<u>(19)</u>
Balance at 3-31-03	<u>\$ 25,000</u>
Balance at 12-31-03	\$ 23,302
(Reversal of) provision for loan losses	–
Loans (charged off), net of recoveries	<u>–</u>
Balance at 3-31-04	<u>\$ 23,302</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 three months ended March 31, 2004:

	For the three months ended March 31,	
	2004	2003
Pension	\$ 303	\$ 331
Thrift/deferred compensation	72	70
Other postretirement benefits	<u>252</u>	<u>243</u>
Total	<u>\$ 627</u>	<u>\$ 644</u>