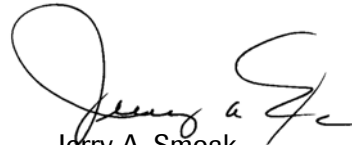


THIRD QUARTER 2003

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Lynn Z. Dantzler
Chief Executive Officer



Jerry A. Smoak
Chairman of the Board

October 29, 2003

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 Palmetto Farm Credit, ACA, (Association) for the period ended September 30, 2003. This information should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements, and the 2002 Annual Report of Palmetto Farm Credit.

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 wide range of agricultural commodities produced in our region, including poultry (broilers, turkeys, and eggs), timber, cotton, fruits and nuts, field crops and grains, beef cattle, horses, hogs, and dairy. Loans to producers of these commodities total \$539,740 or 86.09 percent of the Association's portfolio as of September 30, 2003.

Farm size varies and many Association customers have diversified farming operations. These factors, along with the numerous opportunities for non-farm income in the area, reduce to some degree the level of income dependency on any given commodity.

Production conditions have generally been positive for most of our crop farmer customers during 2003. Heavier than normal rainfall led to an excellent area corn crop, and we are generally optimistic about yield prospects for cotton, soybeans, and peanuts as well.

Prices for soybeans, beef cattle, and cotton have moved up in response to tightening supplies of these products and net farm income from crops and livestock in 2003 should be up significantly compared to the drought-reduced income results of the past several years. Poultry producers continue to enjoy profitable prices and dairy producers have seen some seasonal improvement in milk prices as well.

The very wet weather conditions that have plagued the area timber industry for much of 2003 have finally moderated somewhat due to a return to more normal rainfall patterns. Wood processors may, however, still be

challenged to stockpile sufficient raw product inventories, particularly for hardwood items, prior to the onset of generally wetter winter conditions.

Margins have improved for some wood processors over the past several months as demand for both lumber and chips has strengthened. Prices for stumpage have not fallen materially, however, and operations with significant debt loads still generally face a difficult path to return to previous levels of profitability.

Off-farm income continues to effectively supplement income derived from crop and livestock sales for a large number of our farmer customers. The lower interest rate environment has helped to improve repayment capacity for many of our customers as well. Values for land continue to increase due to nonagricultural demand and values of other agricultural assets have generally remained stable as well.

Due to the improved farm income prospects, a recovering general economy, and the significant diversification present in the association's loan portfolio, management expects the overall quality of the portfolio to improve slightly during the latter part of 2003. Nonearning assets should be reduced also as we collect the USDA guarantee funds due on a large nonaccrual loan that is in bankruptcy.

The gross loan volume of the Association as of September 30, 2003, was \$619,162, an increase of \$141 or less than 1 percent as compared to \$619,021 at December 31, 2002. Net loans outstanding at September 30, 2003 were \$605,172 as compared to \$605,093 at December 31, 2002. Net loans accounted for 95.99 percent of total assets at September 30, 2003, as compared to 95.45 percent of total assets at December 31, 2002.

The slight increase in gross loan volume during the reporting period is attributed primarily to increases in term loans to finance purchases of real estate, offset by reduced seasonal draws and early repayments on annual operating lines of credit. The lending activity related to the purchase of participation loans from other Farm Credit entities, both within and outside the AgFirst district, has also diminished during the reporting period. Some credits presented for purchase did not meet the Association's underwriting and pricing parameters, and prepayments on

several existing participations reduced the participation loan volume carried by the association.

For the past few years, the Association has experienced a continued shift in loan assets. The long-term volume trend has been downward while the short and intermediate-term loan volume trend has been upward. As a result of lower interest rates, many term loans are now being made for ten years or less allowing the borrower to build equity faster and thus reducing risk in the loan portfolio. These shorter repayment terms tend to negatively affect growth in the loan portfolio, however.

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 substantially from \$6,546 at December 31, 2002, to \$3,594 at September 30, 2003. The decrease is the result of payments on and liquidations of existing nonaccrual accounts as well as reinstatements to accrual status while few new transfers to nonaccrual were made.

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, 2003 was \$13,990 compared to \$13,928 at December 31, 2002, and was considered by management to be adequate to cover possible losses. During the quarter, management reviewed the allowance for loan loss and made no provision to the allowance for loan loss due to the relatively flat level of asset growth and to the increased utilization of FSA and Farmer Mac loan guarantees.

RESULTS OF OPERATIONS

For the three months ended September 30, 2003

Net income for the three months ended September 30, 2003, totaled \$2,588 as compared to \$1,373 for the same period in 2002. The increase in net income of \$1,215 is largely due to the addition of \$1,000 in the provision for loan losses during the third quarter in 2002 while no provision was made during the same quarterly period of 2003. Net interest income increased \$764 for the three months ended September 30, 2003, as compared to the same period in 2002. This increase is due primarily to focused repricing activities that increased net spreads while also generally reducing interest rates for customers. This net interest income increase was accomplished despite a generally lower interest rate environment that generated less net interest income from the prime-based portion of the loan portfolio funded by the Association's loanable funds.

At September 30, 2003, interest income on loans decreased \$643 compared to September 30, 2002. The majority of this variance was due to the lower interest rate environment. Nonaccrual income was \$104 for the three months ended September 30, 2003, as compared to \$83 for the same period in 2002. Interest expense decreased \$1,407 for the three months ended September 30, 2003. The decrease is linked to the annual formula change by the district bank in the direct note for variable rate debt and the lower interest rate environment that allowed repricing of many fixed rate loans, which resulted in lower borrower rates and higher Association interest rate spreads.

Noninterest income increased \$99 over the same period last year. The increase is due to higher loan fees and an increase in the equity in the earnings of other Farm Credit institutions.

Noninterest expense for the three months ended September 30, 2003, increased \$579 compared to the same period of 2002. This negative variance is due to an increase in salary and benefits expenses as well as an increase in premiums for the Farm Credit System Insurance Corporation. As is the case with most businesses, health care costs and retirement benefits expense continue to rise, and these costs are included in the Association's benefits expense. Additional funding for the Association's portion of the AgFirst district retirement plan was required due to a combination of negative investment performance and the lower interest rate environment. The Association also paid a special incentive bonus to selected staff members related to the loan repricing efforts in this reporting quarter.

For the nine months ended September 30, 2003

Net income for the nine months ended September 30, 2003, totaled \$6,868, as compared to \$3,586 for the same period in 2002. This increase of \$3,282 or 91.52 percent is attributed to a decrease in the addition to the provision for loan losses and increased net interest income due to higher spreads. At September 30, 2003, interest income on loans decreased \$1,138 compared to September 30, 2002. Nonaccrual income was \$211 for the nine months ended September 30, 2003, as compared to \$190 for the same period in 2002. Interest expense decreased by \$3,364 for the nine months ended September 30, 2003, as compared to the same period of 2002. The decline in interest expense is due to the annual formula change by the district bank in the direct note for variable rate debt and the substantially lower interest rate environment.

Noninterest income for the nine months ended September 30, 2003, totaled \$3,564 as compared to \$3,757 for the same period of 2002, a decrease of \$193. Write-downs in the carrying value of other property owned and

expenses on acquired property for the nine months ended September 30, 2003, totaled \$427 compared to \$35 during the first nine months of 2002. The write-downs were offset by higher fees and higher equity earnings in other Farm Credit institutions.

Noninterest expense for the nine months ended September 30, 2002, increased \$1,597 compared to the same period of 2002. This increase is attributed to higher salary and benefit expenses, additional expense of \$400 for premiums paid to the Farm Credit Insurance Corporation, and additional fees of \$159 in connection with Farmer Mac in-portfolio loan guarantees. The Association recorded a provision for income taxes of \$4 for the nine months ended September 30, 2003, as compared to \$225 for the same period in 2002. The majority of the provision for tax expense in 2002 was related to the write-off of net deferred tax assets. The write-off was necessary due to the formation of the ACA Holding Company effective January 1, 2002.

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 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 September 30, 2003, was \$544,982 as compared to \$550,184 at December 31, 2002. The decrease is primarily attributed to a lower level of nonaccruing loan volume and increased net earnings during the reporting period.

CAPITAL RESOURCES

Total members' equity at September 30, 2003, increased to \$73,268 from the December 31, 2002 total of \$70,525. The increase is primarily attributed to increased earnings during the period that offset retirement of capital stock, participation certificates, and allocated surplus.

Total capital stock and participation certificates were \$4,253 on September 30, 2003 compared to \$4,496 on December 31, 2002. The decrease is attributed to the retirement of protected stock and participation certificates on loans liquidated in the normal course of business, the retirement of excess stock, and new loans being capitalized at 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, 2003, the Association's total surplus ratio and core surplus ratio were 12.37 percent and 8.90 percent, respectively, and the permanent capital ratio was 13.07 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.

Management has taken actions designed to strengthen the Association's capital position. The Association is obtaining additional FSA guarantees on both new and existing credits and has increased the use of the Farmer Mac in-portfolio loan guarantee program as well. As of September 30, 2003, the Association's loan portfolio included \$36.56 million in FSA loan guarantees and \$76.80 million in the Farmer Mac in-portfolio guarantee program.

PROPOSED CONSOLIDATION

In December 2002, the Board of Directors of the Association unanimously approved a resolution to consolidate with AgSouth Farm Credit, ACA, which is headquartered in Statesboro, Georgia. At a special meeting of stockholders held on July 15, 2003, the consolidation was approved. On August 28, 2003, FCA gave its final approval for the consolidation, which will take place effective January 1, 2004. The consolidated association will be called AgSouth Farm Credit, ACA, and will be headquartered in Statesboro, Georgia.

Palmetto Farm Credit, ACA
Consolidated Balance Sheets

<i>(dollars in thousands)</i>	September 30, 2003	December 31, 2002
	<i>(unaudited)</i>	
Assets		
Cash	\$ 604	\$ 1,716
Loans	619,162	619,021
Less: allowance for loan losses	13,990	13,928
Net loans	605,172	605,093
Accrued interest receivable	5,590	5,458
Investment in other Farm Credit institutions	10,937	10,841
Premises and equipment, net	3,267	3,292
Other property owned	1,013	1,825
Other assets	3,852	5,716
Total assets	\$ 630,435	\$ 633,941
Liabilities		
Notes payable to AgFirst Farm Credit Bank	\$ 544,982	\$ 550,184
Accrued interest payable	1,643	1,943
Patronage refund payable	428	1,779
Postretirement benefits other than pensions	3,836	3,314
Minimum pension liability	3,728	3,751
Other liabilities	2,550	2,445
Total liabilities	557,167	563,416
Commitments and contingencies		
Members' Equity		
Protected borrower equity	701	891
Capital stock and participation certificates	3,552	3,605
Retained earnings		
Allocated	33,409	36,974
Unallocated	42,511	35,960
Accumulated other comprehensive income (loss)	(6,905)	(6,905)
Total members' equity	73,268	70,525
Total liabilities and members' equity	\$ 630,435	\$ 633,941

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

Palmetto 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,	
	2003	2002	2003	2002
Interest Income				
Loans	\$ 9,385	\$ 10,028	\$ 28,542	\$ 29,680
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	4,970	6,377	15,961	19,325
Net interest income	4,415	3,651	12,581	10,355
Provision for (reversal of) loan losses	—	1,000	125	2,750
Net interest income after provision for (reversal of) loan losses	4,415	2,651	12,456	7,605
Noninterest Income				
Loan fees	97	22	359	228
Fees for financially related services	16	22	57	62
Equity in earnings of other Farm Credit institutions	1,130	1,120	3,404	3,356
Gains (losses) on other property owned, net	15	18	(427)	(35)
Miscellaneous	36	13	171	146
Total noninterest income	1,294	1,195	3,564	3,757
Noninterest Expense				
Salaries and employee benefits	2,074	1,675	6,116	5,084
Occupancy and equipment	199	190	574	563
Insurance Fund premium	176	49	541	141
Other operating expenses	668	624	1,917	1,763
Total noninterest expense	3,117	2,538	9,148	7,551
Income before income taxes	2,592	1,308	6,872	3,811
Provision (benefit) for income taxes	4	(65)	4	225
Net income	\$ 2,588	\$ 1,373	\$ 6,868	\$ 3,586

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

Palmetto 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, 2001	\$ 1,190	\$ 3,607	\$ 36,989	\$ 35,179	\$ —	\$ 76,965
Net income				3,586		3,586
Protected borrower equity retired	(263)					(263)
Capital stock/participation certificates issued		289				289
Capital stock/participation certificates retired		(283)				(283)
Retained earnings retired			(3,931)			(3,931)
Distribution adjustment			90	(55)		35
Balance at September 30, 2002	\$ 927	\$ 3,613	\$ 33,148	\$ 38,710	\$ —	\$ 76,398
Balance at December 31, 2002	\$ 891	\$ 3,605	\$ 36,974	\$ 35,960	\$ (6,905)	\$ 70,525
Net income				6,868		6,868
Protected borrower equity retired	(190)					(190)
Capital stock/participation certificates issued		272				272
Capital stock/participation certificates retired		(325)				(325)
Retained earnings retired			(3,787)			(3,787)
Distribution adjustment			222	(317)		(95)
Balance at September 30, 2003	\$ 701	\$ 3,552	\$ 33,409	\$ 42,511	\$ (6,905)	\$ 73,268

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 Palmetto 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, 2002, are contained in the 2002 Annual Report to Stockholders. These unaudited third quarter 2003 consolidated financial statements should be read in conjunction with the 2002 Annual Report to Stockholders.

In December 2002, the Board of Directors of the Association unanimously approved a resolution to consolidate with AgSouth Farm Credit, ACA, which is headquartered in Statesboro, Georgia. At a special meeting of stockholders held July 15, 2003, the consolidation of the Association with AgSouth Farm Credit, ACA, was approved. On August 28, 2003, the Farm Credit Administration gave its final approval for the consolidation, which will take place effective January 1, 2004. The consolidated association will be called AgSouth Farm Credit, ACA, and will be headquartered in Statesboro, Georgia.

As disclosed in the 2002 Annual Report, pursuant to a plan of restructuring approved by the Farm Credit Administration and Association shareholders, the Association reorganized its corporate structure effective January 1, 2002. Pursuant to this restructuring, a Federal Land Credit Association (FLCA) and Production Credit Association (PCA) were formed as wholly owned subsidiaries of the Association. The formation of these subsidiaries enables the Association to take advantage of the tax-exempt status of long-term mortgage interest for loans held by the FLCA. This restructuring was accounted for as a reorganization of entities under common control similar to a pooling of interests.

Prior to the restructuring, the Association was subject to federal and state income tax. As a result of the restructuring, long-term lending activity has been separated into a wholly owned FLCA subsidiary which

is exempt from federal and state income tax. The ACA, which is the holding company, along with the wholly owned PCA subsidiary, will continue to be subject to income tax.

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, 2003, are not necessarily indicative of the results to be expected for the year ending December 31, 2003.

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, 2003, 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 12-31-01	\$ 14,848
(Reversal of) provision for loan losses	2,750
Loans (charged off), net of recoveries	<u>(3,753)</u>
Balance at 9-30-02	<u>\$ 13,845</u>
Balance at 12-31-02	\$ 13,928
(Reversal of) provision for loan losses	125
Loans (charged off), net of recoveries	<u>(63)</u>
Balance at 9-30-03	<u>\$ 13,990</u>