
Chattanooga Agricultural Credit Association

FIRST QUARTER 2008

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Chief Executive Officer



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Chief Financial Officer



Howard Moore
Chairman of the Board

April 28, 2008

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 Chattanooga Agricultural Credit Association (the Association) for the period ended March 31, 2008. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2007 Annual Report of the Association. The accompanying consolidated financial statements were prepared under the oversight of the Audit Committee of the Board of Directors.

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 poultry, dairy, livestock and produce. 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, 2008, was \$156,651, an increase of \$9,490 as compared to \$147,161 at December 31, 2007. Net loans outstanding at March 31, 2008, were \$156,002, an increase of \$9,491 as compared to \$146,511 at December 31, 2007. Net loans accounted for 93.95 percent of total assets at March 31, 2008, as compared to 92.98 percent of total assets at December 31, 2007. The increase in gross and net loan volume during the reporting period is partly attributable to an increase in new borrowers financing real estate and the purchase of loans from other financial institutions.

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 from \$100 at December 31, 2007, to \$112 at March 31, 2008. This increase is primarily the result of three accounts transferred to nonaccrual status, offset by payments received in the normal course of business.

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, 2008, was \$649 compared to \$650 at December 31, 2007, and was considered by management to be adequate to cover probable losses.

RESULTS OF OPERATIONS

For the three months ended March 31, 2008

Net income for the three months ended March 31, 2008, totaled \$945, as compared to \$731 for the same period in 2007. Net interest income decreased \$9 for the three months ended March 31, 2008, as compared to the same period in 2007. The change in net interest income is the result of lower interest rates on loans and lendable equity, and the increased participation in the Capitalized Participation Pool Program (the "CPP Program"). Under the CPP Program district associations can offer to sell to the Bank an undivided participation interest in loans originated by the Association. The Association is required to purchase stock in the Bank equal to eight percent of the total amount of loans sold. Income from the sale of loans into the CPP Program is recognized as patronage from the bank and shown as equity in earnings of other Farm Credit institutions. Participation in the program enhances the Association's capital ratios.

Noninterest income for the three months ended March 31, 2008, totaled \$664, as compared to \$440 for the same period of 2007, an increase of \$224. The increase is primarily the result of an increase in equity earnings from other Farm Credit institutions, loan fees, and other non interest income, partially offset by a decrease in fees for financially related services and gains on the sale of rural home loans.

Noninterest expense for the three months ended March 31, 2008, increased \$34 compared to the same period of 2007. The primary reasons for the increase in noninterest expense were increases in salaries and employee benefits, insurance fund premium and other operating expenses, partially offset by a decrease in occupancy and equipment.

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 fund 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, 2008, was \$138,506 as compared to \$129,082 at December 31, 2007.

CAPITAL RESOURCES

Total members' equity at March 31, 2008, increased to \$24,229 from the December 31, 2007 total of \$23,209. The increase is attributed to an increase in member owned stock and the retention of earnings.

Total capital stock and participation certificates were \$3,026 on March 31, 2008, compared to \$2,973 on December 31, 2007. The increase is attributed to an increase in loan volume. The initial borrower investment, through either purchase or transfer, must be in an amount equal to the lesser of two percent of the total loan amount or \$2.

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, 2008, the Association's total surplus ratio and core surplus ratio were 10.64 percent and 8.88 percent, respectively, and the permanent capital ratio was 12.47 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.

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 Stephen Gilbert, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at their website, www.agfirst.com. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 423-624-2169 ext. 18 or writing Sue J. Maiser, Chief Financial Officer, Chattanooga, ACA, P.O. Box 5220, Chattanooga, TN 37406, or accessing the website, www.chattanoogaagcredit.com. The Association prepares a quarterly report within 40 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.

Chattanooga Agricultural Credit Association
Consolidated Balance Sheets

<i>(dollars in thousands)</i>	March 31, 2008 <i>(unaudited)</i>	December 31, 2007 <i>(audited)</i>
Assets		
Cash	\$ 246	\$ 363
Loans	156,651	147,161
Less: allowance for loan losses	649	650
Net loans	156,002	146,511
Other investments	100	118
Accrued interest receivable	1,944	1,676
Investment in other Farm Credit institutions	6,124	5,946
Premises and equipment, net	873	888
Due from AgFirst Farm Credit Bank	548	1,856
Other assets	219	210
Total assets	\$ 166,056	\$ 157,568
Liabilities		
Notes payable to AgFirst Farm Credit Bank	\$ 138,506	\$ 129,082
Accrued interest payable	610	637
Patronage refund payable	25	738
Other liabilities	2,686	3,902
Total liabilities	141,827	134,359
Commitments and contingencies		
Members' Equity		
Capital stock and participation certificates	3,026	2,973
Retained earnings		
Allocated	9,364	9,440
Unallocated	11,839	10,796
Total members' equity	24,229	23,209
Total liabilities and members' equity	\$ 166,056	\$ 157,568

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

Chattanooga Agricultural Credit Association
Consolidated Statements of Income

(unaudited)

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

(dollars in thousands)

	2008	2007
Interest Income		
Investment securities	\$ —	\$ 14
Loans	2,820	2,864
Other	2	2
	2,822	2,880
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	1,836	1,887
Other	2	—
	1,838	1,887
Net interest income	984	993
Provision for (reversal of allowance for) loan losses	—	33
	984	960
Noninterest Income		
Loan fees	92	76
Fees for financially related services	2	3
Equity in earnings of other Farm Credit institutions	549	338
Gains (losses) on sale of rural home loans, net	2	7
Other noninterest income	19	16
	664	440
Noninterest Expense		
Salaries and employee benefits	446	412
Occupancy and equipment	37	40
Insurance Fund premium	51	49
Other operating expenses	169	168
	703	669
Income before income taxes	945	731
Provision (benefit) for income taxes	—	—
	945	731
Net income	\$ 945	\$ 731

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

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

(unaudited)

<i>(dollars in thousands)</i>	Capital Stock and Participation Certificates	Retained Earnings		Total Members' Equity
		Allocated	Unallocated	
Balance at December 31, 2006	\$ 3,127	\$ 7,674	\$ 10,534	\$ 21,335
Net income			731	731
Capital stock/participation certificates issued/retired	24			24
Patronage distribution adjustment		28	(41)	(13)
Balance at March 31, 2007	<u>\$ 3,151</u>	<u>\$ 7,702</u>	<u>\$ 11,224</u>	<u>\$ 22,077</u>
Balance at December 31, 2007	\$ 2,973	\$ 9,440	\$ 10,796	\$ 23,209
Net income			945	945
Capital stock/participation certificates issued/retired	53			53
Patronage distribution adjustment		(76)	98	22
Balance at March 31, 2008	<u>\$ 3,026</u>	<u>\$ 9,364</u>	<u>\$ 11,839</u>	<u>\$ 24,229</u>

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

Chattanooga Agricultural Credit Association

Notes to the Consolidated Financial Statements

*(dollars in thousands, except as noted)
(unaudited)*

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements include the accounts of Chattanooga Agricultural Credit Association (the Association). A description of the organization and operations of the Association, the significant accounting policies followed, and the financial condition and results of operations as of and for the year ended December 31, 2007, are contained in the 2007 Annual Report to Shareholders. These unaudited first quarter 2008 consolidated financial statements should be read in conjunction with the 2007 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 (GAAP) and prevailing practices within the banking industry. The results for the three months ended March 31, 2008, are not necessarily indicative of the results to be expected for the year ending December 31, 2008.

Certain amounts in the prior period's consolidated financial statements may have been reclassified to conform to the current period's 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 GAAP. The loan portfolio is reviewed quarterly to determine the adequacy of the allowance for losses. As of March 31, 2008, the allowance for losses is adequate in management's opinion to provide for possible losses on existing loans.

In December 2007, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141R, "Business Combinations." SFAS No. 141R requires business combinations to be accounted for under the acquisition method of accounting (previously called the purchase method). The acquisition method requires (a) identifying the acquirer, (b) determining the acquisition date, (c) recognizing and measuring the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree, at their acquisition date fair values, and (d) recognizing and measuring goodwill or a gain from a bargain purchase. SFAS No. 141R should be applied

prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Early application is prohibited. The Association is still evaluating the provisions of the Standard, but believes that its adoption will significantly impact its accounting for acquisitions that may occur in 2009 and beyond.

NOTE 2 – ALLOWANCE FOR LOAN LOSSES

An analysis of the allowance for loan losses follows:

	For the three months ended March 31,	
	2008	2007
Balance at beginning of period	\$ 650	\$ 580
Provision for (reversal of) loan losses	–	33
Loans (charged off), net of recoveries	(1)	1
Balance at end of period	\$ 649	\$ 614

NOTE 3 – EMPLOYEE BENEFIT PLANS

The following is a table of retirement and other postretirement benefit expenses for the Association:

	For the three months ended March 31,	
	2008	2007
Pension	\$ 22	\$ 28
401(k)	16	13
Other postretirement benefits	18	23
Total	\$ 56	\$ 64

The following is a table of retirement and other postretirement benefit contributions for the Association:

	Actual YTD Through 3/31/08	Projected Contributions For Remainder of 2008	Projected Total Contributions 2008
Pension	\$ –	\$ –	\$ –
Other postretirement benefits	6	21	27
Total	\$ 6	\$ 21	\$ 27

Market conditions could impact discount rates and return on plan assets which could change the above contribution projections by making additional contributions necessary before the next plan measurement date.