



THIRD QUARTER 2006

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William A. Garrahan
Chief Executive Officer



Juan A. Santiago
Chairman of the Board

October 27, 2006

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 Puerto Rico Farm Credit, ACA (Association) and its subsidiaries for the nine months ended September 30, 2006. These comments should be read in conjunction with the accompanying consolidated financial statements, notes to the consolidated financial statements and the 2005 annual report of the Association. 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 island farmers, rural homeowners and farm-related businesses for financing short and intermediate-term loans and long-term real estate mortgage loans. The Association's predominant local service area agricultural commodities were dairy, livestock and fruits which totaled approximately \$90.8 million or 36.7 percent of all outstanding loan volume at September 30, 2006. The Association also maintains a portfolio of purchased participation loans, originated by other Farm Credit System entities and non-system entities.

The gross loan volume of the Association at September 30, 2006 was \$247,753 a decrease of \$29,715 or 10.7 percent as compared to \$277,468 at December 31, 2005. Following objectives established by the Board of Directors, the Association participated part of its originated loan portfolio to the AgFirst FCB (the Bank) at the beginning of 2006. This action has resulted in a reduction in loan volume of \$7,050. Additionally, during the first quarter, pay offs further reduced loan volume by approximately \$19,000. These reductions have been partially offset by an increase in participation loans purchased. At September 30, 2006, the Association's loan portfolio consisted of \$161,937 in originated loan volume and \$85,816 in participation purchased loan volume.

Net loans outstanding at September 30, 2006 totaled \$247,491. At September 30, 2006 net loans made up 96.5 percent of total assets, compared to 97.4 percent at December 31, 2005. Besides the material decrease in loan volume, other assets increased due to recognizing higher receivables, primarily related to the anticipated dividends from the Bank at year end.

As a percentage of gross loans, nonaccrual loans equaled 1.18 percent at September 30, 2006, compared with .58 percent and at December 31, 2005. Despite the decrease in loan volume, credit quality ratios have not been significantly impacted and remained at relatively higher levels, when compared to the past five years. Credit quality has also been supported and enhanced by the lower interest rate environment, favorable weather and stable product demand, which have also had a favorable impact on delinquency rates.

The allowance for loan losses was \$261 at September 30, 2006, an increase of \$24 from December 31, 2005. The increased allowance recognized a higher level of participation purchased loan volume, including letters of credit. The ratio of allowance to outstanding loan volume was .11 percent at September 30, 2006 compared with .09 percent at December 31, 2005. There were no charge-offs or recoveries during the first nine months of 2006.

RESULTS OF OPERATIONS

Net income for the nine months ended September 30, 2006 totaled \$2,808, an increase of \$686 or 32.3 percent as compared to \$2,122 for the first nine months of 2005. The increase primarily resulted from the Association and the Bank redefining the direct note borrowing relationship, with the expiration of IRS Section 936 as of December 31, 2005. As a result of this change, net interest income decreased by \$397 or 7.8 percent to \$4,702 for the first nine months 2006, as compared to \$5,099 for the first three quarters of 2005. However, this decrease was more than offset by accruing the Bank's projected annual patronage dividend distribution for 2006. For the nine months ended September 30, 2006 equity in earnings of other Farm Credit institutions totaled \$1,194, as compared to no such income recognized during 2005.

During the first nine months of 2006, interest income on accruing loans totaled \$13,552, an increase of \$2,910 or 27.3 percent from \$10,642 as of September 30, 2005. This material increase primarily resulted from the higher interest rate environment. However, interest expense for the first nine months payable to the Bank increased by \$3,307 or 59.7 percent, primarily due to the change in the direct note pricing agreement with the Bank. For all of 2006, the Association expects to show a decrease in net interest income as compared to 2005. However, this decrease will be more than offset by the annual patronage refund distribution to be received from the Bank, at year-end 2006.

During the first nine months of 2006, the association recognized a provision for loan losses of \$24, reducing net income.

Noninterest income for the nine months ended September 30, 2006 was \$1,459, an increase of \$1,192 as compared to the first nine months of 2005. Primarily, this was the result of recording estimated patronage income due from the Bank which totaled \$1,194.

Noninterest expense for the nine months ended September 30, 2006 increased by \$65 or 1.0 percent compared to the same period of 2005. The increase was primarily related to higher insurance fund premium expense of \$161, which was partially offset by a decrease in the guarantee fee. This offsetting relationship between these two expense categories will be in place for the entire year. The insurance fund increased premiums on accruing loans by 140 percent for 2006 and the guarantee fee paid to the Bank expired with the sale of participation loans to the Bank. Other operating expenses increased by \$25 primarily due to the higher costs related to compliance with new governance regulations and the costs of additional examinations.

During the first three quarters of 2006, like 2005, the Association did not record a provision for current year income tax expense. During the second quarter of 2006 the Association made a payment of \$2 related to filing 2005's federal tax return. Additionally, during the third quarter, as part of the Association's conversion to filing the federal tax return for 2006 on a sub-chapter T basis, the balance of the net deferred tax assets were written off. This action, which totaled \$15, reduced net income.

For the three months ended September 30, 2006

Net income for the third quarter of 2006 totaled \$1,033 compared to \$821 for the third quarter of 2005. Net interest income for the three months ended September 30, 2006 was \$1,589 compared to \$1,801 for the three months ended September 30, 2005, reflecting the change in the financing agreement with the Bank.

Noninterest income for the third quarter of 2006 was \$483, an increase of \$381 when compared to the third quarter of 2005. Again, this was the result of recognizing \$389 in estimated patronage due from the Bank.

For the third quarter of 2006, noninterest expense decreased by \$39 to total \$1,046, compared to the third quarter of 2005 which totaled \$1,085. Primarily, this was the result of there being no guarantee fee expense during the quarter, versus \$46 during the third quarter of 2005.

ACCOUNTING FOR DEFINED BENEFIT PENSION AND OTHER POSTRETIREMENT PLANS

On September 29, 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 – Employees' Accounting for Defined Benefit Pension and Other Postretirement Plans. The Standard requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in that funded status in the year in which the changes occur through comprehensive income. The Standard is effective for employers with publicly traded securities for the fiscal year ending after December 15, 2006 and for employers without publicly traded securities for the fiscal year ending after June 15, 2007. The Association will be required to implement the Standard for the year ended December 31, 2007. In addition, this Standard requires that the funded status of a plan be measured as of the date of the year-end financial statements. Currently, the Association uses a measurement date of September 30th. The requirement to measure the funded status as of the fiscal year-end is effective for fiscal years ending after December 15, 2008. The Association is currently evaluating the impact of implementing this Standard. It is anticipated that the impact from the implementation of this Standard will have little to no impact on the income statement and, based on the current funded status of the defined benefit plans, it is not expected to have a material or significant impact on the balance sheet.

Key Results of Operations Ratios:

	Annualized for the nine months ended 9/30/06	For the year ended 12/31/05
Return on Average Assets	1.43%	1.12%
Return on Average Members' Equity	6.91%	5.53%
Net Interest Income as a Percentage of Average Earning Assets	2.47%	2.69%

LIQUIDITY AND FUNDING SOURCES

Liquidity

Liquidity management is the process whereby funds are made available to meet all financial commitments including the extension of credit, payment of operating expenses and payment of debt obligations. The Association receives access to funds through its borrowing relationship with the Bank and from income generated by operations. Sufficient liquid funds have been available to meet all financial obligations.

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 funds are advanced by the Bank to the Association in the form of notes payable. The notes payable are segmented into variable rate and fixed rate sections. The variable rate notes are utilized by the Association to fund variable rate loan advances and operating funds requirements. The total notes payable to the Bank at September 30, 2006 were \$197,119 as compared with \$225,635 at December 31, 2005. The decrease of \$28,516 or 12.6 percent during the first nine months corresponded very closely to the decrease in gross loan volume outstanding and the funding of the 2005 year end dividend.

The Association had no lines of credit outstanding with third parties as of September 30, 2006.

Funds Management

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers variable and fixed rate loan products which are competitively priced according to local market rates. Variable rate loans may be indexed to either the Prime rate or the 90-day London Interbank Offered Rate (LIBOR). The majority of the interest rate risk in the Association balance sheet is transferred to the Bank through the notes payable structure. The Bank, in turn, actively utilizes funds management techniques to identify, quantify and control interest rate risk associated with the loan portfolio.

CAPITAL RESOURCES

Total members' equity at September 30, 2006 increased 5.2 percent to \$55,619 from December 31, 2005 when total members' equity was \$52,853. The increase was primarily attributable to net income retained as unallocated surplus during the first three quarters of 2006.

Total capital stock and participation certificates were \$898 on September 30, 2006 compared to \$940 on December 31, 2005. The decrease of \$42 was the net result of refunding more stock to non-borrowing members than new members purchasing capital stock or participation certificates.

Retained earnings unallocated increased \$2,808 or 5.4 percent from December 31, 2005 when unallocated retained earnings totaled \$51,913. The increase was from net income earned, during the current year.

The Board of directors intends to continue its policy of declaring cash dividends. 2005 was the thirteenth consecutive year of paying dividends. The table below sets forth the amount of dividends declared:

Year	Type	Amount Declared
2005	Patronage	\$ 3,000
2004	Patronage	\$ 2,500
2003	Patronage and Equity	\$ 2,000

The amount of dividends, as always, will depend on continued strong earnings, the overall financial condition of the Association and other factors.

The Association's regulatory permanent capital ratio at September 30, 2006 was 23.89 percent compared to 24.02 percent at December 31, 2005. The Association's total surplus and core surplus ratios were both 23.46 percent at September 30, 2006. All three ratios were well above the minimum regulatory ratios of 7.00 percent for the permanent capital and total surplus ratios and 3.50 percent for the core surplus ratio.

Key financial condition ratios were as follows:

	9/30/06	12/31/05
Members' Equity to Assets	21.68%	18.57%
Debt to Members' Equity	3.61:1	4.39:1

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 Wanda Martin, AgFirst Farm Credit Bank, P.O. Box 1499, Columbia, SC 29202. Information concerning AgFirst Farm Credit Bank can also be obtained at its website, www.agfirst.com. Copies of the Association's annual and quarterly reports are also available upon request free of charge by calling 1-800-981-3323, or writing Bruce M Hoffman, CFO, Puerto Rico Farm Credit, ACA, PO Box 363649, San Juan, PR 00936-3649, or accessing the website, www.puertoricofarmcredit.com. The Association prepares a quarterly report within 45 days after the end of each fiscal quarter, except that no report need be prepared for the fiscal quarter that coincides with the end of the fiscal year of the Association.

Puerto Rico Farm Credit, ACA
Consolidated Balance Sheets

<i>(dollars in thousands)</i>	September 30,		December 31,
	2006	2005	2005
	<i>(unaudited)</i>	<i>(unaudited)</i>	<i>(audited)</i>
Assets			
Cash	\$ —	\$ 10	\$ 27
Loans	247,753	263,989	277,468
Less: allowance for loan losses	261	226	237
Net loans	247,492	263,763	277,231
Accrued interest receivable	2,244	1,893	1,687
Investment in other Farm Credit institutions	2,864	2,712	2,864
Premises and equipment, net	733	462	482
Other property owned	—	150	150
Prepaid retirement expense	1,856	2,188	2,106
Due from AgFirst Farm Credit Bank	1,194	—	—
Other assets	136	143	138
Total assets	<u>\$ 256,519</u>	<u>\$ 271,321</u>	<u>\$ 284,685</u>
Liabilities			
Notes payable to AgFirst Farm Credit Bank	\$ 197,119	\$ 213,312	\$ 225,635
Accrued interest payable	1,017	723	890
Dividends payable	—	—	3,000
Postretirement benefits other than pensions	1,802	1,628	1,696
Other liabilities	962	677	611
Total liabilities	<u>200,900</u>	<u>216,340</u>	<u>231,832</u>
Commitments and contingencies			
Members' Equity			
Capital stock and participation certificates	898	952	940
Unallocated retained earnings	54,721	54,029	51,913
Total members' equity	<u>55,619</u>	<u>54,981</u>	<u>52,853</u>
Total liabilities and members' equity	<u>\$ 256,519</u>	<u>\$ 271,321</u>	<u>\$ 284,685</u>

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

Puerto Rico 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,	
	2006	2005	2006	2005
Interest Income				
Loans	\$ 4,649	\$ 3,900	\$ 13,552	\$ 10,642
Interest Expense				
Notes payable to AgFirst Farm Credit Bank	3,060	2,099	8,850	5,543
Net interest income	1,589	1,801	4,702	5,099
Provision for (reversal of) loan losses	(22)	—	24	—
Net interest income after provision for (reversal of) loan losses	1,611	1,801	4,678	5,099
Noninterest Income				
Loan fees	89	88	230	233
Fees for financially related services	4	14	9	20
Equity in earnings of other Farm Credit institutions	389	—	1,194	—
Other noninterest income	1	—	26	14
Total noninterest income	483	102	1,459	267
Noninterest Expense				
Salaries and employee benefits	686	697	2,140	2,152
Occupancy and equipment	73	58	200	182
Insurance Fund premium	83	40	249	88
Guarantee fee	—	46	16	143
Other operating expenses	203	244	705	680
Losses on other property owned, net	1	—	2	2
Total noninterest expense	1,046	1,085	3,312	3,247
Income before income taxes	1,048	818	2,825	2,119
Provision (benefit) for income taxes	15	(3)	17	(3)
Net income	\$ 1,033	\$ 821	\$ 2,808	\$ 2,122

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

Puerto Rico Farm Credit, ACA

Consolidated Statements of Changes in Members' Equity

(unaudited)

(dollars in thousands)

	Capital Stock and Participation	Retained Earnings Unallocated	Total Members' Equity
Balance at December 31, 2004	\$ 998	\$ 51,906	\$ 52,904
Net income		2,122	2,122
Capital stock/participation certificates issued	29		29
Capital stock/participation certificates retired	(75)		(75)
Distribution adjustment		1	1
Balance at September 30, 2005	<u>\$ 952</u>	<u>\$ 54,029</u>	<u>\$ 54,981</u>
Balance at December 31, 2005	\$ 940	\$ 51,913	\$ 52,853
Net income		2,808	2,808
Capital stock/participation certificates issued	23		23
Capital stock/participation certificates retired	(65)		(65)
Balance at September 30, 2006	<u>\$ 898</u>	<u>\$ 54,721</u>	<u>\$ 55,619</u>

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 Puerto Rico 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, 2005, are contained in the 2005 Annual Report to Shareholders. These unaudited third quarter 2006 consolidated financial statements should be read in conjunction with the 2005 Annual Report to Shareholders.

On September 29, 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 – Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans. The Standard requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and recognize changes in that funded status in the year in which the changes occur through comprehensive income. The Standard is effective for employers with publicly traded securities for the fiscal year ending after December 15, 2006 and for employers without publicly traded securities for the fiscal year ending after June 15, 2007. The Association will be required to implement the Standard for the year ended December 31, 2007. In addition, this Standard requires that the funded status of a plan be measured as of the date of the year-end financial statements. Currently, the Association uses a measurement date of September 30th. The requirement to measure the funded status as of the fiscal year-end is effective for fiscal years ending after December 15, 2008. The Association is currently evaluating the impact of implementing this Standard. It is anticipated that the impact from the implementation of this Standard will have little to no impact on the consolidated income statement and, based on the current funded status of the defined benefit plans, it is not expected to have a material or significant impact on the consolidated balance sheet.

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, 2006, are not necessarily indicative of the results to be expected for the year ending December 31, 2006.

Certain amounts in prior period consolidated financial statements may 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, 2006, 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:

	For the nine months ended September 30,	
	2006	2005
Balance at beginning of period	\$ 237	\$ 198
Provision for (reversal of) loan losses	24	–
Recoveries, net of loans charged off	–	28
Balance at end of period	<u>\$ 261</u>	<u>\$ 226</u>

NOTE 3 – INCOME TAXES

With the expiration of Section 936/30A as of December 31, 2005, the enacted tax law changed beginning January 1, 2006. For 2006, the Association has chosen to operate as a sub-chapter T cooperative for federal tax purposes. Accordingly, under specified conditions, the Association can exclude from taxable income amounts distributed as qualified patronage refunds. It is projected that provisions for federal income tax will be recorded only on those earnings not distributed. The Association intends to distribute 100 percent of patronage income, based on taxable income. During the third quarter of 2006, the Association wrote-off the December 31, 2005 balance of net deferred taxes totaling \$15 and took a charge to tax expense reducing income.

NOTE 4 – COMMITMENTS AND CONTINGENT LIABILITIES

Actions are pending against the Association in which money damages are sought. However, on the basis of information now at hand, management and legal counsel are of the opinion that the ultimate liability, if any, resulting therefrom, would not be material in relation to the overall financial position of the Association.

NOTE 5 – 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 a Districtwide Thrift Plan. Both plans also qualify under Puerto Rico law.

The Association sponsors a plan providing certain benefits (primarily health care) to its retirees. The following table sets forth the components of net periodic benefit costs of the other postretirement benefits plan for the nine months ended September 30, 2006:

	For the nine months ended September 30,	
	2006	2005
Service cost	\$ 37	\$ 33
Interest cost	101	147
Amortization of net transition obligation (asset)	25	25
Recognized net actuarial (gain) loss	24	74
Net periodic benefit cost	<u>\$ 187</u>	<u>\$ 279</u>

The following is a table of retirement and postretirement benefit expense for the nine months ended September 30, 2006:

	For the nine months ended September 30,	
	2006	2005
Pension	\$ 251	\$ 245
Thrift	47	47
Other postretirement benefits	187	279
Total	<u>\$ 485</u>	<u>\$ 571</u>

As of September 30, 2006, no contributions have been made to the pension plan for 2006. The Association does not anticipate making any contributions for the remainder of 2006.