



FIRST QUARTER 2004

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Chief Executive Officer



Juan A. Santiago
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 Puerto Rico Farm Credit, ACA (Association) for the three months 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 business for financing short and intermediate-term loans and long-term real estate mortgage loans. The Association also maintains a portfolio of purchased loans, originated by other Farm Credit System entities and non-system entities. The Association's predominant local service area (LSA) agricultural commodities were dairy, livestock and fruits which totaled approximately \$115 million or 48 percent of all outstanding loan volume at March 31, 2004.

The gross loan volume of the Association at March 31, 2004 was \$238,288, an increase of \$14,967 or 6.7 percent as compared to \$223,321 at December 31, 2003. Net loans outstanding at March 31, 2004 also increased by the same amount, as there was no change in the allowance for loan losses. The improvement in gross loan volume was primarily related to a \$14,827 increase in net participation loans purchased. Otherwise, increased LSA loan volume was mostly offset by scheduled repayment activity.

Net loans at March 31, 2004 made up 97.2 percent of total assets, the same percentage as December 31, 2003. However, this compared to 96.9 percent at March 31, 2003. The increase during the past year was the result of the material increase in loan assets.

As a percentage of gross loans, nonaccrual loans equaled 1.3 percent at March 31, 2004, compared with 1.3 percent and 1.9 percent at December 31 and March 31, 2003, respectively. The year-over-year decrease in the percentage was primarily the result of a partial payment received from the sale of collateral

property related to a large volume account. There is a plan in place to liquidate the remaining collateral. Due to the substantial increase in loan volume, the overall credit quality of the total portfolio continued to show improvement, and is at the best level of the past ten 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 Association maintained an allowance for loan losses in an amount considered by management as sufficient to absorb the estimated risk inherent in the loan portfolio. The allowance for loan losses was the same at March 31, 2004, as at December 31, 2003. The first quarter 2004 analysis identified less risk as a result of a lower level of nonaccrual loans and improved credit quality. The ratio of allowance to gross loan volume was 2.5 percent at March 31, 2004 and 2.7 percent at December 31, 2003. There were no charge-offs or recoveries during the first quarter of 2004.

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.

The Association and the Farm Credit System plan to conduct a study to further refine the 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 \$558, an increase of \$118 or 26.8 percent as compared to the first quarter of 2003. The increase was primarily the result of interest income earned on the higher level of accruing loan volume. At March 31, 2004 net interest income was \$1,547, an increase of \$154, or 11.1 percent compared to the first quarter of 2003. During the first quarter of 2004, interest income on accruing loans increased by \$188, while interest expense decreased by \$14. However, interest income recorded from the collection of nonaccrual loans decreased by \$48 compared to the first quarter of 2003. Management continues to project lower levels of interest income from nonaccrual loans similar to the previous two years, as this category of loans continues to decrease.

During the first quarter of 2004, the allowance was not changed, resulting in no impact to income. Noninterest income for the three months ended March 31, 2004 was \$66, a decrease of \$23 as compared to the first three months of 2003. Primarily this was the result of decreased fee income from the recognition of prepayment penalties related to participation loans during 2003.

Noninterest expense for the three months ended March 31, 2004 increased by \$14 or 1.3 percent compared to the same period of 2003. The increase was primarily related to other operating expenses which increased \$31 year-over-year. This was directly related to the Association initiating a Puerto Rico agricultural products advertising campaign. Other expenses also increased due to higher legal fees related to additional consulting engagements. The increase in other operating expenses was partially offset by small decreases in other categories. Specifically, management projects a material decrease in the insurance fund premium expense during the second half of 2004. The Farm Credit System Insurance Fund has announced a 40 percent decrease in the premium rate assigned to accruing loan volume, beginning July 1, 2004.

As a result of the 2001 restructuring, a majority of the Association's business has been conducted in the tax-exempt subsidiary or as possession-sourced activity eligible for tax credits. During the first quarter of 2004, like 2003, the Association did not record a provision for income tax expense.

Key Results of Operations Ratios:

	Annualized for the three months ended 3/31/04	For the year ended 12/31/03
Return on Average Assets	.99%	1.28%
Return on Average Stockholders' Equity	4.81%	5.94%
Net Interest Income as a Percentage of Average Earning Assets	2.78%	2.80%

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 AgFirst Farm Credit Bank (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 March 31, 2004 was \$189,313 as compared with \$172,671 at December 31, 2003. The increase of \$16,642 or 9.6 percent corresponded to the increase in gross loan volume and the funding of the year-end 2003 dividend.

The Association had no lines of credit outstanding with third parties as of March 31, 2004.

Funds Management

Demand for loan types is a driving force in establishing a funds management strategy. The Association offers variable rate loan products which are competitively priced according to financial 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 stockholders' equity at March 31, 2004 increased 1.2 percent to \$46,411 from December 31, 2003 when total stockholders' equity was \$45,855. The increase was primarily attributable to net income retained as unallocated surplus during the quarter.

Total capital stock and participation certificates were \$1,020 on March 31, 2004 compared to \$1,022 on December 31, 2003. The decrease of \$2 was the net result of refunding more stock to non-borrowing stockholders than new stockholders purchasing capital stock or participation certificates.

Retained earnings unallocated increased \$558 or 1.2 percent from December 31, 2003 when unallocated retained earnings totaled \$46,654. The increase was solely due to net income earned during the first quarter.

The Board of directors intends to continue its policy of declaring cash dividends. 2003 was the eleventh consecutive year of paying dividends. The dividend declared in June will be based upon equity ownership and the December dividend will continue to be based upon client patronage. The table below sets forth the amount of dividends declared:

<u>Year</u>	<u>Type</u>	<u>Amount Declared</u>
2003	Patronage Equity	\$ 1,847
		<u>153</u>
		<u>\$ 2,000</u>
2002	Patronage Equity	\$ 1,602
		<u>149</u>
		<u>\$ 1,751</u>

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 March 31, 2004 was 24.72 percent compared to 25.83 percent at December 31, 2003. The Association's total surplus and core surplus ratios were both 24.13 percent at March 31, 2004. 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.

Key financial condition ratios were as follows:

	3/31/04	12/31/03
Stockholders' Equity to Assets	19.42%	20.50%
Debt to Stockholders' Equity	4.15:1	3.88:1

Puerto Rico Farm Credit, ACA
Consolidated Balance Sheets

<i>(dollars in thousands)</i>	March 31,		December 31,
	2004	2003	2003
	<i>(unaudited)</i>		
Assets			
Cash	\$ 127	\$ 10	\$ 16
Loans	238,288	207,706	223,321
Less: allowance for loan losses	5,983	6,498	5,983
Net loans	232,305	201,208	217,338
Accrued interest receivable	1,046	981	876
Investment in AgFirst Farm Credit Bank	4,712	4,712	4,712
Premises and equipment, net	584	575	482
Other assets	240	121	230
Total assets	\$ 239,014	\$ 207,607	\$ 223,654
Liabilities			
Notes payable to AgFirst Farm Credit Bank	\$ 189,313	\$ 159,030	\$ 172,671
Accrued interest payable	209	213	199
Dividend payable	1	51	1,849
Postretirement benefits other than pensions	1,247	1,031	1,188
Minimum pension liability	1,317	1,367	1,223
Other liabilities	516	637	669
Total liabilities	192,603	162,329	177,799
Commitments and contingencies			
Stockholders' Equity			
Capital stock and participation certificates	1,020	1,013	1,022
Unallocated retained earnings	47,212	46,303	46,654
Accumulated other comprehensive income (loss)	(1,821)	(2,038)	(1,821)
Total stockholders' equity	46,411	45,278	45,855
Total liabilities and stockholders' equity	\$ 239,014	\$ 207,607	\$ 223,654

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 March 31,	
	2004	2003
Interest Income		
Loans	\$ 2,161	\$ 2,021
Interest Expense		
Notes payable to AgFirst Farm Credit Bank	614	628
Net interest income	1,547	1,393
Provision for (reversal of) loan losses	—	—
Net interest income after provision for (reversal of) loan losses	1,547	1,393
Noninterest Income		
Loan fees	47	67
Fees for financially related services	3	4
Other noninterest income	16	18
Total noninterest income	66	89
Noninterest Expense		
Salaries and employee benefits	690	697
Occupancy and equipment	56	53
Insurance Fund premium	52	60
Guarantee fee	52	57
Other operating expenses	205	174
Total noninterest expense	1,055	1,041
Income before income taxes	558	441
Provision (benefit) for income taxes	—	1
Net income	\$ 558	\$ 440

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

Puerto Rico Farm Credit, ACA
**Consolidated Statements of Changes in
 Stockholders' Equity**

(unaudited)

<i>(dollars in thousands)</i>	Capital Stock and Participation Certificates	Retained Earnings Unallocated	Accumulated Other Comprehensive Income	Total Stockholders' Equity
Balance at December 31, 2002	\$ 1,001	\$ 45,914	\$ (2,038)	\$ 44,877
Net income		440		440
Capital stock/participation certificates issued	29			29
Capital stock/participation certificates retired	(17)			(17)
Cash dividends declared		(51)		(51)
Balance at March 31, 2003	<u>\$ 1,013</u>	<u>\$ 46,303</u>	<u>\$ (2,038)</u>	<u>\$ 45,278</u>
Balance at December 31, 2003	\$ 1,022	\$ 46,654	\$ (1,821)	\$ 45,855
Net income		558		558
Capital stock/participation certificates issued	16			16
Capital stock/participation certificates retired	(18)			(18)
Balance at March 31, 2004	<u>\$ 1,020</u>	<u>\$ 47,212</u>	<u>\$ (1,821)</u>	<u>\$ 46,411</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, 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	\$ 6,498
(Reversal of) provision for loan losses	—
Recoveries, net of loans charged off	—
Balance at 3-31-03	<u>\$ 6,498</u>
Balance at 12-31-03	\$ 5,983
(Reversal of) provision for loan losses	—
Recoveries, net of loans charged off	—
Balance at 3-31-04	<u>\$ 5,983</u>

NOTE 3 – 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 4 – 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 Plan.

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 three months ended March 31, 2004:

	For the three months ended March 31,	
	2004	2003
Service cost	\$ 12	\$ 10
Interest cost	42	41
Amortization of net (gain) loss	11	9
Recognized net actuarial (gain) loss	16	14
Net periodic benefit cost	<u>\$ 81</u>	<u>\$ 74</u>

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	\$ 94	\$ 107
Thrift	16	14
Other postretirement benefits	81	74
Total	<u>\$ 191</u>	<u>\$ 195</u>