FEDERAL AGRICULTURAL MORTGAGE CORP
Form 10-Q
May 10, 2011
As filed with the Securities and Exchange Commission on May 10, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2011

Commission File Number 001-14951

FEDERAL AGRICULTURAL MORTGAGE CORPORATION
(Exact name of registrant as specified in its charter)

Federally chartered instrumentality of the United States	52-1578738
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification number)
1133 Twenty-First Street, N.W., Suite 600 Washington, D.C.	20036
(Address of principal executive offices)	(Zip code)

(202) 872-7700
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

As of May 2, 2011 the registrant had 1,030,780 shares of Class A Voting Common Stock, 500,301 shares of Class B Voting Common Stock and 8,812,500 shares of Class C Non-Voting Common Stock outstanding.

PART I - FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

The following information concerning Farmer Mac's interim unaudited condensed consolidated financial statements is included in this report beginning on the pages listed below:

FEDERAL AGRICULTURAL MORTGAGE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(unaudited)

	March 31, 2011	December 31, 2010
	(in thousands)	
Assets:		
Cash and cash equivalents	$779,443	$ 729,920
Investment securities:		
Available-for-sale, at fair value	1,976,522	1,677,233
Trading, at fair value	88,046	86,096
Total investment securities	2,064,568	1,763,329
Farmer Mac Guaranteed Securities:		
Available-for-sale, at fair value	2,909,914	2,907,264
USDA Guaranteed Securities:		
Available-for-sale, at fair value	1,063,540	1,005,679
Trading, at fair value	274,561	311,765
Total USDA Guaranteed Securities	1,338,101	1,317,444
Loans:		
Loans held for sale, at lower of cost or fair value	408,355	1,212,065
Loans held for investment, at amortized cost	1,093,559	90,674
Loans held for investment in consolidated trusts, at amortized cost	1,214,249	1,265,663
Allowance for loan losses	(11,084)	(9,803)
Total loans, net of allowance	2,705,079	2,558,599
Real estate owned, at lower of cost or fair value	2,881	1,992
Financial derivatives, at fair value	39,449	41,492
Interest receivable	65,576	90,295
Guarantee and commitment fees receivable	31,916	34,752
Deferred tax asset, net	12,735	14,530
Prepaid expenses and other assets	5,950	20,297
Total Assets	$9,955,612	$ 9,479,914
Liabilities and Equity:		
Liabilities:		
Notes payable:		
Due within one year	$4,626,382	$ 4,509,419
Due after one year	3,806,727	3,430,656
Total notes payable	8,433,109	7,940,075
Debt securities of consolidated trusts held by third parties	781,971	827,411
Financial derivatives, at fair value	97,820	113,687
Accrued interest payable	42,855	57,131
Guarantee and commitment obligation	28,668	30,308
Accounts payable and accrued expenses	74,368	22,113
Reserve for losses	8,378	10,312

Total Liabilities	9,467,169	9,001,037
Commitments and Contingencies (Note 5)		
Equity:		
Preferred stock:		
Series C, par value $1,000 per share, 100,000 shares authorized, 57,578 shares issued and outstanding	57,578	57,578
Common stock:		
Class A Voting, $1 par value, no maximum authorization, 1,030,780 shares outstanding	1,031	1,031
Class B Voting, $1 par value, no maximum authorization, 500,301 shares outstanding	500	500
Class C Non-Voting, $1 par value, no maximum authorization, 8,770,092 shares outstanding as of March 31, 2011 and 8,752,711 shares outstanding as of December 31, 2010	8,770	8,753
Additional paid-in capital	100,450	100,050
Accumulated other comprehensive income	9,616	18,275
Retained earnings	68,645	50,837
Total Stockholders' Equity	246,590	237,024
Non-controlling interest - preferred stock	241,853	241,853
Total Equity	488,443	478,877
Total Liabilities and Equity	$9,955,612	$ 9,479,914

See accompanying notes to condensed consolidated financial statements.

FEDERAL AGRICULTURAL MORTGAGE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)

	For the Three Months Ended March 31, 2011	March 31, 2010
	(in thousands, except per share amounts)	
Interest income:		
Investments and cash equivalents	$ 7,187	$ 6,483
Farmer Mac Guaranteed Securities and USDA Guaranteed Securities	27,775	20,831
Loans	29,110	33,418
Total interest income	64,072	60,732
Total interest expense	37,053	37,115
Net interest income	27,019	23,617
Provision for loan losses	(1,281)	(2,850)
Net interest income after provision for loan losses	25,738	20,767
Non-interest income:		
Guarantee and commitment fees	6,387	5,919
Gains/(losses) on financial derivatives	4,005	(5,804)
Gains on trading assets	1,311	3,367
Gains on sale of available-for-sale investment securities	157	240
Gains on sale of real estate owned	97	-
Lower of cost or fair value adjustment on loans held for sale	(808)	(2,274)
Other income	3,898	829
Non-interest income	15,047	2,277
Non-interest expense:		
Compensation and employee benefits	4,497	3,511
General and administrative	2,256	2,503
Regulatory fees	591	563
Real estate owned operating costs, net	368	10
Release of reserve for losses	(1,934)	(1,468)
Other expense	900	-
Non-interest expense	6,678	5,119
Income before income taxes	34,107	17,925
Income tax expense	9,517	4,336
Net income	24,590	13,589
Less: Net income attributable to non-controlling interest - preferred stock dividends	(5,547)	(4,068)
Net income attributable to Farmer Mac	19,043	9,521
Preferred stock dividends	(720)	(1,970)
Loss on retirement of preferred stock	-	(5,784)
Net income available to common stockholders	$ 18,323	$ 1,767
Earnings per common share and dividends:		
Basic earnings per common share	$ 1.78	$ 0.17
Diluted earnings per common share	$ 1.72	$ 0.17

Common stock dividends per common share	$ 0.05	$ 0.05

See accompanying notes to condensed consolidated financial statements.

FEDERAL AGRICULTURAL MORTGAGE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(unaudited)

	For the Three Months Ended			
	March 31, 2011		March 31, 2010	
	Shares	Amount	Shares	Amount
	(in thousands)			
Preferred stock:				
Balance, beginning of period	58	$57,578	58	$57,578
Issuance of Series C preferred stock	-	-	-	-
Balance, end of period	58	$57,578	58	$57,578
Common stock:				
Balance, beginning of period	10,284	$10,284	10,142	$10,142
Issuance of Class C common stock	15	15	2	2
Exercise of stock options and SARs	2	2	-	-
Balance, end of period	10,301	$10,301	10,144	$10,144
Additional paid-in capital:				
Balance, beginning of period		$100,050		$97,090
Stock-based compensation expense		715		760
Issuance of Class C common stock		7		11
Exercise, vesting and cancellation of stock options, SARs and restricted stock		(322)		-
Balance, end of period		$100,450		$97,861
Retained earnings:				
Balance, beginning of period		$50,837		$28,127
Net income attributable to Farmer Mac		19,043		9,521
Cash dividends:				
Preferred stock, Series B ($8.33 per share)		-		(1,250)
Preferred stock, Series C ($12.50 per share)		(720)		(720)
Common stock ($0.05 per share)		(515)		(507)
Loss on retirement of preferred stock		-		(5,784)
Cumulative effect of adoption of new accounting standard, net of tax		-		2,679
Balance, end of period		$68,645		$32,066
Accumulated other comprehensive income:				
Balance, beginning of period		$18,275		$3,254
Change in unrealized (loss)/gain on available-for-sale securities, net of tax and reclassification adjustments		(8,659)		4,310
Change in unrealized gain on financial derivatives, net of tax and reclassification adjustments		-		23
Balance, end of period		$9,616		$7,587
Total Stockholders' Equity		$246,590		$205,236
Non-controlling interest:				
Balance, beginning of period		$241,853		$-
Preferred stock - Farmer Mac II LLC		-		241,853
Balance, end of period		$241,853		$241,853
Total Equity		$488,443		$447,089

Comprehensive income:		
Net income	$24,590	$13,589
Change in accumulated other comprehensive income, net of tax	(8,659)	4,333
Comprehensive income	15,931	17,922
Less: Comprehensive income attributable to non-controlling interest	5,547	4,068
Total comprehensive income	$10,384	$13,854

See accompanying notes to condensed consolidated financial statements.

FEDERAL AGRICULTURAL MORTGAGE CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	For the Three Months Ended March 31, 2011	March 31, 2010 (restated)
	(in thousands)	
Cash flows from operating activities:		
Net income	$24,590	$ 13,589
Adjustments to reconcile net income to net cash provided by/(used in) operating activities:		
Net amortization of premiums and discounts on loans, investments, and Farmer Mac Guaranteed Securities and USDA Guaranteed Securities	4,294	1,632
Amortization of debt premiums, discounts and issuance costs	2,790	1,362
Net change in fair value of trading securities, financial derivatives and loans held for sale	(15,135)	(6,262)
Amortization of deferred gains on certain Farmer Mac Guaranteed Securities and USDA Guaranteed Securities	(3,081)	-
Gains on the sale of available-for-sale investment securities	(157)	(240)
Gains on the sale of real estate owned	(97)	-
Total (release)/provision for losses	(653)	1,382
Deferred income taxes	5,786	289
Stock-based compensation expense	715	760
Proceeds from repayment and sale of trading investment securities	382	236
Purchases of loans held for sale	(80,517)	(127,740)
Proceeds from repayment of loans held for sale	35,892	10,195
Net change in:		
Interest receivable	24,719	2,384
Guarantee and commitment fees receivable	2,836	20,821
Other assets	15,342	15,956
Accrued interest payable	(14,276)	7,968
Other liabilities	(349)	(19,931)
Net cash provided by/(used in) operating activities	3,081	(77,599)
Cash flows from investing activities:		
Purchases of available-for-sale investment securities	(658,512)	(284,149)
Purchases of Farmer Mac Guaranteed Securities and USDA Guaranteed Securities	(617,370)	(93,197)
Purchases of loans held for investment	(215,867)	(9,226)
Purchases of defaulted loans	(16,925)	(2,490)
Proceeds from repayment of available-for-sale investment securities	336,681	57,766
Proceeds from repayment of Farmer Mac Guaranteed Securities and USDA Guaranteed Securities	572,505	56,912
Proceeds from repayment of loans held for investment	127,693	107,232
Proceeds from sale of available-for-sale investment securities	78,573	69,175
Proceeds from sale of trading securities - fair value option	-	5,013
Proceeds from sale of Farmer Mac Guaranteed Securities	7,363	7,487
Proceeds from sale of real estate owned	305	-
Net cash used in investing activities	(385,554)	(85,477)
Cash flows from financing activities:		

Proceeds from issuance of discount notes	17,036,947	14,970,627
Proceeds from issuance of medium-term notes	616,503	339,653
Payments to redeem discount notes	(17,021,207)	(15,099,610)
Payments to redeem medium-term notes	(142,000)	(296,590)
Excess tax benefits related to stock-based awards	394	-
Payments to third parties on debt securities of consolidated trusts	(51,839)	(72,971)
Proceeds from common stock issuance	(20)	13
Issuance costs on retirement of preferred stock	-	(5,784)
Proceeds from preferred stock issuance - Farmer Mac II LLC	-	241,853
Retirement of Series B preferred stock	-	(144,216)
Dividends paid - non-controlling interest - preferred stock	(5,547)	(4,005)
Dividends paid on common and preferred stock	(1,235)	(2,477)
Net cash provided by/(used in) financing activities	431,996	(73,507)
Net increase/(decrease) in cash and cash equivalents	49,523	(236,583)
Cash and cash equivalents at beginning of period	729,920	654,794
Cash and cash equivalents at end of period	$ 779,443	$ 418,211

See accompanying notes to condensed consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

Note 1. Accounting Policies

The interim unaudited condensed consolidated financial statements of the Federal Agricultural Mortgage Corporation ("Farmer Mac" or the "Corporation") and subsidiaries have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). These interim unaudited condensed consolidated financial statements reflect all normal and recurring adjustments that are, in the opinion of management, necessary to present a fair statement of the financial position and the results of operations and cash flows of Farmer Mac and subsidiaries for the interim periods presented. Certain information and footnote disclosures normally included in the annual consolidated financial statements have been condensed or omitted as permitted by SEC rules and regulations. On May 10, 2011, Farmer Mac filed with the SEC a report on Form 8-K advising that its 2010 and 2009 consolidated financial statements and its condensed consolidated financial statements for the nine months ended September 30, 2010 and 2009 and for the six months ended June 30, 2010 and 2009 should no longer be relied upon because of incorrect classifications of proceeds from the repayments of certain loans between operating and investing activities on the consolidated statements of cash flows. These misclassifications have no impact on Farmer Mac's previously issued condensed consolidated interim or annual consolidated balance sheets, statements of operations or statements of changes in equity and do not affect core earnings, core capital, minimum capital surplus, or total cash flow. See Note 1(a) for further information. The December 31, 2010 condensed consolidated balance sheet presented in this report has been derived from the Corporation's 2010 consolidated financial statements. Management believes that the disclosures are adequate to present fairly the condensed consolidated financial statements as of the dates and for the periods presented. These interim unaudited condensed consolidated financial statements should be read in conjunction with the 2010 consolidated financial statements of Farmer Mac and subsidiaries included in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2010 filed with the SEC on March 16, 2011. Results for interim periods are not necessarily indicative of those that may be expected for the fiscal year. Below is a summary of Farmer Mac's significant accounting policies.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Farmer Mac and its two subsidiaries: (1) Farmer Mac Mortgage Securities Corporation ("FMMSC"), whose principal activities are to facilitate the purchase and issuance of Farmer Mac Guaranteed Securities and to act as a registrant under registration statements filed with the Securities and Exchange Commission, and (2) Farmer Mac II LLC, whose principal activity is the operation of substantially all of the business related to the Farmer Mac II program – primarily the acquisition of USDA-guaranteed portions. Farmer Mac II LLC was formed as a Delaware limited liability company on December 10, 2009. The business operations of Farmer Mac II LLC began in January 2010. The condensed consolidated financial statements also include the accounts of variable interest entities ("VIEs") in which Farmer Mac determined itself to be the primary beneficiary. See Note 2(g) for more information on consolidated VIEs.

A Farmer Mac guarantee of timely payment of principal and interest is an explicit element of the terms of all Farmer Mac Guaranteed Securities. When Farmer Mac retains such securities in its portfolio, that guarantee is not extinguished. For Farmer Mac Guaranteed Securities in the Corporation's portfolio, Farmer Mac has entered into guarantee arrangements with FMMSC. The guarantee fee rate established between Farmer Mac and FMMSC is an element in determining the fair value of these Farmer Mac Guaranteed Securities, and guarantee fees related to these securities are reflected in guarantee and commitment fees in the condensed consolidated statements of operations. These guarantee fees totaled $2.0 million in the first quarter 2011, compared to $1.7 million in first quarter 2010. The corresponding expense of FMMSC has been eliminated against interest income in consolidation. All other inter-company balances and transactions have been eliminated in consolidation.

(a) Cash and Cash Equivalents and Statements of Cash Flows

Farmer Mac considers highly liquid investment securities with maturities at the time of purchase of three months or less to be cash equivalents. The carrying value of cash and cash equivalents is a reasonable estimate of their fair value. Changes in the balance of cash and cash equivalents are reported in the condensed consolidated statements of cash flows. The following table sets forth information regarding certain cash and non-cash transactions for the three months ended March 31, 2011 and 2010.

	For the Three Months Ended	
	March 31, 2011	March 31, 2010
	(in thousands)	
Cash paid during the period for:		
Interest	$ 26,763	$ 18,799
Income taxes	1,000	1,500
Non-cash activity:		
Real estate owned acquired through loan liquidation	1,460	2,393
Loans acquired and securitized as loans held for investment in consolidated trusts	6,399	763
Purchases of investment securities traded, not yet settled	50,345	-
Consolidation of Farmer Mac I Guaranteed Securities from off-balance sheet to loans held for investment in consolidated trusts	6,399	1,400,371
Consolidation of Farmer Mac I Guaranteed Securities from off-balance sheet to debt securities of consolidated trusts held by third parties	6,399	1,400,371
Transfers of available-for-sale Farmer Mac I Guaranteed Securities to loans held for investment in consolidated trusts, upon the adoption of new consolidation guidance	-	5,385
Transfers of trading Farmer Mac Guaranteed Securities - Rural Utilities to loans held for investment in consolidated trusts, upon the adoption of new consolidation guidance	-	451,448
Transfers of loans held for sale to loans held for investment	878,798	-

Effective January 1, 2011, Farmer Mac transferred $878.8 million of loans in the Farmer Mac I program from held for sale to held for investment because Farmer Mac no longer has the intent to securitize or sell these loans in the foreseeable future. Farmer Mac transferred these loans at their cost, which was lower than the estimated fair value at the time of transfer.

At the time of purchase, loans are classified as either held for sale or held for investment depending upon management's intent and ability to hold the loans for the foreseeable future. On two occasions, once in first quarter 2009 and again in first quarter 2011, consistent with a change in management's intent, Farmer Mac reclassified loans from one classification to the other on the balance sheet. Historically, cash receipts from the repayment of loans were classified within the statements of cash flows consistent with the then current balance sheet classification as opposed to the original balance sheet classification assigned based on management's intent upon purchase of the loan, as prescribed by accounting guidance related to the statement of cash flows. As a result of these incorrect classifications, Farmer Mac will restate its previously issued interim condensed consolidated statements of cash flows for the six and nine month periods ended June 30, and September 30, 2009 and 2010, respectively, and its consolidated statements of cash flows for the years ended December 31, 2009 and 2010 by amending its Annual Report on Form 10-K for the year ended December 31, 2010, which will include the interim periods, subsequent to this filing but as soon as practicable. These corrections have no impact on Farmer Mac's previously issued condensed consolidated interim or annual consolidated balance sheets, statements of operations or statements of changes in equity and do not affect core earnings, core capital, minimum capital surplus, or total cash flow. For each of the six, nine and twelve month periods ended June 30, September 30, and December 31, 2009, respectively, the impact of the restatement will increase net cash provided by operating activities by $65.0 million, $46.7 million and $42.2 million, respectively, with offsetting increases in net cash used in investing activities. For each of the six, nine, and twelve month periods ended June 30, September 30, and December 31, 2010, respectively, the impact of the restatement will increase net cash used in operating activities by $31.6 million, $50.5 million, and $54.6 million, respectively, with offsetting decreases in cash used in investing activities. The condensed consolidated statement of cash flows for the three months ended March 31, 2010 has been restated in this Form 10-Q to reflect increased net cash used in operating activities of $22.8 million offset by decreased net cash used in investing activities.

(b) Allowance for Losses

Farmer Mac maintains an allowance for losses to cover estimated probable losses on loans held ("allowance for loan losses") and loans underlying Long Term Standby Purchase Commitments ("LTSPCs") and Farmer Mac Guaranteed Securities ("reserve for losses") based on available information. Farmer Mac's methodology for determining the allowance for losses separately considers its portfolio segments - Farmer Mac I, Farmer Mac II, and Rural Utilities, and disaggregates its analysis, where relevant, into classes of financing receivables, which currently include loans and AgVantage securities. Further disaggregation to commodity type is performed, where appropriate, in analyzing the need for an allowance for losses.

The allowance for losses is increased through periodic provisions for loan losses that are charged against net interest income and provisions for losses that are charged to non-interest expense and are reduced by charge-offs for actual losses, net of recoveries. Negative provisions, or releases of allowance for losses, are recorded in the event that the estimate of probable losses as of the end of a period is lower than the estimate at the beginning of the period.

The total allowance for losses consists of a general allowance for losses and a specific allowance for impaired loans.

General Allowance for Losses

Farmer Mac I

Farmer Mac's methodology for determining its allowance for losses incorporates the Corporation's automated loan classification system. That system scores loans based on criteria such as historical repayment performance, indicators of current financial condition, loan seasoning, loan size and loan-to-value ratio. For the purposes of the loss allowance methodology, the loans in the Farmer Mac I portfolio and loans underlying Farmer Mac I Guaranteed Securities and LTSPCs have been scored and classified for each calendar quarter since first quarter 2000. The allowance methodology captures the migration of loan scores across concurrent and overlapping three-year time horizons and calculates loss rates separately within each loan classification for (1) loans underlying LTSPCs and (2) loans held and loans underlying Farmer Mac I Guaranteed Securities. The calculated loss rates are applied to the current classification distribution of unimpaired loans in Farmer Mac's portfolio to estimate inherent losses, on the assumption that the historical credit losses and trends used to calculate loss rates will continue in the future. Management evaluates this assumption by taking into consideration factors, including:

- economic conditions;
- geographic and agricultural commodity/product concentrations in the portfolio;
- the credit profile of the portfolio;
- delinquency trends of the portfolio;
- historical charge-off and recovery activities of the portfolio; and
- other factors to capture current portfolio trends and characteristics that differ from historical experience.

Management believes that its use of this methodology produces a reasonable estimate of probable losses, as of the balance sheet date, for all loans held in the Farmer Mac I portfolio and loans underlying Farmer Mac I Guaranteed Securities and LTSPCs. There were no purchases or sales during first quarter 2011 that materially affected the credit profile of the Farmer Mac I portfolio.

Farmer Mac has not provided an allowance for losses for loans underlying Farmer Mac I AgVantage securities. Each AgVantage security is a general obligation of an issuing institution approved by Farmer Mac and is collateralized by eligible loans in an amount at least equal to the outstanding principal amount of the security, with some level of overcollateralization also required for Farmer Mac I AgVantage securities. Farmer Mac excludes the loans that secure AgVantage securities from the credit risk metrics it discloses because of the credit quality of the issuing institutions, the collateralization level for the securities, and because delinquent loans are required to be removed from the pool of pledged loans and replaced with current eligible loans.

Farmer Mac II

No allowance for losses has been provided for USDA Guaranteed Securities or Farmer Mac II Guaranteed Securities. The portions of loans (the "USDA-guaranteed portions") guaranteed by the U.S. Department of Agriculture ("USDA") presented as "USDA Guaranteed Securities" on the condensed consolidated balance sheets, as well as those that collateralize Famer Mac II Guaranteed Securities, are guaranteed by the USDA. Each USDA guarantee is an obligation backed by the full faith and credit of the United States. Farmer Mac excludes these guaranteed portions from the credit risk metrics it discloses because of the USDA guarantee.

Rural Utilities

Farmer Mac separately evaluates the rural utilities loans it owns, as well as the lender obligations and loans underlying or securing its Farmer Mac Guaranteed Securities – Rural Utilities, including AgVantage securities, to determine if there are probable losses inherent in those assets. Each AgVantage security is a general obligation of an issuing institution approved by Farmer Mac and is collateralized by eligible loans in an amount at least equal to the outstanding principal amount of the security. No allowance for losses has been provided for this portfolio segment based on the credit quality of the collateral supporting rural utilities assets and Farmer Mac's counterparty risk analysis. As of March 31, 2011, there were no delinquencies and no probable losses inherent in Farmer Mac's rural utilities loans held or in any Farmer Mac Guaranteed Securities – Rural Utilities.

Specific Allowance for Impaired Loans

Farmer Mac also analyzes assets in its portfolio for impairment in accordance with the Financial Accounting Standards Board ("FASB") standard on measuring individual impairment of a loan. Farmer Mac's impaired assets include:

- non-performing assets (loans 90 days or more past due, in foreclosure, restructured, in bankruptcy – including loans performing under either their original loan terms or a court-approved bankruptcy plan);
- loans for which Farmer Mac has adjusted the timing of borrowers' payment schedules, but still expects to collect all amounts due and has not made economic concessions; and
- additional performing loans that have previously been delinquent or are secured by real estate that produces agricultural commodities or products currently under stress.

For loans with an updated appraised value, other updated collateral valuation or management's estimate of discounted collateral value, this analysis includes the measurement of the fair value of the underlying collateral for individual loans relative to the total recorded investment, including principal, interest and advances and net of any charge-offs. In the event that the collateral value does not support the total recorded investment, Farmer Mac provides an allowance for the loan for the difference between the recorded investment and its fair value, less estimated costs to liquidate the collateral. For the remaining impaired assets without updated valuations, this analysis is performed in the aggregate in consideration of the similar risk characteristics of the assets and historical statistics.

As of March 31, 2011 and 2010, Farmer Mac's specific allowances for losses were $7.5 million and $2.4 million, respectively.

Allowance for Losses

The following is a summary of the changes in the allowance for losses for three months ended March 31, 2011 and 2010:

	For the Three Months Ended					
	March 31, 2011			March 31, 2010		
	Allowance for Loan Losses	Reserve for Losses	Total Allowance for Losses	Allowance for Loan Losses	Reserve for Losses	Total Allowance for Losses
	(in thousands)					
Beginning Balance	$9,803	$10,312	$20,115	$6,292	$7,895	$14,187
Provision/(recovery) for losses	1,281	(1,934)	(653)	2,850	(1,468)	1,382
Charge-offs	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-
Ending Balance	$11,084	$8,378	$19,462	$9,142	$6,427	$15,569

During first quarter 2011, Farmer Mac recorded provisions to its allowance for loan losses of $1.3 million and releases from its reserve for losses of $1.9 million. In first quarter 2011, Farmer Mac purchased two defaulted loans pursuant to the terms of an LTSPC agreement. This resulted in the reclassification of $1.8 million of specific allowance, which had been recorded in fourth quarter 2010, from the reserve for losses to the allowance for loan losses. The provision/(recovery) for losses for first quarter 2011 reflects this reclassification as well as a decline in estimated probable losses related to Farmer Mac's exposure to the ethanol industry.

During first quarter 2010, upon the adoption of new accounting guidance on consolidation on January 1, 2010, Farmer Mac reclassified $2.0 million from the reserve for losses to the allowance for loan losses as a result of Farmer Mac being determined the primary beneficiary of certain VIEs with beneficial interests owned by third party investors. The provision/(recovery) for losses for first quarter 2010 reflects this reclassification as well as provisions to its allowance for loan losses of $0.9 million and provisions to its reserve for losses of $0.5 million. Prior to the adoption of this guidance, Farmer Mac classified these interests as off-balance sheet Farmer Mac I Guaranteed Securities.

Farmer Mac's reserve for losses for off-balance sheet Farmer Mac I Guaranteed Securities and LTSPCs as of March 31, 2011 were $0.6 million and $7.8 million, respectively, compared to $0.6 million and $9.7 million, respectively as of December 31, 2010.

The following tables present the ending balances of Farmer Mac I loans held and loans underlying LTSPCs and Farmer Mac I Guaranteed Securities and the related allowance for losses by impairment method and commodity type as of March 31, 2011 and December 31, 2010.

	As of March 31, 2011						
	Crops	Permanent Plantings	Livestock	Part-time Farm	AgStorage and Processing (including ethanol facilities)	Other	Total
	(in thousands)						
Ending Balance							
Evaluated collectively for impairment	$ 1,732,773	$ 819,134	$ 1,153,805	$ 275,628	$ 226,131	$ 21,173	$ 4,228,644
Evaluated individually for impairment	29,260	29,672	12,789	7,170	6,553	240	85,684
	$ 1,762,033	$ 848,806	$ 1,166,594	$ 282,798	$ 232,684	$ 21,413	$ 4,314,328
Allowance for Losses							
Beginning balance	$ 3,572	$ 3,537	$ 2,749	$ 445	$ 9,797	$ 15	$ 20,115
Provision/(recovery) for losses	350	265	(899)	608	(974)	(3)	(653)
Charge-offs	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-
Ending balance	$ 3,922	$ 3,802	$ 1,850	$ 1,053	$ 8,823	$ 12	$ 19,462
Evaluated collectively for impairment	$ 1,645	$ 1,209	$ 1,320	$ 760	$ 6,973	$ 11	$ 11,918
Evaluated individually for impairment	2,277	2,593	530	293	1,850	1	7,544
	$ 3,922	$ 3,802	$ 1,850	$ 1,053	$ 8,823	$ 12	$ 19,462

	As of December 31, 2010						
	Crops	Permanent Plantings	Livestock	Part-time Farm	AgStorage and Processing (including ethanol facilities)	Other	Total
	(in thousands)						
Ending Balance							
Evaluated collectively for impairment	$ 1,699,477	$ 835,254	$ 1,130,466	$ 282,400	$ 239,933	$ 22,514	$ 4,210,044
Evaluated individually for impairment	31,903	30,221	15,992	8,745	6,790	425	94,076
	$ 1,731,380	$ 865,475	$ 1,146,458	$ 291,145	$ 246,723	$ 22,939	$ 4,304,120
Allowance for Losses							
	$ 1,499	$ 783	$ 2,236	$ 222	$ 7,947	$ 13	$ 12,700

Evaluated collectively for impairment							
Evaluated individually for impairment	2,073	2,754	513	223	1,850	2	7,415
	$ 3,572	$ 3,537	$ 2,749	$ 445	$ 9,797	$ 15	$ 20,115

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Farmer Mac recognized interest income of approximately $0.8 million and $0.5 million on impaired loans during the three months ended March 31, 2011 and 2010, respectively. During first quarter 2011 and 2010, Farmer Mac's average investment in impaired loans was $87.7 million and $92.6 million, respectively.

The following tables present by commodity type the unpaid principal balances, recorded investment and specific allowance for losses related to impaired loans and the recorded investment in loans on nonaccrual status as of March 31, 2011 and December 31, 2010 and the average recorded investment and interest income recognized on impaired loans as of March 31, 2011.

	As of March 31, 2011						
	Crops	Permanent Plantings	Livestock	Part-time Farm	AgStorage and Processing (including ethanol facilities)	Other	Total
	(in thousands)						
Impaired Loans:							
With no specific allowance:							
Recorded investment	$ 13,850	$ 10,510	$ 7,240	$ 859	$ -	$ 117	$ 32,576
Unpaid principal balance	15,954	11,017	7,445	945	-	116	35,477
With a specific allowance:							
Recorded investment	13,627	17,674	5,471	6,292	6,600	125	49,789
Unpaid principal balance	13,306	18,655	5,344	6,225	6,553	124	50,207
Associated allowance	2,277	2,593	530	293	1,850	1	7,544
Total:							
Recorded investment	27,477	28,184	12,711	7,151	6,600	242	82,365
Unpaid principal balance	29,260	29,672	12,789	7,170	6,553	240	85,684
Associated allowance	2,277	2,593	530	293	1,850	1	7,544
Average recorded investment in impaired loans	29,452	28,841	14,318	7,995	6,720	336	87,662
Income recognized on impaired loans	156	27	217	41	382	-	823
Recorded investment of loans on Nonaccrual status:	11,756	24,348	3,490	4,987	-	-	44,581

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	As of December 31, 2010						
	Crops	Permanent Plantings	Livestock	Part-time Farm (in thousands)	AgStorage and Processing (including ethanol facilities)	Other	Total
Impaired Loans:							
With no specific allowance:							
Recorded investment	$ 16,015	$ 10,549	$ 6,873	$ 1,050	$ -	$ -	$ 34,487
Unpaid principal balance	17,274	10,895	7,087	1,072	-	-	36,328
With a specific allowance:							
Recorded investment	15,414	18,949	9,052	7,788	6,839	430	58,472
Unpaid principal balance	14,630	19,326	8,905	7,672	6,790	425	57,748
Associated allowance	2,073	2,754	513	223	1,850	2	7,415
Total:							
Recorded investment	31,429	29,498	15,925	8,838	6,839	430	92,959
Unpaid principal balance	31,904	30,221	15,992	8,744	6,790	425	94,076
Associated allowance	2,073	2,754	513	223	1,850	2	7,415
Recorded Investment of Loans on Nonaccrual Status:	$ 13,828	$ 8,793	$ 3,267	$ 4,380	$ 8,796	$ -	$ 39,064

In accordance with the terms of all applicable trust agreements, Farmer Mac generally acquires all loans that collateralize Farmer Mac Guaranteed Securities that become and remain either 90 or 120 days or more past due (depending on the provisions of the applicable agreement) on the next subsequent loan payment date. In accordance with the terms of all LTSPCs, Farmer Mac acquires loans that are either 90 days or 120 days delinquent (depending on the provisions of the applicable agreement) upon the request of the counterparty.

Farmer Mac records all such defaulted loans at their unpaid principal balance during the period in which Farmer Mac becomes entitled to purchase the loans and therefore regains effective control over the transferred loans.

During first quarter 2011, Farmer Mac purchased 8 defaulted loans having an unpaid principal balance of $16.9 million from pools underlying Farmer Mac I Guaranteed Securities and LTSPCs. During first quarter 2010, Farmer Mac purchased 5 defaulted loans having a principal balance of $2.5 million from pools underlying Farmer Mac I Guaranteed Securities and LTSPCs. The following table presents Farmer Mac's purchases of defaulted loans underlying Farmer Mac I Guaranteed Securities and LTSPCs.

	For the Three Months Ended	
	March 31, 2011	March 31, 2010

		(in thousands)		
Defaulted loans purchased underlying off-balance sheet Farmer Mac I				
Guaranteed Securities		1,369		2,323
Defaulted loans purchased underlying LTSPCs		15,556		167
Total loan purchases	$	16,925	$	2,490

Credit Quality Indicators

The following tables present credit quality indicators related to Farmer Mac I loans held and loans underlying LTSPCs and Farmer Mac I Guaranteed Securities (excluding AgVantage securities) as of March 31, 2011 and December 31, 2010. Farmer Mac uses 90-day delinquency information to evaluate its credit risk exposure on these assets because historically it has been the best measure of borrower credit quality deterioration. Most of the Farmer Mac I loans held and underlying LTSPCs and Farmer Mac I Guaranteed Securities have annual (January 1) or semi-annual (January 1 and July 1) payment dates and are supported by less frequent and less predictable revenue sources, such as the cash flows generated from the maturation of crops, sales of livestock and government farm support programs. Taking into account the reduced frequency of payment due dates and revenue sources, Farmer Mac considers the 90-day delinquency point to be the most significant observation point when evaluating its credit risk exposure.

	As of March 31, 2011						
	Crops	Permanent Plantings	Livestock	Part-time Farm	AgStorage and Processing (including ethanol facilities)	Other	Total
	(in thousands)						
Credit risk profile by internally assigned grade (1)							
Grade:							
Acceptable	$ 1,660,846	$ 778,460	$ 1,003,739	$ 259,363	$ 113,369	$ 18,746	$ 3,834,523
Other assets especially mentioned ("OAEM") (2)	55,386	21,460	99,590	9,755	76,276	1,298	263,765
Substandard (2)	45,801	48,886	63,265	13,680	43,039	1,369	216,040
Total	$ 1,762,033	$ 848,806	$ 1,166,594	$ 282,798	$ 232,684	$ 21,413	$ 4,314,328
Commodity analysis of past due loans (1)							
Greater than 90 days	$ 23,890	$ 22,730	$ 6,975	$ 3,093	$ -	$ 636	$ 57,324
In bankruptcy and REO	4,519	4,692	1,379	1,792	-	-	12,382
Total non-performing	$ 28,409	$ 27,422	$ 8,354	$ 4,885	$ -	$ 636	$ 69,706

(1) Amounts represent unpaid principal balance of risk-rated loans, which is the basis Farmer Mac uses to analyze its Farmer Mac I portfolio, and recorded investment of past due loans. Amounts include real estate owned, at lower of cost or fair value less estimated selling costs, of $2.9 million.

(2) Assets in the OAEM category generally have potential weaknesses due to performance issues but are currently considered to be adequately secured. Substandard assets have a well-defined weakness or weaknesses and there is a distinct possibility that some loss will be sustained if deficiencies are not corrected.

	As of December 31, 2010			
	Permanent		Part-time	AgStorage and Processing (including ethanol

	Crops	Plantings	Livestock	Farm	facilities)	Other	Total
				(in thousands)			
Credit risk profile by internally assigned grade (1)							
Grade:							
Acceptable	$ 1,625,995	$ 792,061	$ 993,542	$ 268,111	$ 116,248	$ 20,321	$ 3,816,278
Other assets especially mentioned ("OAEM")(2)	59,768	17,112	86,500	9,652	76,947	639	250,618
Substandard(2)	45,617	56,302	66,416	13,382	53,528	1,979	237,224
Total	$ 1,731,380	$ 865,475	$ 1,146,458	$ 291,145	$ 246,723	$ 22,939	$ 4,304,120
Commodity analysis of past due loans (1)							
Greater than 90 days	$ 21,423	$ 26,312	$ 7,177	$ 3,803	$ 10,892	$ 641	$ 70,248
In bankruptcy and REO	4,886	3,712	1,395	1,537	-	-	11,530
Total non-performing	$ 26,309	$ 30,024	$ 8,572	$ 5,340	$ 10,892	$ 641	$ 81,778

(1) Amounts represent unpaid principal balance of risk-rated loans, which is the basis Farmer Mac uses to analyze its Farmer Mac I portfolio, and recorded investment of past due loans. Amounts include real estate owned, at lower of cost or fair value less estimated selling costs, of $2.0 million.

(2) Assets in the OAEM category generally have potential weaknesses due to performance issues but are currently considered to be adequately secured. Substandard assets have a well-defined weakness or weaknesses and there is a distinct possibility that some loss will be sustained if deficiencies are not corrected.

Concentrations of Credit Risk

The following table sets forth the geographic and commodity/collateral diversification, as well as the range of original loan-to-value ratios, for all Farmer Mac I loans held and loans underlying Farmer Mac I Guaranteed Securities (excluding AgVantage securities) and LTSPCs as of March 31, 2011 and December 31, 2010:

	As of March 31, 2011	As of December 31, 2010
	(in thousands)	
By commodity/collateral type:		
Crops	$ 1,762,033	$ 1,731,380
Permanent plantings	848,806	865,475
Livestock	1,166,594	1,146,458
Part-time farm	282,798	291,145
AgStorage and processing (including ethanol facilities)	232,684	246,723
Other	21,413	22,939
Total	$ 4,314,328	$ 4,304,120
By geographic region (1):		
Northwest	$ 728,679	$ 660,845
Southwest	1,599,361	1,626,398
Mid-North	915,699	934,879
Mid-South	519,753	521,294
Northeast	308,956	317,715
Southeast	241,880	242,989
Total	$ 4,314,328	$ 4,304,120
By original loan-to-value ratio:		
0.00% to 40.00%	$ 1,054,957	$ 1,030,580
40.01% to 50.00%	753,240	770,744
50.01% to 60.00%	1,242,452	1,246,675
60.01% to 70.00%	1,068,524	1,056,132
70.01% to 80.00%	151,284	155,363
80.01% to 90.00%	43,871	44,626
Total	$ 4,314,328	$ 4,304,120

(1) Geographic regions: Northwest (AK, ID, MT, ND, NE, OR, SD, WA, WY); Southwest (AZ, CA, CO, HI, NM, NV, UT); Mid-North (IA, IL, IN, MI, MN, MO, WI); Mid-South (KS, OK, TX); Northeast (CT, DE, KY, MA, MD, ME, NC, NH, NJ, NY, OH, PA, RI, TN, VA, VT, WV); Southeast (AL, AR, FL, GA, LA, MS, SC).

The original loan-to-value ratio is calculated by dividing the loan principal balance at the time of guarantee, purchase or commitment by the appraised value at the date of loan origination or, when available, the updated appraised value at the time of guarantee, purchase or commitment. Current loan-to-value ratios may be higher or lower than the original loan-to-value ratios.

(c) Financial Derivatives

Farmer Mac enters into transactions involving financial derivatives principally to protect against risk from the effects of market price or interest rate movements on the value of certain assets, future cash flows or debt issuance, not for trading or speculative purposes. Farmer Mac enters into interest rate swap contracts to adjust the characteristics of its short-term debt to match more closely the cash flow and duration characteristics of its longer-term loans and other assets, and also to adjust the characteristics of its long-term debt to match more closely the cash flow and duration characteristics of its short-term assets, thereby reducing interest rate risk and often times deriving an overall lower effective cost of borrowing than would otherwise be available to Farmer Mac in the conventional debt market. Farmer Mac also recognizes certain contracts and commitments as derivatives when the characteristics of those contracts and commitments meet the definition of a derivative.

Farmer Mac manages the interest rate risk related to loans it has committed to acquire, but has not yet purchased and permanently funded, through the use of forward sale contracts on the debt of other government-sponsored enterprises ("GSEs"), futures contracts involving U.S. Treasury securities and interest rate swap contracts. Farmer Mac uses forward sale contracts on GSE securities to reduce its interest rate exposure to changes in both U.S. Treasury rates and spreads on Farmer Mac debt. The notional amounts of these contracts are determined based on a duration-matched hedge ratio between the hedged item and the hedge instrument. Gains or losses generated by these hedge transactions should offset changes in funding costs.

All financial derivatives are recorded on the balance sheet at fair value as a freestanding asset or liability. Farmer Mac does not designate its financial derivatives as fair value hedges or cash flow hedges; therefore, the changes in the fair values of financial derivatives are reported as gains or losses on financial derivatives in the condensed consolidated statements of operations without any corresponding changes in the fair values of the hedged items.

The following tables summarize information related to Farmer Mac's financial derivatives as of March 31, 2011 and December 31, 2010:

March 31, 2011	Notional Amount	Fair Value Asset	Fair Value (Liability)	Weighted-Average Pay Rate	Weighted-Average Receive Rate	Weighted-Average Forward Price	Weighted-Average Remaining Life (in years)
	(dollars in thousands)						
Interest rate swaps:							
Pay fixed non-callable	$ 1,728,684	$ 6,596	$ (94,526)	3.97 %	0.30 %		4.07
Receive fixed non-callable	3,204,995	33,479	(2,017)	0.43 %	1.29 %		1.46
Receive fixed callable	100,000	54	-	0.22 %	0.48 %		1.07
Basis swaps	419,117	141	(1,692)	0.76 %	0.38 %		1.45
Credit default swaps	30,000	-	(203)	1.00 %	0.00 %		0.81
Agency forwards	28,914	-	(50)			106.01	
Treasury futures	7,300	2	-			119.06	
Credit valuation adjustment	-	(823)	668				
Total financial derivatives	$ 5,519,010	$ 39,449	$ (97,820)				

December 31, 2010	Notional Amount	Fair Value Asset	Fair Value (Liability)	Weighted-Average Pay Rate	Weighted-Average Receive Rate	Weighted-Average Forward Price	Weighted-Average Remaining Life (in years)
	(dollars in thousands)						
Interest rate swaps:							
Pay fixed callable	$ 13,144	$ -	$ (69)	5.11 %	0.29 %		7.12
Pay fixed non-callable	1,275,108	2,814	(108,503)	4.69 %	0.30 %		3.93
Receive fixed non-callable	2,874,534	39,551	(1,828)	0.44 %	1.40 %		1.70
Basis swaps	254,991	52	(3,411)	1.34 %	0.38 %		1.71
Credit default swaps	30,000	-	(216)	1.00 %	0.00 %		1.05
Agency forwards	37,336	-	(174)			101.03	
Treasury futures	1,300	-	(6)			119.95	
Credit valuation adjustment	-	(925)	520				
Total financial derivatives	$ 4,486,413	$ 41,492	$ (113,687)				

In the normal course of business, collateral requirements contained in Farmer Mac's derivative contracts are enforced by Farmer Mac and its counterparties. Upon enforcement of the collateral requirements, the amount of collateral posted is typically based on the net fair value of all derivative contracts with the counterparty, i.e., derivative assets net of derivative liabilities at the counterparty level. If Farmer Mac were to be in violation of certain provisions of the derivative contracts, the related counterparty could request payment or full collateralization on the derivative contracts. As of March 31, 2011, the fair value of Farmer Mac's derivatives in a net liability position at the counterparty level, which includes accrued interest but excludes any adjustment for nonperformance risk, was $74.5 million. As of March 31, 2011, Farmer Mac posted cash of $2.2 million as collateral for its derivatives in net liability positions. Farmer Mac records posted cash as a reduction in the outstanding balance of cash and cash equivalents and an increase in the balance of prepaid expenses and other assets. If Farmer Mac had breached certain provisions of the derivative contracts as of March 31, 2011, it could have been required to settle its obligations under the agreements or post additional collateral of $72.3 million.

The following table summarizes the effects of Farmer Mac's financial derivatives on the condensed consolidated statements of operations for the three months ended March 31, 2011 and 2010:

	Gains/(Losses) on Financial Derivatives For the Three Months Ended	
	March 31, 2011	March 31, 2010
	(in thousands)	
Interest rate swaps	$ 4,652	$ (4,546)
Agency forwards	(848)	(598)
Treasury futures	185	(249)
Credit default swaps	16	(377)
	4,005	(5,770)
Amortization of derivatives transition adjustment	-	(34)
Total	$ 4,005	$ (5,804)

As of March 31, 2011, Farmer Mac had outstanding basis swaps with Zions First National Bank, a related party, with a total notional amount of $74.1 million and a fair value of $(1.7) million, compared to $85.0 million and $(3.4) million, respectively, as of December 31, 2010. Under the terms of those basis swaps, Farmer Mac pays Constant Maturity Treasury-based rates and receives LIBOR. Those swaps economically hedge most of the interest rate basis risk related to loans Farmer Mac purchases that pay a Constant Maturity Treasury based-rate and the discount notes Farmer Mac issues to fund the loan purchases (the pricing of discount notes is closely correlated to LIBOR rates). Farmer Mac recorded unrealized gains on those outstanding basis swaps for the three months ended March 31, 2011 and 2010 of $1.7 million and $0.1 million, respectively.

(d) Earnings Per Common Share

Basic earnings per common share is based on the weighted-average number of shares of common stock outstanding. Diluted earnings per common share is based on the weighted-average number of shares of common stock outstanding adjusted to include all potentially dilutive common stock options, stock appreciation rights ("SARs") and nonvested restricted stock awards. The following schedule reconciles basic and diluted earnings per common share ("EPS") for the three months ended March 31, 2011 and 2010:

	For the Three Months Ended					
	March 31, 2011			March 31, 2010		
	Net Income	Shares	$ per Share	Net Income	Shares	$ per Share
	(in thousands, except per share amounts)					
Basic EPS						
Net income available to common stockholders	$ 18,323	10,285	$ 1.78	$ 1,767	10,143	$ 0.17
Effect of dilutive securities(1):						
Stock options, SARs and restricted stock		379	(0.06)		308	-
Diluted EPS	$ 18,323	10,664	$ 1.72	$ 1,767	10,451	$ 0.17

(1) For the three months ended March 31, 2011 and 2010, stock options and SARs of 758,795 and 1,581,965, respectively, were outstanding but not included in the computation of diluted earnings per share of common stock because they were anti-dilutive. For the three months ended March 31, 2011 and 2010, 126,000 and 82,500 contingent shares of nonvested restricted stock were outstanding but not included in the computation of diluted earnings per share because the performance conditions were not met.

(e) Stock-Based Compensation

Farmer Mac's 2008 Omnibus Incentive Compensation Plan authorizes the grants of restricted stock, stock options and SARs, among other alternative forms of equity-based compensation, to directors, officers and other employees. SARs awarded to officers and employees vest annually in thirds. If not exercised or terminated earlier due to the termination of employment, SARs granted to officers or employees expire after ten years. For all SARs granted, the exercise price is equal to the closing price of Farmer Mac's Class C Non-Voting Common Stock on the date of grant. There were no SARs granted to officers in first quarter 2011. As of March 31, 2011, there are no outstanding SARs awarded to directors. Restricted stock awarded to directors during 2010 vested fully on March 31, 2011, approximately one year after grant. Restricted stock awarded to officers during 2009 and 2010 vests after approximately three years and only vests if certain performance conditions are met. Restricted stock awards granted to both directors and officers are not issued until full vesting occurs. No restricted stock was granted in first quarter 2011.

For the three months ended March 31, 2011, Farmer Mac recognized $0.7 million of compensation expense related to stock options, SARs and restricted stock, compared to $0.8 million for the same periods in 2010.

The following tables summarize activity related to stock options, SARs and nonvested restricted stock awards for the three months ended March 31, 2011 and 2010:

	For the Three Months Ended			
	March 31, 2011		March 31, 2010	
	Stock Options and SARs	Weighted-Average Exercise Price	Stock Options and SARs	Weighted-Average Exercise Price
Outstanding, beginning of year	1,924,133	$ 21.16	1,799,465	$ 22.68
Granted	-	-	-	-
Exercised	(5,667)	7.48	-	-
Canceled	(596,005)	25.25	-	-
Outstanding, end of year	1,322,461	$ 19.37	1,799,465	$ 22.68
Options and SARs exercisable at end of year	915,206	$ 23.16	1,398,269	$ 25.17

	For the Three Months Ended			
	March 31, 2011		March 31, 2010	
	Non-vested Restricted Stock	Weighted-Average Grant-date Fair Value	Non-vested Restricted Stock	Weighted-Average Grant-date Fair Value
Outstanding, beginning of year	182,609	$ 9.63	200,548	$ 5.93
Granted	-	-	-	-
Canceled	-	-	-	-
Vested and issued	(56,609)	12.22	-	-
Outstanding, end of year	126,000	$ 8.47	200,548	$ 5.93

The cancellations of stock options, SARs and nonvested restricted stock during the first three months of 2011 were due to vested options terminating unexercised on their expiration date.

For the three months ended March 31, 2011 adjustments to additional paid-in capital from exercises or expiration of stock options and SARs and the vesting or expiration of restricted stock was $0.3 million. There was no such stock-based compensation activity during first quarter 2010. The reduction of income taxes to be paid as a result of the deduction for exercises of stock options and SARs was $0.4 million for the three months ended March 31, 2011.

The following tables summarize information regarding stock options, SARs and nonvested restricted stock outstanding as of March 31, 2011:

	Outstanding		Exercisable		Vested or Expected to Vest	
Range of Exercise Prices	Stock Options and SARs	Weighted-Average Remaining Contractual Life	Stock Options and SARs	Weighted-Average Remaining Contractual Life	Stock Options and SARs	Weighted-Average Remaining Contractual Life
$5.00 - $ 9.99	261,666	8.0 years	101,669	7.9 years	233,667	8.0 years
10.00 - 14.99	302,000	9.1 years	82,333	9.0 years	269,033	9.1 years
15.00 - 19.99	50,786	3.4 years	50,786	3.4 years	50,786	3.4 years
20.00 - 24.99	172,289	4.0 years	172,289	4.0 years	172,289	4.0 years
25.00 - 29.99	452,659	4.0 years	425,068	3.8 years	449,698	4.0 years
30.00 - 34.99	83,061	2.0 years	83,061	2.0 years	83,061	2.0 years
	1,322,461		915,206		1,258,534	

	Outstanding		Expected to Vest	
Weighted-Average Grant-Date Fair Value	Nonvested Restricted Stock	Weighted-Average Remaining Contractual Life	Nonvested Restricted Stock	Weighted-Average Remaining Contractual Life
$5.00 - $ 9.99	75,000	1.0 years	67,500	1.0 years
10.00 - 14.99	51,000	2.0 years	45,900	2.0 years
	126,000		113,400	

There were no stock options, SARs or restricted stock awards granted during first quarter 2011 or first quarter 2010. The weighted-average grant date fair value of SARs granted during 2010 was $9.24 per share. The fair values for SARs were estimated using the Black-Scholes option pricing model based on the following assumptions:

	2010
Risk-free interest rate	2.9%
Expected years until exercise	7 years
Expected stock volatility	91.5%
Dividend yield	1.8%

(f) Fair Value Measurement

Farmer Mac follows accounting guidance for fair value measurements that defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establishes a fair value hierarchy that ranks the quality and reliability of the inputs to valuation techniques used to measure fair value. The hierarchy gives highest rank to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest rank to unobservable inputs (level 3 measurements).

Farmer Mac's assessment of the significance of the input to the fair value measurement requires judgment, and considers factors specific to the financial instrument. Both observable and unobservable inputs may be used to determine the fair value of positions that Farmer Mac has classified within the level 3 category. As a result, the unrealized gains and losses for assets and liabilities within the level 3 category may include changes in fair value that were attributable to both observable (e.g., changes in market interest rates) and unobservable (e.g., changes in long-dated volatilities) inputs.

See Note 7 for more information regarding fair value measurement.

(g) Consolidation of Variable Interest Entities

Farmer Mac has interests in various entities that are considered to be VIEs. These interests include investments in securities issued by VIEs, such as Farmer Mac agricultural mortgage-backed securities created pursuant to Farmer Mac's securitization transactions and mortgage and asset-backed trusts that Farmer Mac did not create. Effective January 1, 2010, Farmer Mac adopted two new accounting standards that eliminated the concept of qualifying special purpose entities ("QSPEs") and amended the accounting for transfers of financial assets and the consolidation model for VIEs. All formerly designated QSPEs were evaluated for consolidation in accordance with the new consolidation model, which changed the method of analyzing which party to a VIE should consolidate the VIE. The new consolidation model uses a qualitative evaluation that requires consolidation of an entity when the reporting enterprise both (1) has the power to direct matters which significantly impact the activities and success of the entity, and (2) has exposure to benefits and/or losses that could potentially be significant to the entity. The reporting enterprise that meets both these conditions is deemed the primary beneficiary of the VIE.

The new consolidation standard requires the incremental assets and liabilities consolidated upon adoption to initially be reported at their carrying amounts. Carrying amount refers to the amount at which the assets and liabilities would have been carried in the consolidated financial statements if the new guidance had been effective when Farmer Mac first met the conditions to be the primary beneficiary of the VIE. If determining the carrying amounts is not practicable, the assets and liabilities of the VIE shall be measured at fair value at the date the new standards first apply. For the outstanding trusts consolidated effective January 1, 2010, Farmer Mac initially recorded the assets and liabilities on the consolidated balance sheet at their carrying amounts, adjusted, where applicable, for fair value option elections that had been made previously. Accrued interest and allowance for losses have also been recognized as appropriate.

Although these new accounting standards did not change the economic risk to Farmer Mac's business, specifically Farmer Mac's liquidity, credit and interest rate risks, the adoption of these new accounting standards had a significant impact on the presentation of Farmer Mac's consolidated financial statements. On the consolidated balance sheet, there was an increase in loans held for investment, interest receivable, debt and accrued interest payable, and a decrease in available-for-sale and trading Farmer Mac Guaranteed Securities, the reclassification of a portion of the reserve for losses to allowance for loan losses, and the elimination of the guarantee and commitment fees receivable and guarantee and commitment obligations related to the consolidated trusts. On the income statement, there was an increase in interest income and interest expense attributable to the assets and liabilities of the consolidated trusts and a reclassification of a portion of guarantee fee income to interest income.

The VIEs in which Farmer Mac has a variable interest are limited to securitization trusts. The major judgment in determining if Farmer Mac is the primary beneficiary was whether Farmer Mac had the power to direct the activities of the trust that potentially had the most significant impact on the economic performance of the trust. Generally, the ability to make decisions regarding default mitigation was evidence of that power. Farmer Mac determined that it was the primary beneficiary for the securitization trusts related to most Farmer Mac I and all Rural Utilities securitization transactions because of its rights as guarantor under both programs to control the default mitigation activities of the trusts. For certain securitization trusts created when loans subject to LTSPCs were converted to Farmer Mac I Guaranteed Securities, Farmer Mac determined that it was not the primary beneficiary since the power to make decisions regarding default mitigation was shared among unrelated parties. For similar securitization transactions where the power to make decisions regarding default mitigation was shared with a related party, Farmer Mac determined that it was the primary beneficiary because the applicable accounting guidance does not permit parties within a related party group to conclude that the power is shared.

For those trusts that Farmer Mac is the primary beneficiary, the assets and liabilities are presented on the condensed consolidated balance sheet as “Loans held for investment in consolidated trusts” and “Debt securities of consolidated trusts held by third parties,” respectively. These assets can only be used to satisfy the obligations of the related trust.

For those trusts where Farmer Mac has a variable interest but has not been determined to be the primary beneficiary, Farmer Mac’s interests are presented as either “Farmer Mac Guaranteed Securities” or “Investment securities” on the condensed consolidated balance sheets. Farmer Mac’s involvement in on-balance sheet VIEs classified as Farmer Mac Guaranteed Securities include securitization trusts under the Farmer Mac II program and trusts related to AgVantage securities. In the case of Farmer Mac II trusts, Farmer Mac was not determined to be the primary beneficiary because it does not have the decision-making power over default mitigation activities. For the AgVantage trusts, Farmer Mac currently does not have the power to direct the activities that have the most significant economic impact to the trust unless, as guarantor, there is a default by the issuer of the trust securities. Should there be a default, Farmer Mac would reassess whether it is the primary beneficiary of those trusts. For VIEs classified as investment securities, which include auction-rate certificates, asset-backed securities and GSE-guaranteed mortgage-backed securities, Farmer Mac was determined not to be the primary beneficiary because of the lack of voting rights or other powers to direct the activities of the trust. As of March 31, 2011, the Farmer Mac Guaranteed Securities trusts and investment securities trusts have carrying amounts on the condensed consolidated balance sheet totaling $1.5 billion and $818.4 million, respectively, which is Farmer Mac’s maximum exposure to loss. In addition, Farmer Mac has a variable interest in off-balance sheet VIEs, which include a guarantee of timely payment of principal and interest, totaling $2.7 billion as of March 31, 2011.

(h) New Accounting Standards

Troubled Debt Restructurings: Accounting Standards Updates 2011-01 and 2011-02

In January 2011, the FASB issued Accounting Standards Update ("ASU") 2011-01, Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20 (discussed below). The effective date of the new disclosures about troubled debt restructurings was delayed to coordinate the disclosures with the FASB project on determining what constitutes a troubled debt restructuring. In April 2011, the FASB completed that project and issued ASU 2011-02, A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring. ASU 2011-02 states that a troubled debt restructuring exists when a creditor concludes that both the restructuring constitutes a concession and the debtor is experiencing financial difficulties and clarifies the guidance on evaluating these criteria. ASU 2011-02 is effective for the first interim or annual period beginning on or after June 15, 2011 and should be applied retrospectively to the beginning of the annual period of adoption (i.e., for Farmer Mac, it will be effective for third quarter 2011 reporting). The troubled debt restructuring disclosures in ASU 2010-20 also will be effective in third quarter 2011. Farmer Mac does not expect the adoption of these standards to have a significant impact on the Corporation's financial position, results of operations or cash flows.

(i) Reclassifications

Certain reclassifications of prior period information were made to conform to the current period presentation.

Note 2. Investment Securities

The following tables present the amortized cost and estimated fair values of Farmer Mac's investments as of March 31, 2011 and December 31, 2010.

	March 31, 2011			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
	(in thousands)			
Available-for-sale:				
Floating rate auction-rate certificates backed by Government guaranteed student loans	$74,100	$-	$(9,561)	$64,539
Floating rate asset-backed securities	134,117	68	(1)	134,184
Floating rate corporate debt securities	159,634	378	(52)	159,960
Fixed rate corporate debt securities	34,715	50	(38)	34,727
Floating rate Government/GSE guaranteed mortgage-backed securities	609,767	4,341	(559)	613,549
Fixed rate GSE guaranteed mortgage-backed securities	4,125	278	-	4,403
Floating rate GSE subordinated debt	70,000	-	(11,031)	58,969
Fixed rate GSE preferred stock	79,922	7,605	-	87,527
Fixed rate senior agency debt	9,999	-	-	9,999
Fixed rate U.S. Treasuries	808,410	296	(41)	808,665
Total available-for-sale	1,984,789	13,016	(21,283)	1,976,522
Trading:				
Floating rate asset-backed securities	5,579	-	(3,889)	1,690
Fixed rate GSE preferred stock	83,603	2,753	-	86,356
Total trading	89,182	2,753	(3,889)	88,046
Total investment securities	$2,073,971	$15,769	$(25,172)	$2,064,568

	December 31, 2010			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
	(in thousands)			
Available-for-sale:				
Floating rate auction-rate certificates backed by Government guaranteed student loans	$74,100	$-	$(9,765)	$64,335
Floating rate asset-backed securities	29,437	24		