

## 2008 Quarterly Report SEPTEMBER 30, 2008

To our Valued Customer-Owners:

The credit crisis that has unfolded over the last quarter has profoundly shaken the public's confidence in the global financial services industry. The rapid failure of a number of prominent financial institutions; the need for emergency infusions of public funds into banks by governments and central banks around the world; and the resulting dislocation of international credit markets have all combined to foster concern among businesses and individuals throughout the world.

However, the credit crisis has also underscored the solid foundation of strength and stability that COBANK and the Farm Credit System have built over our long history. No enterprise, COBANK included, is immune from the impacts of the downturn currently taking place in the global economy. Fundamentally, though, COBANK's financial position remains strong, and we continue to serve as a dependable lender to our agribusiness, energy, water and communications customers across rural America.

As detailed in the pages that follow, COBANK experienced robust growth in earnings and loan volume during the first nine months of the year. Net earnings rose almost 48 percent to \$449 million, compared with \$304 million for the same period in 2007. Total loans and leases outstanding for COBANK increased to \$43.1 billion at September 30, 2008, compared to \$40.5 billion at year-end 2007. These increases reflect the impact of sharply higher prices for commodities and farm inputs throughout much of 2008, particularly in the grain, oilseed and farm supply markets, as well as the continued expansion of our agribusiness and rural utilities businesses.

Credit quality remains good, with approximately 97 percent of all loans and leases falling into the highest regulatory category used to measure credit quality. As previously disclosed, we expect some continued deterioration in credit quality due to ongoing volatility in commodity prices as well as the general decline in the health of the economy, which undoubtedly will impact some of our customers. Overall, however, we remain comfortable with the level of risk in our loan portfolio and continue to manage this risk carefully.

As important as earnings and credit quality are, however, these measures do not fully reflect the true picture of the bank's overall health. In a credit crisis, **liquidity**, **capital** and **confidence** are the three pillars upon which any bank's financial performance and stability ultimately depend. For COBANK's customer-owners, our membership in the Farm Credit System and our history of sound, careful business practices are delivering benefits in all three areas today:

- **Liquidity.** COBANK's investment portfolio totaled \$13.4 billion at quarter end. We continue to manage this portfolio conservatively, and only a nominal amount of our investments carry a rating of less than AAA. In addition, we've made a deliberate effort to bolster our total days' liquidity through the increased use of longer-term debt instruments. At quarter end, we had 289 days of liquidity, compared to 164 days at December 31, 2007. Although we continue to maintain regular access to the debt capital markets, particularly for shorter-dated instruments, our days' liquidity provides the bank with a cushion in the event these markets become further restricted.
- **Capital.** With your continued support, COBANK has strengthened its capital base considerably this year by continuing to access capital from third-party investors. The bank issued \$500 million in subordinated debt in April and \$200 million in Series C preferred stock in July. Those issuances brought our total non-member capital raised since 2001 to \$1.7 billion, and significantly increased the total capacity of the bank to meet the borrowing needs of our customers. At quarter end, our capital ratios remained well in excess of all regulatory minimums.

In September, shareholders overwhelmingly approved a proposal allowing COBANK to issue or reissue preferred stock over the next 10 years, so long as the total amount of preferred stock outstanding does not exceed the bank's bylaw limit of \$1 billion. This authorization significantly enhances our ability to respond quickly to dynamic market conditions.

- **Confidence.** COBANK's financial strength and its membership in the Farm Credit System have enabled the bank to maintain the confidence of investors and, as a result, access to the debt capital markets. Key in this regard has been our ongoing commitment to balance our mission to serve customers in rural America with our fiduciary duty to preserve the safety and soundness of the bank. Despite highly publicized problems involving other government-sponsored enterprises, the strong reputation of COBANK and the System as a whole have proven to be an important competitive advantage in the face of recent market turmoil.

COBANK has been most impacted by the fallout from the credit crisis in our funding cost. Our single largest source of funding for customer loans is debt issued to investors on our behalf by the Federal Farm Credit Banks Funding Corporation. The price of a substantial portion of the debt we issue is tied to LIBOR (the London Interbank Offered Rate), which is the predominant global pricing index for financial contracts. Beginning in mid-September, as a result of negative developments in the financial markets that created a high level of uncertainty and lack of trust among financial institutions, short-term interest rates (particularly U.S. dollar LIBOR) increased dramatically. Although recent actions by governments to stabilize the banking system have restored some level of confidence and USD LIBOR rates have begun to decline, those rates remain elevated.

It is critical that COBANK maintain stable net interest margins – as well as sustainable loan risk premiums – in order to preserve our foundation of financial strength and stability and to continue meeting the borrowing needs of our customers. That means that higher funding costs experienced by the bank will be reflected in the interest rates paid by our customers. We appreciate your ongoing support and understanding as we continue to manage the bank in a prudent manner and generate margins sufficient to maintain our capacity to meet your needs in these volatile markets and to continue accessing both the debt and equity capital markets.

We encourage you to read the enclosed quarterly report in detail and to contact your COBANK relationship manager if you have any questions. We are committed to maintaining transparency in our financial reporting; we believe that doing so is one of the best ways to maintain the trust and confidence of our customer-owners, policymakers and the investors who help fund the bank through the purchase of our debt and equity securities.

As always, we are deeply grateful for the business of our customer-owners and the enormous trust you place in COBANK. We thank you for your ongoing support and look forward to reporting to you on our future progress.

Everett Dobrinski  
Chairman of the Board

Robert B. Engel  
President and Chief Executive Officer

October 31, 2008

# Financial Highlights

COBANK, ACB

*\$ in thousands*

	September 30, 2008 <i>(Unaudited)</i>	December 31, 2007
Total Loans and Leases	\$ 43,109,714	\$ 40,491,486
Less: Allowance for Credit Losses	440,529	447,226
Net Loans and Leases	\$ 42,669,185	\$ 40,044,260
Total Assets	\$ 57,898,963	\$ 52,188,896
Total Shareholders' Equity	3,526,570	3,233,424

## For the Nine Months Ended September 30, *(Unaudited)*

	2008	2007
Net Interest Income	\$ 671,923	\$ 474,319
Provision for Credit Losses	-	-
Net Fee Income	44,772	31,690
Net Income	448,826	303,732
Net Interest Margin	1.55%	1.47%
Return on Average Assets	1.02	0.94
Return on Average Common Shareholders' Equity	19.86	14.42
Return on Average Total Shareholders' Equity	17.80	13.29
Average Loans and Leases	\$ 46,130,147	\$ 34,470,760
Average Earning Assets	57,865,605	43,062,789
Average Assets	58,771,541	43,257,999

# Management's Discussion and Analysis of Financial Condition and Results of Operations

COBANK, ACB

## Business Overview

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COBANK, ACB (COBANK or the Bank) is an Agricultural Credit Bank and is one of the five banks of the Farm Credit System (System), a federally chartered network of borrower-owned lending institutions composed of cooperatives and related service organizations. We are cooperatively owned by our U.S. customers, who consist of agricultural cooperatives, rural energy, communications and water companies, farmer-owned financial institutions, including Agricultural Credit Associations (Associations), and other businesses that serve rural America. We provide a diversified range of financial solutions domestically and internationally to lifeline businesses through four operating segments: Agribusiness Banking Group, Strategic Relationships Division, Communications and Energy Banking Group, and Global Financial Services Group.

The following discussion and analysis should be read in conjunction with the accompanying unaudited condensed consolidated quarterly financial statements and related notes and with our 2007 Annual Report to Shareholders.

## Consolidated Results of Operations

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Net income was \$448.8 million for the nine months ended September 30, 2008, a 48 percent increase over net income of \$303.7 million during the same period in 2007. Increased earnings were driven by a \$197.6 million increase in net interest income largely resulting from strong loan growth across all of our operating segments. Greater fee income of \$13.1 million also contributed to increased earnings. The increase in net interest income and fees was partially offset by increased income tax expense of \$45.1 million related to higher overall earnings and increased noninterest expenses of \$19.7 million.

Our net interest income increased to \$671.9 million for the nine months ended September 30, 2008, compared to \$474.3 million for the same period in 2007. The significant growth in net interest income primarily resulted from an \$11.7 billion increase in average loan and lease volume. The most substantial volume increases were in loans to our agribusiness customers, especially those serving grain, oilseed and farm supply markets where higher and more volatile commodity prices, coupled with increased prices and demand for farm inputs, led to greater customer financing requirements. Our other lending units also experienced strong loan growth. Association-related loan volume increased due to growth in our participations in the direct loans of other System banks to certain of their affiliated Associations and to growth at our two largest affiliated Associations. Growth in our energy and communications portfolios primarily resulted from increased financing requirements from our rural electric distribution, generation and transmission, and communications customers driven in part by lower levels of availability of credit in the broader debt capital markets. In addition, to continue to meet the liquidity requirements associated with loan growth, we increased our average investment securities and highly-liquid holdings by \$3.2 billion as compared to the same prior year period.

Our overall net interest margin for the nine months ended September 30, 2008 increased to 1.55 percent from 1.47 percent during the same prior year period. This increase reflects significant loan growth in our higher-margin loans as well as the benefit of lower short-term market interest rates on our funding position during much of the period. Beginning in mid-September, as a result of negative developments in the financial markets creating a high level of uncertainty among financial institutions, short-term interest rates, particularly the U.S. dollar-denominated London Interbank Offered Rate (USD LIBOR), increased dramatically and remain elevated. While we continue to maintain regular access to the debt capital markets, these higher short-term rates will negatively affect our net interest margins considering our funding position and the significant level of our liabilities that are indexed to USD LIBOR. The favorable effects of growth in higher margin loans and lower short-term interest rates during the first nine months of 2008 were partially offset by the effects of higher leverage on our balance sheet, increased lending to Association and rural energy customers and the increase in

our investment securities. Investment securities, loans to Associations and loans to rural energy customers carry lower margins commensurate with their lower risk profiles and generally lower capital requirements. The benefit on our net interest margin of noninterest-bearing financing (principally equity) was less in the first nine months of 2008 due to significant asset growth, resulting in a decline in equity as a percentage of average earning assets.

We did not record a provision for credit losses for the nine months ended September 30, 2008. While our overall credit quality remains good, nonaccrual loans and leases increased to \$62.7 million at September 30, 2008 from a historically low level of \$14.8 million at December 31, 2007, largely due to credit concerns surrounding a limited number of our agribusiness customers. Nonaccrual loans and leases are likely to increase to levels consistent with historical averages in the fourth quarter of 2008 due primarily to the challenges facing certain of our customers in the livestock/poultry industry as a result of increased feed-ingredient costs and weak market pricing. Net charge-offs for the nine months ended September 30, 2008 were \$6.7 million compared to net recoveries of \$10.3 million for the same period in 2007. The charge-offs in 2008 were primarily related to a limited number of our agribusiness customers.

Noninterest income increased to \$45.6 million for the nine months ended September 30, 2008, as compared to \$33.3 million for the same period in 2007, and is composed primarily of net fee income, loan prepayment fee income and other gains and losses, reduced by losses on early extinguishments of debt. The increase in noninterest income resulted primarily from a \$13.1 million increase in net fee income. Losses on early extinguishments of debt, net of prepayment income, increased to \$7.1 million for the nine months ended September 30, 2008 from \$4.6 million in the prior year period largely due to the timing of debt extinguishments made to offset the impact of prepayments, including an expected customer prepayment which occurred subsequent to September 30, 2008. The level of prepayments increased in the nine months ended September 30, 2008 as compared to the same period of 2007 due to the decline in interest rates over the past year.

Noninterest expenses increased to \$151.8 million for the nine months ended September 30, 2008, as compared to \$132.1 million for the same period in 2007, and included an \$11.4 million increase in statutory insurance fund premiums assessed by the Farm Credit System Insurance Corporation (Insurance Corporation) due to increased loan volume. The basis upon which statutory insurance fund premiums are determined changed effective July 1, 2008 as a result of the enacted legislation described in "Insurance Premiums" on page 12. Our employee compensation expense increased by \$5.8 million due largely to an increase in staffing required to service a higher level of financing requirements from our customers.

Our income tax expense increased to \$116.9 million for the nine months ended September 30, 2008, as compared to \$71.7 million for the same prior year period. Increased tax expense is a direct result of the improvement in our pre-tax earnings. Our effective tax rate was 20.7 percent and was comparable to the same period in 2007.

As a result of our significantly stronger earnings, our annualized return on average common shareholders' equity increased to 19.86 percent for the nine months ended September 30, 2008 from 14.42 percent for the same period in 2007. Due to the growth in higher-margin loans and the benefit of lower short-term market interest rates as noted previously, our annualized return on average assets increased to 1.02 percent for the nine months ended September 30, 2008, as compared to 0.94 percent for the same prior year period.

For the three months ended September 30, 2008, our net income increased to \$140.9 million from \$98.4 million for the same prior year period. The increase is primarily due to a \$70.6 million improvement in net interest income that resulted from growth in loan volume as previously discussed, partially offset by a \$21.4 million increase in income tax expense. Noninterest income increased by \$3.4 million as the impact of greater net fee income and other gains more than offset increased losses on early extinguishments of debt, net of prepayment income. Noninterest expenses increased by \$10.1 million due to an increase in statutory insurance fund premiums that resulted from loan growth, increased salary expense related to the aforementioned staffing increase and slightly higher general and administrative costs.

## Operating Segment Financial Review

As an Agricultural Credit Bank, we provide domestic and international financial solutions to farmer-owned cooperatives; farmer-owned financial associations; energy, communications and water customers; and other related businesses. We conduct our lending and leasing operations through four operating segments: Agribusiness Banking Group (ABG), Strategic Relationships Division (SRD), Communications and Energy Banking Group (CEBG) and Global Financial Services Group (GFSG). Loans and leases outstanding, net of allowance for credit losses, by business segment at September 30, 2008 and 2007, are reported in Note 10 to the accompanying unaudited condensed consolidated financial statements.

Net interest income on investment securities, federal funds sold, securities purchased under resale agreements and other highly-liquid funds is allocated to all segments, whereas underlying investment assets are not allocated.

Net income by operating segment is summarized in the accompanying table and is more fully described in Note 10 to the accompanying unaudited condensed consolidated financial statements.

### Net Income by Operating Segment (\$ in Thousands)

For the Nine Months Ended September 30,	2008	2007
<b>Operating Segment:</b>		
Agribusiness	\$ 239,600	\$ 140,858
Strategic Relationships Division	55,182	40,100
Communications and Energy	110,373	92,439
Global Financial Services	50,882	35,789
Total Operating Segments	456,037	309,186
Corporate/Other	(7,211)	(5,454)
<b>Total</b>	<b>\$ 448,826</b>	<b>\$ 303,732</b>

### *Agribusiness Banking Group (ABG)*

ABG provides financial solutions to cooperatives and other businesses engaged in agricultural activities, including grain handling, farm supply, food processing, dairy, livestock, fruits, nuts, vegetables, cotton, biofuels and agricultural finance. ABG includes Farm Credit Leasing Services Corporation (FCL), which provides lease-related financial services to Association partners, agribusinesses, agricultural producers and rural utilities.

ABG loans and leases outstanding declined to \$10.6 billion at September 30, 2008, a \$3.2 billion or 23 percent decrease from \$13.8 billion at December 31, 2007. Outstanding agribusiness loan volume decreased primarily as a result of the typical seasonal decline in loan and lease volume during the summer months. Average loan and lease volume during the first nine months of 2008 was \$6.0 billion greater than the first nine months of 2007. ABG's average loan and lease volume increased largely due to higher financing requirements from our grain, oilseed and farm supply customers who experienced significant increases and volatility in the prices of their products. Such price increases resulted from increased domestic and international demand for corn, wheat and soybeans and other factors. In addition, the demand for and price of farm inputs (such as seed, fertilizer and fuel) and the resulting impact on inventory financing requirements has similarly increased average loan volume for this sector. During the third quarter of 2008, prices of commodities and certain farm inputs declined, although they still remain high relative to historic norms.

Nonaccrual loans and leases in our ABG portfolio increased to \$42.5 million at September 30, 2008 from a historically low level of \$14.8 million at December 31, 2007. Credit challenges affecting a limited number of agribusiness customers resulted in their loans being transferred to nonaccrual status in 2008.

ABG net income increased 70 percent in the first nine months of 2008 to \$239.6 million from \$140.9 million for the same period in 2007. This increase resulted from a \$133.1 million increase in net interest income due to the significant growth in average agribusiness loan volume, as described previously. In addition, ABG did not record a provision for credit losses for the first nine months of 2008, a result of continued strong credit quality and a low level of charge-offs. ABG's results for the first nine months of 2007 included an \$18.0 million provision for credit losses. Noninterest expenses increased \$12.7 million largely as a result of increased statutory insurance fund premiums related to significant loan growth. ABG's income tax expense increased \$36.3 million due to the growth in its pre-tax earnings.

### ***Strategic Relationships Division (SRD)***

SRD manages the direct funding relationships with our affiliated Association customer-owners (Northwest Farm Credit Services, First Pioneer Farm Credit, Farm Credit of Western New York, Yankee Farm Credit and Farm Credit of Maine), as well as funding relationships with other System institutions. The SRD portfolio primarily consists of loans to our five affiliated Association customers as well as participations in loans made by other System banks to certain of their affiliated Associations.

SRD loans outstanding increased to \$14.8 billion at September 30, 2008 from \$12.2 billion as of December 31, 2007. Average SRD loans grew to \$13.3 billion for the first nine months of 2008 compared to \$10.3 billion in the comparable period of 2007. The increase in loan volume reflects increased participations in loans made by other System banks to certain of their affiliated Associations as well as strong loan growth at our two largest affiliated Associations. The credit quality of the SRD loan portfolio is exceptionally high due to the financial and operating strength of the Associations and the quality and diversification of their loan portfolios. Lower margins in SRD are commensurate with this low-risk profile and lower capital requirements.

SRD net income increased 38 percent to \$55.2 million for the first nine months of 2008 from \$40.1 million for the same prior year period. Improved SRD earnings are primarily the result of stronger net interest income, which grew \$13.7 million due to the \$3.0 billion increase in average loan volume described above. Noninterest income improved by \$3.6 million due to a greater level of patronage income from other System entities.

### ***Communications and Energy Banking Group (CEBG)***

CEBG provides financial solutions to companies in the energy, communications and water industries. Customers include rural electric generation and transmission cooperatives, electric distribution cooperatives, independent power producers, rural local exchange carriers, wireless providers, cable television systems, and water and waste water companies.

CEBG loans outstanding increased to \$10.6 billion at September 30, 2008 from \$8.7 billion at December 31, 2007. Average CEBG loans increased to \$9.6 billion for the first nine months of 2008 from \$7.8 billion for the same period in 2007. Growth in CEBG's loan volume resulted from increased lending activity in the rural electric distribution, generation and transmission, and communications sectors driven by increased customer capital expenditures, loans to new customers and lower levels of availability of credit in the broader debt capital markets.

CEBG credit quality remains strong as a result of our focus on lending to our core rural utility sectors. There were no CEBG nonaccrual loans at either September 30, 2008 or December 31, 2007.

CEBG net income increased 19 percent to \$110.4 million for the first nine months of 2008 from \$92.4 million for the same period in 2007. Improved earnings primarily resulted from stronger net interest income, which increased \$39.0 million due to the \$1.8 billion increase in average loan volume described above. The increase in net interest income was somewhat offset by a \$22.0 million reversal of the allowance for credit losses for the nine months ended September 30, 2007, as compared to no provision for credit losses in the 2008 period. Noninterest income improved \$6.4 million primarily as a result of growth in fee income.

## ***Global Financial Services Group (GFSG)***

GFSG includes our Corporate Finance Division portfolio, consisting of loans to large food and agribusiness customers, and our International Division's lending portfolio. GFSG's International Division provides tailored short-term and medium-term trade financing services to support the export of U.S. agricultural products. The U.S. government-sponsored export guarantee General Sales Manager (GSM) program provides guarantees for a significant portion of the International Division's portfolio, resulting in a lower overall margin that is reflective of this low-risk portfolio. GFSG also provides capital markets and cash management products and services.

GFSG loans outstanding increased to \$7.1 billion at September 30, 2008, compared to \$5.8 billion at December 31, 2007. Our Corporate Finance Division portfolio balances increased to \$4.1 billion at September 30, 2008 from \$3.7 billion at December 31, 2007, primarily due to increased commodity prices and the volatility of such prices. International Division loans outstanding increased to \$3.0 billion at September 30, 2008 from \$2.1 billion at December 31, 2007 as the tightening of global credit markets led to customers increasing their loan commitments with COBANK. In particular, loans granted under U.S. government-guaranteed export-lending programs have increased significantly. Such guaranteed loans represented 68 percent of International Division loans outstanding as of September 30, 2008 compared to 61 percent as of December 31, 2007.

Nonaccrual loans, of which there were none at December 31, 2007, increased to \$20.2 million at September 30, 2008. This increase relates to one customer experiencing credit difficulty. Nonaccrual loans are likely to increase in the Corporate Finance Division portfolio in the fourth quarter as certain of our customers in the livestock/poultry industry experience financial challenges resulting from increased feed-ingredient costs and weak market pricing.

GFSG net income increased 42 percent to \$50.9 million for the first nine months of 2008, compared to \$35.8 million for the same period in 2007. The increase is primarily due to a \$12.2 million increase in net interest income resulting from the growth in average Corporate Finance Division loan volume which increased to \$4.3 billion for the nine months ended September 30, 2008 from \$3.7 billion in the prior year period. A \$5.6 million increase in noninterest income, primarily due to greater fee income, also contributed to the growth in earnings. As a result of continued strong credit quality through September 30, 2008, GFSG did not record a provision for credit losses; however, a \$4.0 million provision was recorded in the same prior year period. Greater income tax expense of \$5.8 million, related to increased pre-tax earnings, somewhat offset these factors.

## **Credit Quality, Liquidity, Capital Resources and Other**

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### ***Credit Quality***

While overall credit quality measurements as of September 30, 2008 remain strong, nonaccrual loans and leases have increased since year end 2007. Nonaccrual loans and leases grew to \$62.7 million at September 30, 2008 from \$14.8 million at December 31, 2007, primarily due to the aforementioned credit concerns affecting a limited number of our agribusiness customers. Nonaccrual loans and leases are likely to increase to a level more consistent with historical averages in the fourth quarter of 2008, due primarily to the challenges facing certain of our customers in the livestock/poultry industry as a result of increased feed-ingredient costs and weak market pricing. We continue to closely monitor the impact of increased input costs and greater financing requirements on the financial condition of our customers.

The following table presents loans and leases and related accrued interest receivable classified pursuant to our regulator's Uniform Loan Classification System, as a percent of total loans and leases and related accrued interest.

### Asset Quality Ratios

	September 30, 2008	December 31, 2007
Acceptable	96.75%	97.00%
Other Assets Especially Mentioned	1.71	1.61
Substandard	1.51	1.38
Doubtful	0.03	0.01
Loss	-	-
Total	100.00%	100.00%

As a result of our good overall credit quality, we did not record a provision for credit losses for the nine months ended September 30, 2008. Net charge-offs for the first nine months of 2008 totaled \$6.7 million and were primarily associated with a limited number of our agribusiness customers. While the Bank and the System currently enjoy good credit quality, agriculture remains a cyclical business and is subject to a variety of economic factors, including volatile commodity prices, and fluctuating weather conditions. Agricultural economic conditions may not be as favorable in the future. In addition, our customers, like most businesses, are likely to be impacted by a general slowdown in the overall U.S. and global economies.

During the first quarter of 2008, we initiated a project to evaluate our methodology for determining the allowance for credit losses and to consider refinements to the process. Our evaluation focuses on more closely aligning the allowance process with our economic capital process while ensuring that a high level of correlation between the allowance and the risk profile of our loan and finance lease portfolio is maintained. We expect to complete our evaluation during the fourth quarter of 2008 with any appropriate changes to the allowance implemented and recorded at that time. However, we do not anticipate any material adjustment to our overall allowance as a result of this evaluation.

### *Liquidity and Investments*

Our liquidity management objectives are designed to meet maturing debt obligations, provide a reliable source of funding to borrowers and fund our operations on a cost-effective basis. We believe that sufficient resources are available to meet liquidity management objectives through the Bank's debt maturity structure, holdings of liquid assets and access to the agency market via the Federal Farm Credit Banks Funding Corporation. As previously noted, the global credit markets have experienced significant, negative events over the last quarter. As a result, the global level of credit availability and investor willingness to purchase debt securities issued by financial institutions has been substantially reduced. Furthermore, traditional relationships between the various interest rate indices, widely used by financial institutions, have become dislocated. Overall market rates have also increased, with a negative impact on the funding costs of financial institutions. As a member of the Farm Credit System, a AAA-rated government sponsored enterprise, COBANK has continued to maintain regular access to the debt-funding markets, particularly for shorter-dated instruments, and has not experienced any significant disruptions in funding. However, overall debt funding costs have increased and our ability to issue longer-maturity debt has been reduced. We have responded by holding higher levels of liquidity and issuing required debt funding when market conditions are favorable. While we expect to continue to issue our debt securities as necessary, the cost of such debt issuances is expected to remain at higher overall levels. While we will increase pricing to customers where appropriate, the elevated level of costs are likely to reduce our overall margins in the near future, but not by material levels. At September 30, 2008, our liquidity was 289 days, compared to 164 days at December 31, 2007. During the first nine months of 2008, we averaged 194 days liquidity, compared to the regulatory minimum of 90 days.

Investment securities, federal funds sold, securities purchased under resale agreements and other highly-liquid funds are primarily held for the purposes of maintaining a liquidity reserve and managing short-term surplus funds. Investment securities increased to \$13.4 billion at September 30, 2008 compared to \$10.4 billion at

December 31, 2007, in response to the liquidity requirements related to higher loan balances and the changing market conditions described above. Investment securities are reported at estimated fair value and include accumulated unrealized losses, net of deferred taxes, of \$140.4 million at September 30, 2008, compared to \$21.7 million at December 31, 2007. While unrealized losses generally result from changes in market interest rates, such losses have increased in recent months due to continued illiquidity in the broader financial markets. We have the ability and intent to hold our investment securities until maturity or such time as the value recovers, and thus, with the exception of one security discussed below, we do not consider these investments to be other-than-temporarily impaired at September 30, 2008 or December 31, 2007. Except for the other-than-temporary impairment recorded for one security, changes in the fair value of these investments are accounted for as a component of accumulated other comprehensive income (loss). For the nine months ended September 30, 2008, we recorded unrealized losses, net of deferred taxes, of \$118.8 million compared to unrealized gains, net of deferred taxes, of \$15.6 million for the same prior year period.

At September 30, 2008, the market value of our investment portfolio was \$13.4 billion, of which 91 percent, or \$12.1 billion, consisted of investments in mortgage-backed or debt securities issued by government sponsored enterprises or guaranteed by the Government National Mortgage Association (Agency Securities). Unrealized losses on such investments were \$112.9 million at September 30, 2008. Another \$947.9 million, or seven percent, of our investment portfolio represents investments in non-agency mortgage-backed securities (Non-Agency Securities) with unrealized losses of \$63.8 million at September 30, 2008. The remaining \$303.9 million, or two percent, of our investment portfolio represents asset-backed securities (ABS), the substantial majority of which are composed of home equity asset-backed securities. Unrealized losses on ABS investments were \$49.4 million at September 30, 2008. Our home equity asset-backed securities are supported by first- or second-lien mortgages with \$236.0 million of them insured by monoline bond insurance companies, principally MBIA Insurance Corporation (MBIA) and Ambac Assurance Corporation (Ambac).

Farm Credit Administration (FCA) regulations require that mortgage- and asset-backed securities be AAA-rated in order to be included as part of our liquidity reserve. As of September 30, 2008, all of our Agency and Non-Agency Securities were AAA-rated with the exception of one \$2.6 million Non-Agency Security discussed below. Of the \$303.9 million in ABS securities, \$170.8 million were AAA-rated by at least one of the major rating agencies as of September 30, 2008. As a result of credit deterioration in financial markets in recent months, including the downgrade of bond insurance companies, seven of our investment securities which carry third-party insurance have been downgraded to ratings below AAA by both Moody's Investors Service (Moody's) and Standard and Poor's Rating Services (S&P) and are no longer included in our liquidity reserve. We have received permission from the FCA to continue to hold these seven investment securities, subject to certain conditions. Such securities consist of the following:

- One ABS security with a \$10.1 million face value (\$4.4 million market value) was downgraded to Caa1 by Moody's and BBB- by S&P as a result of the downgrade of bond insurer Syncora Guarantee Inc. We have determined that this security is other-than-temporarily impaired and we recorded an impairment loss of \$6.0 million during the three month period ended June 30, 2008.
- Three ABS securities with a \$122.8 million face value (\$98.9 million market value) were downgraded to Aa3 by Moody's as a result of the downgrade of Ambac, and two ABS securities with a face value of \$40.6 million (\$29.8 million market value) were downgraded to A2 by Moody's as a result of the downgrade of MBIA. These five securities were downgraded to AA by S&P. Based on the current performance of the underlying collateral, our stress-testing of performance, the credit enhancements embedded in these five securities and the insurance support, we continue to expect to recover all of the book value of these securities.
- One Non-Agency Security with a face value of \$2.9 million (\$2.6 million market value) was downgraded to Aa2 by Moody's and AA by S&P, also as a result of the downgrade of Ambac. Similar to the five ABS securities discussed directly above and, for the same reasons noted above, we expect to recover all of the book value of this security.

In October 2008, two ABS securities totaling \$64.5 million in face value (\$55.2 million market value) were downgraded to Aa2 and Aa3 by Moody's and to AA by S&P. We will request and expect to receive permission from the FCA to continue to hold these securities. Additionally, three securities were downgraded in October to levels no lower than A+ by S&P, but remain Aaa-rated on negative watch by Moody's. We currently expect to recover all of the book value of these securities.

We perform other-than-temporary impairment assessments of our investment securities based on evaluations of both current and future market and credit conditions at each quarter-end. Subsequent changes in market or credit conditions could change these evaluations.

### ***Capital Resources***

We are primarily capitalized by holders of our common stock and participation certificates (which include our Association customers), by our preferred stockholders, and by unallocated retained earnings. Overall, the exceptional levels of loan growth the Bank has experienced, including substantial seasonal loan demand in 2008, have impacted the Bank's regulatory capital ratios. As a result, the Board of Directors and the Bank's shareholders have taken a number of steps to increase the overall capital levels for the Bank, as discussed below.

On July 7, 2008, we issued \$200 million of Series C non-cumulative subordinated perpetual preferred stock, representing four million shares at \$50 per share par value. Dividends on the preferred stock, if declared by the Board of Directors at its sole discretion, are non-cumulative and are payable quarterly in arrears on the first day of January, April, July and October each year, commencing October 1, 2008, and will accrue at an annual rate equal to 11 percent of the par value of \$50 per share from the date of issuance up to, but excluding, July 1, 2013. Thereafter, dividends will accrue at an annual rate equal to 3-month USD LIBOR plus 6.79 percent. The Series C preferred stock is not mandatorily redeemable at any time. However, the Series C preferred stock will be redeemable at par value, in whole or in part, at our option, on July 1, 2013 and each July 1<sup>st</sup> thereafter. The net proceeds from the sale of the preferred stock were used to increase the Bank's capital and for general corporate purposes. This issuance, together with the \$500 million of Series A and B senior preferred stock already outstanding, increases our total preferred stock outstanding to \$700 million at September 30, 2008. The Series C preferred stock ranks junior, both as to dividends and upon liquidation, to our Series A and B preferred stock, and senior to all of our outstanding common stock and participation certificates. For regulatory capital purposes, our Series C preferred stock is included in permanent capital, total surplus and core surplus.

In September 2008, our shareholders approved a measure allowing COBANK to issue or reissue preferred stock, up to the bylaw limit of \$1.0 billion, at any time through September 2018. This measure allows us to access outside capital more quickly and efficiently in response to dynamic market conditions.

In April 2008, we issued \$500 million of 7.875 percent fixed rate unsecured subordinated notes due in 2018 to increase the Bank's regulatory permanent capital and total surplus levels and for general corporate purposes. This issuance, together with the \$500 million of floating rate subordinated debt issued in 2007, increased our total subordinated debt outstanding to \$1.0 billion as of September 30, 2008. This debt is subordinate to all other creditors, including general creditors, and is senior to all classes of shareholders. For regulatory capital purposes, subject to certain limitations, subordinated debt is included in permanent capital and total surplus and excluded from liabilities in the net collateral ratio.

We complied with all regulatory capital adequacy standards at September 30, 2008. Our permanent capital ratio (generally average shareholders' equity and subordinated debt subject to certain limitations as a percentage of average risk-adjusted assets for the most recent three months) was 12.96 percent at September 30, 2008, compared to 12.14 percent at December 31, 2007, both of which exceeded the 7.0 percent minimum regulatory requirement.

Our core surplus ratio (average unallocated retained earnings and other components of equity as allowed by the FCA as a percentage of average risk-adjusted assets for the most recent three months) was 7.00 percent at September 30, 2008, compared to 4.94 percent at December 31, 2007, both of which exceeded the 3.5 percent minimum regulatory requirement. Effective January 1, 2008, the FCA determined that we may include a significant portion of our common stock and participation certificates as core surplus, subject to certain conditions, on a temporary basis that would likely continue until the earlier of December 31, 2012 or in the event the FCA changes its capital regulations in a manner that would be inconsistent with this treatment. As a result of this action, our core surplus ratio increased by approximately 1.6 percent. As part of its determination, the FCA requires that we continue to calculate our core surplus ratio excluding common stock and participation certificates and has established a 3.0 percent minimum for such ratio. As of September 30, 2008, our core surplus ratio excluding common stock and participation certificates was 5.21 percent.

Our net collateral ratio (eligible assets divided by total liabilities excluding subordinated debt and other items, subject to certain limitations) at September 30, 2008 was 107.8 percent, compared to 107.1 percent at December 31, 2007, both of which exceeded the regulatory minimum of 103.0 percent and the higher minimum of 104.0 percent required by our regulator during the period in which we have Series A preferred stock or subordinated debt outstanding.

### ***Interest Rate Risk Management***

Interest rate risk is managed by adjusting the Bank's mix of interest-sensitive assets and liabilities through various interest rate risk management products, including interest rate swaps and other financial instruments (derivatives). Derivatives are recorded at fair value as assets or liabilities on the condensed consolidated balance sheets. Changes in the fair value of these derivatives are accounted for as gains or losses through current period earnings or as a component of accumulated other comprehensive income (loss), depending on the use of the derivatives and whether they qualify for hedge accounting treatment. Changes in the fair value of derivatives recorded in the condensed consolidated statements of income totaled a gain of \$4.5 million in the first nine months of 2008, as compared to a loss of \$1.5 million in the same prior year period. Changes in the fair value of derivatives recorded in other comprehensive income (loss) were losses, net of deferred taxes, of \$1.3 million and \$4.4 million for the first nine months of 2008 and 2007, respectively.

### ***Insurance Premiums***

The Food, Conservation and Energy Act of 2008 was enacted in May 2008 and includes changes that authorize the Insurance Corporation to collect higher levels of premiums and expand the base upon which premiums are charged. Under the new assessment formula, premiums of up to 20 basis points can be charged against Systemwide debt securities reduced by loans and investment securities guaranteed by the U.S. government. Premiums of up to an additional 10 basis points can be charged for any nonaccrual loan volume or investments that are other-than-temporarily impaired. Through June 30, 2008, premiums were only assessed on loan volume (up to 15 basis points on accruing loans and up to 25 basis points on nonaccrual loans). Effective July 1, 2008, the Insurance Corporation modified its premium structure to the new Systemwide debt securities base and charged premium rates of 15 basis points for the third quarter of 2008, with premium surcharges of 10 basis points for nonaccrual loan volume and other-than-temporarily impaired investment securities. Insurance premium rates were raised to 18 basis points for the fourth quarter of 2008 (the aforementioned premium surcharges in the third quarter of 2008 also continue to remain in effect). We have been informed by the Insurance Corporation that our premium rates will be raised to the maximum 20 basis points beginning January 1, 2009. If the new premium assessment formula had been in place January 1, 2008 at the maximum level of 20 basis points, our insurance premium expenses would have been approximately \$16 million higher in the first nine months of 2008.

### ***Restricted Cash and Investment in Farmer Mac***

At September 30, 2008, we placed \$15.5 million into an escrow account, which represents COBANK's proportionate share of an investment made by each of the System banks in the Federal Agricultural Mortgage Corporation (Farmer Mac). On October 1, 2008, funds were released from escrow and System banks collectively invested a total of \$60 million in Series B-1 senior cumulative perpetual preferred stock of Farmer Mac, representing 60,000 shares at \$1,000 per share par value. COBANK's proportionate share of the investment

totaled \$15.5 million, representing 15,500 shares. This transaction is more fully described in Note 8 to the accompanying unaudited condensed consolidated financial statements.

### ***Hedge Contract Terminations***

During the quarter ended September 30, 2008, we terminated approximately \$1.6 billion in notional value of interest rate swaps to reduce our credit exposure with two counterparties. We replaced these positions by entering into \$1.5 billion in notional value of interest rate swaps with different highly-rated counterparties. We received \$42.2 million in proceeds as a result of the hedge contract terminations, which is reflected under operating activities in the accompanying unaudited condensed consolidated statement of cash flows for the nine months ended September 30, 2008.

## **Recent Accounting Pronouncements**

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In March 2008, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 161, Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133 (FAS 161). FAS 161 is intended to enhance the current disclosure framework of Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities (FAS 133). It requires disclosure about the location and amounts of derivative instruments in an entity's financial statements; how derivative instruments and related hedged items are accounted for under FAS 133; and how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. FAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. The adoption of FAS 161 will not have an effect on our consolidated financial position, results of operations or cash flows but will impact our disclosures related to derivatives.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities - Including an amendment of FASB Statement No. 115 (FAS 159). FAS 159 permits entities to choose on an instrument-by-instrument basis, at specified election dates, to measure financial assets and liabilities and certain other items at fair value (the "fair value option"). Unrealized gains and losses on items for which the fair value option has been elected must be reported in earnings at each subsequent reporting date. Up-front costs and fees related to items for which the fair value option is elected shall be recognized in earnings as incurred and not deferred. FAS 159 did not have any effect on our financial position, results of operations or cash flows as we did not elect the fair value option for any of our assets or liabilities during the period ended September 30, 2008; however, we may elect to do so in the future.

Effective January 1, 2008, we adopted the provisions of Statement of Financial Accounting Standards No. 157, Fair Value Measurements (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. See Notes 2 and 4 to the accompanying unaudited condensed consolidated financial statements for a description of FAS 157 and the effect of its adoption.

## **Business Outlook**

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Our Board of Directors and management are committed to continuing our strong financial and operating performance, fulfilling our mission as Rural America's Cooperative Bank serving America's lifeline businesses and being the preferred provider of financial solutions to our customers to enhance their business success.

Our future growth and diversification will be achieved by delivering on our value proposition, creating opportunities to partner with other System institutions, increasing market share, maintaining effective access to the agency debt funding market, optimizing current lending authorities and pursuing various strategic alliances with other financial services organizations.

We seek to enhance our solid financial condition through the continuation of strong earnings, expense discipline, effective risk management, and increased shareholders' equity through the retention of a portion of our earnings and issuance of third-party capital as needed. Although we believe our overall loan portfolio credit quality will continue to be good compared to our historical levels, we expect it will likely decline toward less favorable levels as a result of current conditions affecting certain customer segments. We will continue to closely monitor asset quality and emphasize effective management of credit risk, interest rate risk, liquidity risk and operational risk.

## **Forward-Looking Statements**

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Certain of the statements contained in this unaudited quarterly report that are not historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act. Our actual results may differ materially from those included in the forward-looking statements that relate to our plans, projections, expectations and intentions. Forward-looking statements are typically identified by words such as "believe," "expect," "anticipate," "intend," "estimate," "plan," "project," "may," "will," "should," "would," "could" or similar expressions. Although we believe that the information expressed or implied in such forward-looking statements is reasonable, we can give no assurance that such projections and expectations will be realized or the extent to which a particular plan, projection or expectation may be realized. These forward-looking statements are based on current knowledge and are subject to various risks and uncertainties, including, but not limited to: fluctuations in the agricultural, communications, energy and water, international, financing and leasing sectors; weak U.S. and global economic conditions; sovereign or regulatory actions; macro-economic factors and political policies and developments in the U.S. and other countries in which we make loans; the level of interest rates; changes in assumptions underlying the valuations of financial instruments; changes in the bases for our estimates underlying the allowance for credit losses; economic conditions and credit performance of the loan and lease portfolios, portfolio growth and seasonal factors; failure of our investment portfolio to perform as expected or deterioration in the credit quality of such investments, including the credit quality of insurers of such investments; the effect of banking and financial services reforms; possible amendments to, and interpretations of, risk-based capital guidelines and reporting instructions; the ability of states to adopt more extensive consumer protections through legislation or regulation; the resolution of legal proceedings and related matters; changes in the U.S. government's support of the agriculture industry; weather-related conditions that impact agricultural productivity and income; environmental-related conditions or laws impacting our lending activities; actions taken by the U.S. Congress relative to Government Sponsored Enterprises; actions taken by the Federal Reserve in managing the monetary policy of the U.S.; nonperformance by counterparties to our derivative positions; and our ability to successfully integrate and profitably operate any future business combinations or strategic alliances. We expressly disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

# Condensed Consolidated Statements of Income

COBANK, ACB

*\$ in thousands*

<i>(Unaudited)</i>	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2007	2008	2007
<b>Interest Income</b>				
Loans and Leases	\$ 513,700	\$ 570,469	\$ 1,669,626	\$ 1,702,360
Investment Securities	115,383	114,385	338,248	310,183
Federal Funds Sold, Securities Purchased Under Resale Agreements and Other	4,506	4,861	11,582	17,707
Total Interest Income	633,589	689,715	2,019,456	2,030,250
<b>Interest Expense</b>	411,095	537,772	1,347,533	1,555,931
Net Interest Income	222,494	151,943	671,923	474,319
Provision for Credit Losses	-	-	-	-
Net Interest Income After Provision for Credit Losses	222,494	151,943	671,923	474,319
<b>Noninterest Income / Expense</b>				
Net Fee Income	16,634	11,173	44,772	31,690
Prepayment Income	3,754	1,831	17,106	2,324
Losses on Early Extinguishments of Debt	(13,455)	(6,678)	(24,227)	(6,927)
Other, Net	5,040	2,264	7,914	6,219
Total Noninterest Income	11,973	8,590	45,565	33,306
<b>Noninterest Expenses</b>				
Employee Compensation	25,593	22,730	72,516	66,747
Insurance Fund Premium	12,852	8,572	36,886	25,530
Information Services	4,060	5,014	12,588	13,446
Occupancy and Equipment	1,936	1,627	5,287	4,380
Farm Credit System Related	1,440	1,340	4,311	4,020
Other	9,303	5,815	20,223	18,023
Total Noninterest Expenses	55,184	45,098	151,811	132,146
Income Before Income Taxes	179,283	115,435	565,677	375,479
Provision for Income Taxes	38,400	17,034	116,851	71,747
<b>Net Income</b>	\$ 140,883	\$ 98,401	\$ 448,826	\$ 303,732

The accompanying notes are an integral part of the condensed consolidated financial statements.

# Condensed Consolidated Balance Sheets

COBANK, ACB

*\$ in thousands*

	September 30, 2008 <i>(Unaudited)</i>	December 31, 2007
<b>Assets</b>		
Total Loans and Leases	\$ 43,109,714	\$ 40,491,486
Less: Allowance for Credit Losses	440,529	447,226
Net Loans and Leases	42,669,185	40,044,260
Cash	494,631	40,415
Restricted Cash (Note 8)	15,500	-
Investment Securities	13,386,050	10,434,371
Federal Funds Sold, Securities Purchased		
Under Resale Agreements and Other	155,000	647,400
Interest Rate Swaps and		
Other Financial Instruments	489,376	455,612
Accrued Interest Receivable and Other Assets	689,221	566,838
<b>Total Assets</b>	<b>\$ 57,898,963</b>	<b>\$ 52,188,896</b>
<b>Liabilities</b>		
Bonds and Notes	\$ 52,411,540	\$ 47,563,742
Subordinated Debt (Note 6)	1,000,000	500,000
Interest Rate Swaps and		
Other Financial Instruments	113,515	56,823
Accrued Interest Payable and Other Liabilities	847,338	834,907
Total Liabilities	54,372,393	48,955,472
Commitments and Contingencies (Note 9)		
<b>Shareholders' Equity</b>		
Preferred Stock (Note 7)	700,000	500,000
Common Stock and Participation Certificates	1,334,710	1,291,421
Unallocated Retained Earnings	1,640,115	1,470,191
Accumulated Other Comprehensive Loss	(148,255)	(28,188)
Total Shareholders' Equity	3,526,570	3,233,424
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 57,898,963</b>	<b>\$ 52,188,896</b>

The accompanying notes are an integral part of the condensed consolidated financial statements.

# Condensed Consolidated Statements of Cash Flows

COBANK, ACB

*\$ in thousands*

<b>For the Nine Months Ended September 30, (Unaudited)</b>	<b>2008</b>	<b>2007</b>
<b>Cash Flows Provided by Operating Activities</b>		
Net Income	\$ 448,826	\$ 303,732
Adjustments to Reconcile Net Income to Net Cash Provided By Operating Activities:		
Deferred Income Taxes	71,978	(7,178)
Depreciation, Amortization and Accretion, Net	12,341	13,774
Increase in Accrued Interest Receivable and Other Assets	(100,282)	(61,394)
Increase (Decrease) in Accrued Interest Payable and Other Liabilities	(7,139)	21,297
Net Gains on Interest Rate Swaps and Other Financial Instruments	(7,284)	(1,824)
Proceeds from Termination of Interest Rate Swaps	42,234	-
Other	5,181	1,867
Net Cash Provided by Operating Activities	465,855	270,274
<b>Cash Flows Used in Investing Activities</b>		
Net Increase in Loans and Leases	(2,629,912)	(3,252,719)
Net Increase in Investment Securities	(3,148,271)	(2,061,666)
Net Decrease in Federal Funds Sold, Securities Purchased Under Resale Agreements and Other	492,400	443,100
Other	(15,500)	-
Net Cash Used in Investing Activities	(5,301,283)	(4,871,285)
<b>Cash Flows Provided by Financing Activities</b>		
Net Issuance of Bonds and Notes	4,824,240	4,315,148
Net Issuance of Subordinated Debt	496,750	496,750
Net Retirements of Common Stock and Participation Certificates	(40,678)	(50,425)
Cash Patronage Distribution and Other	(155,013)	(124,160)
Proceeds from Issuance of Preferred Stock, Net	197,560	-
Preferred Stock Dividends	(33,215)	(28,082)
Net Cash Provided by Financing Activities	5,289,644	4,609,231
Net Increase in Cash	454,216	8,220
Cash at Beginning of Period	40,415	6,420
Cash at End of Period	\$ 494,631	\$ 14,640
<b>Supplemental Disclosures:</b>		
<b>Schedule of Noncash Investing and Financing Activities:</b>		
Net Change in Accrued Purchases of Securities	\$ -	\$ 957,265
Net Change in Unrealized Losses on Investment Securities, Before Taxes	(191,534)	23,681
Net Change in Unrealized Losses/Gains on Interest Rate Swaps and Other Financial Instruments, Before Taxes	(2,120)	(7,206)
Patronage in Common Stock and Participation Certificates	83,967	64,168

The accompanying notes are an integral part of the condensed consolidated financial statements.

# Condensed Consolidated Statements of Changes in Shareholders' Equity

COBANK, ACB

*\$ in thousands*

For the Nine Months Ended September 30, <i>(Unaudited)</i>	2008	2007
Balance at Beginning of Period	\$ 3,233,424	\$ 3,040,058
Adjustments for the Adoption of New Accounting Pronouncements (Note 2)	(609)	(250)
Balance at Beginning of Period, as Adjusted	3,232,815	3,039,808
Comprehensive Income:		
Net Income	448,826	303,732
Other Comprehensive Income, Net of Taxes:		
Net Change in Unrealized Losses on Investment Securities	(118,751)	15,559
Net Change in Unrealized Losses/Gains on Interest Rate Swaps and Other Financial Instruments	(1,314)	(4,444)
Net Pension-related Adjustment	(2)	31
Comprehensive Income	328,759	314,878
Preferred Stock Issued	200,000	-
Preferred Stock Issuance Costs	(2,440)	-
Preferred Stock Dividends	(33,215)	(28,082)
Common Stock / Participation Certificates Issued	80	83
Common Stock / Participation Certificates Retired	(40,758)	(50,508)
Cash Patronage Distribution Payable and Other	(158,671)	(114,299)
<b>Balance at End of Period</b>	<b>\$ 3,526,570</b>	<b>\$ 3,161,880</b>

The accompanying notes are an integral part of the condensed consolidated financial statements.

# Notes to Condensed Consolidated Financial Statements

## COBANK, ACB

*(Unaudited) (\$ in Thousands, Except as Noted)*

### **Note 1 – Organization, Lending Authority and Significant Accounting Policies**

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The accompanying unaudited condensed consolidated financial statements include the accounts of COBANK, ACB and its wholly-owned subsidiary, Farm Credit Leasing Services Corporation (FCL), collectively hereinafter referred to as COBANK or the Bank. All material inter-company accounts and transactions have been eliminated. In our opinion, all adjustments considered necessary for a fair presentation of the interim financial condition, results of operations and cash flows have been made. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. Our results of operations for the nine months ended September 30, 2008 are not necessarily indicative of results to be expected for the entire fiscal year.

The accompanying unaudited condensed consolidated financial statements exclude financial information of Northwest Farm Credit Services, ACA (Northwest) as well as the System Associations in the Northeastern region of the United States (Northeast Associations), which are collectively referred to as our affiliated Associations. COBANK and our affiliated Associations are collectively referred to as the “District.” The supplemental information on pages 28 and 29 includes certain unaudited combined financial information of our affiliated Associations and the District.

Copies of COBANK’s financial reports are available on request by calling or visiting one of our banking center locations and through our website at [www.cobank.com](http://www.cobank.com). Copies of financial reports of our affiliated Associations and the System are available on their respective websites, which can also be accessed through links on our COBANK website under “Farm Credit Partners.”

These unaudited quarterly condensed consolidated financial statements should be read in conjunction with the 2007 Annual Report. A description of our organization and lending authority is contained in our 2007 Annual Report. Also included in the 2007 Annual Report is a summary of significant accounting policies as well as the financial condition and consolidated results of operations as of and for the year ended December 31, 2007. These unaudited quarterly condensed consolidated financial statements have been prepared in accordance with these same accounting policies.

### **Note 2 – Adoption of New Accounting Pronouncements**

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In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We adopted FAS 157 effective January 1, 2008. The adoption of FAS 157 did not have a material effect on our financial position, results of operations or cash flows; however, we have expanded our fair value disclosures in accordance with FAS 157 as disclosed in Note 4.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 158, Employers’ Accounting for Defined Benefit Pension and Other Postretirement Benefits (FAS 158). FAS 158 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 to recognize changes in that funded status in the year in which the changes occur through comprehensive income (loss), a component of shareholders’ equity. We adopted these recognition requirements as of December 31, 2007 and the effects were reflected in our audited financial statements as of that date. FAS 158 also requires the measurement date for plan assets and liabilities to coincide with the employer’s fiscal year-end. This requirement is effective for fiscal years ending after

December 15, 2008. See Note 5 for a description of the effect of the adoption of the change in measurement date requirement.

As previously disclosed in our 2007 Annual Report, effective January 1, 2007, we adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (FIN 48). As a result of the adoption of FIN 48, effective January 1, 2007, we recognized a \$250 thousand increase in the liability for unrecognized tax benefits, which was accounted for as a reduction to retained earnings.

### Note 3 – Allowance for Credit Losses

The following tables present a summary of changes in the allowance for credit losses as well as information concerning impaired loans and leases.

#### Allowance for Credit Losses

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2008	2007	2008	2007
Balance at Beginning of Period	\$ 438,490	\$ 445,032	\$ 447,226	\$ 438,231
Provision for Credit Losses	-	-	-	-
Charge-offs	(92)	(91)	(13,073)	(252)
Recoveries	2,131	3,562	6,376	10,524
Balance at End of Period	\$ 440,529	\$ 448,503	\$ 440,529	\$ 448,503

Impaired loans and leases are those loans and leases for which it is probable that all principal and interest will not be collected according to the contractual terms. Impaired loan and lease information is shown in the following table, including loans and leases past due 90 days or more and still accruing interest, which are adequately secured and in the process of collection.

#### Impaired Loan and Lease Information

	September 30, 2008	December 31, 2007
Nonaccrual Loans and Leases	\$ 62,677	\$ 14,808
Accruing Loans and Leases 90 Days or More Past Due	440	1,563
Restructured Loans	204	336
Total Impaired Loans and Leases	\$ 63,321	\$ 16,707
Impaired Loans and Leases with Related Specific Allowance	\$ 49,482	\$ 3,850
Impaired Loans and Leases without Related Specific Allowance	13,839	12,857
Total Impaired Loans and Leases	\$ 63,321	\$ 16,707
Specific Allowance on Impaired Loans and Leases	\$ 12,485	\$ 1,026
Other Property Owned	3	3

  

For the Nine Months Ended September 30,	2008	2007
Average Impaired Loans and Leases	\$ 58,554	\$ 78,407
Interest Income Recognized on Impaired Loans and Leases	8,120	13,053

<b>Allowance for Credit Losses as a Percentage of:</b>	<b>September 30, 2008</b>	<b>December 31, 2007</b>
Total Loans and Leases	1.02%	1.10%
Impaired Loans and Leases	696	2,677
Nonaccrual Loans and Leases	703	3,020

## **Note 4 – Fair Value Measurements**

As described in Note 2, we adopted FAS 157 effective January 1, 2008. FAS 157 establishes a fair value hierarchy for disclosure of fair value measurements to maximize the use of observable inputs, that is, inputs that reflect the assumptions market participants would use in pricing an asset or liability based on market data obtained from sources independent of the reporting entity. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The three levels of inputs and the classification of our financial instruments within the fair value hierarchy are as follows:

### ***Level 1***

Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets. Level 1 assets and liabilities include investment securities and derivative contracts that are traded in an active exchange market, in addition to certain U.S. Treasury securities that are highly-liquid and are actively traded in over-the-counter markets. Our Level 1 assets at September 30, 2008 consist of assets held in a trust fund related to deferred compensation, our supplemental executive retirement plan and our executive retirement plan. The trust fund includes investments in securities that are actively traded and have quoted net asset value prices that are directly observable in the marketplace.

### ***Level 2***

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets; quoted prices in markets that are not active; and inputs that are observable, or can be corroborated, for substantially the full term of the asset or liability. Level 2 assets and liabilities include investment securities that are traded in active, non-exchange markets and derivative contracts that are traded in active, over-the-counter markets.

The fair value of substantially all of our investment securities is determined from third-party valuation models that estimate current market prices. Inputs and assumptions related to third-party market valuation models are typically observable in the marketplace. Such models incorporate prepayment assumptions and underlying mortgage- or asset-backed collateral information to generate cash flows that are discounted using appropriate benchmark interest rate curves and volatilities. Third-party valuations also incorporate information regarding broker/dealer quotes, available trade information, historical cash flows, credit ratings, and other market information. Such valuations represent an estimated exit price, or price to be received by a seller in active markets to sell the investment securities to a willing participant.

The fair value of our derivative financial instruments is the estimated amount to be received to sell a derivative asset or paid to transfer or extinguish a derivative liability in active markets among willing participants at the reporting date. Estimated fair values are determined through internal market valuation models. These models incorporate benchmark interest rate curves, volatilities and other inputs that are observable directly or indirectly in the marketplace. We compare internally calculated derivative valuations to broker/dealer quotes to substantiate the results.

Our Level 2 assets and liabilities at September 30, 2008 include our derivative contracts and investment securities in U.S. government and agency mortgage-backed securities, non-agency mortgage-backed securities and U.S. agency debt securities, all of which have unadjusted values from third-party or internal pricing models. Our Level 2 assets also include federal funds sold, securities purchased under resale agreements and other highly-liquid funds, all of which are non-exchange-traded instruments. The market value of these federal funds sold and other instruments is generally their face value, plus accrued interest, as these instruments are highly-liquid, readily convertible to cash and short-term in nature. Additionally, our Level 2 assets and liabilities include collateral balances, which are required under collateral support and master agreements associated with our derivative contracts. The market value of collateral assets and liabilities is their face value, plus accrued interest, as these instruments are cash balances; therefore, fair value approximates face value.

### ***Level 3***

Level 3 inputs to the valuation methodology are unobservable and supported by limited or no market activity. Level 3 assets and liabilities include investments and derivative contracts whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, and other instruments for which the determination of fair value requires significant management judgment or estimation. Level 3 assets and liabilities also include investments and derivative contracts whose price has been adjusted based on dealer quoted pricing that is different from third-party valuation or internal model pricing.

Our Level 3 assets at September 30, 2008 include our asset-backed investment securities of which substantially all have unadjusted values from third-party pricing models. Based on the continued marketplace illiquidity for home-equity-related asset-backed investments and the lack of marketplace information available as inputs and assumptions to the valuation process, we classified our asset-backed investment portfolio as Level 3 assets. One of our Level 3 asset-backed securities with a fair value of \$4.4 million at September 30, 2008 was determined to be other-than-temporarily impaired resulting in a \$6.0 million loss being recognized during the three months ended June 30, 2008. Our Level 3 liabilities at September 30, 2008 include standby letters of credit whose market value is internally calculated based on information that is not observable either directly or indirectly in the marketplace.

### ***Assets and Liabilities Measured at Fair Value on a Recurring Basis***

The following table presents the assets and liabilities that are measured at fair value on a recurring basis at September 30, 2008 for each of the fair value hierarchy levels.

#### **Assets and Liabilities Measured at Fair Value on a Recurring Basis**

**As of September 30, 2008**

	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>Assets</b>				
Investment Securities	\$ -	\$ 13,082,163	\$ 303,887	\$ 13,386,050
Federal Funds Sold, Securities Purchased Under Resale Agreements and Other	-	155,000	-	155,000
Interest Rate Swaps and Other Financial Instruments	-	489,376	-	489,376
Assets Held in Trust (included in Other Assets)	33,605	-	-	33,605
<b>Total Assets</b>	\$ 33,605	\$ 13,726,539	\$ 303,887	\$ 14,064,031
<b>Liabilities</b>				
Interest Rate Swaps and Other Financial Instruments	\$ -	\$ 106,553	\$ 6,962	\$ 113,515
Collateral Liabilities (included in Bonds and Notes)	-	170,690	-	170,690
<b>Total Liabilities</b>	\$ -	\$ 277,243	\$ 6,962	\$ 284,205

The following table presents the changes in Level 3 assets and liabilities measured at fair value on a recurring basis:

<b>Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis</b>			
		<b>Asset-Backed Investment Securities</b>	<b>Standby Letters of Credit</b>
<b>Balance at January 1, 2008</b>	\$	379,555	\$ 5,077
Total Gains or Losses (Realized/Unrealized):			
Included in Other Noninterest Expense		(6,000)	-
Included in Other Comprehensive Loss		(21,732)	-
Purchases, Sales, Issuances and Settlements, Net		(47,936)	1,885
<b>Balance at September 30, 2008</b>	\$	303,887	\$ 6,962

## **Note 5 – Employee Benefit Plans**

We have employer-funded qualified defined benefit pension plans which are noncontributory and cover employees hired prior to January 1, 2007. We have an employee savings plan pursuant to which we match a certain percentage of employees' elective contributions. Under this plan, employees hired on or after January 1, 2007 receive a fixed percentage of their eligible wages in their retirement account and a higher level of matching contributions than employees hired prior to that date. We also have a noncontributory, unfunded non-qualified supplemental executive retirement plan (SERP) that covers a limited number of our executives and senior managers, as well as an unfunded non-qualified executive retirement plan (ERP) designed to provide enhanced retirement benefits to certain of our most senior executives. In addition, we have other postretirement benefit plans that cover substantially all of our employees. These other postretirement benefit plans are unfunded contributory plans with participant contributions adjusted annually. Substantially all participants pay the full premiums associated with these plans.

We contributed \$15.3 million to our funded qualified defined benefit pension plans during the nine months ended September 30, 2008 and anticipate that we will contribute an additional \$7.9 million to such plans during the remainder of 2008. We expect to contribute a total of \$0.3 million, net of collected retiree premiums, to our other postretirement benefit plans during 2008. During 2008, we have transferred approximately \$2.7 million into our trust funds related to our SERP and ERP.

As described in Note 2, we adopted the recognition provisions of FAS 158 in 2007. FAS 158 also requires the measurement date for plan assets and liabilities to coincide with the employer's fiscal year-end. This requirement is effective for fiscal years ending after December 15, 2008. We have historically used September 30 as the measurement date for our pension and other postretirement benefit plans. FAS 158 provides two approaches for an employer to transition to a fiscal year-end measurement date. We have applied the approach which allows for the use of measurements determined for the year-end reporting as of the fiscal year immediately preceding the year during which the measurement date provisions are applied. Under this alternative, pension and postretirement benefit expense measured for the three-month period October 1, 2007 to December 31, 2007 (determined using the September 2007 measurement date) of \$1.0 million was recorded in retained earnings at January 1, 2008. As a result, we decreased retained earnings by \$0.6 million, net of taxes, decreased other assets by \$0.1 million and increased other liabilities by \$0.5 million.

## **Note 6 – Subordinated Debt**

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In April 2008, we issued \$500 million of 7.875 percent unsecured subordinated notes due in 2018, generating proceeds of \$496.8 million. The proceeds were used to increase our regulatory permanent capital and total surplus pursuant to Farm Credit Administration regulations and for general corporate purposes. This debt is unsecured and subordinate to all other creditors, including general creditors, and is senior to all classes of shareholders. Interest is payable semi-annually on April 15 and October 15. Interest will be deferred if, as of the fifth business day prior to an interest payment due date, any applicable minimum regulatory capital ratios are not satisfied. A deferral period may not last for more than five consecutive years or beyond the maturity date of the subordinated debt. During such a period, we may not declare or pay any dividends or patronage refunds, among certain other restrictions, until interest payments are resumed and all deferred interest has been paid. The subordinated debt is not considered Systemwide debt and is not guaranteed by the Farm Credit System or any banks in the System, other than COBANK. Payments on the subordinated notes are not insured by the Farm Credit Insurance Fund, a statutorily created insurance fund more fully described in Note 9.

## **Note 7 – Preferred Stock**

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In March 2008, our shareholders approved a bylaw amendment to increase the authorized amount of preferred stock the Bank may have outstanding from \$500 million to \$1.0 billion. At that time, our shareholders also approved the issuance of up to \$250 million of preferred stock prior to the end of 2009. On July 7, 2008, we issued \$200 million of Series C non-cumulative subordinated perpetual preferred stock, representing four million shares at \$50 per share par value. This issuance, when combined with our two previous issuances, increased our outstanding preferred stock to \$700 million at September 30, 2008.

The net proceeds from the July sale of the Series C preferred stock were used to increase the Bank's capital and for general corporate purposes. Dividends on the Series C preferred stock, if declared by the Board of Directors at its sole discretion, are non-cumulative and are payable quarterly in arrears on the first day of January, April, July and October each year, commencing October 1, 2008, and will accrue at an annual rate equal to 11 percent of the par value of \$50 per share from the date of issuance up to, but excluding, July 1, 2013. Thereafter, dividends will accrue at an annual rate equal to 3-month USD LIBOR plus 6.79 percent. The Series C preferred stock is not mandatorily redeemable at any time. However, the Series C preferred stock will be redeemable at par value, in whole or in part, at our option, on July 1, 2013 and each July 1<sup>st</sup> thereafter. The Series C preferred stock ranks, both as to dividends and upon liquidation, junior to our Series A and B preferred stock, and senior to all of our outstanding common stock and participation certificates.

In September 2008, our shareholders approved a measure allowing COBANK to issue or reissue preferred stock, up to the bylaw limit of \$1.0 billion, at any time through September 2018.

## **Note 8 – Restricted Cash and Investment in Farmer Mac**

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At September 30, 2008, we placed \$15.5 million into an escrow account, which represents COBANK's proportionate share of an investment made by each System bank in the Federal Agricultural Mortgage Corporation (Farmer Mac), as described below. This amount is classified as restricted cash in our accompanying September 30, 2008 unaudited condensed consolidated balance sheet.

On October 1, 2008, funds were released from escrow and System banks collectively invested an aggregate total of \$60 million of Series B-1 senior cumulative perpetual preferred stock of Farmer Mac, representing 60,000 shares at \$1,000 per share par value. COBANK's proportionate share of the System's investment totaled \$15.5 million, representing 15,500 shares. Dividends on the preferred stock are cumulative and will be payable quarterly, in cash, at an annual interest rate of ten percent, increasing by two percent in each of the first three years, up to a maximum of 16 percent. Interest payments are due in March, June, September and December of each year, beginning in December 2008. The preferred stock is callable at par value after nine months, and on any quarterly dividend date thereafter. Additionally, the stock is redeemable in whole by Farmer Mac beginning nine months after the date of issuance with cash or certain qualifying assets. Farmer Mac will use the net proceeds from the preferred stock sale to strengthen its capital position and comply with its minimum regulatory

capital requirements, thereby promoting the steady and dependable flow of capital to rural America. COBANK and the System will account for this investment using the cost method of accounting; accordingly, the investment will be carried at its historical cost and adjusted for distributions to owners as they occur.

## **Note 9 – Commitments and Contingencies**

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Under the Farm Credit Act of 1971, as amended, COBANK is primarily liable for its portion of Systemwide debt securities. Additionally, we are contingently liable for the Systemwide debt securities of the other System banks. Total Systemwide debt securities of the System were \$173.6 billion at September 30, 2008.

There are several mechanisms in place affecting exposure to statutory joint and several liabilities. These mechanisms include:

- The statutory requirement for System banks to maintain eligible assets at a level at least equal in value to the total amount of debt for which each System bank is primarily liable;
- Maintenance of certain financial criteria by contract which, if not met, could limit or ultimately deny a troubled System bank's access to and participation in System debt issuances; and
- The Farm Credit Insurance Fund, a statutorily created insurance fund to assist in the timely payment of principal and interest on Systemwide debt securities in the event of a default by a System bank to the extent that net assets are available in the insurance fund. At September 30, 2008, the assets of the insurance fund aggregated \$2.8 billion.

At September 30, 2008, various lawsuits were pending or threatened against the Bank in which claims for monetary damages have been or may be asserted. In the opinion of management, based on information currently available and taking into account the advice of legal counsel, the ultimate liability, if any, of pending or threatened legal actions will not have a material adverse impact on our consolidated results of operations or financial position.

## **Note 10 – Segment Financial Information**

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We conduct our lending and leasing operations through four operating segments: Agribusiness Banking Group (ABG), Strategic Relationships Division (SRD), Communications and Energy Banking Group (CEBG) and Global Financial Services Group (GFSG).

The accompanying tables present condensed disaggregated information for the segments. Allocation of resources and corporate items, as well as measurement of financial performance, is made at these operating segment levels. We also allocate net interest income on investment securities, federal funds sold, securities purchased under resale agreements and other highly-liquid funds to our segments. Information to reconcile the total reportable segments to the total COBANK financial statements is shown as "other." Inter-segment transactions are insignificant.

We do not hold significant assets in any foreign country. Our international loans are dollar-denominated and the majority of these loans are guaranteed by a U.S. government-sponsored loan guarantee program.

For the nine months ended September 30, 2008 and 2007, interest earned from an affiliated Association, Northwest, represented nine percent and ten percent, respectively, of our gross interest income and three percent and five percent, respectively, of our net interest income. No other customer made up ten percent or more of our gross or net interest income for the periods presented.

# Condensed Segment Financial Information

## CoBANK, ACB

### For the Three Months Ended September 30, 2008

	ABG	SRD	CEBG	GFSG	Subtotal	Other	Total CoBANK
<b>Results of Operations (\$ in Thousands):</b>							
Net Interest Income	\$ 115,247	\$ 20,984	\$ 59,228	\$ 27,393	\$ 222,852	\$ (358)	\$ 222,494
Provision for Credit Losses	-	-	-	-	-	-	-
Noninterest Income	1,952	2,527	3,597	4,528	12,604	(631)	11,973
Noninterest Expense	24,785	3,737	13,585	9,769	51,876	3,308	55,184
Provision for Income Taxes	23,596	-	9,647	6,052	39,295	(895)	38,400
<b>Net Income</b>	<b>\$ 68,818</b>	<b>\$ 19,774</b>	<b>\$ 39,593</b>	<b>\$ 16,100</b>	<b>\$ 144,285</b>	<b>\$ (3,402)</b>	<b>\$ 140,883</b>

### For the Three Months Ended September 30, 2007

	ABG	SRD	CEBG	GFSG	Subtotal	Other	Total CoBANK
<b>Results of Operations (\$ in Thousands):</b>							
Net Interest Income	\$ 75,518	\$ 15,136	\$ 39,647	\$ 21,865	\$ 152,166	\$ (223)	\$ 151,943
Provision (Reversal) for Credit Losses	3,000	-	(7,000)	4,000	-	-	-
Noninterest Income	4,628	1,211	634	2,446	8,919	(329)	8,590
Noninterest Expense	19,572	2,431	11,804	8,927	42,734	2,364	45,098
Provision (Benefit) for Income Taxes	8,784	(541)	6,946	2,374	17,563	(529)	17,034
<b>Net Income</b>	<b>\$ 48,790</b>	<b>\$ 14,457</b>	<b>\$ 28,531</b>	<b>\$ 9,010</b>	<b>\$ 100,788</b>	<b>\$ (2,387)</b>	<b>\$ 98,401</b>

# Condensed Segment Financial Information

COBANK, ACB

## For the Nine Months Ended September 30, 2008

	ABG	SRD	CEBG	GFSG	Subtotal	Other	Total CoBANK
<b>Results of Operations (\$ in Thousands):</b>							
Net Interest Income	\$ 378,140	\$ 56,804	\$ 160,994	\$ 76,964	\$ 672,902	\$ (979)	\$ 671,923
Provision for Credit Losses	-	-	-	-	-	-	-
Noninterest Income	9,547	7,380	12,951	16,264	46,142	(577)	45,565
Noninterest Expense	70,964	9,002	37,838	26,526	144,330	7,481	151,811
Provision for Income Taxes	77,123	-	25,734	15,820	118,677	(1,826)	116,851
<b>Net Income</b>	<b>\$ 239,600</b>	<b>\$ 55,182</b>	<b>\$ 110,373</b>	<b>\$ 50,882</b>	<b>\$ 456,037</b>	<b>\$ (7,211)</b>	<b>\$ 448,826</b>

### Selected Financial Information (\$ in Millions):

Loans and Leases, Net of Allowance							
for Credit Losses at September 30, 2008	\$ 10,410	\$ 14,811	\$ 10,462	\$ 6,986	\$ 42,669	\$ -	\$ 42,669
Assets at September 30, 2008	\$ 10,564	\$ 14,887	\$ 10,533	\$ 7,031	\$ 43,015	\$ 14,884*	\$ 57,899

\*Other assets are composed of:

Investment Securities						\$ 13,386
Federal Funds Sold, Securities Purchased Under Resale Agreements and Other						155
Other Assets						1,343

## For the Nine Months Ended September 30, 2007

	ABG	SRD	CEBG	GFSG	Subtotal	Other	Total CoBANK
<b>Results of Operations (\$ in Thousands):</b>							
Net Interest Income	\$ 244,995	\$ 43,123	\$ 121,991	\$ 64,789	\$ 474,898	\$ (579)	\$ 474,319
Provision (Reversal) for Credit Losses	18,000	-	(22,000)	4,000	-	-	-
Noninterest Income	12,966	3,758	6,559	10,647	33,930	(624)	33,306
Noninterest Expense	58,297	6,781	34,834	25,647	125,559	6,587	132,146
Provision for Income Taxes	40,806	-	23,277	10,000	74,083	(2,336)	71,747
<b>Net Income</b>	<b>\$ 140,858</b>	<b>\$ 40,100</b>	<b>\$ 92,439</b>	<b>\$ 35,789</b>	<b>\$ 309,186</b>	<b>\$ (5,454)</b>	<b>\$ 303,732</b>

### Selected Financial Information (\$ in Millions):

Loans and Leases, Net of Allowance							
for Credit Losses at September 30, 2007	\$ 10,696	\$ 11,300	\$ 7,897	\$ 5,998	\$ 35,891	\$ -	\$ 35,891
Assets at September 30, 2007	\$ 10,822	\$ 11,410	\$ 7,971	\$ 6,047	\$ 36,250	\$ 11,124*	\$ 47,374

\*Other assets are composed of:

Investment Securities						\$ 10,503
Federal Funds Sold, Securities Purchased Under Resale Agreements and Other						225
Other Assets						396

# Supplemental District Financial Information

## COBANK, ACB AND AFFILIATED ASSOCIATIONS

Our affiliated Associations operate independently and maintain an arms-length relationship with us, except to the limited extent that the Farm Credit Act requires us, as the funding bank, to monitor and approve certain activities of affiliated Associations. Accordingly, the financial information of affiliated Associations is not included in our consolidated financial statements. However, because of the interdependent manner in which COBANK and its affiliated Associations operate, we believe that presenting combined Bank and Association financial information is meaningful for purposes of additional analysis.

The following condensed Combining Balance Sheets and Combining Statements of Income, together with ratios and other financial information, present condensed combined financial information of COBANK and its affiliated Associations, which are collectively referred to as the District. As part of the combining process, all significant transactions between COBANK and its affiliated Associations, including loans made by the Bank to the affiliated Associations and the interest income/interest expense related thereto, and investments of the affiliated Associations in the Bank and the earnings related thereto, have been eliminated.

### Combining Balance Sheets (Condensed)

*\$ in Millions (Unaudited)*

As of September 30, 2008	COBANK	Combined Affiliated Associations	Eliminations	Combined CoBANK District
Investments, Federal Funds Sold and Other Highly-Liquid Assets	\$ 13,541	\$ -	\$ -	\$ 13,541
Loans and Leases	43,110	12,163	(10,673)	44,600
Less: Allowance for Credit Losses	(441)	(71)	-	(512)
Net Loans and Leases	42,669	12,092	(10,673)	44,088
Other Assets	1,689	717	(501)	1,905
<b>Total Assets</b>	<b>\$ 57,899</b>	<b>\$ 12,809</b>	<b>\$ (11,174)</b>	<b>\$ 59,534</b>
Bonds and Notes	\$ 53,412	\$ 10,787	\$ (10,738)	\$ 53,461
Other Liabilities	960	91	(53)	998
<b>Total Liabilities</b>	<b>54,372</b>	<b>10,878</b>	<b>(10,791)</b>	<b>54,459</b>
<b>Total Shareholders' Equity</b>	<b>3,527</b>	<b>1,931</b>	<b>(383)</b>	<b>5,075</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 57,899</b>	<b>\$ 12,809</b>	<b>\$ (11,174)</b>	<b>\$ 59,534</b>

### As of December 31, 2007

Investments, Federal Funds Sold and Other Highly-Liquid Assets	\$ 11,081	\$ -	\$ -	\$ 11,081
Loans and Leases	40,491	10,541	(9,179)	41,853
Less: Allowance for Credit Losses	(447)	(63)	-	(510)
Net Loans and Leases	40,044	10,478	(9,179)	41,343
Other Assets	1,064	744	(531)	1,277
<b>Total Assets</b>	<b>\$ 52,189</b>	<b>\$ 11,222</b>	<b>\$ (9,710)</b>	<b>\$ 53,701</b>
Bonds and Notes	\$ 48,064	\$ 9,302	\$ (9,260)	\$ 48,106
Other Liabilities	892	111	(65)	938
<b>Total Liabilities</b>	<b>48,956</b>	<b>9,413</b>	<b>(9,325)</b>	<b>49,044</b>
<b>Total Shareholders' Equity</b>	<b>3,233</b>	<b>1,809</b>	<b>(385)</b>	<b>4,657</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 52,189</b>	<b>\$ 11,222</b>	<b>\$ (9,710)</b>	<b>\$ 53,701</b>

Supplemental District Financial Information  
COBANK, ACB AND AFFILIATED ASSOCIATIONS

Combining Statements of Income (Condensed)

\$ in Millions (Unaudited)

For the Nine Months Ended September 30,	COBANK	Combined Affiliated Associations	Eliminations	Combined COBANK District
<b>2008</b>				
Net Interest Income	\$ 672	\$ 229	\$ -	\$ 901
Provision for Credit Losses	-	11	-	11
Noninterest Income	45	71	(40)	76
Noninterest Expense	151	118	-	269
Provision for Income Taxes	117	4	-	121
<b>Net Income</b>	<b>\$ 449</b>	<b>\$ 167</b>	<b>\$ (40)</b>	<b>\$ 576</b>
<b>2007</b>				
Net Interest Income	\$ 474	\$ 211	\$ 1	\$ 686
Provision for Credit Losses	-	7	-	7
Noninterest Income	30	59	(31)	58
Noninterest Expense	128	114	-	242
Provision for Income Taxes	72	2	-	74
<b>Net Income</b>	<b>\$ 304</b>	<b>\$ 147</b>	<b>\$ (30)</b>	<b>\$ 421</b>

Key Financial Ratios – Combined COBANK District

(Unaudited)

For the Nine Months Ended September 30,	2008	2007
Return on Average Assets	1.27%	1.26%
Return on Average Capital	15.78	12.58
Net Interest Margin	2.02	2.06
Operating Expense as a Percent of Net Interest Income and Noninterest Income	27.55	32.83
Net Charge-offs (Recoveries) as a Percent of Average Loans and Leases	0.03	(0.04)
	<b>September 30, 2008</b>	<b>December 31, 2007</b>
Capital as a Percent of Total Assets	8.52%	8.67%
Risk Funds as a Percent of Loans and Leases	12.52	12.34
Allowance for Credit Losses as a Percent of Loans and Leases	1.15	1.22
Debt to Capital (:1)	10.73	10.54

Asset Quality Ratios – Combined COBANK District

(Unaudited)

	September 30, 2008	December 31, 2007
Acceptable	95.63%	96.01%
Other Assets Especially Mentioned	2.36	2.18
Substandard	1.98	1.80
Doubtful	0.03	0.01
Loss	-	-
<b>Total</b>	<b>100.00%</b>	<b>100.00%</b>

## Controls and Procedures

### COBANK, ACB

We maintain a system of disclosure controls and procedures. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information disclosed by us in our quarterly and annual reports is accumulated and communicated to our management, including our principal executive officer and our principal financial officer, as appropriate, to allow timely decisions to be made regarding disclosure. The President and Chief Executive Officer and the Chief Financial and Administrative Officer have evaluated our disclosure controls and procedures as of the end of and for the period covered by this quarterly report and have concluded that our disclosure controls and procedures are effective as of that date.

We also maintain a system of internal controls. The term “internal controls,” as defined by the American Institute of Certified Public Accountants’ Codification of Statement on Auditing Standards, AU Section 319, means a process - effected by the board of directors, management and other personnel - designed to provide reasonable assurance regarding the achievement of objectives in reliability of financial reporting, the effectiveness and efficiency of operations and compliance with applicable laws and regulations. We continually assess the adequacy of our internal control over financial reporting and enhance our controls in response to internal control assessments and internal and external audit and regulatory recommendations. There have been no significant changes in our internal controls or in other factors that could significantly affect such controls subsequent to the date we carried out our evaluations. In accordance with our internal control procedures, these financial statements were prepared under the oversight of the Audit Committee of our Board of Directors.

## CERTIFICATION

I, Robert B. Engel, President and Chief Executive Officer of CoBank, ACB (CoBank or the Bank), a federally chartered instrumentality under the Farm Credit Act of 1971, as amended, certify that:

- (1) I have reviewed this quarterly report of CoBank;
- (2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of CoBank as of, and for, the periods presented in this report;
- (4) CoBank's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures and internal control over financial reporting for CoBank and have:
  - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Bank, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. evaluated the effectiveness of the Bank's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. disclosed in this report any change in the Bank's internal control over financial reporting that occurred during the Bank's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting; and
- (5) CoBank's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Bank's auditors and the audit committee of the Bank's board of directors (or persons performing the equivalent functions):
  - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Bank's ability to record, process, summarize, and report financial information; and
  - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the Bank's internal control over financial reporting.

/s/ ROBERT B. ENGEL

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Robert B. Engel  
*President and Chief Executive Officer*

Dated: November 7, 2008

## CERTIFICATION

I, Brian P. Jackson, Executive Vice President and Chief Financial and Administrative Officer of CoBank, ACB (CoBank or the Bank), a federally chartered instrumentality under the Farm Credit Act of 1971, as amended, certify that:

- (1) I have reviewed this quarterly report of CoBank;
- (2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- (3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations, and cash flows of CoBank as of, and for, the periods presented in this report;
- (4) CoBank's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures and internal control over financial reporting for CoBank and have:
  - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Bank, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. evaluated the effectiveness of the Bank's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. disclosed in this report any change in the Bank's internal control over financial reporting that occurred during the Bank's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting; and
- (5) CoBank's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Bank's auditors and the audit committee of the Bank's board of directors (or persons performing the equivalent functions):
  - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Bank's ability to record, process, summarize, and report financial information; and
  - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the Bank's internal control over financial reporting.

/s/ BRIAN P. JACKSON

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Brian P. Jackson  
*Executive Vice President and Chief Financial and  
Administrative Officer*

Dated: November 7, 2008

# Leadership

COBANK, ACB

## *Executive Office*

**Robert B. Engle**, President and Chief Executive Officer

**Robert L. O'Toole**, Human Resources Division

## *Corporate Services Group*

**Brian P. Jackson**, Executive Vice President and Chief Financial and Administrative Officer

**James R. Bernstein**, Chief Information Officer

**David P. Burlage**, Finance Division

**George P. Delaune**, Administrative Services Division

**Arthur C. Hodges, Jr.**, Corporate Communications Division

**Allan S. Kantrowitz**, Legal Division

**Stephen F. Staley**, Senior Vice President

**John Svisco**, Operations Division

## *Agribusiness Banking Group\**

**Philip S. DiPofi**, Executive Vice President

**Robert E. Egerton**, Agribusiness Division – East

**Amy H. Gales**, Agribusiness Division – Central

**Dean W. Moreau**, Agribusiness Division – West

**Russell D. Nelson**, Farm Credit Leasing Services Corporation

## *Communications and Energy Banking Group*

**Mary E. McBride**, Executive Vice President

**Jennifer G. Goss**, Electric Distribution Division

**Candace A. Roper**, Government Relations

**Aivars (Jake) Udris**, Power Supply, Energy Services and Water Division

**Robert F. West**, Communications Division

## *Global Financial Services Group*

**John C. Holsey**, Executive Vice President

**Antony M. Bahr**, Capital Markets Division

**Manuel Fernandez-Quevedo**, International Division

**Richard A. Scholz**, Non-Credit Services Division

**Scott S. Trauth**, Corporate Finance Division

## *Credit and Risk Management Group*

**Douglas E. Wilhelm**, Executive Vice President and Chief Credit and Risk Officer

**Rodney A. Brown**, Asset Review, Collateral and Compliance Division

**Gary M. Fitzgerald**, Internal Audit Division

**Lori L. O'Flaherty**, Credit Approval and Administration Division

\* The Strategic Relationships Division is included within the Agribusiness Banking Group.

## Office Locations

CoBANK, ACB

### ***CoBANK National Office and Denver Banking Center \*\****

5500 S. Quebec St.  
Greenwood Village, CO 80111  
P. O. Box 5110  
Denver, CO 80217  
(303) 740-4000  
(800) 542-8072

### ***Farm Credit Leasing Services Corporation***

600 Highway 169 South, Suite 300  
Minneapolis, MN 55426  
(952) 417-7800  
(800) 444-2929

### ***Washington, DC Office***

50 F Street, N.W., Suite 900  
Washington, DC 20001  
(202) 879-0838

## **U.S. Regional Offices**

### ***Ames Banking Center***

2515 University Boulevard, Suite 104  
Ames, IA 50010  
(515) 292-8828

### ***Arizona Farm Credit Leasing Office\****

3003 S. Fair Lane  
Tempe, AZ 85282  
(602) 438-9811

### ***Atlanta Banking Center \*\****

900 Circle 75 Parkway, Suite 1400  
Atlanta, GA 30339-5946  
(770) 618-3200  
(800) 255-7429  
FCL: (770) 618-3226

### ***California Farm Credit Leasing Office \****

3984 Cherokee Road  
Stockton, CA 95215  
(209) 931-3770

### ***Fargo Banking Center***

Goldmark Office Park  
1711 Gold Drive South, Suite 230  
Fargo, ND 58103  
(701) 277-5007  
(866) 280-2892

### ***Florida Farm Credit Leasing Office \****

11903 Southern Boulevard, Suite 203  
Royal Palm Beach, FL 33411  
(561) 965-9001

### ***Louisville Banking Center \*\****

1601 UPS Drive, Suite 102  
Louisville, KY 40223  
(502) 423-5650  
(800) 262-6599  
FCL: (800) 942-3309

### ***Lubbock Banking Center***

5715 West 50th  
Lubbock, TX 79414  
P.O. Box 6770  
Lubbock, TX 79493  
(806) 785-3978

### ***Maryland Farm Credit Leasing Office \****

1 North Park Drive, Suite 205  
Hunt Valley, MD 21030  
(410) 771-9077  
(800) 225-8325

### ***Minneapolis Banking Center \*\****

600 Highway 169 South, Suite 300  
Minneapolis, MN 55426  
(952) 417-7900  
(800) 282-4150  
FCL: (800) 444-2929

### ***Omaha Banking Center \*\****

11422 Miracle Hills Drive, Suite 300  
Omaha, NE 68154-4404  
(402) 492-2000  
(800) 346-5717

### ***Sacramento Banking Center \*\****

1478 Stone Point Drive, Suite 450  
Roseville, CA 95661  
(916) 380-3524  
(800) 457-0942  
FCL: (800) 289-7080

### ***Spokane Banking Center***

1700 South Assembly Street,  
Suite 103  
Spokane, WA 99224-2121  
P.O. Box 2720  
Spokane, WA 99220-2720  
(509) 363-8700  
(800) 378-5577

### ***Springfield Banking Center \*\****

67 Hunt Street, Suite 3  
Agawam, MA 01001  
P.O. Box 9061  
Springfield, MA 01102-9061  
(413) 821-0200  
(800) 876-3227  
FCL: (413) 821-0214

### ***St. Louis Banking Center \*\****

1630 Des Peres Road, Suite 210  
St. Louis, MO 63131  
(314) 835-4200  
(800) 806-4144  
FCL: (800) 853-5480

### ***Texas Farm Credit Leasing Offices \****

5701 I40 West  
Amarillo, TX 79106  
(806) 352-6310  
403 N. Sunset Strip, Highway 181  
Kenedy, TX 78119  
(830) 583-0000

### ***Wichita Banking Center \*\****

245 North Waco, Suite 230  
Wichita, KS 67202  
P.O. Box 2940  
Wichita, KS 67201-2940  
(316) 290-2000  
(800) 322-3654  
FCL: (800) 322-6558

## **International Office**

### ***Singapore Representative Office***

10 Hoe Chiang Road  
#05-01 Keppel Towers  
Singapore 089315  
(65) 6534-5261

\* *Farm Credit Leasing office only*

\*\* *Farm Credit Leasing office within this CoBANK location*

CoBANK's 2008 *Quarterly and Annual Reports to Shareholders* are available free of charge on request by calling or visiting one of our banking center locations and through our website at [www.cobank.com](http://www.cobank.com) on approximately May 9, 2008, August 8, 2008, November 7, 2008, and March 2, 2009 (Annual Report).