NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORP /DC/
Form 10-Q
April 11, 2018

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

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended February 28, 2018
OR
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number: 1-7102

NATIONAL RURAL UTILITIES
COOPERATIVE FINANCE CORPORATION
(Exact name of registrant as specified in its charter)

District of Columbia	52-0891669
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20701 Cooperative Way, Dulles, Virginia, 20166
(Address of principal executive offices) (Zip Code)
Registrant’s telephone number, including area code: (703) 467-1800

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.
Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer Smaller reporting company Emerging growth company
(Do not check if a smaller reporting company)
If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transaction period for complying with any new or revised financial accounting standards provided pursuant to

Section13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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PART I—FINANCIAL INFORMATION

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A")
FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains certain statements that are considered "forward-looking statements" within the Securities Act of 1933, as amended, and the Exchange Act of 1934, as amended. Forward-looking statements, which are based on certain assumptions and describe our future plans, strategies and expectations, are generally identified by our use of words such as "intend," "plan," "may," "should," "will," "project," "estimate," "anticipate," " "expect," "continue," "potential," "opportunity" and similar expressions, whether in the negative or affirmative. All statements about future expectations or projections, including statements about loan volume, the appropriateness of the allowance for loan losses, operating income and expenses, debt-to-equity ratio, borrower financial performance, impaired loans, and sources and uses of liquidity, are forward-looking statements. Although we believe that the expectations reflected in our forward-looking statements are based on reasonable assumptions, actual results and performance may differ materially from our forward-looking statements due to several factors. Factors that could cause future results to vary from our forward-looking statements include, but are not limited to, general economic conditions, legislative changes including those that could affect our tax status, governmental monetary and fiscal policies, demand for our loan products, lending competition, changes in the quality or composition of our loan portfolio, changes in our ability to access external financing, changes in the credit ratings on our debt, valuation of collateral supporting impaired loans, charges associated with our operation or disposition of foreclosed assets, regulatory and economic conditions in the rural electric industry, nonperformance of counterparties to our derivative agreements, the costs and effects of legal or governmental proceedings involving us or our members and the factors listed and described under "Item 1A. Risk Factors" of our Annual Report on Form 10-K for the fiscal year ended May 31, 2017 ("2017 Form 10-K"). Except as required by law, we undertake no obligation to update or publicly release any revisions to forward-looking statements to reflect events, circumstances or changes in expectations after the date on which the statement is made.
INTRODUCTION

National Rural Utilities Cooperative Finance Corporation ("CFC") is a member-owned cooperative association incorporated under the laws of the District of Columbia in April 1969. CFC's principal purpose is to provide its members with financing to supplement the loan programs of the Rural Utilities Service ("RUS") of the United States Department of Agriculture ("USDA"). CFC makes loans to its rural electric members so they can acquire, construct and operate electric distribution, generation, transmission and related facilities. CFC also provides its members with credit enhancements in the form of letters of credit and guarantees of debt obligations. As a cooperative, CFC is owned by and exclusively serves its membership, which consists of not-for-profit entities or subsidiaries or affiliates of not-for-profit entities. CFC is exempt from federal income taxes under Section 501(c)(4) of the Internal Revenue Code. As a member-owned cooperative, CFC's objective is not to maximize profit, but rather to offer its members cost-based financial products and services. CFC funds its activities primarily through a combination of public and private issuances of debt securities, member investments and retained equity. As a Section 501(c)(4) tax-exempt, member-owned cooperative, we cannot issue equity securities.

Our financial statements include the consolidated accounts of CFC, National Cooperative Services Corporation ("NCSC"), Rural Telephone Finance Cooperative ("RTFC") and subsidiaries created and controlled by CFC to hold foreclosed assets resulting from defaulted loans or bankruptcy. NCSC is a taxable member-owned cooperative that may provide financing to members of CFC, government or quasi-government entities which own electric utility systems that meet the Rural Electrification Act definition of "rural" and for-profit and nonprofit entities that are owned, operated or controlled by, or provide significant benefits to certain members of CFC. RTFC is a taxable Subchapter T cooperative association that provides financing for its rural telecommunications members and their affiliates. CFC did not have any entities that held foreclosed assets as of February 28, 2018 or May 31, 2017. See "Item 1.

Business—Overview” of our 2017 Form 10-K for additional information on the business activities of each of these entities. Unless stated otherwise, references to “we,” “our” or “us” relate to CFC and its consolidated entities. All references to members within this document include members, associates and affiliates of CFC and its consolidated entities.

Management monitors a variety of key indicators to evaluate our business performance. The following MD&A is intended to provide the reader with an understanding of our results of operations, financial condition and liquidity by discussing the drivers of changes from period to period and the key measures used by management to evaluate performance, such as net interest income, net interest yield, loan growth, debt-to-equity ratio, growth and credit quality metrics. The MD&A is provided as a supplement to, and should be read in conjunction with our unaudited condensed consolidated financial statements and related notes in this Report, our audited consolidated financial statements and related notes in our 2017 Form 10-K and additional information contained in our 2017 Form 10-K, including the risk factors discussed under "Part I—Item 1A. Risk Factors," as well as any risk factors identified under "Part II—Item 1A. Risk Factors" in this Report.

SUMMARY OF SELECTED FINANCIAL DATA

Table 1 provides a summary of consolidated selected financial data for the three and nine months ended February 28, 2018 and 2017, and as of February 28, 2018 and May 31, 2017. In addition to financial measures determined in accordance with generally accepted accounting principles in the United States ("GAAP"), management also evaluates performance based on certain non-GAAP measures and metrics, which we refer to as "adjusted" measures. Certain financial covenant provisions in our credit agreements are also based on non-GAAP financial measures. Our key non-GAAP financial measures are adjusted net income, adjusted net interest income, adjusted interest expense, adjusted net interest yield, adjusted times interest earned ratio ("adjusted TIER") and adjusted debt-to-equity ratio. The most comparable GAAP measures are net income, net interest income, interest expense, net interest yield, TIER and debt-to-equity ratio, respectively. The primary adjustments we make to calculate these non-GAAP measures consist of (i) adjusting interest expense and net interest income to include the impact of net periodic derivative cash settlements; (ii) adjusting net income, senior debt and total equity to exclude the non-cash impact of the accounting for derivative financial instruments; (iii) adjusting senior debt to exclude the amount that funds CFC member loans guaranteed by RUS, subordinated deferrable debt and members' subordinated certificates; and (iv) adjusting total equity to include subordinated deferrable debt and members' subordinated certificates and exclude cumulative derivative forward value gains and losses and accumulated other comprehensive income. We believe our non-GAAP adjusted measures, which are not a substitute for GAAP and may not be consistent with similarly titled non-GAAP measures used by other companies, provide meaningful information and are useful to investors because management evaluates performance based on these metrics, and certain financial covenants in our committed bank revolving line of credit agreements and debt indentures are based on adjusted measures. See "Non-GAAP Financial Measures" for a detailed reconciliation of these adjusted measures to the most comparable GAAP measures.

Table 1: Summary of Selected Financial Data

	Three Months Ended February 28,			Nine Months Ended February 28,		
(Dollars in thousands)	2018	2017	Change	2018	2017	Change
Statement of operations						
Interest income	$271,468	$259,920	4%	$803,206	$773,911	4%
Interest expense	(198,071)	(186,740)	6	(585,972)	(551,474)	6
Net interest income	73,397	73,180	—	217,234	222,437	(2)
Fee and other income	3,935	5,810	(32)	13,422	15,437	(13)
Total net revenue	77,332	78,990	(2)	230,656	237,874	(3)
Provision for loan losses	(1,105)	(2,065)	(46)	(503)	(4,731)	(89)
Derivative gains[1]	168,048	42,455	296	247,443	194,822	27
Results of operations of foreclosed assets	—	(29)	**	(34)	(1,690)	(98)
Operating expenses[2]	(22,212)	(20,710)	7	(65,762)	(62,201)	6
Other non-interest expense	(402)	(294)	37	(1,542)	(1,254)	23
Income before income taxes	221,661	98,347	125	410,258	362,820	13
Income tax expense	(632)	(385)	64	(1,491)	(1,815)	(18)

Net income	$221,029	$97,962	126	$408,767	$361,005	13

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	Three Months Ended February 28, 2018	2017	Change	Nine Months Ended February 28, 2018	2017	Change
Adjusted operational financial measures						
Adjusted interest expense[3]	$(216,995)	$(206,094)	5%	$(644,753)	$(615,805)	5%
Adjusted net interest income[3]	54,473	53,826	1	158,453	158,106	—
Adjusted net income[3]	34,057	36,153	(6)	102,543	101,852	1
Selected ratios						
Fixed-charge coverage ratio/TIER [4]	2.12	1.52	60 bps	1.70	1.65	5 bps
Adjusted TIER[3]	1.16	1.18	(2)	1.16	1.17	(1)
Net interest yield[5]	1.16 %	1.19 %	(3)	1.15 %	1.22 %	(7)
Adjusted net interest yield[3][6]	0.86	0.87	(1)	0.84	0.86	(2)
Net charge-off rate[7]	—	—	—	—	0.01	(1)

	February 28, 2018	May 31, 2017	Change
Balance sheet			
Cash and cash equivalents	$250,697	$166,615	50%
Investment securities	337,900	92,554	265
Loans to members[8]	25,342,922	24,367,044	4
Allowance for loan losses	(37,879)	(37,376)	1
Loans to members, net	25,305,043	24,329,668	4
Total assets	26,476,407	25,205,692	5
Short-term borrowings	3,493,736	3,342,900	5
Long-term debt	18,813,136	17,955,594	5
Subordinated deferrable debt	742,375	742,274	—
Members' subordinated certificates	1,379,693	1,419,025	(3)
Total debt outstanding	24,428,940	23,459,793	4
Total liabilities	25,017,303	24,106,887	4
Total equity	1,459,104	1,098,805	33
Guarantees[9]	679,968	889,617	(24)
Selected ratios period end			
Allowance coverage ratio[10]	0.15 %	0.15 %	—
Debt-to-equity ratio[11]	17.15	21.94	(479)
Adjusted debt-to-equity ratio[3]	6.21	5.95	26

———————————

** Change is not meaningful.

[1]Consists of derivative cash settlements and derivative forward value gains (losses). Derivative cash settlement amounts represent net periodic contractual interest accruals related to derivatives not designated for hedge accounting. Derivative forward value gains (losses) represent changes in fair value during the period, excluding net periodic contractual interest accruals, related to derivatives not designated for hedge accounting and expense amounts reclassified into income related to the cumulative transition loss recorded in accumulated other comprehensive income as of June 1, 2001, as a result of the adoption of the derivative accounting guidance that required derivatives to be reported at fair value on the balance sheet.

[2]Consists of salaries and employee benefits and the other general and administrative expenses components of non-interest expense, each of which are presented separately on our consolidated statements of operations.

(3)See "Non-GAAP Financial Measures" for details on the calculation of these non-GAAP adjusted measures and the reconciliation to the most comparable GAAP measures.
(4)Calculated based on net income (loss) plus interest expense for the period divided by interest expense for the period. The fixed-charge coverage ratios and TIER were the same during each period presented because we did not have any capitalized interest during these periods.
(5)Calculated based on annualized net interest income for the period divided by average interest-earning assets for the period.
(6)Calculated based on annualized adjusted net interest income for the period divided by average interest-earning assets for the period.

(7)Calculated based on annualized net charge-offs (recoveries) for the period divided by average total outstanding loans for the period.
(8)Consists of the outstanding principal balance of member loans plus unamortized deferred loan origination costs, which totaled $11 million as of both February 28, 2018 and May 31, 2017.
(9)Reflects the total amount of member obligations for which CFC has guaranteed payment to a third party as of the end of each period. This amount represents our maximum exposure to loss, which significantly exceeds the guarantee liability recorded on our consolidated balance sheets. See "Note 10—Guarantees" for additional information.
(10)Calculated based on the allowance for loan losses at period end divided by total outstanding loans at period end.
(11)Calculated based on total liabilities at period end divided by total equity at period end.

EXECUTIVE SUMMARY

Our primary objective as a member-owned cooperative lender is to provide cost-based financial products to our rural electric members while maintaining a sound financial position required for investment-grade credit ratings on our debt instruments. Our objective is not to maximize net income; therefore, the rates we charge our member-borrowers reflect our adjusted interest expense plus a spread to cover our operating expenses, a provision for loan losses and earnings sufficient to achieve interest coverage to meet our financial objectives. Our goal is to earn an annual minimum adjusted TIER of 1.10 and to maintain an adjusted debt-to-equity ratio at approximately or below 6.00-to-1.

We are subject to period-to-period volatility in our reported GAAP results due to changes in market conditions and differences in the way our financial assets and liabilities are accounted for under GAAP. Our financial assets and liabilities expose us to interest-rate risk. We use derivatives, primarily interest rate swaps, as part of our strategy in managing this risk. Our derivatives are intended to economically hedge and manage the interest-rate sensitivity mismatch between our financial assets and liabilities. We are required under GAAP to carry derivatives at fair value on our consolidated balance sheet; however, the financial assets and liabilities for which we use derivatives to economically hedge are carried at amortized cost. Changes in interest rates and spreads result in periodic fluctuations in the fair value of our derivatives, which may cause volatility in our earnings because we do not apply hedge accounting. As a result, the mark-to-market changes in our derivatives are recorded in earnings. Based on the composition of our derivatives, we generally record derivative losses in earnings when interest rates decline and derivative gains when interest rates rise. This earnings volatility generally is not indicative of the underlying economics of our business, as the derivative forward fair value gains or losses recorded each period may or may not be realized over time, depending on the terms of our derivative instruments and future changes in market conditions that impact actual derivative cash settlement amounts. As such, management uses our adjusted non- GAAP results, which include realized net periodic derivative settlements but exclude the impact of unrealized derivative forward fair value gains and losses, to evaluate our operating performance. Because derivative forward fair value gains and losses do not impact our cash flows, liquidity or ability to service our debt costs, our financial debt covenants are also based on our non-GAAP adjusted results.

Financial Performance

Reported Results

We reported net income of $221 million and a TIER of 2.12 for the quarter ended February 28, 2018 ("current quarter"), compared with net income of $98 million and a TIER of 1.52 for the same prior-year quarter. We reported net income of $409 million and a TIER of 1.70 for the nine months ended February 28, 2018, compared with net income of $361 million and a TIER of 1.65 for the same prior-year period. Our debt-to-equity ratio decreased to 17.15-to-1 as of February 28, 2018, from 21.94-to-1 as of May 31, 2017, primarily due to an increase in equity resulting from our reported net income of $409 million for the nine months ended February 28, 2018, which was partially offset by patronage capital retirement of $45 million in September 2017.

The variance of $123 million between our reported net income of $221 million in the current quarter and net income of $98 million for the same prior-year quarter was driven primarily by mark-to-market changes in the fair value of our derivatives. We recognized derivative gains of $168 million in the current quarter, compared with derivative gains of $42 million in the same prior-year quarter, both of which were attributable to a net increase in the fair value of our pay-fixed swaps as interest rates increased across the swap yield curve during each period. The increase in interest rates, however, was more pronounced during the current quarter, which resulted in the significantly higher derivative gains relative to the same prior-year quarter. Although net interest income of $73 million for the current quarter was relatively unchanged from the same prior-year quarter, net interest yield decreased 3 basis points to 1.16%, largely due to an overall increase in our average cost of funds attributable to the increase in short-term interest rates, which resulted in a higher average cost for our short-term and variable-rate borrowings.

The variance of $48 million between our reported net income of $409 million for the nine months ended February 28, 2018 and our net income of $361 million for the same prior-year period was also driven primarily by mark-to-market changes in the fair value of our derivatives. We recognized derivative gains of $247 million for the nine months ended February 28, 2018, compared with derivative gains of $195 million for the same prior-year period, both due to an increase in interest rates across the swap yield curve. The increase in interest rates, however, was more pronounced during the current nine-month period, with the 10-year and 30-year swap rates increasing by 74 basis points and 53 basis points, respectively, compared with increases of 64 basis points and 44 basis points, respectively, in the same prior year period. We experienced a decrease in net interest income of $5 million due to compression in the net interest yield and an increase in operating expenses of $4 million, which were partially offset by a decrease in the provision for loan losses of $4 million. Our net interest yield was 1.15% for the nine months ended February 28, 2018, a decrease of 7 basis points from the same prior-year period. The decrease was primarily due to an overall increase in our average cost of funds resulting from the higher average cost of our short-term and variable-rate borrowings.

Adjusted Non-GAAP Results

Our adjusted net income totaled $34 million and our adjusted TIER was 1.16 for the current quarter, compared with adjusted net income of $36 million and adjusted TIER of 1.18 for the same prior-year quarter. Our adjusted net income totaled $103 million and our adjusted TIER was 1.16 for the nine months ended February 28, 2018, compared with adjusted net income of $102 million and adjusted TIER of 1.17 for the same prior-year period. Our adjusted debt-to-equity ratio increased to 6.21-to-1 as of February 28, 2018, from 5.95-to-1 as of May 31, 2017, largely due to an increase in debt outstanding to fund loan growth.

Our adjusted net interest income for the current quarter and nine months ended February 28, 2018 remained relatively unchanged from the same prior-year periods, as the compression in the adjusted net interest yield resulting from an increase in our overall average cost of funds was offset by the increase in average interest-earning assets. In addition, the decrease in fee income and the increase in operating expenses were offset by the decrease in the provision for loan losses. Our adjusted net interest yield was 0.86% and 0.84% for the current quarter and the nine months ended February 28, 2018, respectively, reflecting a decrease of 1 basis point and 2 basis points, respectively, from the same prior-year periods due to the overall increase in our average cost of funds driven by the higher average cost of our short-term and variable-rate borrowings resulting from the increase in short-term interest rates.

Lending Activity

Loans to members totaled $25,343 million as of February 28, 2018, an increase of $976 million, or 4%, from May 31, 2017. The increase was primarily due to an increase in CFC distribution loans of $862 million, an increase in NCSC loans of $187 million and an increase in RTFC loans of $9 million, which were partially offset by a decrease in CFC power supply loans of $82 million.

Long-term loan advances totaled $1,864 million during the nine months ended February 28, 2018, with approximately 64% of those advances for capital expenditures by members and 25% for the refinancing of loans made by other lenders. CFC had long-term fixed-rate loans totaling $783 million that were scheduled to reprice during the nine months ended February 28, 2018. Of this total, $646 million repriced to a new long-term fixed rate, $135 million repriced to a long-term variable rate and $2 million were repaid in full.

Financing Activity

Our outstanding debt volume generally increases and decreases in response to member loan demand. As total outstanding loans increased during the nine months ended February 28, 2018, our debt volume also increased. Total debt outstanding was $24,429 million as of February 28, 2018, an increase of $969 million, or 4%, from May 31, 2017. The increase was primarily attributable to a net increase in dealer medium-term notes of $694 million, a net increase in the Federal Agricultural Mortgage Corporation (“Farmer Mac”) notes payable of $292 million, a net increase in member commercial paper, select notes and daily liquidity fund notes of $49 million and a net increase in dealer commercial paper outstanding of $55 million. These increases were partially offset by a net decrease in notes payable to the Federal Financing Bank under the Guaranteed Underwriter Program of the USDA ("Guaranteed Underwriter Program") of $114 million.

We provide additional information on our financing activities below under "Consolidated Balance Sheet Analysis—Debt" and "Liquidity Risk."

Outlook for the Next 12 Months

We currently expect that our net interest income, net interest yield, adjusted net interest income and adjusted net interest yield will increase over the next 12 months as a result of a projected decrease in our average cost of funds and an increase in average outstanding loans. We have scheduled maturities of higher-cost debt over the next 12 months, including $1,830 million in collateral trust bonds with a weighted average coupon rate of 6.98%. We expect that we will be able to replace this higher-cost debt with lower-cost funding, which will reduce our aggregate weighted average cost of funds. We expect the amount of long-term loan advances to exceed anticipated loan repayments over the next 12 months, resulting in an increase in average outstanding loans.

Long-term debt scheduled to mature over the next 12 months totaled $2,862 million as of February 28, 2018. We believe we have sufficient liquidity from the combination of existing cash, member loan repayments, committed bank revolving lines of credit and our ability to issue debt in the capital markets, to our members and in private placements, to meet the demand for member loan advances and to satisfy our obligations to repay long-term debt maturing over the next 12 months. As of February 28, 2018, we had access to liquidity reserves totaling $7,254 million, which consisted of (i) $251 million in cash and cash equivalents, (ii) up to $1,225 million available under committed loan facilities under the Guaranteed Underwriter Program, (iii) up to $3,083 million available under committed bank revolving line of credit agreements, (iv) up to $300 million available under a committed revolving note purchase agreement with Farmer Mac, and (v) up to $2,395 million available under a revolving note purchase agreement with Farmer Mac, subject to market conditions.

We believe we can continue to roll over outstanding member short-term debt of $2,439 million as of February 28, 2018, based on our expectation that our members will continue to reinvest their excess cash in our commercial paper, daily liquidity fund, select notes and medium-term notes. Although we expect to continue accessing the dealer commercial paper market to help meet our liquidity needs, we intend to manage our short-term wholesale funding risk by maintaining outstanding dealer commercial paper at an amount below $1,250 million for the foreseeable future. We expect to continue to be in compliance with the covenants under our committed bank revolving line of credit agreements, which will allow us to mitigate our roll-over risk as we can draw on these facilities to repay dealer or member commercial paper that cannot be
rolled over.

While we are not subject to bank regulatory capital rules, we generally aim to maintain an adjusted debt-to-equity ratio at approximately or below 6.00-to-1. Our adjusted debt-to-equity ratio was 6.21 as of February 28, 2018, above our targeted threshold due to the increase in debt outstanding to fund loan growth. Due to anticipated asset growth, we expect our adjusted debt-to-equity ratio to be above 6.00-to-1 over the next 12 months.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with GAAP requires management to make a number of judgments, estimates and assumptions that affect the amount of assets, liabilities, income and expenses in the consolidated financial statements. Understanding our accounting policies and the extent to which we use management's judgment and estimates in applying these policies is integral to understanding our financial statements.

We provide a discussion of our significant accounting policies under “Note 1—Summary of Significant Accounting Policies” in our 2017 Form 10-K.

We have identified certain accounting policies as critical because they involve significant judgments and assumptions about highly complex and inherently uncertain matters, and the use of reasonably different estimates and assumptions could have a material impact on our results of operations or financial condition. Our most critical accounting policies and estimates involve the determination of the allowance for loan losses and fair value. We evaluate our critical accounting estimates and judgments required by our policies on an ongoing basis and update them as necessary based on changing conditions. There were no material changes in the key inputs and assumptions used in our critical accounting policies during the nine months ended February 28, 2018. Management has discussed significant judgments and assumptions in applying our critical accounting policies with the Audit Committee of our board of directors. We provide additional information on our critical accounting policies and estimates under “MD&A—Critical Accounting Policies and Estimates” in our 2017 Form 10-K. See “Item 1A. Risk Factors” in our 2017 Form 10-K for a discussion of the risks associated with management’s judgments and estimates in applying our accounting policies and methods.

ACCOUNTING CHANGES AND OTHER DEVELOPMENTS

See “Note 1—Summary of Significant Accounting Policies” for information on accounting standards adopted during the current quarter, as well as recently issued accounting standards not yet required to be adopted and the expected impact of these accounting standards. We also discuss the expected impact of the Tax Cuts and Jobs Act (“The Act”), which the President of the United States signed and enacted into law on December 22, 2017. To the extent we believe the adoption of new accounting standards has had or will have a material impact on our consolidated results of operations, financial condition or liquidity, we discuss the impact in the applicable section(s) of this MD&A.

CONSOLIDATED RESULTS OF OPERATIONS

The section below provides a comparative discussion of our condensed consolidated results of operations between the three months ended February 28, 2018 and 2017 and the nine months ended February 28, 2018 and 2017. Following this section, we provide a comparative analysis of our condensed consolidated balance sheets as of February 28, 2018 and May 31, 2017. You should read these sections together with our “Executive Summary—Outlook for the Next 12 Months” where we discuss trends and other factors that we expect will affect our future results of operations.

Net Interest Income

Net interest income represents the difference between the interest income earned on our interest-earning assets, which include loans and investment securities, and the interest expense on our interest-bearing liabilities. Our net interest yield represents the difference between the yield on our interest-earning assets and the cost of our interest-bearing liabilities plus the impact from non-interest bearing funding. We expect net interest income and our net interest yield to fluctuate based on changes in interest rates and changes in the amount and composition of our interest-earning assets and interest-bearing liabilities. We do not fund each individual loan with specific debt. Rather, we attempt to minimize costs and maximize efficiency by funding large aggregated amounts of loans.

Table 2 presents our average balance sheets for the three and nine months ended February 28, 2018 and 2017, and for each major category of our interest-earning assets and interest-bearing liabilities, the interest income earned or interest expense incurred, and the average yield or cost. Table 2 also presents non-GAAP adjusted interest expense, adjusted net interest income and adjusted net interest yield, which reflect the inclusion of net accrued periodic derivative cash settlements in interest expense. We provide reconciliations of our non-GAAP adjusted measures to the most comparable GAAP measures under “Non-GAAP Financial Measures.”

Table 2: Average Balances, Interest Income/Interest Expense and Average Yield/Cost

	Three Months Ended February 28,					
(Dollars in thousands)	2018			2017		
Assets:	Average Balance	Interest Income/Expense	Average Yield/Cost	Average Balance	Interest Income/Expense	Average Yield/Cost
Long-term fixed-rate loans[1]	$22,706,134	$ 250,201	4.47 %	$22,106,076	$ 245,480	4.50 %
Long-term variable-rate loans	972,399	7,020	2.93	811,080	5,047	2.52
Line of credit loans	1,512,664	10,367	2.78	1,162,268	6,538	2.28
TDR loans[2]	12,808	221	7.00	13,381	228	6.91
Other income, net[3]	—	(314)	—	—	(230)	—
Total loans	25,204,005	267,495	4.30	24,092,805	257,063	4.33
Cash, time deposits and investment securities	539,728	3,973	2.99	875,438	2,857	1.32
Total interest-earning assets	$25,743,733	$ 271,468	4.28 %	$24,968,243	$ 259,920	4.22 %
Other assets, less allowance for loan losses	853,563			617,010		
Total assets	$26,597,296			$25,585,253		
Liabilities:						
Short-term borrowings	$3,777,158	$ 14,593	1.57 %	$3,673,501	$ 7,907	0.87 %
Medium-term notes	3,392,554	28,051	3.35	3,377,615	25,166	3.02
Collateral trust bonds	7,590,459	83,730	4.47	7,256,227	85,582	4.78
Guaranteed Underwriter Program notes payable	4,899,496	34,233	2.83	4,864,585	35,086	2.93
Farmer Mac notes payable	2,507,350	13,316	2.15	2,305,681	8,406	1.48
Other notes payable	32,970	369	4.54	38,445	437	4.61
Subordinated deferrable debt	742,351	9,414	5.14	742,217	9,410	5.14
Subordinated certificates	1,372,508	14,365	4.24	1,430,089	14,746	4.18
Total interest-bearing liabilities	$24,314,846	$ 198,071	3.30 %	$23,688,360	$ 186,740	3.20 %
Other liabilities	954,482			798,848		
Total liabilities	25,269,328			24,487,208		
Total equity	1,327,968			1,098,045		
Total liabilities and equity	$26,597,296			$25,585,253		
Net interest spread[4]			0.98 %			1.02 %
Impact of non-interest bearing funding[5]			0.18			0.17
Net interest income/net interest yield[6]		$ 73,397	1.16 %		$ 73,180	1.19 %
Adjusted net interest income/adjusted net interest yield:						
Interest income		$ 271,468	4.28 %		$ 259,920	4.22 %
Interest expense		198,071	3.30		186,740	3.20
Add: Net accrued periodic derivative cash settlements[7]		18,924	0.71		19,354	0.74
Adjusted interest expense/adjusted average cost[8]		$ 216,995	3.62 %		$ 206,094	3.53 %

Adjusted net interest spread(4)		0.66	%		0.69	%
Impact of non-interest bearing funding		0.20			0.18	
Adjusted net interest income/adjusted net interest yield(9)	$ 54,473	0.86	%	$ 53,826	0.87	%

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	Nine Months Ended February 28,					
(Dollars in thousands)	2018			2017		
Assets:	Average Balance	Interest Income/Expense	Average Yield/Cost	Average Balance	Interest Income/Expense	Average Yield/Cost
Long-term fixed-rate loans(1)	$22,510,725	$ 748,491	4.45 %	$21,832,967	$ 733,425	4.49 %
Long-term variable-rate loans	900,067	18,980	2.82	763,831	14,561	2.55
Line of credit loans	1,398,346	27,662	2.64	1,083,863	18,057	2.23
TDR loans(2)	12,954	669	6.90	14,717	677	6.15
Other income, net(3)	—	(852)	—	—	(795)	—
Total loans	24,822,092	794,950	4.28	23,695,378	765,925	4.32
Cash, time deposits and investment securities	476,532	8,256	2.32	749,508	7,986	1.42
Total interest-earning assets	$25,298,624	$ 803,206	4.24 %	$24,444,886	$ 773,911	4.23 %
Other assets, less allowance for loan losses	645,712			634,590		
Total assets	$25,944,336			$25,079,476		
Liabilities:						
Short-term borrowings	$3,330,949	$ 35,248	1.41 %	$3,209,128	$ 18,198	0.76 %
Medium-term notes	3,258,159	80,711	3.31	3,353,107	73,456	2.93
Collateral trust bonds	7,621,435	254,328	4.46	7,255,745	255,582	4.71
Guaranteed Underwriter Program notes payable	4,987,617	105,523	2.83	4,833,701	107,074	2.96
Farmer Mac notes payable	2,503,828	36,753	1.96	2,297,045	22,892	1.33
Other notes payable	34,511	1,150	4.46	40,155	1,353	4.50
Subordinated deferrable debt	742,318	28,247	5.09	742,186	28,247	5.09
Subordinated certificates	1,402,077	44,012	4.20	1,438,578	44,672	4.15
Total interest-bearing liabilities	$23,880,894	$ 585,972	3.28 %	$23,169,645	$ 551,474	3.18 %
Other liabilities	882,937			1,019,306		
Total liabilities	24,763,831			24,188,951		
Total equity	1,180,505			890,525		
Total liabilities and equity	$25,944,336			$25,079,476		
Net interest spread(4)			0.96 %			1.05 %
Impact of non-interest bearing funding(5)			0.19			0.17
Net interest income/net interest yield(6)		$ 217,234	1.15 %		$ 222,437	1.22 %
Adjusted net interest income/adjusted net interest yield:						
Interest income		$ 803,206	4.24 %		$ 773,911	4.23 %
Interest expense		585,972	3.28		551,474	3.18
Add: Net accrued periodic derivative cash settlements(7)		58,781	0.73		64,331	0.82
Adjusted interest expense/adjusted average cost(8)		$ 644,753	3.61 %		$ 615,805	3.55 %
Adjusted net interest spread(4)			0.63 %			0.68 %

Impact of non-interest bearing funding		0.21			0.18	
Adjusted net interest income/adjusted net interest yield[9]	$ 158,453	0.84	%	$ 158,106	0.86	%

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[1]Interest income on long-term, fixed-rate loans includes loan conversion fees, which are generally deferred and recognized as interest income using the effective interest method.
[2]Troubled debt restructuring ("TDR") loans.
[3]Consists of late payment fees and net amortization of deferred loan fees and loan origination costs.

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(4)Net interest spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities. Adjusted net interest spread represents the difference between the average yield on total interest-earning assets and the adjusted average cost of total interest-bearing liabilities.
(5)Includes other liabilities and equity.
(6)Net interest yield is calculated based on annualized net interest income for the period divided by total average interest-earning assets for the period.
(7)Represents the impact of net accrued periodic derivative cash settlements during the period, which is added to interest expense to derive non-GAAP adjusted interest expense. The average (benefit)/cost associated with derivatives is calculated based on annualized net accrued periodic derivative cash settlements during the period divided by the average outstanding notional amount of derivatives during the period. The average outstanding notional amount of derivatives was $10,841 million and $10,610 million for the three months ended February 28, 2018 and 2017, respectively. The average outstanding notional amount of derivatives was $10,808 million and $10,532 million for the nine months ended February 28, 2018 and 2017, respectively.
(8)Adjusted interest expense represents interest expense plus net accrued periodic derivative cash settlements during the period. Net accrued periodic derivative cash settlements are reported on our consolidated statements of operations as a component of derivative gains (losses). Adjusted average cost is calculated based on annualized adjusted interest expense for the period divided by total average interest-bearing liabilities during the period.
(9)Adjusted net interest yield is calculated based on annualized adjusted net interest income for the period divided by total average interest-earning assets for the period.

Table 3 displays the change in net interest income between periods and the extent to which the variance is attributable to: (i) changes in the volume of our interest-earning assets and interest-bearing liabilities or (ii) changes in the interest rates of these assets and liabilities. The table also presents the change in adjusted net interest income between periods.

Table 3: Rate/Volume Analysis of Changes in Interest Income/Interest Expense

	Three Months Ended February 28, 2018 versus 2017			Nine Months Ended February 28, 2018 versus 2017		
		Variance due to:[1]			Variance due to:[1]	
(Dollars in thousands)	Total Variance	Volume	Rate	Total Variance	Volume	Rate
Interest income:						
Long-term fixed-rate loans	$4,721	$6,663	$(1,942)	$15,066	$22,768	$(7,702)
Long-term variable-rate loans	1,973	1,004	969	4,419	2,597	1,822
Line of credit loans	3,829	1,971	1,858	9,605	5,239	4,366
Restructured loans	(7)	(10)	3	(8)	(81)	73
Other income, net	(84)	—	(84)	(57)	—	(57)
Total loans	10,432	9,628	804	29,025	30,523	(1,498)
Cash, time deposits and investment securities	1,116	(1,096)	2,212	270	(2,909)	3,179
Interest income	11,548	8,532	3,016	29,295	27,614	1,681
Interest expense:						
Short-term borrowings	6,686	223	6,463	17,050	691	16,359
Medium-term notes	2,885	111	2,774	7,255	(2,080)	9,335
Collateral trust bonds	(1,852)	3,942	(5,794)	(1,254)	12,881	(14,135)
Guaranteed Underwriter Program notes payable	(853)	252	(1,105)	(1,551)	3,409	(4,960)
Farmer Mac notes payable	4,910	735	4,175	13,861	2,061	11,800
Other notes payable	(68)	(62)	(6)	(203)	(190)	(13)
Subordinated deferrable debt	4	2	2	—	5	(5)
Subordinated certificates	(381)	(594)	213	(660)	(1,133)	473
Interest expense	11,331	4,609	6,722	34,498	15,644	18,854
Net interest income	$217	$3,923	$(3,706)	$(5,203)	$11,970	$(17,173)
Adjusted net interest income:						
Interest income	$11,548	$8,532	$3,016	$29,295	$27,614	$1,681
Interest expense	11,331	4,609	6,722	34,498	15,644	18,854
Net accrued periodic derivative cash settlements[2]	(430)	422	(852)	(5,550)	1,684	(7,234)
Adjusted interest expense[3]	10,901	5,031	5,870	28,948	17,328	11,620
Adjusted net interest income	$647	$3,501	$(2,854)	$347	$10,286	$(9,939)

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[1]The changes for each category of interest income and interest expense are divided between the portion of change attributable to the variance in volume and the portion of change attributable to the variance in rate for that category. The amount attributable to the combined impact of volume and rate has been allocated to each category based on the proportionate absolute dollar amount of change for that category.
[2]For net accrued periodic derivative cash settlements, the variance due to average volume represents the change in derivative cash settlements resulting from the change in the average notional amount of derivative contracts outstanding. The variance due to average rate represents the change in derivative cash settlements resulting from the net difference between the average rate paid and the average rate received for interest rate swaps during the period.
[3]See “Non-GAAP Financial Measures” for additional information on our adjusted non-GAAP measures.

Net interest income of $73 million for the current quarter was relatively unchanged from the same prior-year quarter, as the decrease in the net interest yield of 3% (3 basis points) to 1.16% was offset by an increase in average interest-earning assets of 3%.

Net interest income of $217 million for the nine months ended February 28, 2018 decreased by $5 million, or 2%, from the same prior-year period, driven by a decrease in the net interest yield of 6% (7 basis points) to 1.15%, which was partially offset by an increase in average interest-earning assets of 3%.

- Average Interest-Earning Assets: The increase in average interest-earning assets for the current quarter and nine months ended February 28, 2018 was primarily attributable to growth in average total loans of $1,111 million, or 5% and $1,127 million, or 5%, respectively, over the same prior-year periods, as members obtained advances to fund capital investments and refinanced with us loans made by other lenders.

- Net Interest Yield: The decrease in the net interest yield for the current quarter and nine months ended February 28, 2018 was primarily due to an increase in our average cost of funds. Our average cost of funds increased by 10 basis points during both the current quarter and nine months ended February 28, 2018 to 3.30% and 3.28%, respectively, largely due to increases in the cost of our short-term and variable-rate debt resulting from an increase in short-term interest rates. The 3-month London Interbank Offered Rate ("LIBOR") was 2.02% as of February 28, 2018, an increase of 96 basis points from February 28, 2017, while the federal funds rate ranged from 1.00% to 1.50% as of February 28, 2018, up 75 basis points from February 28, 2017.

Adjusted net interest income of $54 million for the current quarter increased by $1 million, or 1%, from the same prior-year quarter, driven by an increase in average interest-earning assets of 3%, which was partially offset by a decrease in the adjusted net interest yield of 1% (1 basis point) to 0.86%.

Adjusted net interest income of $158 million for the nine months ended February 28, 2018 was relatively unchanged from the same prior-year period, as the increase in average interest-earning assets of 3% was largely offset by a decrease in the adjusted net interest yield of 2% (2 basis points) to 0.84%. The decrease in the adjusted net interest yield was primarily attributable to an overall increase in the adjusted average cost of funds of 6 basis points to 3.61%, driven by the higher average cost of our short-term and variable-rate borrowings resulting from the increase in short-term interest rates.

Our adjusted net interest income and adjusted net interest yield include the impact of net accrued periodic derivative cash settlements during the period. We recorded net periodic derivative cash settlement expense of $19 million for both the three months ended February 28, 2018 and 2017, and $59 million and $64 million for the nine months ended February 28, 2018 and 2017, respectively. See "Non-GAAP Financial Measures" for additional information on our adjusted measures.

Provision for Loan Losses

Our provision for loan losses in each period is primarily driven by the level of allowance that we determine is necessary for probable incurred loan losses inherent in our loan portfolio as of each balance sheet date.

We recorded a provision for loan losses of $1 million for both the three and nine months ended February 28, 2018, compared with a provision for loan losses of $2 million and $5 million, respectively, for the same prior-year periods. The credit quality and performance statistics of our loan portfolio continued to remain strong. We experienced no charge-offs during the three and nine months ended February 28, 2018, and we had no loans classified as nonperforming as of the end of the period. In comparison, we recorded a net charge-off of $2 million during the nine months ended February 28, 2017.

We provide additional information on our allowance for loan losses under "Credit Risk—Allowance for Loan Losses" and "Note 4—Loans and Commitments" of this Report. For additional information on our allowance methodology, see "MD&A—Critical Accounting Policies and Estimates" and "Note 1—Summary of Significant Accounting Policies" in our

2017 Form 10-K.

Non-Interest Income

Non-interest income consists of fee and other income, gains and losses on derivatives not accounted for in hedge accounting relationships and results of operations of foreclosed assets.

Table 4 presents the components of non-interest income recorded in our condensed consolidated results of operations for the three and nine months ended February 28, 2018 and 2017.

Table 4: Non-Interest Income

	Three Months Ended February 28,		Nine Months Ended February 28,	
(Dollars in thousands)	2018	2017	2018	2017
Non-interest income:				
Fee and other income	$3,935	$5,810	$13,422	$15,437
Derivative gains	168,048	42,455	247,443	194,822
Results of operations of foreclosed assets	—	(29)	(34)	(1,690)
Total non-interest income	$171,983	$48,236	$260,831	$208,569

Non-interest income of $172 million for the current quarter increased by $124 million from the same prior-year quarter. Non-interest income of $261 million for the nine months ended February 28, 2018 increased by $52 million from the same prior-year period. The significant variances in non-interest income for the three and nine months ended February 28, 2018 between the same prior-year periods were primarily attributable to changes in net derivative gains recognized in our consolidated statements of operations.

Derivative Gains (Losses)

Our derivative instruments are an integral part of our interest rate risk management strategy. Our principal purpose in using derivatives is to manage our aggregate interest rate risk profile within prescribed risk parameters. The derivative instruments we use primarily include interest rate swaps, which we typically hold to maturity. The primary factors affecting the fair value of our derivatives and derivative gains (losses) recorded in our results of operations include changes in interest rates, the shape of the yield curve and the composition of our derivative portfolio. We generally do not designate our interest rate swaps, which currently account for all of our derivatives, for hedge accounting. Accordingly, changes in the fair value of interest rate swaps are reported in our consolidated statements of operations under derivative gains (losses). We did not have any derivatives designated as accounting hedges as of February 28, 2018 or May 31, 2017.

We currently use two types of interest rate swap agreements: (i) we pay a fixed rate and receive a variable rate ("pay-fixed swaps") and (ii) we pay a variable rate and receive a fixed rate ("receive-fixed swaps"). The benchmark rate for the substantial majority of the floating rate payments under our swap agreements is LIBOR. Table 5 displays the average notional amount outstanding, by swap agreement type, and the weighted-average interest rate paid and received for derivative cash settlements during the three and nine months ended February 28, 2018 and 2017. As indicated in Table 5, our derivative portfolio currently consists of a higher proportion of pay-fixed swaps than receive-fixed swaps. The profile of our derivative portfolio, however, may change as a result of changes in market conditions and actions taken to manage our interest rate risk.

Table 5: Derivative Average Notional Amounts and Average Interest Rates

	Three Months Ended February 28,					
	2018			2017		
(Dollars in thousands)	Average Notional Balance	Weighted-Average Rate Paid	Weighted-Average Rate Received	Average Notional Balance	Weighted-Average Rate Paid	Weighted-Average Rate Received
Pay-fixed swaps	$7,004,710	2.84 %	1.65 %	$6,389,187	2.89 %	0.97 %
Receive-fixed swaps	3,836,499	2.18	2.61	4,220,667	1.40	2.68
Total	$10,841,209	2.60 %	2.00 %	$10,609,854	2.29 %	1.65 %

	Nine Months Ended February 28,					
	2018			2017		
(Dollars in thousands)	Average Notional Balance	Weighted-Average Rate Paid	Weighted-Average Rate Received	Average Notional Balance	Weighted-Average Rate Paid	Weighted-Average Rate Received
Pay-fixed swaps	$7,004,166	2.84 %	1.42 %	$6,673,175	2.91 %	0.82 %
Receive-fixed swaps	3,803,670	1.98	2.63	3,858,890	1.24	2.75
Total	$10,807,836	2.53 %	1.85 %	$10,532,065	2.29 %	1.53 %

The average remaining maturity of our pay-fixed and receive-fixed swaps was 19 years and five years, respectively, as of February 28, 2018. In comparison, the average remaining maturity of our pay-fixed and receive-fixed swaps was 19 years and four years, respectively, as of February 28, 2017.

Pay-fixed swaps generally decrease in value as interest rates decline and increase in value as interest rates rise. In contrast, receive-fixed swaps generally increase in value as interest rates decline and decrease in value as interest rates rise. Because our pay-fixed and receive-fixed swaps are referenced to different maturity terms along the swap yield curve, different changes in the swap yield curve— parallel, flattening or steepening—will result in differences in the fair value of our derivatives. The chart below provides comparative swap yield curves as of the end of February 28, 2018, November 30, 2017, May 31, 2017, February 28, 2017 and May 31, 2016.

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Benchmark rates obtained from Bloomberg.

Table 6 presents the components of net derivative gains (losses) recorded in our condensed consolidated results of operations for the three and nine months ended February 28, 2018 and 2017. Derivative cash settlements represent the net periodic contractual interest amount for our interest-rate swaps for the reporting period. Derivative forward value gains (losses) represent the change in fair value of our interest rate swaps during the reporting period due to changes in expected future interest rates over the remaining life of our derivative contracts.

Table 6: Derivative Gains (Losses)

	Three Months Ended February 28,		Nine Months Ended February 28,	
(Dollars in thousands)	2018	2017	2018	2017
Derivative gains (losses) attributable to:				
Derivative cash settlements	$(18,924)	$(19,354)	$(58,781)	$(64,331)
Derivative forward value gains	186,972	61,809	306,224	259,153
Derivative gains	$168,048	$42,455	$247,443	$194,822

The net derivative gains of $168 million and $247 million for the three and nine months ended February 28, 2018, respectively, were largely attributable to a net increase in the fair value of our pay-fixed swaps as interest rates increased across the yield curve.

The net derivative gains of $42 million and $195 million for the three and nine months ended February 28, 2017, respectively, were primarily attributable to a net increase in the fair value of our swaps due to an overall increase in interest rates during the periods.

As depicted above in the chart of comparative yield curves, the general level of market interest rates as of the end of the three and nine months ended February 28, 2018 was higher relative to the general level of market rates as of the end of the comparative prior-year periods, which resulted in the recognition of significantly higher net derivative gain amounts.

See “Note 8—Derivative Instruments and Hedging Activities” for additional information on our derivative instruments.

Results of Operations of Foreclosed Assets

Results of operations of foreclosed assets consists of the operating results of entities controlled by CFC that hold foreclosed assets, impairment charges related to those entities, gains or losses related to the disposition of the entities and potential subsequent charges related to those assets. On July 1, 2016, we completed the sale of Caribbean Asset Holdings, LLC (“CAH”). As a result, we did not carry any foreclosed assets on our consolidated balance sheet as of February 28, 2018 or May 31, 2017.

We recorded charges related to CAH of less than $1 million for the nine months ended February 28, 2018. These charges were attributable to legal fees. We recorded charges related to CAH of less than $1 million for the three months ended February 28, 2017 and $2 million for the nine months ended February 28, 2017, attributable to the combined impact of adjustments recorded at the closing date of the sale of CAH, post-closing purchase price adjustments and certain legal costs incurred pertaining to CAH.

In connection with the sale of CAH, $16 million of the sale proceeds was deposited into escrow to fund potential indemnification claims for a period of 15 months following the closing. Of this amount, $14.5 million was designated to cover general indemnification claims and $1.5 million was designated to cover indemnification of certain tax liens. On September 27, 2017, we received a claim notice from the purchaser of CAH asserting potential indemnification claims against the general escrow amount of $14.5 million. The claims were not substantiated sufficiently to be funded; therefore, the $14.5 million has been released back to us. The $1.5 million designated for tax liens remains in escrow. We continue to be liable for certain indemnifications regardless of whether amounts are held in escrow.

Non-Interest Expense

Non-interest expense consists of salaries and employee benefit expense, general and administrative expenses, losses on early extinguishment of debt and other miscellaneous expenses.

Table 7 presents the components of non-interest expense recorded in our condensed consolidated results of operations for the three and nine months ended February 28, 2018 and 2017.

Table 7: Non-Interest Expense

	Three Months Ended February 28,		Nine Months Ended February 28,	
(Dollars in thousands)	2018	2017	2018	2017
Non-interest expense:				
Salaries and employee benefits	$(13,011)	$(11,537)	$(36,843)	$(34,412)
Other general and administrative expenses	(9,201)	(9,173)	(28,919)	(27,789)
Gains on early extinguishment of debt	—	192	—	192
Other non-interest expense	(402)	(486)	(1,542)	(1,446)
Total non-interest expense	$(22,614)	$(21,004)	$(67,304)	$(63,455)

Non-interest expense of $23 million for the current quarter increased by $2 million, or 8%, from the same prior-year quarter. Non-interest expense of $67 million for the nine months ended February 28, 2018 increased by $4 million, or 6%, from the prior-year period. These increases were primarily attributable to higher expenses related to salaries and employee benefits and other general and administrative operating expenses.

Net Income (Loss) Attributable to Noncontrolling Interests

Net income (loss) attributable to noncontrolling interests represents 100% of the results of operations of NCSC and RTFC, as the members of NCSC and RTFC own or control 100% of the interest in their respective companies. The fluctuations in net income (loss) attributable to noncontrolling interests are primarily due to changes in the fair value of NCSC's derivative instruments recognized in NCSC's earnings.

We recorded net income attributable to noncontrolling interests of $2 million and $3 million during the three and nine months ended February 28, 2018, respectively. In comparison, we recorded net income attributable to noncontrolling interests of less than $1 million and $2 million for the three and nine months ended February 28, 2017, respectively.

CONSOLIDATED BALANCE SHEET ANALYSIS

Total assets of $26,476 million as of February 28, 2018 increased by $1,271 million, or 5%, from May 31, 2017, primarily due to growth in our loan portfolio. Total liabilities of $25,017 million as of February 28, 2018 increased by $910 million, or 4%, from May 31, 2017, largely due to debt issuances to fund loan growth. Total equity increased by $360 million to $1,459 million as of February 28, 2018, attributable to our reported net income of $409 million for the nine months ended
February 28, 2018, which was partially offset by patronage capital retirement of $45 million.

Following is a discussion of changes in the major components of our assets and liabilities during the nine months ended February 28, 2018. Period-end balance sheet amounts may vary from average balance sheet amounts due to liquidity and balance sheet management activities that are intended to manage liquidity requirements for the company and our customers, and our market risk exposure in accordance with our risk appetite.

Loan Portfolio

We offer long-term fixed- and variable-rate loans and line of credit variable-rate loans. The substantial majority of loans in our portfolio represent advances under secured long-term facilities with terms up to 35 years. Borrowers have the option of selecting a fixed or variable interest rate for each advance for periods ranging from one year to the final maturity of the facility. Line of credit loans are typically revolving facilities and are generally unsecured.

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Loans Outstanding

Table 8 summarizes loans to members, by loan type and by member class, as of February 28, 2018 and May 31, 2017. As indicated in Table 8, long-term fixed-rate loans accounted for 90% and 91% of loans to members as of February 28, 2018 and May 31, 2017, respectively.

Table 8: Loans Outstanding by Type and Member Class

	February 28, 2018		May 31, 2017		Increase/
(Dollars in thousands)	Amount	% of Total	Amount	% of Total	(Decrease)
Loans by type:					
Long-term loans:					
Fixed-rate	$22,737,089	90 %	$22,136,690	91 %	$600,399
Variable-rate	985,714	4	847,419	3	138,295
Total long-term loans	23,722,803	94	22,984,109	94	738,694
Lines of credit	1,609,032	6	1,372,221	6	236,811
Total loans outstanding	25,331,835	100	24,356,330	100	975,505
Deferred loan origination costs	11,087	—	10,714	—	373
Loans to members	$25,342,922	100%	$24,367,044	100%	$975,878
Loans by member class:					
CFC:					
Distribution	$19,687,812	78 %	$18,825,366	77 %	$862,446
Power supply	4,422,600	18	4,504,791	19	(82,191)
Statewide and associate	57,144	—	57,830	—	(686)
CFC total	24,167,556	96	23,387,987	96	779,569
NCSC	800,814	3	613,924	3	186,890
RTFC	363,465	1	354,419	1	9,046
Total loans outstanding	25,331,835	100	24,356,330	100	975,505
Deferred loan origination costs	11,087	—	10,714	—	373
Loans to members	$25,342,922	100%	$24,367,044	100%	$975,878

Loans to members totaled $25,343 million as of February 28, 2018, an increase of $976 million, or 4%, from May 31, 2017. The increase was primarily due to an increase in CFC distribution loans of $862 million, an increase in NCSC loans of $187 million and an increase in RTFC loans of $9 million, which was partially offset by a decrease in CFC power supply loans of $82 million. Long-term loan advances totaled $1,864 million during the nine months ended February 28, 2018, with approximately 64% of those advances for capital expenditures by members and 25% for the refinancing of loans made by other lenders.

We provide additional information on our loan product types in “Item 1. Business—Loan Programs” and “Note 4—Loans and Commitments” in our 2017 Form 10-K. See “Debt—Secured Borrowings” below for information on encumbered and unencumbered loans and “Credit Risk Management” for information on the credit risk profile of our loan portfolio.

Loan Retention Rate

Table 9 presents a comparison between the historical retention rate of CFC’s long-term fixed-rate loans that repriced in accordance with our standard loan provisions, during the nine months ended February 28, 2018 and loans that repriced during fiscal year 2017, and provides information on the percentage of loans that repriced to either another fixed-rate term or a variable rate. The retention rate is calculated based on the election made by the borrower at the repricing date. The average annual retention rate of CFC's repriced loans has been 97% over the last three fiscal years.

Table 9: Historical Retention Rate and Repricing Selection[1]

	Nine Months Ended February 28, 2018		Fiscal Year Ended May 31, 2017	
(Dollars in thousands)	Amount	% of Total	Amount	% of Total
Loans retained:				
Long-term fixed rate selected	$646,448	83 %	$824,415	84 %
Long-term variable rate selected	134,761	17	137,835	14
Total loans retained by CFC	781,209	100	962,250	98
Loans repriced and sold by CFC	—	—	1,401	—
Loans repaid	2,067	—	23,675	2
Total	$783,276	100%	$987,326	100%

[1]Does not include NCSC and RTFC loans.

Debt

We utilize both short-term and long-term borrowings as part of our funding strategy and asset/liability interest rate risk management. We seek to maintain diversified funding sources across products, programs and markets to manage funding concentrations and reduce our liquidity or debt roll-over risk. Our funding sources include a variety of secured and unsecured debt securities in a wide range of maturities to our members and affiliates and in the capital markets.

Debt Outstanding

Table 10 displays the composition, by product type, of our outstanding debt as of February 28, 2018 and May 31, 2017. Table 10 also displays the composition of our debt based on several additional selected attributes.

Table 10: Total Debt Outstanding

(Dollars in thousands)	February 28, 2018	May 31, 2017	Increase/ (Decrease)
Debt product type:			
Commercial paper:			
Members, at par	$1,021,016	$928,158	$92,858
Dealer, net of discounts	1,055,147	999,691	55,456
Total commercial paper	2,076,163	1,927,849	148,314
Select notes to members	674,319	696,889	(22,570)
Daily liquidity fund notes to members	506,921	527,990	(21,069)
Medium-term notes:			
Members, at par	647,706	612,951	34,755
Dealer, net of discounts	3,058,178	2,364,671	693,507
Total medium-term notes	3,705,884	2,977,622	728,262
Collateral trust bonds	7,634,863	7,634,048	815
Guaranteed Underwriter Program notes payable	4,871,532	4,985,484	(113,952)
Farmer Mac notes payable	2,805,376	2,513,389	291,987
Other notes payable	31,814	35,223	(3,409)
Subordinated deferrable debt	742,375	742,274	101
Members' subordinated certificates:			
Membership subordinated certificates	630,391	630,098	293
Loan and guarantee subordinated certificates	528,154	567,830	(39,676)
Member capital securities	221,148	221,097	51
Total members' subordinated certificates	1,379,693	1,419,025	(39,332)
Total debt outstanding	$24,428,940	$23,459,793	$969,147
Security type:			
Unsecured debt	37 %	35 %	
Secured debt	63	65	
Total	100 %	100 %	
Funding source:			
Members	17 %	18 %	
Private placement:			
Guaranteed Underwriter Program notes payable	20	21	
Farmer Mac notes payable	12	11	
Total private placement	32	32	
Capital markets	51	50	
Total	100 %	100 %	
Interest rate type:			
Fixed-rate debt	74 %	74 %	
Variable-rate debt	26	26	
Total	100 %	100 %	
Interest rate type, including the impact of swaps:			
Fixed-rate debt[1]	87 %	87 %	
Variable-rate debt[2]	13	13	
Total	100 %	100 %	

Maturity classification:[3]		
Short-term borrowings	14 %	14 %
Long-term and subordinated debt[4]	86	86
Total	100 %	100 %

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(1) Includes variable-rate debt that has been swapped to a fixed rate, net of any fixed-rate debt that has been swapped to a variable rate.
(2) Includes fixed-rate debt that has been swapped to a variable rate, net of any variable-rate debt that has been swapped to a fixed rate. Also includes commercial paper notes, which generally have maturities of less than 90 days. The interest rate on commercial paper notes does not change once the note has been issued; however, the interest rate for new commercial paper issuances changes daily.
(3) Borrowings with an original contractual maturity of one year or less are classified as short-term borrowings. Borrowings with an original contractual maturity of greater than one year are classified as long-term debt.
(4) Consists of long-term debt, subordinated deferrable debt and total members' subordinated debt reported on the condensed consolidated balance sheets. Maturity classification is based on the original contractual maturity as of the date of issuance of the debt.

Our outstanding debt volume generally increases and decreases in response to member loan demand. As outstanding loan balances increased during the nine months ended February 28, 2018, our debt volume also increased. Total debt outstanding was $24,429 million as of February 28, 2018, an increase of $969 million, or 4%, from May 31, 2017. The increase was primarily attributable to a net increase in dealer medium-term notes of $694 million, a net increase in Farmer Mac notes payable of $292 million, a net increase in member commercial paper, select notes and daily liquidity fund notes of $49 million and a net increase in dealer commercial paper outstanding of $55 million. These increases were partially offset by a net decrease in Guaranteed Underwriter Program notes payable of $114 million.

Below is a summary of significant financing activities during the nine months ended February 28, 2018.

- On November 9, 2017, we closed a $750 million committed loan facility ("Series M") from the Federal Financing Bank under the Guaranteed Underwriter Program.

- On November 20, 2017, we amended and restated the three-year and five-year committed bank revolving line of credit agreements to extend the maturity dates to November 20, 2020 and November 20, 2022, respectively, and to terminate certain third-party bank commitments.

- On January 16, 2018, we redeemed $325 million of notes payable outstanding, with an effective interest rate of 2.10% and an original maturity of April 15, 2026, under the Guaranteed Underwriter Program.

- On February 7, 2018, we issued $700 million aggregate principal amount of 3.40% collateral trust bonds due 2028.

- On February 26, 2018, we amended the revolving note purchase agreement with Farmer Mac, dated March 24, 2011. Under the amended agreement, we currently can borrow, subject to market conditions, up to $5,200 million at any time through January 11, 2022.

Member Investments

Debt securities issued to our members represent an important, stable source of funding. Table 11 displays outstanding member debt, by debt product type, as of February 28, 2018 and May 31, 2017.

Table 11: Member Investments

	February 28, 2018		May 31, 2017		
(Dollars in thousands)	Amount	% of Total (1)	Amount	% of Total (1)	Increase/ (Decrease)
Commercial paper	$1,021,016	49 %	$928,158	48 %	$92,858

Select notes	674,319	100	696,889	100	(22,570)
Daily liquidity fund notes	506,921	100	527,990	100	(21,069)
Medium-term notes	647,706	17	612,951	20	34,755
Members' subordinated certificates	1,379,693	100	1,419,025	100	(39,332)
Total outstanding member debt	$4,229,655		$4,185,013		$ 44,642
Percentage of total debt outstanding	17	%	18	%	

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(1) Represents outstanding debt attributable to members for each debt product type as a percentage of the total outstanding debt for each debt product type.

Member investments accounted for 17% and 18% of total debt outstanding as of February 28, 2018 and May 31, 2017, respectively. Over the last three fiscal years, outstanding member investments have averaged $4,297 million on a quarterly basis.

Short-Term Borrowings

Short-term borrowings consist of borrowings with an original contractual maturity of one year or less and do not include the current portion of long-term debt. Short-term borrowings totaled $3,494 million and accounted for 14% of total debt outstanding as of February 28, 2018, compared with $3,343 million, or 14%, of total debt outstanding as of May 31, 2017. See Table 27: Short-Term Borrowings below under “Liquidity Risk” for detail on the composition of our short-term borrowings.

Long-Term and Subordinated Debt

Long-term debt, defined as debt with an original contractual maturity term of greater than one year, primarily consists of medium-term notes, collateral trust bonds, notes payable under the Guaranteed Underwriter Program and notes payable under our note purchase agreement with Farmer Mac. Subordinated debt consists of subordinated deferrable debt and members’ subordinated certificates. Our subordinated deferrable debt and members’ subordinated certificates have original contractual maturity terms of greater than one year.

Long-term and subordinated debt totaled $20,935 million and accounted for 86% of total debt outstanding as of February 28, 2018, compared with $20,117 million, or 86%, of total debt outstanding as of May 31, 2017. As discussed above, the increase in total debt outstanding, including long-term and subordinated debt, was primarily due to the issuance of debt to fund the growth in our loan and investments portfolios. See Table 28: Issuances and Repayments of Long-Term and Subordinated Debt below under “Liquidity Risk” for a summary of long-term subordinated debt issuances and repayments during the nine months ended February 28, 2018.

Collateral Pledged

We are required to pledge loans or other collateral in borrowing transactions under our collateral trust bond indentures, note purchase agreements with Farmer Mac and bond agreements under the Guaranteed Underwriter Program. We are required to maintain pledged collateral equal to at least 100% of the face amount of outstanding borrowings. However, we typically maintain pledged collateral in excess of the required percentage to ensure that required collateral levels are maintained and to facilitate the timely execution of debt issuances by reducing or eliminating the lead time to pledge additional collateral. Under the provisions of our committed bank revolving line of credit agreements, the excess collateral that we are allowed to pledge cannot exceed 150% of the outstanding borrowings under our collateral trust bond indentures, Farmer Mac note purchase agreements or the Guaranteed Underwriter Program. In certain cases, provided that all conditions of eligibility under the different programs are satisfied, we may withdraw excess pledged collateral or transfer collateral from one borrowing program to another to facilitate a new debt issuance.

Table 12 displays the collateral coverage ratios as of February 28, 2018 and May 31, 2017 for the debt agreements noted above that require us to pledge collateral.

Table 12: Collateral Pledged

	Requirement/Limit		Actual[1]	
Debt Agreement	Debt Indenture Minimum	Committed Bank Revolving	February 28, 2018	May 31, 2017

		Line of Credit Agreements Maximum		
Collateral trust bonds 1994 indenture	100 %	150 %	113 %	117 %
Collateral trust bonds 2007 indenture	100	150	112	115
Guaranteed Underwriter Program notes payable	100	150	120	117
Farmer Mac notes payable	100	150	120	117
Clean Renewable Energy Bonds Series 2009A	100	150	115	113

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(1) Calculated based on the amount of collateral pledged divided by the face amount of outstanding secured debt.

Of our total debt outstanding of $24,429 million as of February 28, 2018, $15,323 million, or 63%, was secured by pledged loans totaling $18,061 million. In comparison, of our total debt outstanding of $23,460 million as of May 31, 2017, $15,146 million, or 65%, was secured by pledged loans totaling $17,941 million. Total debt outstanding on our condensed consolidated balance sheet is presented net of unamortized discounts and issuance costs. However, our collateral pledging requirements are based on the face amount of secured outstanding debt, which does not take into consideration the impact of net unamortized discounts and issuance costs.

Table 13 displays the unpaid principal balance of loans pledged for secured debt, the excess collateral pledged and unencumbered loans as of February 28, 2018 and May 31, 2017.

Table 13: Unencumbered Loans

(Dollars in thousands)	February 28, 2018	May 31, 2017
Total loans outstanding[1]	$25,331,835	$24,356,330
Less: Loans required to be pledged for secured debt [2]	(15,606,414)	(15,435,062)
Loans pledged in excess of requirement [2][3]	(2,454,694)	(2,505,804)
Total pledged loans	(18,061,108)	(17,940,866)
Unencumbered loans	$7,270,727	$6,415,464
Unencumbered loans as a percentage of total loans	29 %	26 %

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(1) Reflects unpaid principal balance. Excludes unamortized deferred loan origination costs of $11 million as of both February 28, 2018 and May 31, 2017.
(2) Reflects unpaid principal balance of pledged loans.
(3) Excludes cash collateral pledged to secure debt. If there is an event of default under most of our indentures, we can only withdraw the excess collateral if we substitute cash or permitted investments of equal value.

As displayed above in Table 13, we had excess loans pledged as collateral totaling $2,455 million and $2,506 million as of February 28, 2018 and May 31, 2017, respectively. We typically pledge loans in excess of the required amount for the following reasons: (i) our distribution and power supply loans are typically amortizing loans that require scheduled principal payments over the life of the loan, whereas the debt securities issued under secured indentures and agreements typically have bullet maturities; (ii) distribution and power supply borrowers have the option to prepay their loans; and (iii) individual loans may become ineligible for various reasons, some of which may be temporary.

We provide additional information on our borrowings, including the maturity profile, below in “Liquidity Risk.” Refer to “Note 4—Loans and Commitments—Pledging of Loans” for additional information related to pledged collateral. Also refer to “Note 6—Short-Term Borrowings,” “Note 7—Long-Term Debt,” “Note 8—Subordinated Deferrable Debt” and “Note 9—Members’ Subordinated Certificates” in our 2017 Form 10-K for a more detailed description of each of our debt product types.

Equity

Total equity increased by $360 million to $1,459 million as of February 28, 2018. The increase was primarily attributable to our net income of $409 million for the nine months ended February 28, 2018, which was partially offset by patronage capital retirement of $45 million in September 2017.

In July 2017, the CFC Board of Directors authorized the allocation of fiscal year 2017 adjusted net income as follows: $90 million to members in the form of patronage capital; $43 million to members' capital reserve; and $1 million to the Cooperative Educational Fund. The amount of patronage capital allocated each year by CFC's Board of Directors is based on adjusted non-GAAP net income, which excludes the impact of derivative forward value gains (losses). See "Non-GAAP Financial Measures" for information on adjusted net income.

In July 2017, the CFC Board of Directors authorized the retirement of patronage capital totaling $45 million, which represented 50% of the fiscal year 2017 allocation of patronage capital of $90 million. We returned the $45 million to members in cash in September 2017. The remaining portion of the allocated amount will be retained by CFC for 25 years under guidelines adopted by the CFC Board of Directors in June 2009.

The CFC Board of Directors is required to make annual allocations of adjusted net income, if any. CFC has made annual retirements of allocated net earnings in 38 of the last 39 fiscal years; however, future retirements of allocated amounts are determined based on CFC's financial condition. The CFC Board of Directors has the authority to change the current practice for allocating and retiring net earnings at any time, subject to applicable laws. See "Item 1. Business—Allocation and Retirement of Patronage Capital" of our 2017 Form 10-K for additional information.

OFF-BALANCE SHEET ARRANGEMENTS

In the ordinary course of business, we engage in financial transactions that are not presented on our condensed consolidated balance sheets, or may be recorded on our condensed consolidated balance sheets in amounts that are different from the full contract or notional amount of the transaction. Our off-balance sheet arrangements consist primarily of guarantees of member obligations and unadvanced loan commitments intended to meet the financial needs of our members.

Guarantees

We provide guarantees for certain contractual obligations of our members to assist them in obtaining various forms of financing. Table 14 displays the notional amount of our outstanding guarantee obligations, by guarantee type and by company, as of February 28, 2018 and May 31, 2017.

Table 14: Guarantees Outstanding

(Dollars in thousands)	February 28, 2018	May 31, 2017	Increase/ (Decrease)
Guarantee type:			
Long-term tax-exempt bonds	$317,960	$468,145	$(150,185)
Letters of credit	248,124	307,321	(59,197)
Other guarantees	113,884	114,151	(267)
Total	$679,968	$889,617	$(209,649)
Company:			
CFC	$663,235	$874,920	$(211,685)
NCSC	15,159	13,123	2,036
RTFC	1,574	1,574	—
Total	$679,968	$889,617	$(209,649)

Of the total notional amount of our outstanding guarantee obligations of $680 million and $890 million as of February 28, 2018 and May 31, 2017, respectively, 53% and 67%, respectively, were secured by a mortgage lien on substantially all of the assets and future revenue of the borrowers. We recorded a guarantee liability of $8 million and $15 million as of February 28, 2018 and May 31, 2017, respectively, related to the contingent and noncontingent exposures for guarantee and liquidity obligations associated with our members' debt.

We were the liquidity provider as well as guarantor for long-term variable-rate, tax-exempt bonds issued for our member cooperatives totaling $251 million as of February 28, 2018. This amount is included above in Table 14 as a component of the long-term tax-exempt bonds totaling $318 million as of February 28, 2018. As liquidity provider on these tax-exempt bonds, we may be required to purchase bonds that are tendered or put by investors. Investors provide notice to the remarketing agent that they will tender or put a certain amount of bonds at the next interest rate reset date. If the remarketing agent is unable to sell such bonds to other investors by the next interest rate reset date, we have unconditionally agreed to purchase such bonds. We were not required to perform as liquidity provider pursuant to these obligations during the nine months ended February 28, 2018 or the prior fiscal year.

We had outstanding letters of credit for the benefit of our members totaling $248 million as of February 28, 2018, which are related to obligations for which we may be required to advance funds based on various trigger events specified in the letters of credit agreements. If we are required to advance funds, the member is obligated to repay the advance amount, and accrued interest, to us.

In addition to the letters of credit presented in Table 14, we had master letter of credit facilities in place as of February 28, 2018, under which we may be required to issue up to an additional $66 million in letters of credit to third parties for the benefit of our members. All of our master letter of credit facilities as of February 28, 2018 were subject to material adverse change clauses at the time of issuance. Prior to issuing a letter of credit under these facilities, we confirm that there has been no material adverse change in the business or condition, financial or otherwise, of the borrower since the time the loan was approved and that the borrower is currently in compliance with the letter of credit terms and conditions.

Table 15 presents the maturities for each of the next five fiscal years and thereafter of the notional amount of our outstanding guarantee obligations as of February 28, 2018.

Table 15: Maturities of Guarantee Obligations

	Outstanding	Maturities of Guaranteed Obligations					
(Dollars in thousands)	Amount	2018	2019	2020	2021	2022	Thereafter
Guarantees	$ 679,968	$128,126	$153,908	$52,090	$122,136	$27,854	$195,854

We provide additional information about our guarantee obligations in “Note 10—Guarantees.”

Unadvanced Loan Commitments

Unadvanced loan commitments represent approved and executed loan contracts for which funds have not been advanced to borrowers. Our line of credit commitments include both contracts that are subject to material adverse change clauses and contracts that are not subject to material adverse change clauses, while our long-term loan commitments are typically subject to material adverse change clauses.

Table 16 displays the amount of unadvanced loan commitments, which consist of line of credit and long-term loan commitments, as of February 28, 2018 and May 31, 2017.

Table 16: Unadvanced Loan Commitments

	February 28, 2018		May 31, 2017		Increase/
(Dollars in thousands)	Amount	% of Total	Amount	% of Total	(Decrease)
Line of credit commitments:					
Conditional[1]	$4,658,370	38 %	$5,170,393	41 %	$(512,023)
Unconditional[2]	2,776,918	23	2,602,262	21	174,656
Total line of credit unadvanced commitments	7,435,288	61	7,772,655	62	(337,367)
Total long-term loan unadvanced commitments[1]	4,715,976	39	4,802,319	38	(86,343)
Total unadvanced loan commitments	$12,151,264	100%	$12,574,974	100%	$(423,710)

[1]Represents amount related to facilities that are subject to material adverse change clauses.
[2]Represents amount related to facilities that are not subject to material adverse change clauses.

Table 17 presents the amount of unadvanced loan commitments, by loan type, as of February 28, 2018 and the maturities of the commitment amounts for each of the next five fiscal years and thereafter.

Table 17: Notional Maturities of Unadvanced Loan Commitments

	Available	Notional Maturities of Unadvanced Loan Commitments					
(Dollars in thousands)	Balance	2018	2019	2020	2021	2022	Thereafter
Line of credit loans	$7,435,288	$226,587	$4,057,079	$782,079	$995,502	$707,497	$666,544
Long-term loans	4,715,976	71,913	924,921	585,953	637,024	1,742,934	753,231
Total	$12,151,264	$298,500	$4,982,000	$1,368,032	$1,632,526	$2,450,431	$1,419,775

Unadvanced line of credit commitments accounted for 61% of total unadvanced loan commitments as of February 28, 2018, while unadvanced long-term loan commitments accounted for 39% of total unadvanced loan commitments. Unadvanced line of credit commitments are typically revolving facilities for periods not to exceed five years. Unadvanced line of credit commitments generally serve as supplemental back-up liquidity to our borrowers. Historically, borrowers have not drawn the full commitment amount for line of credit facilities, and we have experienced a very low utilization rate on line of credit loan facilities regardless of whether or not we are obligated to fund the facility where a material adverse change exists. Our unadvanced long-term loan commitments have a five-year draw period under which a borrower may advance funds prior to the expiration of the commitment. We expect that the majority of the long-term unadvanced loan commitments of $4,716 million will be advanced prior to the expiration of the commitment.

Because we historically have experienced a very low utilization rate on line of credit loan facilities, which account for the majority of our total unadvanced loan commitments, we believe the unadvanced loan commitment total of $12,151 million as of February 28, 2018 is not necessarily representative of our future funding cash requirements.

Unadvanced Loan Commitments—Conditional

The substantial majority of our line of credit commitments and all our unadvanced long-term loan commitments include material adverse change clauses. Unadvanced loan commitments subject to material adverse change clauses totaled $9,374 million and $9,973 million as of February 28, 2018 and May 31, 2017, respectively, and accounted for 77% and 79% of the combined total of unadvanced line of credit and long-term loan commitments as of February 28, 2018 and May 31, 2017, respectively. Prior to making advances on these facilities, we confirm that there has been no material adverse change in the borrower's business or condition, financial or otherwise, since the time the loan was approved and confirm that the borrower is currently in compliance with loan terms and conditions. In some cases, the borrower's access to the full amount of the facility is further constrained by use of proceeds restrictions, imposition of borrower-specific restrictions, or by additional conditions that must be met prior to advancing funds. Since we generally do not charge a fee for the borrower to have an unadvanced amount on a loan facility that is subject to a material adverse change clause, our borrowers tend to request amounts in excess of their immediate estimated loan requirements.

Unadvanced Loan Commitments—Unconditional

Unadvanced loan commitments not subject to material adverse change clauses at the time of each advance consisted of unadvanced committed lines of credit totaling $2,777 million and $2,602 million as of February 28, 2018 and May 31, 2017, respectively. For contracts not subject to a material adverse change clause, we are generally required to advance amounts on the committed facilities as long as the borrower is in compliance with the terms and conditions of the facility.

Syndicated loan facilities, where the pricing is set at a spread over LIBOR as agreed upon by all of the participating banks based on market conditions at the time of syndication, accounted for 85% of unconditional line of credit commitments as of February 28, 2018. The remaining 15% represented unconditional committed line of credit loans which under any new advance would be made at rates determined by us based on our cost, and we have the option to pass on to the borrower any cost increase related to the advance.

Table 18 presents the maturities for each of the next five fiscal years and thereafter of the notional amount of unconditional committed lines of credit not subject to a material adverse change clause as of February 28, 2018.

Table 18: Maturities of Notional Amount of Unconditional Committed Lines of Credit

(Dollars in thousands)	Available Balance	Notional Maturities of Unconditional Committed Lines of Credit					
		2018	2019	2020	2021	2022	Thereafter
Committed lines of credit	$2,776,918	$130,000	$306,122	$515,691	$645,083	$487,908	$692,114

See "MD&A—Off-Balance Sheet Arrangements" in our 2017 Form 10-K for additional information on our off-balance sheet arrangements.

RISK MANAGEMENT

Overview

We face a variety of risks that can significantly affect our financial performance, liquidity, reputation and ability to meet the expectations of our members, investors and other stakeholders. As a financial services company, the major categories of risk exposures inherent in our business activities include credit risk, liquidity risk, market risk and operational risk. These risk categories are summarized below.

- Credit risk is the risk that a borrower or other counterparty will be unable to meet its obligations in accordance with agreed-upon terms.

- Liquidity risk is the risk that we will be unable to fund our operations and meet our contractual obligations or that we will be unable to fund new loans to borrowers at a reasonable cost and tenor in a timely manner.

- Market risk is the risk that changes in market variables, such as movements in interest rates, may adversely affect the match between the timing of the contractual maturities, re-pricing and prepayments of our financial assets and the related financial liabilities funding those assets.

- Operational risk is the risk of loss resulting from inadequate or failed internal controls, processes, systems, human error or external events. Operational risk also includes compliance risk, fiduciary risk, reputational risk and litigation risk.

Effective risk management is critical to our overall operations and in achieving our primary objective of providing cost-based financial products to our rural electric members while maintaining the sound financial results required for investment-grade credit ratings on our debt instruments. Accordingly, we have a risk management framework that is intended to govern the principal risks we face in conducting our business and the aggregate amount of risk we are willing to accept, referred to as risk appetite, in the context of CFC's mission and strategic objectives and initiatives. We provide information on our risk management framework in our 2017 Form 10-K under "Item 7. MD&A—Risk Management—Risk Management Framework."

CREDIT RISK

Our loan portfolio, which represents the largest component of assets on our balance sheet, and guarantees account for the substantial majority of our credit risk exposure. We also engage in certain non-lending activities that may give rise to credit and counterparty settlement risk, including the purchase of investment securities and entering into derivative transactions to manage our interest rate risk. Our primary credit exposure is to rural electric cooperatives that provide essential electric services to end-users, the majority of which are residential customers. We also have a limited portfolio of loans to not-for-profit and for-profit telecommunication companies.

Credit Risk Management

We manage portfolio and borrower credit risk consistent with credit policies established by the CFC Board of Directors and through credit underwriting, approval and monitoring processes and practices adopted by management. Our board- established credit policies include guidelines regarding the types of credit products we offer, limits on credit we extend to individual borrowers, approval authorities delegated to management, and use of syndications and loan sales. We maintain an internal risk rating system in which we assign a rating to each borrower and credit facility. We review and update the risk ratings at least annually. Assigned risk ratings inform our credit approval, borrower monitoring and portfolio review processes. Our Corporate Credit Committee approves individual credit actions within its own authority and together with our Credit Risk Management group, establishes standards for credit underwriting, oversees credits deemed to be higher risk, reviews assigned risk ratings for accuracy, and monitors the overall credit quality and performance statistics of our loan portfolio and guarantees.

Loan and Guarantee Portfolio Credit Risk

Below we provide information on the credit risk profile of our loan portfolio and guarantees, including security provisions, loan concentration, credit performance and our allowance for loan losses.

Security Provisions

Except when providing line of credit loans, we generally lend to our members on a senior secured basis. Long-term loans are generally secured on parity with other secured lenders (primarily RUS), if any, by all assets and revenue of the borrower with exceptions typical in utility mortgages. Line of credit loans are generally unsecured. In addition to the collateral pledged to secure our loans, distribution and power supply borrowers also are required to set rates charged to customers to achieve certain specified financial ratios.

Table 19 presents, by loan type and by company, the amount and percentage of secured and unsecured loans in our loan portfolio as of February 28, 2018 and May 31, 2017. Of our total loans outstanding, 91% were secured and 9% were unsecured as of February 28, 2018. Of our total loans outstanding, 92% were secured and 8% were unsecured as of
May 31, 2017.

Table 19: Loan Portfolio Security Profile[1]

	February 28, 2018				
(Dollars in thousands)	Secured	% of Total	Unsecured	% of Total	Total
Loan type:					
Long-term loans:					
Long-term fixed-rate loans	$22,162,866	97 %	$574,223	3 %	$22,737,089
Long-term variable-rate loans	941,772	96	43,942	4	985,714
Total long-term loans	23,104,638	97	618,165	3	23,722,803
Line of credit loans	68,267	4	1,540,765	96	1,609,032
Total loans outstanding	$23,172,905	91	$2,158,930	9	$25,331,835
Company:					
CFC	$22,183,116	92 %	$1,984,440	8 %	$24,167,556
NCSC	641,526	80	159,288	20	800,814
RTFC	348,263	96	15,202	4	363,465
Total loans outstanding	$23,172,905	91	$2,158,930	9	$25,331,835

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	May 31, 2017				
(Dollars in thousands)	Secured	% of Total	Unsecured	% of Total	Total
Loan type:					
Long-term loans:					
Long-term fixed-rate loans	$21,503,871	97 %	$632,819	3 %	$22,136,690
Long-term variable-rate loans	795,326	94	52,093	6	847,419
Total long-term loans	22,299,197	97	684,912	3	22,984,109
Line of credit loans	54,258	4	1,317,963	96	1,372,221
Total loans outstanding	$22,353,455	92	$2,002,875	8	$24,356,330
Company:					
CFC	$21,591,723	92 %	$1,796,264	8 %	$23,387,987
NCSC	424,636	69	189,288	31	613,924
RTFC	337,096	95	17,323	5	354,419
Total loans outstanding	$22,353,455	92	$2,002,875	8	$24,356,330

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(1) Excludes deferred loan origination costs of $11 million as of both February 28, 2018 and May 31, 2017.

As part of our strategy in managing our credit risk exposure, we entered into a long-term standby purchase commitment agreement with Farmer Mac on August 31, 2015, as amended on May 31, 2016. Under this agreement, we may designate certain loans to be covered under the commitment, as approved by Farmer Mac, and in the event any such loan later goes into payment default for at least 90 days, upon request by us, Farmer Mac must purchase such loan at par value. The outstanding principal balance of loans covered under this agreement totaled $777 million as of February 28, 2018, compared with $843 million as of May 31, 2017. No loans have been put to Farmer Mac for purchase pursuant to this agreement. In addition, RUS guaranteed long-term loans totaling $163 million and $167 million as of February 28, 2018 and
May 31, 2017, respectively.

Credit Concentration

As a tax-exempt, member-owned finance cooperative, CFC's principal focus is to provide funding to its rural electric utility cooperative members to assist them in acquiring, constructing and operating electric distribution, transmission and related facilities. We serve electric and telecommunications members throughout the United States and its territories, including 49 states, the District of Columbia, American Samoa and Guam. Our consolidated membership totaled 1,447 members and 217 associates as of February 28, 2018. Texas had the largest concentration of outstanding loans to borrowers in any one state, with approximately 15% of total loans outstanding as of both February 28, 2018 and May 31, 2017. Outstanding loans to electric utility organizations represented approximately 99% of the total outstanding loan portfolio as of February 28, 2018, unchanged from May 31, 2017. As a result of lending primarily to our members, we have a loan portfolio with single-industry and single-obligor concentration risk. Despite our credit concentration risks, we historically have experienced limited defaults and very low credit losses in our electric loan portfolio.

Single-Obligor Concentration

Table 20 displays the outstanding exposure of the 20 largest borrowers, by exposure type and by company, as of February 28, 2018 and May 31, 2017. The 20 largest borrowers consisted of 10 distribution systems, 9 power supply systems and 1 NCSC associate member as of both February 28, 2018 and May 31, 2017. The largest total outstanding exposure to a single borrower or controlled group represented approximately 2% of total loans and guarantees outstanding as of both February 28, 2018 and May 31, 2017.

Table 20: Credit Exposure to 20 Largest Borrowers

	February 28, 2018		May 31, 2017		
(Dollars in thousands)	Amount	% of Total	Amount	% of Total	Change
By exposure type:					
Loans	$5,906,771	23 %	$5,749,885	23 %	$156,886
Guarantees	145,770	—	354,619	1	(208,849)
Total exposure to 20 largest borrowers	6,052,541	23	6,104,504	24	(51,963)
Less: Loans covered under Farmer Mac standby purchase commitment	(386,185)	(1)	(351,699)	(1)	(34,486)
Net exposure to 20 largest borrowers	$5,666,356	22 %	$5,752,805	23 %	$(86,449)
By company:					
CFC	$5,793,218	22 %	$5,899,709	23 %	$(106,491)
NCSC	259,323	1	204,795	1	54,528
Total exposure to 20 largest borrowers	6,052,541	23	6,104,504	24	(51,963)
Less: Loans covered under Farmer Mac standby purchase commitment	(386,185)	(1)	(351,699)	(1)	(34,486)
Net exposure to 20 largest borrowers	$5,666,356	22 %	$5,752,805	23 %	$(86,449)

Credit Performance

As part of our credit risk management process, we monitor and evaluate each borrower and loan in our loan portfolio and assign numeric internal risk ratings based on quantitative and qualitative assessments. Our ratings are intended to align with the federal banking regulatory credit risk rating classification definitions of pass, special mention, substandard and doubtful. The special mention, substandard, and doubtful categories are intended to comply with the definition of criticized loans by the banking regulatory authorities. Internal risk ratings and payment status trends are indicators, among others, of the level of credit risk in our loan portfolio.

The overall credit risk of our loan portfolio remained low, as evidenced by our strong asset quality metrics, including senior secured positions on most of our loans and low levels of criticized exposure, nonaccrual loans and charge-offs. As displayed in Table 19 above, 91% and 92% of our total outstanding loans were secured as of February 28, 2018 and May 31, 2017, respectively. As displayed in "Note 4—Loans and Commitments," 0.4% and 0.5% of the loans in our portfolio were classified as criticized as of February 28, 2018 and May 31, 2017, respectively. Below we provide information on certain additional credit quality indicators, including modified loans that are considered to be troubled debt restructurings ("TDRs"), nonperforming loans and net charge-offs.

Troubled Debt Restructurings

We actively monitor problem loans and, from time to time, attempt to work with borrowers to manage such exposures through loan workouts or modifications that better align with the borrower's current ability to pay. A loan restructuring or modification of terms is accounted for as a TDR if, for economic or legal reasons related to the borrower's financial difficulties, a concession is granted to the borrower that we would not otherwise consider. TDR loans generally are initially placed on nonaccrual status, although in many cases such loans were already on nonaccrual status prior to modification. Interest accrued but not collected at the date a loan is placed on nonaccrual status is reversed against earnings. These loans may be returned to performing status and the accrual of interest resumed if the borrower performs under the modified terms for an extended period of time, and we expect the borrower to continue to perform in accordance with the modified terms. In certain limited circumstances in which a TDR loan is current at the modification date, the loan may remain on accrual status at the time of modification.

Table 21 presents the carrying value of loans modified as TDRs in prior periods as of February 28, 2018 and May 31, 2017. These loans were considered individually impaired as of the end of each period presented.

Table 21: TDR Loans

(Dollars in thousands)	February 28, 2018 Carrying Amount	% of Total Loans Outstanding		May 31, 2017 Carrying Amount	% of Total Loans Outstanding	
TDR loans:						
CFC	$6,507	0.03	%	$6,581	0.02	%
RTFC	6,216	0.02		6,592	0.03	
Total TDR loans	$12,723	0.05	%	$13,173	0.05	%
Performance status of TDR loans:						
Performing TDR loans	$12,723	0.05	%	$13,173	0.05	%

As indicated in Table 21, we did not have any TDR loans classified as nonperforming as of February 28, 2018 or May 31, 2017. TDR loans as of February 28, 2018 and May 31, 2017 were performing in accordance with the terms of their respective restructured loan agreement and on accrual status as of the respective reported dates.

Nonperforming Loans

In addition to TDR loans that may be classified as nonperforming, we also may have nonperforming loans that have not been modified as a TDR loan. We classify such loans as nonperforming at the earlier of the date when we determine: (i) interest or principal payments on the loan is past due 90 days or more; (ii) as a result of court proceedings, the collection of interest or principal payments based on the original contractual terms is not expected; or (iii) the full and timely collection of interest or principal is otherwise uncertain. Once a loan is classified as nonperforming, we generally place the loan on nonaccrual status. Interest accrued but not collected at the date a loan is placed on nonaccrual status is reversed against earnings. We had no loans classified as nonperforming as of February 28, 2018 or May 31, 2017. In addition, we did not have any past due loans as of either February 28, 2018 or May 31, 2017.

We provide additional information on the credit quality of our loan portfolio in “Note 4—Loans and Commitments.”

Net Charge-Offs

Table 22 presents charge-offs, net of recoveries, and the net charge-off rate for the three and nine months ended February 28, 2018 and 2017.

Table 22: Net Charge-Offs (Recoveries)

(Dollars in thousands)	Three Months Ended February 28, 2018		2017		Nine Months Ended February 28, 2018		2017	
Charge-offs:								
RTFC	$—		$—		$—		$2,119	
Recoveries:								
CFC	—		(53	)	—		(159	)
Net charge-offs (recoveries)	$—		$(53	)	$—		$1,960	
Average total loans outstanding	$25,204,005		$24,092,805		$24,822,092		$23,695,378	
Net charge-off rate[(1)]	—	%	—	%	—	%	0.01	%

(1)Calculated based on annualized net charge-offs (recoveries) for the period divided by average total outstanding loans for the period.

As displayed in Table 22, we experienced no charge-offs during the nine months ended February 28, 2018. Charge-offs totaled $2 million during the nine months ended February 28, 2017, all of which were related to telecommunications loans in the RTFC portfolio. Our average annual net charge-off rate has been less than 0.01% over the last three fiscal years.

Allowance for Loan Losses

The allowance for loan losses represents management’s estimate of probable losses inherent in our loan portfolio as of each balance sheet date. We determine the allowance based on borrower risk ratings, historical loss experience, specific problem loans, economic conditions and other pertinent factors that, in management’s judgment, may affect the risk of loss in our loan portfolio.

Table 23 summarizes changes in the allowance for loan losses for the three and nine months ended February 28, 2018 and 2017, and provides a comparison of the allowance by company as of February 28, 2018 and May 31, 2017.

Table 23: Allowance for Loan Losses

	Three Months Ended February 28,		Nine Months Ended February 28,	
(Dollars in thousands)	2018	2017	2018	2017
Beginning balance	$36,774	$33,911	$37,376	$33,258
Provision for loan losses	1,105	2,065	503	4,731
Net recoveries (charge-offs)	—	53	—	(1,960)
Ending balance	$37,879	$36,029	$37,879	$36,029

	February 28, 2018	May 31, 2017
Allowance for loan losses by company:		
CFC	$29,305	$29,499
NCSC	3,848	2,910
RTFC	4,726	4,967
Total	$37,879	$37,376
Allowance coverage ratios:		
Loans to members	$25,342,922	$24,367,044
Percentage of loans to members	0.15%	0.15%

The allowance for loan losses of $38 million as of February 28, 2018 increased by less than $1 million from fiscal year end May 31, 2017, while the allowance coverage ratio remained unchanged at 0.15%. The credit quality and performance statistics of our loan portfolio remained strong. We had no loans classified as nonperforming as of February 28, 2018 or May 31, 2017. We experienced no charge-offs during the nine months ended February 28, 2018. In comparison, we recorded a net charge-off of $2 million during the nine months ended February 28, 2017. Loans designated as individually impaired totaled $13 million as of both February 28, 2018 and May 31, 2017, and the specific allowance related to those loans totaled $1 million and $2 million, respectively.

For additional information on our methodology for determining the allowance for loan losses and the judgment and assumptions involved, see “MD&A—Critical Accounting Policies and Estimates—Allowance for Loan Losses” and “Note 1—Summary of Significant Accounting Policies” in our 2017 Form 10-K. See “Note 4—Loans and Commitments” of this Report for additional information on the credit quality of our loan portfolio and the allowance for loan losses.

Counterparty Credit Risk

We are exposed to counterparty risk related to the performance of the parties with which we entered into financial transactions, primarily for derivative instruments, cash, time deposits and investment securities that we have with various financial institutions. To mitigate this risk, we only enter into these transactions with financial institutions with investment-grade ratings. Our cash and time deposits with financial institutions generally have an original maturity of less than one year.

We manage our derivative counterparty credit risk by requiring that derivative counterparties participate in one of our committed bank revolving line of credit agreements, monitoring the overall credit worthiness of each counterparty, using counterparty specific credit risk limits, executing master netting arrangements and diversifying our derivative transactions among multiple counterparties. Our derivative counterparties had credit ratings ranging from Aa3 to Baa2 by Moody's Investors Service ("Moody's") and from AA- to A- by S&P Global Ratings ("S&P") as of February 28, 2018. Our largest counterparty exposure, based on the outstanding notional amount, represented approximately 22% and 23% of the total outstanding notional amount of derivatives as of February 28, 2018 and May 31, 2017, respectively.

Credit Risk-Related Contingent Features

Our derivative contracts typically contain mutual early termination provisions, generally in the form of a credit rating trigger. Under the mutual credit rating trigger provisions, either counterparty may, but is not obligated to, terminate and settle the agreement if the credit rating of the other counterparty falls to a level specified in the agreement. If a derivative contract is terminated, the amount to be received or paid by us would be equal to the mark-to-market value, as defined in the agreement, as of the termination date.

Our senior unsecured credit ratings from Moody's and S&P were A2 and A, respectively, as of February 28, 2018. Both Moody's and S&P had our ratings on stable outlook as of February 28, 2018. Table 24 displays the notional amounts of our derivative contracts with rating triggers as of February 28, 2018, and the payments that would be required if the contracts were terminated as of that date because of a downgrade of our unsecured credit ratings or the counterparty's unsecured credit ratings below A3/A-, below Baa1/BBB+ to or below Baa2/BBB, below Baa3/BBB- or to or below Ba2/BB+ by Moody's or S&P, respectively. In calculating the payment amounts that would be required upon termination of the derivative contracts, we assumed that the amounts for each counterparty would be netted in accordance with the provisions of the counterparty's master netting agreements. The net payment amounts are based on the fair value of the underlying derivative instrument, excluding the credit risk valuation adjustment, plus any unpaid accrued interest amounts.

Table 24: Rating Triggers for Derivatives

(Dollars in thousands)	Notional Amount	Payable Due From CFC	Receivable Due to CFC	Net (Payable)/Receivable
Impact of rating downgrade trigger:				
Falls below A3/A-[(1)]	$54,890	$(10,007)	$ —	$ (10,007)
Falls below Baa1/BBB+	7,237,155	(61,923)	40,825	(21,098)
Falls to or below Baa2/BBB [(2)]	503,125	—	5,191	5,191
Falls below Baa3/BBB-	258,923	(12,974)	—	(12,974)
Total	$8,054,093	$(84,904)	$ 46,016	$ (38,888)

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[(1)] Rating trigger for CFC falls below A3/A-, while rating trigger for counterparty falls below Baa1/BBB+ by Moody's or S&P, respectively.

(2) Rating trigger for CFC falls to or below Baa2/BBB, while rating trigger for counterparty falls to or below Ba2/BB+ by Moody's or S&P, respectively.

The aggregate fair value amount, including the credit risk valuation adjustment, of all interest rate swaps with rating triggers that were in a net liability position was $85 million as of February 28, 2018. There were no counterparties that fell below the rating trigger levels in our interest swap contracts as of February 28, 2018. If a counterparty has a credit rating that falls below the rating trigger level specified in the interest swap contract, we have the option to terminate all derivatives with the counterparty. However, we generally do not terminate such agreements early because our interest rate swaps are critical to our matched funding strategy.

See "Item 1A. Risk Factors" in our 2017 Form 10-K for additional information about credit risk related to our business.

LIQUIDITY RISK

We consider liquidity to be the ability to access funding or convert assets to cash quickly and efficiently, or to rollover or issue new debt, both under normal operating conditions and under periods of market stress, at a reasonable cost to ensure that we can meet borrower loan requests and other short-term cash obligations.

Liquidity Risk Management

Our liquidity risk management framework is designed to meet our liquidity objectives of providing a reliable source of funding to members, meet maturing debt and other obligations, issue new debt and fund our operations on a cost-effective basis under normal operating conditions as well as under CFC-specific and/or market stress conditions. We engage in various activities to manage liquidity risk and achieve our liquidity objectives. Our Asset Liability Committee establishes guidelines that are intended to ensure that we maintain sufficient, diversified sources of liquidity to cover potential funding requirements as well as unanticipated contingencies. Our Treasury group develops strategies to manage our targeted liquidity position, projects our funding needs under various scenarios, including adverse circumstances, and monitors our liquidity position on an ongoing basis.

Liquidity Reserve

As part of our strategy in meeting our liquidity objectives, we seek to maintain access to liquidity in the form of both on-balance sheet and off-balance sheet funding sources that are readily accessible for immediate liquidity needs. Table 25 below presents the components of our liquidity reserve and a comparison of the amounts available as of February 28, 2018 and May 31, 2017.

Table 25: Liquidity Reserve

	February 28, 2018			May 31, 2017		
(Dollars in millions)	Total	Accessed	Available	Total	Accessed	Available
Cash and cash equivalents	$251	$—	$ 251	$167	$—	$ 167
Committed bank revolving line of credit agreements—unsecured[1]	3,085	2	3,083	3,165	1	3,164
Guaranteed Underwriter Program committed facilities—secured[2]	6,548	5,323	1,225	5,798	5,073	725
Farmer Mac revolving note purchase agreement, dated March 24, 2011—secured[3]	5,200	2,805	2,395	4,500	2,513	1,987
Farmer Mac revolving note purchase agreement, dated July 31, 2015—secured	300	—	300	300	—	300
Total	$15,384	$ 8,130	$ 7,254	$13,930	$ 7,587	$ 6,343

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[1] The accessed amount of $2 million and $1 million as of February 28, 2018 and May 31, 2017, respectively, relates to letters of credit issued pursuant to the line of credit agreement.

[2] The committed facilities under the Guaranteed Underwriting Program are not revolving.

[3] Availability subject to market conditions.

Borrowing Capacity

In addition to cash, our liquidity reserve includes access to funds under committed revolving line of credit agreements with banks, committed loan facilities under the Guaranteed Underwriter Program and our revolving note purchase agreements with Farmer Mac. Following is a discussion of our borrowing capacity and key terms and conditions under each of these facilities.

Committed Bank Revolving Line of Credit Agreements—Unsecured

Our committed bank revolving lines of credit may be used for general corporate purposes; however, we generally rely on them as a backup source of liquidity for our member and dealer commercial paper. We had $3,085 million of commitments under committed bank revolving line of credit agreements as of February 28, 2018. Under our current committed bank revolving line of credit agreements, we have the ability to request up to $300 million of letters of credit, which would result in a reduction in the remaining available amount under the facilities.

On November 20, 2017, we amended and restated the three-year and five-year committed bank revolving line of credit agreements to extend the maturity dates to November 20, 2020 and November 20, 2022, respectively, and to terminate certain third-party bank commitments totaling $40 million under the three-year agreement and $40 million under the five- year agreement. As a result, the total commitment amount from third-parties under the three-year facility and the five-year facility is $1,493 million and $1,592 million, respectively, resulting in a combined total commitment amount under the two facilities of $3,085 million.

Table 26 presents the total commitment, the net amount available for use and the outstanding letters of credit under our committed bank revolving line of credit agreements as of February 28, 2018. We did not have any outstanding borrowings under our bank revolving line of credit agreements as of February 28, 2018.

Table 26: Committed Bank Revolving Line of Credit Agreements

	February 28, 2018				
(Dollars in millions)	Total Commitment	Letters of Credit Outstanding	Net Available for Advance	Maturity	Annual Facility Fee [1]
3-year agreement	$1,493	$ —	$ 1,493	November 20, 2020	7.5 bps
5-year agreement	1,592	2	1,590	November 20, 2022	10 bps
Total	$3,085	$ 2	$ 3,083		

[1]Facility fee based on CFC's senior unsecured credit ratings in accordance with the established pricing schedules at the inception of the related agreement.

Our committed bank revolving line of credit agreements do not contain a material adverse change clause or rating triggers that would limit the banks' obligations to provide funding under the terms of the agreements; however, we must be in compliance with the covenants to draw on the facilities. We have been and expect to continue to be in compliance with the covenants under our committed bank revolving line of credit agreements. As such, we could draw on these facilities to repay dealer or member commercial paper that cannot be rolled over. See "Debt Covenants and Financial Ratios" below for additional information, including the specific financial ratio requirements under our committed bank revolving line of credit agreements.

Guaranteed Underwriter Program Committed Facilities—Secured

Under the Guaranteed Underwriter Program we can borrow from the Federal Financing Bank and use the proceeds to refinance existing indebtedness. As part of the program, we pay fees, based on outstanding borrowings, that support the USDA Rural Economic Development Loan and Grant program. The borrowings under this program are guaranteed by RUS.

On November 9, 2017, we closed on a $750 million committed loan facility ("Series M") from the Federal Financing Bank under the Guaranteed Underwriter Program. Pursuant to this facility, we may borrow any time before July 15,

2022. Each advance is subject to quarterly amortization and a final maturity not longer than 20 years from the advance date. The closing of this committed loan facility increased the amount available for access under the Guaranteed Underwriter Program to $1,225 million as of February 28, 2018. Of this amount, $100 million is available for advance through January 15, 2019, $375 million is available for advance through October 15, 2019 and $750 million is available through July 15, 2022.

We are required to pledge eligible distribution system or power supply system loans as collateral in an amount at least equal to the total outstanding borrowings under the Guaranteed Underwriter Program. See “Consolidated Balance Sheet Analysis—Debt—Collateral Pledged” and “Note 4—Loans and Commitments” for additional information on pledged collatera

Farmer Mac Revolving Note Purchase Agreements—Secured

As indicated in Table 25, we have two revolving note purchase agreements with Farmer Mac, which together allow us to borrow up to $5,500 million from Farmer Mac. On February 26, 2018, we amended our first revolving note purchase agreement with Farmer Mac, dated March 24, 2011. Under the amended agreement we can borrow, subject to market conditions, up to $5,200 million at any time through January 11, 2022, and such date shall automatically extend on each anniversary date of the closing for an additional year, unless prior to any such anniversary date, Farmer Mac provides us with a notice that the draw period will not be extended beyond the remaining term. This revolving note purchase agreement allows us to borrow, repay and re-borrow funds at any time through maturity, as market conditions permit, provided that the outstanding principal amount at any time does not exceed the total available under the agreement. Each borrowing under the note purchase agreement is evidenced by a pricing agreement setting forth the interest rate, maturity date and other related terms as we may negotiate with Farmer Mac at the time of each such borrowing. We may select a fixed rate or variable rate at the time of each advance with a maturity as determined in the applicable pricing agreement. We had outstanding secured notes payable totaling $2,805 million and $2,513 million as of February 28, 2018 and May 31, 2017, respectively, under the Farmer Mac revolving note purchase agreement of $5,200 million. The available borrowing amount totaled $2,395 million as of February 28, 2018.

Under the terms of the second revolving note purchase agreement with Farmer Mac dated July 31, 2015, we can borrow up to $300 million at any time through July 31, 2018 at a fixed spread over LIBOR. This agreement also allows us to borrow, repay and re-borrow funds at any time through maturity, provided that the outstanding principal amount at any time does not exceed the total available under the agreement. We had no outstanding notes payable under this agreement as of
February 28, 2018 and May 31, 2017.

Pursuant to both Farmer Mac revolving note purchase agreements, we are required to pledge eligible distribution system or power supply system loans as collateral in an amount at least equal to the total principal amount of notes outstanding. See “Consolidated Balance Sheet Analysis—Debt—Collateral Pledged” and “Note 4—Loans and Commitments” additional information on pledged collateral.

Short-Term Borrowings

We rely on short-term borrowings, which we refer to as our short-term funding portfolio, as a source to meet our daily, near-term funding needs. Our short-term funding portfolio consists of commercial paper, which we offer to members and dealers, select notes and daily liquidity fund notes offered to members, and bank-bid notes and medium-term notes offered to members and dealers. Table 27 displays the composition of our short-term borrowings as of February 28, 2018 and
May 31, 2017.

Table 27: Short-Term Borrowings

(Dollars in thousands)	February 28, 2018 Amount Outstanding	% of Total Debt Outstanding		May 31, 2017 Amount Outstanding	% of Total Debt Outstanding	
Short-term borrowings:						
Commercial paper:						
Commercial paper to dealers, net of discounts	$1,055,147	4	%	$999,691	4	%
Commercial paper to members, at par	1,021,016	4		928,158	4	
Total commercial paper	2,076,163	8		1,927,849	8	
Select notes to members	674,319	3		696,889	3	
Daily liquidity fund notes to members	506,921	2		527,990	2	
Medium-term notes to members	236,333	1		190,172	1	
Total short-term borrowings	$3,493,736	14	%	$3,342,900	14	%

	February 28, 2018 Amount Outstanding	% of Total Short-Term Borrowings		May 31, 2017 Amount Outstanding	% of Total Short-Term Borrowings	
Funding source:						
Members	$2,438,589	70	%	$2,343,209	70	%
Capital markets	1,055,147	30		999,691	30	
Total short-term borrowings	$3,493,736	100	%	$3,342,900	100	%

Our short-term borrowings totaled $3,494 million and accounted for 14% of total debt outstanding as of February 28, 2018, compared with $3,343 million, or 14%, of total debt outstanding as of May 31, 2017. Member borrowings accounted for 70% of our total short-term borrowings as of both February 28, 2018 and May 31, 2017. Of the total outstanding commercial paper, $1,055 million and $1,000 million was issued to dealers as of February 28, 2018 and May 31, 2017, respectively. Our intent is to manage our short-term wholesale funding risk by maintaining outstanding dealer commercial paper at an amount below $1,250 million for the foreseeable future.

Long-Term and Subordinated Debt

Long-term and subordinated debt represents the most significant component of our funding. The issuance of long-term debt allows us to reduce our reliance on short-term borrowings and manage our refinancing and interest rate risk, due in part to the multi-year contractual maturity structure of long-term debt. In addition to access to private debt facilities, we also issue debt in the public capital markets. Under the SEC rules, we are classified as a "well-known seasoned issuer." In November 2017, we filed a new shelf registration statement for our senior and subordinated debt securities under which we can register an unlimited amount of senior and subordinated debt securities, including medium-term notes, member capital securities and subordinated deferrable debt, until November 2020. Notwithstanding the foregoing, we have contractual limitations with respect to the amount of senior indebtedness we may incur. See "MD&A—Liquidity Risk" of our 2017 Form 10-K for additional information on our shelf registration statements with the SEC.

As discussed in "Consolidated Balance Sheet Analysis—Debt," long-term and subordinated debt totaled $20,935 million and accounted for 86% of total debt outstanding as of February 28, 2018, compared with $20,117 million, or 86%, of total debt outstanding as of May 31, 2017. The increase in total debt outstanding, including long-term and subordinated debt, was primarily due to the issuance of debt to fund loan portfolio growth. Table 28 summarizes long-term and subordinated debt issuances and repayments during the nine months ended February 28, 2018.

Table 28: Issuances and Repayments of Long-Term and Subordinated Debt[1]

	Nine Months Ended February 28, 2018		
(Dollars in thousands)	Issuances	Repayments[1]	Increase/Decrease
Long-term and subordinated debt activity:[2]			
Collateral trust bonds	$700,000	$ 705,000	$ (5,000)
Guaranteed Underwriter Program notes payable	250,000	363,978	(113,978)
Farmer Mac notes payable	325,000	33,013	291,987
Medium-term notes sold to members	183,169	194,575	(11,406)
Medium-term notes sold to dealers	706,166	11,343	694,823
Other notes payable	—	3,565	(3,565)
Members' subordinated certificates	4,802	44,134	(39,332)
Total	$2,169,137	$ 1,355,608	$ 813,529

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[1]Repayments include principal maturities, scheduled amortizations payments, repurchases and redemptions,.
[2]Amounts exclude unamortized debt issuance costs and discounts.

Table 29 summarizes the scheduled amortization of the principal amount of long-term debt, subordinated deferrable debt and members' subordinated certificates as of February 28, 2018.

Table 29: Principal Maturity of Long-Term and Subordinated Debt

(Dollars in thousands)	Amount Maturing [1]	% of Total
Fiscal year ending:		
May 31, 2018	$289,956	1 %
May 31, 2019	2,717,712	13
May 31, 2020	1,469,165	7
May 31, 2021	1,640,398	8
May 31, 2022	1,590,796	8
Thereafter	13,226,651	63
Total	$20,934,678	100%

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[1]Excludes $0.5 million in subscribed and unissued member subordinated certificates for which a payment has been received. Member loan subordinated certificates totaling $274 million amortize annually based on the unpaid principal balance of the related loan.

We provide additional information on our financing activities above under "Consolidated Balance Sheet Analysis—Debt."

Investment Portfolio

In addition to our primary sources of liquidity discussed above, we have an investment portfolio, composed of time deposits, available-for-sale investment securities and held-to-maturity investment securities, which totaled $339 million and $319 million as of February 28, 2018 and May 31, 2017, respectively. We intend for our investment portfolio to remain adequately liquid to serve as a contingent supplemental source of liquidity for unanticipated liquidity needs.

During the second quarter of fiscal year 2018, we commenced the purchase of additional investment securities, consisting primarily of certificates of deposit, commercial paper, corporate debt securities, commercial mortgage-backed securities, and other asset-backed securities. Pursuant to our investment policy guidelines, all fixed-income securities, at the time of purchase, must be rated at least investment grade and on stable outlook based on external credit ratings from at least two of the leading global credit rating agencies, when available, or the corresponding equivalent, when not available. Securities rated investment grade, that is those rated Baa3 or higher by Moody’s or BBB- or higher by S&P, are generally considered by the rating agencies to be of lower credit risk than non-investment grade securities. We have the positive intent and ability to hold these securities to maturity. As such, we have classified them as held to maturity on our condensed consolidated balance sheet.

Our investment portfolio is unencumbered and structured so that securities have active secondary or resale markets under normal market conditions. The objective of the portfolio is to achieve returns commensurate with the level of risk assumed subject to CFC's investment policy guidelines and liquidity requirements.

We provide additional information on available-for-sale and held-to-maturity investment securities held in our our investment portfolio in "Note 3—Investment Securities."

Projected Near-Term Sources and Uses of Liquidity

As discussed above, our primary sources of liquidity include cash flows from operations, our short-term funding portfolio, our liquidity reserve and the issuance of long-term and subordinated debt, as well as loan principal and interest payments. Our primary uses of liquidity include loan advances to members, principal and interest payments on borrowings, periodic settlement payments related to derivative contracts, costs related to the disposition of foreclosed assets and operating expenses.

Table 30 below displays our projected sources and uses of cash, by quarter, over the next six quarters through the quarter ending August 31, 2019. Our projected liquidity position reflects our current plan to expand our investment portfolio. Our assumptions also include the following: (i) the estimated issuance of long-term debt, including collateral trust bonds and private placement of term debt, is based on maintaining a matched funding position within our loan portfolio with our bank revolving lines of credit serving as a backup liquidity facility for commercial paper and on maintaining outstanding dealer commercial paper at an amount below $1,250 million; (ii) long-term loan scheduled amortization payments represent the scheduled long-term loan payments for loans outstanding as of February 28, 2018, and our current estimate of long-term loan prepayments, which the amount and timing of are subject to change; (iii) other loan repayments and other loan advances primarily relate to line of credit repayments and advances; (iv) long-term debt maturities reflect scheduled maturities of outstanding term debt for the periods presented; and (v) long-term loan advances reflect our current estimate of member demand for loans, the amount and timing of which are subject to change.

Table 30: Projected Sources and Uses of Liquidity[(1)]

(Dollars in millions)	Projected Sources of Liquidity				Projected Uses of Liquidity				
	Long-Term Debt Issuance	Anticipated Long-Term Loan Repayments[(2)]	Other Loan Repayments[(3)]	Total Projected Sources of Liquidity	Long-Term Debt Maturities	Long-Term Loan Advances[(4)]	Other Loan Advances[(5)]	Total Projected Uses of Liquidity	Other Sources/ (Uses) of Liquidity[(6)]
4Q FY 2018	$365	$ 300	$ 220	$ 885	$336	$ 405	$ —	$ 741	$ (244)
1Q FY 2019	150	316	52	518	166	480	—	646	135
2Q FY 2019	1,875	327	—	2,202	1,601	528	13	2,142	(66)
3Q FY 2019	1,175	306	—	1,481	760	549	—	1,309	(172)
4Q FY 2019	510	282	—	792	407	354	—	761	(32)
1Q FY 2020	295	309	—	604	167	405	—	572	(30)
Total	$4,370	$ 1,840	$ 272	$ 6,482	$3,437	$ 2,721	$ 13	$ 6,171	$ (409)

(1) The dates presented represent the end of each quarterly period through the quarter ending August 31, 2019.

(2) Anticipated long-term loan repayments include scheduled long-term loan amortizations, anticipated cash repayments at repricing date and sales.
(3) Other loan repayments include anticipated short-term loan repayments.
(4) Long-term debt maturities also includes medium-term notes with an original maturity of one year or less and expected early redemptions of debt.
(5) Other loan advances include anticipated short-term loan advances.
(6) Includes net increase or decrease to dealer commercial paper, and purchases and maturity of investments.

As displayed in Table 30, we currently project long-term advances of $1,962 million over the next 12 months, which we anticipate will exceed anticipated loan repayments over the same period of $1,249 million by approximately $713 million. The estimates presented above are developed at a particular point in time based on our expected future business growth and funding. Our actual results and future estimates may vary, perhaps significantly, from the current projections, as a result of changes in market conditions, management actions or other factors.

Credit Ratings

Our funding and liquidity, borrowing capacity, ability to access capital markets and other sources of funds and the cost of these funds are partially dependent on our credit ratings. Rating agencies base their ratings on numerous factors, including liquidity, capital adequacy, industry position, member support, management, asset quality, quality of earnings and the probability of systemic support. Significant changes in these factors could result in different ratings. Table 31 displays our credit ratings as of February 28, 2018, which were unchanged as of the date of the filing of this Report.

Table 31: Credit Ratings

	February 28, 2018		
	Moody's	S&P	Fitch
Long-term issuer credit rating[(1)]	A2	A	A
Senior secured debt[(2)]	A1	A	A+
Senior unsecured debt[(3)]	A2	A	A
Subordinated debt	A3	BBB+	BBB+
Commercial paper	P-1	A-1	F1
Outlook	Stable	Stable	Stable

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[(1)] Based on our senior unsecured debt rating.
[(2)]Applies to our collateral trust bonds.
[(3)]Applies to our medium-term notes.

During the second quarter of fiscal year 2018, Moody's and S&P affirmed our ratings and outlook. In order to access the commercial paper markets at attractive rates, we believe we need to maintain our current commercial paper credit ratings of P-1 by Moody's, A-1 by S&P and F1 by Fitch. In addition, the notes payable to the Federal Financing Bank and guaranteed by RUS under the Guaranteed Underwriter Program contain a provision that if during any portion of the fiscal year, our senior secured credit ratings do not have at least two of the following ratings: (i) A3 or higher from Moody's, (ii) A- or higher from S&P, (iii) A- or higher from Fitch or (iv) an equivalent rating from a successor rating agency to any of the above rating agencies, we may not make cash patronage capital distributions in excess of 5% of total patronage capital. See "Credit Risk—Counterparty Credit Risk—Credit Risk-Related Contingent Features" above for information on credit rating provisions related to our derivative contracts.

Financial Ratios

Our debt-to-equity ratio decreased to 17.15-to-1 as of February 28, 2018, from 21.94-to-1 as of May 31, 2017, primarily due to an increase in equity resulting from our reported net income of $409 million for the nine months ended February 28, 2018, which was partially offset by patronage capital retirement of $45 million in September 2017.

Our adjusted debt-to-equity ratio increased to 6.21-to-1 as of February 28, 2018, from 5.95-to-1 as of May 31, 2017, largely due to an increase in debt outstanding to fund loan growth. We provide a reconciliation of our adjusted debt-to-equity ratio to the most comparable GAAP measure and an explanation of the adjustments below in "Non-GAAP Financial Measures."

Debt Covenants

As part of our short-term and long-term borrowing arrangements, we are subject to various financial and operational covenants. If we fail to maintain specified financial ratios, such failure could constitute a default by CFC of certain debt covenants under our committed bank revolving line of credit agreements and senior debt indentures. We were in compliance with all covenants and conditions under our committed bank revolving line of credit agreements and senior debt indentures as of February 28, 2018.

As discussed above in "Summary of Selected Financial Data," the financial covenants set forth in our committed bank revolving line of credit agreements and senior debt indentures are based on adjusted financial measures, including adjusted TIER. We provide a reconciliation of adjusted TIER and other non-GAAP measures disclosed in this Report to the most comparable GAAP measures and an explanation of the adjustments below in "Non-GAAP Financial Measures."

MARKET RISK

Interest rate risk represents our primary market risk. Interest rate risk is the risk arising from movements in interest rates that may result in differences between the timing of contractual maturities, re-pricing characteristics and prepayments on our assets and their related liabilities.

Interest Rate Risk Management

Our interest rate risk exposure is primarily related to the funding of the fixed-rate loan portfolio. Our Asset Liability Committee provides oversight over maintaining our interest rate position within a prescribed policy range using approved strategies. The Asset Liability Committee reviews a complete interest rate risk analysis, reviews proposed modifications, if any, to our interest rate risk management strategy and considers adopting strategy changes. Our Asset Liability Committee monitors interest rate risk and meets quarterly to review and discuss information such as national economic forecasts, federal funds and interest rate forecasts, interest rate gap analysis, our liquidity position, loan and debt maturities, short-term and long-term funding needs, anticipated loan demands, credit concentration risk, derivative counterparty exposure and financial forecasts. The Asset Liability Committee also discusses the composition of fixed-rate versus variable-rate lending, new funding opportunities, changes to the nature and mix of assets and liabilities for structural mismatches, and interest rate swap transactions.

Matched Funding Objective

Our funding objective is to manage the matched funding of asset and liability repricing terms within a range of adjusted total assets (calculated by excluding derivative assets from total assets) deemed appropriate by the Asset Liability Committee based on the current environment and extended outlook for interest rates. We refer to the difference between fixed-rate loans scheduled for amortization or repricing and the fixed-rate liabilities and equity funding those loans as our interest rate gap. Our primary strategies for managing our interest rate risk include the use of derivatives and limiting the amount of fixed-rate assets that can be funded by variable-rate debt to a specified percentage of adjusted total assets based on market conditions.

We provide our members with many options on loans with regard to interest rates, the term for which the selected interest rate is in effect and the ability to convert or prepay the loan. Long-term loans generally have maturities of up to 35 years. Borrowers may select fixed interest rates for periods of one year through the life of the loan. We do not match fund the majority of our fixed-rate loans with a specific debt issuance at the time the loans are advanced. We fund the amount of fixed-rate assets that exceed fixed-rate debt and members' equity with short-term debt, primarily commercial paper.

Interest Rate Gap Analysis

To monitor and mitigate interest rate risk in the funding of fixed-rate loans, we perform a monthly interest rate gap analysis that provides a comparison between fixed-rate assets repricing or maturing by year and fixed-rate liabilities and members' equity maturing by year.

We maintain an unmatched position on our fixed-rate assets within a targeted range of adjusted total assets. The limited unmatched position is intended to provide flexibility to ensure that we are able to match the current maturing portion of long-term fixed rate loans based on maturity date and the opportunity in the current low interest rate environment to increase the gross yield on our fixed rate assets without taking what we would consider to be excessive risk.

Table 32 displays the scheduled amortization and repricing of fixed-rate assets and liabilities outstanding as of February 28, 2018. We exclude variable-rate loans from our interest rate gap analysis as we do not consider the interest rate risk on these loans to be significant because they are subject to repricing at least monthly. Loans with variable interest rates accounted for 10% and 9% of our total loan portfolio as of February 28, 2018 and May 31, 2017, respectively. Fixed-rate liabilities include debt issued at a fixed rate as well as variable-rate debt swapped to a fixed rate using interest rate swaps. Fixed-rate debt swapped to a variable rate using interest rate swaps is excluded from the analysis since it is used to match fund the variable-rate loan pool. With the exception of members' subordinated certificates, which are generally issued with extended maturities, and commercial paper, our liabilities have average maturities that closely match the repricing terms (but not the maturities) of our fixed-rate loans.

Table 32: Interest Rate Gap Analysis

(Dollars in millions)	Prior to 5/31/18	Two Years 6/1/18 to 5/31/20	Two Years 6/1/20 to 5/31/22	Five Years 6/1/22 to 5/31/27	10 Years 6/1/27 to 5/31/37	6/1/37 and Thereafter	Total
Asset amortization and repricing	$442	$3,543	$3,002	$5,758	$6,905	$3,305	$22,955
Liabilities and members' equity:							
Long-term debt [1]	$212	$3,830	$2,575	$5,401	$5,543	$1,622	$19,183
Subordinated certificates	5	53	48	974	156	579	1,815
Members' equity[2]	—	23	24	105	293	906	1,351
Total liabilities and members' equity[3]	$217	$3,906	$2,647	$6,480	$5,992	$3,107	$22,349
Gap [4]	$225	$(363)	$355	$(722)	$913	$198	$606
Cumulative gap	225	(138)	217	(505)	408	606	
Cumulative gap as a % of total assets	0.85 %	(0.52)%	0.82 %	(1.91)%	1.54 %	2.29 %	
Cumulative gap as a % of adjusted total assets[5]	0.86	(0.53)	0.83	(1.93)	1.56	2.31	

[1] Includes long-term fixed-rate debt and net fixed-rate swaps.
[2] Includes the portion of the allowance for loan losses and subordinated deferrable debt allocated to fund fixed-rate assets and excludes noncash adjustments from the accounting for derivative financial instruments.
[3] Debt is presented based on call date.
[4] Calculated based on the amount of assets amortizing and repricing less total liabilities and members' equity.
[5] Adjusted total assets represents total assets reported in our condensed consolidated balance sheets less derivative assets.

The difference, or interest rate gap, of $606 million between the fixed-rate loans scheduled for amortization or repricing of $22,955 million and the fixed-rate liabilities and equity funding the loans of $22,349 million presented in Table 32 reflects the amount of fixed-rate assets that are funded with short-term and variable-rate debt as of February 28, 2018. The gap of $606 million represented 2.29% of total assets and 2.31% of adjusted total assets (total assets excluding derivative assets) as of February 28, 2018. As discussed above, we manage this gap within a prescribed range because funding long-term, fixed-rate loans with short-term and variable-rate debt may expose us to higher interest rate and liquidity risk.

NON-GAAP FINANCIAL MEASURES

In addition to financial measures determined in accordance with GAAP, management evaluates performance based on certain non-GAAP measures, which we refer to as "adjusted" measures. We provide a discussion of each of these non-GAAP measures in our 2017 Form 10-K under "Item 7. MD&A—Non-GAAP Measures." Below we provide a reconciliation of our adjusted measures to the most comparable GAAP measures in this section. We believe our non-GAAP adjusted metrics, which are not a substitute for GAAP and may not be consistent with similarly titled non-GAAP measures used by other companies, provide meaningful information and are useful to investors because management uses these metrics to compare operating results across financial reporting periods, for internal budgeting and forecasting purposes, for compensation decisions and for short- and long-term strategic planning decisions. In addition, certain of the financial covenants in our committed bank revolving line of credit agreements and debt indentures are based on our adjusted measures.

Statements of Operations Non-GAAP Adjustments

Table 33 provides a reconciliation of adjusted interest expense, adjusted net interest income and adjusted net income to the comparable GAAP measures three and nine months ended February 28, 2018 and 2017. The adjusted amounts are used in the calculation of our adjusted net interest yield and adjusted TIER.

Table 33: Adjusted Financial Measures — Income Statement

	Three Months Ended February 28,		Nine Months Ended February 28,	
(Dollars in thousands)	2018	2017	2018	2017
Interest expense	$(198,071)	$(186,740)	$(585,972)	$(551,474)
Include: Derivative cash settlements	(18,924)	(19,354)	(58,781)	(64,331)
Adjusted interest expense	$(216,995)	$(206,094)	$(644,753)	$(615,805)
Net interest income	$73,397	$73,180	$217,234	$222,437
Include: Derivative cash settlements	(18,924)	(19,354)	(58,781)	(64,331)
Adjusted net interest income	$54,473	$53,826	$158,453	$158,106
Net income	$221,029	$97,962	$408,767	$361,005
Exclude: Derivative forward value gains	186,972	61,809	306,224	259,153
Adjusted net income	$34,057	$36,153	$102,543	$101,852

We consider the cost of derivatives to be an inherent cost of funding and hedging our loan portfolio and, therefore, economically similar to the interest expense that we recognize on debt issued for funding. We therefore include derivative cash settlements in our adjusted interest expense and exclude the unrealized forward value of derivatives from our adjusted net income.

TIER and Adjusted TIER

Table 34 presents our TIER and adjusted TIER for the three and nine months ended February 28, 2018 and 2017.

Table 34: TIER and Adjusted TIER

	Three Months Ended February 28,		Nine Months Ended February 28,	
	2018	2017	2018	2017
TIER [(1)]	2.12	1.52	1.70	1.65
Adjusted TIER [(2)]	1.16	1.18	1.16	1.17

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(1) TIER is calculated based on net income plus interest expense for the period divided by interest expense for the period.

(2) Adjusted TIER is calculated based on adjusted net income plus adjusted interest expense for the period divided by adjusted interest expense for the period.

Debt-to-Equity and Adjusted Debt-to-Equity

Table 35 provides a reconciliation between the liabilities and equity used to calculate the debt-to-equity and the adjusted debt-to-equity ratios as of February 28, 2018 and May 31, 2017. As indicated in the table below, subordinated debt is treated in the same manner as equity in calculating our adjusted-debt-to-equity ratio.

Table 35: Adjusted Financial Measures — Balance Sheet

(Dollars in thousands)	February 28, 2018	May 31, 2017
Total liabilities	$25,017,303	$24,106,887
Exclude:		
Derivative liabilities	282,892	385,337
Debt used to fund loans guaranteed by RUS	162,531	167,395
Subordinated deferrable debt	742,375	742,274
Subordinated certificates	1,379,693	1,419,025
Adjusted total liabilities	$22,449,812	$21,392,856
Total equity	$1,459,104	$1,098,805
Include:		
Subordinated deferrable debt	742,375	742,274
Subordinated certificates	1,379,693	1,419,025
Total subordinated debt and certificates	2,122,068	2,161,299
Exclude:		
Prior year-end cumulative derivative forward value losses	(340,976)	(520,357)
Current year derivative forward value gains	306,224	179,381
Total cumulative derivative forward value losses	(34,752)	(340,976)
Accumulated other comprehensive income (1)	3,159	3,702
Adjusted total equity	$3,612,765	$3,597,378

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(1) Represents the AOCI related to derivatives. See “Note 9—Equity” for a breakout of our AOCI components.

Table 36 displays the calculations of our debt-to-equity and adjusted debt-to-equity ratios as of February 28, 2018 and May 31, 2017.

Table 36: Debt-to-Equity Ratio

	February 28, 2018	May 31, 2017
Debt-to-equity ratio (1)	17.15	21.94
Adjusted debt-to-equity ratio (2)	6.21	5.95

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(1) Calculated based on total liabilities as of the end of the period divided by total equity as of the end of the period.
(2) Calculated based on adjusted total liabilities at period end divided by adjusted total equity at period end.

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Item 1. Financial Statements

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended February 28,		Nine Months Ended February 28,	
(Dollars in thousands)	2018	2017	2018	2017
Interest income	$271,468	$259,920	$803,206	$773,911
Interest expense	(198,071)	(186,740)	(585,972)	(551,474)
Net interest income	73,397	73,180	217,234	222,437
Provision for loan losses	(1,105)	(2,065)	(503)	(4,731)
Net interest income after provision for loan losses	72,292	71,115	216,731	217,706
Non-interest income:				
Fee and other income	3,935	5,810	13,422	15,437
Derivative gains	168,048	42,455	247,443	194,822
Results of operations of foreclosed assets	—	(29)	(34)	(1,690)
Total non-interest income	171,983	48,236	260,831	208,569
Non-interest expense:				
Salaries and employee benefits	(13,011)	(11,537)	(36,843)	(34,412)
Other general and administrative expenses	(9,201)	(9,173)	(28,919)	(27,789)
Gains on early extinguishment of debt	—	192	—	192
Other non-interest expense	(402)	(486)	(1,542)	(1,446)
Total non-interest expense	(22,614)	(21,004)	(67,304)	(63,455)
Income before income taxes	221,661	98,347	410,258	362,820
Income tax expense	(632)	(385)	(1,491)	(1,815)
Net income	221,029	97,962	408,767	361,005
Less: Net income attributable to noncontrolling interests	(1,614)	(404)	(2,646)	(2,289)
Net income attributable to CFC	$219,415	$97,558	$406,121	$358,716

See accompanying notes to condensed consolidated financial statements.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

	Three Months Ended February 28,		Nine Months Ended February 28,	
(Dollars in thousands)	2018	2017	2018	2017
Net income	$221,029	$97,962	$408,767	$361,005
Other comprehensive income (loss):				
Unrealized gains (losses) on available-for-sale investment securities	(1,763)	3,923	(2,906)	2,151
Reclassification of losses on foreclosed assets to net income	—	—	—	9,823
Reclassification of derivative gains to net income	(157)	(195)	(543)	(591)
Defined benefit plan adjustments	128	45	381	133
Other comprehensive income (loss)	(1,792)	3,773	(3,068)	11,516
Total comprehensive income	219,237	101,735	405,699	372,521
Less: Total comprehensive income attributable to noncontrolling interests	(1,614)	(404)	(2,646)	(2,289)
Total comprehensive income attributable to CFC	$217,623	$101,331	$403,053	$370,232

See accompanying notes to condensed consolidated financial statements.

NATIONAL RURAL UTILITIES COOPERATIVE FINANCE CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(Dollars in thousands)	February 28, 2018	May 31, 2017
Assets:		
Cash and cash equivalents	$ 250,697	$ 166,615
Restricted cash	6,951	21,806
Time deposits	1,000	226,000
Investment securities:		
Available for		