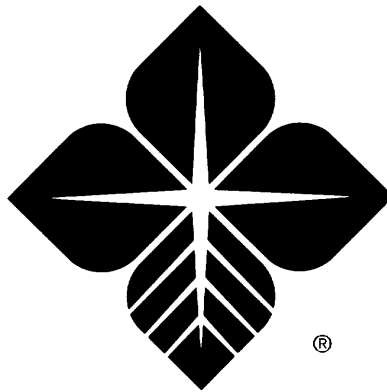


LONE STAR, ACA

2009 Quarterly Report Third Quarter



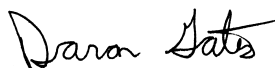
For the Quarter Ended September 30, 2009

REPORT OF MANAGEMENT

To meet its responsibility for reliable financial information, management depends on the Farm Credit Bank of Texas' and the Association's accounting and internal control systems, which have been designed to provide reasonable, but not absolute, assurance that assets are safeguarded and transactions are properly authorized and recorded. The systems have been designed to recognize that the cost of controls must be related to the benefits derived. The consolidated financial statements are audited by PricewaterhouseCoopers LLP, independent accountants, who conduct a review of internal controls solely for the purpose of establishing a basis for reliance thereon in determining the nature, extent and timing of audit tests applied in the audit of the consolidated financial statements in accordance with auditing standards generally accepted in the United States of America. The Association is also examined by the Farm Credit Administration.

The audit committee has oversight responsibility for the Association's systems of internal control and financial reporting. The audit committee consults regularly with management and meets periodically with the independent auditors and the internal auditors to review the scope and results of their work. The independent auditors and the internal auditor have direct access to the audit committee.

The undersigned certify that this annual report has been prepared in accordance with all applicable statutory or regulatory requirements and that the information contained herein is true, accurate and complete to the best of his or her knowledge or belief.



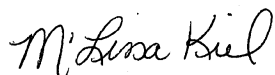
Daron Gates, Chief Executive Officer

Oct 30, 2009



Bruce Duncan, Chairman, Board of Directors

Oct 30, 2009



M'Lissa Kiel, Chief Financial Officer

Oct 30, 2009



Don Crawford, Audit Committee

Oct 30, 2009

LONE STAR, ACA
MANAGEMENT'S DISCUSSION AND ANALYSIS
(all dollars in thousands unless otherwise noted)

The following commentary reviews the financial performance of the Lone Star, ACA (Agricultural Credit Association), referred to as the Association, for the quarter and nine months ended September 30, 2009. These comments should be read in conjunction with the accompanying financial statements and the December 31, 2008, Annual Report of the Association.

The association is a member of the Farm Credit System (System), a nationwide network of cooperatively owned financial institutions established by and subject to the provisions of the Farm Credit Act of 1971, as amended, and the regulations of the Farm Credit Administration (FCA) promulgated thereunder.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The consolidated financial statements were prepared under the oversight of the Association's audit committee.

Loan Portfolio:

Total loans outstanding at September 30, 2009, including nonaccrual loans and sales contracts, were \$1,160,257 compared to \$1,155,381 at December 31, 2008, reflecting an increase of 0.4 percent. Nonaccrual loans as a percentage of total loans outstanding were 1.5 percent at September 30, 2009, compared to 1.0 percent at December 31, 2008.

Association loan volume remained steady through the first three quarters of 2009. The slow down in growth from prior years is attributed to the current market conditions and is reflective of the Farm Credit system as a whole. Agricultural borrowers and lenders are experiencing the negative financial effects of a declining economy. Loss of jobs, limited commercial banking options, high input cost for feed, fertilizer and fuel along with lower margin on sales have added to the stress of Association borrowers. The Association's increase in high risk assets is also reflective of the economy and resulted in an increase in the provision for loan losses as shown on the Consolidated Statement of Income. High risk assets increased for the quarter due to the addition of two large borrowers being transferred to non-accrual. The high risk assets also increased due to the acquisitions of real estate from two large borrowers.

High-risk assets include nonaccrual loans, loans that are past due 90 days or more and still accruing interest, formally restructured loans and other property owned. The following table illustrates the Association's components and trends of high-risk assets.

	September 30, 2009		December 31, 2008	
	Amount	%	Amount	%
Nonaccrual	\$ 16,826	56.6%	\$ 11,042	98.7%
90 days past due and still accruing interest	86	0.3%	50	0.5%
Other property owned, net	12,824	43.1%	92	0.8%
Total	\$ 29,736	100.0%	\$ 11,184	100.0%

For the nine months ended September 30, 2009, high risk assets increased \$18,552 as compared to the period ended December 31, 2008. The increase is primarily due to the addition of \$12,732 in property acquired through foreclosure and an increase of \$5,784 in nonaccrual loans. Additional loan volume was moved to nonaccrual status during the quarter with the majority of the volume being tied to the timber and beef cattle industries. In addition, other property owned increased due to the acquisition of the assets related to one borrower involved in the dairy industry and one beef cattle operation.

The Association management continues to review the loan portfolio in order to identify and report problem loans and address risk exposure by providing allowance reserves as appropriate. These reviews have indicated problems within the dairy and beef cattle industry. Loan servicing continues to be conducted on an individual customer basis as management works with each customer to develop plans designed to return the operation to viability or result in an orderly debt reduction through the liquidation of the collateral. Some of these plans include taking possession of the collateral and marketing the property through channels that will be most beneficial to the Association and our stockholders.

Results of Operations:

The Association had net (loss) income of \$(1,721) and \$9,573 for the three and nine months ended September 30, 2009, as compared to net income of \$6,006 and \$18,286 for the same periods in 2008 reflecting an decrease of 128.7 and 47.7 percent, respectively. Net interest income was \$8,153 and \$24,653 for the three and nine months ended September 30, 2009, as compared to net interest income of \$7,867 and \$22,684 for the same periods in 2008. Interest income for the first nine months of 2009 decreased by \$4,602 or 8.6 percent from the same periods of 2008, primarily due to a decrease in overall interest rates. Interest expense for the first nine months of 2009 decreased by \$6,571, or 21.3 percent, from the same periods of 2008 due to a decrease in average cost of debt. Average loan volume for the third quarter of 2009 was \$1,172,259, compared to \$1,115,099 in the third quarter of 2008. The average spread on the loan portfolio for the third quarter 2009 was 2.40 percent, compared to 2.35 percent in the third quarter of 2008.

The Association had noninterest income of \$1,086 and \$3,945 for the three and nine month ended September 30, 2009, as compared to noninterest income of \$1,490 and \$4,587 for the same periods in 2008. The decrease in noninterest income is largely attributable to a decrease in loan fees and a decrease in gain on other property owned for the three and nine months ended September 30, 2009, as compared to the same period in 2008.

The Association's decrease in net income is mostly attributable to an increase in provisions for loan losses. The Association recorded provisions for loan losses of \$7,542 and \$8,980 for the three and nine months ended September 30, 2009, as compared to provisions of loan losses of \$578 and \$617 for the same periods in 2008. The association transferred three loans to non-accrual and recognized a charge off of approximately six million for these loans to the same borrower in which the borrower had been providing falsified information and appears to have been involved in fraudulent activity. The Association is currently working with the FBI and local authorities in relation to these loans and the outcome of recovering additional funds is not known at this time. Loans tied to the beef cattle industry and dairy industry also required additional provision for loan losses during the 3rd quarter 2009. Additionally, the decrease in net income can be attributed to an increase in noninterest expense. The Association had noninterest expense of \$3,148 and \$9,758 for the three and nine month ended September 30, 2009, as compared to noninterest expense of \$2,773 and \$8,368 for the three and nine months ended September 30, 2008. Most of the increase in noninterest expense is attributable to an increase in salaries and employee benefits and insurance fund premiums. Salaries and employee benefits increased \$261 for the three months ended September 30, 2009, as compared to the three months ended September 30, 2008. For the nine months ended September 30, 2009, salaries and employee benefits increased \$957, as compared to the nine months ended September 30, 2008. Insurance fund premiums increased \$143 for the three months ended September 30, 2009, as compared to the three months ended September 30, 2008. For the nine months ended September 30, 2009, insurance fund premiums increased \$335 as compared to the nine months ended September 30, 2008. This increase can be attributed to loan volume growth and an increase in insurance premium rates.

The Association recorded \$26 in recoveries and \$8,147 in charge-offs for the quarter ended September 30, 2009, and \$3 in recoveries and \$492 in charge-offs for the same period in 2008. The Association's allowance for loan losses was 0.2 percent and 0.1 percent of total loans outstanding as of September 30, 2009, and December 31, 2008, respectively. See Note 2 Allowance for Loan Losses for additional information.

The Association's return on average assets for the nine months ended September 30, 2009, was 1.05 and 2.17 percent for the same period in 2008. The Association's return on average equity for the nine months ended September 30, 2009, was 7.57 and 16.17 percent for the same period in 2008.

Liquidity and Funding Sources:

The Association secures the majority of its lendable funds through a direct loan from the Farm Credit Bank of Texas (The Bank), which obtains its funds through the issuance of Systemwide obligations and with lendable equity. The interest rate risk inherent in the Association's loan portfolio is substantially mitigated through the funding and relationship with the Bank. The Bank manages interest rate risk through its direct loan pricing and asset/liability management process. The following schedule summarizes the Association's borrowings.

	September 30, 2009	December 31, 2008
Note payable to the Bank	\$ 1,035,426	\$ 1,016,383
Accrued interest on note payable	2,559	3,176
Total	<u>\$ 1,037,985</u>	<u>\$ 1,019,559</u>

The increase of \$18,426 for the nine months ended September 30, 2009, is attributable to the increase in the Association's loan volume. The note carried a weighted average interest rate of 2.94 percent as of September 30, 2009, compared to 3.63 percent as of

December 31, 2008. The indebtedness is collateralized by a pledge of substantially all of the Association's assets to the Bank and is governed by a financing agreement.

The liquidity policy of the Associations is to manage cash balances to maximize debt reduction, and to increase accrual loan volume. This policy will continue to be pursued during 2009. As borrower payments are received they are applied to the Association's note payable with the Bank.

The Association will continue to fund its operations through direct borrowings from the Bank, capital surplus from prior years, and borrowers stock. It is management's opinion that funds available to the Association are sufficient to fund its operations for the current year.

Capital Resources:

The Association's capital position increased by \$9,526 as of September 30, 2009, compared to December 31, 2008. The Association's debt as a percentage of members' equity was 6.14:1 as of September 30, 2009, compared to 6.43:1 as of December 31, 2008.

Under regulations governing minimum permanent capital adequacy and other capitalization issues, the Association is required to maintain a minimum adjusted permanent capital of 7 percent of risk-adjusted assets as defined by the FCA. The Association's permanent capital ratio at September 30, 2009, was 13.5 percent, which is in compliance with the FCA's minimum permanent capital standard and meets the Association's goal of exceeding 12 percent. The Association's core surplus ratio and total surplus ratio at September 30, 2009, were 13.1 and 13.1 percent, respectively, which is in compliance with the FCA's minimum surplus standard and exceeds the Association goals of, equal to or greater than 5 percent and 10 percent, respectively. See Note 3 Capital for additional information.

Relationship with the Farm Credit Bank of Texas:

The Association's financial condition may be impacted by factors that affect the Bank. The financial condition and results of operations of the Bank may materially affect the stockholder's investment in the Association. The Management's Discussion and Analysis and Notes to Financial Statements contained in the December 31, 2008, Annual Report of Lone Star, ACA more fully describe the Association's relationship with the Bank.

The Tenth Farm Credit District's (District) annual and quarterly stockholder reports are available free of charge, upon request. These reports can be obtained by writing to Farm Credit Bank of Texas, The Ag Agency, P.O. Box 202590, Austin, Texas 78720, or by calling (512) 483-9260. Copies of the District's quarterly and annual stockholder reports also can be requested by e-mail at fcb@farmcreditbank.com. The District makes its annual and quarterly stockholder reports available on its web site at www.farmcreditbank.com.

The Association's quarterly stockholder reports are also available free of charge, upon request. These reports can be obtained by writing to Lone Star ACA, 1612 Summit Ave Suite 300, Fort Worth, TX 76102 or calling (817)332-6565. Copies of the Association's quarterly stockholder reports can also be requested by e-mailing Kimberly.Thomas@LoneStarAgCredit.com.

LONE STAR, ACA

CONSOLIDATED BALANCE SHEET

(dollars in thousands)

(unaudited)

	September 30, 2009	December 31, 2008
<u>ASSETS</u>		
Cash	\$ 39	\$ 380
Loans	1,160,257	1,155,381
Less: allowance for loan losses	(1,776)	(917)
Net loans	1,158,481	1,154,464
Accrued interest receivable	14,821	12,491
Investment in and receivable from the Bank:		
Capital stock	19,400	19,400
Other	4,558	1,927
Other property owned, net	12,824	92
Premises and equipment	1,732	1,684
Other assets	603	266
Total assets	\$ 1,212,458	\$ 1,190,704
<u>LIABILITIES</u>		
Note payable to the Bank	\$ 1,035,426	\$ 1,016,383
Advance conditional payments	24	220
Accrued interest payable	2,559	3,173
Drafts outstanding	164	197
Dividends Payable	5	5,430
Other liabilities	4,577	5,125
Total liabilities	1,042,755	1,030,528
<u>MEMBERS' EQUITY</u>		
Capital stock and participation certificates	4,780	4,752
Unallocated retained earnings	164,810	155,237
Accumulated other comprehensive income (loss)	113	187
Total members' equity	169,703	160,176
Total liabilities and members' equity	\$ 1,212,458	\$ 1,190,704

LONE STAR, ACA

CONSOLIDATED STATEMENT OF INCOME

(dollars in thousands)

(unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2009	2008	2009	2008
<u>INTEREST INCOME</u>				
Loans	\$ 16,058	\$ 17,790	\$ 48,930	\$ 53,532
Total interest income	16,058	17,790	48,930	53,532
<u>INTEREST EXPENSE</u>				
Note payable to the Bank	7,905	9,923	24,277	30,847
Advance conditional payments	-	-	-	1
Total interest expense	7,905	9,923	24,277	30,848
Net interest income	8,153	7,867	24,653	22,684
<u>PROVISION FOR LOSSES</u>				
Provision for loan losses	7,542	578	8,980	617
Provision for acquired property losses	270	-	287	-
Net interest income after provision for loan losses	341	7,289	15,386	22,067
<u>NONINTEREST INCOME</u>				
Income from the bank:				
Patronage income	534	544	1,616	1,639
Loan fees	406	778	2,055	2,672
Financially related services income	61	30	130	78
Gain on other property owned, net	85	149	67	142
Gain (loss) on sale of premises and equipment, net	-	(11)	17	2
Other noninterest income	-	-	60	54
Total noninterest income	1,086	1,490	3,945	4,587
<u>NONINTEREST EXPENSES</u>				
Salaries and employee benefits	1,617	1,356	4,967	4,010
Directors' expense	22	26	195	200
Purchased services	196	243	658	665
Travel	120	136	332	327
Occupancy and equipment	190	175	540	473
Communications	50	50	142	142
Advertising	94	85	241	288
Public and member relations	104	62	385	280
Supervisory and exam expense	89	82	254	233
Insurance Fund premiums	501	358	1,492	1,157
Other noninterest expense	165	200	552	593
Total noninterest expenses	3,148	2,773	9,758	8,368
Income before income taxes	(1,721)	6,006	9,573	18,286
Net income (loss)	\$ (1,721)	\$ 6,006	\$ 9,573	\$ 18,286

LONE STAR, ACA

CONSOLIDATED STATEMENT OF CHANGES IN MEMBERS' EQUITY

(dollars in thousands)
(unaudited)

	Capital Stock/ Participation Certificates	Retained Earnings		Accumulated Other Comprehensive Income (Loss)	Total Members' Equity
		Allocated	Unallocated		
Balance at December 31, 2007	\$ 4,643	\$ -	\$ 136,800	\$ 434	\$ 141,877
Net income	-	-	18,286	-	18,286
Amortization of costs included in periodic retirement benefit costs	-	-	-	(107)	(107)
Capital stock/participation certificates:					
Issued	673	-	-	-	673
Retired	(560)	-	-	-	(560)
Balance at September 30, 2008	\$ 4,756	\$ -	\$ 155,086	\$ 327	\$ 160,169
Net income	-	-	5,581	-	5,581
Amortization of costs included in periodic retirement benefit costs	-	-	-	(140)	(140)
Capital stock/participation certificates:					
Issued	143	-	-	-	143
Retired	(147)	-	-	-	(147)
Patronage distributions declared:					
Cash	-	-	(5,430)	-	(5,430)
Balance at December 31, 2008	\$ 4,752	\$ -	\$ 155,237	\$ 187	\$ 160,176
Net income	-	-	9,573	-	9,573
Amortization of costs included in periodic retirement benefit costs	-	-	-	(74)	(74)
Capital stock/participation certificates:					
Issued	475	-	-	-	475
Retired	(447)	-	-	-	(447)
Patronage distributions declared:					
Cash	-	-	-	-	-
Balance at September 30, 2009	\$ 4,780	\$ -	\$ 164,810	\$ 113	\$ 169,703

LONE STAR, ACA
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1 — ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES:

The Lone Star, ACA (Agricultural Credit Association), referred to as the Association, is a member-owned cooperative that provides credit and credit-related services to or for the benefit of eligible borrowers/stockholders for qualified agricultural purposes. The Association serves the counties of Hood, Johnson, Somervell, Tarrant, Denton, Wise, Dallas, Bowie, Camp, Cass, Morris, Titus, Delta, Lamar, Red River, Cooke, Fannin, Grayson, Eastland, Erath, Palo Pinto, Parker, Shackelford, Stephens, Throckmorton, Young, Borden, Fisher, Kent, Mitchell, Nolan, Scurry and Taylor in the State of Texas. The Association is a lending institution of the Farm Credit System (the System), which was established by Acts of Congress to meet the needs of American agriculture.

Effective January 1, 2009, the Association adopted Financial Accounting Standards Board (FASB) Statement No. 157-2, "Effective Date of FASB Statement No. 157" (FSP 157-2). This FSP delayed the effective date of Statement of Financial Accounting Standard (SFAS) No. 157, "Fair Value Measurements" (SFAS 157) for nonfinancial assets and nonfinancial liabilities. The impact of adoption resulted in additional fair value disclosures but does not have an impact on the Association's financial condition or results of operations.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events," which sets forth general standards of accounting for and disclosures of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Recognized subsequent events should be recognized in the financial statements since the condition existed at the date of the balance sheet. Nonrecognized subsequent events are not recognized in the financial statements since the conditions arose after the balance sheet date but before the financial statements are issued or are available to be issued. This Standard, which includes a required disclosure of the date through which an entity has evaluated subsequent events, is effective for interim or annual periods ended after June 15, 2009. See Note 5 for the date through which subsequent events were evaluated by the Association.

The accompanying consolidated financial statements contain all adjustments necessary for a fair presentation of the interim financial condition and results of operations and conform with generally accepted accounting principles, except for the inclusion of a statement of cash flows. Generally accepted accounting principles require a business enterprise that provides a set of financial statements reporting both financial position and results of operations to also provide a statement of cash flows for each period for which results of operations are provided. In regulations issued by FCA, associations have the option to exclude statements of cash flows in interim financial statements. Therefore, the Association has elected not to include a statement of cash flows in these consolidated financial statements.

The consolidated financial statements comprise the operations of the ACA and its wholly-owned subsidiaries. The preparation of these consolidated financial statements requires the use of management's estimates. The results for the quarter and the nine months ended September 30, 2009, are not necessarily indicative of the results to be expected for the year ended December 31, 2009. Certain amounts in the prior period's financial statements have been reclassified to conform to current financial statement presentation.

NOTE 2 — ALLOWANCE FOR LOAN LOSSES:

The loan portfolio is comprised of long-term real estate mortgages which generally have maturities ranging up to 40 years. Short-term and intermediate-term production and equipment loans have maturities of 10 years or less. Loans are carried at their principal amount outstanding less unearned income. Interest on loans is accrued and credited to interest income based upon the daily principal amount outstanding.

The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but typically includes farmland and income-producing property, such as crops and livestock, as well as receivables. Long-term real estate loans are secured by the first liens on the underlying real property. Federal regulations state that long-term real estate loans are not to exceed 85 percent (or 97 percent if guaranteed by a government agency) of the property's appraised value. However, a decline in a property's market value subsequent to loan origination or advances, or other actions necessary to protect the financial interest of the Association in the collateral, may result in the loan-to-value ratios in excess of the regulatory maximum.

The major commodity concentrations within the Association's loan volume are timber, cattle, dairies, and field crops.

The Association has obtained loan guarantees in the form of standby commitments to purchase qualifying loans from the Federal Agricultural Mortgage Corporation through an arrangement with the Bank. At September 30, 2009 and December 31, 2008, loans totaling \$63,992 and \$70,848, respectively, were guaranteed by the commitments. Fees paid for these guarantees totaled \$198 as of September 30, 2009, and \$302 as of December 31, 2008, and are reflected in "other noninterest expense."

Impaired loans are loans for which it is probable that not all principal and interest will be collected according to the contractual terms. The following table presents information concerning impaired loans:

	September 30, 2009	September 30, 2008
Balance at beginning of quarter	\$ 2,354	\$ 777
Provision for loan losses	7,542	577
Charge-offs	(8,147)	(492)
Recoveries	27	3
Balance at end of quarter	<u>\$ 1,776</u>	<u>\$ 865</u>

The following table presents information concerning impaired loans:

	September 30, 2009	September 30, 2008
Impaired loans with related allowance	\$ 6,719	\$ 175
Impaired loans with no related allowance	10,193	3,879
Total impaired loans	<u>\$ 16,912</u>	<u>\$ 4,054</u>
Allowance on impaired loans	\$ 160	\$ 62
Average impaired loans	\$ 10,346	\$ 3,481
Interest income on impaired loans for the quarter	\$ 2	\$ 25

NOTE 3 — CAPITAL:

The Association's board of directors has established a Capital Adequacy Plan (Plan) that includes the capital targets that are necessary to achieve the institution's capital adequacy goals as well as the minimum permanent capital standards. The Plan monitors projected dividends, equity retirements and other actions that may decrease the Association's permanent capital. In addition to factors that must be considered in meeting the minimum standards, the board of directors also monitors the following factors: capability of management; quality of operating policies, procedures, and internal controls; quality and quantity of earnings; asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan and lease portfolios; sufficiency of liquid funds; needs of an institution's customer base; and any other risk-oriented activities, such as funding and interest rate risk, potential obligations under joint and several liability, contingent and off-balance-sheet liabilities or other conditions warranting additional capital. At least quarterly, management reviews the Association's goals and objectives with the board.

NOTE 4 — EMPLOYEE BENEFIT PLANS:

The following table summarizes the components of net periodic benefit costs for the nine months ended September 30, 2009:

	Other Benefits	
	2009	2008
Service cost	\$ 41	\$ 36
Interest cost	76	69
Amortization of prior service costs	(106)	(107)
Amortizations of net (gain) loss	32	1
Net periodic benefit cost	<u>\$ 43</u>	<u>\$ (1)</u>

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 158 “Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans” (SFAS 158), which required the recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. The balance sheet recognition provisions of SFAS 158 were adopted at December 31, 2007. SFAS 158 also requires that employers measure the benefit obligation and plan assets as of the fiscal year end for fiscal years ended after December 15, 2008. In fiscal 2007 and earlier, we used a September 30 measurement date for pension and other postretirement benefit plans. The Standard provides two approaches for an employer to transition to a fiscal year end measurement date. We have applied the second approach, which allows for the use of the measurements determined for the prior year end.

The Association previously disclosed in its financial statements for the year ended December 31, 2008, that it expected to contribute \$54 to its defined pension plan in 2009. As of September 30, 2009, \$38 of contributions have been made.

NOTE 5 — SUBSEQUENT EVENTS:

The Association has evaluated subsequent events through October 30, 2009, which is the date the financial statements were available to be issued.