

MIDSOUTH BANCORP INC  
Form 10-Q  
November 13, 2006

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

FORM 10Q

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

For the quarterly period ended **September 30, 2006**

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 **1-11826**

**MIDSOUTH BANCORP, INC.**

(Exact name of registrant as specified in its charter)

**Louisiana**

(State of other jurisdiction of incorporation or organization)

**72 -1020809**

(I.R.S. Employer Identification No.)

**102 Versailles Boulevard, Lafayette, Louisiana 70501**

(Address of principal executive offices, including zip code)

**(337) 237-8343**

(Registrant's telephone number, including area code)

Indicate by checkmark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act 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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

YES  NO

As of October 31, 2006, there were 6,251,929 shares of the registrant's Common Stock, par value \$.10 per share, outstanding.

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Index**MIDSOUTH BANCORP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CONDITION**

| <b>ASSETS</b>   | September 30,<br>2006<br>(unaudited) | December 31,<br>2005<br>(audited) |
|---|--------------------------------------|-----------------------------------|
| Cash and due from banks   | \$ 26,168,760                        | \$ 25,973,101                     |
| Interest bearing deposits in banks  | 34,825                               | 323,901                           |
| Federal funds sold  | -                                    | 26,140,000                        |
| Total cash and cash equivalents   | 26,203,585                           | 52,437,002                        |
| Securities available-for-sale, at fair value (cost of \$185,905,588 at September 30, 2006 and \$140,993,091 at December 31, 2005)   | 184,536,237                          | 139,428,403                       |
| Securities held-to-maturity (estimated fair value of \$16,716,938 at September 30, 2006 and \$20,151,389 at December 31, 2005)  | 16,399,477                           | 19,611,230                        |
| Loans, net of allowance for loan losses of \$4,910,028 at September 30, 2006 and \$4,354,530 at December 31, 2005   | 490,474,700                          | 438,439,219                       |
| Other investments   | 2,922,014                            | 2,011,403                         |
| Bank premises and equipment, net  | 29,112,870                           | 23,606,039                        |
| Accrued interest receivable   | 5,458,811                            | 4,919,294                         |
| Goodwill  | 9,271,432                            | 9,271,432                         |
| Intangibles   | 738,346                              | 985,264                           |
| Cash surrender value of life insurance  | 4,030,022                            | 3,794,510                         |
| Other assets  | 3,945,383                            | 4,310,625                         |
| <b>Total assets</b>   | <b>\$ 773,092,877</b>                | <b>\$ 698,814,421</b>             |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                                      |                                   |
| Deposits:   |                                      |                                   |
| Non-interest bearing  | \$ 179,919,828                       | \$ 177,946,159                    |
| Interest bearing  | 511,426,605                          | 446,991,941                       |
| <b>Total deposits</b>   | <b>691,346,433</b>                   | <b>624,938,100</b>                |
| Securities sold under repurchase agreements and federal funds purchased   | 3,912,669                            | 1,731,797                         |
| Accrued interest payable  | 833,532                              | 936,584                           |
| Junior subordinated debenture   | 15,465,000                           | 15,465,000                        |
| Other liabilities   | 2,499,080                            | 2,557,372                         |
| <b>Total liabilities</b>  | <b>714,056,714</b>                   | <b>645,628,853</b>                |
| Commitments and contingencies   | -                                    | -                                 |
| Stockholders' Equity:   |                                      |                                   |
| Common stock, \$.10 par value- 10,000,000 shares authorized, 6,353,446 and 6,258,089 issued and 6,256,131 and 6,189,649 outstanding at September 30, 2006 and December 31, 2005, respectively | 635,345                              | 500,647                           |
| Surplus   | 42,809,967                           | 41,910,122                        |
| Unearned ESOP shares  | (279,798)                            | (47,194)                          |
| Accumulated other comprehensive income  | (903,772)                            | (1,032,694)                       |
| Treasury stock - 97,315 at September 30, 2006 and 68,440 shares at December 31, 2005, at cost   | (1,884,933)                          | (1,229,213)                       |
| Retained earnings   | 18,659,354                           | 13,083,900                        |

|   |    |             |    |             |
|---|----|-------------|----|-------------|
| <b>Total stockholders' equity</b>                 |    | 59,036,163  |    | 53,185,568  |
| <b>Total liabilities and stockholders' equity</b> | \$ | 773,092,877 | \$ | 698,814,421 |

See notes to unaudited consolidated financial statements.

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CONSOLIDATED STATEMENTS OF EARNINGS (UNAUDITED)**

|   | Three Months Ended<br>September 30, |                  | Nine Months Ended<br>September 30, |                   |
|---|-------------------------------------|------------------|------------------------------------|-------------------|
|   | 2006                                | 2005             | 2006                               | 2005              |
| <b>INTEREST INCOME:</b>   |                                     |                  |                                    |                   |
| Loans, including fees   | \$ 10,860,528                       | \$ 8,342,155     | \$ 30,143,044                      | \$ 23,331,518     |
| Securities  |                                     |                  |                                    |                   |
| Taxable   | 1,251,978                           | 759,500          | 3,389,423                          | 2,306,471         |
| Nontaxable  | 900,593                             | 706,266          | 2,467,370                          | 2,014,437         |
| Federal funds sold  | 68,081                              | 49,057           | 768,667                            | 141,840           |
| Other interest income   | 22,518                              | 25,433           | 61,638                             | 58,320            |
| <b>TOTAL</b>  | <b>13,103,698</b>                   | <b>9,882,411</b> | <b>36,830,901</b>                  | <b>27,852,586</b> |
| <b>INTEREST EXPENSE:</b>  |                                     |                  |                                    |                   |
| Deposits  | 4,268,473                           | 2,634,764        | 11,603,901                         | 6,649,432         |
| Securities sold under repurchase<br>agreements, federal funds purchased<br>and advances | 58,332                              | 27,688           | 107,247                            | 129,219           |
| Long term debt  | 334,699                             | 295,362          | 984,300                            | 867,079           |
| <b>TOTAL</b>  | <b>4,661,504</b>                    | <b>2,957,814</b> | <b>12,695,448</b>                  | <b>7,645,730</b>  |
| <b>NET INTEREST INCOME</b>  | <b>8,442,194</b>                    | <b>6,924,597</b> | <b>24,134,694</b>                  | <b>20,206,856</b> |
| <b>PROVISION FOR LOAN LOSSES</b>  | <b>50,000</b>                       | <b>300,000</b>   | <b>670,000</b>                     | <b>679,737</b>    |
| <b>NET INTEREST INCOME AFTER<br/>PROVISION FOR LOAN LOSSES</b>                          | <b>8,392,194</b>                    | <b>6,624,597</b> | <b>23,646,694</b>                  | <b>19,527,119</b> |
| <b>OTHER OPERATING INCOME:</b>  |                                     |                  |                                    |                   |
| Service charges on deposits   | 2,459,671                           | 2,088,513        | 6,560,086                          | 6,414,593         |
| Gains (losses) on securities, net   | (7,553)                             | -                | (7,553)                            | 385               |
| Credit life insurance   | 40,887                              | 40,602           | 129,761                            | 121,568           |
| Other charges and fees  | 920,797                             | 711,373          | 1,724,761                          | 2,896,825         |
| <b>TOTAL OTHER INCOME</b>   | <b>3,413,802</b>                    | <b>2,840,488</b> | <b>9,328,055</b>                   | <b>9,433,371</b>  |
| <b>OTHER EXPENSES:</b>  |                                     |                  |                                    |                   |
| Salaries and employee benefits  | 4,249,564                           | 3,653,280        | 11,972,079                         | 10,160,905        |
| Occupancy expense   | 1,722,830                           | 1,462,505        | 4,833,038                          | 4,047,115         |
| Other   | 2,516,205                           | 2,203,097        | 7,248,727                          | 7,250,942         |
| <b>TOTAL OTHER EXPENSES</b>   | <b>8,488,599</b>                    | <b>7,318,882</b> | <b>24,053,844</b>                  | <b>21,458,962</b> |
| <b>INCOME BEFORE INCOME<br/>TAXES</b>   | <b>3,317,397</b>                    | <b>2,146,203</b> | <b>8,738,905</b>                   | <b>7,501,528</b>  |
| <b>PROVISION FOR INCOME<br/>TAXES</b>   | <b>900,260</b>                      | <b>512,315</b>   | <b>2,267,494</b>                   | <b>1,903,964</b>  |

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|                    |    |           |    |           |    |           |    |           |
|--------------------|----|-----------|----|-----------|----|-----------|----|-----------|
| NET EARNINGS       | \$ | 2,417,137 | \$ | 1,633,888 | \$ | 6,471,411 | \$ | 5,597,564 |
| EARNINGS PER SHARE |    |           |    |           |    |           |    |           |
| Basic              | \$ | 0.39      | \$ | 0.27      | \$ | 1.04      | \$ | 0.91      |
| Diluted            | \$ | 0.38      | \$ | 0.26      | \$ | 1.02      | \$ | 0.88      |

See notes to unaudited consolidated financial statements.

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**MIDSOUTH BANCORP, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)**  
**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005**

|  | <b>Three Months<br/>Ended<br/>September 30,<br/>2006</b> | <b>Three Months<br/>Ended<br/>September 30,<br/>2005</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2006</b> | <b>Nine Months<br/>Ended<br/>September 30,<br/>2005</b> |
|--|--|--|---|---|
| Net Income   | \$ 2,417,137   | \$ 1,633,888   | \$ 6,471,411  | \$ 5,597,564  |
| Other comprehensive income (loss):   |  |  |   |   |
| Unrealized gain(loss) on securities<br>available-for-sale, net:  |  |  |   |   |
| Unrealized holding gains (losses)<br>arising during the year net of income tax<br>(benefit) of \$1,042,550, (\$244,672),<br>\$66,414, and (\$464,429) respectively | 2,018,789  | (474,952)  | 123,937   | (901,285)   |
| Less reclassification adjustment for<br>gains included in net income net of<br>income tax of (\$2,568), -0-, (\$2,568),<br>and \$131, respectively                 | 4,985  | -  | 4,985   | (254)   |
| Total other comprehensive income<br>(loss)   | 2,023,774  | (474,952)  | 128,922   | (901,539)   |
| Total comprehensive income   | \$ 4,440,911   | \$ 1,158,936   | \$ 6,600,333  | \$ 4,696,025  |

See notes to unaudited consolidated financial statements.

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MIDSOUTH BANCORP, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY  
(UNAUDITED)  
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2006

|   | UNREALIZED<br>GAINS<br>(LOSSES)<br>ON |            |               |                    |                        |                   |                      | TOTAL         |
|---|---------------------------------------|------------|---------------|--------------------|------------------------|-------------------|----------------------|---------------|
|   | COMMON STOCK<br>SHARES                | AMOUNT     | SURPLUS       | ESOP<br>OBLIGATION | SECURITIES<br>AFS, NET | TREASURY<br>STOCK | RETAINED<br>EARNINGS |               |
| <b>Balance -<br/>January 1, 2006</b>  | 6,276,786                             | \$ 627,679 | \$ 41,783,090 | (\$47,194)         | (\$1,032,694)          | (\$1,229,213)     | \$ 13,083,900        | \$ 53,185,568 |
| Dividends on<br>common stock,<br>\$.14 per share  |                                       |            |               |                    |                        |                   | (895,957)            | (895,957)     |
| Exercise of stock<br>options  | 76,660                                | 7,666      | 334,145       |                    |                        |                   |                      | 341,811       |
| Tax benefit<br>resulting from<br>exercise of stock<br>options   |                                       |            | 594,899       |                    |                        |                   |                      | 594,899       |
| Purchase of<br>treasury stock   |                                       |            |               |                    |                        | (655,720)         |                      | (655,720)     |
| Net earnings  |                                       |            |               |                    |                        |                   | 6,471,411            | 6,471,411     |
| Increase in ESOP<br>obligation, net of<br>repayments  |                                       |            |               | (232,604)          |                        |                   |                      | (232,604)     |
| Excess of market<br>value over book<br>value of ESOP<br>shares released,<br>net adjustment            |                                       |            | 52,500        |                    |                        |                   |                      | 52,500        |
| Stock option<br>expense   |                                       |            | 45,333        |                    |                        |                   |                      | 45,333        |
| Net change in<br>unrealized gains(<br>losses) on<br>securities<br>available-for-sale,<br>net of taxes |                                       |            |               |                    |                        | 128,922           |                      | 128,922       |
| <b>Balance -<br/>September 30,<br/>2006</b>   | 6,353,446                             | \$ 635,345 | \$ 42,809,967 | (\$279,798)        | (\$903,772)            | (\$1,884,933)     | \$ 18,659,354        | \$ 59,036,163 |

See notes to unaudited consolidated financial statements.



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**MIDSOUTH BANCORP, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**  
**FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005**

|   | Sept. 30,<br>2006 | Sept. 30,<br>2005 |
|---|-------------------|-------------------|
| Cash flows from operating activities:   |                   |                   |
| Net earnings  | \$ 6,471,411      | \$ 5,597,564      |
| Adjustments to reconcile net income to net cash provided by operating activities: |                   |                   |
| Depreciation and amortization   | 2,044,232         | 1,573,702         |
| Provision for loan losses   | 670,000           | 679,737           |
| Deferred income taxes (benefit)   | (255,005)         | 56,699            |
| Amortization of premiums on securities, net                                       | 538,165           | 669,026           |
| (Gain) loss on sale of securities, net  | 7,553             | (385)             |
| Change in accrued interest receivable   | (539,517)         | (896,947)         |
| Change in accrued interest payable  | (103,052)         | (155,825)         |
| Other, net  | 1,187,234         | 353,766           |
| Net cash provided by operating activities   | 10,021,021        | 7,877,337         |
| Cash flows from investing activities, net of effect of acquisitions:              |                   |                   |
| Proceeds from sales of securities available-for-sale                              | 2,988,590         | 9,099,585         |
| Proceeds from maturities and calls of securities held-to-maturity                 | 3,219,900         | 1,973,244         |
| Proceeds from maturities and calls of securities available-for-sale               | 26,308,619        | 26,597,665        |
| Purchases of securities available-for-sale  | (74,763,571)      | (27,471,843)      |
| Purchases of other investments, net of redemptions                                | (910,950)         | (138,100)         |
| Loan originations, net of repayments  | (53,029,037)      | (48,501,118)      |
| Purchases of premises and equipment   | (7,304,836)       | (4,102,047)       |
| Proceeds from sales of other real estate owned                                    | 151,450           | 455,726           |
| Net cash used in investing activities   | (103,339,285)     | (42,086,888)      |
| Cash flows from financing activities, net of effect of acquisitions:              |                   |                   |
| Change in deposits  | 66,408,333        | 56,021,447        |
| Change in repurchase agreements   | 980,872           | (1,721,392)       |
| Change in federal funds purchased   | 1,200,000         | (8,500,000)       |
| Proceeds from FHLB advances   | -                 | 5,000,000         |
| Repayment of FHLB advances  | -                 | (5,000,000)       |
| Purchase of treasury stock  | (655,720)         | (295,392)         |
| Payment of dividends on common stock  | (1,190,449)       | (1,069,218)       |
| Proceeds from exercise of stock options   | 341,811           | 120,632           |
| Cash for fractional shares  | -                 | (10,640)          |
| Net cash provided by financing activities   | 67,084,847        | 44,545,437        |
| Net (decrease) increase in cash and cash equivalents                              | (26,233,417)      | 10,335,886        |

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|  |    |            |    |            |
|--|----|------------|----|------------|
| Cash and cash equivalents, beginning of year |    | 52,437,002 |    | 17,396,850 |
| Cash and cash equivalents, end of quarter    | \$ | 26,203,585 | \$ | 27,732,736 |

See notes to unaudited consolidated financial statements.

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**MIDSOUTH BANCORP, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENT**

**1. Basis of Presentation**

The accompanying unaudited consolidated financial statements and notes thereto contain all adjustments, consisting only of normal recurring adjustments, necessary to present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the Company and its subsidiaries as of September 30, 2006 and the results of their operations and their cash flows for the periods presented. The interim financial information should be read in conjunction with the annual consolidated financial statements and the notes thereto included in the Company's 2005 Annual Report and Form 10K.

The results of operations for the nine month period ended September 30, 2006 are not necessarily indicative of the results to be expected for the entire year.

*Use of Estimates* - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

*Stock Compensation* - In December 2004, the FASB revised SFAS No. 123 ("SFAS No. 123 (R)"). SFAS 123 (R), *Share-Based Payment*, requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. SFAS No. 123 (R) is effective for periods beginning after December 15, 2005. The Company adopted the provisions of SFAS No. 123 (R) on January 1, 2006. For the three and nine month period ended September 30, 2006, the required compensation expense totaled \$32,000 and \$45,333, respectively. Prior period pro forma disclosure is provided in the table below:

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|  | Three Months<br>Ended<br>Sept. 30,<br>2005 | Nine Months<br>Ended<br>Sept. 30,<br>2005 |
|--|--|---|
| Net earnings available to<br>common stockholders (in<br>thousands):            |  |   |
| As reported  | \$ 1,634                                   | \$ 5,598                                  |
| Deduct total stock based<br>compensation determined under<br>fair value method | (15)                                       | (45)                                      |
| Pro forma  | \$ 1,619                                   | \$ 5,553                                  |
| Basic earnings per share:  |  |   |
| As reported  | \$ 0.27                                    | \$ 0.91                                   |
| Pro forma  | \$ 0.26                                    | \$ 0.90                                   |
| Diluted earnings per share:  |  |   |
| As reported  | \$ 0.26                                    | \$ 0.88                                   |
| Pro forma  | \$ 0.26                                    | \$ 0.87                                   |

**Recent Accounting Pronouncements** - In September 2006, the Financial Accounting Standards Board (“FASB”) issued SFAS No. 158, *Employers’ Accounting for Defined Benefit Pension and Other Post Retirement Plans*, which amended FASB Statements No. 87, 88, 106, and 132(R). SFAS No. 158 requires the recognition of the funded status of a benefit plan on the balance sheet and recognition of the adjustment necessary to record the funded status as a component of other comprehensive income, net of tax. The Company must implement the funding status and disclosure requirement of SFAS No. 158 in the fourth quarter of 2006. SFAS No. 158 also requires to the Company to measure plan assets and obligations as of the date of the Company’s financial statements in fiscal 2009. The Company believes the implementation of the provisions of SFAS No. 158 will not have a significant impact on its financial statements, results of operations or cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 provides enhanced guidance to provide consistency and comparability in using fair value measurement of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Statement defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. The Statement does not require any new fair value measurements. The Company believes the implementation of the provisions of SFAS No. 157 will not have a significant impact on its financial statements, results of operations or cash flows.

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, which defines the threshold for recognizing the benefits of uncertain tax return positions in the financial statements. Interpretation No. 48 is effective for accounting changes and corrections of errors made in fiscal years beginning on or after December 15, 2006. The Company believes that the implementation of the provisions of Interpretation No. 48 will not have a significant impact on the Company’s financial position, results of operations or cash flows.

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In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments - an amendment of SFAS No. 133 and 140*. This statement provides entities with relief from having to separately determine the fair value of an embedded derivative that would otherwise be required to be bifurcated from its host contract in accordance with the requirements of SFAS 133. The effective date of this standard is for all financial instruments acquired, issued or subject to a remeasurement event occurring after the beginning of an entity's fiscal year that begins after September 15, 2006. The Company currently has no derivatives and therefore, SFAS No. 155 has no impact on the Company's current financial position, results of operations or cash flows.

In May 2005, the FASB issued Statement of Accounting Standards No. 154 (SFAS 154), *Accounting Changes and Error Corrections*. SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. The Statement was effective for fiscal years beginning after December 15, 2005 and did not have an impact on the Company's financial condition, results of operations or cash flows.

## 2. Allowance for Loan Losses

A summary of the activity in the allowance for loan losses is as follows (in thousands):

|                                | Nine Months Ended |          |
|--------------------------------|-------------------|----------|
|                                | September 30,     |          |
| (in thousands)                 | 2006              | 2005     |
| Balance at beginning of period | \$ 4,355          | \$ 3,851 |
| Provision for loan losses      | 670               | 680      |
| Recoveries                     | 266               | 162      |
| Loans charged off              | (381)             | (482)    |
| Balance at end of period       | \$ 4,910          | \$ 4,211 |

## 3. Declaration of Dividends

On September 13, 2006, the Company declared a 25% stock split on the common stock to holders of record on September 29, 2006 payable on October 23, 2006. All per share data has been adjusted accordingly. The Company also paid a \$.06 cash dividend for the third quarter 2006 and expects to pay a \$.06 cash dividend for the fourth quarter 2006. The Company will consider a special dividend to be paid in conjunction with fourth quarter 2006 dividend at year-end.

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**Part 1. Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS**

MidSouth Bancorp, Inc. ("the Company") is a two-bank holding company that conducts substantially all of its business through its wholly-owned subsidiary banks (the "Banks"), MidSouth Bank, N. A., headquartered in Lafayette, Louisiana and Lamar Bank, headquartered in Beaumont, Texas. The Company recently announced a name change for the Texas subsidiary from Lamar Bank to MidSouth Bank. The name change is expected to be executed in December 2006. Following is management's discussion of factors that management believes are among those necessary for an understanding of the Company's financial statements. The discussion should be read in conjunction with the Company's consolidated financial statements and the notes thereto presented herein and with the financial statements, the notes thereto and related Management's Discussion & Analysis in the Company's 10-K for the year ended December 31, 2005.

On October 23, 2006, the Company paid a five-for-four (25%) stock split to common shareholders of record on September 29, 2006. All per share data included in this filing has been adjusted accordingly.

**Forward Looking Statements**

The Private Securities Litigation Act of 1995 provides a safe harbor for disclosure of information about a company's anticipated future financial performance. This act protects a company from unwarranted litigation if actual results differ from management expectations. This management's discussion and analysis reflects management's current views and estimates of future economic circumstances, industry conditions, the Company's performance and financial results based on reasonable assumptions. A number of factors and uncertainties could cause actual results to differ materially from the anticipated results and expectations expressed in the discussion. These factors and uncertainties include, but are not limited to:

- changes in interest rates and market prices that could affect the net interest margin, asset valuation, and expense levels;
- changes in local economic and business conditions that could adversely affect customers and their ability to repay borrowings under agreed upon terms and/or adversely affect the value of the underlying collateral related to the borrowings;
- increased competition for deposits and loans which could affect rates and terms;
- changes in the levels of prepayments received on loans and investment securities that adversely affect the yield and value of the earning assets;
- a deviation in actual experience from the underlying assumptions used to determine and establish the Allowance for Loan Losses ("ALL");
- changes in the availability of funds resulting from reduced liquidity or increased costs;
- the timing and impact of future acquisitions, the success or failure of integrating operations, and the ability to capitalize on growth opportunities upon entering new markets;
- the ability to acquire, operate and maintain effective and efficient operating systems;

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- increased asset levels and changes in the composition of assets which would impact capital levels and regulatory capital ratios;
- loss of critical personnel and the challenge of hiring qualified personnel at reasonable compensation levels;
- changes in government regulations and accounting principles, policies and guidelines applicable to financial holding companies and banking; and
- acts of terrorism, weather, or other events beyond the Company's control.

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**Critical Accounting Policies**

Certain critical accounting policies affect the more significant judgments and estimates used in the preparation of the consolidated financial statements. The Company's significant accounting policies are described in the notes to the consolidated financial statements included in Form 10-K for the year ended December 31, 2005. The accounting principles followed by the Company and the methods of applying these principles conform with accounting principles generally accepted in the United States of America ("GAAP") and general banking practices. The Company's most critical accounting policy relates to its allowance for loan losses, which reflects the estimated losses resulting from the inability of its borrowers to make loan payments. If the financial condition of its borrowers were to deteriorate, resulting in an impairment of their ability to make payments, the Company's estimates would be updated and additional provisions for loan losses may be required. See "Asset Quality". Another of the Company's critical accounting policies relates to its goodwill and intangible assets. Goodwill represents the excess of the purchase price over the fair value of net assets acquired. In accordance with SFAS No. 142, "Goodwill and Other Intangible Assets," goodwill is not amortized but evaluated for impairment annually. If the fair value of an asset exceeds the carrying amount of the asset, no charge to goodwill is made. If the carrying amount exceeds the fair value of the asset, goodwill will be adjusted through a charge to earnings.

**Results of Operations**

Third quarter 2006 earnings totaled \$2,417,137 for the quarter ended September 30, 2006, a 47.9% increase over earnings of \$1,633,888 for the same period in 2005. Diluted earnings per share were \$.38 for the third quarter of 2006, compared to \$.26 per share for the third quarter of 2005. Earnings per share data have been adjusted to reflect a five-for-four (25%) stock split on the Company's common stock to holders of record as of September 29, 2006 paid on October 23, 2006.

For the nine months ended September 30, 2006, the Company earned \$6,471,411, a 15.6% increase over the \$5,597,564 reported for the nine months ended September 30, 2005. Diluted earnings per share were \$1.02 for the first nine months of 2006 versus \$.88 per share for the first nine months of 2005. The first nine months of 2005 included a \$631,000 pre-tax special distribution of proceeds to the Company from the merger of Pulse EFT Association and Discover Financial Services, Inc. Additionally, the first nine months of 2005 included a \$102,000 pre-tax write-down of a branch facility. Excluding the \$349,000 after-tax effect of these non-recurring transactions, the Company's earnings for the nine months ended September 30, 2006 improved by \$1,222,847, or 23.3%, over 2005.

Return on average equity was 16.98% for the third quarter of 2006 compared to 12.51% for the third quarter of 2005. The leverage capital ratio was 8.50% at September 30, 2006 compared to 8.97% at September 30, 2005.

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Net interest income for the third quarter of 2006 increased 21.9% to \$8,442,194 compared to \$6,924,597 for the third quarter of 2005. Net interest margin, on a fully taxable-equivalent basis, was 4.97% in the third quarter of 2006, an improvement of 10 basis points from 4.87% in the third quarter of 2005. Net interest income for the nine months ended September 30, 2006 increased 19.4% to \$24,134,694 compared to \$20,206,856 at September 30, 2005. The taxable-equivalent net interest margin remained constant at 4.93% for the two nine month periods compared.

Total consolidated assets increased \$113.6 million, or 17.2%, from \$659.5 million at the end of the third quarter of 2005 to \$773.1 million at the end of the third quarter of 2006. Total loans grew \$60.9 million, or 14.0%, from \$434.5 million at September 30, 2005 to \$495.4 million at September 30, 2006, primarily in commercial and industrial loans, real estate and construction loans. Total deposits increased \$104.9 million, or 17.9%, from \$586.4 million at September 30, 2005 to \$691.3 million at September 30, 2006. Deposit growth has been primarily in the Company's Platinum money market and checking accounts, which represented 34.8% of total deposits at September 30, 2006. The Platinum money market and checking accounts offer competitive rates of interest that adjust to changes in market rates and are more economically beneficial to the Company.

Nonperforming assets, including loans 90 days or more past due, totaled \$2.4 million at September 30, 2006, compared to \$3.0 million at September 30, 2005. As a percentage of total assets, nonperforming assets were .31% and .45% for September 30, 2006 and 2005, respectively. Included in nonperforming assets for September 30, 2006 is approximately \$1.2 million in government-guaranteed loans past due 90 days or over.

Net charge-offs to total loans decreased to .02% for the third quarter of 2006 compared to .07% for the third quarter of 2005. Allowance for loan loss provisions totaling \$50,000 were taken in the third quarter of 2006 compared to \$300,000 in the third quarter of 2005. As a percentage to total loans, the allowance for loan losses for the quarter ended September 30, 2006 and 2005 was .99% and .97%, respectively. The Company has not experienced an increase in delinquencies or charge-offs due to Hurricanes Katrina and Rita although management continues to monitor the rebuilding process in the Company's affected market area.

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The primary source of earnings for the Company is the difference between interest earned on loans and investments (earning assets) and interest paid on deposits and other liabilities (interest-bearing liabilities). Changes in the volume and mix of earning assets and interest-bearing liabilities combined with changes in market rates of interest greatly affect net interest income.

The Company's net interest margin on a taxable-equivalent basis, which is net income as a percentage of average earning assets, was 4.97% at September 30, 2006, up 10 basis points from 4.87% at September 30, 2005. Tables 1 through 4 following this discussion analyze the changes in taxable-equivalent net interest income for the two quarters ended and the two nine-month periods ended September 30, 2006 and 2005.

Average earning assets increased \$116.3 million, or 19.8%, from \$587.8 million in September 2005 to \$704.1 million in September 2006. The average yield on earning assets improved 73 basis points, from 6.86% at September 30, 2005 to 7.59% at September 30, 2006, but the mix of average earning assets shifted from 71.9% in average loans to total average earning assets in the third quarter of 2005 to 69.5% in the third quarter of 2006. The shift occurred during the first half of 2006 as deposit growth exceeded loan funding and excess deposit dollars were invested in short term investments.

The impact of the change in asset mix was offset by an increase in loan yields of 98 basis points, from 7.83% for the quarter ended September 30, 2005 to 8.81% for the quarter ended September 30, 2006, and a 39 basis point increase in the average taxable-equivalent yield on investment securities, from 4.46% to 4.85%, respectively. The average volume of investment securities increased \$50.6 million, from \$159.2 million at September 30, 2005 to \$209.8 million at September 30, 2006.

The Company's strong core deposit mix reflected improvement in the average volume of non-interest bearing deposits from \$136.7 million, or 23.8% of average total deposits at September 30, 2005, to \$176.3 million, or 25.5% of average total deposits at September 30, 2006. The average volume of NOW, Money Market and Savings deposits increased \$82.7 million from \$320.9 million, or 55.8% of average total deposits at September 30, 2005, to \$403.6 million, or 58.4% of average total deposits at September 30, 2006.

The average volume of Certificates of Deposit ("CD's") decreased \$5.5 million, from \$117.2 million at September 30, 2005 to \$111.7 million at September 30, 2006 and represented 20.4% of total deposits at September 30, 2005 compared to 16.2% at September 30, 2006. The decrease in CD's reflects the Company's retail strategy of developing long-term banking relationships with depositors. The retail strategy targets deposit growth in demand deposit accounts. That strategy, along with competitive market rates, yielded growth in the Company's Platinum Money Market and Platinum Checking accounts. The competitive rates on the Platinum accounts contributed greatly to the 90 basis point increase in the average rate paid on average interest-bearing deposits between the two quarters compared, from 2.39% at September 30, 2005 to 3.29% at September 30, 2006.

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The average rate paid on the Company's junior subordinated debentures increased 101 basis points from third quarter 2005 to third quarter 2006 due to increases in the floating rate paid on the \$8.2 million of such debentures issued in the third quarter of 2004 to partially fund the Lamar acquisition. The debentures carry a floating rate equal to the 3-month LIBOR plus 2.50%, adjustable and payable quarterly. The rate at September 30, 2006 was 7.89%. The debentures mature on September 20, 2034 and, under certain circumstances, are subject to repayment on September 20, 2009 or thereafter. In February 2001, the Company issued \$7,217,000 of junior subordinated debentures. The debentures carry a fixed interest rate of 10.20% and mature on February 22, 2031.

The impact of the changes in yield and volume of the earning assets and interest-bearing liabilities discussed above resulted in an increase of \$1.6 million to taxable-equivalent net interest income from September 30, 2005 to September 30, 2006.

Net interest income, on a taxable-equivalent basis, increased \$4.1 million for the nine-month period ended September 30, 2006, from \$21.0 million at September 30, 2005 to \$25.1 million at September 30, 2006. During the same period, average earning assets increased \$112.0 million, or 19.6%, from \$570.6 million in 2005 to \$682.6 million in 2006. The average yield on earning assets improved 69 basis points in nine-month comparison, from 6.72% at September 30, 2005 to 7.41% at September 30, 2006. The volume of total interest-bearing liabilities increased \$73.6 million, or 16.6%, from \$443.0 million for the nine months ended September 30, 2005 to \$516.7 million for the nine months ended September 30, 2006. The average yield on total interest-bearing liabilities increased 98 basis points in the same period, from 2.31% to 3.29%.

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**Table 1 - Consolidated Average Balances, Interest and Rates  
Taxable-equivalent basis (2)  
(in thousands)**

|   | Three Months Ended<br>September 30, 2006 |          |                       | Three Months Ended<br>September 30, 2005 |          |                       |
|---|--|----------|-----------------------|--|----------|-----------------------|
|   | Average<br>Volume                        | Interest | Average<br>Yield/Rate | Average<br>Volume                        | Interest | Average<br>Yield/Rate |
| <b>ASSETS</b>   |  |          |                       |  |          |                       |
| Interest Bearing Deposits   | \$ 100                                   | \$ 1     | 5.40%                 | \$ 82                                    | \$ 1     | 2.92%                 |
| Investment Securities (1)   |  |          |                       |  |          |                       |
| Taxable   | 108,637                                  | 1,250    | 4.60%                 | 77,809                                   | 765      | 3.93%                 |
| Tax Exempt (2)  | 98,710                                   | 1,271    | 5.15%                 | 78,697                                   | 987      | 5.02%                 |
| Equity Securities   | 2,442                                    | 23       | 3.69%                 | 2,686                                    | 25       | 3.79%                 |
| Total Investments   | 209,789                                  | 2,544    | 4.85%                 | 159,192                                  | 1,777    | 4.46%                 |
| Federal Funds Sold and<br>Securities<br>Purchased Under Agreements to<br>Resell | 5,157                                    | 68       | 5.24%                 | 5,926                                    | 49       | 3.28%                 |
| Loans (3)   |  |          |                       |  |          |                       |
| Commercial and Real Estate  | 390,297                                  | 8,742    | 8.89%                 | 327,941                                  | 6,418    | 7.77%                 |
| Installment   | 98,772                                   | 2,119    | 8.51%                 | 94,646                                   | 1,924    | 8.06%                 |
| Total Loans   | 489,069                                  | 10,861   | 8.81%                 | 422,587                                  | 8,342    | 7.83%                 |
| Total Earning Assets  | 704,115                                  | 13,474   | 7.59%                 | 587,787                                  | 10,169   | 6.86%                 |
| Allowance for Loan Losses   | (4,882)                                  |          |                       | (4,073)                                  |          |                       |
| Nonearning Assets   | 72,658                                   |          |                       | 66,505                                   |          |                       |
| Total Assets  | \$ 771,891                               |          |                       | \$ 650,219                               |          |                       |
| <b>LIABILITIES AND<br/>STOCKHOLDERS' EQUITY</b>                                 |  |          |                       |  |          |                       |
| NOW, Money Market, and<br>Savings   | \$ 403,623                               | \$ 3,286 | 3.23%                 | \$ 320,864                               | \$ 1,811 | 2.24%                 |
| Time Deposits   | 111,735                                  | 982      | 3.49%                 | 117,194                                  | 824      | 2.79%                 |
| Total Interest Bearing Deposits   | 515,358                                  | 4,268    | 3.29%                 | 438,058                                  | 2,635    | 2.39%                 |
| Federal Funds Purchased,<br>Securities Sold Under<br>Agreements to Repurchase   | 4,686                                    | 58       | 4.94%                 | 2,895                                    | 24       | 3.28%                 |
| Junior Subordinated Debentures  | 15,465                                   | 335      | 8.59%                 | 15,465                                   | 295      | 7.58%                 |
| Federal Home Loan Bank<br>Advances  | -  | -        |                       | 389                                      | 4        | 3.83%                 |
| Total Interest Bearing Liabilities  | 535,509                                  | 4,661    | 3.45%                 | 456,807                                  | 2,958    | 2.57%                 |
| Demand Deposits   | 176,282                                  |          |                       | 136,696                                  |          |                       |
| Other Liabilities   | 3,615                                    |          |                       | 4,903                                    |          |                       |
| Stockholders' Equity  | 56,485                                   |          |                       | 51,813                                   |          |                       |
|   | \$ 771,891                               |          |                       | \$ 650,219                               |          |                       |

Total Liabilities and  
Stockholders' Equity

|  |          |       |          |       |
|--|----------|-------|----------|-------|
| NET<br>TAXABLE-EQUIVALENT<br>INTEREST INCOME AND<br>SPREAD | \$ 8,813 | 4.14% | \$ 7,211 | 4.29% |
| NET<br>TAXABLE-EQUIVALENT<br>YIELD ON EARNING<br>ASSETS    |          | 4.97% |          | 4.87% |

- (1) Securities classified as available-for-sale are included in average balances and interest income figures reflect interest earned on such securities.
- (2) Interest income of \$370,467 for 2006 and \$286,350 for 2005 is added to interest earned on tax-exempt obligations to reflect tax-equivalent yields using a 34% tax rate.
- (3) Interest income includes loan fees of \$840,842 for 2006 and \$752,394 for 2005. Nonaccrual loans are included in average balances and income on such loans is recognized on a cash basis.

Index**Table 2 - Changes in Taxable-Equivalent Net Interest Income  
(in thousands)**

|  | Three Months Ended                                   |                           |              |
|--|--|---------------------------|--------------|
|  | September 30, 2006 compared to<br>September 30, 2005 | Change<br>Attributable to |              |
|  | Total<br>Increase<br>(Decrease)                      | Volume                    | Rates        |
| Taxable-equivalent interest earned on:                                       |  |                           |              |
| Investment Securities  |  |                           |              |
| Taxable  | 485  | 394                       | 91           |
| Tax Exempt   | 284  | 257                       | 27           |
| Equity Securities  | (2)  | (2)                       | -            |
| Federal Funds Sold and Securities Purchased Under<br>Agreement to Resell     |  |                           |              |
| Loans, including fees  | 19   | (5)                       | 24           |
|  | 2,519  | 1,404                     | 1,115        |
| <b>TOTAL</b>   | <b>3,305</b>   | <b>2,048</b>              | <b>1,257</b> |
| Interest Paid On:  |  |                           |              |
| Interest Bearing Deposits  |  |                           |              |
| Federal Funds Purchased and Securities Sold Under<br>Agreement to Repurchase | 1,633  | 520                       | 1,113        |
| Federal Home Loan Bank Advances  | 34   | 19                        | 15           |
| Junior Subordinated Debentures   | (4)  | (4)                       | -            |
|  | 40   | -                         | 40           |
| <b>TOTAL</b>   | <b>1,703</b>   | <b>535</b>                | <b>1,168</b> |
| Taxable-equivalent net interest income                                       | \$ 1,602   | \$ 1,513                  | \$ 89        |

NOTE: Changes due to both volume and rate has generally been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts to the changes in each.

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**Table 3 - Consolidated Average Balances, Interest and Rates**  
**Taxable-equivalent basis (2)**  
**(in thousands)**

|   | Nine Months Ended<br>September 30, 2006 |               |                       | Nine Months Ended<br>September 30, 2005 |               |                       |
|---|---|---------------|-----------------------|---|---------------|-----------------------|
|   | Average<br>Volume                       | Interest      | Average<br>Yield/Rate | Average<br>Volume                       | Interest      | Average<br>Yield/Rate |
| <b>ASSETS</b>   |   |               |                       |   |               |                       |
| Interest Bearing Deposits   | \$ 260                                  | \$ 10         | 5.35%                 | \$ 63                                   | \$ 1          | 3.11%                 |
| Investment Securities (1)   |   |               |                       |   |               |                       |
| Taxable   | 100,609                                 | 3,379         | 4.48%                 | 79,655                                  | 2,305         | 3.86%                 |
| Tax Exempt (2)  | 91,047                                  | 3,479         | 5.10%                 | 76,583                                  | 2,835         | 4.94%                 |
| Equity Securities   | 2,271                                   | 62            | 3.62%                 | 2,631                                   | 58            | 2.96%                 |
| Total Investments   | 193,927                                 | 6,920         | 4.76%                 | 158,869                                 | 5,198         | 4.36%                 |
| Federal Funds Sold and<br>Securities Purchased Under<br>Agreements to Resell  | 22,045                                  | 769           | 4.66%                 | 6,801                                   | 142           | 2.79%                 |
| Loans (3)   |   |               |                       |   |               |                       |
| Commercial and Real Estate  | 370,079                                 | 24,074        | 8.70%                 | 316,447                                 | 17,958        | 7.59%                 |
| Installment   | 96,299                                  | 6,069         | 8.43%                 | 88,428                                  | 5,374         | 8.13%                 |
| Total Loans   | 466,378                                 | 30,143        | 8.64%                 | 404,875                                 | 23,332        | 7.70%                 |
| <b>Total Earning Assets</b>   | <b>682,610</b>                          | <b>37,842</b> | <b>7.41%</b>          | <b>570,608</b>                          | <b>28,673</b> | <b>6.72%</b>          |
| Allowance for Loan Losses   | (4,615)                                 |               |                       | (3,979)                                 |               |                       |
| Nonearning Assets   | 71,913                                  |               |                       | 63,202                                  |               |                       |
| <b>Total Assets</b>   | <b>\$ 749,908</b>                       |               |                       | <b>\$ 629,831</b>                       |               |                       |
| <b>LIABILITIES AND<br/>STOCKHOLDERS' EQUITY</b>                               |   |               |                       |   |               |                       |
| NOW, Money Market, and<br>Savings   | \$ 380,179                              | \$ 8,626      | 3.03%                 | \$ 303,893                              | \$ 4,502      | 1.98%                 |
| Time Deposits   | 117,858                                 | 2,978         | 3.38%                 | 117,271                                 | 2,147         | 2.45%                 |
| Total Interest Bearing<br>Deposits  | 498,037                                 | 11,604        | 3.12%                 | 421,164                                 | 6,649         | 2.11%                 |
| Federal Funds Purchased,<br>Securities Sold Under<br>Agreements to Repurchase | 3,159                                   | 107           | 4.54%                 | 5,091                                   | 102           | 2.67%                 |
| Junior Subordinated Debentures  | 15,465                                  | 984           | 8.51%                 | 15,465                                  | 867           | 7.50%                 |
| Federal Home Loan Bank<br>Advances  | -                                       | -             |                       | 1,310                                   | 28            | 2.81%                 |
| Total Interest Bearing<br>Liabilities   | 516,661                                 | 12,695        | 3.29%                 | 443,030                                 | 7,646         | 2.31%                 |
| Demand Deposits   | 175,137                                 |               |                       | 131,923                                 |               |                       |
| Other Liabilities   | 3,233                                   |               |                       | 4,354                                   |               |                       |
| Stockholders' Equity  | 54,877                                  |               |                       | 50,524                                  |               |                       |
| <b>Total Liabilities and<br/>Stockholders' Equity</b>                         | <b>\$ 749,908</b>                       |               |                       | <b>\$ 629,831</b>                       |               |                       |

|  |           |       |           |       |
|--|-----------|-------|-----------|-------|
| NET<br>TAXABLE-EQUIVALENT<br>INTEREST INCOME AND<br>SPREAD | \$ 25,147 | 4.12% | \$ 21,027 | 4.41% |
| NET<br>TAXABLE-EQUIVALENT<br>YIELD ON EARNING<br>ASSETS    |           | 4.93% |           | 4.93% |

- (1) Securities classified as available-for-sale are included in average balances and interest income figures reflect interest earned on such securities.
- (2) Interest income of \$1,012,414 for 2006 and \$820,322 for 2005 is added to interest earned on tax-exempt obligations to reflect tax-equivalent yields using a 34% tax rate.
- (3) Interest income includes loan fees of \$2,611,267 for 2006 and \$2,270,574 for 2005. Nonaccrual loans are included in average balances and income on such loans is recognized on a cash basis.

Index**Table 4 - Changes in Taxable-Equivalent Net Interest Income  
(in thousands)**

|  | Nine Months Ended                                    |                           |              |
|--|--|---------------------------|--------------|
|  | September 30, 2006 compared to<br>September 30, 2005 | Change<br>Attributable to |              |
|  | Total<br>Increase<br>(Decrease)                      | Volume                    | Rates        |
| Taxable-equivalent interest earned on:                                       |  |                           |              |
| Interest Bearing Deposits  | \$ 9   | \$ 6                      | \$ 3         |
| Investment Securities  |  |                           |              |
| Taxable  | 1,074  | 854                       | 220          |
| Tax Exempt   | 644  | 548                       | 96           |
| Equity Securities  | 4  | (6)                       | 10           |
| Federal Funds Sold and Securities Purchased Under<br>Agreement to Resell     |  |                           |              |
| Loans, including fees  | 627  | 483                       | 144          |
|  | 6,811  | 3,787                     | 3,024        |
| <b>TOTAL</b>   | <b>9,169</b>   | <b>5,672</b>              | <b>3,497</b> |
| Interest Paid On:  |  |                           |              |
| Interest Bearing Deposits  | 4,955  | 1,368                     | 3,587        |
| Federal Funds Purchased and Securities Sold Under<br>Agreement to Repurchase |  |                           |              |
| Federal Home Loan Bank Advances  | 5  | (49)                      | 54           |
| Junior Subordinated Debentures   | (28)   | (28)                      | -            |
|  | 117  | -                         | 117          |
| <b>TOTAL</b>   | <b>5,049</b>   | <b>1,291</b>              | <b>3,758</b> |
| Taxable-equivalent net interest income                                       | \$ 4,120   | \$ 4,381                  | (\$261)      |

NOTE: Changes due to both volume and rate has generally been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts to the changes in each.

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**Non-Interest Income  
Excluding Securities Transactions**

Total non-interest income for the third quarter 2006 increased \$573,314 to \$3,413,802, compared to \$2,840,488 for the third quarter of 2005. The Company's primary source of non-interest income is service charges and fees on deposit accounts, which include insufficient funds ("NSF") fees. Income from service charges on deposit accounts increased from September 2005 to September 2006 in three and nine-month comparisons by \$371,158 and \$145,493, respectively. The increase resulted primarily from a higher number of deposit accounts within the Company's customer base and from increased volume of NSF activity, primarily in the third quarter of 2006. Additionally, the Company increased the NSF processing fee from \$23.47 per NSF item processed to \$24.47 per item effective July 1, 2006. Despite the increase in the fee, the \$24.47 per item charge remains lower than most competitors' charges within the Company's markets.

In third quarter 2005, the Company experienced a decrease of approximately \$60,000 in service charges on deposit accounts due to a decrease in NSF activity as a result of Hurricanes Katrina and Rita. The Company continued to experience decreased NSF activity throughout the fourth quarter of 2005 and a reduction in service charges on deposit accounts in that quarter of approximately \$240,000.

Income from other charges and fees increased \$209,424 for the three months ended September 30, 2006 as compared to September 30, 2005. The increase resulted primarily from an increase of \$114,299 in ATM and debit card processing fees due to a higher volume of transactions. For the nine months ended September 30, 2006, income from other charges and fees decreased \$251,064 as compared to the nine months ended September 30, 2005, primarily due to the \$631,000 pre-tax special distribution of proceeds to the Company from Pulse included in 2005 income. An increase of \$377,619 in ATM and debit card processing fees for the nine months ended September 30, 2006 compared to the nine months ended September 30, 2005 partially offset the impact of the special distribution on the net change in other charges and fees in year-to-date comparison.

**Securities Transactions**

On September 27, 2006, the Company's Louisiana subsidiary, MidSouth Bank, purchased two agency securities from the investment portfolio of the Texas subsidiary, Lamar Bank, for the purpose of providing additional liquidity at Lamar Bank and to maintain intercompany borrowings within regulatory limits. Minimal losses totaling \$7,553 were recorded on the sale of the two securities.

Index**Non-interest Expenses**

Non-interest expenses increased \$1,169,717 in quarterly comparison and \$2,594,882 in year-to-date comparison, primarily in salaries and employee benefit costs and occupancy expenses related to the new retail stores added over the past twelve months. Salaries and benefit costs increased \$596,284 in quarter-to-date comparison and \$1,811,174 in year-to-date comparison due to the addition of 41 full-time equivalent employees, from 323 at September 30, 2005 to 364 at September 30, 2006. Occupancy expenses increased \$260,325 and \$785,923 in quarterly and nine months comparison, respectively, due to the added retail stores. Delays in expansion projects lessened the impact of occupancy expenses in third quarter comparison.

Other expenses increased \$313,108 and decreased \$2,215 for the same periods, respectively. The quarterly increase resulted primarily from increases of \$135,360 in marketing costs, \$74,603 in ATM and debit card processing expenses, and \$52,544 in professional fees, including accounting fees. The minimal decrease in the nine-month comparison resulted primarily from decreases in the amortization of intangibles (\$164,974), expenses associated with other real estate and other assets (\$124,064), professional fees (\$52,706), education and travel expenses (\$44,780) and other miscellaneous expenses, which were offset by increases of \$214,877 in ATM and debit card processing expense and \$212,077 in marketing costs. The increase in marketing costs in three and nine-month comparisons resulted primarily from expenses associated with promotions surrounding the opening of the new retail stores. Additionally, the Company sponsors several trade shows in its various markets. The increases noted in ATM and debit card processing expenses resulted from a higher volume of electronic transactions.

**Analysis of Statement of Condition**

Consolidated assets totaled \$773.1 million at September 30, 2006, up \$74.3 million from \$698.8 million at December 31, 2005. The increase resulted primarily from growth in deposits of \$66.4 million. The deposit growth is attributed to new retail branch offices and to increased corporate and government spending due to rebuilding efforts in the Company's markets. Fluctuations in large corporate deposits during the third quarter 2006 resulted in a \$ 12.8 million decrease in period end deposits compared to June 30, 2006. The fluctuations resulted primarily from corporate spending, business transactions and tax payments.

Total loans grew \$52.6 million, from \$442.8 million at year-end 2005 to \$495.4 million at September 30, 2006. Loan growth was below internal projections primarily due to payoffs, but is expected to improve with recent hires, new retail stores and good loan demand in the Company's markets. The loan growth occurred primarily in the Company's commercial and industrial, commercial real estate and construction loan portfolios as reflected in the table below.

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| Loan Portfolio (in thousands)           | September 30, 2006 |         | December 30, 2005 |         |
|---|--------------------|---------|-------------------|---------|
|   | Amount             | Percent | Amount            | Percent |
| Commercial, industrial and agricultural | \$ 171,351         | 34.59%  | \$ 154,359        | 34.86%  |
| Lease financing receivable              | 7,467              | 1.51%   | 6,108             | 1.38%   |
| Real estate - commercial                | 126,369            | 25.51%  | 109,905           | 24.82%  |
| Real estate - mortgage                  | 64,328             | 12.99%  | 60,990            | 13.77%  |
| Real estate - construction              | 51,431             | 10.38%  | 39,202            | 8.85%   |
| Consumer                                | 74,439             | 15.03%  | 72,230            | 16.31%  |
| Total loans                             | \$ 495,385         | 100.00% | \$ 442,794        | 100.00% |

Securities available-for-sale totaled \$184.5 million at September 30, 2006, up \$45.1 million from \$139.4 million at December 31, 2005. Cash flows from deposit growth in the first nine months of 2006, net of loan fundings, were invested in tax-free municipal securities and short-term agency securities that added to the available-for sale portfolio. The purchased securities offered some yield improvement over the rate earned on federal funds sold. The portfolio of securities held-to-maturity decreased \$3.2 million, from \$19.6 million at December 31, 2005 to \$16.4 million at September 30, 2006, due to maturities and calls within that portfolio.

Bank premises and equipment increased \$5.5 million for the first nine months of 2006 and reflected the impact of the Company's continued expansion.

**Liquidity**

Liquidity is the availability of funds to meet operational cash flow requirements and to meet contractual obligations as they become due. The Banks' primary liquidity needs involve their ability to accommodate customers' demands for deposit withdrawals as well as their requests for credit. Liquidity is deemed adequate when sufficient cash to meet these needs can be promptly raised at a reasonable cost to the Banks. Liquidity is provided primarily by three sources: a stable base of funding sources, an adequate level of assets that can be readily converted into cash, and borrowing lines with correspondent banks. The Banks' core deposits are their most stable and important source of funding. Further, the low variability of the core deposit base lessens the need for liquidity. Cash deposits at other banks, federal funds sold, principal payments received on loans and mortgage-backed securities, and maturities of investment securities provide additional primary sources of asset liquidity for the Banks. The Banks also have significant borrowing capacity with the FHLB of Dallas, Texas and borrowing lines with other correspondent banks.

At the parent company level, cash is needed primarily to meet interest payments on the junior subordinated debentures and pay dividends on common stock. An \$8.2 million issuance of junior subordinated debentures was completed on September 20, 2004, the proceeds of which were partially used to fund the Lamar Bancshares merger. The parent company previously issued \$7.2 million in junior subordinated debentures in February 2001. Dividends from the Banks primarily provide liquidity for the parent company. As a publicly traded company, the parent company also has the ability to issue additional trust preferred and other securities instruments to provide funds as needed for operations and future growth.

Index**Capital**

The Company and the Banks are required to maintain certain minimum capital levels. Risk-based capital requirements are intended to make regulatory capital more sensitive to the risk profile of an institution's assets. At September 30, 2006, the Company and the Banks were in compliance with statutory minimum capital requirements and were classified as "well capitalized". Minimum capital requirements include a total risk-based capital ratio of 8.0%, with Tier 1 capital not less than 4.0%, and a leverage ratio (Tier 1 to total average adjusted assets) of 4.0% based upon the regulators latest composite rating of the institution. As of September 30, 2006, the Company's leverage ratio was 8.50%, Tier 1 capital to risk-weighted assets was 11.13% and total capital to risk-weighted assets was 11.97%.

**Asset Quality****Credit Risk Management**

The Company manages its credit risk by observing written, board approved policies which govern all underwriting activities. The risk management program requires that each individual loan officer review his or her portfolio on a quarterly basis and assign recommended credit ratings on each loan. These efforts are supplemented by independent reviews performed by the loan review officer and other validations performed by the internal audit department. The results of the reviews are reported directly to the Audit Committee of the Board of Directors. Additionally, bank concentrations are monitored and reported to the Board of Directors quarterly whereby individual customer and aggregate industry leverage, profitability, risk rating distributions, and liquidity are evaluated for each major standard industry classification segment.

**Nonperforming Assets and Loans Past Due 90 Days and Over**

The following table summarizes the Company's nonperforming assets and loans past due 90 days and over for the quarters ending September 30, 2006 and 2005 and for the year-ended December 31, 2005.

| (in thousands)  | Quarter Ended Sept. 30, |          | % Chg  | Year Ended       |
|---|-------------------------|----------|--------|------------------|
|   | 2006                    | 2005     |        | Dec. 31,<br>2005 |
| Nonaccrual loans  | \$ 501                  | \$ 2,125 | -76.4% | \$ 660           |
| Loans past due 90 days and over   | 1,789                   | 561      | 218.9% | 2,511            |
| Total nonperforming loans   | 2,290                   | 2,686    | -14.7% | 3,171            |
| Other real estate owned   | 24                      | 111      | -78.4% | 98               |
| Other foreclosed assets   | 58                      | 154      | -62.3% | 176              |
| Total nonperforming assets  | \$ 2,372                | \$ 2,951 | -19.6% | \$ 3,445         |
| Nonperforming assets to total assets                                    | 0.31%                   | 0.45%    | -31.1% | 0.49%            |
| Nonperforming assets to total loans<br>+ OREO + other foreclosed assets | 0.48%                   | 0.68%    | -29.4% | 0.78%            |
| ALL to nonperforming assets   | 207.00%                 | 142.70%  | 45.1%  | 126.42%          |
| ALL to nonperforming loans  | 214.41%                 | 156.78%  | 36.8%  | 137.34%          |
| ALL to total loans  | 0.99%                   | 0.97%    | 2.1%   | 0.98%            |
| Year-to-date charge-offs  | \$ 381                  | \$ 482   | -21.0% | \$ 702           |
| Year-to-date recoveries   | 266                     | 164      | 62.2%  | 226              |
| Year-to-date net charge-offs  | \$ 115                  | \$ 318   | -63.8% | \$ 476           |

|                                    |       |       |        |       |
|------------------------------------|-------|-------|--------|-------|
| Net YTD charge-offs to total loans | 0.02% | 0.07% | -71.4% | 0.11% |
|------------------------------------|-------|-------|--------|-------|

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Nonperforming assets, including loans 90 days or more past due, totaled \$2.4 million at September 30, 2006, compared to \$3.0 million at September 30, 2005. As a percentage of total assets, nonperforming assets were .31% and .45% for September 30, 2006 and 2005, respectively. Included in nonperforming assets for September 30, 2006 is approximately \$1.2 million in government-guaranteed loans, which are expected to be paid in full or returned to a current status. The past-due status of the \$1.2 million in government-guaranteed loans is not related to Hurricanes Katrina or Rita.

Net charge-offs to total loans decreased to .02% for the third quarter of 2006 compared to .07% for the third quarter of 2005. Allowance for loan loss provisions totaling \$50,000 were taken in the third quarter of 2006 compared to \$300,000 in the third quarter of 2005. The decrease in the provision between the two quarters compared resulted primarily from minimal net charge-offs and improved asset quality ratios. As a percentage to total loans, the allowance for loan losses for the quarters ended September 30, 2006 and 2005 was .99% and .97%, respectively. The Company has not experienced an increase in delinquencies or charge-offs due to Hurricanes Katrina and Rita, although management continues to monitor the rebuilding process in the Company's affected market area.

Specific reserves have been established in the ALL to cover probable losses on nonperforming assets. The ALL is analyzed quarterly and additional reserves, if needed, are allocated at that time. Factors considered in determining provisions include estimated losses in significant credits; known deterioration in concentrations of credit; historical loss experience; trends in nonperforming assets; volume, maturity and composition of the loan portfolio; off balance sheet credit risk; lending policies and control systems; national and local economic conditions; the experience, ability and depth of lending management and the results of examinations of the loan portfolio by regulatory agencies and others. The processes by which management determines the appropriate level of the allowance, and the corresponding provision for probable credit losses, involves considerable judgment; therefore, no assurance can be given that future losses will not vary from current estimates. Management believes the \$4,910,028 in the allowance as of September 30, 2006 is sufficient to cover probable losses in nonperforming assets and in the loan portfolio.

**Impact of Inflation and Changing Prices**

The consolidated financial statements of and notes thereto, presented herein, have been prepared in accordance with generally accepted accounting principles, which require the measurement of financial position and operating results in terms of historical dollars without considering the change in the relative purchasing power of money over time and due to inflation. The impact of inflation is reflected in the increased cost of the Company's operations. Unlike most industrial companies, nearly all the assets and liabilities of the Company are financial. As a result, interest rates have a greater impact on the Company's performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

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**Part I. Item 3. Qualitative and Quantitative Disclosures About Market Risk**

In the normal course of conducting business, the Company is exposed to market risk, principally interest rate risk, through operation of its subsidiaries. Interest rate risk arises from market fluctuations in interest rates that affect cash flows, income, expense and values of financial instruments. The Asset/Liability Management Committee (“ALCO”) is responsible for managing the Company’s interest rate risk position in compliance with policy approved by the Board of Directors.

There have been no significant changes from the information regarding market risk disclosed under the heading “Interest Rate Sensitivity” in the Company’s Annual Report for the year ended December 31, 2005.

**Part I. Item 4. Controls and Procedures**

The Company’s Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the disclosure controls and procedures (as such term is defined in Rules 13a-14(c) and 15d-14(c) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). As of the end of the period covered by this Quarterly Report on Form 10-Q (the “Evaluation Date”), the principal executive officer and principal financial officer have concluded that such disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

During the third quarter of 2006, there were no significant changes in the Company’s internal controls over financial reporting that has materially affected, or is reasonably likely to affect, the Company’s internal controls over financial reporting.

**Part II. Other Information**

**Item 1. Legal Proceedings**

The Banks have been named as a defendant in various legal actions arising from normal business activities in which damages of various amounts are claimed. While the amount, if any, of ultimate liability with respect to such matters cannot be currently determined, management believes, after consulting with legal counsel, that any such liability will not have a material adverse effect on the Company’s consolidated financial position, results of operations, or cash flows.

Index**Item 1.A. Risk Factors** - No change**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table provides information with respect to purchases made by or on behalf of the Company or any “affiliated purchaser,” as defined in Securities Exchange Act Rule 10b-8(a)(3), of equity securities during the quarter ended September 30, 2006.

|                | Total Number of<br>Shares Purchased | Average Price Paid per<br>Share | Total Number of<br>Shares Purchased as<br>Part of a Publicly<br>Announced Plan <sup>1</sup> | Maximum Number of<br>Shares That May Yet<br>be Purchased Under<br>the Plan <sup>1</sup> |
|----------------|-------------------------------------|---------------------------------|---|---|
| July 2006      | 3,257                               | \$22.88                         | 3,257   | 224,522   |
| August 2006    | 1,593                               | \$24.04                         | 1,593   | 221,265   |
| September 2006 | 908                                 | \$26.42                         | 908   | 220,357   |

<sup>1</sup> -Under a share repurchase program approved by the Company’s Board of Directors on November 13, 2002, the Company can repurchase up to 5% of its common stock outstanding through open market or privately negotiated transactions. The repurchase program does not have an expiration date.

**Item 3. Defaults Upon Senior Securities**

None

**Item 4. Submission of Matters to a Vote of Security Holders**

None

**Item 5. Other Information**

None

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**Item 6. Exhibits and Reports on Form 8-K**

**(a) Exhibits**

| <u>Exhibit Number</u> | <u>Document Description</u>   |
|-----------------------|---|
| <u>11</u>             | Computation of earnings per share                                       |
| <u>31.1</u>           | Certification pursuant to Exchange Act Rules 13(a) - 14(a)              |
| <u>31.2</u>           | Certification pursuant to Exchange Act Rules 13(a) - 14(a)              |
| <u>32.1</u>           | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| <u>32.2</u>           | Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

**(b) Reports Filed on Form 8-K**

A press release regarding the Company's earnings for the quarter ended June 30, 2006 was attached as Exhibit 99.1 to the Form 8-K filed on July 25, 2006.

A press release regarding the Company's appointment of a Principal Officer was attached as Exhibit 99.1 to the Form 8-K filed on September 20, 2006. Exhibit 10.1 to the filing detailed the terms of the principal officer's employment agreement with the Company.

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**Signatures**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

MidSouth Bancorp, Inc.  
(Registrant)

Date: November 10, 2006

/s/ C. R. Cloutier

C. R. Cloutier, President /CEO

/s/ J. E. Corrigan, Jr.

J. E. Corrigan, Jr., Executive Vice President/CFO

/s/ Teri S. Stelly

Teri S. Stelly, SVP/Controller