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**SCHEDULE 14A  
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Ehud Gelblum;JPMorgan;Analyst  
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## **Presentation**

Operator: Good morning, and thank you for holding. Welcome to this Motorola conference call. [OPERATOR INSTRUCTIONS] Today's call is being recorded.

Thank you. And now I would like to introduce Mr. Dean Lindroth, Motorola's Corporate Vice President of investor relations. Mr. Lindroth, you may begin.

Dean Lindroth: Thank you, and good afternoon, everyone. A replay of this webcast including questions and answers will also be available later on our website. Forward-looking statements will be made during this teleconference. Forward-looking statements are any statements that are not historical facts. Such statements are based on the current expectations of Motorola and there can be no assurance that these expectations will prove to be correct. Because forward-looking statements involve risks and uncertainties, Motorola's actual results could differ materially from these statements. Information about factors that could cause, and in some cases have caused such differences can be found in today's press release on pages -- and on pages 16-24 of item 1-A of Motorola's form 10-K for the fiscal period year-end December 31, 2006 and in Motorola's other SEC filings.

This conference call is occurring on March 21, 2007. The context of this call contain time[sensitive information that is current only at the time of this live broadcast. If any portion of this call is retransmitted at a later date , Motorola will not be reviewing or updating materials contained herein. This call is the exclusive property of Motorola. Any redistribution, retransmission or rebroadcast of this call in any form without the express written consent of Motorola is strictly prohibited.

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With that, I'd like now to turn the call over to Ed Zander, Chairman and CEO.

Ed Zander: Good afternoon. With me this afternoon are Greg Brown, our new President and Chief Operating Officer, and Dave Devonshire, our CFO. I'm sure you've all seen the press release we issued today. On this call, I want to give you as much color as I possibly can and talk about the actions we're taking and the changes we're making. We'll do our best to answer your questions, but please keep in mind that we have not yet finished the quarter. We'll update you further on our earnings call on April 18th, when we will provide you with more perspective for the full year.

I know today's announcement has disappointed our shareholders. No one understands the gravity of this situation more than my team and I do. In January at our New York analyst meeting we discussed our outlook for the first quarter and the full year and we gave you the best information we had at that time. We also laid out a plan to improve the performance of the mobile device business. Our key element of the plan was that we were going to be more selective about pursuing market segments and product tiers that demonstrate the best opportunity for higher gross margin. Let me remind you it has always been my objective to grow market share profitability. Let me underscore the word profitability. We will not chase market share for the sake of market share at the expense of margin and profits.

As you know, about a month ago there was a change in management in Mobile Devices. After that change it became apparent that the actions that we outlined in January were not progressing fast enough, if at all. These included minimum movement on the cost structure changes, continued delays in some of our newer 3G products, and implementation of our simplified software platform and silicon strategy. Given this situation, we recognized the need to move faster. In addition, competitive pricing in emerging markets intensified throughout the quarter. We chose not to match these price cuts, which in turn lower our unit volumes, and we are working -- and we are also seeing some product increases in the channel, which should work through over the next few months.

Further, our performance in Europe continues to be below expectations because we had a limited 3G product portfolio. As a result and as you can see in today's press release, Q1 for Mobile Devices will be very difficult and disappointing. We also anticipate that Q2 will be difficult. There is much that has to be done to restore the Mobile Device business to where it can be. This is going to take more time and greater effort, but we expect the business to gradually recover in the second half of this year and to be profitable for the year. We need to get back to focusing on innovation, operational discipline and execution.

So today, we announced a series of actions designed to improve our execution, drive profitable growth and enhanced value for shareholders. These include: Steps to strengthen the performance of Mobile Devices; the appointment of Greg Brown to President and Chief Operating Officer of Motorola; the appointment of Thomas Meredith to acting Chief Financial Officer and the retirement of Dave Devonshire; an accelerated

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repurchase of \$2 billion in common stock; and increase our existing share repurchase program by \$3 billion to \$7.5 billion.

As in the press release, our guidance is now as follows. We expect sales for the first quarter to be in the range of \$9.2 billion to \$9.3 billion. First quarter GAAP earnings are expected to be a loss in the range of \$0.07 to \$.09 per share, including expense of \$0.09 in highlighted items. As we said, the revised guidance is attributable to lower-than-anticipated sales and operating earnings in our Mobile Device business. That business expects to report an operating loss for the quarter. Again, this is due to lower unit volumes, difficult pricing environment, particularly in lower tier, and a limited 3G product portfolio in Europe. The lower volume's do primarily to our affirmative shift to focus on long-term gross margin improvement rather than focusing primarily on market share growth. The growth in emerging markets, such as India, Africa, Middle East and South Asia, competitors lowered prices at a faster rate than anticipated.

Given the renewed focus on gross margin improvement, we chose not to match price cuts in all instances. However, Mobile Devices business continues to track in North America, Latin America and North Asia. We believe we still have a compelling iconic mid-tier product line up. And it shouldn't go up unnoticed that our Connected Home Solutions and Networks and Enterprise businesses continue to perform generally in line with our expectations. We are pleased with the progress we're making in cable, wireline, enterprise, government and emerging broadband wireless technologies.

For the full year, we expect overall sales profitability and operating cash flow to be substantially below our prior guidance. The corporation expects to be profitable for the full year and have positive operating cash flow for the year. My intention to provide you with more perspective for the full year on our April 18th earnings call. We expect the Mobile Device business to experience a gradual recovery in the second half of 2007 and have an operating profit for the full year. As we said back in January, we anticipate lowering our annualized cost structure by \$400 million, which includes a previously-announced work force reduction of 3,500 and acceleration of site rationalizations. In addition, we will continue to make further adjustments to our cost structure in line with the revised revenue expectations, as necessary. For Network and Enterprise and Connected Home Solution businesses, we are reaffirming our previously stated guidance for 2007. The Networks and Enterprise we expect mid-teen annual growth and double-digit operating margins, and for Connected Home, we expect sales growth to exceed market growth and operating earnings to increase as compared to the full-year 2006.

Let me now talk about some of the organizational changes. We are announcing today that Greg Brown, President of our current Network and Enterprise business, will assume the role of President and Chief Operating Officer effective immediately. Greg will be responsible for overseeing all of our divisions, including Mobile Devices, Network and Enterprise, Connected Home, our supply chain and our quality organization. Greg has more than 25 years of high-tech experience, including leadership positions in telecommunications, software and wireless industries. His keen understanding of Motorola strategy and customer requirements will be invaluable, as we execute our

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revitalized operating plan for the benefit of our customers, employees and shareholders. We are excited he has accepted this position. And Greg will be spending a good deal of his time working with the new leadership in Mobile Devices.

Today we also announced that Dave Devonshire is retiring from Motorola and the Company announced Tom Meredith as acting Chief Financial Officer effective April 1st. Dave will remain with the Company to insure a smooth transition. As a valued member of the senior management team, Dave has been essential in bringing tighter financial controls to our business, strengthening our balance sheet and leading the first stock repurchase program in the Company's history. I appreciate his commitment to insuring a seamless transition and wish him best in his retirement. The board and I are delighted Tom will serve as acting CFO. Tom is a seasoned professional with tremendous financial expertise. He comes with an in-depth knowledge of Motorola. Tom is able to hit the ground running. He was a CFO for Dell for eight years and is a general manager of Meritage Capital and Chief Executive Officer of MFI Capital. We are thrilled that he is here to assist us with our planned actions to improve execution, drive profitable growth and enhance shareholder value.

Let me now talk about our continuing efforts to return capital to our shareholders. Motorola has a proven track record of shareholder returns and we regularly review our capital allocation strategy. Today we are announcing that we are up-sizing our current repurchase program to \$7.5 billion. We are also announcing an accelerated repurchase of \$2 billion of our common stock and we're using available cash on hand to make those repurchases. In a little under two years, since May 2005, we have repurchased a total of approximately \$7 billion of our common stock out of a total authorization of \$11.5 billion. We've listened to our shareholders and these actions today reflect our commitment to returning additional capital to them.

And finally back to Mobile Devices and some of the specific things we are doing. As you know, this is a fast-moving industry and it's all about innovation, operational discipline, and execution. We have to get it right in all three areas to maintain the kind of performance we have shown over the past few years. Let me reiterate what I said earlier. I'm committed to growing market share, but profitable market share. We need to get back to basics. Our goal is for every product and every price tier and every geography to make money. The Mobile Devices business enjoyed great success over the past almost three years on the back of innovative and differentiated products like RAZR, SLIVR, PEBL, MING and others. We did not exploit that success effectively, and now endeavor to match our prior success again.

Let me speak to the definitive actions we are taking with Mobile Devices to return that business to the past levels of performance. First, we are moving our contacts and relationships with our customers. I've spent time in the last week in fact, on the road, meeting and listening to them and making sure our roadmaps are aligned. We are deploying open standard Linux Java software across mid and high-tier devices to enhance the experiences available on handsets, music; videos, photos, messaging and other cool experiences. We are accelerating a multi-source cost competitive silicon strategy, and we

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will shift our marketing approach to include experience as well as design as a product value proposition. We've got a great brand and we're going to drive it. We will prioritize and accelerate the introduction of new feature-rich products that deliver compelling mobile experience, especially in 3G. We are simplifying our platforms and product portfolio while transitioning out of legacy platforms. And finally we are overhauling our product design processes to achieve more competitive price points.

As you can imagine, my team and I, especially Greg in his new role, are spending time on the Mobile Device business, helping them with strategy, marketing, product priorities and working with customers to continue our long-term relationships. And we have a terrific team with two strong leaders, Ray Roman and Terry Vega, running the business, now reporting to Greg. Terry led the remarkable turnaround of our CDMA product line, and she has been promoted to handle our global product organization. Ray has been with the Company for five years. He led our return to number one in North America profitably and is running our global field operations. Not to mention, we have bench strength in our field sales organizations in Mobile Devices, and as you've seen in the past few years, I truly believe he has one of the best engineering and product design teams in the industry. The Mobile Device industry is healthy. This is a good business, one we can win at and make money. In short, it's about innovation, operational discipline, and execution, having the right product at the right price in the right market at the right time.

Today, I have focused on Mobile Devices. We're going to get that business turned around, but beyond that we have great opportunities for growth. In the Connected Home business, we have built one of the most robust wireline and cable next-generation video delivery systems. In the Network space, we are a clear leader in next-generation broadband wireless, with early leadership in intellectual property, field trials and contracts. And in private networks, we lead in Homeland Security and mission-critical communications. And in the Enterprise space we are well positioned for acquisition of simple technologies. This is a great Company. We've got the right assets. We have great people who are resilient and determined. We have a powerful brand, a strong IP portfolio, our heritage of innovation, and a solid balance sheet. But make no mistake about it, even though we have work to do. And the most important thing I can do right now as CEO is to insure this Company performs for our shareholders, customers, partners and employees. Thank you.

Operator, now let's go to questions.

Operator: Thank you.

Dean Lindroth: Operator? I'd like to just remind everyone before the questions start that I'd like everyone to limit themselves to one question so that we can accommodate as many participants as possible. So, operator, if you'd like to provide the instructions once again and then we can take the first question.

## **Q&A Session**

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Operator: Thank you. [OPERATOR INSTRUCTIONS] Your first question is coming from Ittai Kidron of CIBC World Markets. Please go ahead.

Ittai Kidron: Hello, gentlemen. One clarification and one question. First one for you, Dave, the clarification with regards to the buyback. Out of this new target of \$7.5 billion, can you tell us how much has been used to date and again, just to clarify is the \$2 billion you're accelerating is that going to be part of the \$7.5? And a second question to Ed. Now we have two very important positions in the Company that are vacant that I would assume Greg is not going to stay as head of Networks and Enterprise, correct me if I'm wrong? Mobile Devices and Network and Enterprise now open slots. How do you think about restaffing those positions on a permanent basis? Are you looking for internal/external talent and what's going to be the process and timeline for refilling those positions?

Dave Devonshire: Okay, well, a lot of questions there. First of all, on the subject of share repurchase, against the \$7.5 billion, all told, it's about \$1.1 billion that we have spent, excluding the announcement that we're making today. So we are going into the market and doing an accelerated share buyback for an additional \$2 billion, so that would be \$3.1 billion in essence that we've committed to spend and now, out of the \$7.5 billion total share repurchase. So that's roughly 40%.

Ittai Kidron: Okay, so out of the \$7.5 only \$1.1 has been done to date?

Dave Devonshire: That's correct.

Ittai Kidron: Okay, very good.

Ed Zander: Ittai, the second question I'm going to turn the question over to Greg, but one of the reasons -- many reasons I put Greg in here is he had an opportunity to look at the organization across it, so we have some very strong leaders there and we are excited by the work that, for example, Ray and Terry are doing today but I'm going to let Greg comment.

Greg Brown: Yes, Ed mentioned, Terry Vaga and Ray Roman's qualifications. I think that duo significantly makes us stronger with their leadership. In addition to that, with Networks and Enterprise, as you mentioned, I will retain operational responsibility for that organization, as well. We do not have an organizational update or announcement at this point in time. Having said that, the general managers globally in Networks and Enterprise I think are extremely strong and represent a great cross section of the best of the best, as we took the previous networks in the organization and merged them together.

Dean Lindroth: Next question, please?

Operator: Your next question is coming from Tim Long of Banc of America. Please go ahead.

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Tim Long: Thank you. Could you talk a little bit -- clarify a little of your comments about the pricing pressures in the entry part of the market, if you could quantify for that? And just how does that relate maybe to some of the product transitions you're going through from the C-series to the W-series and the Modafone, is that related to it? And also on that topic, [Ron Garrics] used to talk about the cost of losing shelf space. Is it fair to assume that you don't hold that strategy, that market share there? Lost is lost for good? Thank you.

Ed Zander: Well, I think you kind of have it tagged on the low end. We have some pretty good products there and the prices in some of these growth industries have moved down. and you need the profitability if you're going to go play that game and we've got some really good products, but we have to work on our cost structure in that area and our investment profile. You can't be everywhere around the world investing in all these dollars without the ability to generate profit, so I think we're not backing away from market share. I'm a market share, have always been, but I think you have to do it in a very deliberate and organized fashion to keep generating the profit. So the W, the series and the Modafone are all on a feature basis excellent products, but if we're going to move down scale in pricing, we need the cost structure to go with it and that's what we're going to work on in the low end and that's what Terry is.

I think the second question was, I forgot. Oh, market share and shelf space. I think that we've proven time and time again -- I mean, CDMA business here in the United States several years ago, when I got here we had no market share. I mean, low single-digit. Today we're -- I think we're number one just about in CDMA in some of these carriers, with very iconic -- I mean, Terry has taken that business from being literally unprofitable to being very good profitability here in just a couple of years with the right products and the right price points. So I prefer to get on the shelves with products that I can make money with, and not just chase market share and I think we just have reverse that. It may mean we have to go back a little bit , but I think we know what to do here and we're going to go drive it. And Ray's doing it now and Terry and with Greg's leadership.

Dean Lindroth: Next question, please?

Operator: Okay your next question is coming from Brant Thompson of Goldman Sachs. Please go ahead.

Brant Thompson: I was wondering if you could give us a little bit more clarity on terms of the pricing impact in the quarter? You talked about, obviously, the low-end pricing coming down, but on the high end, the price reduction we saw on the high end in the last quarter really had a big impact. Did you see further erosion of those prices or should we look at the pricing change in the high end to be more like the 3G? Just trying to understand what happened at the very high end of the market.

Ed Zander: This is Ed. I think that there's now the high end and the mid range. I'd like to say we had a very strong brand and a very strong set of products in the mid range, and clearly, as we said in Q4, there was movement in the beginning of the quarter to move

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those down in prices and we expected the higher-end [inaudible] products to take that space. Well, I think you know, you just hit it on -- you just said it. The 3G products moved in, especially in Europe and even in places here in the U.S, So at the "high end," we need to get our 3G portfolio and we are starting to ship some products. It does take awhile to ramp up. If you were at Barcelona you saw the new "kick slider" that I think was the best-in-class there, but we need more like that and we've got to get the -- we've got to protect the mid range. One of the things you're seeing here is we've got a great mid range, but if you don't have the high end then it's very difficult to compete in the low end So we need to get both of those areas and that's what I just read about what Terry's focus is. Greg, do you want to add anything?

Greg Brown: No. I think you're right. I mean, obviously from a pricing standpoint, the competitive pricing on the low end in the emerging markets intensified. As we've said, we're not going to chase market share for just the sake of market share, and at the expense of margins and profits. So we chose not to match these price cuts, which in turn lowered our overall unit volumes. On the higher end, our performance in Europe continues to be below expectations, and as has already been referenced, it's primarily because we have a limited 3G product portfolio at this point in time.

Dean Lindroth: Next question, please?

Operator: Your next question is coming from Maynard Um of UBS. Please go ahead.

Maynard Um: Hi, thank you. A quick clarification and a question, if I could. Of the \$.09 charge, can you just quantify the charges specifically for Mobile Devices? And then the question, if you can just talk about how much of the impact in Q1 was end market related or industry related versus a Motorola-specific issue that's under your control to fix? Thanks.

Greg Brown: Yes. First of all on the charges, we'll get into a lot more detail on April the 18th, but as we said earlier, they are really a combination of acquisition related cost and the reduction in force.

Ed Zander: So again, the acquisitions plus the -- when we talked back in January about the reductions across the Company that were previously planned, I think the second question was about pricing?

Greg Brown: Well I think you mentioned external and internal and I think the answer is both. We described the external pricing environment and some of the incremental changes that occurred within the quarter. In terms of other things under our control, as we already said, referencing the outlines -- the actions outlined in January, we just didn't progress fast enough. So I think it was a combination of both.

Ed Zander: I think with the quarter closes and we've still got a couple of weeks here, we can give you more insight on April 18th on the dynamics.

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Maynard Um: But more of an issue on pricing, not end unit demand, is that correct?

Ed Zander: Well, again, I think what you saw in Q4 -- and we had a lot of demand and the question is, you've got to make money, so I think we've got to get back to -- as I said in my talk, we just need to go back to grow market share profitable and to make money and to -- our strategy has to be way more disciplined and determined about it. It's a fast-moving market, a very competitive market, and if you want to play in a space where people are cutting prices, you better have the cost structure to respond and the product cost structuring and that's what we're going to go do.

Dean Lindroth: Okay, next question, please?

Operator: Your next question is coming from Phil Cusick of Bear, Stearns. Please go ahead.

Phil Cusick: Hi, guys. Thanks for taking the call. You mentioned in the release about an accelerated silicon transition. Can you get into that a little bit more here? What should we expect from the single-chip architecture in terms of timing to hit real volumes here? Thanks.

Ed Zander: Well I'd rather not give away all of the specifics. As you know, we had a silicon supplier for most of our products as part of the separation a couple years ago. And if you're going to be as big as we are -- I think we outlined this in January -- that we need to have multiple sources of silicon for different price points across our product line, whether it's 3G at the high end or whether it's some of the products at the low end. And so we need to diversify real time here and we've got to accelerate that, and I don't think I saw the kind of acceleration and commitment to a silicon strategy. Terry's had now, since she took over, a complete accelerated task force to get this done. So it's important when we're talking about like we just said about the low end that we have a silicon strategy there that is very competitive. And if we're talk about 3G and cool experiences a silicon strategy there. And we saw it on 3G products and one of the challenges was one size doesn't fit all, because the 3G market has many different price points in it. So we just got to get this done and with that, by the way, the software platform, the Linux Java platform, which allows you to build the kind of experiences that we want at the high end.

Phil Cusick: Ed can I follow-up on that a little bit? Given the change in the ownership structure at that supplier , do you think that they've pulled back a little bit from the development platform since that happened?

Ed Zander: I don't want to comment on that.

Dean Lindroth: Okay, next -- we'll take the next question, please.

Operator: Your next question is coming from Ehud Gelblum of JPMorgan. Please go ahead.

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Ehud Gelblum: A couple things actually. When you look at this, it looks like there's something a little bit bigger going on here with execution, and I calculate that units were somewhere in the mid 40s in terms of million units this quarter. Margin's obviously negative in the handset side. Ed, you didn't mention the RAZR once, although volumes are probably still fairly decent. What I'm trying just to understand is as you go forward and you fix this business, do you need just better product -- just better products that are out there or it's something execution wise in the manufacturing side have to get better?

Ed Zander: I don't think it's the manufacturing as much as it is -- I think the team over there has done a phenomenal job. If you notice, we aren't talking like we were years ago about missed deliveries and product issues and lateness and quality, so they've done a great job. What we really got to do is -- first of all the RAZR, I did talk I think that we have -- RAZR, and that's all it's derivatives, because when we talk RAZR we now have RIZR out there and the KRAZR is doing well in some of our carriers. It's a mid -- they're mid-tier products. They're feature-phone market. I think we still own that. We just need to get way better at the experiences at the high end, and at the low end, you need product cost structure that is going to allow you to compete effectively. And those are the two areas that we have been more selective and focused on gross margin percentage as opposed to just gross margin dollars, and there's a fundamental difference there in terms of whether you drive market share or you drive profitable market share.

Ehud Gelblum: Well, I'm trying to actually get a picture as to what you have in mind as to what the business looks like at the end of the day. Is it look like similar to what you had before, with a lot of high end to a lot of mid range or low end or is it more focused to the mid range and to the high end, or is it more to the low end?

Ed Zander: No.

Ehud Gelblum: And where is the margin of the business end up? Is it back in double-digits?

Ed Zander: Well, hopefully, we can talk a little bit more about that April 18th [when it's closed the quarter.] I think we got good products in all areas. I do think we're a little weaker in the high end, and you need to do that because that's a great margin pool, and a great area of profitability. I think for awhile, we did prove in the low end we can compete. It's just a matter of you got expenses at the low end, too, in terms of driving retail and driving brand and you got to just do that at a very, very calculated and disciplined fashion. So I think we outlined a little bit in the press release, but we'll -- we have to address, for example, the basic UMTS products at the entry level of UMTS, so I think as we get around and talk to you after the quarter and on the 18th maybe we can maybe just give you a little more insight into what we're doing here.

Dean Lindroth: Okay, next?

Greg Brown: Just the other thing I think to add to that is obviously we have to maintain and I think recommit a high level of customer orientation and get product roadmaps

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aligned with some of our top customers and over lay that and reinforce it with marketing -- crisper marketing and some compelling value propositions to continue to stimulate demand as well.

Dean Lindroth: Okay, next question, please?

Operator: Thank you. Your next question is come from Mike Ounjian of Credit Suisse. Please go ahead.

Mike Ounjian: Great, thanks. Ed, the thing about the handset business, obviously it's good to see the focus on profitability and now I know scale has also been a focus and sort of relative to competitors over time, as well. I mean, how are you thinking about the scale that's necessary in terms of -- I don't know if it's market share or volumes relative to your competitors to hit the profitability targets over the long term?

Ed Zander: Well, I think you do need some scale and we do have scale , but I think you need profitability at any given point as you move up that scale. And to be honest with you, I think we got a little bit -- on this word profitable market share, I think we got the market share right as we moved up in the scale game. But you got to make money, because the money you need, you need to invest back into getting both the cool experiences at the high end, but more importantly, the infrastructure to compete in these growth and emerging markets. So you just can't announce products and cut prices and lower gross margin and expect to -- that game's not going to play and it didn't. And if we have to regroup a little bit we will, but we did this in second half of 2004-2005 with a very, very, I think, focused effort.

We [inaudible] CDMA, for example, in the United States here, and around the world we were no where with single-digit market share. And what Terry and her team has done is now -- I think we've got some of the best CDMA products in the business at the many of the U.S. carriers today and in places in Asia. And I think we have to just -- we have to understand that concept of discipline, innovation and execution, and we're going to try to fo --- and I think when -- Greg's sitting here, I don't know if you want to comment --that's what he's going to really drive with Terry and Ray in that area. Greg?

Greg Brown: No, I agree. At the end of the day, it's going to be about innovation and operational discipline and execution and we have a tremendous amount of key assets. And I really do think we have a deep bench strength of talent, whether it be engineering or development design teams to go to market and we've just got to get it back aligned with all products and all tiers and get back on our game with it.

Dean Lindroth: Next question, please?

Operator: Your next question is coming from Tal Liani of Merrill Lynch. Please go ahead.

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Tal Liani: Hi, guys. I have a question and just one clarification for Ed. Starting with the more important one, the question is about second half. If I try to work back your margin for the quarter -- and this is a rough estimate based on the press release -- I get -5.5% margin. So if I take your comment of profitable for the year, the second half should be +5% or +6%, so there is a big improvement throughout the year. I know you don't want to preannounce any model, but would you mind to take us through the model assumptions, your effort assumptions? What takes the margins this way apart from cost cuts? What are you planning to put out -- and again, big bucket, we don't have to go into more of a specific model -- so that's the first question. Second question, which I think is obvious for now, I just want to put it to bed. One of the speculations in the market were that you cancelled the CTIA presentation because you were working on an LBO or you're working on buying Palm and I just want you to -- if possible to relate to these two issues. Thank you.

Ed Zander: I'll take the second one. I'm going to give Greg back the first one. You know, I'm just amazed at the CTIA. I have a personal family thing that -- and I don't believe I'm even talking about this because it's amazing to me -- and I team up with my family that we called CTIA a few weeks ago and said, do you have a replacement and could you accommodate me, and it was no big deal. They had plenty of back ups and I chose -- I've been working really, really full day here and that's what this is about this weekend, and so that's that. That's all I'm telling you. I'm not going to go any further into my personal life. As far as the models go, Greg?

Greg Brown: Yes, in terms of the financials, the quantification and clarity of it is outlined in the press release. As we mentioned it's primarily driven by Mobile Devices, and net-net Q1 was both difficult and disappointing. Having said that, Q2 will be difficult as well, and we mentioned the fact that the recovery will be gradual and substantially less than what we originally thought back in January and we'll provide a little bit more perspective on that on April 18th.

Tal Liani: Right. This is clear, but the question is whether the recovery is based on new models in the market, new 3G handsets? Is it new platforms apart from [inaudible]? Just more color on what leads to the recovery.

Greg Brown: Yes, I think it's probably all of the above, but stay tuned and we'll give you a little bit more color on that on the 18th.

Dean Lindroth: Next question, please?

Operator: Okay. Your next question is coming from Scott Coleman of Morgan Stanley. Please go ahead.

Scott Coleman: Sure, thanks, maybe one clarification and then a question. In terms of the clarification, Ed, I think if I heard correctly, you said you chose not to match price cuts, and that hurt unit volume, but that there also was some pricing pressure that hurt you guys this quarter. Can you help me reconcile those two statements? And then I guess the

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second question -- or the question would be you talk about improving gross margin in the handset business, yet this isn't a number that you report. Would you consider reporting gross margin by segment as a way to improve your transparency? I think this would also help investors understand what the spending levels, maybe for sales and marketing and R & D, are around your handset business and where you could become more competitive against some of your competitors.

Ed Zander: The first one was the pricing. Again, when you have the kind of revenue numbers that we've had this quarter and [inaudible] back to Q4, it just continued into Q1, and when we got a chance to have some of the management changes -- and as I said, Ray and Terry there really taking charge and get myself and Dave and some of the other people, we got a chance to really look way under the covers, and I spent a lot of time with customers and I think there was -- it was a number of different things. It's always not one thing. There is price cuts going on in emerging growth markets. I'm not sure it's necessarily here in the mid markets or feature phones or -- there's always that pressure when you're dealing with any of the parts of this business, but -- And we deliberately in a lot of areas, not all areas, chose not to necessarily follow prices down because what it would have done, it might have given us more units and more volume and more revenue but the gross margin percentage would have continued to be under pressure. Now, you can't see that yet because when you take the down turn -- we did this for the long term so you get back to some pricing discipline in the marketplace that'll help you in future quarters.

I think you said and some of the other fellows on the phone about the high end is much more of a feature competitive. UMTS in Europe, especially, which is a -- as we've always said a big source of the profit pools. It's beginning to happen here in the U.S. And there we just need more products. We've got some out, but you need a lot of products and a lot of geographies with a lot of the carriers and the branded services, and I think it's what we did with the mid tier -- or at that time, the entire family of iconic products that we introduced, we did a hell of a job in 2004 and 2005. We just got to recreate that again. And then in the low end we just got to pick our spots and go after market share where we can make money.

I think there was another question there? Or maybe that was it. I got it all. Oh, gross margin transparency. Good input. We'll take a look at that. Obviously, a look at competition and what everything else has done here before I give away anything that I don't want to give away with, but that's something that we'll take under consideration.

Dean Lindroth: Next question, please?

Operator: Thank you. Your next question is coming from Bill Choi of Jefferies. Please go ahead.

Bill Choi: Okay, thanks. Just looking at the negative margins on the handset business, did you take inventory write downs in the quarter or expect to take one in the near term? And as far as pricing coming down, how much should we be looking at for rebates or price

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protection of products in the channel that you mentioned might take a couple months to sell through and its impact to -- potential impact to Q1 and Q2?

Ed Zander: The an -- go ahead, Dave.

Dave Devonshire: The answer to that is we don't have that level of detail yet. And for sure, there are absolutely no inventory write downs included in our estimate.

Ed Zander: We're working with our channel partners. Again, we sold these products, they're working them through and we work on marketing programs to move these products into different geographies. But I think we said so in the release, we expect the channel to work through this over the next couple months.

Dave Devonshire: And some of the channels and certain geographies, so it's not -- certain geographies are okay.

Dean Lindroth: Operator, we'll take our last question, please?

Operator: Thank you. Your last question is coming from Daryl Armstrong with Citigroup. Please go ahead.

Daryl Armstrong: Thank you very much. I just wanted to touch back on one of the things. From a high-end product portfolio [inaudible] number of times that UMTS phones are quite important, what we haven't heard is relative to smart phones. How do you think smart phones are going to fit into product portfolio, let's say, over the next six to 12 months?

Ed Zander: Well, I think they're good. It's still the percentage [inaudible]. but we just introduced. This is the thing. We got to get our marketing out. We've had the Q here only in CDMA and pretty much North America. We are just coming now into shipping two new products, a GSM version, which will be available in a lot of geographies, which again where there's no 3G, Latin America, China, and other places, you have to do, of course, the software ports and platform ports. And the other one is our UMTS HSDPA Q, which I've been using, and I think it's the best product we've produced in some time, and that'll be rolling out, also. So there again, think are products like that. There are products like the "kick slider" in Europe that will be shipping, I think, in the May-June time frame.

And we need to get more of those out. It's not that we can't do them. We need to get the silicon strategy right so we can go with a different price points in that space. Some of these were appearing with Linux Java and as we roll these out, we need to roll them out in more places where 3G is prevalent, and with more of the applications and solutions. And we're a little late and and we need -- I don't know if the focus was there in the past year to the degree it should have been, nor do I think the cost structure in design of products at the low end was there. Down at that point, every dollar -- in fact, I'll say every \$0.10 matters and we got to get back to that discipline. If we aren't meeting our cost targets by \$0.10, it doesn't ship and that's the kind of thing we got to get back to. So I

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think market share is great, but sometimes it gets in the way of getting back to the basics and that's what the we got to go do here.

Dean Lindroth: Okay, during this call, we've made a number of forward-looking statements. Forward-looking statements are any statements that are not historical facts. These forward-looking statements are based on the current expectations of Motorola and there could be no assurance that such expectations will prove to be correct. Such forward-looking statements include, but are not limited our comments and answers relating the to following topics: Motorola sales and earnings per share for the first quarter of 2007; Motorola sales, profitability and cash flow for the full-year 2007; expectations regarding the volume and impact of our stock repurchase program and our accelerated repurchase program; the impact on Motorola's performance and financial results from strategic acquisitions and divestitures, including those that are recently completed, those that are pending and those that may occur in the future; work force reductions and the cost savings and financial impact relating to the Company's ongoing reorganization activities; future strategic plans, sales, profitability, operating earnings, operating margin and market share for each of Motorola's business segments; expected timing for the announcement, launch and shipment of new products; the sales impact and pricing of our products.

Because forward-looking statements involve risks and uncertainties, Motorola's actual results could differ materially from those stated in the forward-looking statements. Information about factors that could cause such differences can be found in this afternoon's press release and on pages 16-24 of item 1-A of Motorola's 2006 Annual Report on Form 10-K and Motorola's other SEC filings. This now concludes our call.

Operator: Thank you. This concludes today's Motorola conference call. You may now disconnect your lines, at this time, and have a wonderful day.

#### **DISCLAIMER**

**THE INFORMATION CONTAINED IN THIS TRANSCRIPT IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON FINANCIAL OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.**

#### **ADDITIONAL INFORMATION AND WHERE TO FIND IT**

While Motorola does not believe that this communication constitutes solicitation material in respect of Motorola's solicitation of proxies in connection with its 2007 Annual Stockholders Meeting, this communication may be deemed to be solicitation material. In connection with the solicitation of proxies, Motorola has filed with the Securities and Exchange Commission (the "SEC") a definitive proxy statement on March 15, 2007 (the "Proxy Statement"). THE PROXY STATEMENT CONTAINS IMPORTANT INFORMATION ABOUT MOTOROLA AND THE 2007 ANNUAL STOCKHOLDERS MEETING. MOTOROLA'S STOCKHOLDERS ARE URGED TO READ THE PROXY STATEMENT CAREFULLY.

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On March 19, 2007, Motorola began the process of mailing the Proxy Statement, together with a WHITE proxy card. Stockholders may obtain additional free copies of the Proxy Statement and other documents filed with the SEC by Motorola through the website maintained by the SEC at [www.sec.gov](http://www.sec.gov). The Proxy Statement and other relevant documents may also be obtained free of charge from Motorola by contacting Investor Relations in writing at Motorola, Inc., 1303 E. Algonquin Road, Schaumburg, IL 60196; or by phone at 1-800-262-8509; or by email at [investors@motorola.com](mailto:investors@motorola.com). The Proxy Statement is also available on Motorola's website at [www.motorola.com/investor](http://www.motorola.com/investor). The contents of the websites referenced above are not deemed to be incorporated by reference into the Proxy Statement. In addition, copies of the Proxy Statement may be requested contacting our proxy solicitor, D.F. King & Co. Inc. by phone toll-free at 1-800-488-8095.

Motorola and its directors and executive officers and other members of management and employees may be deemed to be participants in the solicitation of proxies in connection with the 2007 Annual Stockholders Meeting. You can find information about Motorola's executive officers and directors in the Proxy Statement.

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Cash surrender value of life insurance

13,690

13,622

Other real estate

3,908

4,187

Other assets

7,039

6,352

Total assets

\$

1,916,551

\$

1,927,733

Liabilities and Shareholders' Equity

Liabilities:

Deposits:

Non-interest-bearing

\$  
383,684

\$  
374,261

Interest-bearing

1,174,519

1,176,589

Total deposits

1,558,203

1,550,850

Securities sold under agreements to repurchase

87,879

85,957

Short-term Federal Home Loan Bank advances

—

25,000

Long-term Federal Home Loan Bank advances

25,744

25,851

Junior subordinated debentures

22,167

22,167

Other liabilities

6,704

4,771

Total liabilities

1,700,697

1,714,596

Commitments and contingencies

Shareholders' equity:

Series B Preferred stock, no par value; 5,000,000 shares authorized, 32,000 shares issued and outstanding at March 31, 2016 and December 31, 2015

32,000

32,000

Series C Preferred stock, no par value; 100,000 shares authorized, 91,200 shares issued and outstanding at March 31, 2016 and December 31, 2015

9,120

9,120

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Common stock, \$0.10 par value; 30,000,000 shares authorized, 11,362,150 shares issued and outstanding at March 31, 2016 and December 31, 2015

1,136

1,136

Additional paid-in capital

110,958

110,771

Unearned ESOP shares

(1,284

)

(1,093

)

Accumulated other comprehensive income

2,331

509

Retained earnings

61,593

60,694

Total shareholders' equity

215,854

213,137

Total liabilities and shareholders' equity

\$

1,916,551

\$

1,927,733

See notes to unaudited consolidated financial statements.

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MidSouth Bancorp, Inc. and Subsidiaries  
 Consolidated Statements of Earnings (unaudited)  
 (in thousands, except per share data)

	Three Months Ended March 31,	
	2016	2015
Interest income:		
Loans, including fees	\$17,123	\$18,054
Securities and other investments:		
Taxable	2,036	1,925
Nontaxable	458	584
Federal funds sold	5	2
Time and interest bearing deposits in other banks	94	37
Other investments	88	79
Total interest income	19,804	20,681
Interest expense:		
Deposits	907	947
Securities sold under agreements to repurchase	233	230
Other borrowings and payables	113	97
Junior subordinated debentures	167	150
Total interest expense	1,420	1,424
Net interest income	18,384	19,257
Provision for loan losses	2,800	6,000
Net interest income after provision for loan losses	15,584	13,257
Non-interest income:		
Service charges on deposits	2,313	2,332
Gain on sale of securities, net	—	115
ATM and debit card income	1,609	1,629
Other charges and fees	565	765
Total non-interest income	4,487	4,841
Non-interest expenses:		
Salaries and employee benefits	7,990	7,942
Occupancy expense	3,597	3,685
ATM and debit card expense	785	663
Data processing	458	457
FDIC insurance	429	281
Legal and professional fees	383	345
Other	3,117	2,788
Total non-interest expenses	16,759	16,161
Income before income taxes	3,312	1,937
Income tax expense	963	446
Net earnings	2,349	1,491
Dividends on preferred stock	427	173
Net earnings available to common shareholders	\$1,922	\$1,318



Earnings per share:

Basic	\$0.17	\$0.12
Diluted	\$0.17	\$0.12
Weighted average number of shares outstanding:		
Basic	11,262	11,318
Diluted	11,262	11,351
Dividends declared per common share	\$0.09	\$0.09

See notes to unaudited consolidated financial statements.

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MidSouth Bancorp, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income (unaudited)

(in thousands)

	Three Months Ended March 31,	
	2016	2015
Net earnings	\$2,349	\$1,491
Other comprehensive income, net of tax:		
Unrealized gains on securities available-for-sale:		
Unrealized holding gains arising during the year	2,802	1,701
Less: reclassification adjustment for gains on sales of securities available-for-sale	—	(115 )
Total other comprehensive income, before tax	2,802	1,586
Income tax effect related to items of other comprehensive income	(980 )	(555 )
Total other comprehensive income, net of tax	1,822	1,031
Total comprehensive income	\$4,171	\$2,522
See notes to unaudited consolidated financial statements.		

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MidSouth Bancorp, Inc. and Subsidiaries  
 Consolidated Statement of Shareholders' Equity (unaudited)  
 For the Three Months Ended March 31, 2016  
 (in thousands, except share and per share data)

	Preferred Stock		Common Stock		Additional Paid-in Capital	Unearned ESOP Shares	Accumulated Other Comprehensive Income	Retained Earnings	Total
	Shares	Amount	Shares	Amount					
Balance - December 31, 2015	123,200	\$41,120	11,362,150	\$1,136	\$110,771	\$(1,093)	\$509	\$60,694	\$213,137
Net earnings	—	—	—	—	—	—	—	2,349	2,349
Dividends on Series B and Series C preferred stock	—	—	—	—	—	—	—	(427)	(427)
Dividends on common stock, \$0.09 per share	—	—	—	—	—	—	—	(1,023)	(1,023)
Increase in ESOP obligation, net of repayments	—	—	—	—	—	(191)	—	—	(191)
Tax benefit resulting from distribution from Directors	—	—	—	—	39	—	—	—	39
Deferred Compensation Plan Stock option and restricted stock compensation expense	—	—	—	—	97	—	—	—	97
ESOP compensation expense	—	—	—	—	(36)	—	—	—	(36)
Tax benefit for dividends paid to the ESOP	—	—	—	—	87	—	—	—	87
Change in accumulated other comprehensive income	—	—	—	—	—	—	1,822	—	1,822
Balance – March 31, 2016	123,200	\$41,120	11,362,150	\$1,136	\$110,958	\$(1,284)	\$2,331	\$61,593	\$215,854

See notes to unaudited consolidated financial statements.

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MidSouth Bancorp, Inc. and Subsidiaries  
Consolidated Statements of Cash Flows (unaudited)  
(in thousands)

	For the Three Months Ended March 31,	
	2016	2015
Cash flows from operating activities:		
Net earnings	\$2,349	\$1,491
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation	1,512	1,555
Accretion of purchase accounting adjustments	(288)	(189)
Provision for loan losses	2,800	6,000
Deferred tax benefit	(503)	(1,951)
Amortization of premiums on securities, net	681	633
Stock option expense	84	85
Restricted stock expense	13	—
Excess of book value over market value of ESOP shares released	(36)	—
Net gain on sale of investment securities	—	(115)
Net loss (gain) on sale of other real estate owned	24	(50)
Net write down of other real estate owned	120	29
Net gain on sale/disposal of premises and equipment	(14)	(1)
Change in accrued interest receivable	(135)	(106)
Change in accrued interest payable	(9)	(4)
Change in other assets & other liabilities, net	454	1,684
Net cash provided by operating activities	7,052	9,061
Cash flows from investing activities:		
Proceeds from maturities and calls of securities available-for-sale	18,379	17,988
Proceeds from maturities and calls of securities held-to-maturity	2,919	3,326
Proceeds from sale of securities available-for-sale	—	34,509
Purchases of securities available-for-sale	—	(73,853)
Proceeds from sale of other investments	—	349
Purchases of other investments	(7)	(3)
Net change in loans	12,293	(28,461)
Purchases of premises and equipment	(915)	(1,362)
Proceeds from sale of premises and equipment	40	4
Proceeds from sale of other real estate owned	245	532
Net cash provided by (used in) investing activities	32,954	(46,971)
Cash flows from financing activities:		
Change in deposits	7,366	30,901
Change in securities sold under agreements to repurchase	1,922	25,248
Borrowings on Federal Home Loan Bank advances	25,000	25,000
Repayments of Federal Home Loan Bank advances	(50,017)	(25,015)
Proceeds and tax benefit from exercise of stock options	—	80
Tax benefit resulting from distribution from Directors Deferred Compensation Plan	39	420
Tax benefit for dividends paid to ESOP	87	—
Payment of dividends on preferred stock	(171)	(174)
Payment of dividends on common stock	(1,023)	(1,020)

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Net cash (used in) provided by financing activities	(16,797 )	55,440
Net increase in cash and cash equivalents	23,209	17,530
Cash and cash equivalents, beginning of period	89,201	86,872
Cash and cash equivalents, end of period	\$ 112,410	\$ 104,402
Supplemental cash flow information:		
Interest paid	\$ 1,429	\$ 1,427
Noncash investing and financing activities:		
Transfer of loans to other real estate	110	866
Change in accrued common stock dividends	—	1
Change in accrued preferred stock dividends	256	—
Net change in loan to ESOP	(191 )	(268 )

See notes to unaudited consolidated financial statements.

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MidSouth Bancorp, Inc. and Subsidiaries  
Notes to Interim Consolidated Financial Statements  
March 31, 2016  
(Unaudited)

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 (“GAAP”), the financial position of MidSouth Bancorp, Inc. (the “Company”) and its subsidiaries as of March 31, 2016 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 2015 Annual Report on Form 10-K.

The results of operations for the three-month period ended March 31, 2016 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 GAAP 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.

Summary of Significant Accounting Policies — The accounting and reporting policies of the Company conform with GAAP and general practices within the banking industry. There have been no material changes or developments in the application of accounting principles or in our evaluation of the accounting estimates and the underlying assumptions or methodologies that we believe to be Critical Accounting Policies and Estimates as disclosed in our 2015 Annual Report on Form 10-K.

Recent Accounting Pronouncements — ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities is the first ASU issued under the FASB's financial instruments project. ASU 2016-01 primarily affects the accounting for equity investments, financial liabilities under the fair value option, and the presentation and disclosure requirements for financial instruments. The guidance in this ASU requires all equity securities with readily determinable fair values to be measured at fair value on the balance sheet, with changes in fair value recorded through earnings. For financial liabilities that are measured at fair value in accordance with the fair value option, the guidance requires changes in the fair value of a financial liabilities attributable to a change in instrument-specific credit risk to be recorded separately in other comprehensive income. This ASU eliminates the requirement to disclose the methods and significant assumptions used to estimate fair value. It does require public entities to use the exit price when measuring the fair value of financial instruments measured at amortized cost for disclosure purposes. In addition, the new guidance requires financial assets and financial liabilities to be presented separately in the notes to the financial statements, grouped by measurement category and form of financial asset. The effective date of this Update is for fiscal years beginning on or after December 15, 2017. The Company is evaluating the impact, if any, that ASU 2016-01 will have on its financial position, results of operations, and its financial statement disclosures.

ASU 2016-02, Leases (Topic 842) was issued with the intention of improving financial reporting about leasing transactions. Under the new guidance, a lessee will be required to recognize assets and liabilities for leases with lease terms of more than 12 months. Consistent with current GAAP, the recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease. However, unlike current GAAP - which requires only capital leases to be recognized on the balance

sheet - the guidance in the ASU will require both types of leases to be recognized on the balance sheet. The ASU also will require disclosures to help investors and other financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. These disclosures include qualitative and quantitative requirements, providing additional information about the amounts recorded in the financial statements. The effective date of this Update is for fiscal years beginning on or after December 15, 2018. The Company is evaluating the impact that ASU 2016-02 will have on its financial position, results of operations, and its financial statement disclosures.

ASU 2016-09, Compensation - Stock Compensation (Topic 718) was issued as part of the FASB's simplification initiative. Under the new guidance, several aspects of the accounting for share-based payment award transactions are simplified, including: (a) income tax consequences; (b) classification of awards as either equity or liabilities; and (c) classification on the statement of cash flows. The effective date of this Update is for fiscal years beginning on or after December 15, 2016. The Company is evaluating the impact that ASU 2016-09 will have on its financial position, results of operations, and its financial statement disclosures.

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## 2. Investment Securities

The portfolio of investment securities consisted of the following (in thousands):

	March 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Obligations of state and political subdivisions	\$23,624	\$ 625	\$ 10	\$24,239
GSE mortgage-backed securities	81,030	2,890	24	83,896
Collateralized mortgage obligations: residential	187,859	871	744	187,986
Collateralized mortgage obligations: commercial	3,951	—	43	3,908
Mutual funds	2,100	22	—	2,122
	\$298,564	\$ 4,408	\$ 821	\$302,151

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
Obligations of state and political subdivisions	\$30,750	\$ 770	\$ 27	\$31,493
GSE mortgage-backed securities	84,946	2,321	229	87,038
Collateralized mortgage obligations: residential	194,067	297	2,276	192,088
Collateralized mortgage obligations: commercial	5,512	1	65	5,448
Mutual funds	2,100	—	8	2,092
	\$317,375	\$ 3,389	\$ 2,605	\$318,159

	March 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Held-to-maturity:				
Obligations of state and political subdivisions	\$43,430	\$ 935	\$ 4	\$44,361
GSE mortgage-backed securities	53,423	1,256	12	54,667
Collateralized mortgage obligations: residential	10,429	—	193	10,236
Collateralized mortgage obligations: commercial	6,341	26	—	6,367
	\$113,623	\$ 2,217	\$ 209	\$115,631

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Held-to-maturity:				
Obligations of state and political subdivisions	\$43,737	\$ 697	\$ 6	\$44,428
GSE mortgage-backed securities	55,696	705	131	56,270
Collateralized mortgage obligations: residential	10,803	—	361	10,442
Collateralized mortgage obligations: commercial	6,556	2	—	6,558
	\$116,792	\$ 1,404	\$ 498	\$117,698



With the exception of two private-label collateralized mortgage obligations (“CMOs”) with a combined balance remaining of \$23,000 at March 31, 2016, all of the Company’s CMOs are government-sponsored enterprise (“GSE”) securities.

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The amortized cost and fair value of debt securities at March 31, 2016 by contractual maturity are shown in the following table (in thousands) with the exception of other asset-backed securities, mortgage-backed securities, CMOs, and the collateralized debt obligation. Expected maturities may differ from contractual maturities for mortgage-backed securities and CMOs because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Available-for-sale:		
Due in one year or less	\$ 2,249	\$ 2,276
Due after one year through five years	17,887	18,379
Due after five years through ten years	2,871	2,973
Due after ten years	617	611
Mortgage-backed securities and collateralized mortgage obligations:		
Residential	268,889	271,882
Commercial	3,951	3,908
Mutual funds	2,100	2,122
	\$ 298,564	\$ 302,151

	Amortized Cost	Fair Value
Held-to-maturity:		
Due in one year or less	\$ 479	\$ 479
Due after one year through five years	3,454	3,501
Due after five years through ten years	11,390	11,691
Due after ten years	28,107	28,690
Mortgage-backed securities and collateralized mortgage obligations:		
Residential	63,852	64,903
Commercial	6,341	6,367
	\$ 113,623	\$ 115,631

Details concerning investment securities with unrealized losses are as follows (in thousands):

	March 31, 2016		March 31, 2016		Total	
	Securities with losses under 12 months		Securities with losses over 12 months		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Available-for-sale:						
Obligations of state and political subdivisions	\$ 597	\$ 4	\$ 610	\$ 6	\$ 1,207	\$ 10
GSE mortgage-backed securities	11,054	24	—	—	11,054	24
Collateralized mortgage obligations: residential	56,918	269	26,003	475	82,921	744
Collateralized mortgage obligations: commercial	1,236	2	2,673	41	3,909	43
	\$ 69,805	\$ 299	\$ 29,286	\$ 522	\$ 99,091	\$ 821



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	December 31, 2015					
	Securities with losses under 12 months		Securities with losses over 12 months		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Available-for-sale:						
Obligations of state and political subdivisions	\$1,192	\$ 27	\$—	\$ —	\$1,192	\$ 27
GSE mortgage-backed securities	21,607	229	—	—	21,607	229
Collateralized mortgage obligations: residential	140,999	1,207	30,029	1,069	171,028	2,276
Collateralized mortgage obligations: commercial	—	—	2,946	65	2,946	65
Other asset-backed securities	2,092	8	—	—	2,092	8
	\$165,890	\$ 1,471	\$32,975	\$ 1,134	\$198,865	\$ 2,605

	March 31, 2016					
	Securities with losses under 12 months		Securities with losses over 12 months		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Held-to-maturity:						
Obligations of state and political subdivisions	\$—	\$ —	\$505	\$ 4	\$505	\$ 4
GSE mortgage-backed securities	6,915	12	—	—	6,915	12
Collateralized mortgage obligations: residential	—	—	10,235	193	10,235	193
	\$6,915	\$ 12	\$10,740	\$ 197	\$17,655	\$ 209

	December 31, 2015					
	Securities with losses under 12 months		Securities with losses over 12 months		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Held-to-maturity:						
Obligations of state and political subdivisions	\$541	\$ 1	\$505	\$ 5	\$1,046	\$ 6
GSE mortgage-backed securities	—	—	7,021	131	7,021	131
Collateralized mortgage obligations: residential	—	—	10,442	361	10,442	361
	\$541	\$ 1	\$17,968	\$ 497	\$18,509	\$ 498

Management evaluates each quarter whether unrealized losses on securities represent impairment that is other than temporary. For debt securities, the Company considers its intent to sell the securities or if it is more likely than not the Company will be required to sell the securities. If such impairment is identified, based upon the intent to sell or the more likely than not threshold, the carrying amount of the security is reduced to fair value with a charge to earnings. Upon the result of the aforementioned review, management then reviews for potential other than temporary impairment based upon other qualitative factors. In making this evaluation, management considers changes in market rates relative to those available when the security was acquired, changes in market expectations about the timing of cash flows from securities that can be prepaid, performance of the debt security, and changes in the market's

perception of the issuer's financial health and the security's credit quality. If determined that a debt security has incurred other than temporary impairment, then the amount of the credit related impairment is determined. If a credit loss is evident, the amount of the credit loss is charged to earnings and the non-credit related impairment is recognized through other comprehensive income.

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As of March 31, 2016, 32 securities had unrealized losses totaling 0.87% of the individual securities' amortized cost basis and 0.25% of the Company's total amortized cost basis. Of the 32 securities, 15 had been in an unrealized loss position for over twelve months at March 31, 2016. These 15 securities had an amortized cost basis and unrealized loss of \$40.7 million and \$719,000, respectively. The unrealized losses on debt securities at March 31, 2016 resulted from changing market interest rates over the yields available at the time the underlying securities were purchased. Management identified no impairment related to credit quality. At March 31, 2016, management had the intent and ability to hold impaired securities and no impairment was evaluated as other than temporary. As a result, no other than temporary impairment losses were recognized during the three months ended March 31, 2016.

During the three months ended March 31, 2016, the Company did not sell any securities. During the three months ended March 31, 2015, the Company sold 18 securities classified as available-for-sale at a net gain of \$115,000. Of the 18 securities sold, 8 were sold with gains totaling \$250,000 and 10 securities were sold at a loss of \$135,000.

Securities with an aggregate carrying value of approximately \$321.1 million and \$285.4 million at March 31, 2016 and December 31, 2015, respectively, were pledged to secure public funds on deposit and for other purposes required or permitted by law.

### 3. Credit Quality of Loans and Allowance for Loan Losses

The loan portfolio consisted of the following (in thousands):

	March 31, 2016	December 31, 2015
Commercial, financial and agricultural	\$441,160	\$454,028
Real estate - construction	84,790	74,952
Real estate – commercial	467,648	471,141
Real estate – residential	149,961	149,064
Installment loans to individuals	103,181	111,009
Lease financing receivable	1,590	1,968
Other	1,719	1,483
	1,250,049	1,263,645
Less allowance for loan losses	(20,347 )	(19,011 )
	\$1,229,702	\$1,244,634

The Company monitors loan concentrations and evaluates individual customer and aggregate industry leverage, profitability, risk rating distributions, and liquidity for each major standard industry classification segment. At March 31, 2016, one industry segment concentration, the oil and gas industry, constituted more than 10% of the loan portfolio. The Company's exposure in the oil and gas industry, including related service and manufacturing industries, totaled approximately \$252.5 million, or 20.2% of total loans. Additionally, the Company's exposure to loans secured by commercial real estate is monitored. At March 31, 2016, loans secured by commercial real estate (including commercial construction, farmland and multifamily loans) totaled approximately \$532.5 million. Of the \$532.5 million, \$467.6 million represent CRE loans, 54% of which are secured by owner-occupied commercial properties. Of the \$532.5 million in loans secured by commercial real estate, \$26.0 million, or 4.9%, were on nonaccrual status at March 31, 2016.

#### Allowance for Loan Losses

The allowance for loan losses is a valuation account available to absorb probable losses on loans. All losses are charged to the allowance for loan losses when the loss actually occurs or when a determination is made that a loss is

likely to occur. Recoveries are credited to the allowance for loan losses at the time of recovery. Quarterly, the probable level of losses in the existing portfolio is estimated through consideration of various factors. Based on these estimates, the allowance for loan losses is increased by charges to earnings and decreased by charge offs (net of recoveries).

The allowance is composed of general reserves and specific reserves. General reserves are determined by applying loss percentages to segments of the portfolio. The loss percentages are based on each segment's historical loss experience, generally over the past twelve to eighteen months, and adjustment factors derived from conditions in the Company's internal and external environment. All loans considered to be impaired are evaluated on an individual basis to determine specific reserve allocations in accordance with GAAP. Loans for which specific reserves are provided are excluded from the calculation of general reserves.

Loans acquired in business combinations are initially recorded at fair value, which includes an estimate of credit losses expected to be realized over the remaining lives of the loans, and therefore no corresponding allowance for loan losses is recorded for these loans at

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acquisition. Methods utilized to estimate any subsequently required allowance for loan losses for acquired loans not deemed credit-impaired at acquisition are similar to originated loans; however, the estimate of loss is based on the unpaid principal balance and then compared to any remaining unaccreted purchase discount. To the extent that the calculated loss is greater than the remaining unaccreted purchase discount, an allowance is recorded for such difference.

The Company has an internal loan review department that is independent of the lending function to challenge and corroborate the loan grade assigned by the lender and to provide additional analysis in determining the adequacy of the allowance for loan losses.

A rollforward of the activity within the allowance for loan losses by loan type and recorded investment in loans for the three months ended March 31, 2016 and 2015 is as follows (in thousands):

	March 31, 2016							Total
	Coml, Fin, and Agric	Real Estate Construc-tion	Commercial	Residential	Installment loans to individuals	Lease financing receivable	Other	
Allowance for loan losses:								
Beginning balance	\$ 11,268	\$ 819	\$ 4,614	\$ 816	\$ 1,468	\$ 14	\$ 12	\$ 19,011
Charge-offs	(1,307 )	—	—	(4 )	(283 )	—	—	(1,594 )
Recoveries	26	—	76	3	25	—	—	130
Provision	2,194	(420 )	861	(170 )	336	(3 )	2	2,800
Ending balance	\$ 12,181	\$ 399	\$ 5,551	\$ 645	\$ 1,546	\$ 11	\$ 14	\$ 20,347
Ending balance: individually evaluated for impairment	\$ 1,021	\$ —	\$ 2,586	\$ 267	\$ 278	\$ —	\$ —	\$ 4,152
Ending balance: collectively evaluated for impairment	\$ 11,160	\$ 399	\$ 2,965	\$ 378	\$ 1,268	\$ 11	\$ 14	\$ 16,195
Loans:								
Ending balance	\$ 441,160	\$ 84,790	\$ 467,648	\$ 149,961	\$ 103,181	\$ 1,590	\$ 1,719	\$ 1,250,049
Ending balance: individually evaluated for impairment	\$ 29,097	\$ 35	\$ 27,511	\$ 2,230	\$ 506	\$ —	\$ —	\$ 59,379
Ending balance: collectively evaluated for impairment	\$ 412,063	\$ 84,755	\$ 439,530	\$ 147,653	\$ 102,675	\$ 1,590	\$ 1,719	\$ 1,189,985
Ending balance: loans acquired with deteriorated credit quality	\$ —	\$ —	\$ 607	\$ 78	\$ —	\$ —	\$ —	\$ 685



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March 31, 2015

## Real Estate

	Coml, Fin, and Agric	Constr-uct	Com	Commercial Residential	Installment loans to individuals	Lease financing receivable	Other	Total
Allowance for loan losses:								
Beginning balance	\$5,729	\$954	\$2,402	\$810	\$1,311	\$16	\$4	\$11,226
Charge-offs	(1,001 )	(6 )	—	(2 )	(323 )	—	—	(1,332 )
Recoveries	132	—	6	2	26	—	—	166
Provision	5,523	3	202	7	260	4	1	6,000
Ending balance	\$10,383	\$951	\$2,610	\$817	\$1,274	\$20	\$5	\$16,060
Ending balance: individually evaluated for impairment	\$737	\$—	\$645	\$57	\$206	\$—	\$—	\$1,645
Ending balance: collectively evaluated for impairment	\$9,646	\$951	\$1,965	\$760	\$1,068	\$20	\$5	\$14,415
Loans:								
Ending balance	\$484,508	\$76,964	\$471,737	\$153,647	\$115,284	\$6,350	\$2,439	\$1,310,929
Ending balance: individually evaluated for impairment	\$2,427	\$477	\$7,977	\$1,471	\$405	\$—	\$—	\$12,757
Ending balance: collectively evaluated for impairment	\$482,081	\$76,487	\$463,106	\$152,087	\$114,879	\$6,350	\$2,439	\$1,297,429
Ending balance: loans acquired with deteriorated credit quality	\$—	\$—	\$654	\$89	\$—	\$—	\$—	\$743

## Non-Accrual and Past Due Loans

Loans are considered past due if the required principal and interest payment have not been received as of the date such payments were due. Loans are placed on non-accrual status when, in management's opinion, the probability of collection of interest is deemed insufficient to warrant further accrual. For loans placed on non-accrual status, the accrual of interest is discontinued and subsequent payments received are applied to the principal balance. Interest income is recorded after principal has been satisfied and as payments are received. Non-accrual loans may be returned to accrual status if all principal and interest amounts contractually owed are reasonably assured of repayment within a reasonable period and there is a period of at least six months to one year of repayment performance by the borrower depending on the contractual payment terms.

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An age analysis of past due loans (including both accruing and non-accruing loans) is as follows (in thousands):

March 31, 2016							
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Current	Total Loans	Recorded Investment > 90 days and Accruing
Commercial, financial, and agricultural	\$6,021	\$1,922	\$24,116	\$32,059	\$409,101	\$441,160	\$ 204
Commercial real estate - construction	260	—	11	271	64,549	64,820	—
Commercial real estate - other	10,754	—	16,275	27,029	440,619	467,648	—
Residential - construction	1,468	—	—	1,468	18,502	19,970	—
Residential - prime	1,046	97	1,625	2,768	147,193	149,961	—
Consumer - credit card	37	17	16	70	5,648	5,718	16
Consumer - other	625	306	478	1,409	96,054	97,463	38
Lease financing receivable	—	—	—	—	1,590	1,590	—
Other loans	66	3	—	69	1,650	1,719	—
	\$20,277	\$2,345	\$42,521	\$65,143	\$1,184,906	\$1,250,049	\$ 258
December 31, 2015							
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Current	Total Loans	Recorded Investment > 90 days and Accruing
Commercial, financial, and agricultural	\$1,362	\$2,317	\$25,696	\$29,375	\$424,653	\$454,028	\$ 59
Commercial real estate - construction	1,047	—	12	1,059	55,839	56,898	—
Commercial real estate - other	1,164	514	19,512	21,190	449,951	471,141	—
Residential - construction	—	—	—	—	18,054	18,054	—
Residential - prime	1,703	367	1,563	3,633	145,431	149,064	19
Consumer - credit card	38	25	22	85	5,970	6,055	22
Consumer - other	984	219	387	1,590	103,364	104,954	47
Lease financing receivable	—	—	—	—	1,968	1,968	—
Other loans	101	4	—	105	1,378	1,483	—
	\$6,399	\$3,446	\$47,192	\$57,037	\$1,206,608	\$1,263,645	\$ 147

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Non-accrual loans are as follows (in thousands):

	March 31, December 31,	
	2016	2015
Commercial, financial, and agricultural	\$ 24,900	\$ 27,705
Commercial real estate – construction	35	37
Commercial real estate - other	25,951	19,907
Residential - construction	—	—
Residential - prime	2,322	1,998
Consumer - credit card	—	—
Consumer - other	506	404
Lease financing receivable	—	—
Other	—	—
	\$ 53,714	\$ 50,051

The amount of interest that would have been recorded on non-accrual loans, had the loans not been classified as non-accrual, totaled approximately \$757,000 and \$342,000 for the three months ended March 31, 2016 and 2015, respectively. Interest actually received on non-accrual loans subsequent to their transfer to non-accrual status totaled at March 31, 2016 and 2015 was \$59,000 and \$11,000, respectively.

**Impaired Loans**

Loans are considered impaired when, based upon current information, it is probable the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. All loans classified as special mention, substandard, or doubtful, based on credit risk rating factors, are reviewed to determine whether impairment testing is appropriate. An allowance for each impaired loan is calculated based on the present value of expected future cash flows discounted at the loan's effective interest rate or at the loan's observable market price or the fair value of the collateral if the loan is collaterally dependent. All impaired loans are reviewed, at a minimum, on a quarterly basis. Existing valuations are reviewed to determine if additional discounts or new appraisals are required. After this review, when comparing the resulting collateral valuation to the outstanding loan balance, if the discounted collateral value exceeds the loan balance no specific allocation is reserved. Acquired impaired loans are generally not subject to individual evaluation for impairment and are not reported with impaired loans or troubled debt restructurings, even if they would otherwise qualify for such treatment.

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Loans that are individually evaluated for impairment are as follows (in thousands):

	March 31, 2016				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial, financial, and agricultural	\$26,064	\$ 26,328	\$ —	\$ 24,297	\$ 267
Commercial real estate – construction	35	35	—	36	—
Commercial real estate – other	7,564	7,564	—	6,725	45
Residential – prime	1,181	1,201	—	1,273	10
Consumer – other	24	24	—	29	—
Subtotal:	34,868	35,152	—	32,360	322
With an allowance recorded:					
Commercial, financial, and agricultural	3,033	3,033	1,021	4,111	374
Commercial real estate – other	19,947	19,947	2,586	16,976	208
Residential – prime	1,049	1,049	267	794	7
Consumer – other	482	496	278	426	5
Subtotal:	24,511	24,525	4,152	22,307	594
Totals:					
Commercial	56,643	56,907	3,607	52,145	894
Residential	2,230	2,250	267	2,067	17
Consumer	506	520	278	455	5
Grand total:	\$59,379	\$ 59,677	\$ 4,152	\$ 54,667	\$ 916

	December 31, 2015				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial, financial, and agricultural	\$22,529	\$ 22,793	\$ —	\$ 11,484	\$ 745
Commercial real estate – construction	37	37	—	45	—
Commercial real estate – other	5,886	5,886	—	3,903	97
Residential – prime	1,365	1,385	—	954	17
Consumer – other	34	34	—	56	—
Subtotal:	29,851	30,135	—	16,442	859
With an allowance recorded:					
Commercial, financial, and agricultural	5,189	6,373	961	3,704	138
Commercial real estate – other	14,004	14,004	1,585	9,236	161
Residential – prime	538	538	160	533	7
Consumer – other	370	384	221	334	8
Subtotal:	20,101	21,299	2,927	13,807	314
Totals:					
Commercial	47,645	49,093	2,546	28,372	1,141
Residential	1,903	1,923	160	1,487	24
Consumer	404	418	221	390	8
Grand total:	\$49,952	\$ 51,434	\$ 2,927	\$ 30,249	\$ 1,173

Credit Quality



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The Company manages credit risk by observing written underwriting standards and lending policy established by the Board of Directors and management to govern all lending 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 a 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.

Loans can be classified into the following three risk rating grades: pass, special mention, and substandard/doubtful. Factors considered in determining a risk rating grade include debt service capacity, capital structure/liquidity, management, collateral quality, industry risk, company trends/operating performance, repayment source, revenue diversification/customer concentration, quality of financial information, and financing alternatives. Pass grade signifies the highest quality of loans to loans with reasonable credit risk, which may include borrowers with marginally adequate financial performance, but have the ability to repay the debt. Special mention loans have potential weaknesses that warrant extra attention from the loan officer and other management personnel, but still have the ability to repay the debt. Substandard classification includes loans with well-defined weaknesses with risk of potential loss. Loans classified as doubtful are considered to have little recovery value and are charged off.

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The following tables present the classes of loans by risk rating (in thousands):

March 31, 2016

Commercial Credit Exposure  
Credit Risk Profile by  
Creditworthiness Category

	Commercial, financial, and agricultural	Commercial real estate - construction	Commercial real estate - other	Total	% of Total	
Pass	\$368,557	\$ 64,602	\$ 406,237	\$839,396	86.22	%
Special mention	24,933	99	24,759	49,791	5.11	%
Substandard	47,466	119	36,652	84,237	8.65	%
Doubtful	204	—	—	204	0.02	%
	\$441,160	\$ 64,820	\$ 467,648	\$973,628	100.00	%

Residential Credit Exposure  
Credit Risk Profile by  
Creditworthiness Category

	Residential - construction	Residential - prime	Total	% of Total	
Pass	\$ 19,970	\$ 145,302	\$165,272	97.26	%
Special mention	—	1,122	1,122	0.66	%
Substandard	—	3,537	3,537	2.08	%
	\$ 19,970	\$ 149,961	\$169,931	100.00	%

Consumer and Commercial Credit Exposure  
Credit Risk Profile Based on  
Payment Activity

	Consumer - credit card	Consumer - other	Lease financing receivable	Other	Total	% of Total	
Performing	\$ 5,702	\$96,919	\$ 1,590	\$ 1,719	\$105,930	99.47	%
Nonperforming	16	544	—	—	560	0.53	%
	\$ 5,718	\$97,463	\$ 1,590	\$ 1,719	\$106,490	100.00	%

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December 31, 2015

Commercial Credit Exposure  
Credit Risk Profile by  
Creditworthiness Category

	Commercial, financial, and agricultural	Commercial real estate - construction	Commercial real estate - other	Total	% of Total
Pass	\$ 383,897	\$ 56,740	\$ 412,141	\$852,778	86.84 %
Special mention	32,506	34	28,217	60,757	6.18 %
Substandard	37,353	124	30,783	68,260	6.95 %
Doubtful	272	—	—	272	0.03 %
	\$ 454,028	\$ 56,898	\$ 471,141	\$982,067	100.00%

Residential Credit Exposure  
Credit Risk Profile by  
Creditworthiness Category

	Residential - construction	Residential - prime	Total	% of Total
Pass	\$ 18,054	\$ 144,704	\$162,758	97.39 %
Special mention	—	1,225	1,225	0.73 %
Substandard	—	3,135	3,135	1.88 %
	\$ 18,054	\$ 149,064	\$167,118	100.00%

Consumer and Commercial Credit Exposure  
Credit Risk Profile Based on  
Payment Activity

	Consumer - credit card	Consumer - other	Lease financing receivable	Other	Total	% of Total
Performing	\$6,033	\$ 104,503	\$ 1,968	\$ 1,483	\$113,987	99.59 %
Nonperforming	22	451	—	—	473	0.41 %
	\$6,055	\$ 104,954	\$ 1,968	\$ 1,483	\$114,460	100.00%

## Troubled Debt Restructurings

A troubled debt restructuring (“TDR”) is a restructuring of a debt made by the Company to a debtor for economic or legal reasons related to the debtor’s financial difficulties that it would not otherwise consider. The Company grants the concession in an attempt to protect as much of its investment as possible.

Information about the Company’s TDRs is as follows (in thousands):



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	March 31, 2016			
	Current	Past Due Greater Than 30 Days	Nonaccrual TDRs	Total TDRs
Commercial, financial and agricultural	\$ 16	\$ 3,943	\$ 20,708	\$ 24,667
Real estate - commercial	1,716	—	—	1,716
	\$ 1,732	\$ 3,943	\$ 20,708	\$ 26,383
	December 31, 2015			
	Current	Past Due Greater Than 30 Days	Nonaccrual TDRs	Total TDRs
Commercial, financial and agricultural	\$ 16	\$ —	\$ 20,865	\$ 20,881
Real estate - commercial	—	148	—	148
	\$ 16	\$ 148	\$ 20,865	\$ 21,029

During the three months ended March 31, 2016, one loan relationship with a pre-modification balance of \$5.5 million was identified as a TDR after conversion of the loans to interest only for a limited amount of time. Subsequent to its conversion to TDR status, this one relationship totaling \$5.5 million defaulted on the modified terms during the three months ended March 31, 2016. During the three months ended March 31, 2015, there were no loans identified as a TDR, and there were no defaults on any loans that were modified as TDRs during the preceding twelve months. For purposes of the determination of an allowance for loan losses on these TDRs, as an identified TDR, the Company considers a loss probable on the loan and, as a result is reviewed for specific impairment in accordance with the Company's allowance for loan loss methodology. If it is determined losses are probable on such TDRs, either because of delinquency or other credit quality indicator, the Company establishes specific reserves for these loans. As of March 31, 2016, there were no commitments to lend additional funds to debtors owing sums to the Company whose terms have been modified in TDRs.

## 4. Intangibles

A summary of core deposit intangible assets as of March 31, 2016 and December 31, 2015 is as follows (in thousands):

	March 31, December 31,	
	2016	2015
Gross carrying amount	\$ 11,674	\$ 11,674
Less accumulated amortization	(6,223 )	(5,946 )
Net carrying amount	\$ 5,451	\$ 5,728

## 5. Other Comprehensive Income

The following is a summary of the tax effects allocated to each component of other comprehensive income (in thousands):

	Three Months Ended March 31,	
	2016	2015

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	Before Tax Amount	Tax Effect	Net of Tax Amount	Before Tax Amount	Tax Effect	Net of Tax Amount
Other comprehensive income:						
Securities available-for-sale:						
Change in unrealized gains during period	\$2,802	\$(980)	\$1,822	\$1,701	\$(595)	\$1,106
Reclassification adjustment for gains included in net income	—	—	—	(115 )	40	(75 )
Total other comprehensive income	\$2,802	\$(980)	\$1,822	\$1,586	\$(555)	\$1,031

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The reclassifications out of accumulated other comprehensive income into net income are presented below (in thousands):

	Three Months Ended March 31,	
	2016	2015
Details about	Reclassifications	Reclassifications
Accumulated Other	Out	Out of
Comprehensive Income	of	Accumulated
Components	Income Statement	Income Statement
	Accumulated	Other Line Item
	Other	Comprehensive
	Comprehensive	Income
	Income	
Unrealized gains and losses on securities available-for-sale:		
	\$ Gain on sale of securities, net	\$(115) Gain on sale of securities, net
	—Tax expense	40 Tax expense
	\$ Net of tax	\$(75 ) Net of tax

## 6. Earnings Per Common Share

Following is a summary of the information used in the computation of earnings per common share (in thousands):

	Three Months Ended March 31,	
	2016	2015
Net earnings available to common shareholders	\$1,922	\$1,318
Dividends on Series C preferred stock	—	—
Adjusted net earnings available to common shareholders	\$1,922	\$1,318
Weighted average number of common shares outstanding used in computation of basic earnings per common share	11,262	11,318
Effect of dilutive securities:		
Stock options	—	29
Convertible preferred stock and warrants	—	4
Weighted average number of common shares outstanding plus effect of dilutive securities – used in computation of diluted earnings per share	11,262	11,351

Options and warrants on 448,760 shares of common stock and 11,250 shares of restricted stock were not included in computing diluted earnings per share for the quarter ended March 31, 2016 because the effects of these shares were anti-dilutive. Options to acquire 134,822 shares of common stock were not included in computing diluted earnings per share for the quarter ended March 31, 2015 because the effects of these shares were anti-dilutive. 507,072 and 518,086 shares issuable upon the conversion of outstanding convertible preferred stock were anti-dilutive and not included in the computation of diluted earnings per shares for the three months ended March 31, 2016 and 2015, respectively.

## 7. Fair Value Measurement

The Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

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Following is a description of valuation methodologies used for assets and liabilities which are either recorded or disclosed at fair value.

**Cash and Due From Banks, Interest-Bearing Deposits in Banks and Federal Funds Sold**—The carrying value of these short-term instruments is a reasonable estimate of fair value.

**Securities Available-for-Sale**—Securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange and U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter market funds. Securities are classified as Level 2 within the valuation hierarchy when the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the bond's terms and conditions, among other things. Level 2 inputs are used to value U.S. Agency securities, mortgage-backed securities, asset-backed securities, municipal securities, single issue trust preferred securities, certain pooled trust preferred securities, collateralized debt obligations and certain equity securities that are not actively traded.

**Securities Held-to-Maturity**—The fair value of securities held-to-maturity is estimated using the same measurement techniques as securities available-for-sale.

**Other Investments**—The carrying value of other investments is a reasonable estimate of fair value.

**Loans**—For disclosure purposes, the fair value of fixed rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings. For variable rate loans, the carrying amount is a reasonable estimate of fair value. The Company does not record loans at fair value on a recurring basis. No adjustment to fair value is taken related to illiquidity discounts. However, from time to time, a loan is considered impaired and an allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management uses one of three methods to measure impairment, which, include collateral value, market value of similar debt, and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. Impaired loans where an allowance is established based on the fair value of collateral or where the loan balance has been charged down to fair value require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and adjusts the appraisal value by taking an additional discount for market conditions and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3.

For non-performing loans, collateral valuations currently in file are reviewed for acceptability in terms of timeliness and applicability. Although each determination is made based on the facts and circumstances of each credit, generally valuations are no longer considered acceptable when there has been physical deterioration of the property from when it was last appraised, or there has been a significant change in the underlying assumptions of the appraisal. If the valuation is deemed to be unacceptable, a new appraisal is ordered. New appraisals are typically received within 4-6 weeks. While awaiting new appraisals, the valuation in the file is utilized, net of discounts. Discounts are derived from available relevant market data, selling costs, taxes, and insurance. Any perceived collateral deficiency utilizing

the discounted value is specifically reserved (as required by ASC Topic 310) until the new appraisal is received or charged off. Thus, provisions or charge-offs are recognized in the period the credit is identified as non-performing.

The following sources are utilized to set appropriate discounts: in-market real estate agents, current local sales data, bank history for devaluation of similar property, Sheriff's valuations and buy/sell contracts. If a real estate agent is used to market and sell the property, values are discounted 10% for selling costs. Additional discounts may be applied if research from the above sources indicates a discount is appropriate given devaluation of similar property from the time of the initial valuation.

Other Real Estate—Other real estate (“ORE”) properties are adjusted to fair value upon transfer of the loans to other real estate, and annually thereafter to insure other real estate assets are carried at the lower of carrying value or fair value. Exceptions to obtaining initial appraisals are properties where a buy/sell agreement exists for the loan value or greater, or where a Sheriff's valuation has been received for properties liquidated through a Sheriff sale. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the ORE as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and adjusts the appraisal value by taking an additional discount for market conditions and there is no observable market prices, the Company records the ORE asset as nonrecurring Level 3.

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Cash Surrender Value of Life Insurance Policies—Fair value for life insurance cash surrender value is based on cash surrender values indicated by the insurance companies.

Deposits—The fair value of demand deposits, savings accounts, NOW accounts, and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities. The estimated fair value does not include customer related intangibles.

Securities Sold Under Agreements to Repurchase—The fair value approximates the carrying value of securities sold under agreements to repurchase due to their short-term nature.

Short-term Federal Home Loan Bank Advances—The fair value approximates the carrying value of short-term FHLB advances due to their short-term nature.

Long-term Federal Home Loan Bank Advances—The fair value of long-term FHLB advances is estimated using a discounted cash flow analysis that applies interest rates currently being offered on similar types of borrowings with similar terms.

Junior Subordinated Debentures—For junior subordinated debentures that bear interest on a floating basis, the carrying amount approximates fair value. For junior subordinated debentures that bear interest on a fixed rate basis, the fair value is estimated using a discounted cash flow analysis that applies interest rates currently being offered on similar types of borrowings.

Commitments to Extend Credit, Standby Letters of Credit and Credit Card Guarantees—Because commitments to extend credit and standby letters of credit are generally short-term and made using variable rates, the carrying value and estimated fair value associated with these instruments are immaterial.

## Assets Recorded at Fair Value

The table below presents information about certain assets and liabilities measured at fair value on a recurring basis (in thousands):

Description	Assets / Liabilities Fair Value Measured Measurements at Fair at March 31, 2016 Value at		
	March 31, 2016	Level 1	Level 2 Level 3
Available-for-sale securities:			
Obligations of state and political subdivisions	\$ 24,239	\$—	\$ 24,239
GSE mortgage-backed securities	83,896	—	83,896
Collateralized mortgage obligations: residential	187,986	—	187,986
Collateralized mortgage obligations: commercial	3,908	—	3,908
Mutual funds	2,122	2,122	—
	Assets / Liabilities	Fair Value Measurements	

Description	Measured at December 31, at Fair Value at December 31, 2015			
	Level 1	Level 2	Level 3	
Available-for-sale securities:				
Obligations of state and political subdivisions	31,493	—	31,493	—
GSE mortgage-backed securities	87,038	—	87,038	—
Collateralized mortgage obligations: residential	192,088	—	192,088	—
Collateralized mortgage obligations: commercial	5,448	—	5,448	—
Mutual funds	2,092	2,092	—	—

Certain assets and liabilities are measured at fair value on a nonrecurring basis and are included in the table below (in thousands). Impaired loans are Level 2 assets measured using appraisals from external parties of the collateral less any prior liens. Other real estate properties are also Level 2 assets measured using appraisals from external parties.



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Description	Assets / Liabilities Fair Value Measured Measurements at Fair at March 31, 2016 Value at		
	March 31, 2016	Level 1 Level 2	Level 3
Impaired loans	\$ 20,628	\$—\$ 20,628	\$ —
Other real estate	3,908	— 3,908	—

Description	Assets / Liabilities Fair Value Measured Measurements at Fair at December 31, 2015 Value at		
	December 31, 2015	Level 1 Level 2	Level 3
Impaired loans	\$ 17,487	\$—\$ 17,487	\$ —
Other real estate	4,187	— 4,187	—

## Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on many judgments. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Significant assets and liabilities that are not considered financial instruments include deferred income taxes and premises and equipment. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in the estimates.

The carrying amounts and estimated fair values of the Company's financial instruments are as follows at March 31, 2016 and December 31, 2015 (in thousands):

	Carrying Value	Fair Value Measurements at March 31, 2016 Using:		
		Level 1	Level 2	Level 3
Financial assets:				
Cash and due from banks, interest-bearing deposits in banks and federal funds sold	\$ 112,410	\$ 112,410	\$ —	\$ —
Securities available-for-sale	302,151	2,122	300,029	—
Securities held-to-maturity	113,623	—	115,631	—
Other investments	11,195	11,195	—	—
Loans, net	1,229,702	—	20,628	1,216,866

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Cash surrender value of life insurance policies	13,690	—	13,690	—
Financial liabilities:				
Non-interest-bearing deposits	383,684	—	383,684	—
Interest-bearing deposits	1,174,519	—	1,007,935	166,236
Securities sold under agreements to repurchase	87,879	87,879	—	—
Long-term Federal Home Loan Bank advances	25,744	—	—	26,561
Junior subordinated debentures	22,167	—	22,167	—

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	Carrying Value	Fair Value Measurements at December 31, 2015 Using:		
		Level 1	Level 2	Level 3
Financial assets:				
Cash and due from banks, interest-bearing deposits in banks and federal funds sold	\$ 89,201	\$ 89,201	\$ —	—
Securities available-for-sale	318,159	2,092	316,067	—
Securities held-to-maturity	116,792	—	117,698	—
Other investments	11,188	11,188	—	—
Loans, net	1,244,634	—	17,487	1,232,497
Cash surrender value of life insurance policies	13,622	—	13,622	—
Financial liabilities:				
Non-interest-bearing deposits	374,261	—	374,261	—
Interest-bearing deposits	1,176,589	—	1,007,137	168,633
Securities sold under agreements to repurchase	85,957	85,957	—	—
Short-term Federal Home Loan Bank advances	25,000	—	25,000	—
Long-term Federal Home Loan Bank advances	25,851	—	—	26,508
Junior subordinated debentures	22,167	—	22,167	—

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### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operation.

MidSouth Bancorp, Inc. (the "Company") is a financial holding company headquartered in Lafayette, Louisiana that conducts substantially all of its business through its wholly owned subsidiary bank, MidSouth Bank, N.A. (the "Bank"). We offer complete banking services to commercial and retail customers in Louisiana and south and central Texas with 58 locations and are connected to a worldwide ATM network that provides customers with access to more than 55,000 surcharge-free ATMs. We are community oriented and focus primarily on offering commercial and consumer loan and deposit services to individuals, small businesses, and middle market businesses.

The following discussion and analysis identifies significant factors that have affected our financial position and operating results during the periods included in the financial statements accompanying this report. We encourage you to read this discussion in conjunction with our consolidated financial statements and the notes thereto presented herein and with the financial statements, the notes thereto, and related Management's Discussion and Analysis of Financial Condition and Results of Operation in the Company's Annual Report on Form 10-K for the year ended December 31, 2015.

#### Forward-Looking Statements

Certain statements included in this Report, other than statements of historical fact, are forward-looking statements (as such term is defined in Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and the regulations thereunder), which are intended to be covered by the safe harbors created thereby. Forward-looking statements include, but are not limited to certain statements under the captions "Business," "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations."

The words "anticipate," "believe," "estimate," "expect," "intend," "may," "plan," "will," "would," "could," "should," "guidance," "continue," "project," "forecast," "confident," and similar expressions are typically used to identify forward-looking statements. These statements are based on assumptions and assessments made by management in light of their experience and their perception of historical trends, current conditions, expected future developments and other factors they believe to be appropriate. Any forward-looking statements are not guarantees of our future performance and are subject to risks and uncertainties and may be affected by various factors that may cause actual results, developments and business decisions to differ materially from those in the forward-looking statements. Some of the factors that may cause actual results, developments and business decisions to differ materially from those contemplated by such forward-looking statements include the factors discussed under the caption "Risk Factors" in our 2015 Annual Report on form 10-K and under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this Report and the following:

- 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, including, without limitation, changes related to the oil and gas industries, that could adversely affect customers and their ability to repay borrowings under agreed upon terms, adversely affect the value of the underlying collateral related to their borrowings, and reduce demand for loans;
- increased competition for deposits and loans which could affect compositions, 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 our allowance for loan losses ("ALL"), which could result in greater than expected loan losses;
- changes in the availability of funds resulting from reduced liquidity or increased costs;
-

the timing, ability to complete and the impact of proposed and/or future acquisitions, the success or failure of integrating acquired operations, and the ability to capitalize on growth opportunities upon entering new markets;

the timing, ability to complete and the impact of proposed and/or future efficiency initiatives;

the ability to acquire, operate, and maintain effective and efficient operating systems;

increased asset levels and changes in the composition of assets that would impact capital levels and regulatory capital ratios;

loss of critical personnel and the challenge of hiring qualified personnel at reasonable compensation levels;

legislative and regulatory changes, including the changes in the regulatory capital framework under the Federal Reserve Board's Basel III regulatory capital reforms, the impact of regulations under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act"), including the implementation of the Consumer Financial Protection Bureau, and other changes in banking, securities and tax laws and regulations and their application by our regulators, changes in the scope and cost of Federal Deposit Insurance Corporation ("FDIC") insurance and other coverage;

regulations and restrictions resulting from our participation in government sponsored programs such as the U.S. Treasury's Small Business Lending Fund, including potential retroactive changes in such programs;

changes in accounting principles, policies, and guidelines applicable to financial holding companies and banking;

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acts of war, terrorism, cyber intrusion, weather, or other catastrophic events beyond our control; and the ability to manage the risks involved in the foregoing.

We can give no assurance that any of the events anticipated by the forward-looking statements will occur or, if any of them does, what impact they will have on our results of operations and financial condition. We disclaim any intent or obligation to publicly update or revise any forward-looking statements, regardless of whether new information becomes available, future developments occur or otherwise.

### Critical Accounting Policies

Certain critical accounting policies affect the more significant judgments and estimates used in the preparation of the consolidated financial statements. Our significant accounting policies are described in the notes to the consolidated financial statements included in this report. The accounting principles we follow and the methods of applying these principles conform to accounting principles generally accepted in the United States of America (“GAAP”) and general banking practices. Our most critical accounting policy relates to the determination of the allowance for loan losses, which reflects the estimated losses resulting from the inability of its borrowers to make loan payments. The determination of the adequacy of the allowance involves significant judgment and complexity and is based on many factors. If the financial condition of our borrowers were to deteriorate, resulting in an impairment of their ability to make payments, the estimates would be updated and additional provisions for loan losses may be required. See Asset Quality – Nonperforming Assets and Allowance for Loan Losses and Note 1 and Note 3 of the footnotes to the consolidated financial statements.

Another of our critical accounting policies relates to the valuation of goodwill, intangible assets and other purchase accounting adjustments. We account for acquisitions in accordance with ASC Topic No. 805, which requires the use of the purchase method of accounting. Under this method, we are required to record assets acquired and liabilities assumed at their fair value, including intangible assets. Determination of fair value involves estimates based on internal valuations of discounted cash flow analyses performed, third party valuations, or other valuation techniques that involve subjective assumptions. Additionally, the term of the useful lives and appropriate amortization periods of intangible assets is subjective. Resulting goodwill from an acquisition under the purchase method of accounting represents the excess of the purchase price over the fair value of net assets acquired. Goodwill is not amortized, but is evaluated for impairment annually or more frequently if deemed necessary. 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. Given the instability of the economic environment, it is reasonably possible that the methodology of the assessment of potential loan losses and goodwill impairment could change in the near-term or could result in impairment going forward.

A third critical accounting policy relates to deferred tax assets and liabilities. We record deferred tax assets and deferred tax liabilities for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Future tax benefits, such as net operating loss carry forwards, are recognized to the extent that realization of such benefits is more likely than not. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which the assets and liabilities are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income tax expense in the period that includes the enactment date. In the event the future tax consequences of differences between the financial reporting bases and the tax bases of our assets and liabilities results in deferred tax assets, an evaluation of the probability of being able to realize the future benefits indicated by such assets is required. A valuation allowance is provided when it is more likely than not that a portion or the full amount of the deferred tax asset will not be realized. In assessing the ability to realize the deferred tax assets, management considers the scheduled reversals of deferred tax liabilities, projected future taxable income, and tax planning strategies. A deferred tax liability is not recognized for portions of the allowance for loan losses for

income tax purposes in excess of the financial statement balance. Such a deferred tax liability will only be recognized when it becomes apparent that those temporary differences will reverse in the foreseeable future. A tax position is recognized as a benefit only if it is “more likely than not” that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% more likely of being realized on examination. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded.

## Results of Operations

For the Three Months Ended March 31, 2016 and 2015

Net earnings available to common shareholders totaled \$1.9 million for the first quarter of 2016, compared to net earnings available to common shareholders of \$1.3 million reported for the first quarter of 2015. Diluted earnings for the first quarter of 2016 were \$0.17 per common share, compared to \$0.12 per common share reported for the first quarter of 2015. The first quarter of 2015 included gain on sales of securities of \$115,000. Excluding this non-operating income, operating earnings per share for the first quarter of 2015 was \$0.11.

Fully taxable-equivalent ("FTE") net interest income was \$18.6 million for the first quarter of 2016, a \$940,000 decrease compared to \$19.6 million for the first quarter of 2015. Our annualized net interest margin, on a FTE basis, was 4.24% for the three months ended

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March 31, 2016, compared to 4.44% for the same period in 2015. Excluding the impact of purchase accounting adjustments, the FTE margin decreased 21 basis points, from 4.32% to 4.11% for the three months ended March 31, 2015 and 2016, respectively.

Excluding non-operating income of \$115,000 for the first quarter of 2015, noninterest income decreased \$239,000 in quarterly comparison, from \$4.7 million for the three months ended March 31, 2015 to \$4.5 million for the three months ended March 31, 2016. The decrease in noninterest income resulted primarily from a \$86,000 reduction in letter of credit income in addition to a \$44,000 decrease in mortgage program fee income.

Noninterest expenses increased \$598,000 in quarterly comparison. The increase in total noninterest expenses in prior year quarterly comparison resulted primarily from a \$148,000 increase in FDIC premiums and a \$181,000 increase in expenses on other real estate owned. The provision for loan losses decreased \$3.2 million in quarterly comparison, from \$6.0 million for the three months ended March 31, 2015 to \$2.8 million for the three months ended March 31, 2016. The \$6.0 million provision for loan losses for the three months ended March 31, 2015 resulted primarily from a \$41.1 million increase in classified assets during the first quarter of 2015. Income tax expense increased \$517,000 in quarterly comparison.

Dividends on the Series B Preferred Stock issued to the Treasury as a result of our participation in the Small Business Lending Fund ("SBLF") totaled \$336,000 for the first quarter of 2016 based on a dividend rate of 4.2%. The dividend rate increased to 9% on February 25, 2016. Dividends on the Series C Preferred Stock issued with the December 28, 2012 acquisition of PSB Financial Corporation totaled \$91,000 for the three months ended March 31, 2016.

#### Net Interest Income

Our primary source of earnings is net interest income, which is the difference between interest earned on loans and investments and interest paid on deposits and other 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. Our net interest margin on a taxable equivalent basis, which is net interest income as a percentage of average earning assets, was 4.24% and 4.44% for the three months ended March 31, 2016 and 2015, respectively. Tables 1 and 2 below analyze the changes in net interest income in the three months ended March 31, 2016 and 2015.

Fully taxable-equivalent ("FTE") net interest income totaled \$18.6 million and \$19.6 million for the quarters ended March 31, 2016 and 2015, respectively. The FTE net interest income decreased \$940,000 in prior year quarterly comparison primarily due to a \$931,000 decrease in interest income on loans. Interest income on loans decreased due to a \$45.6 million decrease in the average balance of loans as well a decrease in the average yield on loans of 14 basis points, from 5.64% to 5.50%. The purchase accounting adjustments added 24 basis points to the average yield on loans for the first quarter of 2016 and 13 basis points to the average yield on loans for the first quarter of 2015. Excluding the impact of the purchase accounting adjustments, average loan yields declined 25 basis points in prior year quarterly comparison, from 5.51% to 5.26%. Loan yields have declined primarily as the result of a sustained low interest rate environment and a higher volume of loans on nonaccrual status.

Investment securities totaled \$415.8 million, or 21.7% of total assets at March 31, 2016, versus \$435.0 million, or 22.6% of total assets at December 31, 2015. The investment portfolio had an effective duration of 3.3 years and a net unrealized gain of \$5.6 million at March 31, 2016. The average volume of investment securities increased \$8.3 million in prior year quarterly comparison. The average tax equivalent yield on investment securities decreased 13 basis points, from 2.71% to 2.58%.

The average yield on all earning assets decreased 20 basis points in prior year quarterly comparison, from 4.77% for the first quarter of 2015 to 4.57% for the first quarter of 2016. Excluding the impact of purchase accounting



adjustments, the average yield on total earning assets decreased 28 basis points, from 4.67% to 4.39% for the three month periods ended March 31, 2015 and 2016, respectively.

Interest expense decreased \$4,000 in prior year quarterly comparison. A \$40,000 decrease in interest expense on deposits was partially offset by a \$15,000 increase in interest expense on short-term FHLB advances and a \$17,000 increase on junior subordinated debentures. Excluding purchase accounting adjustments on acquired certificates of deposit and FHLB borrowings, the average rate paid on interest-bearing liabilities was 0.45% for the three months ended March 31, 2016, compared to 0.47% for the three months ended March 31, 2015.

Long-term FHLB advances totaled \$25.7 million at March 31, 2016, compared to \$25.9 million at December 31, 2015. The FHLB advances are fixed rate advances with rates ranging from 1.99% to 5.06% and have a range of maturities from April 2016 to January 2019. The FHLB advances are collateralized by a blanket lien on first mortgages and other qualifying loans.

As a result of these changes in volume and yield on earning assets and interest-bearing liabilities, the FTE net interest margin decreased 20 basis points, from 4.44% for the first quarter of 2015 to 4.24% for the first quarter of 2016. Excluding purchase

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accounting adjustments on loans, deposits and FHLB borrowings, the FTE margin decreased 21 basis points, from 4.32% for the first quarter of 2015 to 4.11% for the first quarter of 2016.

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Table 1  
Consolidated Average Balances, Interest and Rates  
(in thousands)

	Three Months Ended March 31,							
	2016		2015		2016		2015	
	Average Volume	Interest	Average Yield/Rate	Average Volume	Interest	Average Yield/Rate		
<b>Assets</b>								
<b>Investment securities<sup>1</sup></b>								
Taxable	\$358,623	\$2,036	2.27 %	\$336,337	\$1,925	2.29 %		
Tax exempt <sup>2</sup>	64,971	699	4.30 %	78,948	892	4.52 %		
Total investment securities	423,594	2,735	2.58 %	415,285	2,817	2.71 %		
Federal funds sold	3,843	5	0.51 %	3,816	2	0.21 %		
Time and interest bearing deposits in other banks	74,271	94	0.50 %	59,225	37	0.25 %		
Other investments	11,189	88	3.15 %	9,754	79	3.24 %		
Total loans <sup>3</sup>	1,252,742	17,123	5.50 %	1,298,317	18,054	5.64 %		
Total earning assets	1,765,639	20,045	4.57 %	1,786,397	20,989	4.77 %		
Allowance for loan losses	(19,499 )			(10,942 )				
Nonearning assets	185,764			191,297				
Total assets	\$1,931,904			\$1,966,752				
<b>Liabilities and shareholders' equity</b>								
Total interest bearing deposits	\$1,180,581	\$907	0.31 %	\$1,192,086	\$947	0.32 %		
Securities sold under repurchase agreements	85,756	233	1.09 %	79,630	230	1.17 %		
Short-term FHLB advances	22,802	23	0.40 %	25,000	8	0.13 %		
Long-term FHLB advances	25,794	90	1.38 %	26,219	89	1.36 %		
Junior subordinated debentures	22,167	167	2.98 %	22,167	150	2.71 %		
Total interest bearing liabilities	1,337,100	1,420	0.43 %	1,345,102	1,424	0.43 %		
Demand deposits	371,636			400,067				
Other liabilities	6,569			9,598				
Shareholders' equity	216,599			211,985				
Total liabilities and shareholders' equity	\$1,931,904			\$1,966,752				
Net interest income and net interest spread		\$18,625	4.14 %		\$19,565	4.34 %		
Net interest margin			4.24 %			4.44 %		

- Securities classified as available-for-sale are included in average balances. Interest income figures reflect interest earned on such securities.
- Interest income of \$241,000 for 2016 and \$308,000 for 2015 is added to interest earned on tax-exempt obligations to reflect tax equivalent yields using a tax rate of 35%.
- Interest income includes loan fees of \$1,191,000 for 2016 and \$1,362,000 for 2015. Nonaccrual loans are included in average balances and income on such loans is recognized on a cash basis.

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

	Three Months Ended March 31, 2016 compared to March 31, 2015		
	Total Increase (Decrease)	Change Attributable To Volume	Rates
Taxable-equivalent earned on:			
Investment securities			
Taxable	\$111	\$127	\$(16 )
Tax exempt	(193 )	(152 )	(41 )
Federal funds sold	3	—	3
Time and interest bearing deposits in other banks	57	11	46
Other investments	9	11	(2 )
Loans, including fees	(931 )	(663 )	(268 )
Total	(944 )	(666 )	(278 )
Interest paid on:			
Interest bearing deposits	(40 )	(9 )	(31 )
Securities sold under repurchase agreements	3	17	(14 )
Short-term FHLB advances	15	(1 )	16
Long-term FHLB advances	1	(1 )	2
Junior subordinated debentures	17	—	17
Total	(4 )	6	(10 )
Taxable-equivalent net interest income	\$(940)	\$(672)	\$(268)

Note: In Table 2, changes due to volume and rate have generally been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts to the changes in each.

## Non-interest Income

Total non-interest income was \$4.5 million and \$4.8 million for the three month periods ended March 31, 2016 and 2015, respectively. Our recurring non-interest income includes service charges on deposit accounts, ATM and debit card income, mortgage lending and increase in cash value of life insurance.

Table 3 presents non-interest income for the three months ended March 31, 2016 and 2015.

Table 3  
Non-Interest Income  
(in thousands)

	Three Months Ended March 31, 2016 2015	
Service charges on deposit accounts	2,313	2,332
ATM and debit card income	1,609	1,629

Gain on securities, net	—	115
Mortgage lending	109	153
Increase in cash value of life insurance	70	90
Credit card income	99	105
Letter of credit income	1	87
Other	286	330
Total non-interest income	4,487	4,841

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Non-interest income decreased \$354,000 in quarterly comparison, from \$4.8 million for the three months ended March 31, 2015 to \$4.5 million for the three months ended March 31, 2016. The first quarter of 2015 included \$115,000 of gain on sales of securities. Excluding this non-operating item, noninterest income decreased \$239,000 in quarterly comparison.

## Non-interest Expense

Total non-interest expense was \$16.8 million and \$16.2 million for the three month periods ended March 31, 2016 and 2015, respectively. Our recurring non-interest expense consists of salaries and employee benefits, occupancy expense, ATM and debit card expense and other operating expenses.

Table 4 presents non-interest expense for the three months ended March 31, 2016 and 2015.

Table 4

Non-Interest Expense  
(in thousands)

	Three Months Ended March 31,	
	2016	2015
Salaries and employee benefits	7,990	7,942
Occupancy expense	3,597	3,685
ATM and debit card	785	663
Legal and professional fees	383	345
FDIC premiums	429	281
Marketing	381	287
Corporate development	335	320
Data processing	458	457
Printing and supplies	188	225
Expenses on ORE, net	194	13
Amortization of core deposit intangibles	277	277
Other non-interest expense	1,742	1,666
Total non-interest income	16,759	16,161

Noninterest expenses increased \$598,000 in quarterly comparison and primarily consisted of increases of \$148,000 in FDIC premiums, \$181,000 in expenses on ORE, \$94,000 in marketing expenses, \$69,000 in other assets expense and \$122,000 in ATM/debit card expense.

Salaries and employee benefits costs increased \$48,000 in prior year quarterly comparison. A \$171,000 increase in group health costs was partially offset by a decrease in salaries and payroll tax expense. A reduction in the number of full-time equivalent (“FTE”) employees from 549 FTE employees at March 31, 2015 to 522 FTE employees at March 31, 2016 reduced salaries and payroll tax expense by \$97,000 year-over-year. The 27 FTE employee decrease was achieved primarily through attrition and process improvement initiatives over the twelve month period.

A \$122,000 increase in ATM and debit card expense in year-over-year comparison was primarily driven by a \$142,000 increase in losses on ATM/debit card processing for the same period. Losses on ATM/debit card processing for the three months ended March 31, 2015 included a \$55,000 insurance reimbursement for losses sustained in 2014. Excluding this insurance reimbursement, ATM and debit card expenses increased \$67,000 for the three months ended

March 31, 2016 compared to the three months ended March 31, 2015 and losses on ATM/debit card processing increased \$87,000 for the same period.

FDIC premiums increased \$148,000, or 52.7%, from the first quarter of 2015 primarily due to an increase in our nonperforming loans.

Net expenses on ORE increased \$181,000, from \$13,000 for the three months ended March 31, 2015 to \$194,000 for the three months ended March 31, 2016, primarily due to a \$91,000 increase in losses on valuation of ORE and a \$24,000 increase in losses on sale of ORE.

#### Analysis of Balance Sheet

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Total consolidated assets remained constant at \$1.9 billion for the quarters ended March 31, 2016 and December 31, 2015. Deposits increased \$7.4 million from year-end 2015. Our stable core deposit base, which excludes time deposits, totaled \$1.4 billion at March 31, 2016 and December 31, 2015 and accounted for 89.3% of deposits compared to 89.1% of deposits, respectively.

Securities available-for-sale totaled \$302.2 million at March 31, 2016, a decrease of \$16.0 million from \$318.2 million at December 31, 2015. The securities available-for-sale portfolio decreased primarily due to \$18.4 million in calls, maturities and pay-downs. Securities held-to-maturity decreased \$3.2 million, from \$116.8 million at December 31, 2015 to \$113.6 million at March 31, 2016. The investment securities portfolio had an effective duration of 3.3 years and a net unrealized gain of \$5.6 million at March 31, 2016.

Total loans decreased \$13.6 million for the three months ended March 31, 2016.

Table 5  
Composition of Loans  
(in thousands)

	March 31, 2016	December 31, 2015
Commercial, financial, and agricultural (C&I)	\$441,160	\$454,028
Real estate – construction	84,790	74,952
Real estate – commercial (CRE)	467,648	471,141
Real estate – residential	149,961	149,064
Installment loans to individuals	103,181	111,009
Lease financing receivable	1,590	1,968
Other	1,719	1,483
	\$1,250,049	\$1,263,645
Less allowance for loan losses	(20,347 )	(19,011 )
Net loans	\$1,229,702	\$1,244,634

Our energy-related loan portfolio at March 31, 2016 totaled \$252.5 million, or 20.2% of total loans, down from \$264.7 million at December 31, 2015. The majority of MidSouth's energy lending is focused on oil field service companies. Of the 431 total relationships in our energy-related loan portfolio, 23 relationships totaling \$50.3 million were classified, with \$24.1 million on nonaccrual status at March 31, 2016.

At March 31, 2016, reserves for potential energy-related loan losses approximated 3.1% of energy loans. Included in the 3.1% is 0.6% reserved for potential yet unidentified losses in the energy-related portfolio. During the first quarter of 2016, one energy-related credit relationship totaling \$5.5 million was classified as a troubled debt restructuring ("TDR"). The TDR defaulted on its restructured terms during the first quarter of 2016.

Within the \$467.6 million commercial real estate portfolio, \$434.7 million is secured by commercial property, \$17.5 million is secured by multi-family property, and \$15.4 million is secured by farmland. Of the \$434.7 million secured by commercial property, \$252.4 million, or 58.1%, is owner-occupied. Of the \$150.0 million residential real estate portfolio, 87.6% represented loans secured by first liens.

#### Off-Balance Sheet Arrangements

In the normal course of operations, the Company engages in a variety of financial transactions that, in accordance with GAAP, are not recorded in the financial statements. These transactions involve, to varying degrees, elements of



credit, interest rate, and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments, letters of credit and lines of credit. For the period ended March 31, 2016, we did not engage in any off-balance sheet transactions reasonably likely to have a material impact on our financial condition, results of operations, or cash flows.

## Liquidity and Capital

### Bank Liquidity

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Liquidity is the availability of funds to meet maturing contractual obligations and to fund operations. The Bank's primary liquidity needs involve its ability to accommodate customers' demands for deposit withdrawals as well as customers' requests for credit. Liquidity is deemed adequate when sufficient cash to meet these needs can be promptly raised at a reasonable cost to the Bank.

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. Although the Bank historically has not utilized brokered deposits, this is a fourth potential source of liquidity, albeit one that is more costly and volatile. Our core deposits are our most stable and important source of funding. Cash deposits at other banks, federal funds sold, and principal payments received on loans and mortgage-backed securities provide additional primary sources of liquidity. Approximately \$55.9 million in projected cash flows from securities repayments for the remainder of 2016 provides an additional source of liquidity.

The Bank also has significant borrowing capacity with the FRB-Atlanta and with the FHLB-Dallas. As of March 31, 2016, we had no borrowings with the FRB-Atlanta. Long-term FHLB-Dallas advances totaled \$25.7 million at March 31, 2016 and are fixed rate advances with rates ranging from 1.99% to 5.06% and have a range of maturities from April 2016 to January 2019. Under existing agreements with the FHLB-Dallas, our borrowing capacity totaled \$244.6 million at March 31, 2016. The Bank has the ability to post additional collateral of approximately \$92.6 million if necessary to meet liquidity needs. Additionally, \$213.3 million in loan collateral is pledged under a Borrower-in-Custody line with the FRB-Atlanta. Unsecured borrowing lines totaling \$53.5 million are available through correspondent banks. We utilize these contingency funding alternatives to meet deposit volatility, which is more likely in the current environment, given unusual competitive offerings within our markets.

## Company Liquidity

At the Company level, cash is needed primarily to meet interest payments on the junior subordinated debentures, dividends on our common stock and dividend payments on the Series B and Series C Preferred Stocks. The weighted average dividend rate on the \$32.0 million of Series B Preferred Stock issued to the U.S. Treasury for participation in the Small Business Lending Fund ("SBLF") was 4.2% for the three month period ended March 31, 2016. The dividend rate increased to 9% on February 25, 2016. Management is reviewing options to repay all or a portion of the \$32.0 million.

On December 28, 2012, the Company issued 756,511 shares of common stock and 99,971 shares of Series C Preferred Stock in connection with the PSB acquisition. As of March 31, 2016, there were 91,200 shares of Series C Preferred Stock issued and outstanding. The Series C Preferred Stock is entitled to the payment of noncumulative dividends, if and when declared by the Company's Board of Directors, at the rate of 4.00% per annum, payable quarterly in arrears on January 15, April 15, July 15 and October 15 of each year. The Series C Preferred Stock paid dividends totaling \$91,000 for the three months ended March 31, 2016.

Dividends from the Bank totaling \$2.0 million provided additional liquidity for the Company during the three months ended March 31, 2016. As of March 31, 2016, the Bank had the ability to pay dividends to the Company of approximately \$7.9 million without prior approval from its primary regulator. As a publicly traded company, the Company also has the ability, subject to market conditions, to issue additional shares of common stock and other securities to provide funds as needed for operations and future growth of the Company. The Company renewed a \$75.0 million Universal Shelf Registration during the third quarter of 2015.

## Capital

The Company and the Bank 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. Effective January 1, 2015, the Company and the Bank adopted the Basel III rules which included new minimum risk-based and leverage ratios, and modified capital and asset definitions for purposes of calculating these ratios. These rules also created a new regulatory capital standard based on Tier 1 common equity and increased the minimum leverage and risk-based capital ratios applicable to all banking organizations.

In addition, the Basel III rules subject banking organizations to certain limitations on capital distributions and discretionary bonus payments to executive officers if the organization does not maintain a capital conservation buffer phased in by 2019 of 2.5% above the new regulatory minimum capital ratios. The effect of the capital conservation buffer once fully implemented in 2019 will be to increase the minimum common equity Tier 1 capital ratio to 7.0%, the minimum Tier 1 risk-based capital ratio to 8.5% and the minimum total risk-based capital ratio to 10.5%, for banking organizations seeking to avoid the limitations on capital distributions and discretionary bonus payments to executive officers. The new minimum capital requirements were effective on January 1, 2015 for community banking organizations, such as MidSouth, whereas other requirements of the Basel III rules including the conservation buffer phase in over time.

At March 31, 2016, the Company and the Bank 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 6.0%, a Tier 1 leverage ratio (Tier 1 to total average adjusted assets) of 4.0% based upon the regulators latest composite rating of the institution, and a common equity Tier 1 capital to total risk-weighted assets of 4.5%. As of March 31, 2016, the Company's Tier 1 leverage ratio

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was 10.17%, Tier 1 capital to risk-weighted assets was 13.28%, total capital to risk-weighted assets was 14.53% and common equity Tier 1 capital to risk-weighted assets was 8.90%. The Bank had a Tier 1 leverage capital ratio of 9.38% at March 31, 2016.

### Asset Quality

#### Credit Risk Management

We manage credit risk primarily by observing written, board approved policies that govern all credit underwriting and approval activities. Our Chief Credit Officer (“CCO”) is responsible for credit underwriting and loan operations for the Bank. The role of the CCO includes on-going review and development of lending policies, commercial credit analysis, centralized consumer underwriting, loan operations documentation and funding, and overall credit risk management procedures. The current risk management process 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. We believe the conservative nature of our underwriting practices has resulted in strong credit quality in our loan portfolio. Completed loan applications, credit bureau reports, financial statements, and a committee approval process remain a part of credit decisions. Documentation of the loan decision process is required on each credit application, whether approved or denied, to ensure thorough and consistent procedures. Additionally, we have historically recognized and disclosed significant problem loans quickly and taken prompt action to address material weaknesses in those credits.

Credit concentrations are monitored and reported quarterly whereby individual customer and aggregate industry leverage, profitability, risk rating distributions, and liquidity are evaluated for each major standard industry classification segment. At March 31, 2016, one industry segment concentration, the oil and gas industry, aggregated more than 10% of our loan portfolio. Our exposure in the oil and gas (energy-related) industry, including related service and manufacturing industries, totaled approximately \$252.5 million, or 20.2% of total loans. Of the 431 credit relationships in the energy-related loan portfolio, 23 relationships totaling \$50.3 million were classified with \$24.1 million on nonaccrual status at March 31, 2016.

Additionally, we monitor our exposure to loans secured by commercial real estate. At March 31, 2016, loans secured by commercial real estate (including commercial construction, farmland and multifamily loans) totaled approximately \$532.5 million. Of the \$532.5 million, \$467.6 million represent CRE loans, 54% of which are secured by owner-occupied commercial properties. Of the \$532.5 million in loans secured by commercial real estate, \$26.0 million, or 4.9%, were on nonaccrual status at March 31, 2016. Additional information regarding credit quality by loan classification is provided in Note 3 – Credit Quality of Loans and Allowance for Loan Losses and Note 8 – Fair Value Measurement in the notes to the interim consolidated financial statements.

#### Nonperforming Assets and Allowance for Loan Loss

Table 6 summarizes the Company's nonperforming assets for the quarters ending March 31, 2016 and 2015, and December 31, 2015.

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Table 6

Nonperforming Assets and Loans Past Due 90 Days or More and Still Accruing  
(in thousands)

	March 31, 2016	December 31, 2015	March 31, 2015		
Nonaccrual loans	\$53,714	\$50,051	\$12,894		
Loans past due 90 days and over and still accruing	258	147	40		
Total nonperforming loans	53,972	50,198	12,934		
Other real estate	3,908	4,187	4,589		
Other foreclosed assets	265	38	43		
Total nonperforming assets	\$58,145	\$54,423	\$17,566		
Troubled debt restructurings, accruing	\$5,675	\$164	\$407		
Nonperforming assets to total assets	3.03	% 2.82	% 0.88		%
Nonperforming assets to total loans + ORE + other assets repossessed	4.64	% 4.29	% 1.34		%
ALL to nonperforming loans	37.70	% 37.87	% 124.17		%
ALL to total loans	1.63	% 1.50	% 1.23		%
QTD charge-offs	\$1,594	\$3,091	\$1,332		
QTD recoveries	130	163	166		
QTD net charge-offs	\$1,464	\$2,928	\$1,166		
Annualized net charge-offs to total loans	0.47	% 0.92	% 0.36		%

Nonperforming assets totaled \$58.1 million at March 31, 2016, an increase of \$3.7 million from the \$54.4 million reported at year-end 2015 and an increase of \$40.6 million from the \$17.6 million reported at March 31, 2015. The increase in the first three months of 2016 resulted primarily from a \$5.6 million commercial real estate loan unrelated to energy that was placed on nonaccrual during the quarter. The \$5.6 million increase was partially offset by a \$786,000 partial charge-off of an energy related relationship.

Allowance coverage for nonperforming loans was 37.7% at March 31, 2016 compared to 37.87% at December 31, 2015 and 124.17% at March 31, 2015. The ALL/total loans ratio increased to 1.63% at March 31, 2016, compared to 1.50% at year-end 2015 and 1.23% at March 31, 2015. Including valuation accounting adjustments on acquired loans, the total adjustments and ALL was 1.87% of loans at March 31, 2016. The ratio of annualized net charge-offs to total loans was 0.47% for the three months ended March 31, 2016, compared to 0.92% for the three months ended December 31, 2015, and 0.36% for the three months ended March 31, 2015. Energy-related charge-offs totaled \$786,000 in the first quarter of 2016.

Total nonperforming assets to total loans plus ORE and other assets repossessed increased to 4.64% at March 31, 2016 from 4.29% at December 31, 2015 and 1.34% at March 31, 2015. Performing troubled debt restructurings (“TDRs”) totaled \$5.7 million at March 31, 2016, compared to \$164,000 at December 31, 2015 and \$407,000 at March 31, 2015. The \$5.5 million of loans restructured during the first quarter of 2016 represented a single, energy-related relationship. Classified assets, including ORE, increased \$16.3 million, or 21.3%, to \$92.9 million at March 31, 2016 compared to \$76.6 million at December 31, 2015. The increase in classified assets during the quarter ended March 31, 2016 is primarily due to the downgrade of two energy-related relationships totaling \$11.5 million and the downgrade of two non energy-related loans totaling \$3.8 million. Additional information regarding impaired loans is included in Note 3 – Credit Quality of Loans and Allowance for Loan Losses and Note 8 – Fair Value Measurement in the notes to the interim consolidated financial statements.

Quarterly evaluations of the allowance for loan losses are performed in accordance with GAAP and regulatory guidelines. The ALL is comprised of specific reserves assigned to each impaired loan for which a probable loss has been identified as well as general reserves to maintain the allowance at an acceptable level for other loans in the portfolio where historical loss experience is available that indicates certain probable losses may exist. 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 we determine the appropriate level of the ALL, 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. We believe the \$20.3 million in the ALL as of March 31, 2016 is sufficient to cover probable losses in the loan portfolio.

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Impact of Inflation and Changing Prices

The consolidated financial statements and notes thereto, presented herein, have been prepared in accordance with GAAP, 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 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.

Non-GAAP Financial Measures

Certain financial information included in the Management's Discussion and Analysis of Financial Condition and Results of Operations is determined by methods other than in accordance with GAAP. Table 7 below presents a reconciliation of these non-GAAP financial measures to the most comparable GAAP financial measures. These non-GAAP financial measures include "core net interest income", "core net interest margin", "diluted earnings per share, operating" and "operating earnings available to common shareholders". "Core net interest income" is defined as net interest income excluding net purchase accounting adjustments. "Core net interest margin" is defined as core net interest income expressed as a percentage of average earnings assets. "Diluted earnings per share, operating" is defined as net earnings available to common shareholders adjusted for specified one-time items divided by diluted weighted-average shares. "Operating earnings available to common shareholders" is defined as net income available to common shareholders less tax-effected nonoperating income and expense items, including securities gains/losses.

We use non-GAAP measures because we believe they are useful for evaluating our financial condition and performance over periods of time, as well as in managing and evaluating our business and in discussions about our performance. We also believe these non-GAAP financial measures provide users of our financial information with a meaningful measure for assessing our financial condition as well as comparison to financial results for prior periods. These results should not be viewed as a substitute for results determined in accordance with GAAP, and are not necessarily comparable to non-GAAP performance measures that other companies may use.

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Table 7

Reconciliation of Non-GAAP Financial Measures  
(in thousands except per share data)

	Three Months Ended March 31,	
	2016	2015
Core Net Interest Margin		
Net interest income (FTE)	18,625	19,565
Less purchase accounting adjustments	(565 )	(465 )
Core net interest income, net of purchase accounting adjustments	A 18,060	19,100
Total average earning assets	1,765,639	1,786,397
Add average balance of loan valuation discount	3,323	5,179
Average earnings assets, excluding loan valuation discount	B 1,768,962	1,791,576
Core net interest margin	A/B4.11	% 4.32 %
Diluted Earnings Per Share, Operating		
Diluted earnings per share	0.17	0.12
Effect of net gain on sale of securities, after-tax	—	(0.01 )
Diluted earnings per share, operating	0.17	0.11
Operating Earnings Available to Common Shareholders		
Net earnings available to common shareholders	1,922	1,318
Non-interest income adjustments:		
Net gain on sale of securities, after-tax	—	(75 )
Operating earnings available to common shareholders	1,922	1,243



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Item 3. Quantitative and Qualitative Disclosures About Market Risk.

There have been no significant changes from the information regarding market risk disclosed under the heading “Funding Sources - Interest Rate Sensitivity” in the Company’s Annual Report on Form 10-K for the year ended December 31, 2015.

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-15(e) and 15d-15(e) 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 Chief Executive Officer and Chief 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 first quarter of 2016, there was no change in the Company’s internal controls over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

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Part II – Other Information

Item 1. Legal Proceedings.

The Bank has 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. However, in the event of unexpected future developments in these matters, if the ultimate resolution of any such matter is unfavorable, the result may be material to the Company’s consolidated financial position, consolidated results of operations or consolidated cash flows.

Item 1A. Risk Factors.

There have been no material changes from the risk factors previously disclosed in our Form 10-K for the year ended December 31, 2015.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The Company did not sell any unregistered equity securities or repurchase any equity securities during the quarter ended March 31, 2016.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

None.

Item 5. Other Information.

None.

Item 6. Exhibits.

Exhibit Number	Document Description
3.1	Amended and Restated Articles of Incorporation of MidSouth Bancorp, Inc. (restated solely for purposes of Item 601(b)(3) of Regulation S-K) (filed as Exhibit 3.1 to MidSouth’s Annual Report on Form 10-K filed on March 18, 2013 and incorporated herein by reference).
3.2	Amended and Restated By-laws of MidSouth Bancorp, Inc. effective as of September 26, 2012 (restated solely for purposes of Item 601(b)(3) of Regulation S-K (filed as Exhibit 3.3 to MidSouth’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2012 and incorporated herein by reference).
31.1	Certification pursuant to Exchange Act Rules 13(a) – 14(a)

- 31.2 Certification pursuant to Exchange Act Rules 13(a) – 14(a)
- 32.1 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101 The following financial information from the Registrant’s Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2016, formatted in Extensible Business Reporting Language (“XBRL”):  
(i) Consolidated Statements of Operations, (ii) Consolidated Balance Sheets, (iii) Consolidated Statements of Cash Flows and (iv) Notes to Consolidated Financial Statements.\*

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Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not to be “filed” or part of a \*registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, or Section 18 of the Securities Act of 1934, as amended, and otherwise are not subject to liability under these sections.

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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: May 10, 2016

/s/ C. R. Cloutier  
C. R. Cloutier, President and CEO  
(Principal Executive Officer)

/s/ James R. McLemore  
James R. McLemore, CFO  
(Principal Financial Officer)

/s/ Teri S. Stelly  
Teri S. Stelly, Controller  
(Principal Accounting Officer)