TRUSTMARK CORP
Form 10-Q
May 06, 2011

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

Form 10-Q

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

For the quarterly period ended March 31, 2011

or

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

For the transition period from ___________________ to ___________________

Commission file number 000-03683

Trustmark Corporation
(Exact name of registrant as specified in its charter)

Mississippi (State or other jurisdiction of incorporation or organization)	64-0471500 (I.R.S. Employer Identification No.)
248 East Capitol Street, Jackson, Mississippi (Address of principal executive offices)	39201 (Zip Code)

(601) 208-5111
(Registrant’s telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b of the Exchange Act.

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of April 25, 2011, there were 63,991,264 shares outstanding of the registrant's common stock (no par value).

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

Trustmark Corporation and Subsidiaries
Consolidated Balance Sheets
($ in thousands)

	(Unaudited) March 31, 2011	December 31, 2010
Assets		
Cash and due from banks (noninterest-bearing)	$ 193,087	$ 161,544
Federal funds sold and securities purchased under reverse repurchase agreements	1,726	11,773
Securities available for sale (at fair value)	2,309,704	2,177,249
Securities held to maturity (fair value: $113,828-2011; $145,143-2010)	110,054	140,847
Loans held for sale	112,981	153,044
Loans	5,964,089	6,060,242
Less allowance for loan losses	93,398	93,510
Net loans	5,870,691	5,966,732
Premises and equipment, net	141,524	142,289
Mortgage servicing rights	53,598	51,151
Goodwill	291,104	291,104
Identifiable intangible assets	15,532	16,306
Other real estate	89,198	86,704
Other assets	325,263	355,159
Total Assets	$ 9,514,462	$ 9,553,902
Liabilities		
Deposits:		
Noninterest-bearing	$ 1,668,104	$ 1,636,625
Interest-bearing	5,758,170	5,407,942
Total deposits	7,426,274	7,044,567
Federal funds purchased and securities sold under repurchase agreements	550,919	700,138
Short-term borrowings	154,585	425,343
Subordinated notes	49,814	49,806
Junior subordinated debt securities	61,856	61,856
Other liabilities	110,785	122,708
Total Liabilities	8,354,233	8,404,418
Shareholders' Equity		
Common stock, no par value:		
Authorized: 250,000,000 shares		
Issued and outstanding: 63,987,064 shares - 2011;		
63,917,591 shares - 2010	13,333	13,318
Capital surplus	260,297	256,675
Retained earnings	898,222	890,917
Accumulated other comprehensive loss, net of tax	(11,623)	(11,426)
Total Shareholders' Equity	1,160,229	1,149,484

Total Liabilities and Shareholders' Equity	$9,514,462	$9,553,902

See notes to consolidated financial statements.

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Trustmark Corporation and Subsidiaries
Consolidated Statements of Income
($ in thousands except per share data)
(Unaudited)

	Three Months Ended March 31,	
	2011	2010
Interest Income		
Interest and fees on loans	$76,270	$81,597
Interest on securities:		
Taxable	19,992	19,735
Tax exempt	1,383	1,417
Interest on federal funds sold and securities purchased under reverse repurchase agreements	8	8
Other interest income	332	383
Total Interest Income	97,985	103,140
Interest Expense		
Interest on deposits	9,719	13,904
Interest on federal funds purchased and securities sold under repurchase agreements	338	226
Other interest expense	1,553	1,592
Total Interest Expense	11,610	15,722
Net Interest Income	86,375	87,418
Provision for loan losses	7,537	15,095
Net Interest Income After Provision for Loan Losses	78,838	72,323
Noninterest Income		
Service charges on deposit accounts	11,907	12,977
Insurance commissions	6,512	6,837
Wealth management	5,986	5,355
Bank card and other fees	6,475	5,880
Mortgage banking, net	4,722	6,072
Other, net	762	879
Securities gains, net	7	369
Total Noninterest Income	36,371	38,369
Noninterest Expense		
Salaries and employee benefits	44,036	42,854
Services and fees	10,270	10,255
Net occupancy - premises	5,073	5,034
Equipment expense	5,144	4,303
FDIC assessment expense	2,750	3,147
ORE/Foreclosure expense	3,213	3,061
Other expense	9,532	7,707
Total Noninterest Expense	80,018	76,361
Income Before Income Taxes	35,191	34,331
Income taxes	11,178	10,876

Net Income	$24,013	$23,455
Earnings Per Common Share		
Basic	$0.38	$0.37
Diluted	$0.37	$0.37
Dividends Per Common Share	$0.23	$0.23

See notes to consolidated financial statements.

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Trustmark Corporation and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
($ in thousands)
(Unaudited)

	2011	2010
Balance, January 1,	$1,149,484	$1,110,060
Net income per consolidated statements of income	24,013	23,455
Other comprehensive income:		
Net change in fair value of securities available for sale	(950)	5,583
Net change in defined benefit plans	753	505
Comprehensive income	23,816	29,543
Common stock dividends paid	(14,866)	(14,817)
Common stock issued-net, long-term incentive plans:		
Stock options	401	2,296
Restricted stock	(620)	(592)
Excess tax benefit from stock-based compensation arrangements	976	807
Compensation expense, long-term incentive plans	1,038	1,292
Other	-	(60)
Balance, March 31,	$1,160,229	$1,128,529

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Cash Flows
($ in thousands)
(Unaudited)

	Three Months Ended March 31, 2011	2010
Operating Activities		
Net income	$24,013	$23,455
Adjustments to reconcile net income to net cash provided		
by operating activities:		
Provision for loan losses	7,537	15,095
Depreciation and amortization	5,853	5,798
Net amortization of securities	1,559	429
Securities gains, net	(7)	(369)
Gains on sales of loans, net	(3,101)	(3,755)
Deferred income tax benefit	(355)	(165)
Proceeds from sales of loans held for sale	242,755	250,012
Purchases and originations of loans held for sale	(195,964)	(197,088)
Originations and sales of mortgage servicing rights	(3,480)	(3,761)
Net decrease in other assets	29,455	18,425
Net decrease in other liabilities	(9,728)	(10,000)
Other operating activities, net	1,480	4,263
Net cash provided by operating activities	100,017	102,339
Investing Activities		
Proceeds from calls and maturities of securities held to maturity	30,806	17,122
Proceeds from calls and maturities of securities available for sale	147,958	86,620
Proceeds from sales of securities available for sale	-	12,453
Purchases of securities available for sale	(283,517)	(108,094)
Net decrease (increase) in federal funds sold and securities purchased under reverse repurchase agreements	10,047	(5,225)
Net decrease in loans	68,952	118,184
Purchases of premises and equipment	(2,487)	(935)
Proceeds from sales of premises and equipment	374	1
Proceeds from sales of other real estate	15,399	11,827
Net cash (used in) provided by investing activities	(12,468)	131,953
Financing Activities		
Net increase (decrease) in deposits	381,707	(41,412)
Net decrease in federal funds purchased and securities sold under repurchase agreements	(149,219)	(81,321)
Net decrease in short-term borrowings	(274,385)	(120,799)
Common stock dividends	(14,866)	(14,817)
Common stock issued-net, long-term incentive plans	(219)	1,704
Excess tax benefit from stock-based compensation arrangements	976	807
Net cash used in financing activities	(56,006)	(255,838)
Increase (decrease) in cash and cash equivalents	31,543	(21,546)

Cash and cash equivalents at beginning of period	161,544	213,519
Cash and cash equivalents at end of period	$193,087	$191,973

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 1 – Business, Basis of Financial Statement Presentation and Principles of Consolidation

Trustmark Corporation (Trustmark) is a multi-bank holding company headquartered in Jackson, Mississippi. Through its subsidiaries, Trustmark operates as a financial services organization providing banking and financial solutions to corporate institutions and individual customers through over 150 offices in Florida, Mississippi, Tennessee and Texas.

The consolidated financial statements in this quarterly report on Form 10-Q include the accounts of Trustmark and all other entities in which Trustmark has a controlling financial interest. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements and should be read in conjunction with the consolidated financial statements, and notes thereto, included in Trustmark's 2010 annual report on Form 10-K.

Operating results for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year or any future period. Certain reclassifications have been made to prior period amounts to conform to the current period presentation. In the opinion of Management, all adjustments (consisting of normal recurring accruals) considered necessary for the fair presentation of these consolidated financial statements have been included. The preparation of financial statements in conformity with these accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and income and expense during the reporting period and the related disclosures. Although Management's estimates contemplate current conditions and how they are expected to change in the future, it is reasonably possible that in 2011 actual conditions could vary from those anticipated, which could affect our results of operations and financial condition. The allowance for loan losses, the valuation of other real estate, the fair value of mortgage servicing rights, the valuation of goodwill and other identifiable intangibles, the status of contingencies and the fair values of financial instruments are particularly subject to change. Actual results could differ from those estimates.

Note 2 – Business Combinations

On April 15, 2011, Trustmark announced the acquisition of Heritage Banking Group, a 90-year old financial institution headquartered in Carthage, Mississippi, from the Federal Deposit Insurance Corporation. At March 31, 2011, Heritage had approximately $228.3 million in assets and $205.0 million in deposits. Substantially all loans and other real estate acquired are covered by a loss share agreement in which the FDIC will reimburse Trustmark for 80.0% of the losses incurred. The assets covered by loss sharing agreements total approximately $156.0 million. Trustmark purchased Heritage for an asset discount of approximately $23.0 million and a deposit premium of 0.15%. The acquisition is expected to generate an estimated one-time $4.0 million to $6.0 million after-tax gain in the second quarter of 2011.

Note 3 – Securities Available for Sale and Held to Maturity

The following table is a summary of the amortized cost and estimated fair value of securities available for sale and held to maturity ($ in thousands):

	Securities Available for Sale				Securities Held to Maturity			
March 31, 2011	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value
U.S. Government agency obligations								
Issued by U.S. Government agencies	$ 10	$ -	$ -	$ 10	$ -	$ -	$ -	$ -
Issued by U.S. Government sponsored agencies	139,080	196	(3,108)	136,168	-	-	-	-
Obligations of states and political subdivisions	158,945	3,805	(841)	161,909	49,129	2,728	(2)	51,855
Mortgage-backed securities								
Residential mortgage pass-through securities								
Guaranteed by GNMA	11,423	656	-	12,079	5,650	135	-	5,785
Issued by FNMA and FHLMC	423,785	1,057	(7,820)	417,022	-	-	-	-
Other residential mortgage-backed securities								
Issued or guaranteed by FNMA, FHLMC or GNMA	1,449,533	39,919	(2,580)	1,486,872	52,272	928	-	53,200
Commercial mortgage-backed securities								
Issued or guaranteed by FNMA,	94,292	1,921	(569)	95,644	3,003	1	(16)	2,988

FHLMC or GNMA								
Total	$ 2,277,068	$ 47,554	$ (14,918)	$ 2,309,704	$ 110,054	$ 3,792	$ (18)	$ 113,828
December 31, 2010								
U.S. Government agency obligations								
Issued by U.S. Government agencies	$ 12	$ -	$ -	$ 12	$ -	$ -	$ -	$ -
Issued by U.S. Government sponsored agencies	124,093	114	(2,184)	122,023	-	-	-	-
Obligations of states and political subdivisions	159,418	2,259	(2,040)	159,637	53,246	2,628	(10)	55,864
Mortgage-backed securities								
Residential mortgage pass-through securities								
Guaranteed by GNMA	11,719	723	-	12,442	6,058	171	-	6,229
Issued by FNMA and FHLMC	432,162	1,188	(6,846)	426,504	-	-	-	-
Other residential mortgage-backed securities								
Issued or guaranteed by FNMA, FHLMC or GNMA	1,361,339	43,788	(4,311)	1,400,816	78,526	1,503	-	80,029
Commercial mortgage-backed securities								
Issued or guaranteed by FNMA, FHLMC or GNMA	54,331	2,007	(523)	55,815	3,017	6	(2)	3,021
Total	$ 2,143,074	$ 50,079	$ (15,904)	$ 2,177,249	$ 140,847	$ 4,308	$ (12)	$ 145,143

Temporarily Impaired Securities

The table below includes securities with gross unrealized losses segregated by length of impairment ($ in thousands):

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	Less than 12 Months		12 Months or More		Total	
March 31, 2011	Estimated Fair Value	Gross Unrealized (Losses)	Estimated Fair Value	Gross Unrealized (Losses)	Estimated Fair Value	Gross Unrealized (Losses)
U.S. Government agency obligations						
Issued by U.S. Government sponsored agencies	$ 85,994	$ (3,108)	$ -	$ -	$ 85,994	$ (3,108)
Obligations of states and political subdivisions	36,755	(837)	306	(6)	37,061	(843)
Mortgage-backed securities						
Residential mortgage pass-through securities						
Issued by FNMA and FHLMC	320,938	(7,820)	-	-	320,938	(7,820)
Other residential mortgage-backed securities						
Issued or guaranteed by FNMA, FHLMC or GNMA	227,871	(2,580)	-	-	227,871	(2,580)
Commercial mortgage-backed securities						
Issued by FNMA and FHLMC	28,716	(585)	-	-	28,716	(585)
Total	$ 700,274	$ (14,930)	$ 306	$ (6)	$ 700,580	$ (14,936)
December 31, 2010						
U.S. Government agency obligations						
Issued by U.S. Government sponsored agencies	$ 86,917	$ (2,184)	$ -	$ -	$ 86,917	$ (2,184)
Obligations of states and political subdivisions	65,523	(2,045)	307	(5)	65,830	(2,050)
Mortgage-backed securities						
Residential mortgage pass-through securities						
Issued by FNMA and FHLMC	312,787	(6,846)	-	-	312,787	(6,846)
Other residential mortgage-backed securities						
Issued or guaranteed by FNMA, FHLMC or GNMA	232,279	(4,311)	-	-	232,279	(4,311)
Commercial mortgage-backed securities						
Issued or guaranteed by FNMA, FHLMC or GNMA	21,073	(525)	-	-	21,073	(525)
Total	$ 718,579	$ (15,911)	$ 307	$ (5)	$ 718,886	$ (15,916)

Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of the impairment related to other factors is recognized in other comprehensive income. In estimating other-than-temporary impairment losses, Management considers, among other things, the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer and the intent and ability of Trustmark to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value. The unrealized losses shown above are primarily due to increases in market rates over the yields available at the time of purchase of the underlying securities and not credit quality. Because Trustmark does not intend to sell these securities and it is more likely than not that Trustmark will not be required to sell the investments before recovery of their amortized cost bases, which may be maturity, Trustmark does not consider these investments to be other-than-temporarily impaired at March 31, 2011. There were no other-than-temporary impairments for the three months ended March 31, 2011 and 2010.

Security Gains and Losses

Gains and losses as a result of calls and dispositions of securities were as follows ($ in thousands):

	Three Months Ended March 31,	
Available for Sale	2011	2010
Proceeds from sales of securities	$ -	$ 12,453
Gross realized gains	-	364
Held to Maturity		
Proceeds from calls of securities	$ 1,290	$ 1,705
Gross realized gains	7	5

Realized gains and losses are determined using the specific identification method and are included in noninterest income as securities gains, net.

Contractual Maturities

The amortized cost and estimated fair value of securities available for sale and held to maturity at March 31, 2011, by contractual maturity, are shown below ($ in thousands). Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Securities Available for Sale		Securities Held to Maturity	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$13,052	$13,132	$3,302	$3,334
Due after one year through five years	44,071	45,253	15,512	16,015
Due after five years through ten years	215,508	214,369	21,914	23,314
Due after ten years	25,404	25,333	8,401	9,192
	298,035	298,087	49,129	51,855
Mortgage-backed securities	1,979,033	2,011,617	60,925	61,973
Total	$2,277,068	$2,309,704	$110,054	$113,828

Note 4 – Loans and Allowance for Loan Losses

For the periods presented, loans consisted of the following ($ in thousands):

	March 31, 2011	December 31, 2010
Loans secured by real estate:		
Construction, land development and other land loans	$ 552,956	$ 583,316
Secured by 1-4 family residential properties	1,737,018	1,732,056
Secured by nonfarm, nonresidential properties	1,488,711	1,498,108
Other	216,986	231,963
Commercial and industrial loans	1,082,258	1,068,369
Consumer loans	357,870	402,165
Other loans	528,290	544,265
Loans	5,964,089	6,060,242
Less allowance for loan losses	93,398	93,510
Net loans	$ 5,870,691	$ 5,966,732

The following table details loans individually and collectively evaluated for impairment at March 31, 2011 and December 31. 2010 ($ in thousands):

	March 31, 2011		
	Loans Evaluated for Impairment		
	Individually	Collectively	Total
Loans secured by real estate:			
Construction, land development and other land loans	$44,151	$508,805	$552,956
Secured by 1-4 family residential properties	24,825	1,712,193	1,737,018
Secured by nonfarm, nonresidential properties	32,237	1,456,474	1,488,711
Other	5,648	211,338	216,986
Commercial and industrial loans	17,159	1,065,099	1,082,258
Consumer loans	1,516	356,354	357,870
Other loans	1,254	527,036	528,290
Total	$126,790	$5,837,299	$5,964,089

	December 31, 2010		
	Loans Evaluated for Impairment		
	Individually	Collectively	Total
Loans secured by real estate:			
Construction, land development and other land loans	$57,831	$525,485	$583,316
Secured by 1-4 family residential properties	30,313	1,701,743	1,732,056
Secured by nonfarm, nonresidential properties	29,013	1,469,095	1,498,108
Other	6,154	225,809	231,963
Commercial and industrial loans	16,107	1,052,262	1,068,369
Consumer loans	2,112	400,053	402,165
Other loans	1,393	542,872	544,265
Total	$142,923	$5,917,319	$6,060,242

Loan Concentrations

Trustmark does not have any loan concentrations other than those reflected in the preceding table, which exceed 10% of total loans. At March 31, 2011, Trustmark's geographic loan distribution was concentrated primarily in its Florida, Mississippi, Tennessee and Texas markets. A substantial portion of construction, land development and other land loans are secured by real estate in markets in which Trustmark is located. Accordingly, the ultimate collectability of a substantial portion of these loans and the recovery of a substantial portion of the carrying amount of other real estate owned, are susceptible to changes in market conditions in these areas.

Nonaccrual/Impaired Loans

At March 31, 2011 and December 31, 2010, the carrying amounts of nonaccrual loans, which are considered for impairment analysis, were $126.8 million and $142.9 million, respectively. When a loan is deemed impaired, the full difference between the carrying amount of the loan and the most likely estimate of the asset's fair value less cost to sell, is charged-off. At March 31, 2011 and December 31, 2010, specifically evaluated impaired loans totaled $87.1 million and $97.6 million, respectively. In addition, these specifically evaluated impaired loans had a related allowance of $7.9 million and $8.3 million at the end of the respective periods. Specific charge-offs related to impaired loans totaled $5.3 million and $9.8 million while the provisions charged to net income for these loans totaled $1.0 million and $1.8 million for the first three months of 2011 and 2010, respectively.

At March 31, 2011 and December 31, 2010, nonaccrual loans, not specifically impaired and written down to fair value less cost to sell, totaled $39.7 million and $45.3 million, respectively. In addition, these nonaccrual loans had allocated allowance for loan losses of $3.2 million and $3.5 million at the end of the respective periods. No material interest income was recognized in the income statement on impaired or nonaccrual loans for each of the periods ended March 31, 2011 and 2010.

At March 31, 2011 and December 31, 2010, loans classified as troubled debt restructurings (TDRs) totaled $22.8 million and $19.2 million, respectively. For TDRs, Trustmark had a related loan loss allowance of $1.9 million at the end of each respective period. Specific charge-offs related to TDRs totaled $631 thousand for the three months ended March 31, 2011. Loans that are TDRs are charged down to the most likely fair value estimate less cost to sell, which would approximate net realizable value.

At March 31, 2011 and December 31, 2010, the carrying amount of impaired loans consisted of the following ($ in thousands):

	March 31, 2011					
	Unpaid Principal Balance	Total Loans with No Related Allowance Recorded	Total Loans with an Allowance Recorded	Total Carrying Amount	Related Allowance	Average Recorded Investment
Loans secured by real estate:						
Construction, land development and other land loans	$ 64,745	$ 15,688	$ 28,464	$ 44,152	$ 6,242	$ 50,991
Secured by 1-4 family residential properties	34,482	4,212	20,612	24,824	680	27,568
Secured by nonfarm, nonresidential properties	40,155	23,113	9,123	32,236	1,415	30,625
Other	6,554	5,042	606	5,648	41	5,902
Commercial and industrial loans	18,527	9,053	8,106	17,159	2,670	16,632
Consumer loans	1,859	-	1,517	1,517	18	1,815
Other loans	2,752	990	264	1,254	53	1,324
Total	$ 169,074	$ 58,098	$ 68,692	$ 126,790	$ 11,119	$ 134,857

	December 31, 2010					
	Unpaid Principal Balance	Total Loans with No Related Allowance Recorded	Total Loan is with an Allowance Recorded	Total Carrying Amount	Related Allowance	Average Recorded Investment
Loans secured by real estate:						
Construction, land development and other land loans	$ 81,945	$ 33,201	$ 24,630	$ 57,831	$ 6,782	$ 69,817
Secured by 1-4 family residential properties	41,475	3,082	27,230	30,312	1,745	30,888
Secured by nonfarm, nonresidential properties	35,679	18,582	10,431	29,013	1,580	23,535
Other	7,009	5,042	1,113	6,155	95	4,126
Commercial and industrial loans	17,413	9,172	6,935	16,107	1,514	11,369
Consumer loans	2,420	-	2,112	2,112	23	1,544
Other loans	2,868	1,107	286	1,393	58	765
Total	$ 188,809	$ 70,186	$ 72,737	$ 142,923	$ 11,797	$ 142,044

Credit Quality Indicators

Trustmark's loan portfolio credit quality indicators focus on six key quality ratios that are compared against bank tolerances. The loan indicators are total classified outstanding, total criticized outstanding, nonperforming loans, nonperforming assets, delinquencies and net loan losses. Due to the homogenous nature of consumer loans, Trustmark does not assign a formal internal risk rating to each credit and therefore the criticized and classified measures are unique to commercial loans.

In addition to monitoring portfolio credit quality indictors, Trustmark also measures how effectively the lending process is being managed and risks are being identified. As part of an ongoing monitoring process, Trustmark grades the commercial portfolio as it relates to financial statement exceptions, total policy exceptions, collateral exceptions and violations of law as shown below:

- Financial Statement Exceptions – focuses on the officers' ongoing efforts to obtain, evaluate and/or document sufficient information to determine the quality and status of the credits. This area includes the quality and condition of the files in terms of content, completeness and organization. Included is an evaluation of the systems/procedures used to insure compliance with policy such as financial statements, review memos and loan agreement covenants.
- Underwriting/Policy – evaluates whether credits are adequately analyzed, appropriately structured and properly approved within requirements of bank loan policy. A properly approved credit is approved by adequate authority in a timely manner with all conditions of approval fulfilled. Total policy exceptions measure the level of exceptions to loan policy within a loan portfolio.
- Collateral Documentation – focuses on the adequacy of documentation to support the obligation, perfect Trustmark's collateral position and protect collateral value. There are two parts to this measure:
  - ü Collateral exceptions where certain collateral documentation is either not present, is not considered current or has expired.
  - ü 90 days and over collateral exceptions are where certain collateral documentation is either not present, is not considered current or has expired and the exception has been identified in excess of 90 days.
- Compliance with Law – focuses on underwriting, documentation, approval and reporting in compliance with banking laws and regulations. Primary emphasis is directed to Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) and Regulation O requirements.

Commercial Credits

Trustmark has established a Loan Grading System that consists of ten individual Credit Risk Grades (Risk Ratings) that encompass a range from loans where the expectation of loss is negligible to loans where loss has been established. The model is based on the risk of default for an individual credit and establishes certain criteria to delineate the level of risk across the ten unique Credit Risk Grades. Credit risk grade definitions are as follows:

- Risk Rate (RR) 1 through RR 6 – Grades one through six represent groups of loans that are not subject to adverse criticism as defined in regulatory guidance. Loans in these groups exhibit characteristics that represent low to moderate risk measured by using a variety of credit risk criteria such as cash flow coverage, debt service coverage, balance sheet leverage, liquidity, management experience, industry position, prevailing economic conditions, support from secondary sources of repayment and other credit factors that may be relevant to a specific loan. In general, these loans are supported by properly margined collateral and guarantees of principal parties.
- OAEM (RR 7) – a loan that has a potential weakness that if not corrected will lead to a more severe rating. This rating is for credits that are currently protected but potentially weak because of an adverse feature or condition that if not corrected will lead to a further downgrade.
- Substandard (RR 8) – a loan that has at least one identified weakness that is well defined. This rating is for credits where the primary sources of repayment are not viable at this time or where either the capital or collateral is not adequate to support the loan and the secondary means of repayment do not provide a sufficient level of support to offset the identified weakness but are sufficient to prevent a loss at this time. While these credits do not demonstrate any level of loss at this time, further deterioration would lead to a further downgrade.
- Doubtful (RR 9) – a loan with an identified weakness that does not have a valid secondary source of repayment. Generally these credits have an impaired primary source of repayment and secondary sources are not sufficient to prevent a loss in the credit.
- Loss (RR 10) – a loan or a portion of a loan that is deemed to be uncollectible.

By definition, credit risk grades OAEM (RR 7), substandard (RR 8), doubtful (RR 9) and loss (RR 10) are criticized loans while substandard (RR 8), doubtful (RR 9) and loss (RR 10) are classified loans. These definitions are standardized by all bank regulatory agencies and are generally equally applied to each individual lending institution. The remaining credit risk grades are considered pass credits and are solely defined by Trustmark.

The credit risk grades represent the probability of default (PD) for an individual credit and as such is not a direct indication of loss given default (LGD). The LGD aspect of the subject risk ratings is neither uniform across the nine primary commercial loan groups or constant between the geographic areas. To account for the variance in the LGD aspects of the risk rate system, the loss expectations for each risk rating is integrated into the allowance for loan loss methodology where the calculated LGD is allotted for each individual risk rating with respect to the individual loan group and unique geographic area. The LGD aspect of the reserve methodology is calculated each quarter as a component of the overall reserve factor for each risk grade by loan group and geographic area.

To enhance this process, loans of a certain size that are rated in one of the criticized categories are routinely reviewed to establish an expectation of loss, if any, and if such examination indicates that the level of reserve is not adequate to cover the expectation of loss, a special reserve or impairment is generally applied.

Each loan officer assesses the appropriateness of the internal risk rating assigned to their credits on an ongoing basis. Trustmark's Asset Review area conducts independent credit quality reviews of the majority of the bank's commercial loan portfolio concentrations both on the underlying credit quality of each individual loan portfolio as well as the adherence to bank loan policy and the loan administration process. In general, Asset Review conducts reviews of each lending area within a six to eighteen month window depending on the overall credit quality results of the individual area.

In addition to the ongoing internal risk rate monitoring described above, Trustmark conducts monthly credit quality reviews (CQR) as well as semi-annual analysis and stress testing on all residential real estate development credits and non-owner occupied commercial real estate (CRE) credits of $1.0 million or more as described below:

- Trustmark's Credit Quality Review Committee meets monthly and performs the following functions: detailed review and evaluation of all loans of $100 thousand or more that are either delinquent thirty days or more or on nonaccrual, including determination of appropriate risk ratings, accrual status, and appropriate servicing officer; review of risk rate changes for relationships of $100 thousand or more; quarterly review of all nonaccruals less than $100 thousand to determine whether the credit should be charged off, returned to accrual, or remain in nonaccrual status; monthly/quarterly review of continuous action plans for all credits rated seven or worse for relationships of $100 thousand or more; monthly review of all commercial charge-offs of $25 thousand or more for the preceding month.

- Residential real estate developments - a development project analysis is performed on all projects regardless of size. Performance of the development is assessed through an evaluation of the number of lots remaining, the payout ratios, and the loan-to-value ratios. Results are stress tested as to absorption and price of lots. This information is reviewed by each senior credit officer for that market to determine the need for any risk rate or accrual status changes.

- Non-owner occupied commercial real estate – a cash flow analysis is performed on all projects with an outstanding balance of $1.0 million or more. In addition, credits are stress tested for vacancies and rate sensitivity. Confirmation is obtained that guarantor's financial statements are current, taxes have been paid, and that there are no other issues that need to be addressed. This information is reviewed by each senior credit officer for that market to determine the need for any risk rate or accrual status changes.

Consumer Credits

Loans that do not meet a minimum custom credit score are reviewed quarterly by Management. The Retail Credit Review Committee reviews the volume and percentage of approvals that did not meet the minimum passing custom score by region, individual location, and officer. To assure that Trustmark continues to originate quality loans, this process allows Management to make necessary changes such as changes to underwriting procedures, credit policies, or changes in loan authority to Trustmark personnel.

Trustmark monitors the levels and severity of past due consumer loans on a daily basis through its collection activities. A detailed assessment of consumer loan delinquencies is performed monthly at both a product and market level by delivery channel, which incorporates the perceived level of risk at time of underwriting. Trustmark also monitors its consumer loan delinquency trends by comparing them to quarterly industry averages.

The allowance calculation methodology delineates the consumer loan portfolio into homogeneous pools of loans that contain similar structure, repayment, collateral and risk profile, which include residential mortgage, direct consumer loans, auto finance, credit cards, and overdrafts. For these pools, the historical loss experience is determined by calculating a 20-quarter rolling average and that loss factor is applied to each homogeneous pool to establish the quantitative aspect of the methodology. Where the loss experience does not fully cover the anticipated loss for a pool, an estimate is also applied to each homogeneous pool to establish the qualitative aspect of the methodology. The qualitative portion is the allocation of perceived risks across the loan portfolio to derive the potential losses that exist at the current point in time. This methodology utilizes five separate factors where each factor is made up of unique components that when weighted and combined produce an estimated level of reserve for each of the loan pools. The five factors include economic indicators, performance trends, management experience, lending policy measures, and credit concentrations.

The table below illustrates the carrying amount of loans by credit quality indicator at March 31, 2011 and December 31, 2010 ($ in thousands):

	March 31, 2011				
	Commercial Loans				
	Pass - Categories 1-6	Special Mention - Category 7	Substandard - Category 8	Doubtful - Category 9	Subtotal
Loans secured by real estate:					
Construction, land development and other land loans	$ 323,839	$ 39,218	$ 132,171	$ -	$ 495,228
Secured by 1-4 family residential properties	115,732	577	22,084	224	138,617
Secured by nonfarm, nonresidential properties	1,345,584	14,062	127,679	431	1,487,756
Other	201,610	317	6,856	-	208,783
Commercial and industrial loans	994,624	27,545	54,545	1,409	1,078,123
Consumer loans	647	-	-	-	647
Other loans	519,273	207	3,885	135	523,500
	$ 3,501,309	$ 81,926	$ 347,220	$ 2,199	$ 3,932,654

	Consumer Loans					
	Current	Past Due 30-89 Days	Past Due Greater Than 90 days	Nonaccrual	Subtotal	Total Loans
Loans secured by real estate:						
Construction, land development and other land loans	$ 55,367	$ 416	$ -	$ 1,945	$ 57,728	$ 552,956
Secured by 1-4 family residential properties	1,564,509	13,788	2,530	17,574	1,598,401	1,737,018
Secured by nonfarm, nonresidential properties	955	-	-	-	955	1,488,711
Other	8,121	48	-	34	8,203	216,986
Commercial and industrial loans	4,030	72	-	33	4,135	1,082,258
Consumer loans	344,666	8,815	2,226	1,516	357,223	357,870
Other loans	4,639	151	-	-	4,790	528,290
	$ 1,982,287	$ 23,290	$ 4,756	$ 21,102	$ 2,031,435	$ 5,964,089

	December 31, 2010				
	Commercial Loans				
	Pass -	Special Mention -	Substandard -	Doubtful - Category 9	Subtotal

	Categories 1-6	Category 7	Category 8		
Loans secured by real estate:					
Construction, land development and other land loans	$ 347,287	$ 44,459	$ 134,503	$ 512	$ 526,761
Secured by 1-4 family residential properties	113,776	780	25,167	226	139,949
Secured by nonfarm, nonresidential properties	1,353,794	16,858	126,050	431	1,497,133
Other	216,022	180	7,418	-	223,620
Commercial and industrial loans	977,793	25,642	58,307	1,416	1,063,158
Consumer loans	524	-	-	-	524
Other loans	535,110	210	3,633	146	539,099
	$ 3,544,306	$ 88,129	$ 355,078	$ 2,731	$ 3,990,244

	Consumer Loans		
Past Due	Past Due Greater		Total