MIDSOUTH BANCORP INC
Form 10-K
March 16, 2010

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

FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2009
Commission File number 1-11826
MIDSOUTH BANCORP, INC.
(Exact name of registrant as specified in its charter)

Louisiana	72-1020809
(State of Incorporation)	(I.R.S. EIN Number)

102 Versailles Boulevard, Lafayette, Louisiana 70501
(Address of principal executive offices)

Registrant's telephone number, including area code: (337) 237-8343

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $.10 par value	New York Stock Exchange AMEX

Securities registered pursuant to Section 12(g) of the Act: none

Indicate by check mark if this registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes ¨ No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act.
Yes ¨ No þ

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 þ No ¨

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

Indicate by check mark if disclosure of delinquent filers in response to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K þ

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a nonaccelerated filer. A large accelerated filer ¨ An accelerated filer ¨ A nonaccelerated filer þ A smaller reporting company ¨

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

The aggregate market value of the voting and nonvoting common equity held by nonaffiliates of the registrant at June 30, 2009 was approximately $67,825,346 based upon the closing market price on NYSE Amex as of such date. As of March 15, 2010 there were 9,723,268 outstanding shares of MidSouth Bancorp, Inc. common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company’s Proxy Statement for its 2010 Annual Meeting of Shareholders are incorporated by reference into Part III, Items 9-13 of this Form 10-K.

MIDSOUTH BANCORP, INC.
2009 Annual Report on Form 10-K
TABLE OF CONTENTS

Table of Contents

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements included in this Report and the documents incorporated by reference herein, 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," "gui "continue," "project," "forecast," "confident," and similar expressions are typically used to identify forward-lookin 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 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 ("ALLL"), which could result in greater than expected loan losses;
- changes in the availability of funds resulting from reduced liquidity or increased costs;
- the timing and impact of future acquisitions, the success or failure of integrating operations, and the ability to capitalize on growth opportunities upon entering new markets;
- the ability to acquire, operate, and maintain effective and efficient operating systems;
- 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 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, and changes in the U.S. Treasury's Capital Purchase Program;
- changes in accounting principles, policies, and guidelines applicable to bank holding companies and banking;
- acts of war, terrorism, 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 do, 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.

Table of Contents

Part I

Item 1 - Business

Overview

The Company was incorporated in 1984 as a Louisiana corporation and a registered bank holding company headquartered in Lafayette, Louisiana. Since February 2008, its operations have been conducted primarily through its wholly owned bank subsidiary, MidSouth Bank, N.A. Prior to February 2008, we owned and operated two separate banking subsidiaries that we merged together in order to consolidate operations and reduce expenses. The Bank, a national banking association, was chartered and commenced operations in 1985. As of December 31, 2009, the Bank operated through a network of 35 offices and more than 50 ATMs located in south Louisiana and southeast Texas.

Unless otherwise indicated or unless the context requires otherwise, all references in this report to the “Company,” “we,” “us,” “our,” or similar references, mean MidSouth Bancorp, Inc. and our subsidiaries, including our banking subsidiary, MidSouth Bank, N.A., on a consolidated basis. References to “MidSouth Bank” or the “Bank” mean our wholly owned banking subsidiary, MidSouth Bank, N.A.

Products and Services

The Bank is community oriented and focuses primarily on offering commercial and consumer loan and deposit services to small and middle market businesses, their owners and employees, and other individuals in our markets. Our community banking philosophy emphasizes personalized service and building broad customer relationships. Deposit products and services offered by the Bank include interest-bearing and noninterest-bearing checking accounts, investment accounts, cash management services, electronic banking services, including remote deposit capturing services and credit cards. Most of the Bank’s deposit accounts are FDIC-insured up to the maximum allowed and the Bank is a member of the Pulse network, which provides customers with ATM services through the Pulse and Cirrus networks throughout the world.

Loans offered by the Bank include commercial and industrial loans, commercial real estate loans (both owner-occupied and non-owner occupied), other loans secured by real estate and consumer loans. We commenced operations during a severe economic downturn in Louisiana almost 25 years ago. Our survival and growth in the ensuing years has instilled in us a conservative operating philosophy. Our conservative attitude impacts our credit and funding decisions, including underwriting loans primarily based on the cash flows of the borrower (rather than just relying on collateral valuations) and focusing lending efforts on working capital and equipment loans to small and mid-sized businesses along with owner-occupied properties.

Our conservative operating philosophy extends to managing the various risks we face. We maintain a separate risk management group to help identify and manage these various risks. This group, which reports directly to the Chairman of our Audit Committee, not to other members of the senior management team, includes our audit, collections, compliance, in-house legal counsel, loan review and security functions and is staffed with experienced accounting and legal professionals.

We are committed to maintaining an exceptional level of customer care. We maintain our own in-house call center so that customers enjoy live interaction with employees of the Bank rather than an automated telephone system. Additionally, we provide our employees with the training and technological tools to improve customer care. We have also implemented a customer relationship management database that serves not only as a sales tool but also helps us ensure delivery of outstanding service to our customers. In addition, we conduct focus groups within the communities we serve and strive to create a two-way dialog to ensure that we are offering the banking products and services that our customers and communities need.

Markets

We operate in south Louisiana and southeast Texas along the Interstate 10, Interstate 49 and Highway 90 corridors. As of December 31, 2009, our market area in south Louisiana included 27 offices and is bound by Houma to the south, Baton Rouge to the east, Opelousas to the north and Lake Charles to the west. Our market area in southeast Texas included eight offices and includes the Beaumont, College Station, Conroe and Houston areas. For additional information regarding our properties, see Item 2 – Properties of this Report.

Table of Contents

We believe that high energy prices and continued rebuilding from the storms of 2005 in Louisiana and Texas have partially insulated our markets from the full impact of the national recession. Furthermore, our markets have not experienced the severity of real estate price declines that have plagued so much of the country, and have generally suffered fewer job losses than the rest of the U.S. Oil and gas is the key industry within our markets. However, technology and research companies continue to develop within these markets thereby diversifying the economy. Additionally, numerous major universities located within our market areas, including Louisiana State University, University of Houston, Rice University, Texas A&M University and University of Louisiana at Lafayette, provide a substantial number of jobs and help to contribute to the educated work force within our current markets.

We believe our current financial condition coupled with our scalable operational capabilities, will facilitate future growth, both organically and through acquisition, including potential growth in new market areas.

Competition

We face strong competition in our market areas from both traditional and nontraditional financial services providers, such as commercial banks; savings banks; credit unions; finance companies; mortgage, leasing, and insurance companies; money market mutual funds; brokerage houses; and branches that provide credit facilities. Several of the financial services competitors in our market areas are substantially larger and have far greater resources, however we have effectively competed by building long-term customer relationships. Customer loyalty has been built through our continued focus on quality customer care enhanced by current technology and effective delivery systems.

Other factors, including economic, legislative, and technological changes, also impact our competitive environment. Management continually evaluates competitive challenges in the financial services industry and develops appropriate responses consistent with our overall market strategy.

Employees

As of December 31, 2009, the Bank employed approximately 416 full-time equivalent employees. The Company has no employees who are not also employees of the Bank. Through the Bank, employees receive customary employee benefits, which include an employee stock ownership plan; a 401(K) plan; and life, health and disability insurance plans. Our directors, officers, and employees are important to the success of the Company and play a key role in business development by actively participating in the communities served by the Company. The Company considers the relationship of the Bank with its employees to be excellent.

Additional Information

More information on the Company and the Bank is available on the Bank’s website at www.midsouthbank.com. The Company is not incorporating by reference into this Report the information contained on its website and, therefore, the content of the website is not a part of this Report. Copies of this Report and other reports filed or furnished by the Company pursuant to Section 13(a) or 15(d) of the Exchange Act, including exhibits, are available free of charge on the Company’s website under the “Investor Relations” link as soon as reasonably practicable after they have been filed or furnished electronically to the Securities and Exchange Commission (“SEC”). Copies of these filings may also be obtained free of charge on the SEC’s website at www.sec.gov.

Supervision and Regulation

Under Federal Reserve policy, we are expected to act as a source of financial strength for, and to commit resources to support, the Bank. This support may be required at times when, absent such Federal Reserve policy, we may not be inclined to provide such support. In addition, any capital loans by a bank holding company to any of its banking subsidiaries are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary banks. In the event of a bank holding company's bankruptcy, any commitment by a bank holding company to a federal bank regulatory agency to maintain the capital of a banking subsidiary will be assumed by the bankruptcy trustee and entitled to a priority of payment.

Prompt Corrective Action

The Federal Deposit Insurance Corporation Improvement Act of 1991 (“FDICIA”) established a system of prompt corrective action to resolve the problems of undercapitalized institutions. Under this system, the federal banking regulators have established five capital categories (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized), and are required to take certain mandatory

Table of Contents

supervisory actions, and are authorized to take other discretionary actions, with respect to institutions in the three undercapitalized categories. The severity of the action will depend upon the capital category in which the institution is placed. Generally, subject to a narrow exception, the banking regulator must appoint a receiver or conservator for an institution that is critically undercapitalized. The federal banking agencies have specified by regulation the relevant capital level for each category.

An institution that is categorized as undercapitalized, significantly undercapitalized, or critically undercapitalized is required to submit an acceptable capital restoration plan to its appropriate federal regulatory agency. A bank holding company must guarantee that a subsidiary depository institution meets its capital restoration plan, subject to certain limitations. The controlling holding company's obligation to fund a capital restoration plan is limited to the lesser of 5.0% of an undercapitalized subsidiary's assets or the amount required to meet regulatory capital requirements. An undercapitalized institution is also generally prohibited from increasing its average total assets, making acquisitions, establishing any branches or engaging in any new line of business, except under an accepted capital restoration plan or with FDIC approval. In addition, the appropriate federal regulatory agency may treat an undercapitalized institution in the same manner as it treats a significantly undercapitalized institution if it determines that those actions are necessary.

At December 31, 2009, the Bank had the requisite capital level to qualify as “well capitalized” under the regulatory framework for prompt corrective action.

FDIC Insurance Assessments

The Bank is a member of, and pays its deposit insurance assessments to the Deposit Insurance Fund (the “DIF”), as well as assessments by the FDIC to pay interest on Financing Corporation (“FICO”) bonds. The FDIC establishes rates for the payment of premiums by federally insured banks and federal savings associations for deposit insurance. The FDIC has revised its risk-based assessment system as required by the FDICIA. Under current FDIC rules, banks and federal savings associations must pay assessments to the FDIC for federal deposit insurance protection at rates based on their risk classification. Institutions assigned to higher risk classifications (that is, institutions that pose a higher risk of loss to the FDIC’s DIF under this assessment system) pay assessments at higher rates than institutions that pose a lower risk. An institution’s risk classification is assigned based on its capital levels and the level of supervisory concern the institution poses to the regulators. In addition, the FDIC can impose special assessments in certain instances.

Beginning on January 1, 2009, the FDIC raised the assessment rate schedule, uniformly across all four risk categories into which the FDIC assigns insured institutions, by seven basis points (annualized) of insured deposits. On February 27, 2009, the FDIC adopted a new final rule, effective April 1, 2009, which changes the FDIC’s deposit insurance assessment system’s evaluation of risk, makes corresponding changes to risk assessment rates beginning with the second quarter of 2009 and makes other changes to the deposit insurance assessment rules. The new rule includes: (1) a potential decrease in assessment rates for FDIC members using long-term unsecured debt, including senior and subordinated debt and, for small institutions with assets under $10 billion, a portion of tier 1 capital; (2) a potential increase in assessment rates for secured liabilities above a threshold amount; and (3) for non-Risk Category I institutions, a potential increase in assessment rates for brokered deposits above a threshold amount. For institutions in Risk Category I, the brokered deposit adjustment is only applicable if the institution’s brokered deposits are funding “rapid asset growth” which is defined as having assets greater than 40% four years ago, after adjusting for mergers and acquisitions. The new brokered deposit adjustment is intended to discourage the use of such deposits as wholesale funding for the growth of an institution.

Risk Category	First Quarter 2009 Deposit Insurance	Second Quarter 2009 Deposit Insurance

	Assessment Rate	Initial Base Assessment Rate
I	12 to 14 basis points	12 to 16 basis points
II	17 basis points	22 basis points
III	35 basis points	32 basis points
IV	50 basis points	45 basis points

In addition, on May 22, 2009, the FDIC adopted a final rule imposing an emergency special assessment of five basis points on each FDIC-insured depository institution's assets, minus its Tier 1 capital, as of June 30, 2009. The Bank's special assessment was approximately $416,000. On November 12, 2009, the FDIC issued a final rule

Table of Contents

requiring insured institutions to prepay their estimated quarterly risk-based assessments for the fourth quarter of 2009, and for all of 2010, 2011, and 2012. The prepaid assessment for these periods was collected on December 30, 2009, along with each institution's regular quarterly risk-based deposit insurance assessment for the third quarter of 2009. For purposes of estimating an institution's assessments for the fourth quarter of 2009, and for all of 2010, 2011, and 2012, and calculating the amount that an institution will prepay on December 30, 2009, the institution's assessment rate was its total base assessment rate in effect on September 30, 2009. The amount of our prepayment was approximately $4.7 million. Under the final rule, the FDIC may exercise its discretion as supervisor and insurer to exempt an institution from the prepayment requirement if the FDIC determines that the prepayment would adversely affect the safety and soundness of the institution. The FDIC Board also voted to adopt a uniform three basis point increase in assessment rates effective on January 1, 2011, and to extend the restoration period from seven to eight years. The FDIC may require additional special assessments and/or further increases in deposit insurance premiums.

Financial institutions that participate in the FDIC Temporary Liquidity Guarantee Program's ("TLGP") noninterest bearing transaction account guarantee, including the Bank, will pay the FDIC an annual assessment of 10 basis points on the amounts in such accounts above the amounts covered by FDIC deposit insurance through December 31, 2009, and if not opted out on or before November 2, 2009, an assessment of 15, 20, or 25 basis points for the extended period of January 1, 2010 through June 30, 2010 depending on an institution's risk profile. Based on the Bank's current risk profile, our assessment rate for the extended period of January 1, 2010 through June 30, 2010 is 15 basis points. Neither the Bank nor the Company has issued debt under the TLGP. To the extent that these FDIC TLGP assessments are insufficient to cover any loss or expenses arising from the FDIC TLGP, the FDIC is authorized to impose an emergency special assessment on FDIC-insured depository institutions. Legislation has been proposed to give the FDIC authority to impose charges for the FDIC TLGP upon depository institution holding companies as well.

As indicated above, the Bank's deposit insurance costs increased significantly in 2009 and may increase further. Any additional increase in insurance assessments could have an adverse effect on the Bank's earnings.

FICO assessments are set by the FDIC quarterly and are used towards the retirement of FICO bonds issued in the 1980s to assist in the recovery of the savings and loan industry. These assessments will continue until the FICO Bonds mature in 2017. The FICO assessment rate increased to 1.14 basis points for the first quarter of 2009, but declined to 1.02 basis points for the fourth quarter of 2009. The FICO assessment rate for the first quarter of 2010 is 1.06 basis points.

Allowance for Loan and Lease Losses

The Allowance for Loan and Lease Losses (the "ALLL") represents one of the most significant estimates in the Bank's financial statements and regulatory reports. Because of its significance, the Bank has established a system by which it develops, maintains, and documents a comprehensive, systematic, and consistently applied process for determining the amounts of the ALLL and the provision for loan and lease losses. The Interagency Policy Statement on the ALLL, issued on December 13, 2006, encourages all banks and federal savings institutions to ensure controls are in place to consistently determine the ALLL in accordance with generally accepted accounting principles in the United States, the federal savings association's stated policies and procedures, management's best judgment and relevant supervisory guidance. The Bank's estimate of credit losses reflects consideration of significant factors that affect the collectability of the portfolio as of the evaluation date.

Safety and Soundness Standards

The Federal Deposit Insurance Act, as amended by the FDICIA and the Riegle Community Development and Regulatory Improvement Act of 1994, requires the federal bank regulatory agencies to prescribe standards, by regulations or guidelines, relating to internal controls, information systems and internal audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, asset quality, earnings, stock valuation and compensation, fees and benefits, and such other operational and managerial standards as the agencies deem appropriate. The federal bank regulatory agencies have adopted a set of guidelines prescribing safety and soundness standards pursuant to FDICIA, as amended. The guidelines establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth and compensation and fees and benefits. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as

Table of Contents

excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director, or principal shareholder. In addition, the agencies adopted regulations that authorize, but do not require, an agency to order an institution that has been given notice by an agency that it is not satisfying any of such safety and soundness standards to submit a compliance plan. If, after being so notified, an institution fails to submit an acceptable compliance plan or fails in any material respect to implement an acceptable compliance plan, the agency must issue an order directing action to correct the deficiency and may issue an order directing other actions of the types to which an undercapitalized institution is subject under the "prompt corrective action" provisions of FDICIA. See "-Prompt Corrective Action" above. If an institution fails to comply with such an order, the agency may seek to enforce such order in judicial proceedings and to impose civil money penalties. The federal regulatory agencies also proposed guidelines for asset quality and earnings standards.

Community Reinvestment Act

Under the Community Reinvestment Act ("CRA") the Bank, as an FDIC insured institution, has a continuing and affirmative obligation to help meet the credit needs of the entire community, including low- and moderate-income neighborhoods, consistent with safe and sound banking practices. The CRA requires the appropriate federal regulator, in connection with its examination of an insured institution, to assess the institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications, such as applications for a merger or the establishment of a branch. An unsatisfactory rating may be used as the basis for the denial of an application by the federal banking regulator. The Bank received a satisfactory rating in its most recent CRA examination.

Restrictions on Transactions with Affiliates

We are subject to the provisions of Section 23A of the Federal Reserve Act. Section 23A places limits on: the amount of a bank's loans or extensions of credit to affiliates; a bank's investment in affiliates; assets a bank may purchase from affiliates, except for real and personal property exemption by the Federal Reserve; the amount of loans or extensions of credit to third parties collateralized by the securities or obligations of affiliates; and a bank's guarantee, acceptance or letter of credit issued on behalf of an affiliate.

The total amount of the above transactions is limited in amount, as to any one affiliate, to 10.0% of a bank's capital and surplus and, as to all affiliates combined, to 20.0% of a bank's capital and surplus. In addition to the limitation on the amount of these transactions, each of the above transactions must also meet specified collateral requirements. The Bank must also comply with other provisions designed to avoid the taking of low-quality assets.

We are also subject to the provisions of Section 23B of the Federal Reserve Act which, among other things, prohibit an institution from engaging in the above transactions with affiliates unless the transactions are on terms substantially the same, or at least as favorable to the institution or its subsidiaries, as those prevailing at the time for comparable transactions with nonaffiliated companies.

The Bank is also subject to restrictions on extensions of credit to its executive officers, directors, principal shareholders and their related interests. These extensions of credit must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third parties, and must not involve more than the normal risk of repayment or present other unfavorable features.

USA Patriot Act of 2001

In October 2001, the USA Patriot Act of 2001 (the "Patriot Act") was enacted in response to the terrorist attacks in New York, Pennsylvania, and Washington, D.C. that occurred on September 11, 2001. The Patriot Act impacts financial institutions in particular through its anti-money laundering and financial transparency laws. The Patriot Act amended the Bank Secrecy Act and the rules and regulations of the Office of Foreign Assets Control to establish regulations which, among others, set standards for identifying customers who open an account and promoting cooperation with law enforcement agencies and regulators in order to effectively identify parties that may be associated with, or involved in, terrorist activities or money laundering.

In 2006, Congress passed the USA Patriot Act Improvement and Reauthorization Act of 2005. This act reauthorized all provisions of the Patriot Act that would otherwise have expired, made 14 of the 16 sunsetting provisions permanent, and extended the sunset period of the remaining two for an additional four years.

Table of Contents

Privacy

Financial institutions are required to disclose their policies for collecting and protecting confidential information. Customers generally may prevent financial institutions from sharing personal financial information with nonaffiliated third parties except for third parties that market the institutions' own products and services.

Additionally, financial institutions generally may not disclose consumer account numbers to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing through electronic mail to consumers. The Bank has established policies and procedures designed to safeguard its customers' personal financial information and to ensure compliance with applicable privacy laws.

Other Regulations

Interest and other charges collected or contracted for by the Bank are subject to federal laws concerning interest rates. The Bank's loan operations are also subject to federal laws applicable to credit transactions, such as the:

- Federal Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
- Home Mortgage Disclosure Act of 1975, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed, or other prohibited factors in extending credit;
- Fair Credit Reporting Act of 1978, governing the use and provision of information to credit reporting agencies; and
- rules and regulations of the various federal agencies charged with the responsibility of implementing these federal laws.

The deposit operations of the Bank are subject to the following:

- the Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
- the Electronic Funds Transfer Act and Regulation E issued by the Federal Reserve to implement that act, which govern automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services; and
- the Truth in Savings Act, which requires disclosure of yields and costs of deposits and deposit accounts.

Effect of Governmental Monetary Policies

Our earnings are affected by the monetary and fiscal policies of the United States government and its agencies, as well as general domestic economic conditions. The Federal Reserve's power to implement national monetary policy has had, and is likely to continue to have, an important impact on the operating results of financial institutions. The Federal Reserve affects the levels of bank loans, investments, and deposits through its control over the issuance of U.S. government securities and through its regulation of the discount rate on borrowings of member banks and the reserve requirements against member bank deposits. It is not possible to predict the nature or impact of future changes in monetary and fiscal policies.

In 2008 and 2009, the Federal Reserve has taken various actions to increase market liquidity and reduce interest rates. The Federal Reserve lowered its target federal funds rate from 5.25% per annum on August 7, 2007 to 3.00% on January 30, 2008, and finally to a range of 0% to 0.25% on December 16, 2008. The Federal Reserve's discount rate was reduced on December 16, 2008 to its current rate of 0.50% per annum, down from 5.75% on September 17, 2007, 4.75% on January 2, 2008 and 1.25% on October 29, 2008. The Federal Reserve has extended the term for which institutions can borrow from the discount window to up to 90 days, and it has developed a program, called the

Term Auction Facility, under which predetermined amounts of credit are auctioned to depository institutions for terms of up to 84 days. These innovations resulted in large increases in the amount of Federal Reserve credit extended to the banking system.

In addition, the Federal Reserve and the Treasury have jointly announced a Term Asset-Backed Securities Loan Facility (“TALF”) that currently will lend against AAA-rated asset-backed securities that are determined eligible by

Table of Contents

the Federal Reserve. The Federal Reserve Bank of New York presently intends to make up to $200 billion of loans under TALF and may expand this loan program under TALF in the future. TALF loans will be non-recourse loans, secured by eligible ABS, and have three year terms. The Treasury has provided $20 billion of credit support to theFederal Reserve in connection with TALF, but may provide additional support in the future to enable expansion of the TALF.

Beginning October 6, 2008, the Federal Reserve began paying interest on depository institutions' required and excess reserve balances. The payment of interest on excess reserve balances was expected to give the Federal Reserve greater scope to use its lending programs to address conditions in credit markets while also maintaining the federal funds rate close to the target rate established by the Federal Open Market Committee.

The nature and timing of any changes in fiscal and monetary policies and their effect on our business cannot be predicted.

Emergency Economic Stabilization Act of 2008 and Subsequent Legislation
The Emergency Economic Stabilization Act of 2008 ("EESA") was enacted on October 3, 2008. EESA authorizes the U.S. Department of the Treasury ("Treasury") to invest up to $700 billion in troubled assets, to provide capital, or to otherwise provide assistance to U.S. banks, federal savings institutions and their holding companies ("TARP"). Pursuant to authority granted under EESA, the Treasury will invest or has invested up to $250 billion in senior preferred stock of U.S. banks and federal savings institutions or their holding companies under the Capital Purchase Program (the "CPP"). Qualifying financial institutions may issue senior preferred stock with a value equal to not less than 1% of risk-weighted assets and not more than the lesser of $25 billion or 3% of risk-weighted assets. In January 2009, we issued $20.0 million in Series A Preferred Stock to the Treasury under the CPP, which was promulgated under TARP.

As a result of our participation in the CPP, we are subject to the Treasury's standards for executive compensation and corporate governance as long as the Treasury holds the equity issued under the CPP. These standards generally apply to the chief executive officer, chief financial officer and the three next most highly compensated senior executive officers. The standards include: (1) ensuring that incentive compensation for senior executives does not encourage unnecessary and excessive risks that threaten the value of the financial institution; (2) required clawback of any bonus or incentive compensation paid to a senior executive based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate; (3) prohibitions on making golden parachute payments to senior executives; and (4) an agreement not to deduct for tax purposes executive compensation in excess of $500,000 for each senior executive.

On February 10, 2009, the Treasury announced the Financial Stability Plan (the "Financial Stability Plan"), which earmarked $350 billion of the TARP funds authorized under EESA. Among other things, the Financial Stability Plan includes:

- a capital assistance program ("CAP") that will invest in mandatory convertible preferred stock of certain qualifying institutions determined on a basis and through a process similar to the CPP;
- a consumer and business lending initiative to fund new consumer loans, small business loans and commercial mortgage asset-backed securities issuances;
- a new public-private investment fund that will leverage public and private capital with public financing to purchase up to $500 billion to $1 trillion of legacy "toxic assets" from financial institutions; and
- assistance for homeowners by providing up to $75 billion to reduce mortgage payments and interest rates and establishing loan modification guidelines for government and private programs.

Institutions receiving assistance under the Financial Stability Plan going forward will be subject to higher transparency, corporate governance and accountability standards, including restrictions on dividends, acquisitions, executive compensation and additional disclosure requirements.

On February 17, 2009, the American Recovery and Reinvestment Act (the "ARRA") became law. The ARRA purports to retroactively impose certain new executive compensation and corporate expenditure limits and corporate governance standards on all current and future recipients of TARP funds, including us, that are in addition to those previously announced by the Treasury, until the institution has repaid the Treasury.

Table of Contents

Recent Proposed Regulatory Changes

Legislative and regulatory proposals regarding changes in banking, and the regulation of banks, federal savings institutions, and other financial institutions and bank and bank holding company powers are being considered by the executive branch of the federal government, Congress and various state governments. Certain of these proposals, if adopted, could significantly change the regulation or operations of banks and the financial services industry. New regulations and statutes are regularly proposed that contain wide-ranging proposals for altering the structures, regulations, and competitive relationships of the nation's financial institutions. On June 17, 2009, Treasury released a white paper entitled "Financial Regulatory Reform – A New Foundation: Rebuilding Financial Supervision and Regulation" (the "Proposal") which calls for sweeping regulatory and supervisory reforms for the entire financial sector and seeks to advance the following five key objectives: (i) promote robust supervision and regulation of financial firms, (ii) establish comprehensive supervision of financial markets, (iii) protect consumers and investors from financial abuse, (iv) provide the government with additional powers to monitor systemic risks, supervise and regulate financial products and markets, and to resolve firms that threaten financial stability, and (v) raise international regulatory standards and improve international cooperation.

The Proposal includes the creation of a new federal government agency, the National Bank Supervisor ("NBS") that would charter and supervise all federally chartered depository institutions, and all federal branches and agencies of foreign banks. It is proposed that the NBS take over the responsibilities of the OCC, which currently charters and supervises nationally chartered banks, such as the Bank, and the responsibility for the institutions currently supervised by the Office of Thrift Supervision, which supervises federally chartered savings institutions and federal savings institution holding companies.

The elimination of the OCC, as proposed by the administration, also would result in a new regulatory authority for the Bank. There is no assurance as to how this new supervision by the NBS will affect our operations going forward.

The Proposal also includes the creation of a new federal agency designed to enforce consumer protection laws. The Consumer Financial Protection Agency ("CFPA") would have authority to protect consumers of financial products and services and to regulate all providers (bank and non-bank) of such services. The CFPA would be authorized to adopt rules for all providers of consumer financial services, supervise and examine such institutions for compliance, and enforce compliance through orders, fines, and penalties. The rules of the CFPA would serve as a "floor" and individual states would be permitted to adopt and enforce stronger consumer protection laws. If adopted as proposed, we may become subject to multiple laws affecting its provision of loans and other credit services to consumers, which may substantially increase the cost of providing such services.

Item 1A – Risk Factors

An investment in our stock involves a number of risks. Investors should carefully consider the following risks as well as the other information in this Report and the documents incorporated by reference before making an investment decision. The realization of any of the risks described below could have a material adverse effect on the Company and the price of our common stock.

Risks Relating to Our Business

The current economic environment poses significant challenges and could adversely affect our financial condition and results of operations.

There was significant disruption and volatility in the financial and capital markets during 2008 and 2009. The financial markets and the financial services industry in particular suffered unprecedented disruption, causing a number of institutions to fail or require government intervention to avoid failure. These conditions were largely the result of the erosion of the U.S. and global credit markets, including a significant and rapid deterioration in mortgage lending and related real estate markets. Continued declines in real estate values, high unemployment and financial stress on borrowers as a result of the uncertain economic environment could have an adverse effect on our borrowers or their customers, which could have a material adverse effect on our business, prospects, financial condition and results of operations.

As a consequence of the difficult economic environment, we experienced a significant decrease in earnings resulting primarily from increased provisions for loan losses. There can be no assurance that the economic conditions that have adversely affected the financial services industry, and the capital, credit and real estate markets generally, will improve in the near term, in which case we could continue to experience write-downs of assets, and could face capital and liquidity constraints or other business challenges. A further deterioration in economic conditions, particularly within our market areas, could result in the following consequences, any of which could have a material adverse effect on our business, prospects, financial condition and results of operations:

- Loan delinquencies may further increase causing additional increases in our provision and allowance for loan losses.
- Our ability to assess the creditworthiness of our customers may be impaired if the models and approaches we use to select, manage, and underwrite our customers become less predictive of future charge-offs.
- Collateral for loans made by the Bank, especially real estate, may continue to decline in value, in turn reducing a customer's borrowing power, and reducing the value of assets and collateral associated with our loans.
- Consumer confidence levels may decline and cause adverse changes in payment patterns, resulting in increased delinquencies and default rates on loans and other credit facilities and decreased demand for our products and services.

Our market areas are heavily dependent on, and we have significant credit exposure to, the oil and gas industry.

The economy in a large portion of our market areas is heavily dependent on the oil and gas industry. Many of our customers provide transportation and other services and products that support oil and gas exploration and production activities. Accordingly, as of December 31, 2009, we had approximately $117.5 million in loans to borrowers in the oil and gas industry, representing approximately 20.1% of our total loans outstanding as of that date. The oil and gas industry, especially in Louisiana and Texas, has been subject to significant volatility, including the "oil bust" of the 1980s that severely impacted the economies of many of our market areas. Recently, President Obama's administration proposed a number of legislative changes that could significantly impact the oil and gas industry, including the elimination of certain tax breaks, such as the intangible drilling and development costs, percentage depletion and manufacturing deduction, and the implementation of an excise tax focused specifically on production in the Gulf of Mexico. If there is a significant downturn in the oil and gas industry, generally the cash flows of our customers in this industry would be adversely impacted which could impair their ability to service our loans outstanding to them and/or reduce demand for loans. This could have a material adverse effect on our business, prospects, financial condition and results of operations.

We may suffer losses in our loan portfolio in excess of our allowance for loan losses.

We have experienced increases in the levels of our non-performing assets and loan charge-offs in recent periods. Our total non-performing assets amounted to $17.4 million, or 1.79% of our total assets, at December 31, 2009 and $11.0 million, or 1.17% of our total assets, at December 31, 2008. We had $5.0 million of net loan charge-offs for the year ended December 31, 2009 compared to $2.4 million for the year ended December 31, 2008. Our provision for loan losses was $5.5 million for the year ended December 31, 2009, compared to $4.6 million for the year ended December 31, 2008. At December 31, 2009, the ratios of our ALLL to non-performing loans and to total loans outstanding was 48.28% and 1.37%, respectively, compared to 73.22% and 1.25%, respectively, at December 31, 2008. Additional increases in our non-performing assets or loan charge-offs could have a material adverse effect on our financial condition and results of operations.

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. These practices include analysis of a borrower's prior credit history, financial statements, tax returns and cash flow projections, valuation of collateral based on reports of independent appraisers and verification of liquid assets. Although we believe that our underwriting criteria are appropriate for the various kinds of loans we make, we still may incur losses on loans that meet our underwriting criteria, and these losses may exceed the amounts set aside as reserves in our ALLL. We create an ALLL in our accounting records, based on, among other considerations, the following:

- industry historical losses as reported by the FDIC;
- historical experience with our loans;
- evaluation of economic conditions;
- regular reviews of the quality mix, including our distribution of loans by risk grade within our portfolio, and size of our overall loan portfolio;

Table of Contents

- regular reviews of delinquencies; and
- the quality of the collateral underlying our loans.

Although we maintain an ALLL at a level that we believe is adequate to absorb losses inherent in our loan portfolio, changes in economic, operating and other conditions, including conditions which are beyond our control such as a sharp decline in real estate values and changes in interest rates, may cause our actual loan losses to exceed our current allowance estimates. Additions to the ALLL could result in a decrease in net earnings and capital and could hinder our ability to grow. Further, if our actual loan losses exceed the amount reserved, it could have a material adverse effect on our financial condition and results of operations.

We cannot predict the effect of recent or future legislative and regulatory initiatives.
Financial institutions have been the subject of substantial legislative and regulatory changes and may be the subject of further legislation or regulation in the future, including: (i) changes in banking, securities and tax laws and regulations and their application by our regulators; (ii) changes in the scope and cost of FDIC insurance and other coverages; and (iii) changes in the CPP under TARP administered by the Treasury which we participated in by issuing $20.0 million in shares of our Series A Preferred Stock and associated common stock warrants to the Treasury in January 2009 (the "CPP Transaction"), none of which is within our control. Significant new laws or regulations or changes in, or repeals of, existing laws or regulations may cause our results of operations to differ materially from those we currently anticipate. In addition, the cost and burden of compliance with applicable laws and regulations have significantly increased and could adversely affect our ability to operate profitably. Further, federal monetary policy significantly affects credit conditions for us, as well as for our borrowers, particularly as implemented by the Federal Reserve Board, primarily through open market operations in U.S. government securities, the discount rate for bank borrowings and reserve requirements. A material change in any of these conditions could have a material impact on us or our borrowers, and therefore on our business, prospects, financial condition and results of operations.

On October 3, 2008, the EESA was enacted in an effort to stabilize the financial markets. Pursuant to the EESA, the Treasury was granted the authority to take a range of actions for the purpose of stabilizing and providing liquidity to the U.S. financial markets and has proposed several programs in addition to TARP, including the purchase by the Treasury of certain troubled assets from financial institutions. There can be no assurance, however, as to the actual impact that the foregoing or any other governmental program will have on the financial markets. The failure of the financial markets to stabilize and a continuation or worsening of current financial market conditions could have a material adverse effect on our business, prospects, financial condition, results of operations, access to credit or the trading price of our common stock. In addition, current initiatives of President Obama's administration with respect to the financial services industry could have a material adverse effect on our business, prospects, financial condition and results of operations.

We expect to face increased regulation and supervision of our industry as a result of the existing financial crisis, and there may be additional requirements and conditions imposed on us as a result of our issuance of the Series A Preferred Stock in the CPP Transaction. Such additional regulation and supervision may increase our costs and limit our ability to pursue business opportunities. The affects of such recently enacted, and proposed, legislation and regulatory programs on us cannot reliably be determined at this time.

We have a concentration of exposure to a number of individual borrowers. Given the size of these loan relationships relative to capital levels and earnings, a significant loss on any one of these loans could materially and adversely affect us.
We have a concentration of exposure to a number of individual borrowers. Our largest exposure to one borrowing relationship as of December 31, 2009, was approximately $8.0 million, which is 6.16% of our total capital. In addition, as of December 31, 2009, the aggregate exposure to the ten largest borrowing relationships was approximately $56.5 million, which was 9.66% of loans and 43.36% of total capital. As a result of this concentration,

a change in the financial condition of one or more of these borrowers could result in significant loan losses and have a material adverse effect on our financial condition and results of operations.

Table of Contents

A large percentage of our deposits is attributable to a relatively small number of customers. The loss of all or some of these customers or a significant decline in their deposit balances may have a material adverse effect on our liquidity and results of operations.

Our 20 largest depositors accounted for approximately 15.98% of our total deposits and our five largest depositors accounted for approximately 8.84% of our total deposits as of December 31, 2009. The ability to attract these types of deposits has a positive effect on our net interest margin as they provide a relatively low cost of funds to the Bank. While we believe we have strong, long-term relationships with each of these customers, the loss of one or more of our 20 largest customers, or a significant decline in the deposit balances would adversely affect our liquidity and require us to attract new deposits, purchase federal funds or borrow funds on a short term basis to replace such deposits, possibly at interest rates higher than those currently paid on these deposits. This could increase our total cost of funds and could result in a decrease in our net interest income and net earnings. If we were unable to develop alternative funding sources, we may have difficulty funding loans or meeting other deposit withdrawal requirements.

We occasionally purchase non-recourse loan participations from other banks based in part on information provided by the selling bank.
From time to time, we purchase loan participations from other banks in the ordinary course of business, usually without recourse to the selling bank. As of December 31, 2009, we had approximately $49.8 million in purchased loan participations, or approximately 8.5% of our total loan portfolio. When we purchase loan participations, we apply the same underwriting standards as we would to loans that we directly originate and seek to purchase only loans that would satisfy these standards. However, we are less likely to be familiar with the borrower and may rely to some extent on information provided to us by the selling bank and typically must rely on the selling bank's administration of the loan relationship. We therefore have less control over, and may incur more risk with respect to, loan participations that we purchase from selling banks as compared to loans that we originate.

Our focus on lending to small to mid-sized community-based businesses may increase our credit risk.
Most of our commercial business and commercial real estate loans are made to small business or middle market customers. These businesses generally have fewer financial resources in terms of capital or borrowing capacity than larger entities and have a heightened vulnerability to economic conditions. If general economic conditions in the markets in which we operate negatively impact this important customer sector, our results of operations and financial condition and the value of our common stock may be adversely affected. Moreover, a portion of these loans have been made by us in recent years and the borrowers may not have experienced a complete business or economic cycle. Furthermore, the deterioration of our borrowers' businesses may hinder their ability to repay their loans with us, which could have a material adverse effect on our financial condition and results of operations.

Our loan portfolio includes a substantial percentage of commercial and industrial loans, which may be subject to greater risks than those related to residential loans.
Our loan portfolio includes a substantial percentage of commercial and industrial loans. Commercial and industrial loans generally carry larger loan balances and historically have involved a greater degree of financial and credit risks than residential first mortgage loans. Repayment of our commercial and industrial loans is often dependent on cash flow of the borrower, which may be unpredictable, and collateral securing these loans may fluctuate in value. Our commercial and industrial loans are primarily made based on the cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. Most often, this collateral is accounts receivable, inventory, equipment, or real estate. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers. Other collateral securing loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business. At December 31, 2009, commercial and industrial loans totaled approximately 32.9% of our total loan portfolio. Adverse changes in local economic conditions

impacting our business borrowers could have a material adverse effect on our business, prospects, financial condition and results of operations.

We have a high concentration of loans secured by real estate, and the current downturn in the real estate market could have a material adverse effect on our financial condition and results of operations.
A significant portion of our loan portfolio is dependent on real estate. At December 31, 2009, approximately 52% of our loans had real estate as a primary or secondary component of collateral. The collateral in each case provides an alternate source of repayment if the borrower defaults and may deteriorate in value during the time the credit is

Table of Contents

extended. An adverse change in the economy affecting values of real estate in our primary markets could significantly impair the value of real estate collateral and the ability to sell real estate collateral upon foreclosure. Furthermore, it is likely that we would be required to increase the provision for loan losses. A related risk in connection with loans secured by real estate is the effect of unknown or unexpected environmental contamination, which could make the real estate effectively unmarketable or otherwise significantly reduce its value as collateral. If we were required to liquidate real estate collateral securing a loan to satisfy the debt during a period of reduced real estate values or to increase the allowance for loan losses, it could have a material adverse effect on our financial condition and results of operations.

We may face risks with respect to future expansion and acquisition opportunities.
We have expanded our business in part through acquisitions and will continue to look at future acquisitions as a way to further increase our growth. However, we cannot assure you that we will be successful in completing any future acquisitions. Further, failure to realize the potential expected revenue increases, cost savings, increases in geographic or product presence, and/or other projected benefits from an acquisition could have a material adverse effect on our business, prospects, financial condition and results of operations.

We may seek merger or acquisition partners that are culturally similar and have experienced management and possess either significant market presence or have potential for improved profitability through financial management, economies of scale or expanded services. We do not currently have any specific plans, arrangements or understandings regarding such expansion. We cannot say with any certainty that we will be able to consummate, or if consummated, successfully integrate future acquisitions or that we will not incur disruptions or unexpected expenses in integrating such acquisitions. In attempting to make such acquisitions, we anticipate competing with other financial institutions, many of which have greater financial and operational resources. Acquiring other banks, businesses, or branches involves various risks commonly associated with acquisitions, including, among other things:

- potential exposure to unknown or contingent liabilities of the target company;
- expansion into new markets that may have different characteristics than our current markets and may otherwise present management challenges;
- exposure to potential asset quality issues of the target company;
- difficulty and expense of integrating the operations and personnel of the target company;
- potential disruption to our business;
- potential diversion of management’s time and attention;
- the possible loss of key employees and customers of the target institution;
- difficulty in estimating the value of the target company; and
- potential changes in banking, accounting or tax laws or regulations that may affect the target institution.

If we acquire the assets and liabilities of one or more target banks that are in receivership through the FDIC bid process for failed institutions, such an acquisition will require us, through our bank subsidiary, to enter into a Purchase & Assumption Agreement (the “P&A Agreement”) with the FDIC. The P&A Agreement is a form document prepared by the FDIC, and our ability to negotiate the terms of this agreement is limited. As a result, we expect that any P&A Agreement would provide for limited disclosure about, and limited indemnification for, risks associated with the target bank. There is a risk that such disclosure regarding, and indemnification for, the assets and liabilities of target banks will not be sufficient and we will incur unanticipated losses. There is also a risk that we may be required to make an additional payment to the FDIC under certain circumstances following the completion of an FDIC-assisted acquisition if, for example, actual losses related to the target bank’s assets acquired are substantially less than expected at the time the P&A Agreement was entered into.

In addition, the FDIC bid process for failed depository institutions is competitive. We cannot provide any assurances that we will be successful in bidding for any target bank or for other failed depository institutions.

Our future earnings could be adversely affected by non-cash charges for goodwill impairment, if a future test of goodwill indicates that goodwill has been impaired.
As prescribed by Accounting Standards Codification ("ASC") Topic 350, "Intangibles — Goodwill and Other," we undertake an annual review of the goodwill asset balance reflected in our financial statements. We conduct an annual review in the fourth quarter of each year, unless there has been a triggering event prescribed by applicable

accounting rules that warrants an earlier interim testing for possible goodwill impairment. During the first quarter of 2009, we conducted an interim test and, upon review and analysis of the factors influencing value and utilizing the market value and investment value approaches, concluded there was no goodwill impairment as of such date. In addition, after our annual review in the fourth quarter of 2009, we concluded there was no goodwill impairment as of such date. As of December 31, 2009, we had $9.5 million in goodwill. Future goodwill impairment tests may result in future non-cash charges, which could adversely affect our earnings for any such future period.

Changes in the fair value of our securities may reduce our shareholders' equity and net income.
At December 31, 2009, $271.8 million of our securities (at fair value) were classified as available-for-sale. At such date, the aggregate net unrealized gain on our available-for-sale securities was $5.9 million. We increase or decrease shareholders' equity by the amount of change from the unrealized gain or loss (the difference between the estimated fair value and the amortized cost) of our available-for-sale securities portfolio, net of the related tax, under the category of accumulated other comprehensive income/loss. Therefore, a decline in the estimated fair value of this portfolio will result in a decline in reported shareholders' equity, as well as book value per common share and tangible book value per common share. This decrease will occur even though the securities are not sold. In the case of debt securities, if these securities are never sold and there are no credit impairments, the decrease will be recovered over the life of the securities. In the case of equity securities which have no stated maturity, the declines in fair value may or may not be recovered over time.

We continue to monitor the fair value of our entire securities portfolio as part of our ongoing other than temporary impairment ("OTTI") evaluation process. No assurance can be given that we will not need to recognize OTTI charges related to securities in the future. In addition, as a condition to membership in the Federal Home Loan Bank of Dallas ("FHLB-Dallas"), we are required to purchase and hold a certain amount of FHLB-Dallas stock. Our stock purchase requirement is based, in part, upon the outstanding principal balance of advances from the FHLB-Dallas. At December 31, 2009, we had stock in the FHLB-Dallas totaling approximately $562,000. The FHLB-Dallas stock held by us is carried at cost and is subject to recoverability testing under applicable accounting standards. For the year ended December 31, 2009, we did not recognize an impairment charge related to our FHLB-Dallas stock holdings. There can be no assurance, however, that future negative changes to the financial condition of the FHLB-Dallas may not require us to recognize an impairment charge with respect to such holdings.

We rely heavily on our management team and the loss of key officers may adversely affect operations.
Our success has been and will continue to be greatly influenced by the ability to retain existing senior management and, with expansion, to attract and retain qualified additional senior and middle management. C.R. Cloutier, President and Chief Executive Officer, and other executive officers have been instrumental in developing and managing our business. We recently had a number of changes in our senior management team, including the appointment of a new Chief Financial Officer and the resignations of our chief lending officer and the head of the retail division of the Bank. The loss of the services of these individuals, or future unexpected loss of services of Mr. Cloutier or any other current executive could have an adverse effect on us. We do not have an employment agreement with Mr. Cloutier and a formal management succession plan has not been established. No assurance can be provided that we will be able to locate and hire a qualified replacement for any of the recently departed officers or otherwise on a timely basis.

Our participation in the CPP Transaction could also have an adverse effect on our ability to attract and retain qualified executive officers. The American Recovery and Reinvestment Act of 2009 included amendments to the executive compensation provisions of the EESA under which the CPP was established, including extensive new restrictions on our ability to pay retention awards, bonuses and other incentive compensation during the period in which we have any outstanding securities held by the Treasury that were issued in the CPP Transaction. Many of the restrictions are not limited to our senior executives and cover other employees whose contributions to revenue and performance can be significant. The limitations may adversely affect our ability to recruit and retain these key employees in addition to our senior executive officers, especially if we are competing for talent against institutions that are not subject to the same CPP restrictions. The Federal Reserve, and perhaps the FDIC, are contemplating proposed rules governing the compensation practices of financial institutions and these rules, if adopted, may adversely affect our management retention and limit our ability to promote our objectives through our compensation and incentive programs and, as a result, adversely affect our results of operations and financial position.

The full scope and impact of these limitations are uncertain and difficult to predict. The Treasury has adopted standards that implement certain compensation limitations, but these standards have not yet been broadly interpreted

Table of Contents

and remain, in many respects, ambiguous. The new and potential future legal requirements and implementing standards under the CPP may have unforeseen or unintended adverse effects on the financial services industry as a whole, and particularly on CPP participants, including us. It will likely require significant time, effort and resources on our part to interpret and apply them. If any of our regulators believe that our response to new and future legal requirements and implementing standards does not fully comply with them, it could subject us to regulatory actions or otherwise adversely affect our management retention and, as a result, our results of operations and financial condition.

Even if we redeem our Series A Preferred Stock and repurchase the warrant that we issued to the Treasury, we will continue to be subject to evolving legal and regulatory requirements that may, among other things, require increasing amounts of our time, effort and resources to ensure compliance.

A natural disaster, especially one affecting one of our market areas, could adversely affect us.
Since most of our business is conducted in Louisiana and Texas, most of our credit exposure is in those states. Historically, Louisiana and Texas have been vulnerable to natural disasters. Therefore, we are susceptible to the risks of natural disasters, such as hurricanes, floods and tornados. Natural disasters could harm our operations directly through interference with communications, including the interruption or loss of our websites, which would prevent us from gathering deposits, originating loans and processing and controlling our flow of business, as well as through the destruction of facilities and our operational, financial and management information systems. A natural disaster or recurring power outages may also impair the value of our largest class of assets, our loan portfolio, as uninsured or underinsured losses, including losses from business disruption, may reduce borrowers' ability to repay their loans. Disasters may also reduce the value of the real estate securing our loans, impairing our ability to recover on defaulted loans through foreclosure and making it more likely that we would suffer losses on defaulted loans. Although we have implemented several back-up systems and protections (and maintain business interruption insurance), these measures may not protect us fully from the effects of a natural disaster. The occurrence of natural disasters in our market areas could have a material adverse effect on our business, prospects, financial condition and results of operations.

Our profitability is vulnerable to interest rate fluctuations.
Our profitability is dependent to a large extent on net interest income, which is the difference between our interest income on interest-earning assets, such as loans and investment securities, and interest expense on interest-bearing liabilities, such as deposits and borrowings. When interest-bearing liabilities mature or reprice more quickly than interest-earning assets in a given period, a significant increase in market rates of interest could adversely affect net interest income. Conversely, when interest-earning assets mature or reprice more quickly than interest-bearing liabilities, falling interest rates could result in a decrease in net interest income. For example, as securities in our investment portfolio have matured, they have been replaced by securities paying a lower yield. We expect this trend to continue during 2010. These changes in our investment portfolio have negatively impacted, and are expected to continue to negatively impact, our net interest margin. Furthermore, some of our variable interest rate loans have minimum fixed interest rates ("floors") that are currently above the contractual variable interest rate. If interest rates rise, the interest income from our variable interest rate loans with floors may not increase as quickly as interest expense on our liabilities, which would negatively impact our net interest income.

In periods of increasing interest rates, loan originations may decline, depending on the performance of the overall economy, which may adversely affect income from lending activities. Also, increases in interest rates could adversely affect the market value of fixed income assets. In addition, an increase in the general level of interest rates may affect the ability of certain borrowers to pay the interest and principal on their obligations.

Non-performing assets take significant time to resolve and adversely affect our results of operations and financial condition.

Non-performing assets adversely affect our net earnings in various ways. Until economic and market conditions improve, we expect to continue to incur provisions for loan losses relating to an increase in non-performing assets. We generally do not record interest income on non-performing loans or other real estate owned, thereby adversely affecting our earnings, and increasing our loan administration costs. When we take collateral in foreclosures and similar proceedings, we are required to mark the related asset to the then fair market value of the collateral less estimated selling costs, which may ultimately result in a loss. An increase in the level of non-performing assets increases our risk profile and may impact the capital levels our regulators believe are appropriate in light of the ensuing risk profile. While we reduce problem assets through loan sales, workouts, restructurings and otherwise,

Table of Contents

decreases in the value of the underlying collateral, or in these borrowers' performance or financial condition, whether or not due to economic and market conditions beyond our control, could adversely affect our business, results of operations and financial condition. In addition, the resolution of non-performing assets requires significant commitments of time from management and our directors, which can be detrimental to the performance of their other responsibilities. There can be no assurance that we will not experience future increases in non-performing assets.

The soundness of other financial institutions could negatively affect us.
Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and we routinely execute transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by a counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due to us. Any such losses could have a material adverse effect on our business, prospects, financial condition and results of operations.

Higher FDIC deposit insurance premiums and assessments could adversely affect our financial condition.
FDIC insurance premiums increased substantially in 2009, and we expect to pay significantly higher FDIC premiums in the future. As the large number of recent bank failures continues to deplete the DIF, the FDIC adopted a revised risk-based deposit insurance assessment schedule in February 2009, which raised deposit insurance premiums. The FDIC also implemented a five basis point special assessment of each insured depository institution's assets minus Tier 1 capital as of June 30, 2009, which special assessment amount was capped at 10 basis points times the institution's assessment base for the second quarter of 2009. The amount of our special assessment was approximately $416,000. In addition, the FDIC recently announced a proposed rule that will require financial institutions, such as the Bank, to prepay their estimated quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010 through and including 2012 in order to re-capitalize the DIF. The proposed rule also provides for increasing the FDIC-assessment rates by three basis points effective January 1, 2011. The amount of our prepayment, which was made in December 2009, was approximately $4.7 million.

We operate within a highly regulated environment and our business and results are significantly affected by the regulations to which we are subject.
We operate within a highly regulated environment. The regulations to which we are subject will continue to have a significant impact on our operations and the degree to which we can grow and be profitable. Certain regulators, to which we are subject, have significant power in reviewing our operations and approving our business practices. In recent years the Bank, as well as other financial institutions, has experienced increased regulation and regulatory scrutiny, often requiring additional resources. In addition, investigations or proceedings brought by regulatory agencies may result in judgments, settlements, fines, penalties, or other results adverse to us. There is no assurance that any change to the regulatory requirements to which we are subject, or the way in which such regulatory requirements are interpreted or enforced, will not have a negative effect on our ability to conduct our business and our results of operations.

We rely heavily on technology and computer systems. The negative effects of computer system failures and unethical individuals with the technological ability to cause disruption of service could significantly affect our reputation and our ability to generate deposits.
Our ability to compete depends on our ability to continue to adapt and deliver technology on a timely and cost-effective basis to meet customers' demands for financial services. We currently provide our customers the ability to bank online and many customers now remotely submit deposits to us through remote-capture systems. The secure transmission of confidential information over the Internet is a critical element of these services. Our network could be

vulnerable to unauthorized access, computer viruses, phishing schemes and other security problems. We may be required to spend significant capital and other resources to protect against the threat of security breaches and computer viruses, or to alleviate problems caused by security breaches or viruses. To the extent that our activities or the activities of our customers involve the storage and transmission of confidential information, security breaches and viruses could expose us to claims, litigation and other possible liabilities. Any inability to prevent security breaches or computer viruses could also cause existing customers to lose confidence in our systems and could adversely affect our reputation and our ability to generate deposits.

Table of Contents

Risks Relating to an Investment in Our Common Stock

Share ownership may be diluted by the issuance of additional shares of common stock in the future.
Our stock incentive plan provides for the granting of stock incentives to directors, officers, and employees. As of December 31, 2009, there were 61,368 shares issued under options granted under that plan. Likewise, subject to the availability of shares of our common stock, up to approximately 586,000 shares, including shares issuable under currently outstanding options, may be issued in the future to directors, officers, and employees under our existing equity incentive plans. In addition, on January 9, 2009, the Company issued $20.0 million in preferred stock to the Treasury in the CPP Transaction. As part of the CPP Transaction, we also granted the Treasury a 10-year stock purchase warrant. Under the warrant, the Treasury has the right to purchase 104,384 shares of our common stock at an exercise price of $14.37 per share. It is probable that options and or/warrants will be exercised during their respective terms if the stock price exceeds the exercise price of the particular option or warrant. The incentive plan also provides that all issued options automatically and fully vest upon a change in control. If the options are exercised, share ownership will be diluted.

In addition, our articles of incorporation authorize the issuance of up to 10,000,000 shares of common stock and 5,000,000 shares of preferred stock, but do not provide for preemptive rights to the shareholders and, therefore, shareholders will not automatically have the right to subscribe for additional shares. As a result, if we issue additional shares to raise additional capital or for other corporate purposes, you may be unable to maintain a pro rata ownership in the Company. Excluding shares reserved for issuance upon the exercise of outstanding stock options and the warrant issued to the Treasury, we currently have less than 111,000 shares, including treasury shares, that remain available for issuance by us. As a result, we expect to seek approval to amend our articles of incorporation to increase the number of shares of stock that we are authorized to issue. Any such amendment would require approval by an affirmative vote of the holders of a majority of the shares present and entitled to vote at such meeting. There can be no assurance that we will seek such an amendment or, if such an amendment is submitted to a vote of our shareholders, that it would be approved by our shareholders.

The holders of our preferred stock and trust preferred securities have rights that are senior to those of shareholders and that may impact our ability to pay dividends on our common stock and with net income available to our common shareholders.
At December 31, 2009, we had outstanding $15.5 million of trust preferred securities. These securities are senior to shares of common stock. As a result, we must make payments on our trust preferred securities before any dividends can be paid on our common stock; moreover, in the event of our bankruptcy, dissolution, or liquidation, the obligations outstanding with respect to our trust preferred securities must be satisfied before any distributions can be made to our shareholders. While we have the right to defer dividends on the trust preferred securities for a period of up to five years, if any such election is made, no dividends may be paid to our common or preferred shareholders during that time.

In addition, with respect to the $20.0 million in Series A Preferred Stock outstanding that was issued to the Treasury in the CPP Transaction, we are required to pay cumulative dividends on the Series A Preferred Stock at an annual rate of 5.0% for the first five years and 9.0% thereafter, unless we redeem the shares earlier. Dividends paid on our Series A Preferred Stock will also reduce the net income available to our common shareholders and our earnings per common share. We may not declare or pay dividends on our common stock or repurchase shares of our common stock without first having paid all accrued cumulative preferred dividends that are due. Until January 2012, we also may not increase our per share common stock dividend rate or repurchase shares of our common shares without the Treasury's consent, unless the Treasury has transferred to third parties all the Series A Preferred Stock originally issued to it.

There can be no assurance whether or when the Series A Preferred Stock can be redeemed or whether or when the related warrant can be repurchased.

Subject to approval of our regulators, we generally have the right to repurchase the shares of Series A Preferred Stock and the associated warrant issued to the Treasury in the CPP Transaction. However, there can be no assurance as to when the Series A Preferred Stock and the warrant will be repurchased, if at all. As a result, we will remain subject to the uncertainty of additional future changes to the CPP, which could put us at a competitive disadvantage. Until such time as the Series A Preferred Stock and the warrant are repurchased, we will remain subject to the terms and conditions of those instruments, which, among other things, require us to obtain regulatory approval to

Table of Contents

repurchase or redeem our common stock or our other preferred stock or increase the annual aggregate dividends on our common stock over $0.28 per share, except in limited circumstances.

Holders of the Series A Preferred Stock may, under certain circumstances, have the right to elect two directors to our board of directors.
In the event that we fail to pay dividends on the Series A Preferred Stock for an aggregate of six quarterly dividend periods or more, the authorized number of directors then constituting our board of directors will be increased by two. Holders of the Series A Preferred Stock, together with the holders of any outstanding parity stock with the same voting rights, will be entitled to elect the two additional members of the board of directors at the next annual meeting (or at a special meeting called for this purpose) and at each subsequent annual meeting until all accrued and unpaid dividends for all past dividend periods have been paid in full.

Only a limited trading market exists for our common stock, which could lead to price volatility.
Our common stock is listed for trading on the NYSE Amex under the trading symbol “MSL,” but there is low trading volume in our common stock. The limited trading market for our common stock may cause fluctuations in the market value of our common stock to be exaggerated, leading to price volatility in excess of that which might occur in a more active trading market of our common stock. Future sales of substantial amounts of common stock in the public market, or the perception that such sales may occur, could adversely affect the prevailing market price of our common stock. In addition, even if a more active market in our common stock develops, we cannot assure you that such a market will continue.

Our directors and executive management own a significant number of shares of stock, allowing further control over business and corporate affairs.
Our directors and executive officers beneficially own approximately 2.6 million shares, or 26.4%, of our outstanding common stock as of December 31, 2009. As a result, in addition to their day-to-day management roles, they will be able to exercise significant influence on our business as shareholders, including influence over election of the Board and the authorization of other corporate actions requiring shareholder approval. In deciding on how to vote on certain proposals, our shareholders should be aware that our directors and executive officers may have interests that are different from, or in addition to, the interests of our shareholders generally.

Provisions of our articles of incorporation and by-laws, Louisiana law, and state and federal banking regulations, could delay or prevent a takeover by a third party.
Our articles of incorporation and by-laws could delay, defer, or prevent a third party takeover, despite possible benefit to the shareholders, or otherwise adversely affect the price of our common stock. Our governing documents:

- permit directors to be removed by shareholders only for cause and only upon an 80% vote;
- require 80% of the voting power for shareholders to amend the by-laws, call a special meeting, or amend the articles of incorporation, in each case if the proposed action was not approved by the Board;
- authorize a class of preferred stock that may be issued in series with terms, including voting rights, established by the Board without shareholder approval;
- authorize approximately 10 million shares of common stock and 5 million shares of preferred stock that may be issued by the Board without shareholder approval;
- classify our Board with staggered three year terms, preventing a change in a majority of the Board at any annual meeting;
- require advance notice of proposed nominations for election to the Board and business to be conducted at a shareholder meeting; and
- require 80% of the voting power for shareholders to approve business combinations not approved by the Board.

These provisions would likely preclude a third party from removing incumbent directors and simultaneously gaining control of the Board by filling the vacancies thus created with its own nominees. Under the classified Board provisions, it would take at least two elections of directors for any individual or group to gain control of the Board. Accordingly, these provisions could discourage a third party from initiating a proxy contest, making a tender offer or otherwise attempting to gain control. These provisions may have the effect of delaying consideration of a shareholder proposal until the next annual meeting unless a special meeting is called by the Board or the chairman of

Table of Contents

the Board. Moreover, even in the absence of an attempted takeover, the provisions make it difficult for shareholders dissatisfied with the Board to effect a change in the Board's composition, even at annual meetings.

Also, we are subject to the provisions of the Louisiana Business Corporation Law ("LBCL"), which provides that we may not engage in certain business combinations with an "interested shareholder" (generally defined as the holder of 10.0% or more of the voting shares) unless (1) the transaction was approved by the Board before the interested shareholder became an interested shareholder or (2) the transaction was approved by at least two-thirds of the outstanding voting shares not beneficially owned by the interested shareholder and 80% of the total voting power or (3) certain conditions relating to the price to be paid to the shareholders are met.

The LBCL also addresses certain transactions involving "control shares," which are shares that would have voting power with respect to the Company within certain ranges of voting power. Control shares acquired in a control share acquisition have voting rights only to the extent granted by a resolution approved by our shareholders. If control shares are accorded full voting rights and the acquiring person has acquired control shares with a majority or more of all voting power, shareholders of the issuing public corporation have dissenters' rights as provided by the LBCL.

Our future ability to pay dividends and repurchase stock is subject to restrictions.
Since we are a holding company with no significant assets other than the Bank, we have no material source of income other than dividends received from the Bank. Therefore, our ability to pay dividends to our shareholders will depend on the Bank's ability to pay dividends to us. Moreover, banks and bank holding companies are both subject to certain federal and state regulatory restrictions on cash dividends. We are also restricted from paying dividends if we have deferred payments of the interest on, or an event of default has occurred with respect to, our trust preferred securities or Series A Preferred Stock. Additionally, terms and conditions of our outstanding shares of preferred stock place certain restrictions and limitations on our common stock dividends and repurchases of our common stock.

A shareholder's investment is not an insured deposit.
An investment in our common stock is not a bank deposit and is not insured or guaranteed by the FDIC or any other government agency. Your investment in our common stock will be subject to investment risk and you may lose all or part of your investment.

Item 1B – Unresolved Staff Comments

None.

Item 2 - Properties

We lease our principal executive and administrative offices and principal facility in Lafayette, Louisiana under a lease expiring March 31, 2017. We have two 5-year renewal options thereafter that we may exercise. In addition to our principal facility, we also have eight other branches located in Lafayette, Louisiana, three in New Iberia, Louisiana, three in Baton Rouge, Louisiana, two in Lake Charles, Louisiana, two in Houma, Louisiana, and one banking office in each of the following Louisiana cities: Breaux Bridge, Cecilia, Larose, Jeanerette, Opelousas, Morgan City, Jennings, Sulphur, and Thibodaux. Seventeen of these offices are owned and ten are leased.

In our Texas market area, we have three full service branches located in Beaumont, Texas, two of which are owned and one leased. Our additional full service branches in the Texas market area are located in Vidor, College Station, Houston, and Conroe. The Company also operates a loan production office located in Conroe, Texas. Of these offices, three are owned and two are leased.

Item 3 - 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.

Item 4 – (Removed and Reserved)

Table of Contents

Executive Officers of the Registrant

The names, ages as of December 31, 2009, and positions of our executive officers are listed below along with their business experience during the past five years.

C. R. Cloutier, 62 – President, Chief Executive Officer and Director of the Company and the Bank since 1984.

James R. McLemore, 50–Senior Executive Vice President and Chief Financial Officer for the Company and the Bank since July 2009. Prior to joining the Company and the Bank, Mr. McLemore served as Executive Vice President and Chief Financial Officer of Security Bank Corporation from 2002 until July 2009. In July 2009, subsequent to Mr. McLemore's departure, the six subsidiary banks of Security Bank Corporation were closed and the FDIC was appointed receiver of the banks. Security Bank Corporation subsequently filed for bankruptcy in August of 2009.

Karen L. Hail, 56 – Senior Executive Vice President and Chief Operations Officer of the Bank since 2002; Secretary and Treasurer of the Company since 1984; and Director of the Bank since 1988. Effective April 1, 2010, Ms. Hail will serve as Senior Executive Vice President and Director of Asset Procurement for the Bank. As a result of this new position, Ms. Hail will no longer serve as Chief Operations Officer of the Company, but will continue to serve as a Director of the Company and the Bank.

Donald R. Landry, 53 – Senior Executive Vice President and Chief Lending Officer of the Bank since 1995 and Executive Vice President since 2002. Mr. Landry tendered his resignation effective January 25, 2010 to join another local financial institution. Mr. Landry's responsibilities, which are predominantly related to credit production, will be assumed within each of our six regions on an interim basis by MidSouth Bank's Regional Bank Presidents.

Teri S. Stelly, 50 – Senior Vice President and Controller of the Company since 1998. Ms. Stelly acted as the interim Chief Financial Officer from January 15, 2009 to July 12, 2009.

All executive officers are appointed for one year terms expiring at the first meeting of the Board of Directors after the annual shareholders meeting next succeeding his or her election and until his or her successor is elected and qualified.

Table of Contents

PART II

Item 5 - Market for Registrant's Common Equity, Related Shareholder Matters, and Issuer Purchases of Equity Securities

As of February 26, 2010, there were 864 common shareholders of record. The Company’s common stock trades on the NYSE AMEX under the symbol “MSL.” The high and low sales price for the past eight quarters has been provided in the Selected Quarterly Financial Data tables that are included with this filing under Item 8 and is incorporated herein by reference.

Cash dividends totaling $1.8 million were declared to common shareholders during 2009. The regular quarterly dividend of $0.07 per share was paid for all four quarters of 2009, for a total of $0.28 per share for the year. Cash dividends totaling $2.1 million were declared to common shareholders during 2008. A quarterly dividend of $0.07 per share was paid for each quarter of 2008 and a special dividend of $0.04 per share was declared in addition to the $0.07 per share for the fourth quarter of 2008. Cash dividends paid in 2008 totaled $0.32 per share.

Under the Louisiana law, we may not pay a dividend if (i) we are insolvent or would thereby be made insolvent, or (ii) the declaration or payment thereof would be contrary to any restrictions contained in our articles of incorporation. Our primary source of funds for dividends is the dividends we receive from the Bank; therefore, our ability to declare dividends is highly dependent upon future earnings, financial condition, and results of operation of the Bank as well as applicable legal restrictions on the Bank’s ability to pay dividends and other relevant factors. The Bank currently has the ability to declare dividends to us without prior approval of our primary regulators. However, the Bank’s ability to pay dividends to us will be prohibited if the result would cause the Bank’s regulatory capital to fall below minimum requirements. Additionally, dividends to us cannot exceed a total of the Bank’s current year and prior two years’ earnings, net of dividends paid to us in those years.

Pursuant to the terms of the agreements between us and the Treasury governing the CPP Transaction, we may not declare or pay any dividend or make any distribution on our common stock other than (i) regular quarterly cash dividends not exceeding an annual aggregate of $0.28 per share; (ii) dividends payable solely in shares of our common stock; and (iii) dividends or distributions of rights of junior stock in connection with a shareholders’ rights plan. Further, the terms of our trust preferred securities prohibit us from paying dividends on our common stock during any period in which we have deferred interest payments on the trust preferred securities.

Share Repurchases

Pursuant to the terms of the agreements between us and the Treasury governing the CPP Transaction, we are currently prohibited from repurchasing shares of our common stock. As a result, we did not repurchase any shares of our common stock during the year ended December 31, 2009.

Table of Contents

Securities Authorized for Issuance under Equity Compensation Plans

As of December 31, 2009, the Company had outstanding stock options granted under our incentive compensation plans, which were approved by the Company's shareholders. Provided below is information regarding the Company's equity compensation plans under which the Company's equity securities are authorized for issuance as of December 31, 2009, subject to the Company's available authorized shares.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants, and rights (a)	Weighted-average exercise price of outstanding options (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)	
Equity compensation plans approved by security holders	61,368	$ 12.26	525,000	1
Equity compensation plans not approved by security holders	-	-	-	
Total	61,368	$ 12.26	525,000	

1 Represents shares reserved under 2007 Omnibus Incentive Compensation Plan. The Board of Directors has suspended additional award grants under this Plan until such time as our shareholders approve an increase in authorized common stock. A proposal for such increase will be presented at our 2010 Annual Meeting.

Table of Contents

The following graph compares the cumulative total return on our common stock over a period beginning December 31, 2004 with (1) the cumulative total return on the stocks included in the Russell 3000 and (2) the cumulative total return on the stocks included in the SNL Securities, LC ("SNL") $250M - $500M and the SNL $500M - $1B Bank Index. The comparison assumes an investment in our common stock on the indices of $100 at December 31, 2004 and assumes that all dividends were reinvested during the applicable period.

MidSouth Bancorp, Inc.

	Period Ending					
Index	12/31/04	12/31/05	12/31/06	12/31/07	12/31/08	12/31/09
MidSouth Bancorp, Inc.	100.00	111.19	161.96	128.71	71.82	80.03
Russell 3000	100.00	106.12	122.80	129.11	80.94	103.88
SNL Bank $250M-$500M	100.00	106.17	110.93	90.16	51.49	47.66
SNL Bank $500M-$1B	100.00	104.29	118.61	95.04	60.90	58.00

The stock price information shown above is based on historical data and should not be considered indicative of future price performance.

Table of Contents

Item 6 – Five Year Summary of Selected Financial Data

	At and For the Year Ended December 31,				
	2009	2008	2007	2006	2005
	(dollars in thousands, except per share data)				
Interest income	$50,041	$55,472	$57,139	$50,235	$38,556
Interest expense	(10,220)	(16,085)	(20,534)	(17,692)	(10,824)
Net interest income	39,821	39,387	36,605	32,543	27,732
Provision for loan losses	(5,450)	(4,555)	(1,175)	(850)	(980)
Noninterest income	15,046	15,128	14,259	12,379	12,286
Noninterest expenses	(44,693)	(43,974)	(38,634)	(33,124)	(29,326)
Earnings before income taxes	4,724	5,986	11,055	10,948	9,712
Income tax expense	(125)	(449)	(2,279)	(2,728)	(2,438)
Net income	$4,599	$5,537	$8,776	$8,220	$7,274
Preferred dividend requirement	(1,175)	-	-	-	-
Net income available to common shareholders	$3,424	$5,537	$8,776	$8,220	$7,274
Basic earnings per common share[1]	$0.51	$0.84	$1.34	$1.26	$1.13
Diluted earnings per common share[1]	$0.51	$0.83	$1.32	$1.24	$1.10
Dividends per common share[1]	$0.28	$0.32	$0.29	$0.22	$0.22
Total loans	$585,042	$608,955	$569,505	$499,046	$442,794
Total assets	972,142	936,815	854,056	805,022	698,814
Total deposits	773,285	766,704	733,517	716,180	624,938
Cash dividends on common stock	1,846	2,120	1,920	1,463	1,425
Long-term obligations	15,465	15,465	15,465	15,465	15,465
Selected ratios:					
Loans to assets	60.18%	65.00%	66.68%	61.99%	63.36%
Loans to deposits	75.66%	79.43%	77.64%	69.68%	70.85%
Deposits to assets	79.54%	81.84%	85.89%	88.96%	89.43%
Return on average assets	0.37%	0.60%	1.06%	1.08%	1.13%
Return on average common equity	4.35%	7.79%	13.83%	14.68%	14.24%

1 On October 23, 2007, the Company paid a 5% stock dividend to common shareholders of record on September 21, 2007. On October 23, 2006, a 25% stock dividend was paid to common shareholders of record on September 29, 2006. On August 19, 2005, a 10% stock dividend was paid to common shareholders of record on July 29, 2005. Per common share data has been adjusted accordingly.

Table of Contents

Item 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations

The purpose of this discussion and analysis is to focus on significant changes in the financial condition of the Company and on its results of operations during 2009, 2008, and 2007. This discussion and analysis is intended to highlight and supplement information presented elsewhere in this annual report on Form 10-K, particularly the consolidated financial statements and related notes appearing in Item 8.

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 with accounting principles generally accepted in the United States of America ("GAAP") and general banking practices. Our most critical accounting policy relates to the allowance for loan losses, which reflects the estimated losses resulting from the inability of its borrowers to make loan payments. If the financial condition of 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 – Allowance for Loan Losses.

Another of our critical accounting policies relates to goodwill and intangible assets. Goodwill 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.

As part of our compensation program, we provide stock-based compensation. Compliance with accounting for stock-based compensation requires that we make assumptions including stock price volatility and employee turnover that are utilized to measure compensation expense. The fair value of stock options granted is estimated at the date of grant using the Black-Scholes option-pricing model. This model requires the input of highly subjective assumptions.

Given the current instability of the economic environment, it is reasonably possible that the methodology of the assessment of potential loan losses, goodwill impairment, and other fair value measurements could change in the near-term or could result in impairment going forward.

Overview

We are a bank holding company, headquartered in Lafayette, Louisiana, that through our community banking subsidiary, MidSouth Bank, N.A., operated 35 offices in south Louisiana and southeast Texas. We had approximately $972.1 million in consolidated assets as of December 31, 2009. We derive the majority of our income from interest received on our loans and investments. Our primary source of funds for making these loans and investments is our deposits, on which we pay interest. Approximately 77.3% of our total deposits are interest-bearing. Consequently, one of the key measures of our success is our amount of net interest income, or the difference between the income on our interest-earning assets, such as loans and investments, and the expense on our interest-bearing liabilities, such as deposits and borrowings. Another key measure is the spread between the yield we earn on these interest-earning assets and the rate we pay on our interest-bearing liabilities, which is called our net interest spread.

There are risks inherent in all loans, so we maintain an allowance for loan losses to absorb probable losses on existing loans that may become uncollectible. We maintain this allowance by charging a provision for loan losses against our operating earnings for each period. We have included a detailed discussion of this process, as well as several tables describing our allowance for loan losses. Our financial performance for the years ended December 31, 2008 and 2009 were, and continue to be, significantly impacted by the disruptions in the national economy and the resulting financial uncertainty that has severely impacted the banking industry. While we believe our market areas have faired better than the national economy during this most recent economic downturn, the economic uncertainty and difficult real estate markets had an impact on our loan losses, loan demand and our interest rate spread.

Table of Contents

In addition to earning interest on our loans and investments, we earn income through fees and other charges to our customers. We have also included a discussion of the various components of this noninterest income, as well as of our noninterest expense.

We plan to continue to grow both organically and through acquisitions, including potential expansion into new market areas. To support our growth, in December 2009, we completed a public offering of approximately 3.1 million shares of our common stock for which we received net proceeds of approximately $37.3 million (including shares issued upon the underwriters exercise of their over-allotment option in January 2010). As a result of the offering, we were also able to cut in half the number of shares underlying the warrants we issued to the Treasury as part of the CPP Transaction. We believe our current financial condition, coupled with our scalable operational capabilities will allow us to act upon growth opportunities afforded within the current banking environment.

The following discussion and analysis also identifies significant factors that have affected our financial position and operating results during the periods included in the financial statements accompanying or incorporated by reference in this report. We encourage you to read this discussion and analysis in conjunction with our financial statements and the other statistical information included and incorporated by reference in this report.

Results of Operations

Net income available to common shareholders for the year ended December 31, 2009 totaled $3.4 million compared to $5.5 million for the year ended December 31, 2008, a decrease of $2.1 million, or 38.2%. Dividends recorded on our Series A Preferred Stock reduced net earnings available to common shareholders by $1,175,000 for the year ended December 31, 2009. Basic earnings per share were $0.51 and $0.84 for the years ended December 31, 2009 and 2008, respectively. Diluted earnings per share were $0.51 for the year ended December 31, 2009, compared to $0.83 per share earned for the year ended December 31, 2008.

Total consolidated assets increased $35.3 million, or 3.8%, from $936.8 million at December 31, 2008, to $972.1 million at December 31, 2009. The increase in assets resulted primarily from our public offering of 2.7 million shares of our common stock at $12.75 per share which closed on December 22, 2009. We received net proceeds of approximately $32.4 million. Subsequent to December 31, 2009, the underwriters exercised the over-allotment option granted to them in the offering, resulting in the issuance of an additional 405,000 shares and net proceeds of approximately $4.9 million. We plan to use the net proceeds from the offering for general corporate purposes including, as discussed above, potential acquisition opportunities. The additional capital increased our leverage capital ratio from 8.38% at December 31, 2008 to 13.95% at December 31, 2009. Tier 1 risk weighted capital and total risk weighted capital ratios were 19.34% and 20.54% at December 31, 2009, compared to 11.04% and 12.16% at December 31, 2008, respectively. Return on average common equity was 4.35% for 2009 compared to 7.79% for 2008. Return on average assets was 0.37% compared to 0.60% for the same periods, respectively. Deposits totaled $773.3 million as of December 31, 2009, an increase of $6.6 million, compared to $766.7 million on December 31, 2008. Total loans were $585.0 million, a decrease of $24.0 million, or 3.9%, from the $609.0 million reported as of December 31, 2008. Loans decreased throughout 2009 as commercial customers used cash flows to pay down debt and continued economic concerns stemmed loan production in both commercial and retail credits.

Net earnings before dividends on Series A Preferred Stock decreased $938,000, from $5.5 million at December 31, 2008 to $4.6 million at December 31, 2009, primarily due to a $895,000 increase in our provision for loan losses. The increase in provision expense was primarily driven by a $2.6 million increase in net charge-offs in 2009, which included $1.8 million charged-off on a national participation credit. Although our total loans decreased, net interest income increased $434,000 as deposit rate reductions throughout 2009 lowered interest expense and offset the decreased interest income from earning assets.

Non-interest income decreased $82,000 in annual comparison. Increases of $327,000 in ATM and debit card income and $124,000 in service charges on deposit accounts were partially offset by a $533,000 decrease in other noninterest income. The $533,000 decrease resulted primarily from a $178,000 impairment charge on an equity security, a $120,000 decrease in income from a third party investment advisory firm and a $131,000 one-time payment recorded in other non-interest income in 2008. The one-time payment resulted from VISA's mandatory redemption of a portion of its Class B shares outstanding in connection with its initial public offering.

Table of Contents

Non-interest expense increased $719,000 in year-to-date comparison. Salary and benefits costs increased $792,000 and occupancy expenses increased $601,000. Included in other noninterest expense, a $1,178,000 increase in FDIC premiums was offset by significant decreases of $977,000 in marketing costs, $278,000 in corporate developmentand training expenses, $197,000 in professional fees, and $213,000 in expenses recorded in 2008 related to the data conversion and merger of our former Texas bank charter into our Louisiana charter. Income tax expense decreased $324,000 due to the effect of certain federal tax credits combined with lower annual pre-tax profits and sustained tax exempt income levels.

Nonaccrual loans totaled $16.2 million as of December 31, 2009, compared to $9.4 million as of December 31, 2008. Of the $16.2 million at December 31, 2009, $12.2 million, or 75.1%, represented two large commercial real estate loan relationships in the Baton Rouge market. Loans past due 90 days or more and still accruing totaled $0.4 million at December 31, 2009, a decrease of $600,000 from the $1.0 million reported for December 31, 2008. Total nonperforming assets to total assets were 1.79% at December 31, 2009, compared to 1.17% at December 31, 2008.

Allowance coverage for nonperforming loans was 48.28% at December 31, 2009, compared to 73.22% at December 31, 2008. Excluding the effect of the two large commercial real estate loans in the Baton Rouge market, allowance coverage for nonperforming loans was 158.37% at December 31, 2009 and 342.88% at December 31, 2008. Year-to-date net charge-offs were 0.86% of total loans as of December 31, 2009 compared to 0.40% as of December 31, 2008. The ALLL/total loans ratio was 1.37% at December 31, 2009 compared to 1.25% at December 31, 2008.

Table 1
Summary of Return on Equity and Assets

	2009		2008		2007	
Return on average assets	0.37	%	0.60	%	1.06	%
Return on average common equity	4.35	%	7.79	%	13.83	%
Dividend payout ratio on common stock	54.90	%	38.55	%	21.97	%
Average equity to average assets	10.43	%	7.75	%	7.69	%

Earnings Analysis

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 4.88%, 4.93%, and 5.10% for the years ended December 31, 2009, 2008, and 2007, respectively. Tables 2 and 3 analyze the changes in net interest income in the years ended December 31, 2009, 2008, and 2007.

During 2009, securities in our investment portfolio that have matured have generally been replaced by new securities that, as a result of the current interest rate environment, pay us a lower yield compared to the matured securities they are replacing. As a result, during 2009 we experienced some contraction in our net interest margin and expect to continue to experience additional contraction into 2010. However, because of our base of core deposits described below under “Funding Sources – Deposits,” we expect our net interest margin to remain strong.

-30-

Table of Contents

Table 2
Consolidated Average Balances, Interest, and Rates
(in thousands)

	Year Ended December 31, 2009			2008			2007		
	Average Volume	Interest	Average Yield/ Rate	Average Volume	Interest	Average Yield/ Rate	Average Volume	Interest	Average Yield/ Rate
Assets									
Investment securities1									
Taxable	$ 101,556	$ 3,905	3.85 %	$ 97,363	$ 4,381	4.50 %	$ 85,999	$ 4,089	4.75 %
Tax exempt2	115,176	6,159	5.35 %	112,801	6,100	5.41 %	110,256	5,846	5.30 %
Other investments	4,445	130	2.92 %	4,172	136	3.26 %	3,533	156	4.42 %
Total investments	221,177	10,194	4.61 %	214,336	10,617	4.95 %	199,788	10,091	5.05 %
Federal funds sold	17,617	37	0.21 %	29,406	669	2.24 %	15,554	788	5.00 %
Loans									
Commercial and real estate	483,626	31,992	6.62 %	461,382	35,404	7.67 %	426,038	38,314	8.99 %
Installment	109,963	9,349	8.50 %	113,973	10,128	8.89 %	109,688	9,651	8.80 %
Total loans3	593,589	41,341	6.96 %	575,355	45,532	7.91 %	535,726	47,965	8.95 %
Other earning assets	20,222	275	1.34 %	15,892	447	2.81 %	118	7	5.93 %
Total earning assets	852,605	51,847	6.08 %	834,989	57,265	6.86 %	751,186	58,851	7.83 %
Allowance for loan losses	(7,650)			(5,910)			(5,079)		
Nonearning assets	89,579			88,808			79,327		
Total assets	$ 934,534			$ 917,887			$ 825,434		
Liabilities and shareholders' equity									
NOW, money market, and savings	$ 439,655	$ 4,632	1.05 %	$ 453,531	$ 7,958	1.75 %	$ 419,983	$ 13,017	3.10 %
Time deposits	141,159	3,471	2.46 %	146,272	5,952	4.07 %	121,238	5,089	4.20 %
Total interest-bearing deposits	580,814	8,103	1.40 %	599,803	13,910	2.32 %	541,221	18,106	3.35 %
Borrowings:									
Securities sold under agreements to	44,940	1,075	2.39 %	35,999	875	2.39 %	13,880	531	3.77 %

repurchase and federal funds purchased									
FHLB advances	-	-	-	452	16	3.48 %	8,309	500	5.94 %
Federal Reserve discount window	4,625	23	0.50 %	4,491	65	1.45 %	-	-	-
Total borrowings	49,565	1,098	2.22 %	40,942	956	2.30 %	22,189	1,031	4.58 %
Junior subordinated debentures	15,465	1,019	6.50 %	15,465	1,219	7.75 %	15,465	1,397	8.91 %
Total interest-bearing liabilities	645,844	10,220	1.58 %	656,210	16,085	2.45 %	578,875	20,534	3.55 %
Demand deposits	185,757			185,113			178,933		
Other liabilities	5,468			5,466			4,158		
Shareholders' equity	97,465			71,098			63,468		
Total liabilities and shareholders' equity	$ 934,534			$ 917,887			$ 825,434		
Net interest income and net interest spread		$ 41,627	4.50 %		$ 41,180	4.41 %		$ 38,317	4.28 %
Net yield on interest-earning assets			4.88 %			4.93 %			5.10 %

1 Securities classified as available-for-sale are included in average balances and interest income figures and reflect interest earned on such securities.

2 Interest income of $1,806,000 for 2009, $1,792,000 for 2008, and $1,712,000 for 2007 is added to interest earned on tax-exempt obligations to reflect tax-equivalent yields using a 34% tax rate.

3 Interest income includes loan fees of $3,184,000 for 2009, $3,801,000 for 2008, and $3,352,000 for 2007. Nonaccrual loans are included in average balances and income on such loans is recognized on a cash basis.

Table of Contents

Table 3
Changes in Taxable-Equivalent Net Interest Income
(in thousands)

	2009 Compared to 2008			2008 Compared to 2007		
	Total Increase (Decrease)	Change Attributable to Volume	Rates	Total Increase (Decrease)	Change Attributable to Volume	Rates
Taxable-equivalent interest earned on:						
Investment securities and interest-bearing deposits						
Taxable	$(476)	$183	$(659)	$292	$519	$(227)
Tax-exempt	59	127	(68)	254	137	117
Other investments	(6)	9	(15)	(20)	25	(45)
Federal funds sold	(632)	(192)	(440)	(119)	468	(587)
Loans, including fees	(4,191)	1,407	(5,598)	(2,433)	3,387	(5,820)
Other earning assets	(172)	102	(274)	440	444	(4)
Total	(5,418)	1,636	(7,054)	(1,586)	4,980	(6,566)
Interest paid on:						
Interest-bearing deposits	(5,807)	(428)	(5,379)	(4,196)	1,804	(6,000)
Securities sold under agreements to repurchase and federal funds purchased	200	214	(14)	344	657	(313)
FHLB Advances	(16)	(16)	-	(484)	(366)	(118)
Federal Reserve discount window	(42)	2	(44)	65	33	32
Junior subordinated debentures	(200)	-	(200)	(178)	-	(178)
Total	(5,865)	(228)	(5,637)	(4,449)	2,128	(6,577)
Taxable-equivalent net interest income	$447	$1,864	$(1,417)	$2,863	$2,852	$11

NOTE: Changes due to both 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.

Net interest income on a taxable-equivalent basis increased $447,000 for 2009 over 2008 and $2.9 million for 2008 over 2007. The $447,000 increase in taxable-equivalent net interest income resulted primarily from a $5.9 million decrease in interest expense on interest-bearing liabilities, offset by a $5.4 million decrease in taxable-equivalent interest income on earning assets. Interest expense on interest-bearing liabilities decreased primarily due to a 92 basis point decrease in the average rate paid on interest-bearing deposits, from 2.32% at December 31, 2008 to 1.40% at December 31, 2009. Additionally, the average volume of interest bearing deposits declined $19.0 million, from $599.8 million at December 31, 2008 to $580.8 million at December 31, 2009. Increased interest expense on securities sold under agreements to repurchase in 2009, due to an $8.9 million increase in average volume, was offset by a decrease in interest expense due to rate reductions on borrowings and the junior subordinated debentures.

A 78 basis points decrease in the average yield on earning assets, from 6.86% at December 31, 2008 to 6.08% at December 31, 2009, offset a $17.6 million, or 2.1%, increase in the average volume of earning assets, from $835.0 million at December 31, 2008, to $852.6 million at December 31, 2009, to net a $5.4 million decrease in taxable-equivalent interest income. Average loan yields decreased 95 basis points, from 7.91% at December 31, 2008, to 6.96% at December 31, 2009, primarily due to maturing and repricing loans adjusting to lower rates of interest in the current environment. An increase in loan volume of $18.2 million, or 3.2%, partially offset the decrease in rates and resulted in a $4.2 million decrease in interest earned on loans for 2009. Taxable-equivalent yields also fell 34 basis points on investment securities, from 4.95% at December 31, 2008 to 4.61% at December 31, 2009, as new purchases were added at much lower rates in 2009.

Table of Contents

In 2008, net interest income on a taxable-equivalent basis increased $2.9 million over 2007, primarily due to an $83.8 million increase in average earning assets, from $751.2 million at December 31, 2007, to $835.0 million at December 31, 2008. The yield on average earning assets decreased 97 basis points, from 7.83% to 6.86% in annual comparison. Average loan yields decreased 104 basis points, from 8.95% at December 31, 2007, to 7.91% at December 31, 2008, primarily due to the Company's variable rate loans that adjusted with Prime. The Prime rate decreased 400 basis points during 2008, from 7.25% to 3.25% at year end. An increase in loan volume of $39.6 million, or 7.4%, partially offset the decrease in rates and resulted in a $2.4 million decrease in interest earned on loans for 2008. Rate decreases on earning assets offset volume increases and resulted in a decrease of $1.6 million in taxable-equivalent interest income. The $1.6 million decrease was offset by a $4.4 million decrease in interest paid on interest-bearing liabilities. Interest paid on average interest-bearing deposits decreased $4.2 million due to a 103 basis point decrease in the average rate from 3.35% at December 31, 2007 to 2.32% at December 31, 2008. The decrease in average cost of deposits was partially offset by a $58.6 million increase in average interest-bearing deposit volume. The cost of total interest-bearing liabilities decreased 110 basis points from 3.55% at December 31, 2007 to 2.45% at December 31, 2008.

Noninterest Income

Noninterest income totaled $15.2 million at December 31, 2009, compared to $15.1 million at December 31, 2008 and $14.3 million at December 31, 2007. Service charges and fees on deposit accounts represent the primary source of noninterest income for the Company. Income from service charges and fees on deposit accounts, including insufficient funds fees ("NSF" fees), increased $124,000 in 2009 compared to a $384,000 increase in 2008. Beginning in 2010, we expect recent changes that, once implemented, will allow customers to opt out of debit transactions that would result in insufficient funds in their accounts. We expect these changes will have a material impact on our insufficient funds fees. Income on ATM and debit card transactions increased $327,000 in 2009 and $635,000 in 2008 as the result of an increase in electronic transactions processed. Other noninterest income decreased $355,000 in 2009 and $150,000 in 2008. The $355,000 decrease in 2009 resulted primarily from a $178,000 impairment charge on an equity security, a $120,000 decrease in income from a third party investment advisory firm, and a $131,000 one-time payment recorded in other non-interest income in 2008. The one-time payment resulted from VISA's mandatory redemption of a portion of its Class B shares outstanding in connection with its initial public offering. The $131,000 one-time payment recorded in 2008 partially offset a $205,000 decrease in mortgage processing fee income in 2008.

Noninterest Expense

Total noninterest expense increased 2.0%, or $0.9 million, from 2008 to 2009, and 13.8%, or $5.3 million, from 2007 to 2008. Salaries and employee benefits increased $0.8 million, or 3.8%, in 2009 and the total of full-time equivalent ("FTE") employees was 416, a decrease of 3 employees from 419 FTE employees at year-end 2008. Salary and benefit costs increased in 2009 primarily due to a $570,000 increase in group health insurance costs. Salaries and employee benefits increased $1.0 million, or 5.0%, in 2008, primarily due to annual salary adjustments and an increase of 9 employees over the 410 FTE employees at year-end 2007.

Occupancy expenses increased $601,000 in 2009 and $1,810,000 in 2008. The $601,000 increase in 2009 resulted primarily from a $123,000 increase in lease expense and a $353,000 increase in depreciation expense primarily as a result of the 2008 renovation of our corporate headquarters. The $1,810,000 increase in occupancy expense in 2008 resulted primarily from a full year of increased operating costs on four new facilities and three replacement facilities completed in 2007 and the corporate headquarters renovation. The increased operating costs primarily included $616,000 in depreciation expense, $369,000 in lease expense, and $377,000 in maintenance costs. Premises and equipment additions and leasehold improvements totaled approximately $1.8 million, $4.8 million, and $11.3 million for the years 2009, 2008, and 2007, respectively.

ATM and debit card processing fees decreased $121,000 in 2009 primarily due to a $160,000 reduction in fraud losses on transactions. Processing fees increased $268,000 in 2008 due to a higher volume of transactions processed. Total other noninterest expense decreased $375,000 in 2009 and increased $2.3 million in 2008. Efforts to reduce controllable expenses in 2009 resulted in significant reductions in marketing costs ($974,000), professional fees ($309,000), corporate development ($123,000), training expenses ($155,000), and other noninterest expense categories. These noninterest expense reductions offset increased FDIC premiums of $1,178,000, or a 232.8% increase over the $506,000 in premiums expensed in 2008. In 2007, we qualified for a one-time credit totaling approximately $240,000, which reduced FDIC premiums to $157,000 in that year and resulted in a $349,000 increase in premiums in 2008.

Table of Contents

Contributing to the $2.3 million increase in other noninterest expense in 2008 compared to 2007, marketing and corporate development expenses increased $646,000 due to promotions related to franchise growth. Professional fees increased $410,000 primarily due to consulting fees related to external assistance with corporate strategic initiatives and certain finance and operations related projects. Data processing expenses increased $287,000 primarily due to the merger of our two bank charters in the first quarter of 2008.

Income Taxes

Income tax expense decreased by $324,000 in 2009 and $1,830,000 in 2008 and approximated 3% and 8% of income before taxes in 2009 and 2008, respectively. For 2009, the lower effective tax rate was due to the lower pretax income which resulted in a larger impact by the nontaxable municipal interest on the statutory tax rate than in 2008. Additionally, the lower tax rates for 2009 and 2008 resulted from recognition of the Work Opportunity Tax Credit under the Katrina Emergency Tax Relief Act of 2005, which reduced income tax expense by $108,000 in 2009 and $225,000 in 2008. The notes to the consolidated financial statements provide additional information regarding income tax considerations.

Balance Sheet Analysis

Investment Securities

Total investment securities increased $42.4 million in 2009, from $232.4 million in 2008 to $274.9 million at December 31, 2009. The increase resulted primarily from the purchase of approximately $52.4 million in short-term agency securities in December 2009 with excess overnight funds and proceeds from our capital stock offering. Average duration of the portfolio was 3.27 years as of December 31, 2009 and the average taxable-equivalent yield was 4.61%. For the year ended December 31, 2008, average duration of the portfolio was 3.92 years and the average taxable-equivalent yield was 4.95%. Unrealized net gains before tax effect in the securities available-for-sale portfolio were $5.9 million at December 31, 2009, compared to unrealized net gain before tax effect of $2.6 million at December 31, 2008. These amounts result from interest rate fluctuations.

At December 31, 2009, approximately $51.9 million, or 19.1%, of the securities available-for-sale portfolio represented mortgage-backed securities and CMOs. All of the mortgage-backed securities and CMOs are government agency sponsored with the exception of two privately issued CMOs with a current market value of $141,000. Risk due to changes in interest rates on mortgage-backed pools is monitored by monthly reviews of prepayment speeds, duration, and purchase yields as compared to current market yields on each security. CMOs totaled $36.3 million and represented pools that each had a book value of less than 10% of shareholders' equity at December 31, 2009. All CMOs held in the portfolio are bank-qualified and not considered "high-risk" securities under the Federal Financial Institutions Examination Council ("FFIEC") tests. We do not own any "high-risk" securities as defined by the FFIEC. An additional 37.7% of the available-for-sale portfolio consisted of U.S. Agency securities, while municipal and other securities represented 43.1% and 0.1% of the portfolio, respectively. A detailed credit analysis on each municipal offering is reviewed prior to purchase by our investment advisory firm. In addition, we limit the amount of securities of any one municipality purchased and the amount purchased within specific geographic regions to reduce the risk of loss within the nontaxable municipal securities portfolio. The held-to-maturity portfolio consisted of $2.6 million in nontaxable and $0.4 million in taxable municipal securities. We retain the services of a qualified investment advisory firm that manages the securities portfolio and monitors the credit quality of bonds held in the portfolio.

Table of Contents

Table 4
Composition of Investment Securities
December 31
(in thousands)

	2009	2008	2007	2006	2005
Available-for-sale securities					
U. S. Treasuries	$-	$-	$-	$1,986	$1,966
U. S. Agencies	102,523	39,747	45,229	51,280	38,499
Obligations of state and political subdivisions	117,301	118,613	100,966	95,676	61,534
GSE mortgage-backed securities	15,634	19,661	24,250	29,888	33,715
Collateralized mortgage obligations	36,278	47,829	10,797	854	1,086
Corporate securities	-	-	-	990	2,629
Financial institution equity security	72	94	210	-	-
Total available-for-sale securities	$271,808	$225,944	$181,452	$180,674	$139,429
Held-to-maturity securities					
Obligations of state and political subdivisions	$3,043	$6,490	$10,746	$15,901	$19,611
Total held-to-maturity securities	$3,043	$6,490	$10,746	$15,901	$19,611
Total investment securities	$274,851	$232,434	$192,198	$196,575	$159,040

Table 5
Investment Securities Portfolio
Maturities and Average Taxable-Equivalent Yields
For the Year Ended December 31, 2009
(dollars in thousands)

	Within 1 Year		After 1 but Within 5 Years		After 5 but Within 10 Year		After 10 Years		
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Total
Securities available-for-sale:									
U.S. Treasury and U.S. Agency securities	$ -	-	$ 102,523	1.59 %	$ -	-	$ -	-	$ 102,523
Obligations of state and political subdivisions	4,778	6.09 %	45,270	4.91 %	49,091	5.50 %	18,162	5.63 %	117,301
GSE mortgage-backs and CMOs	11	6.82 %	792	4.80 %	871	4.57 %	50,238	4.99 %	51,912
Financial institution equity security	-	-	-	-	-	-	72	1.17 %	72
Total fair value	$ 4,789		$ 148,585		$ 49,962		$ 68,472		$ 271,808

	Within 1 Year		After 1 but Within 5 Years		After 5 but Within 10 Year		After 10 Years		
Held-to-Maturity:	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Total
Obligations of state and political subdivisions	$ 1,205	7.82 %	$ 1,838	6.96 %	$ -	-	$ -	-	$ 3,043

-35-

Table of Contents

Loan Portfolio

The loan portfolio totaled $585.0 million at December 31, 2009, down 3.9%, or $24.0 million, from $609.0 million at December 31, 2008. Loans decreased as commercial customers used cash flows to pay down debt and continued economic concerns stemmed loan production in both commercial and retail credits. In 2008, loans grew 6.9%, or $39.5 million. Of the $39.5 million growth in 2008, $18.3 million was in real estate loans secured by mortgages. The real estate loan growth consisted primarily of commercial credits that have ten to fifteen year amortization terms with rates fixed primarily for three years, but up to five years. We believe the short-term structure of these real estate mortgage credits allows greater flexibility in controlling interest rate risk. The commercial portfolio, including financial and agricultural loans, decreased $17.7 million in 2009. The installment loan portfolio decreased $10.4 million in 2009. Total real estate construction loans decreased $25.8 million, a portion of which reflected interim construction loan balances converted to permanent financing within the real estate mortgage loan portfolio, which increased $30.6 million.

The loan portfolio at December 31, 2009 consisted of approximately 53% in fixed rate loans, with the majority maturing within five years. Approximately 47% of the portfolio earns a variable rate of interest, the greater majority of which adjusts to changes in the Prime rate and a smaller portion that adjusts on a scheduled repricing date. The mix of variable and fixed rate loans provides some protection from changes in market rates of interest.

Table 6
Composition of Loans
December 31
(in thousands)

	2009	2008	2007	2006	2005
Commercial, financial, and agricultural	$ 192,347	$ 210,058	$ 190,946	$ 155,098	$ 153,737
Lease financing receivable	7,589	8,058	8,089	7,902	6,108
Real estate - mortgage	265,175	234,588	216,305	192,583	170,895
Real estate - construction	39,544	65,327	65,448	64,126	39,202
Installment loans to individuals	79,476	89,901	87,775	78,613	72,230
Other	911	1,023	942	724	622
Total loans	$ 585,042	$ 608,955	$ 569,505	$ 499,046	$ 442,794

NOTE: The December 31, 2007 loan composition reflects a reclassification in real estate – construction, real estate – mortgage, and commercial, financial, and agricultural loans.

Table 7
Loan Maturities and Sensitivity to Interest Rates
For the Year Ended December 31, 2009
(in thousands)

	Fixed and Variable Rate Loans at Stated Maturities				Amounts Over One Year With		
	1 Year or Less	1 Year – 5 Years	Over 5 years	Total	Predetermined Rates	Floating Rates	Total
Commercial, financial, and agricultural	$79,909	$90,355	$22,083	$192,347	$74,452	$37,986	$112,438
	269	7,223	97	7,589	7,320	-	7,320

Lease financing receivables							
Real estate - mortgage	23,346	93,021	148,808	265,175	104,375	137,454	241,829
Real estate - construction	26,603	8,882	4,059	39,544	7,727	5,214	12,941
Installment loans to individuals	18,430	59,681	1,365	79,476	57,545	3,501	61,046
Other	911	-	-	911	-	-	-
Total	$149,468	$259,162	$176,412	$585,042	$251,419	$184,155	$435,574

-36-

Table of Contents

We have maintained our credit policy and underwriting procedures and have not relaxed these procedures to stimulate loan growth. 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 insure thorough and consistent procedures.

Asset Quality

Credit Risk Management

We manage credit risk by observing written, board approved policies that govern all underwriting activities. The risk management program requires that each individual loan officer review his or her portfolio on a quarterly basis and assign recommended credit ratings on each loan. These efforts are supplemented by independent reviews performed by the loan review officer and other validations performed by the internal audit department. The results of the reviews are reported directly to the Audit Committee of the Board of Directors. Additionally, Bank concentrations are monitored and reported quarterly whereby individual customer and aggregate industry leverage, profitability, risk rating distributions, and liquidity are evaluated for each major standard industry classification segment. At December 31, 2009, we identified two industry segment concentrations that aggregate more than 10% of our loan portfolio. The oil and gas industry, including related service and manufacturing industries, totaled approximately $117.5 million, or 20.1% and the commercial real estate segment, the majority of which is owner-occupied real estate, represented approximately $90.7 million, or 15.5%, of the total loan portfolio.

Nonperforming Assets

Table 8 contains information about nonperforming assets, including loans past due 90 days or greater (“90 days or >”) and still accruing.

Table 8

Asset Quality Information

December 31

(in thousands)

	2009	2008	2007	2006	2005
Loans on nonaccrual	$16,183	$9,355	$1,602	$1,793	$660
Loans past due 90 days or >	378	1,005	980	98	2,510
Total nonperforming loans	16,561	10,360	2,582	1,891	3,170
Other real estate owned, net	792	329	143	368	98
Other assets repossessed	51	306	280	55	176
Total nonperforming assets	$17,404	$10,995	$3,005	$2,314	$3,444
Nonperforming loans to total loans	2.83 %	1.70 %	0.45 %	0.38 %	0.72 %
Nonperforming assets to total assets	1.79 %	1.17 %	0.35 %	0.29 %	0.49 %
Allowance as a percentage of nonperforming loans	48.28 %	73.22 %	217.35 %	263.19 %	137.38 %

Nonperforming assets, including loans past due, totaled $17.4 million at December 31, 2009 and $11.0 million at December 31, 2008. The increase in nonperforming assets in 2009 and 2008 resulted primarily from two large commercial loans in the Baton Rouge market secured by real estate. The first loan was placed on nonaccrual status in 2008 and is an $8.3 million commercial real estate loan in the Baton Rouge market which primarily funded construction of a condominium complex. As part of a work-out plan, the units are now being leased as apartments, with 57% of the units under lease agreements as of December 31, 2009. The second loan was placed on nonaccrual status in 2009 and is a $3.9 million national participation loan. In the fourth quarter of 2009, an additional $300,000 was charged off on the loan, bringing the total charged off in 2009 to $1.8 million. The loan will be a long term work-out based on actions taken by the lead bank.

Allowance coverage for nonperforming loans was 48.28% at December 31, 2009, compared to 73.22% at December 31, 2008. Excluding the effect of the two large commercial real estate loans in the Baton Rouge market, allowance coverage for nonperforming loans was 158.37% at December 31, 2009 and 342.88% at December 31, 2008. Year-to-date net charge-offs were 0.86% of total loans as of December 31, 2009 compared to 0.40% as of December 31,

Table of Contents

2008. The increased charge-off activity in the loan portfolio is reflective of the current economic environment. The ALLL/total loans ratio was 1.37% at December 31, 2009 compared to 1.25% at December 31, 2008.

Consumer and commercial loans are placed on nonaccrual status when principal or interest is 90 days past due, or sooner if the full collectibility of principal or interest is doubtful, except if the underlying collateral fully supports both the principal and accrued interest and the loan is in the process of collection. Our policies provide that retail (consumer) loans that become 120 days delinquent be routinely charged off. Loans classified for regulatory purposes but not included in Table 8 do not represent material amounts that we have serious doubts as to the ability of the borrower to comply with loan repayment terms.

Allowance for Loan Losses

Provisions totaling $5,450,000, $4,555,000, and $1,175,000, for the years 2009, 2008, and 2007, respectively, were considered necessary to bring the allowance for loan losses to a level we believe sufficient to cover probable losses in the loan portfolio. Table 9 analyzes activity in the allowance for 2009, 2008, 2007, 2006, and 2005.

Table 9
Summary of Loan Loss Experience
(in thousands)

	2009	2008	2007	2006	2005
Balance at beginning of year	$7,586	$5,612	$4,977	$4,355	$3,851