

FIRST MID ILLINOIS BANCSHARES INC
Form 10-K
March 05, 2009

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, 2008

or

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

For the transition period from _____ to _____

Commission file number: 0-13368

FIRST MID-ILLINOIS BANCSHARES, INC.

(Exact name of Registrant as specified in its charter)

Delaware

37-1103704

(State or other jurisdiction of incorporation or
organization)

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

1515 Charleston Avenue, Mattoon, Illinois

61938

(Address of Principal Executive Offices)

(Zip Code)

(217) 234-7454

(Registrant's telephone number, including area code)

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

NONE

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

Common stock, par value \$4.00 per share,
and related Common Stock Purchase Rights

(Title of class)

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ☐ Yes ☒ No

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

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

☒ No ☐

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Indicate by check mark if disclosure of delinquent filers pursuant 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. [X]

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer []

Accelerated filer [X]

Non-accelerated filer []

Smaller reporting company []

(Do not check if 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 [X] No

The aggregate market value of the outstanding common stock, other than shares held by persons who may be deemed affiliates of the Registrant, as of the last business day of the Registrant's most recently completed second fiscal quarter was approximately \$101,786,000. Determination of stock ownership by non-affiliates was made solely for the purpose of responding to this requirement and the Registrant is not bound by this determination for any other purpose.

As of March 4, 2009, 6,122,877 shares of the Registrant's common stock, \$4.00 par value, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Document

Into Form 10-K Part:

Portions of the Proxy Statement for 2009 Annual

Meeting of Shareholders to be held on April 29, 2009

III

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PART I

ITEM 1.BUSINESS

Company and Subsidiaries

First Mid-Illinois Bancshares, Inc. (the “Company”) is a financial holding company. The Company is engaged in the business of banking through its wholly owned subsidiary, First Mid-Illinois Bank & Trust, N.A. (“First Mid Bank”). The Company provides data processing services to affiliates through another wholly owned subsidiary, Mid-Illinois Data Services, Inc. (“MIDS”). The Company offers insurance products and services to customers through its wholly owned subsidiary, The Checkley Agency, Inc. (“Checkley”). The Company also wholly owns two statutory business trusts, First Mid-Illinois Statutory Trust I (“Trust I”), and First Mid-Illinois Statutory Trust II (“Trust II”), both unconsolidated subsidiaries of the Company.

The Company, a Delaware corporation, was incorporated on September 8, 1981, and pursuant to the approval of the Board of Governors of the Federal Reserve System (the “Federal Reserve Board”) became the holding company owning all of the outstanding stock of First National Bank, Mattoon (“First National”) on June 1, 1982. First National changed its name at that time to First Mid-Illinois Bank & Trust, N.A. in 1992. The Company acquired all of the outstanding stock of a number of community banks or thrift institutions on the following dates, and subsequently combined their operations with those of the Company:

- Mattoon Bank, Mattoon on April 2, 1984
- State Bank of Sullivan on April 1, 1985
- Cumberland County National Bank in Neoga on December 31, 1985
- First National Bank and Trust Company of Douglas County on December 31, 1986
 - Charleston Community Bank on December 30, 1987
- Heartland Federal Savings and Loan Association on July 1, 1992
 - Downstate Bancshares, Inc. on October 4, 1994
 - American Bank of Illinois on April 20, 2001

In 1997, First Mid Bank acquired the Charleston, Illinois branch location and the customer base of First of America Bank and in 1999 acquired the Monticello, Taylorville and DeLand branch offices and deposit base of Bank One Illinois, N.A.

First Mid Bank has also opened a de novo branch in Decatur, Illinois and a banking center in the Student Union of Eastern Illinois University in Charleston, Illinois (2000); de novo branches in Champaign, Illinois and Maryville, Illinois (2002), and a de novo branch in Highland, Illinois (2005).

In 2002, the Company acquired all of the outstanding stock of Checkley, an insurance agency located in Mattoon.

On May 1, 2006, the Company acquired Mansfield Bancorp, Inc. (“Mansfield”), and its wholly owned subsidiary, Peoples State Bank of Mansfield (“Peoples”) with locations in Mansfield, Mahomet and Weldon, Illinois. On September 8, 2006, Peoples merged with and into First Mid Bank with First Mid Bank being the surviving entity. This cash acquisition added approximately \$108 million to total deposits, \$55.8 million to loans, \$1.5 million to premises and equipment and \$11.5 million to goodwill and core deposit intangible assets.

Employees

The Company, MIDS, Checkley and First Mid Bank, collectively, employed 343 people on a full-time equivalent basis as of December 31, 2008. The Company places a high priority on staff development, which involves extensive training, including customer service training. New employees are selected on the basis of both technical skills and customer service capabilities. None of the employees are covered by a collective bargaining agreement with the Company. The Company offers a variety of employee benefits.

Business Lines

The Company has chosen to operate in three primary lines of business—community banking and wealth management through First Mid Bank and insurance brokerage through Checkley. Of these, the community banking line contributes approximately 89% of the Company's total revenues and profits. Within the community banking line, the Company serves commercial, retail and agricultural customers with a broad array of deposit and loan related products. The wealth management line provides estate planning, investment and farm management services for individuals and employee benefit services for business enterprises. The insurance brokerage line provides commercial lines insurance to businesses as well as homeowner, automobile and other types of personal lines insurance to individuals.

All three lines emphasize a “hands on” approach to service so that products and services can be tailored to fit the specific needs of existing and potential customers. Management believes that by emphasizing this personalized approach, the Company can, to a degree, diminish the trend towards homogeneous financial services, thereby differentiating the Company from competitors and allowing for slightly higher operating margins in each of the three lines.

Business Strategies

Strategy for Growth

The Company believes that growth of its revenue stream and of its customer base is vital to the goal of increasing the value of its shareholders' investment. Management attempts to grow in two primary ways:

- by organic growth through adding new customers and selling more products and services to existing customers; and
- by acquisitions.

Virtually all of the Company's customer-contact personnel, in each of its business lines, are engaged in organic growth efforts to one degree or another. These personnel are trained to engage in needs-based selling whereby they make an attempt to match its products and services with the particular financial needs of individual customers and prospective customers. Most senior officers of the organization are required to attend monthly sales meetings where they report on their business development efforts and results. Executive management uses these meetings as an educational and risk management opportunity as well. Cross-selling opportunities are encouraged between the business lines.

Within the community banking line, the Company has focused on growing business operating and real estate loans. Total commercial real estate loans have increased from \$255 million at December 31, 2004 to \$317 million at December 31, 2008. Approximately 67% of the Company's total revenues are derived from lending activities. The Company has also focused on growing the commercial and retail deposit base through growth in checking, money markets and customer repurchase agreement balances. The wealth management line has focused its growth efforts on estate planning, investment and farm management services for individuals and employee benefit services for businesses. The insurance brokerage line has focused on increasing property and casualty insurance for businesses and personal lines insurance to individuals.

Growth through a series of small acquisitions has been an integral part of the Company's strategy for an extended period of time. When reviewing acquisition possibilities, the Company focuses on those organizations where there is a cultural fit with its existing operations and where there is a strong likelihood of adding to shareholder value. Most past acquisitions have been cash-based transactions. While the Company expects to continue this trend in the future, it would consider a stock-based acquisition if the strategic and financial metrics were compelling. The emphasis on smaller acquisitions is due to the inherent risks accompanying acquisitions and the preference for cash financing rather than use of the Company's common stock.

This overall growth strategy has been to grow the customer base without significantly increasing the shareholder base. This requires a certain amount of financial leverage and the Company monitors its capital base carefully to satisfy all regulatory requirements while maintaining flexibility. The Company has maintained a Dividend Reinvestment Plan as well as various forms of equity compensation for directors and key managers. It has also maintained an ongoing share buy back program both as a service to shareholders and a means of maintaining optimal levels of capital. The Company uses various forms of long-term debt to augment its capital when appropriate.

Strategy for Operations and Risk Management

Operationally, the Company centralizes as many administrative and clerical tasks as possible within its home office location in Mattoon, Illinois. This allows branches to maintain customer focus, helps assure compliance with banking regulations, keeps fixed administrative costs at as low a level as is practicable, and better manages the various forms of risk inherent in this business. This approach also allows for the best possible use of technology in day-to-day banking activities thereby reducing the potential for human error. While the Company does not employ every new technology that is introduced, it does attempt to be near the leading edge with respect to operational technology.

The Company has a comprehensive set of operational policies and procedures that have been developed over time to address risk. These policies are intended to be as close as possible to "best practices" of the financial services industry and are subjected to continual review by management and the Board of Directors. The Company's internal audit

function incorporates procedures to determine compliance with these policies.

In the business of banking, credit risk is the single most important risk as losses from uncollectible loans can significantly diminish capital, earnings and shareholder value. In order to address this risk, the lending function of First Mid Bank receives significant attention from executive management and the Board of Directors. An important element of credit risk management is the quality, experience and training of the loan officers of First Mid Bank. The Company has invested, and will continue to invest, significant resources to ensure the quality, experience and training of First Mid Bank's loan officers in order to keep credit losses at a minimum. In addition to the human element of credit risk management, the Company's loan policies address the additional aspects of credit risk. Most lending personnel have signature authority that allows them to lend up to a certain amount based on their own judgment as to the creditworthiness of a borrower. The amount of the signature authority is based on the lending officers' experience and training. The Senior Loan Committee, consisting of the most experienced lenders within the organization, must approve all underwriting decisions in excess of \$1.5 million. The Board of Directors must approve all underwriting decisions in excess of \$2 million.

While the underlying nature of lending will result in some amount of loan losses, First Mid Bank's loan loss experience has been good with average net charge offs amounting to \$1,021,000 (.15% of average loans) over the past five years. Nonperforming loans were \$7,285,000 (.98% of total loans) at December 31, 2008. These percentages have historically compared well with peer financial institutions.

Interest rate and liquidity risk are two other forms of risk embedded in the business of financial intermediation. The Company's Asset Liability Management Committee, consisting of experienced individuals who monitor all aspects of interest rates and maturities of interest earning assets and interest paying liabilities, manages these risks. The underlying objectives of interest rate and liquidity risk management are to shelter the Company's net interest margin from changes in interest rates while maintaining adequate liquidity reserves to meet unanticipated funding demands. The Company uses financial modeling technology as a tool, employing a variety of "what if" scenarios to properly plan its activities. Despite the tools and methods used to monitor this risk, a sustained unfavorable interest rate environment will lead to some amount of compression in the net interest margin. During 2008, the Company's net interest margin increased to 3.73% from 3.43% in 2007. This was the result of a greater decrease in borrowing and deposit rates compared to the decrease in interest-earning asset rates.

Markets and Competition

The Company has active competition in all areas in which First Mid Bank presently does business. First Mid Bank competes for commercial and individual deposits, loans, and trust business with many east central Illinois banks, savings and loan associations, and credit unions. The principal methods of competition in the banking and financial services industry are quality of services to customers, ease of access to facilities, and pricing of services, including interest rates paid on deposits, interest rates charged on loans, and fees charged for fiduciary and other banking services.

First Mid Bank operates facilities in the Illinois counties of Bond, Champaign, Christian, Coles, Cumberland, Dewitt, Douglas, Effingham, Macon, Madison, Moultrie, and Piatt. Each facility primarily serves the community in which it is located. First Mid Bank serves nineteen different communities with twenty-six separate locations in the towns of Altamont, Arcola, Champaign, Charleston, Decatur, Effingham, Highland, Mansfield, Mahomet, Maryville, Mattoon, Monticello, Neoga, Pocahontas, Sullivan, Taylorville, Tuscola, Urbana, and Weldon Illinois. Within the areas of service, there are numerous competing financial institutions and financial services companies.

Website

The Company maintains a website at www.firstmid.com. All periodic and current reports of the Company and amendments to these reports filed with the Securities and Exchange Commission ("SEC") can be accessed, free of charge, through this website as soon as reasonably practicable after these materials are filed with the SEC.

SUPERVISION AND REGULATION

General

Financial institutions, financial services companies, and their holding companies are extensively regulated under federal and state law. As a result, the growth and earnings performance of the Company can be affected not only by management decisions and general economic conditions, but also by the requirements of applicable state and federal statutes and regulations and the policies of various governmental regulatory authorities including, but not limited to, the Office of the Comptroller of the Currency (the "OCC"), the Federal Reserve Board, the Federal Deposit Insurance Corporation (the "FDIC"), the Internal Revenue Service and state taxing authorities. Any change in applicable laws, regulations or regulatory policies may have material effects on the business, operations and prospects of the Company and First Mid Bank. The Company is unable to predict the nature or extent of the effects that fiscal or monetary policies, economic controls or new federal or state legislation may have on its business and earnings in the future.

Federal and state laws and regulations generally applicable to financial institutions and financial services companies, such as the Company and its subsidiaries, regulate, among other things, the scope of business, investments, reserves against deposits, capital levels relative to operations, the nature and amount of collateral for loans, the establishment of branches, mergers, consolidations and dividends. The system of supervision and regulation applicable to the Company and its subsidiaries establishes a comprehensive framework for their respective operations and is intended primarily for the protection of the FDIC's deposit insurance funds and the depositors, rather than the stockholders, of financial institutions.

The following references to material statutes and regulations affecting the Company and its subsidiaries are brief summaries thereof and do not purport to be complete, and are qualified in their entirety by reference to such statutes and regulations. Any change in applicable law or regulations may have a material effect on the business of the Company and its subsidiaries.

Financial Modernization Legislation

The 1999 Gramm-Leach-Bliley Act (the “GLB Act”) significantly changed financial services regulation by expanding permissible non-banking activities of bank holding companies and removing certain barriers to affiliations among banks, insurance companies, securities firms and other financial services entities. These activities and affiliations can be structured through a holding company structure or, in the case of many of the activities, through a financial subsidiary of a bank. The GLB Act also established a system of federal and state regulation based on functional regulation, meaning that primary regulatory oversight for a particular activity generally resides with the federal or state regulator having the greatest expertise in the area. Banking is supervised by banking regulators, insurance by state insurance regulators and securities activities by the SEC and state securities regulators. The GLB Act also requires the disclosure of agreements reached with community groups that relate to the Community Reinvestment Act, and contains various other provisions designed to improve the delivery of financial services to consumers while maintaining an appropriate level of safety in the financial services industry.

The GLB Act repeals the anti-affiliation provisions of the Glass-Steagall Act and revises the Bank Holding Company Act of 1956 (the “BHCA”) to permit qualifying holding companies, called “financial holding companies,” to engage in, or to affiliate with companies engaged in, a full range of financial activities, including banking, insurance activities (including insurance portfolio investing), securities activities, merchant banking and additional activities that are “financial in nature,” incidental to financial activities or, in certain circumstances, complementary to financial activities. A bank holding company’s subsidiary banks must be “well-capitalized” and “well-managed” and have at least a “satisfactory” Community Reinvestment Act rating for the bank holding company to elect and maintain its status as a financial holding company.

A significant component of the GLB Act’s focus on functional regulation relates to the application of federal securities laws and SEC oversight of some bank securities activities previously exempt from broker-dealer registration. Among other things, the GLB Act amends the definitions of “broker” and “dealer” under the Securities Exchange Act of 1934 to remove the blanket exemption for banks. Under the GLB Act, banks may conduct securities activities without broker-dealer registration only if the activities fall within a set of activity-based exemptions designed to allow banks to conduct only those activities traditionally considered to be primarily banking or trust activities. Securities activities outside these exemptions, as a practical matter, need to be conducted by registered broker-dealer affiliate. By several orders, the SEC extended the blanket exemption for banks from the definition of “broker” and “dealer” while it considered implementing rules. In 2003, the SEC adopted amendments to its rules relating to the “dealer” exemption for banks. In September 2007, the SEC and the Federal Reserve Board adopted a regulation to implement the broker activities exemption of the GLB Act that became effective for First Mid Bank beginning January 1, 2009. The GLB Act also amends the Investment Advisers Act of 1940 to require the registration of banks that act as investment advisers for mutual funds. The Company believes that it has taken the necessary actions to comply with these requirements of the GLB Act and the regulations adopted under them.

Anti-Terrorism Legislation

The USA PATRIOT Act of 2001 included the International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001 (the "IMLAFA"). The IMLAFA contains anti-money laundering measures affecting insured depository institutions, broker-dealers, and certain other financial institutions. The IMLAFA requires U.S. financial institutions to adopt policies and procedures to combat money laundering and grants the Secretary of the Treasury broad authority to establish regulations and to impose requirements and restrictions on financial institutions' operations. The Company has established policies and procedures for compliance with the IMLAFA and the related regulations. The Company has designated an officer solely responsible for ensuring compliance with existing regulations and monitoring changes to the regulations as they occur.

Emergency Economic Stabilization Act of 2008

In response to recent unprecedented financial market turmoil, the Emergency Economic Stabilization Act of 2008 ("EESA") was enacted on October 3, 2008. EESA authorizes the U.S. Treasury Department to provide up to \$700 billion in funding for the financial services industry. Pursuant to the EESA, the Treasury was initially authorized to use \$350 billion for the Troubled Asset Relief Program (TARP). Of this amount, Treasury allocated \$250 billion to the TARP Capital Purchase Program. On January 15, 2009, the second \$350 billion of TARP monies was released to the Treasury. The Secretary's authority under TARP expires on December 31, 2009 unless the Secretary certifies to Congress that extension is necessary provided that his authority may not be extended beyond October 3, 2010. The Company decided to not participate in the TARP Capital Purchase Program.

Before and after EESA, there have been numerous actions by the Federal Reserve Board, Congress, the Treasury, the FDIC, the SEC and others to further the economic and banking industry stabilization efforts, including the American Recovery and Reinvestment Act. It remains unclear at this time what further legislative and regulatory measures will be implemented under EESA affecting the Company. To date, the Company or the Bank has elected to participate only in the FDIC's Debt Guarantee Program, which provides for the guarantee of eligible newly issued senior unsecured debt of participating entities, and the FDIC's Transaction Account Guarantee Program, which provides, without charge to depositors, a full guarantee on all non-interest bearing transaction accounts held by any depositor, regardless of dollar amount, through December 31, 2009. Participation in the Transaction Account Guarantee Program will cost the Company 10 basis points annually on the amount of the deposits. Both of these programs are part of the FDIC's Temporary Liquidity Guarantee Program.

The Company

General. As a registered bank holding company under the BHCA that has elected to become a financial holding company under the GLB Act, the Company is subject to regulation by the Federal Reserve Board. In accordance with Federal Reserve Board policy, the Company is expected to act as a source of financial strength to First Mid Bank and to commit resources to support First Mid Bank in circumstances where the Company might not do so absent such policy. The Company is subject to inspection, examination, and supervision by the Federal Reserve Board.

Activities. As a financial holding company, the Company may affiliate with securities firms and insurance companies and engage in other activities that are financial in nature or incidental or complementary to activities that are financial in nature. A bank holding company that is not also a financial holding company is limited to engaging in banking and such other activities as determined by the Federal Reserve Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto.

No Federal Reserve Board approval is required for the Company to acquire a company (other than a bank holding company, bank, or savings association) engaged in activities that are financial in nature or incidental to activities that are financial in nature, as determined by the Federal Reserve Board. However, the Company generally must give the Federal Reserve Board after-the-fact notice of these activities. Prior Federal Reserve Board approval is required

before the Company may acquire beneficial ownership or control of more than 5% of the voting shares or substantially all of the assets of a bank holding company, bank, or savings association.

If any subsidiary bank of the Company ceases to be “well-capitalized” or “well-managed” under applicable regulatory standards, the Federal Reserve Board may, among other actions, order the Company to divest its depository institution. Alternatively, the Company may elect to conform its activities to those permissible for a bank holding company that is not also a financial holding company.

If any subsidiary bank of the Company receives a rating under the Community Reinvestment Act of less than “satisfactory”, the Company will be prohibited, until the rating is raised to “satisfactory” or better, from engaging in new activities or acquiring companies other than bank holding companies, banks, or savings associations.

Capital Requirements. Bank holding companies are required to maintain minimum levels of capital in accordance with Federal Reserve Board capital adequacy guidelines. The Federal Reserve Board’s capital guidelines establish the following minimum regulatory capital requirements for bank holding companies: a risk-based requirement expressed as a percentage of total risk-weighted assets, and a leverage requirement expressed as a percentage of total assets. The risk-based requirement consists of a minimum ratio of total capital to total risk-weighted assets of 8%, at least one-half of which must be Tier 1 capital. The leverage requirement consists of a minimum ratio of Tier 1 capital to total assets of 3% for the most highly rated companies, with minimum requirements of at least 4% for all others. For purposes of these capital standards, Tier 1 capital consists primarily of permanent stockholders’ equity, which includes the Series B 9% Non-Cumulative Perpetual Convertible Preferred Stock issued by the Company on February 11, 2009, less intangible assets (other than certain mortgage servicing rights and purchased credit card relationships), and total capital means Tier 1 capital plus certain other debt and equity instruments which do not qualify as Tier 1 capital, limited amounts of unrealized gains on equity securities and a portion of the Company’s allowance for loan and lease losses.

The risk-based and leverage standards described above are minimum requirements, and higher capital levels will be required if warranted by the particular circumstances or risk profiles of individual banking organizations. For example, the Federal Reserve Board's capital guidelines contemplate that additional capital may be required to take adequate account of, among other things, interest rate risk, or the risks posed by concentrations of credit, nontraditional activities or securities trading activities. Further, any banking organization experiencing or anticipating significant growth would be expected to maintain capital ratios, including tangible capital positions (i.e., Tier 1 capital less all intangible assets), well above the minimum levels.

In December 2007, the U.S. bank regulatory agencies adopted final rules that require large, internationally active financial services organizations to use the most sophisticated and complex methodology for calculating capital requirements reflected in the New Basel Capital Accord, developed by the Basel Committee on Banking Supervision. These rules became operational in April 2008, but are mandatory only for "core banks," i.e., banks with consolidated total assets of \$250 billion or more. In July 2008, the U.S. bank regulatory agencies also published a notice of proposed rule-making that would provide all non-core banking organizations with the option to adopt a standardized approach under these rules, which reflects a simpler methodology than the advanced approaches required of core banks.

As of December 31, 2008, the Company had regulatory capital, calculated on a consolidated basis, in excess of the Federal Reserve Board's minimum requirements, and its capital ratios exceeded those required for categorization as well-capitalized under the capital adequacy guidelines established by bank regulatory agencies with a total risk-based capital ratio of 11.99%, a Tier 1 risk-based ratio of 11.02% and a leverage ratio of 8.41%.

Control Acquisitions. The Change in Bank Control Act prohibits a person or group of person from acquiring "control" of a bank holding company unless the Federal Reserve Board has been notified and has not objected to the transaction. Under a rebuttable presumption established by the Federal Reserve Board, the acquisition of 10% or more of a class of voting stock of a bank holding company with a class of securities registered under Section 12 of the Exchange Act, such as the Company, would, under the circumstances set forth in the presumption, constitute acquisition of control of the Company.

In addition, any company is required to obtain the approval of the Federal Reserve Board under the BHCA before acquiring 25% (5% in the case of an acquirer that is a bank holding company) or more of the outstanding common of the Company, or otherwise obtaining control of a "controlling influence" over the Company or First Mid Bank.

Interstate Banking and Branching. The Riegle-Neal Act enacted in 1994 permits an adequately capitalized and adequately managed bank holding company, with Federal Reserve Board approval, to acquire banking institutions located in states other than the bank holding company's home state without regard to whether the transaction is prohibited under state law. In addition, national banks and state banks with different home states are permitted to merge across state lines, with the approval of the appropriate federal banking agency, unless the home state of a participating banking institution has passed legislation prior to that date that expressly prohibits interstate mergers. De novo interstate branching is permitted if the laws of the host state so authorize. Moreover, national banks, such as First Mid Bank, may provide trust services in any state to the same extent as a trust company chartered by that state.

Privacy and Security. The GLB Act establishes a minimum federal standard of financial privacy by, among other provisions, requiring banks to adopt and disclose privacy policies with respect to consumer information and setting forth certain rules with respect to the disclosure to third parties of consumer information. The Company has adopted and disseminated its privacy policies pursuant to the GLB Act. Regulations adopted under the GLB Act set standards for protecting the security, confidentiality and integrity of customer information, and require notice to regulators, and in some cases, to customers, in the event of security breaches. A number of states have adopted their own statutes requiring notification of security breaches. In addition, the GLB Act requires the disclosure of agreements reached with community groups that relate to the CRA, and contains various other provisions designed to improve the delivery of financial services to consumers while maintaining an appropriate level of safety in the financial services industry.

First Mid Bank

General. First Mid Bank is a national bank, chartered under the National Bank Act. The FDIC insures the deposit accounts of First Mid Bank. As a national bank, First Mid Bank is a member of the Federal Reserve System and is subject to the examination, supervision, reporting and enforcement requirements of the OCC, as the primary federal regulator of national banks, and the FDIC, as administrator of the deposit insurance fund.

Deposit Insurance. As an FDIC-insured institution, First Mid Bank is required to pay deposit insurance premium assessments to the FDIC. Under the FDIC's risk-based insurance assessment system, as amended by the Federal Deposit Insurance Reform Act and implementing regulations effective for 2007, each insured bank is required to pay deposit insurance premium assessments to the FDIC. Each insured bank is placed in one of four risk categories based on its level of capital, supervisory ratings and other risk measures, including debt ratings for large institutions, and its insurance assessment rate is determined by its risk category. There was a 38 basis point spread between the highest and lowest assessment rates, so that banks classified by the FDIC in Risk Category I were subject in 2007 to an insurance assessment of five to seven basis points (according to the FDIC's assessment of the bank's strength), and banks classified by the FDIC in Risk Category IV were subject to an insurance assessment rate of .43%. First Mid Bank's annual assessment rate for 2008 was 5.33 to 5.50 basis points.

In addition to its insurance assessment, each insured bank is subject, in 2008, to quarterly debt service assessments in connection with bonds issued by a government corporation that financed the federal savings and loan bailout. The first quarter 2009 debt service assessment was .0114%.

Banks which paid assessments prior to December 31, 1996 were eligible for certain one-time credits against these assessments from a pool provided for in the legislation. First Mid Bank received a one-time credit of approximately \$701,000 of which approximately \$381,000 and \$320,000 was applied in 2008 and 2007, respectively.

On October 16, 2008, the FDIC published a restoration plan designed to replenish the Deposit Insurance Fund over a period of five years and to increase the deposit insurance reserve ratio, which decreased to 1.01% of insured deposits on June 30, 2008, to the statutory minimum of 1.15% of insured deposits by December 31, 2013. In order to implement the restoration plan, the FDIC proposes to change both its risk-based assessment system and its base assessment rates. For the first quarter of 2009 only, the FDIC increased all FDIC deposit assessment rates by 7 basis points. These new rates range from 12-14 basis points for Risk Category I institutions to 50 basis points for Risk Category IV institutions. Under the FDIC's restoration plan, the FDIC proposes to establish new initial base assessment rates that will be subject to adjustment as described below. Beginning April 1, 2009, the base assessment rates would range from 10-14 basis points for Risk Category I institutions to 45 basis points for Risk Category IV institutions. Changes to the risk-based assessment system would include increasing premiums for institutions that rely on excessive amounts of brokered deposits, including CDARS, increasing premiums for excessive use of secured liabilities, including Federal Home Loan Bank advances, lowering premiums for smaller institutions with very high capital levels, and adding financial ratios and debt issuer ratings to the premium calculations for banks with over \$10 billion in assets, while providing a reduction for their unsecured debt. Either an increase in the Risk Category of the Bank or adjustments to the base assessment rates could have a material adverse effect on our earnings.

The enactment of EESA temporarily raised the basic limit on federal deposit insurance coverage from \$100,000 to \$250,000 per depositor. The temporary increase in deposit insurance coverage became effective on October 3, 2008. EESA provides that the basic deposit insurance limit will return to \$100,000 after December 31, 2009.

The FDIC may terminate the deposit insurance of any insured depository institution if the FDIC determines, after a hearing, that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, order, or any condition imposed in writing by, or written agreement with, the FDIC. The FDIC may also suspend deposit insurance temporarily during the hearing process for a permanent termination of insurance if the institution has no tangible capital. Management of the Company is not aware of any activity or condition that could result in termination of the deposit insurance of First Mid Bank.

On October 14, 2008, the FDIC announced the Temporary Liquidity Guarantee Program (TLGP). The final rule was adopted on November 21, 2008. The FDIC stated that the program's purpose is to strengthen confidence and encourage liquidity in the banking system by guaranteeing newly issued senior unsecured debt of 31 days or greater, of banks, thrifts, and certain holding companies, and by providing full FDIC insurance coverage for all non-interest bearing transaction accounts, regardless of dollar amount. Inclusion in the program was voluntary. Institutions participating in the senior unsecured debt portion of the program are assessed fees based on a sliding scale, depending on length of maturity. Shorter-term debt has a lower fee structure and longer-term debt has a higher fee. The range is from 50 basis points on debt of 180 days or less, to a maximum of 100 basis points for debt with maturities of one year or longer, on an annualized basis. A 10-basis point surcharge is added to a participating institution's current insurance assessment in exchange for final coverage for all transaction accounts.

First Mid Bank elected to participate in both parts of the TLGP. The amount of greater than 30 day unsecured senior debt that is eligible for the program is limited to 125% of the amount of such debt outstanding as of September 30, 2008. If there was no unsecured senior debt outstanding at September 30, 2008, the amount available under the program is limited to two percent of total liabilities as of September 30, 2008. As the Bank did not have any unsecured senior debt outstanding as of September 30, 2008, the maximum amount of unsecured senior debt that can be issued under the program is limited to two percent of its total liabilities as of September 30, 2008 (approximately \$18.3 million).

On February 27, 2009, the FDIC adopted an interim rule to impose a 20 basis point emergency special assessment on June 30, 2009. The assessment will be collected on September 30, 2009. The interim rule also provides that, after June 30, 2009, if the reserve ratio of the Deposit Insurance Fund is estimated to fall to a level that the Board believes would adversely affect public confidence or to a level which shall be close to zero or negative at the end of a calendar

quarter, an emergency special assessment of up to 10 basis points may be imposed by a vote of the Board on all insured depository institutions based on each institution's assessment base calculated for the corresponding assessment period. The Company is currently evaluating the impact this special assessment will have on its consolidated financial statements.

OCC Assessments. All national banks are required to pay supervisory fees to the OCC to fund the operations of the OCC. The amount of such supervisory fees is based upon each institution's total assets, including consolidated subsidiaries, as reported to the OCC. During the year ended December 31, 2008, First Mid Bank paid supervisory fees to the OCC totaling \$223,000.

Capital Requirements. The OCC has established the following minimum capital standards for national banks, such as First Mid Bank: a leverage requirement consisting of a minimum ratio of Tier 1 capital to total assets of 3% for the most highly-rated banks with minimum requirements of at least 4% for all others, and a risk-based capital requirement consisting of a minimum ratio of total capital to total risk-weighted assets of 8%, at least one-half of which must be Tier 1 capital. For purposes of these capital standards, Tier 1 capital and total capital consists of substantially the same components as Tier 1 capital and total capital under the Federal Reserve Board's capital guidelines for bank holding companies (See "The Company—Capital Requirements").

The capital requirements described above are minimum requirements. Higher capital levels will be required if warranted by the particular circumstances or risk profiles of individual institutions. For example, the regulations of the OCC provide that additional capital may be required to take adequate account of, among other things, interest rate risk or the risks posed by concentrations of credit, nontraditional activities or securities trading activities.

During the year ended December 31, 2008, First Mid Bank was not required by the OCC to increase its capital to an amount in excess of the minimum regulatory requirements, and its capital ratios exceeded those required for categorization as well-capitalized under the capital adequacy guidelines established by bank regulatory agencies with a total risk-based capital ratio of 13.00%, a Tier 1 risk-based ratio of 12.02% and a leverage ratio of 9.16%.

Prompt Corrective Action. Federal law provides the federal banking regulators with broad power to take prompt corrective action to resolve the problems of undercapitalized institutions. The extent of the regulators' powers depends on whether the institution in question is "well-capitalized," "adequately-capitalized," "undercapitalized," "significantly undercapitalized" or "critically undercapitalized." Depending upon the capital category to which an institution is assigned, the regulators' corrective powers include: requiring the submission of a capital restoration plan; placing limits on asset growth and restrictions on activities; requiring the institution to issue additional capital stock (including additional voting stock) or to be acquired; restricting transactions with affiliates; restricting the interest rate the institution may pay on deposits; ordering a new election of directors of the institution; requiring that senior executive officers or directors be dismissed; prohibiting the institution from accepting deposits from correspondent banks; requiring the institution to divest certain subsidiaries; prohibiting the payment of principal or interest on subordinated debt; and in the most severe cases, appointing a conservator or receiver for the institution.

Dividends. The National Bank Act imposes limitations on the amount of dividends that may be paid by a national bank, such as First Mid Bank. Generally, a national bank may pay dividends out of its undivided profits, in such amounts and at such times as the bank's board of directors deems prudent. Without prior OCC approval, however, a national bank may not pay dividends in any calendar year which, in the aggregate, exceed the bank's year-to-date net income plus the bank's adjusted retained net income for the two preceding years.

The payment of dividends by any financial institution or its holding company is affected by the requirement to maintain adequate capital pursuant to applicable capital adequacy guidelines and regulations, and a financial institution generally is prohibited from paying any dividends if, following payment thereof, the institution would be undercapitalized. As described above, First Mid Bank exceeded its minimum capital requirements under applicable guidelines as of December 31, 2008. As of December 31, 2008, approximately \$5.2 million was available to be paid as dividends to the Company by First Mid Bank. Notwithstanding the availability of funds for dividends, however, the OCC may prohibit the payment of any dividends by First Mid Bank if the OCC determines that such payment would constitute an unsafe or unsound practice.

Affiliate and Insider Transactions. First Mid Bank is subject to certain restrictions under federal law, including Regulation W of the Federal Reserve Board, on extensions of credit to the Company and its subsidiaries, on investments in the stock or other securities of the Company and its subsidiaries and the acceptance of the stock or other securities of the Company or its subsidiaries as collateral for loans. Certain limitations and reporting requirements are also placed on extensions of credit by First Mid Bank to its directors and officers, to directors and officers of the Company and its subsidiaries, to principal stockholders of the Company, and to "related interests" of such directors, officers and principal stockholders.

First Mid Bank is subject to restrictions under federal law that limits certain transactions with the Company, including loans, other extensions of credit, investments or asset purchases. Such transactions by a banking subsidiary with any one affiliate are limited in amount to 10 percent of the bank's capital and surplus and, with all affiliates together, to an aggregate of 20 percent of the bank's capital and surplus. Furthermore, such loans and extensions of credit, as well as certain other transactions, are required to be secured in specified amounts. These and certain other transactions, including any payment of money to the Company, must be on terms and conditions that are or in good faith would be offered to nonaffiliated companies.

In addition, federal law and regulations may affect the terms upon which any person becoming a director or officer of the Company or one of its subsidiaries or a principal stockholder of the Company may obtain credit from banks with which First Mid Bank maintains a correspondent relationship.

Safety and Soundness Standards. The federal banking agencies have adopted guidelines that establish operational and managerial standards to promote the safety and soundness of federally insured depository institutions. The guidelines set forth standards for internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, fees and benefits, asset quality and earnings. In general, the guidelines prescribe the goals to be achieved in each area, and each institution is responsible for

establishing its own procedures to achieve those goals. If an institution fails to comply with any of the standards set forth in the guidelines, the institution's primary federal regulator may require the institution to submit a plan for achieving and maintaining compliance. The preamble to the guidelines states that the agencies expect to require a compliance plan from an institution whose failure to meet one or more of the guidelines are of such severity that it could threaten the safety and soundness of the institution. Failure to submit an acceptable plan, or failure to comply with a plan that has been accepted by the appropriate federal regulator, would constitute grounds for further enforcement action.

Community Reinvestment Act. First Mid Bank is subject to the Community Reinvestment Act (CRA). The CRA and the regulations issued thereunder are intended to encourage banks to help meet the credit needs of their service areas, including low and moderate income neighborhoods, consistent with the safe and sound operations of the banks. These regulations also provide for regulatory assessment of a bank's record in meeting the needs of its service area when considering applications to establish branches, merger applications and applications to acquire the assets and assume the liabilities of another bank. The Financial Institutions Reform, Recovery and Enforcement Act of 1989 requires federal banking agencies to make public a rating of a bank's performance under the CRA. In the case of a bank holding company, the CRA performance record of its bank subsidiaries is reviewed by federal banking agencies in connection with the filing of an application to acquire ownership or control of shares or assets of a bank or thrift or to merge with any other bank holding company. An unsatisfactory record can substantially delay or block the transaction. First Mid Bank received a satisfactory CRA rating from its regulator in its most recent CRA examination.

Consumer Laws and Regulations. In addition to the laws and regulations discussed above, First Mid Bank is also subject to certain consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth herein is not exhaustive, these laws and regulations include the Truth in Lending Act, the Truth in Savings Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Fair Credit Reporting Act, the Fair and Accurate Credit Transactions Act and the Real Estate Settlement Procedures Act, among others. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans to or marketing to or engaging in other types of transactions with such customers. Failure to comply with these laws and regulations could lead to substantial penalties, operating restrictions and reputational damage to the financial institution.

Supplemental Item – Executive Officers of the Registrant

The executive officers of the Company are elected annually by the Company's board of directors and are identified below.

Name (Age)	Position With Company
	Chairman of the Board of Directors, President and Chief Executive Officer
William S. Rowland (61)	Executive Officer
Michael L. Taylor (40)	Executive Vice President and Chief Financial Officer
John W. Hedges (60)	Executive Vice President
Laurel G. Allenbaugh (48)	Executive Vice President
Kelly A. Downs (41)	Senior Vice President
Christopher L. Slabach (46)	Senior Vice President
Eric S. McRae (43)	Vice President
Charles A. LeFebvre (39)	Vice President

William S. Rowland, age 61, has been Chairman of the Board of Directors, President and Chief Executive Officer of the Company since May 1999. He served as Executive Vice President of the Company from 1997 to 1999 and as Treasurer and Chief Financial Officer from 1989 to 1999. He also serves as Chairman of the Board of Directors and Chief Executive Officer of First Mid Bank.

Michael L. Taylor, age 40, has been the Executive Vice President and Chief Financial Officer of the Company since May 2007. He served as Vice President and Chief Financial Officer from May 2000 to May 2007. He was with AMCORE Bank in Rockford, Illinois from 1996 to 2000.

John W. Hedges, age 60, has been Executive Vice President of the Company and the President of First Mid Bank since September 1999. He was with National City Bank in Decatur, Illinois from 1976 to 1999.

Laurel G. Allenbaugh, age 48, has been Executive Vice President of Operations since April 2008. She served as Vice President of Operations from February 2000 to April 2008. She served as Controller of the Company and First Mid Bank from 1990 to February 2000 and has been President of MIDS since 1998.

Kelly A. Downs, age 41, has been Senior Vice President of Human Resources since April 2008, has served as Vice President of Human Resources from 2001 to April 2008, and has been with the Company since 1991.

Christopher L. Slabach, age 46, has been Senior Vice President of the Company since 2007 and Senior Vice President, Risk Management of First Mid Bank since 2008. He served as Vice President, Audit from 1998-2007.

Eric S. McRae, age 43, has been Vice President of the Company and Executive Vice President, Chief Credit Officer of First Mid Bank since December 2008. He served as President of the Decatur region from 2001 to December 2008.

Charles A. LeFebvre, age 39, has been Vice President of the Company and Executive Vice President of the Trust and Wealth Management Division of First Mid Bank since 2007. He was an attorney with the law firm of Thomas, Mamer & Haughey from 2001 to 2007.

ITEM 1A. RISK FACTORS

Various risks and uncertainties, some of which are difficult to predict and beyond the Company's control, could negatively impact the Company. As a financial institution, the Company is exposed to interest rate risk, liquidity risk, credit risk, operational risk, risks from economic or market conditions, and general business risks among others. Adverse experience with these or other risks could have a material impact on the Company's financial condition and results of operations, as well as the value of its common stock.

Difficult economic conditions and market disruption have adversely impacted the banking industry and financial markets generally and may significantly affect our business, financial condition, or results of operation. Our success depends, to a certain extent, upon economic and political conditions, local and national, as well as governmental monetary policies. Conditions such as inflation, recession, unemployment, changes in interest rates, money supply and other factors beyond our control may adversely affect our asset quality, deposit levels and loan demand and, therefore, our earnings.

Dramatic declines in the housing market beginning in the latter half of 2007, with falling home prices and increasing foreclosures, unemployment and underemployment, have negatively impacted the credit performance of mortgage loans and resulted in significant write-downs of asset values by some financial institutions. The resulting write-downs to assets of financial institutions have caused many financial institutions to merge with other institutions and, in some cases, to seek government assistance or bankruptcy protection.

The capital and credit markets, including the fixed income markets, have been experiencing volatility and disruption for over a year. In some cases, the markets have produced downward pressure on stock prices and credit capacity for certain issuers without regard to those issuers' financial strength.

Many lenders and institutional investors have reduced and, in some cases, ceased to provide funding to borrowers, including to other financial institutions because of concern about the stability of the financial markets and the strength of counterparties. It is difficult to predict how long these economic conditions will exist, and which of our markets, products or other businesses will ultimately be affected. Accordingly, the resulting lack of available credit, lack of confidence in the financial sector, decreased consumer confidence, increased volatility in the financial markets and reduced business activity could materially and adversely affect our business, financial condition and results of operations.

As a result of the challenges presented by economic conditions, we may face the following risks in connection with these events:

- Inability of our borrowers to make timely repayments of their loans, or decreases in value of real estate collateral securing the payment of such loans resulting in significant credit losses, which could result in increased delinquencies, foreclosures and customer bankruptcies, any of which could have a material adverse effect on our operating results.
- Increased regulation of our industry, including heightened legal standards and regulatory requirements. Compliance with such regulation will likely increase our costs and may limit our ability to pursue business opportunities.
- Further disruptions in the capital markets or other events, including actions by rating agencies and deteriorating investor expectations, may result in an inability to borrow on favorable terms or at all from other financial institutions.

Our profitability depends significantly on economic conditions in the geographic region in which we operate. A large percentage of our loans are to individuals and businesses in Illinois, consequently, any decline in the economy of this market area could have a materially adverse effect on our financial condition and results of operations.

The strength and stability of other financial institutions may adversely affect our business. The actions and commercial soundness of other financial institutions could affect our ability to engage in routine funding transactions. Financial services to institutions are interrelated as a result of clearing, counterparty or other relationships. We have exposure to different industries and counterparties, and execute transactions with various counterparties in the financial industry. Recent defaults by financial services institutions, and even rumors or questions about one or more financial services institution or the financial services industry in general, have led to market-wide liquidity problems and could lead to losses or defaults by us or by other institutions. Many of these transactions expose us to credit risk in the event of default of its counterparty or client. Any such losses could materially and adversely affect our results of operations.

Changes in interest rates may negatively affect our earnings. Changes in market interest rates and prices may adversely affect the Company's financial condition or results of operations. The Company's net interest income, its largest source of revenue, is highly dependent on achieving a positive spread between the interest earned on loans and investments and the interest paid on deposits and borrowings. Changes in interest rates could negatively impact the Company's ability to attract deposits, make loans, and achieve a positive spread resulting in compression of the net interest margin.

The Company may not have sufficient cash or access to cash to satisfy current and future financial obligations, including demands for loans and deposit withdrawals, funding operating costs, and for other corporate purposes. This type of liquidity risk arises whenever the maturities of financial instruments included in assets and liabilities differ. The Company's liquidity can be affected by a variety of factors, including general economic conditions, market disruption, operational problems affecting third parties or the Company, unfavorable pricing, competition, the Company's credit rating and regulatory restrictions. Participation in the FDIC's Temporary Liquidity Guarantee Program may not fully mitigate these risks.

If the Company were unable to borrow funds through access to capital markets, we may not be able to meet the cash flow requirements of our depositors, creditors, and borrowers, or the operating cash needed to fund corporate expansion and other corporate activities. Liquidity policies and limits are established by the board of directors, with operating limits set based upon the ratio of loans to deposits and percentage of assets funded with non-core or wholesale funding. The Company regularly monitors the overall liquidity position of First Mid Bank and the parent company to ensure that various alternative strategies exist to cover unanticipated events that could affect liquidity. The Company also establishes policies and monitors guidelines to diversify First Mid Bank's wholesale funding sources to avoid concentrations in any one market source. Wholesale funding sources include Federal funds purchased, securities sold under repurchase agreements, non-core deposits, and debt. First Mid Bank is also a member of the Federal Home Loan Bank of Chicago (FHLB), which provides funding through advances to members that are collateralized with mortgage-related assets.

We maintain a portfolio of securities that can be used as a secondary source of liquidity. There are other sources of liquidity available to us should they be needed. These sources include the sale or securitization of loans, the ability to acquire additional national market, non-core deposits, issuance of additional collateralized borrowings such as FHLB advances, the issuance of debt securities, and the issuance of preferred or common securities in public or private transactions. The Bank also can borrow from the Federal Reserve's discount window.

Starting in the middle of 2007, there has been significant turmoil and volatility in worldwide financial markets which is, at present, ongoing. These conditions have resulted in a disruption in the liquidity of financial markets, and could directly impact us to the extent we need to access capital markets to raise funds to support our business and overall liquidity position. This situation could affect the cost of such funds or our ability to raise such funds. If we were unable to access any of these funding sources when needed, we might be unable to meet customers' needs, which could adversely impact our financial condition, results of operations, cash flows, and level of regulatory-qualifying capital. We may, from time to time, consider opportunistically retiring our outstanding securities, including our trust preferred securities and common shares in privately negotiated or open market transactions for cash. For further discussion, see the "Liquidity" section.

Loan customers or other counter-parties may not be able to perform their contractual obligations resulting in a negative impact on the Company's earnings. Overall economic conditions affecting businesses and consumers, including the current difficult economic conditions and market disruptions, could impact the Company's credit losses. In addition, real estate valuations could also impact the Company's credit losses as the Company maintains \$521 million in loans secured by commercial, agricultural, and residential real estate. A significant decline in real estate values could have a negative effect on the Company's financial condition and results of operations. In addition, the Company's total loan balances by industry exceeded 25% of total risk-based capital for each of four industries as of December 31, 2008. A listing of these industries is contained in under "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations -- Loans" herein. A significant change in one of these industries such as a significant decline in agricultural crop prices, could adversely impact the Company's credit losses.

The allowance for loan losses may prove inadequate or be negatively affected by credit risk exposures. Our business depends on the creditworthiness of our customers. We periodically review the allowance for loan and lease losses for adequacy considering economic conditions and trends, collateral values and credit quality indicators, including past charge-off experience and levels of past due loans and nonperforming assets. There is no certainty that the allowance for loan losses will be adequate over time to cover credit losses in the portfolio because of unanticipated adverse changes in the economy, market conditions or events adversely affecting specific customers, industries or markets. If the credit quality of the customer base materially decreases, if the risk profile of a market, industry or group of customers changes materially, or if the allowance for loan losses is not adequate, our business, financial condition, liquidity, capital, and results of operations could be materially adversely affected.

Declines in the value of securities held in our investment portfolio may negatively affect our earnings. The value of an investment in our portfolio could decrease due to changes in market factors. The market value of certain investment

securities is volatile and future declines or other-than-temporary impairments could materially adversely affect our future earnings and regulatory capital. Continued volatility in the market value of certain of our investment securities, whether caused by changes in market perceptions of credit risk, as reflected in the expected market yield of the security, or actual defaults in the portfolio could result in significant fluctuations in the value of the securities. This could have a material adverse impact on our accumulated other comprehensive loss and shareholders' equity depending upon the direction of the fluctuations.

Furthermore, future downgrades or defaults in these securities could result in future classifications as other-than-temporarily impaired. The Company has invested in trust preferred securities issued by financial institutions and insurance companies, corporate securities of financial institutions, and stock in the Federal Home Loan Bank of Chicago and Federal Reserve Bank of Chicago. Deterioration of the financial stability of the underlying financial institutions for these investments could result in other-than-temporary impairment charges to the Company and could have a material impact on future earnings. For further discussion of the Company's investments, see Note 4 – "Investment Securities."

If our stock price declines from levels at December 31, 2008, we will evaluate our goodwill balances for impairment, and if the values of our businesses have declined, we could recognize an impairment charge for our goodwill. We performed an annual goodwill impairment assessment as of September 30, 2008. Based on our analyses, we concluded that the fair value of our reporting units exceeded the fair value of our assets and liabilities and, therefore, goodwill was not considered impaired at any of those dates. It is possible that our assumptions and conclusions regarding the valuation of our lines of business could change adversely, which could result in the recognition of impairment for our goodwill, which could have a material effect on our financial position and future results of operations.

Human error, inadequate or failed internal processes and systems, and external events may have adverse effects on the Company. Operational risk includes compliance or legal risk, which is the risk of loss from violations of, or noncompliance with, laws, rules, regulations, prescribed practices, or ethical standards. Operational risk also encompasses transaction risk, which includes losses from fraud, error, the inability to deliver products or services, and loss or theft of information. Losses resulting from operational risk could take the form of explicit charges, increased operational costs, harm to our reputation or forgone opportunities. Any of these could potentially have a material adverse effect on our financial condition and results of operations.

The Company is exposed to various business risks that could have a negative effect on the financial performance of the Company. These risks include: changes in customer behavior, changes in competition, new litigation or changes to existing litigation, claims and assessments, environmental liabilities, real or threatened acts of war or terrorist activity, adverse weather, changes in accounting standards, legislative or regulatory changes, taxing authority interpretations, and an inability on the Company's part to retain and attract skilled employees.

In addition to these risks identified by the Company, investments in the Company's common stock involve risk. The market price of the Company's common stock may fluctuate significantly in response to a number of factors including: volatility of stock market prices and volumes, rumors or erroneous information, changes in market valuations of similar companies, changes in securities analysts' estimates of financial performance, and variations in quarterly or annual operating results.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company or First Mid Bank own all of the following properties except those specifically identified as being leased.

First Mid Bank

Mattoon. First Mid Bank's main office is located at 1515 Charleston Avenue, Mattoon, Illinois. The office building consists of a one-story structure with occupied basement, which was opened in 1965 with approximately 36,000 square feet of office space, four walk-up teller stations, and four sit-down teller stations. Adjacent to this building is a parking lot with parking for approximately seventy cars. A drive-up facility with nine drive-up lanes and a drive-up automated teller machine ("ATM") is located across the street from First Mid Bank's main office.

First Mid Bank has a facility at 333 Broadway Avenue East, Mattoon, Illinois. The one-story office building contains approximately 7,600 square feet of office space. The main floor provides space for five teller windows, two private offices, a safe deposit vault and four drive-up lanes. There is adequate parking located adjacent to the building. A drive-up ATM is located adjacent to the building.

First Mid Bank leases a facility at 1504-A Lakeland Boulevard, Mattoon, Illinois that provides space for three tellers, two drive-up lanes and a drive-up ATM.

First Mid Bank owns a facility located at 1520 Charleston Avenue, Mattoon, Illinois, which is used as the corporate headquarters of the Company and is used by MIDS for its data processing and back room operations for the Company and First Mid Bank. The office building consists of a two-story structure with an occupied basement that has approximately 20,000 square feet of office space.

The Company owns a facility at 1500 Wabash Avenue, Mattoon, Illinois, which is used by the loan and deposit services departments of First Mid Bank. The office building consists of a two-story structure with a basement that has approximately 11,200 square feet of office space.

First Mid Bank leases a facility located at 14th and Charleston, Mattoon, Illinois. The office space, comprised of approximately 2,100 square feet, contains five offices, one conference rooms, a file room and a waiting/reception area. Adequate parking is available to serve customers.

There are four additional ATMs located in Mattoon. They are located in the Administration building of Lake Land College, in the main lobby of Sarah Bush Lincoln Health Center, at R.R. Donnelley & Sons Co. on North Route 45 and County Market at 2000 Western Avenue.

Sullivan. First Mid Bank operates one location in Sullivan, Illinois. The main office is located at 200 South Hamilton Street, Sullivan, Illinois. Its office building is a one-story structure containing approximately 11,400 square feet of office space with five teller windows, six private offices and four drive-up lanes. Adequate customer parking is available on two sides of the main office building. There is also a walk-up ATM located in the Sullivan Citgo Station at 105 West Jackson.

Neoga. First Mid Bank's office in Neoga, Illinois, is located at 102 East Sixth Street, Neoga, Illinois. The building consists of a one-story structure containing approximately 4,000 square feet of office space. The main office building provides space for four tellers in the lobby of the building, two drive-up tellers, four private offices, two night depositories, and an ATM. Adequate customer parking is available on three sides of the main office building.

Tuscola. First Mid Bank operates an office in Tuscola, Illinois, which is located at 410 South Main Street. The all brick building consists of a one-story structure with approximately 4,000 square feet of office space. This main office building provides for four lobby tellers, two drive-up tellers, four private offices, a conference room, four drive-through lanes, including one with a drive-up ATM and one with a drive-up night depository. Adequate customer parking is available outside the main entrance.

Charleston. The main office, acquired in March 1997, is located at 500 West Lincoln Avenue, Charleston, Illinois. This one-story facility contains approximately 8,400 square feet with five teller stations, eight private offices and four drive-up lanes.

A second facility is located at 701 Sixth Street, Charleston, Illinois. It is a one-story facility with an attached two-bay drive-up structure and consists of approximately 5,500 square feet of office space. Adequate parking is available to serve its customers. The office space is comprised of three teller stations, three private offices, storage area, and a night depository. Approximately 2,200 square feet of this building is rented out to non-affiliated companies.

The third facility consists of approximately 400 square feet of leased space at the Martin Luther King Student Union on the Eastern Illinois University campus. The facility has two walk-up teller stations and two sit-down teller/CSR stations.

Seven ATMs are located in Charleston. One drive-up ATM is located in the parking lot of the facility at 500 West Lincoln Avenue, one in the parking lot of Save-A-Lot at 1400 East Lincoln Avenue, and one drive-up ATM is located in the parking lot of the Sixth Street facility. The fourth is an off-site walk-up ATM located in the Student Union at Eastern Illinois University and the fifth is a walk-up ATM located in Lantz Arena at Eastern Illinois University. The sixth ATM is a drive-up unit located on the Eastern Illinois University campus in a parking lot at the corner of Ninth Street and Roosevelt and the seventh is a drive-up unit located on the Eastern Illinois University campus in a parking lot at the corner of Fourth Street and Roosevelt.

Champaign. First Mid Bank leases a facility at 2229 South Neil Street, Champaign, Illinois. The office space, comprised of approximately 3,496 square feet, contains six lobby teller windows, two drive-up lanes, one drive-up ATM, a night depository, four private offices, and a conference room. Adequate customer parking is available to serve customers.

Urbana. First Mid Bank owns a facility located at 601 South Vine Street, Urbana, Illinois. Its office building consists of a one-story structure and contains approximately 3,600 square feet. The office building provides space for three tellers, two private offices and two drive-up lanes. An ATM machine is located in front of the building. An adequate customer parking lot is located on the south side of the building.

Effingham. First Mid Bank operates a facility at 902 North Keller Drive, Effingham, Illinois. The building is a two-story structure with approximately 4,000 square feet of office space. This office space consists of four teller stations, three drive-up teller lanes, five private offices and a night depository. Adequate parking is available to customers in front of the facility.

First Mid Bank also owns property at 900 North Keller Drive, Effingham, Illinois that provides additional customer parking along with a drive-up ATM.

Altamont. First Mid Bank has a banking facility located at 101 West Washington Street, Altamont, Illinois. This building is a one-story structure that has approximately 4,300 square feet of office space. The office space consists of nine teller windows, three drive-up teller lanes (one of which facilitates an ATM), seven private offices, one conference room and a night depository. Adequate parking is available on three sides of the building.

Arcola. First Mid Bank leases a facility at 324 South Chestnut Street, Arcola, Illinois. This building is a one-story structure with approximately 1,140 square feet of office space. This office space consists of two lobby teller stations, one loan station, two drive-up teller lanes, one private office and a night depository. A drive-up ATM lane is available adjacent to the teller lanes. Adequate parking is available to customers in front of the facility. There are also two additional ATMs located at the Arcola Citgo Station on Route 133 at Interstate Five and the Arthur Citgo Station at 209 North Vine.

Monticello. First Mid Bank has two offices in Monticello. The main facility is located on the northeast corner of the historic town square at 100 West Washington Street. This building is a two-story structure that has 8,000 square feet of office space consisting of five teller stations, seven private offices, and a night depository. The second floor is furnished and the basement is used for storage. Adequate parking is available to customers in back of the facility.

A second facility is located at 219 West Center Street, Monticello, Illinois. It is a one-story facility with two lobby teller stations and an attached two-bay drive-up structure with a drive-up ATM and a night depository. Adequate parking is available to serve its customers.

Taylorville. First Mid Bank has a banking facility located at 200 North Main Street, Taylorville, Illinois. This one-story building has approximately 3,700 square feet with five teller stations, three private offices, one drive-up lane, and a finished basement. A drive-up ATM is located in the parking lot and adequate customer parking is available adjacent to the building.

Decatur. First Mid Bank leases a facility at 111 E. Main Street, Decatur, Illinois. The office space comprised of 4,340 square feet contains three lobby teller windows, two drive-up lanes, a night depository, three private offices, safe deposit and loan vaults, and a conference room. Customer parking is available adjacent to the building.

Highland. First Mid Bank owns a facility located at 12616 State Route 143, Highland, Illinois. The building is a two-story structure with approximately 6,720 square feet of office space, a portion of which is leased to an unaffiliated business. This office space consists of a customer service area and teller windows, three drive-up teller lanes, an

ATM and four private offices. Adequate parking is available to serve customers.

First Mid Bank leases a facility located at 1301 Broadway, Highland, Illinois. The office space, comprised of 1300 square feet, contains three lobby teller windows, two drive-up lanes and one drive-up ATM, a night depository, two private offices, safe deposit and loan vaults and a conference room. Adequate parking is available to serve customers.

St. Jacob. First Mid Bank rents property at 705 N. Douglas Street, St. Jacob, Illinois where a drive-up ATM is located.

Pocahontas. First Mid Bank owns a facility located at 103 Park Street, Pocahontas, Illinois. The building is a one-story brick structure with approximately 3,360 square feet of office space. This office space consists of a customer processing room, three private offices and three bank vaults. Adequate parking is available to serve customers.

First Mid Bank also has an ATM at 4 O'Fallon Street in Powhatten Restaurant.

Maryville. First Mid leases a facility located at 2930 North Center Street, Maryville, Illinois. The office space, comprised of approximately 6,684 square feet, contains four lobby teller windows, including one sit-down teller, two drive-up lanes, one drive-up ATM, a night depository, three private offices, a vault, and a conference room. Adequate customer parking is available to serve customers.

Mansfield. First Mid Bank owns a facility at 1 Jefferson, Mansfield, Illinois. The building is a one-story structure with approximately 3,695 square feet of office space which contains a lobby with teller windows, one drive-up lane, three private offices, a vault, a conference room and a basement used for storage. Customer parking is available adjacent to the building.

Mahomet. First Mid Bank owns a facility located at 504 E. Oak Street, Mahomet, Illinois. The building is a one-story structure with approximately 3,045 square feet of office space which contains a lobby with teller windows, a drive-up lane, an ATM, two private offices, a vault, a conference room and a basement used for storage. Adequate customer parking is available to serve customers.

Weldon. First Mid Bank owns a facility located at Oak and Maple, Weldon, Illinois. The building is a two-story structure with approximately 5,964 square feet of office space which contains a lobby with teller windows, a drive-up lane, four private offices, two vaults, a conference room and a basement used for storage. Offices on the second floor have been leased to a separate entity. Adequate customer parking is available to serve customers.

On September 29, 2007, the Company closed its banking facilities located at 435 South Hamilton, Sullivan, Illinois in the IGA and at 220 North Highway Avenue, DeLand, Illinois. The customers and operations of both of these facilities were moved to other facilities in Sullivan and Monticello, Illinois. The closing of these facilities did not have a material impact on the Company's other operations or on its financial reporting and disclosures.

Checkley

Mattoon. Checkley leases a facility located at 100 Lerna South, Mattoon, Illinois. The office space, comprised of approximately 8,829 square feet, contains ten offices, two conference rooms, a file room and an open work area that can accommodate nine workstations. Adequate parking is available to serve customers.

ITEM 3. LEGAL PROCEEDINGS

Since First Mid Bank acts as a depository of funds, it is named from time to time as a defendant in lawsuits (such as garnishment proceedings) involving claims to the ownership of funds in particular accounts. Management believes that all such litigation as well as other pending legal proceedings, in which the Company is involved, constitute ordinary routine litigation incidental to the business of the Company and that such litigation will not materially adversely affect the Company's consolidated financial condition or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER OF PURCHASES OF EQUITY SECURITIES

The Company's common stock was held by approximately 633 shareholders of record as of December 31, 2008 and is included for quotation on the over-the-counter electronic bulletin board.

The following table shows the high and low bid prices per share of the Company's common stock for the indicated periods. These quotations represent inter-dealer prices without retail mark-ups, mark-downs or commissions and may not necessarily represent actual transactions.

Quarter	High	Low
2008		
4th	\$26.00	\$13.00
3rd	\$28.50	\$24.45
2nd	\$27.75	\$24.90
1st	\$26.15	\$23.40
2007		
4th	\$27.00	\$25.75
3rd	\$27.25	\$25.70
2nd	\$27.80	\$25.93
1st	\$27.95	\$27.17

The following table sets forth the cash dividends per share on the Company's common stock for the last two years.

Date Declared	Date Paid	Dividend Per Share
12-16-2008	1-05-2009	\$.190
4-30-2008	6-16-2008	\$.190
12-11-2007	1-07-2008	\$.190
4-24-2007	6-15-2007	\$.187

On June 29, 2007, the Company effected a three-for-two stock split in the form of a 50% stock dividend. Par value remained at \$4 per share. All share and per share amounts have been restated for years prior to 2007 to give retroactive recognition to the stock split.

The Company's shareholders are entitled to receive such dividends as are declared by the Board of Directors, which considers payment of dividends semi-annually. The ability of the Company to pay dividends, as well as fund its operations, is dependent upon receipt of dividends from First Mid Bank. Regulatory authorities limit the amount of dividends that can be paid by First Mid Bank without prior approval from such authorities. For further discussion of First Mid Bank's dividend restrictions, see Item 1 – "Business" – "First Mid Bank" – "Dividends" and Note 17 – "Dividend

Restrictions” herein. The Board of Directors of the Company declared cash dividends semi-annually during the two years ended December 31, 2008.

The following table summarizes share repurchase activity for the fourth quarter of 2008:

ISSUER PURCHASES OF EQUITY SECURITIES				
Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs at End of Period
October 1, 2008 – October 31, 2008	0	\$0.00	0	\$649,000
November 1, 2008 – November 30, 2008	0	\$0.00	0	\$649,000
December 1, 2008 – December 31, 2008	65,676	\$24.51	65,676	\$4,039,000
Total	65,676	\$24.51	65,676	\$4,039,000

Since August 5, 1998, the Board of Directors has approved repurchase programs pursuant to which the Company may repurchase a total of approximately \$54.2 million of the Company's common stock. The repurchase programs approved by the Board of Directors are as follows:

- On August 5, 1998, repurchases of up to 3%, or \$2 million, of the Company's common stock.
- In March 2000, repurchases up to an additional 5%, or \$4.2 million of the Company's common stock.
- In September 2001, repurchases of \$3 million of additional shares of the Company's common stock.
- In August 2002, repurchases of \$5 million of additional shares of the Company's common stock.
- In September 2003, repurchases of \$10 million of additional shares of the Company's common stock.
- On April 27, 2004, repurchases of \$5 million of additional shares of the Company's common stock.
- On August 23, 2005, repurchases of \$5 million of additional shares of the Company's common stock.
- On August 22, 2006, repurchases of \$5 million of additional shares of the Company's common stock.
- On February 27, 2007, repurchases of \$5 million of additional shares of the Company's common stock.
- On November 13, 2007, repurchases of \$5 million of additional shares of the Company's common stock.
- On December 16, 2008, repurchases of \$5 million of additional shares of the Company's common stock.

ITEM 6. SELECTED FINANCIAL DATA

The following sets forth a five-year comparison of selected financial data (dollars in thousands, except per share data).

	2008	2007	2006	2005	2004
Summary of Operations					
Interest income	\$ 57,066	\$ 59,931	\$ 55,556	\$ 44,580	\$ 40,024
Interest expense	21,344	28,429	24,712	15,687	11,644
Net interest income	35,722	31,502	30,844	28,893	28,380
Provision for loan losses	3,559	862	760	1,091	588
Other income	15,264	14,661	13,380	12,518	11,639
Other expense	31,460	30,055	28,423	25,385	25,139
Income before income taxes	15,967	15,246	15,041	14,935	14,292
Income tax expense	5,443	5,087	5,032	5,128	4,541
Net income	\$ 10,524	\$ 10,159	\$ 10,009	\$ 9,807	\$ 9,751
Per Common Share Data (1)					
Basic earnings per share	\$ 1.69	\$ 1.60	\$ 1.54	\$ 1.48	\$ 1.44
Diluted earnings per share	1.67	1.57	1.51	1.44	1.42
Dividends per common share	.38	.38	.35	.33	.30
Book value per common share	13.50	12.82	11.78	10.98	10.35
Capital Ratios					
Total capital to risk-weighted assets	11.99%	11.13%	10.91%	11.87%	11.71%
Tier 1 capital to risk-weighted assets	11.02%	10.32%	10.10%	11.14%	10.94%
Tier 1 capital to average assets	8.41%	7.89%	7.56%	8.55%	7.99%
Financial Ratios					
Net interest margin	3.73%	3.43%	3.51%	3.70%	3.75%
Return on average assets	1.03%	1.03%	1.07%	1.18%	1.20%
Return on average common equity	12.87%	13.06%	13.31%	13.64%	14.24%
Dividend payout ratio	22.49%	23.75%	22.51%	22.55%	20.92%
Average equity to average assets	8.00%	7.90%	8.01%	8.64%	8.44%
Allowance for loan losses as a percent of total loans	1.02%	0.82%	0.81%	0.73%	0.77%
Year End Balances					
Total assets	\$ 1,049,700	\$ 1,016,338	\$ 980,559	\$ 850,573	\$ 826,728
Net loans	734,351	742,043	717,692	631,707	590,539
Total deposits	806,354	770,583	770,595	649,069	650,240
Total equity	82,778	80,452	75,786	72,326	69,154
Average Balances					
Total assets	\$ 1,022,734	\$ 985,230	\$ 938,784	\$ 832,752	\$ 811,061
Net loans	733,681	722,672	686,069	606,064	568,271
Total deposits	795,786	771,561	737,344	650,116	638,445
Total equity	81,793	77,787	75,174	71,911	68,459

(1) All share and per share data have been restated to reflect the 3-for-2 stock splits effective June 29, 2007 and July 16, 2004.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis is intended to provide a better understanding of the consolidated financial condition and results of operations of the Company and its subsidiaries for the years ended December 31, 2008, 2007 and 2006. This discussion and analysis should be read in conjunction with the consolidated financial statements, related notes and selected financial data appearing elsewhere in this report.

Forward-Looking Statements

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, such as discussions of the Company's pricing and fee trends, credit quality and outlook, liquidity, new business results, expansion plans, anticipated expenses and planned schedules. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and is including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of the Company, are identified by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project," or similar expressions. Actual results can differ materially from the results indicated by these statements because the realization of those results is subject to many uncertainties including: changes in interest rates, general economic conditions and those in the Company's market area, legislative/regulatory changes, monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board, the quality or composition of the loan or investment portfolios and the valuation of the investment portfolio, demand for loan products, deposit flows, competition, demand for financial services in the Company's market area and accounting principles, policies and guidelines. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Further information concerning the Company and its business, including additional factors that could materially affect the Company's financial results, is included in Item 1A of this Annual Report on Form 10-K captioned "Risk Factors" and elsewhere in the filing and the Company's other filings with the SEC. Furthermore, forward-looking statements speak only as of the date they are made. Except as required under the federal securities laws or the rules and regulations of the SEC, we do not undertake any obligation to update or review any forward-looking information, whether as a result of new information, future events or otherwise.

For the Years Ended December 31, 2008, 2007 and 2006

Overview

This overview of management's discussion and analysis highlights selected information in this document and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources, and critical accounting estimates, you should carefully read this entire document. These have an impact on the Company's financial condition and results of operations.

Net income was \$10.52 million, \$10.16 million, and \$10.01 million and diluted earnings per share were \$1.67, \$1.57, and \$1.51 for the years ended December 31, 2008, 2007, and 2006, respectively. The increase in net income in 2008 was primarily the result of higher net interest income and greater non-interest income. The increase in earnings per share in 2008 was the result of improved net income and a decrease in the number of shares outstanding due to share repurchases made through the Company's stock buy-back program. During 2008, the Company acquired 262,877 shares for a total investment of \$6,784,000. The following table shows the Company's annualized performance ratios for the years ended December 31, 2008, 2007 and 2006:

	2008	2007	2006
Return on average assets	1.03%	1.03%	1.07%
Return on average equity	12.87%	13.06%	13.31%
Average equity to average assets	8.00%	7.90%	8.01%

Total assets at December 31, 2008, 2007, and 2006 were \$1,049.7 million, \$1,016.3 million, and \$980.6 million, respectively. The increase in net assets during 2008 was primarily due to an increase in interest-bearing deposits held by the Company, offset by decreases in available-for-sale securities that were called or matured and were not immediately replaced, and net loans. The increase in net assets during 2007 was primarily the result of increases in loan balances. Net loan balances decreased to \$733.8 million at December 31, 2008, from \$740.1 million at December 31, 2007 and compared to \$715.5 million at December 31, 2006. The decrease in 2008 of \$6.3 million or 0.9% was due to a decline in commercial operating loans. Total deposit balances increased to \$806.4 million at December 31, 2008, from \$770.6 million at December 31, 2007 and 2006. The increase in 2008 was primarily due to increased balances in interest bearing deposits and savings accounts.

Net interest margin, defined as net interest income divided by average interest-earning assets, was 3.73% for 2008, 3.43% for 2007 and 3.51% for 2006. The increase in interest margin during 2008 was the result of greater decrease in borrowing and deposit rates compared to the decrease in interest-earning asset rates. The decrease in net interest margin during 2007 was attributable to a greater increase in borrowing and deposit rates compared to the increase in interest-earning asset rates. This was primarily due to the inversion of the interest rate yield curve where rates on short-term financial instruments have increased faster than rates on longer-term instruments.

Net interest income increased from \$30.8 million in 2006 to \$31.5 million in 2007 and to \$35.7 million in 2008. This increase was the result of management's business development efforts that led to increasing levels of average interest-earning assets of \$877.1 million in 2006, to \$919.7 million in 2007 and to \$958.1 million in 2008. The ability of the Company to continue to grow net interest income is largely dependent on management's ability to succeed in its overall business development efforts. Management expects these efforts to continue but does not intend to compromise credit quality and prudent management of the maturities of interest-earning assets and interest-paying liabilities in order to achieve growth.

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Non-interest income increased to \$15.3 million in 2008 compared to \$14.7 million in 2007 and \$13.4 million in 2006. The primary reasons for the increase of \$.6 million or 4.1% during 2008 were increases in ATM and debit card transaction fees during 2008 compared to 2007, and approximately \$291,000 in proceeds on life insurance the Company maintained on former executive and director, Daniel E. Marvin, Jr., who died in April of 2008. The primary reasons for the increase of \$1.3 million or 9.6% during 2007 were increases in trust revenues, insurance commissions and ATM and debit card transaction fees during 2007 compared to 2006.

Non-interest expenses increased \$1.4 million, to \$31.5 million in 2008 compared to \$30.1 million in 2007 and \$28.4 million in 2006. The primary factors in the increase during 2008 were additional salaries and benefits expense as a result of merit increases for continuing employees, increases in loan collection expenses and the write down of the DeLand property of \$132,000 during the first quarter of 2008. The primary factor in the increase during 2007 was additional salaries and benefits expense as a result of merit increases for continuing employees, additional employees from the Mansfield acquisition for the full year of 2007 and increases in legal and other professional expenses resulting from the new disclosure requirements for the proxy statement for the 2007 annual meeting of stockholders.

Following is a summary of the factors that contributed to the changes in net income (in thousands):

	2008 vs 2007	2007 vs 2006
Net interest income	\$4,220	\$ 658
Provision for loan losses	(2,697)	(102)
Other income, including securities transactions	603	1,281
Other expenses	(1,405)	(1,632)
Income taxes	(356)	(55)
Increase in net income	\$ 365	\$ 150

Credit quality is an area of importance to the Company. Year-end total nonperforming loans were \$7.3 million at December 31, 2008 compared to \$7.5 million at December 31, 2007 and \$3.7 million at December 31, 2006. The decline in 2008 occurred as a result of the bank taking possession of real estate collateral and moving the balances to other real estate owned offset by loans that became nonperforming during the year. Other real estate owned balances totaled \$2.4 million at December 31, 2008 compared to \$.5 million at December 31, 2007. The Company's provision for loan losses was \$3,559,000 for 2008 compared to \$862,000 for 2007. At December 31, 2008, the composition of the loan portfolio remained similar to 2007. Loans secured by both commercial and residential real estate comprised 70% and 69% of the loan portfolio as of December 31, 2008 and 2007, respectively.

The Company's capital position remains strong and the Company has consistently maintained regulatory capital ratios above the "well-capitalized" standards. The Company's Tier 1 capital ratio to risk weighted assets ratio at December 31, 2008, 2007, and 2006 was 11.02%, 10.32%, and 10.10%, respectively. The Company's total capital to risk weighted assets ratio at December 31, 2008, 2007, and 2006 was 11.99%, 11.13%, and 10.91%, respectively. The increase in 2008 was primarily the result of an increase in retained earnings due to the Company's increase in net income and changes in federal banking and thrift regulatory agencies rules that permit banking organizations to reduce the amount of goodwill that must be deducted from tier 1 capital by any associated deferred tax liability. The increase in 2007 was primarily the result of an increase in retained earnings due to the Company's increase in net income.

The Company's liquidity position remains sufficient to fund operations and meet the requirements of borrowers, depositors, and creditors. The Company maintains various sources of liquidity to fund its cash needs. See "Liquidity" herein for a full listing of its sources and anticipated significant contractual obligations. Additionally, on February 11, 2009, the Company raised \$22,635,000 by selling its Series B 9% Non-Cumulative Perpetual Convertible Preferred Stock.

The Company enters into financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include lines of credit, letters of credit and other commitments to extend credit. The total outstanding commitments at December 31, 2008, 2007 and 2006 were \$152.9 million, \$152.7 million and \$131.9 million, respectively. See Note 12 – “Disclosure of Fair Values of Financial Instruments” and Note 18 – “Commitments and Contingent Liabilities” herein for further information.

Critical Accounting Policies and Use of Significant Estimates

The Company has established various accounting policies that govern the application of U.S. generally accepted accounting principles in the preparation of the Company’s financial statements. The significant accounting policies of the Company are described in the footnotes to the consolidated financial statements. Certain accounting policies involve significant judgments and assumptions by management that have a material impact on the carrying value of certain assets and liabilities; management considers such accounting policies to be critical accounting policies. The judgments and assumptions used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and assumptions made by management, actual results could differ from these judgments and assumptions, which could have a material impact on the carrying values of assets and liabilities and the results of operations of the Company.

Allowance for Loan Losses. The Company believes the allowance for loan losses is the critical accounting policy that requires the most significant judgments and assumptions used in the preparation of its consolidated financial statements. We determine probable incurred losses inherent in our loan portfolio and establish an allowance for those losses by considering factors including historical loss rates, expected cash flows and estimated collateral values. In assessing these factors, we use organizational history and experience with credit decisions and related outcomes. The allowance for loan losses represents our best estimate of losses inherent in the existing loan portfolio. The allowance for loan losses is increased by the provision for loan losses charged to expense and reduced by loans charged off, net of recoveries. We evaluate our allowance for loan losses quarterly. If our underlying assumptions later prove to be inaccurate based on subsequent loss evaluations, the allowance for loan losses is adjusted.

We estimate the appropriate level of allowance for loan losses by separately evaluating impaired and nonimpaired loans. A specific allowance is assigned to an impaired loan when expected cash flows or collateral do not justify the carrying amount of the loan. The methodology used to assign an allowance to a nonimpaired loan is more subjective. Generally, the allowance assigned to nonimpaired loans is determined by applying historical loss rates to existing loans with similar risk characteristics, adjusted for qualitative factors including the volume and severity of identified classified loans, changes in economic conditions, changes in credit policies or underwriting standards, and changes in the level of credit risk associated with specific industries and markets. Because the economic and business climate in any given industry or market, and its impact on any given borrower, can change rapidly, the risk profile of the loan portfolio is continually assessed and adjusted when appropriate. Notwithstanding these procedures, there still exists the possibility that our assessment could prove to be significantly incorrect and that an immediate adjustment to the allowance for loan losses would be required.

Other Real Estate Owned. Other real estate owned acquired through loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. The adjustment at the time of foreclosure is recorded through the allowance for loan losses. Due to the subjective nature of establishing the fair value when the asset is acquired, the actual fair value of the other real estate owned or foreclosed asset could differ from the original estimate. If it is determined that fair value declines subsequent to foreclosure, a valuation allowance is recorded through noninterest expense. Operating costs associated with the assets after acquisition are also recorded as noninterest expense. Gains and losses on the disposition of other real estate owned and foreclosed assets are netted and posted to other noninterest expense.

Investment in Debt and Equity Securities. We classify our investments in debt and equity securities as either held-to-maturity or available-for-sale in accordance with Statement of Financial Accounting Standards No. 115, Accounting for Certain Investments in Debt and Equity Securities. Securities classified as held-to-maturity are recorded at cost or amortized cost. Available-for-sale securities are carried at fair value. Fair value calculations are based on quoted market prices when such prices are available. If quoted market prices are not available, estimates of fair value are computed using a variety of techniques, including extrapolation from the quoted prices of similar instruments or recent trades for thinly traded securities, fundamental analysis, or through obtaining purchase quotes. Due to the subjective nature of the valuation process, it is possible that the actual fair values of these investments could differ from the estimated amounts, thereby affecting our financial position, results of operations and cash flows. If the estimated value of investments is less than the cost or amortized cost, we evaluate whether an event or change in circumstances has occurred that may have a significant adverse effect on the fair value of the investment. If such an event or change has occurred and we determine that the impairment is other-than-temporary, we expense the impairment of the investment in the period in which the event or change occurred.

Deferred Income Tax Assets/Liabilities. Our net deferred income tax asset arises from differences in the dates that items of income and expense enter into our reported income and taxable income. Deferred tax assets and liabilities are established for these items as they arise. From an accounting standpoint, deferred tax assets are reviewed to determine if they are realizable based on the historical level of our taxable income, estimates of our future taxable income and the reversals of deferred tax liabilities. In most cases, the realization of the deferred tax asset is based on our future profitability. If we were to experience net operating losses for tax purposes in a future period, the realization of our

deferred tax assets would be evaluated for a potential valuation reserve.

Additionally, the Company reviews its uncertain tax positions annually under FASB Interpretation 48, Accounting for Uncertainty in Income Taxes. An uncertain tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount actually recognized is the largest amount of tax benefit that is greater than 50% likely to be recognized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. A significant amount of judgment is applied to determine both whether the tax position meets the "more likely than not" test as well as to determine the largest amount of tax benefit that is greater than 50% likely to be recognized. Differences between the position taken by management and that of taxing authorities could result in a reduction of a tax benefit or increase to tax liability, which could adversely affect future income tax expense.

Impairment of Goodwill and Intangible Assets. Core deposit and customer relationships, which are intangible assets with a finite life, are recorded on our balance sheets. These intangible assets were capitalized as a result of past acquisitions and are being amortized over their estimated useful lives of up to 15 years. Core deposit intangible assets, with finite lives will be tested for impairment when changes in events or circumstances indicate that its carrying amount may not be recoverable. Core deposit intangible assets were tested for impairment during 2008 and 2007, as part of the goodwill impairment test and no impairment was deemed necessary.

As a result of our acquisition activity, goodwill, an intangible asset with an indefinite life, was reflected on our balance sheet in prior periods. Goodwill is evaluated for impairment annually, unless there are factors present that indicates a potential impairment, in which case, the goodwill impairment test is performed more frequently than annually.

Fair Value Measurements. The fair value of a financial instrument is defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The Company estimates the fair value of a financial instrument using a variety of valuation methods. Where financial instruments are actively traded and have quoted market prices, quoted market prices are used for fair value. When the financial instruments are not actively traded, other observable market inputs, such as quoted prices of securities with similar characteristics, may be used, if available, to determine fair value. When observable market prices do not exist, the Company estimates fair value. The Company's valuation methods consider factors such as liquidity and concentration concerns. Other factors such as model assumptions, market dislocations, and unexpected correlations can affect estimates of fair value. Imprecision in estimating these factors can impact the amount of revenue or loss recorded.

FASB Statement No. 157, Fair Value Measurements, establishes a framework for measuring the fair value of financial instruments that considers the attributes specific to particular assets or liabilities and establishes a three-level hierarchy for determining fair value based on the transparency of inputs to each valuation as of the fair value measurement date. The three levels are defined as follows:

- Ø Level 1 — quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Ø Level 2 — inputs include quoted prices for similar assets and liabilities in active markets, quoted prices of identical or similar assets or liabilities in markets that are not active, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Ø Level 3 — inputs that are unobservable and significant to the fair value measurement.

At the end of each quarter, the Company assesses the valuation hierarchy for each asset or liability measured. From time to time, assets or liabilities may be transferred within hierarchy levels due to changes in availability of observable market inputs to measure fair value at the measurement date. Transfers into or out of hierarchy levels are based upon the fair value at the beginning of the reporting period. A more detailed description of the fair values measured at each level of the fair value hierarchy can be found in Note 12 – “Disclosures of Fair Values of Financial Instruments.”

Mergers and Acquisitions

On May 1, 2006, the Company completed the acquisition, for \$24 million in cash, of all of the outstanding common stock of Mansfield and its wholly-owned subsidiary, Peoples, with locations in Mansfield, Mahomet and Weldon, Illinois, in order to expand its market presence in this area. The Company financed the purchase price through a dividend of \$5 million from First Mid Bank, an issuance of \$10 million of trust preferred securities through Trust II and a \$9.5 million draw on the Company’s line of credit with The Northern Trust Company. Following the completion of the acquisition during the third quarter of 2006, Mansfield merged with and into Peoples and Peoples merged with and into First Mid Bank. Following the completion of these mergers, Mansfield and Peoples ceased to exist and Peoples’ operations were merged into First Mid Bank’s.

The transaction has been accounted for as a purchase, and the results of operations of Mansfield and Peoples since the acquisition date have been included in the consolidated financial statements. See Note 20 – “Acquisitions” herein for further information.

Properties

On September 29, 2007, the Company closed its facilities located at 435 South Hamilton, Sullivan, Illinois in the IGA and at 220 North Highway Avenue, DeLand, Illinois. The customers and operations of both of these facilities were moved to other facilities in Sullivan and Monticello, Illinois. These actions did not have a material impact on the Company’s consolidated financial statements.

During the first quarter of 2008, the Company obtained an independent appraisal of the DeLand property in anticipation of possibly donating or selling this property. Subsequently, the Company adjusted its carrying value of the property to the appraised value which resulted in a loss of \$132,000 in the consolidated financial statements.

Federal Deposit Insurance Corporation Insurance Coverage

As with all banks insured by the FDIC, the Company’s depositors are protected against the loss of their insured deposits by the FDIC. The FDIC recently made two changes to the rules that broadened the FDIC insurance. On October 3, 2008, the FDIC temporarily increased basic FDIC insurance coverage from \$100,000 to \$250,000 per depositor until December 31, 2009. In addition, on October 14, 2008 the FDIC instituted a Temporary Liquidity Guaranty Program (“TLGP”) which provides full deposit coverage for non-interest bearing transaction deposit accounts, regardless of dollar amount. The FDIC defines a “non-interest bearing transaction account” as a transaction account on

which the insured depository institution pays no interest and does not reserve the right to require advance notice of intended withdrawals. This coverage is over and above the \$250,000 in coverage otherwise provided to a customer.

The Company opted into the TLGP. The additional cost of this program, assessed on a quarterly basis, is a 10 basis point annualized surcharge (2.5 basis points quarterly) on balances in non-interest bearing transactions accounts that exceed \$250,000. The Company does not believe this amount will have a material effect on its consolidated financial statements.

Results of Operations

Net Interest Income

The largest source of operating revenue for the Company is net interest income. Net interest income represents the difference between total interest income earned on earning assets and total interest expense paid on interest-bearing liabilities. The amount of interest income is dependent upon many factors, including the volume and mix of earning assets, the general level of interest rates and the dynamics of changes in interest rates. The cost of funds necessary to support earning assets varies with the volume and mix of interest-bearing liabilities and the rates paid to attract and retain such funds.

The Company's average balances, interest income and expense and rates earned or paid for major balance sheet categories are set forth in the following table (dollars in thousands):

	Year Ended December 31, 2008			Year Ended December 31, 2007			Year Ended December 31, 2006		
	Average Balance	Average Interest	Average Rate	Average Balance	Average Interest	Average Rate	Average Balance	Average Interest	Average Rate
ASSETS									
Interest-bearing deposits	\$ 26,697	\$ 423	1.59%	\$ 265	\$ 13	5.02%	\$ 628	\$ 31	4.94%
Federal funds sold	19,266	336	1.75%	4,012	201	5.00%	5,517	276	5.00%
Investment securities									
Taxable	151,752	7,725	5.09%	169,425	8,448	4.99%	161,351	7,490	4.64%
Tax-exempt (1)	20,312	834	4.11%	17,242	712	4.13%	17,900	771	4.31%
Loans (2) (3)	740,083	47,748	6.45%	728,790	50,557	6.94%	691,726	46,988	6.79%
Total earning assets	958,110	57,066	5.96%	919,734	59,931	6.52%	877,122	55,556	6.33%
Cash and due from banks	19,433			19,361			18,974		
Premises and equipment	15,160			15,888			16,082		
Other assets	36,433			36,365			32,263		
Allowance for loan losses	(6,402)			(6,118)			(5,657)		
Total assets	\$1,022,734			\$985,230			\$938,784		
LIABILITIES AND STOCKHOLDERS' EQUITY									
Deposits:									
Demand deposits, interest-bearing	\$288,057	3,635	1.26%	\$271,117	6,459	2.38%	\$246,035	5,319	2.16%
Savings deposits	74,236	680	0.92%	60,654	349	0.58%	62,279	323	0.52%
Time deposits	313,729	12,277	3.91%	325,397	14,783	4.54%	323,283	12,944	4.00%
Securities sold under agreements to repurchase									
FHLB advances	41,370	1,991	4.81%	34,912	1,728	4.95%	34,063	1,562	4.59%
Federal funds purchased	-	-	-%	3,907	206	5.27%	3,432	159	4.63%
Subordinated debentures	20,620	1,396	6.77%	20,620	1,570	7.61%	17,367	1,315	7.57%
Other debt	15,113	493	3.26%	14,345	915	6.39%	10,611	679	6.40%
Total interest-bearing liabilities	814,233	21,344	2.62%	785,914	28,429	3.62%	752,459	24,712	3.28%
Demand deposits	119,764			114,393			105,747		
Other liabilities	6,944			7,136			5,404		

Stockholders' equity	81,793	77,787	75,174
Total liabilities & equity	\$1,022,734	\$985,230	\$938,784
Net interest income	\$35,722	\$31,502	\$30,844
Net interest spread	3.34%	2.90%	3.05%
Impact of non-interest bearing funds	.39%	.53%	.46%
Net yield on interest-earning assets	3.73%	3.43%	3.51%
(1) The tax-exempt income is not recorded on a tax equivalent basis.			
(2) Nonaccrual loans have been included in the average balances.			
(3) Includes loans held for sale.			

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Changes in net interest income may also be analyzed by segregating the volume and rate components of interest income and interest expense. The following table summarizes the approximate relative contribution of changes in average volume and interest rates to changes in net interest income for the past two years (in thousands):

	2008 Compared to 2007			2007 Compared to 2006		
	Increase – (Decrease)			Increase – (Decrease)		
	Total	Volume (1)	Rate (1)	Total	Volume (1)	Rate (1)
Change				Change		
Earning Assets:						
Interest-bearing deposits	\$ 410	\$ 425	\$ (15)	\$ (18)	\$ (19)	\$ 1
Federal funds sold	135	337	(202)	(75)	(75)	-
Investment securities:						
Taxable	(723)	(890)	167	958	382	576
Tax-exempt (2)	122	126	(4)	(59)	(28)	(31)
Loans (3)	(2,809)	780	(3,589)	3,569	2,527	1,042
Total interest income	(2,865)	778	(3,643)	4,375	2,787	1,588
Interest-Bearing Liabilities:						
Deposits:						
Demand deposits, interest-bearing	(2,824)	381	(3,205)	1,140	571	569
Savings deposits	331	92	239	26	(9)	35
Time deposits	(2,506)	(515)	(1,991)	1,839	85	1,754
Securities sold under						
agreements to repurchase	(1,547)	244	(1,791)	8	(19)	27
FHLB advances	263	313	(50)	166	40	126
Federal funds purchased	(206)	(206)	-	47	12	35
Subordinated debentures	(174)	-	(174)	255	117	138
Other debt	(422)	48	(470)	236	110	126
Total interest expense	(7,085)	357	(7,442)	3,717	907	2,810
Net interest income	\$ 4,220	\$ 421	\$ 3,799	\$ 658	\$ 1,880	\$ (1,222)

(1) Changes attributable to the combined impact of volume and rate have been allocated proportionately to the change due to volume and the change due to rate.

(2) The tax-exempt income is not recorded on a tax equivalent basis.

(3) Nonaccrual loans are not material and have been included in the average balances.

Net interest income increased \$4,220,000, or 13.4% in 2008, compared to an increase of \$658,000, or 2.1% in 2007. The increase in net interest income in 2008 was primarily due to a greater decline in rates on interest-bearing liabilities than the decline in rates on interest-bearing assets. The increase in net interest income in 2007 was primarily due to growth in interest-earning assets primarily composed of loan growth that was offset by an increase in the cost of interest-bearing liabilities.

In 2008, average earning assets increased by \$38.4 million, or 4.2%, and average interest-bearing liabilities increased \$28.3 million or 3.6% compared with 2007. In 2007, average earning assets increased by \$42.6 million, or 4.9%, and average interest-bearing liabilities increased \$33.5 million or 4.4% compared with 2006. Changes in average balances are shown below:

- Ø Average interest-bearing deposits held by the Company increased \$26.4 million or 9962.3% in 2008 compared to 2007. In 2007, average interest-bearing deposits held by the Company decreased \$.4 million or 57.8%.
 - Ø Average federal funds sold increased \$15.3 million or 381.4% in 2008 compared to 2007. In 2007, average federal funds sold decreased \$1.5 million or 27.3%.
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- Ø Average loans increased by \$11.3 million or 1.6% in 2008 compared to 2007. In 2007, average loans increased by \$37.1 million or 5.4% compared to 2006.
- Ø Average securities decreased by \$14.6 million or 7.8% in 2008 compared to 2007. In 2007, average securities increased by \$7.4 million or 4.1% compared to 2006.
- Ø Average deposits increased by \$18.9 million or 2.9% in 2008 compared to 2007. In 2007, average deposits increased by \$25.6 million or 4.1% compared to 2006.
- Ø Average securities sold under agreements to repurchase increased by \$6.1 million or 11.1% in 2008 compared to 2007. In 2007, average securities sold under agreements to repurchase decreased by \$.4 million or .7% compared to 2006.
- Ø Average borrowings and other debt increased by \$3.3 million or 4.5% in 2008 compared to 2007. In 2007, average borrowings and other debt increased by \$8.3 million or 12.7% compared to 2006.
- Ø The federal funds rate decreased to a range of 0-.25% at December 31, 2008 from 4.25% at December 31, 2007. The federal funds rate was 5.25% at December 31, 2006.
- Ø Net interest margin increased to 3.73% compared to 3.43% in 2007 and 3.51% in 2006. Asset yields decreased by 56 basis points in 2008, while interest-bearing liabilities decreased by 100 basis points.

To compare the tax-exempt yields on interest-earning assets to taxable yields, the Company also computes non-GAAP net interest income on a tax equivalent basis (TE) where the interest earned on tax-exempt securities is adjusted to an amount comparable to interest subject to normal income taxes, assuming a federal tax rate of 34% (referred to as the tax equivalent adjustment). The TE adjustments to net interest income for 2008, 2007 and 2006 were \$430,000, \$366,000 and \$397,000, respectively. The net yield on interest-earning assets (TE) was 3.79% in 2008, 3.48% in 2007 and 3.56% in 2006.

Provision for Loan Losses

The provision for loan losses in 2008 was \$3,559,000 compared to \$862,000 in 2007 and \$760,000 in 2006. Nonperforming loans decreased to \$7,285,000 at December 31, 2008 from \$7,481,000 at December 31, 2007 and compared to \$3,668,000 at December 31, 2006. A portion of the decline in 2008 occurred as a result of the bank taking possession of real estate collateral and moving the balances to other real estate owned. Net charge-offs were \$2,090,000 during 2008, \$620,000 during 2007, and \$937,000 during 2006. For information on loan loss experience and nonperforming loans, see “Nonperforming Loans” and “Loan Quality and Allowance for Loan Losses” herein.

Other Income

An important source of the Company’s revenue is derived from other income. The following table sets forth the major components of other income for the last three years (in thousands):

	\$ Change From Prior Year					
	2008		2007		2006	
Trust	\$ 2,666	\$	2,607	\$	2,489	\$
Brokerage	574		528		533	
Insurance commissions	1,978		1,950		1,689	
					28	261

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Service charges	5,571	5,621	5,308	(50)	313
Securities gains	293	256	164	37	92
Mortgage banking	437	482	394	(45)	88
Other	3,745	3,217	2,803	528	414
Total other income	\$ 15,264	\$ 14,661	\$ 13,380	\$ 603	\$ 1,281

Total non-interest income increased to \$15,264,000 in 2008 compared to \$14,661,000 in 2007 and \$13,380,000 in 2006. The primary reasons for the more significant year-to-year changes in other income components are as follows:

Ø Trust revenues increased \$59,000 or 2.3% to \$2,666,000 in 2008 from \$2,607,000 in 2007, compared to \$2,489,000 in 2006. The increase from 2007 to 2008 in trust revenues was due to an increase in revenues from farm agency and employee benefits accounts. Trust assets were \$413.8 million at December 31, 2008 compared to \$453.9 million and \$431.6 million at December 31, 2007 and 2006, respectively.

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- Ø Revenue from brokerage annuity sales increased \$46,000 or 8.7% to \$574,000 in 2008 from \$528,000 in 2007, compared to \$533,000 in 2006. The increase from 2007 to 2008 was due to one-time fees received in connection with conversion to a new broker, Raymond James, and greater-than-expected commissions received from prior broker offset by a reduction in commissions received from the sale of annuities.
- Ø Insurance commissions increased \$28,000 or 1.4% to \$1,978,000 in 2008 from \$1,950,000 in 2007, compared to \$1,689,000 in 2006. The increase from 2007 to 2008 was due to an increase in commissions received on sales of business property and casualty insurance.
- Ø Fees from service charges decreased \$50,000 or .9% to \$5,571,000 in 2008 from \$5,621,000 in 2007, compared to \$5,308,000 in 2006. This decrease from 2007 to 2008 was primarily the result of a decrease in the number of overdrafts.
- Ø Net securities gains in 2008 were \$293,000 compared to net securities gains of \$256,000 in 2007, and were \$164,000 in 2006. Several securities in the investment portfolio were sold to improve the overall portfolio mix and the margin in 2008, 2007 and 2006.
- Ø Mortgage banking income decreased \$45,000 or 9.3% to \$437,000 in 2008 from \$482,000 in 2007, compared to \$394,000 in 2006. This decrease from 2007 to 2008 was due to a decrease in the volume of fixed rate loans originated and sold by First Mid Bank. Loans sold balances are as follows:

- Ø \$46 million (representing 381 loans) in 2008
- Ø \$48 million (representing 421 loans) in 2007
- Ø \$34 million (representing 322 loans) in 2006

- Ø Other income increased \$528,000 or 16.4% to \$3,745,000 in 2008 from \$3,217,000 in 2007, compared to \$2,803,000 in 2006. This increase from 2007 to 2008 was primarily due to approximately \$291,000 in proceeds from a life insurance policy the Company maintained on former executive officer and director, Daniel E. Marvin, Jr., who died in April of 2008 and increased ATM and debit card service fees.

Other Expense

The major categories of other expense include salaries and employee benefits, occupancy and equipment expenses and other operating expenses associated with day-to-day operations. The following table sets forth the major components of other expense for the last three years (in thousands):

	\$ Change From Prior Year					
	2008	2007	2006	2008	2007	
Salaries and benefits	\$ 16,876	\$ 16,408	\$ 15,418	\$ 468	\$ 990	
Occupancy and equipment	4,959	4,831	4,797	128	34	
Amortization of other intangibles	766	821	761	(55)	60	
Other real estate owned, net	234	82	114	152	(32)	
Stationery and supplies	557	547	583	10	(36)	
Legal and professional fees	1,820	1,641	1,324	179	317	
Marketing and promotion	847	911	945	(64)	(34)	
Other	5,401	4,814	4,481	587	333	
Total other expense	\$ 31,460	\$ 30,055	\$ 28,423	\$ 1,405	\$ 1,632	

Total non-interest expense increased to \$31,460,000 in 2008 from \$30,055,000 in 2007 and \$28,423,000 in 2006. The primary reasons for the more significant year-to-year changes in other expense components are as follows:

- Ø Salaries and employee benefits, the largest component of other expense, increased \$468,000 or 2.9% to \$16,876,000 in 2008 from \$16,408,000 in 2007, compared to \$15,418,000 in 2006. The increase in 2008 was as primarily due to merit increases for continuing employees. The increase in 2007 and 2006 was as a result of the acquisition of Mansfield and merit increases for continuing employees. There were 343 full-time equivalent employees at December 31, 2008 compared to 346 at December 31, 2007 and 347 at December 31, 2006.
 - Ø Occupancy and equipment expense increased \$128,000 or 2.6% to \$4,959,000 in 2008 from \$4,831,000 in 2007, compared to \$4,797,000 in 2006. In 2008, this increase was primarily due to increases in computer software maintenance. In 2007, this increase was due to an increase in occupancy expenses for Mansfield.
 - Ø Amortization of other intangibles expense decreased \$55,000 in 2008 due to complete amortization of one core deposit intangible in July 2007.
 - Ø Other operating expenses increased \$587,000 or 12.2% to 5,401,000 in 2008 from \$4,814,000 in 2007, compared to \$4,481,000 in 2006. In 2008, this increase was due to the write down of property in DeLand, Illinois to its appraised value, expenses related to loan collections and increases in various expenses. The increase in 2007 resulted from an increase in various expenses including ATM and debit card expenses.
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Ø On a net basis, all other categories of operating expenses increased \$277,000 or 8.7% to \$3,458,000 in 2008 from \$3,181,000 in 2007, compared to \$2,966,000 in 2006. In 2008, the increase was primarily due to increases in losses on foreclosed real estate sales and marketing and promotion expenses. The increase in 2007 was primarily due to increases in legal and other professional expenses resulting from the new disclosure requirements for the proxy statement for the 2007 annual meeting of stockholders.

Income Taxes

Income tax expense amounted to \$5,443,000 in 2008 compared to \$5,087,000 in 2007 and \$5,032,000 in 2006. Effective tax rates were 34.1%, 33.4% and 33.5%, respectively, for 2008, 2007 and 2006.

The Company adopted the provisions of FASB Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes," on January 1, 2007. The implementation of FIN 48 did not impact the Company's financial statements. The Company files U.S. federal and state of Illinois income tax returns. The Company is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2004.

Analysis of Balance Sheets

Loans

The loan portfolio (net of unearned discount) is the largest category of the Company's earning assets. The following table summarizes the composition of the loan portfolio for the last five years (in thousands):

	2008	2007	2006	2005	2004
Real estate – mortgage	\$ 520,587	\$ 517,892	\$ 510,735	\$ 450,435	\$ 427,154
Commercial & agricultural	167,735	172,294	161,085	150,598	137,733
Installment	48,578	52,875	47,017	34,385	30,587
Other	5,038	5,100	4,731	2,715	2,375
Total loans	\$ 741,938	\$ 748,161	\$ 723,568	\$ 638,133	\$ 597,849

Loan balances decreased by \$6.2 million or .8% from December 31, 2007 to December 31, 2008 primarily due to a decrease in commercial operating loan balances of \$4.6 million and a decrease in installment loan balances of \$4.3 million. Prior to 2008, the Company had an increase in commercial real estate loans outstanding resulting from demand for credit for commercial real estate projects in central Illinois and business development efforts. Also, corporate borrowers have required additional capital for inventory and company expansion. The growth was primarily in the communities of Champaign, Decatur, Effingham, Highland, and Maryville. Balances of loans sold into the secondary market were \$46 million in 2008, compared to \$48 million in 2007. The balance of real estate loans held for sale, included in the balances shown above, amounted to \$537,000 and \$1,974,000 as of December 31, 2008 and 2007, respectively.

At December 31, 2008, the Company had loan concentrations in agricultural industries of \$120.4 million, or 16.2%, of outstanding loans and \$114.2 million, or 15.3%, at December 31, 2007. In addition, the Company had loan concentrations in the following industries as of December 31, 2008 and 2007 (dollars in thousands):

2008		2007	
Principal	% Outstanding	Principal	% Outstanding

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	balance	loans	balance	loans
Lessors of non-residential buildings	\$ 68,987	9.30%	\$ 68,322	9.13%
Lessors of residential buildings & dwellings	48,648	6.56%	49,517	6.62%
Hotels and motels	45,518	6.14%	30,841	4.12%

The Company had no further industry loan concentrations in excess of 25% of total risk-based capital.

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The following table presents the balance of loans outstanding as of December 31, 2008, by maturities (in thousands):

	Maturity (1)			
	Over 1			Total
	One year or less(2)	Through 5 years	Over 5 years	
Real estate – mortgage	\$ 180,026	\$ 302,318	\$ 38,243	\$ 520,587
Commercial & agricultural	119,866	44,927	2,942	167,735
Installment	22,294	26,278	6	48,578
Other	1,098	2,604	1,336	5,038
Total loans	\$ 323,284	\$ 376,127	\$ 42,527	\$ 741,938

(1) Based upon remaining maturity.

(2) Includes demand loans, past due loans and overdrafts.

As of December 31, 2008, loans with maturities over one year consisted of \$366 million in fixed rate loans and \$52 million in variable rate loans. The loan maturities noted above are based on the contractual provisions of the individual loans. The Company has no general policy regarding rollovers and borrower requests, which are handled on a case-by-case basis.

Nonperforming Loans and Nonperforming Other Assets

Nonperforming loans include: (a) loans accounted for on a nonaccrual basis; (b) accruing loans contractually past due ninety days or more as to interest or principal payments; and (c) loans not included in (a) and (b) above which are defined as “renegotiated loans”. Nonperforming other assets include repossessed assets including real estate and automobiles. The following table presents information concerning the aggregate amount of nonperforming loans and nonperforming other assets (in thousands):

	December 31,				
	2008	2007	2006	2005	2004
Nonaccrual loans	\$ 7,285	\$ 7,460	\$ 3,639	\$ 3,458	\$ 3,106
Renegotiated loans which are performing in accordance					
with revised terms	-	21	29	-	-
Total nonperforming loans	7,285	7,481	3,668	3,458	3,106
Repossessed assets	2,388	524	1,396	420	913
Total nonperforming loans and nonperforming other assets	\$ 9,673	\$ 8,005	\$ 5,064	\$ 3,878	\$ 4,019
Nonperforming loans to loans, before allowance for loan losses	.98%	1.00%	.51%	.54%	.52%
Nonperforming loans and nonperforming other assets to loans,					
before allowance for loan losses	1.30%	1.07%	.70%	.61%	.67%

At December 31, 2008, \$2.7 million of the nonperforming loans resulted from insufficient cash flow on commercial real estate loans to three borrowers and \$1.4 million on agricultural real estate loans to one borrower. The \$175,000 decrease in nonaccrual loans during the year resulted from the net of \$5,440,000 of loans put on nonaccrual status, offset by \$2,230,000 of loans transferred to other real estate owned, \$1,296,000 of loans charged off and \$2,089,000 of loans becoming current or paid-off.

Interest income that would have been reported if nonaccrual and renegotiated loans had been performing totaled \$274,000, \$426,000 and \$123,000 for the years ended December 31, 2008, 2007 and 2006, respectively.

The Company's policy is to discontinue the accrual of interest income on any loan for which principal or interest is ninety days past due. The accrual of interest is discontinued earlier when, in the opinion of management, there is reasonable doubt as to the timely collection of interest or principal. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal.

Loan Quality and Allowance for Loan Losses

The allowance for loan losses represents management's estimate of the reserve necessary to adequately account for probable losses existing in the current portfolio. The provision for loan losses is the charge against current earnings that is determined by management as the amount needed to maintain an adequate allowance for loan losses. In determining the adequacy of the allowance for loan losses, and therefore the provision to be charged to current earnings, management relies predominantly on a disciplined credit review and approval process that extends to the full range of the Company's credit exposure. The review process is directed by overall lending policy and is intended to identify, at the earliest possible stage, borrowers who might be facing financial difficulty.

Once identified, the magnitude of exposure to individual borrowers is quantified in the form of specific allocations of the allowance for loan losses. Management considers collateral values and guarantees in the determination of such specific allocations. Additional factors considered by management in evaluating the overall adequacy of the allowance include historical net loan losses, the level and composition of nonaccrual, past due and renegotiated loans, trends in volumes and terms of loans, effects of changes in risk selection and underwriting standards or lending practices, lending staff changes, concentrations of credit, industry conditions and the current economic conditions in the region where the Company operates. Given the current state of the economy, management did assess the impact of the recession on each category of loans and adjusted historical loss factors for more recent economic trends.

Management utilizes a five-year loss history as one component in assessing the probability of inherent future losses. Given the decline in economic conditions over the past year, management has also increased its allocation to various loan categories for economic factors. Some of the economic factors include the potential for reduced cash flow for commercial operating loans from reduction in sales or increased operating costs, decreased occupancy rates for commercial buildings, reduced levels of home sales for commercial land developments, the decline in and uncertainty regarding grain prices and increased operating costs for farmers, and increased levels of unemployment and bankruptcy impacting consumer's ability to pay. Each of these economic uncertainties was taken into consideration in developing the level of the reserve. Management considers the allowance for loan losses a critical accounting policy.

Management recognizes there are risk factors that are inherent in the Company's loan portfolio. All financial institutions face risk factors in their loan portfolios because risk exposure is a function of the business. The Company's operations (and therefore its loans) are concentrated in east central Illinois, an area where agriculture is the dominant industry. Accordingly, lending and other business relationships with agriculture-based businesses are critical to the Company's success. At December 31, 2008, the Company's loan portfolio included \$120.4 million of loans to borrowers whose businesses are directly related to agriculture. The balance increased \$6.2 million from \$114.2 million at December 31, 2007. While the Company adheres to sound underwriting practices, including collateralization of loans, any extended period of low commodity prices, significantly reduced yields on crops and/or reduced levels of government assistance to the agricultural industry could result in an increase in the level of problem agriculture loans and potentially result in loan losses within the agricultural portfolio.

In addition, the Company has \$45.5 million of loans to motels, hotels and tourist courts. The performance of these loans is dependent on borrower specific issues as well as the general level of business and personal travel within the region. While the Company adheres to sound underwriting standards, a prolonged period of reduced business or personal travel could result in an increase in non-performing loans to this business segment and potentially in loan losses. The Company also has \$69 million of loans to lessors of non-residential buildings and \$48.6 million of loans to lessors of residential buildings and dwellings. A significant widespread decline in real estate values could result in an increase in non-performing loans to this segment and potentially in loan losses.

Loan loss experience for the past five years are summarized as follows (dollars in thousands):

	2008	2007	2006	2005	2004
Average loans outstanding, net of unearned income	\$ 740,083	\$ 728,790	\$ 691,726	\$ 610,781	\$ 572,836
Allowance-beginning of year	\$ 6,118	\$ 5,876	\$ 4,648	\$ 4,621	\$ 4,426
Balance added through acquisitions	-	-	1,405	-	-
Charge-offs:					
Real estate-mortgage	1,640	368	231	122	23
Commercial, financial and agricultural	479	180	595	757	436
Installment	119	100	142	278	129
Other	184	215	188	130	-
Total charge-offs	2,422	863	1,156	1,287	588
Recoveries:					

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Real estate-mortgage	75	9	8	63	-
Commercial, financial and agricultural	98	48	30	75	146
Installment	38	33	49	42	49
Other	121	153	132	43	-
Total recoveries	332	243	219	223	195
Net charge-offs	2,090	620	937	1,064	393
Provision for loan losses	3,559	862	760	1,091	588
Allowance-end of year	\$ 7,587	\$ 6,118	\$ 5,876	\$ 4,648	\$ 4,621
Ratio of net charge-offs to average loans	.28%	.09%	.14%	.17%	.07%
Ratio of allowance for loan losses to loans outstanding (at end of year)	1.02%	.82%	.81%	.73%	.77%
Ratio of allowance for loan losses to nonperforming loans	104.1%	81.8%	160.2%	134.4%	148.8%

The ratio of the allowance for loan losses to non-performing loans is 104.1% as of December 31, 2008 compared to 81.8% as of December 31, 2007. The increase in the balance of the allowance for loan losses and the decline in total non-performing loans led to the improvement of this ratio. Given the current economic environment and probable losses in the loan portfolio, management increased the allowance balance. The decrease in non-performing loans is primarily due to the bank taking possession of real estate collateral and moving the balances to other real estate owned offset by loans that became nonperforming during the year.

The Company minimizes credit risk by adhering to sound underwriting and credit review policies. These policies are reviewed at least annually, and the Board of Directors approves all changes. Senior management is actively involved in business development efforts and the maintenance and monitoring of credit underwriting and approval. The loan review system and controls are designed to identify, monitor and address asset quality problems in an accurate and timely manner. On a quarterly basis, the Board of Directors reviews the status of problem loans. In addition to internal policies and controls, regulatory authorities periodically review asset quality and the overall adequacy of the allowance for loan losses.

During 2008, the Company had net charge-offs of \$2,090,000 compared to \$620,000 in 2007 and \$937,000 in 2006. During 2008, the Company's significant charge-offs included \$204,000 on commercial loans of one borrower, \$200,000 of real estate mortgage loans of one borrower and \$1,181,000 of commercial real estate mortgage loans of three borrowers. During 2007, the Company's significant charge-offs included \$165,000 on commercial loans of three borrowers, \$66,000 of real estate mortgage loans of one borrower and \$250,000 of commercial real estate mortgage loans of two borrowers. During 2006, the Company's significant charge-offs included \$565,000 on commercial loans of five borrowers and \$168,000 of commercial and real estate mortgage loans of one borrower.

At December 31, 2008, the allowance for loan losses amounted to \$7,587,000, or 1.02% of total loans, and 104.1% of nonperforming loans. At December 31, 2007, the allowance for loan losses amounted to \$6,118,000, or .82% of total loans, and 81.8% of nonperforming loans. The ratio of the allowance for loan losses to total loans has increased to reflect management's estimate of probable losses in the loan portfolio.

The allowance for loan losses, in management's judgment, is allocated as follows to cover probable loan losses (dollars in thousands):

	December 31, 2008		December 31, 2007		December 31, 2006	
	Allowance	% of	Allowance	% of	Allowance	% of
	for	loans	for	loans	for	loans
	loan	to total	loan	to total	loan	to total
	losses	loans	losses	loans	losses	loans
Real estate-mortgage	\$ 510	70.2%	\$ 214	69.2%	\$ 215	70.6%
Commercial, financial						
and agricultural	5,607	22.6%	4,359	23.0%	4,002	22.3%
Installment	319	6.5%	404	7.1%	382	6.5%
Other	78	.7%	22	.7%	26	.6%
Total allocated	6,514		4,999		4,625	
Unallocated	1,073	N/A	1,119	N/A	1,251	N/A
Allowance at end of year	\$ 7,587	100.0%	\$ 6,118	100.0%	\$ 5,876	100.0%

	December 31, 2005		December 31, 2004	
	Allowance	% of	Allowance	% of
	for	loans	for	loans

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	loan losses	to total loans	loan losses	to total loans
Real estate-mortgage	\$ 134	70.6%	\$ 240	71.4%
Commercial, financial and agricultural	3,249	23.6%	3,124	23.1%
Installment	319	5.4%	150	5.1%
Other	18	.4%	-	.4%
Total allocated	3,720		3,514	
Unallocated	928	N/A	1,107	N/A
Allowance at end of year	\$ 4,648	100.0%	\$ 4,621	100.0%

The allowance is allocated to the individual loan categories by a specific allocation for all classified loans plus a percentage of loans not classified based on historical losses and other factors. The unallocated allowance represents an estimate of the probable, inherent, but yet undetected, losses in the loan portfolio. It is based on factors that cannot necessarily be associated with a specific credit or loan category and represents management's estimate to ensure that the overall allowance of loan losses appropriately reflects a margin for the imprecision necessarily inherent in the estimates of expected credit losses.

Securities

The Company's overall investment goal is to maximize earnings while maintaining liquidity in securities having minimal credit risk. The types and maturities of securities purchased are primarily based on the Company's current and projected liquidity and interest rate sensitivity positions.

The following table sets forth the year-end amortized cost of the Company's securities for the last three years (dollars in thousands):

	December 31,					
	2008		2007		2006	
	Amount	Weighted Average Yield	Amount	Weighted Average Yield	Amount	Weighted Average Yield
U.S. Treasury securities and obligations of U.S. government						
corporations and agencies	\$ 72,074	4.72%	\$ 106,175	4.82%	\$ 140,924	4.81%
Obligations of states and political subdivisions	22,042	4.10%	17,820	4.15%	16,637	4.17%
Mortgage-backed securities	61,102	5.66%	49,798	5.33%	15,491	4.50%
Trust preferred securities	9,328	6.23%	9,587	6.30%	6,815	8.76%
Other securities	6,210	4.56%	35	-%	532	4.94%
Total securities	\$ 170,756	5.05%	\$ 183,415	4.96%	\$ 180,399	4.85%

At December 31, 2008, the Company's investment portfolio reflected an increase in mortgage-backed securities and obligations of states and political subdivisions securities and a decrease in U.S. Treasury securities and obligations of U.S. government corporations and agencies. There was also an increase in other securities which are corporate debt securities of financial institutions. This change in the portfolio mix improved the characteristics of the portfolio relating to interest rate risk exposure and portfolio yield. The increase in mortgage-backed securities consisted of collateralized mortgage obligations and mortgage-backed securities issued by FNMA and FHLMC. No investments were made in securities backed by collateralized debt obligations, which is a type of security that has resulted in losses for some banks. When purchasing investment securities, the Company considers its overall liquidity and interest rate risk profile, as well as the adequacy of expected returns relative to the risks assumed.

The following table indicates the expected maturities of investment securities classified as available-for-sale and held-to-maturity, presented at amortized cost, at December 31, 2008 (dollars in thousands) and the weighted average yield for each range of maturities. Mortgage-backed securities are aged according to their weighted average life. All other securities are shown at their contractual maturity.

One	After 1	After 5	After
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	year or less	through 5 years	through 10 years	10 years	Total
Available-for-sale:					
U.S. Treasury securities and obligations of U.S.					
government corporations and agencies	\$ 26,026	\$ 34,000	\$ 12,048	\$ -	\$ 72,074
Obligations of state and political subdivisions	2,667	2,949	15,011	816	21,443
Mortgage-backed securities	14,765	46,337	-	-	61,102
Trust preferred securities	323	9,005			9,328
Other securities	-	6,175	-	35	6,210
Total investments	\$ 43,781	\$ 98,466	\$ 27,059	\$ 851	\$ 170,157
Weighted average yield	4.99%	5.16%	4.78%	4.32%	5.05%
Full tax-equivalent yield	5.11%	5.21%	5.80%	6.30%	5.17%
Held-to-maturity:					
Obligations of state and political subdivisions	\$ 403	\$ 196	\$ -	\$ -	\$ 599
Weighted average yield	5.17%	5.38%	-%	-%	5.24%
Full tax-equivalent yield	7.58%	7.65%	-%	-%	7.61%

The weighted average yields are calculated on the basis of the amortized cost and effective yields weighted for the scheduled maturity of each security. Full tax-equivalent yields have been calculated using a 34% tax rate. With the exception of obligations of the U.S. Treasury and other U.S. government agencies and corporations, there were no investment securities of any single issuer the book value of which exceeded 10% of stockholders' equity at December 31, 2008.

Declines in the fair value of available for sale investment securities are recorded as either temporary impairment or other-than-temporary impairment (OTTI). Temporary adjustments are recorded when the fair value of a security fluctuates from its historical cost. Temporary adjustments are recorded in accumulated other comprehensive income, and impact our equity position. Temporary adjustments do not impact net income. A recovery of available for sale security prices also is recorded as an adjustment to other comprehensive income for securities that are temporarily impaired, and results in a positive impact to the Company's equity position. OTTI is recorded when the fair value of an available for sale security is less than historical cost, and it is probable that all contractual cash flows will not be collected. OTTI is recorded to noninterest income, and therefore, results in a negative impact to net income. Because the available for sale securities portfolio is recorded at fair value, the conclusion as to whether an investment decline is other-than-temporarily impaired, does not significantly impact the Company's equity position, as the amount of the temporary adjustment has already been reflected in accumulated other comprehensive income/loss. A recovery in the value of an other-than-temporarily impaired security is recorded as additional interest income over the remaining life of the security.

The table below presents the credit ratings as of December 31, 2008, for certain investment securities:

	Amortized Cost	Estimated Fair Value	Average Credit Rating of Fair Value at December 31, 2008 (1)						
			AAA	AA +/-	A+/-	BBB +/-	< BBB -	Not rated	
U.S. Treasury securities and obligations of U.S. government corporations and agencies	\$ 72,074	\$ 74,632	\$ 74,632	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Obligations of state and political subdivisions	22,042	21,532	753	11,248	2,043	3,231	-	-	4,257
Mortgage-backed securities (2)	61,102	62,802	-	-	-	-	-	-	62,802
Trust preferred securities	9,328	5,378	-	-	1,641	-	3,737	-	-
Other securities	6,210	5,742	-	3,026	2,709	-	-	-	7
Total investments	\$ 170,756	\$ 170,086	\$ 75,385	\$ 14,274	\$ 6,393	\$ 3,231	\$ 3,737	\$ -	\$ 67,066

(1) Credit ratings reflect the lowest current rating assigned by a nationally recognized credit rating agency.

(2) Mortgage-backed securities include mortgage-backed securities (MBS) and collateralized mortgage obligation (CMO) issues from the following government sponsored enterprises: FHLMC, FNMA, GNMA and FHLB. While MBS and CMOs are no longer explicitly rated by credit rating agencies, the industry recognizes that they are backed by agencies which have an implied government guarantee.

At December 31, 2008, there was one obligation of a U.S. government agency with a fair value of \$5,707,000 and unrealized loss of \$9,300 in a continuous unrealized loss position for twelve months or more. This position was due

to short-term and intermediate rates increasing since the purchase of these securities resulting in the market value of the security being lower than book value. There were also two trust preferred securities with a fair value of \$1,930,000 and unrealized losses of \$3,108,000 in a continuous unrealized loss position for twelve months or more. In addition there was one trust preferred security with a fair value of \$1,807,000 in a continuous loss position of less than twelve months but rated below BBB. These unrealized losses were primarily due to the long-term nature of the trust preferred securities, a lack of demand or inactive market for these securities, and concerns regarding the underlying financial institutions that have issued the trust preferred securities. Cash flow analyses show it is probable the Company will receive all contractual principal and interest with no deferral of interest payments projected.

The Company does not believe any individual unrealized loss as of December 31, 2008 represents OTTI. However, given the continued disruption in the financial markets, the Company may be required to recognize OTTI losses in future periods with respect to its available for sale investment securities portfolio. The amount and timing of any additional OTTI will depend on the decline in the underlying cash flows of the securities. The Company has the intent and ability to hold these securities until recovery in value or maturity. See Note 4 – “Investment Securities” herein for a more detailed description of these securities.

Investment securities carried at approximately \$152,598,000 and \$163,872,000 at December 31, 2008 and 2007, respectively, were pledged to secure public deposits and repurchase agreements and for other purposes as permitted or required by law.

Deposits

Funding of the Company's earning assets is substantially provided by a combination of consumer, commercial and public fund deposits. The Company continues to focus its strategies and emphasis on retail core deposits, the major component of funding sources. The following table sets forth the average deposits and weighted average rates for 2008, 2007 and 2006 (dollars in thousands):

	2008		2007		2006	
	Average Balance	Weighted Average Rate	Average Balance	Weighted Average Rate	Average Balance	Weighted Average Rate
Demand deposits:						
Non-interest bearing	\$ 119,764	-	\$ 114,393	-	\$ 105,744	-
Interest bearing	288,057	1.26%	271,117	1.98%	246,035	2.16%
Savings	74,236	.92%	60,654	.58%	62,279	.52%
Time deposits	313,729	3.91%	325,397	4.54%	323,283	4.00%
Total average deposits	\$ 795,786	2.08%	\$ 771,561	2.66%	\$ 737,341	2.52%

	December 31,		
(dollars in thousands)	2008	2007	2006
High month-end balances of total deposits	\$ 810,756	\$ 784,597	\$ 799,002
Low month-end balances of total deposits	777,337	756,222	651,392

In 2008, the average balance of deposits increased by \$24.2 million from 2007. The increase was primarily attributable to increases in savings account balances. Average non-interest bearing deposits increased by \$5.4 million, average money market account balances increased by \$4.7 million, and NOW account balances increased by \$12.2 million offset by a decline in consumer CD balances. In 2007, the average balance of deposits increased by \$34.2 million from 2006. The increase was primarily attributable to money market account balances. Average non-interest bearing deposits increased by \$8.6 million, average money market account balances increased by \$20.8 million, and consumer CD balances increased by \$38.1 million offset by a decline in brokered CD balances.

In 2008, the Company's significant deposits included brokered CDs, time deposits with the State of Illinois and deposit relationships with various public entities. As of December 31, 2008, the Company had three brokered CDs which totaled \$15 million. State of Illinois time deposits maintained with the Company totaled \$4.4 million as of December 31, 2008. These balances are subject to bid annually. In addition, the Company maintains account relationships with various public entities throughout its market areas. Five public entities had total balances of \$21.9 million in various checking accounts and time deposits as of December 31, 2008. These balances are subject to change depending upon the cash flow needs of the public entity.

The following table sets forth the maturity of time deposits of \$100,000 or more (in thousands):

	December 31,		
	2008	2007	2006
3 months or less	\$ 31,748	\$ 17,883	\$ 38,468
Over 3 through 6 months	18,189	25,339	20,004
Over 6 through 12 months	61,421	47,160	45,532
Over 12 months	24,865	7,670	11,896
Total	\$ 136,223	\$ 98,052	\$ 115,900

The balance of time deposits of \$100,000 or more increased by \$38.2 million from December 31, 2007 to December 31, 2008. The increase in balances was primarily attributable to an increase in brokered CD balances. The balance of time deposits of \$100,000 or more decreased by \$17.8 million from December 31, 2006 to December 31, 2007. The decrease in balances was primarily attributable to brokered CD balances that matured and were not immediately replaced.

Balances of time deposits of \$100,000 or more includes brokered CDs, time deposits maintained for public entities, and consumer time deposits. The balance of brokered CDs was \$15 million as of December 31, 2008. The Company had no brokered CDs at December 31, 2007. The Company also maintains time deposits for the State of Illinois with balances of \$4.4 million, \$3 million and \$3.1 million as of December 31, 2008, 2007 and 2006, respectively. The State of Illinois deposits are subject to bid annually and could increase or decrease in any given year.

Repurchase Agreements and Other Borrowings

Securities sold under agreements to repurchase are short-term obligations of First Mid Bank. First Mid Bank collateralizes these obligations with certain government securities that are direct obligations of the United States or one of its agencies. First Mid Bank offers these retail repurchase agreements as a cash management service to its corporate customers. Other borrowings consist of Federal Home Loan Bank (“FHLB”) advances, federal funds purchased, junior subordinated debentures and loans (short-term or long-term debt) that the Company has outstanding.

Information relating to securities sold under agreements to repurchase and other borrowings for the last three years is presented below (dollars in thousands):

	2008	2007	2006
At December 31:			
Federal funds purchased	\$ -	\$ -	\$ 6,800
Securities sold under agreements to repurchase	80,708	68,300	66,693
Federal Home Loan Bank advances:			
Fixed term – due in one year or less	5,000	15,000	7,000