

TRUSTMARK CORP  
Form 10-Q  
August 07, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended June 30, 2018

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 000-03683

Trustmark Corporation

(Exact name of registrant as specified in its charter)

Mississippi 64-0471500  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

248 East Capitol Street, Jackson, Mississippi 39201  
(Address of principal executive offices) (Zip Code)

(601) 208-5111

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of July 31, 2018, there were 67,621,369 shares outstanding of the registrant’s common stock (no par value).

## Forward-Looking Statements

Certain statements contained in this Quarterly Report on Form 10-Q constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. You can identify forward-looking statements by words such as “may,” “hope,” “will,” “should,” “expect,” “plan,” “anticipate,” “intend,” “believe,” “estimate,” “predict,” “potentially,” “could,” “future” or the negative of those terms or other words of similar meaning. You should read statements that contain these words carefully because they discuss our future expectations or state other “forward-looking” information. These forward-looking statements include, but are not limited to, statements relating to anticipated future operating and financial performance measures, including net interest margin, credit quality, business initiatives, growth opportunities and growth rates, among other things, and encompass any estimate, prediction, expectation, projection, opinion, anticipation, outlook or statement of belief included therein as well as the management assumptions underlying these forward-looking statements. You should be aware that the occurrence of the events described under the caption “Risk Factors” in Trustmark’s filings with the Securities and Exchange Commission could have an adverse effect on our business, results of operations and financial condition. Should one or more of these risks materialize, or should any such underlying assumptions prove to be significantly different, actual results may vary significantly from those anticipated, estimated, projected or expected.

Risks that could cause actual results to differ materially from current expectations of Management include, but are not limited to, changes in the level of nonperforming assets and charge-offs, local, state and national economic and market conditions, including potential market impacts of efforts by the Federal Reserve Board to reduce the size of its balance sheet, conditions in the housing and real estate markets in the regions in which Trustmark operates and the extent and duration of the current volatility in the credit and financial markets as well as crude oil prices, changes in our ability to measure the fair value of assets in our portfolio, material changes in the level and/or volatility of market interest rates, the performance and demand for the products and services we offer, including the level and timing of withdrawals from our deposit accounts, the costs and effects of litigation and of unexpected or adverse outcomes in such litigation, our ability to attract noninterest-bearing deposits and other low-cost funds, competition in loan and deposit pricing, as well as the entry of new competitors into our markets through de novo expansion and acquisitions, economic conditions, including the potential impact of issues relating to the European financial system and monetary and other governmental actions designed to address credit, securities, and/or commodity markets, the enactment of legislation and changes in existing regulations or enforcement practices or the adoption of new regulations, changes in accounting standards and practices, including changes in the interpretation of existing standards, that affect our consolidated financial statements, changes in consumer spending, borrowings and savings habits, technological changes, changes in the financial performance or condition of our borrowers, changes in our ability to control expenses, greater than expected costs or difficulties related to the integration of acquisitions or new products and lines of business, cyber-attacks and other breaches which could affect our information system security, natural disasters, environmental disasters, acts of war or terrorism, and other risks described in our filings with the Securities and Exchange Commission.

Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct. Except as required by law, we undertake no obligation to update or revise any of this information, whether as the result of new information, future events or developments or otherwise.

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## Trustmark Corporation and Subsidiaries

## Consolidated Balance Sheets

(\$ in thousands)

	(Unaudited)	
	June 30, 2018	December 31, 2017
<b>Assets</b>		
Cash and due from banks (noninterest-bearing)	\$387,119	\$335,768
Federal funds sold and securities purchased under reverse repurchase agreements	—	615
Securities available for sale (at fair value)	1,974,675	2,238,635
Securities held to maturity (fair value: \$954,638-2018; \$1,046,247-2017)	985,845	1,056,486
Loans held for sale (LHFS)	196,217	180,512
Loans held for investment (LHFI)	8,678,983	8,569,967
Less allowance for loan losses, LHFI	83,566	76,733
Net LHFI	8,595,417	8,493,234
Acquired loans	173,107	261,517
Less allowance for loan losses, acquired loans	3,046	4,079
Net acquired loans	170,061	257,438
Net LHFI and acquired loans	8,765,478	8,750,672
Premises and equipment, net	177,686	179,339
Mortgage servicing rights	97,411	84,269
Goodwill	379,627	379,627
Identifiable intangible assets, net	13,677	16,360
Other real estate	39,667	43,228
Other assets	507,863	532,442
<b>Total Assets</b>	<b>\$13,525,265</b>	<b>\$13,797,953</b>
<b>Liabilities</b>		
<b>Deposits:</b>		
Noninterest-bearing	\$2,958,354	\$2,978,074
Interest-bearing	8,114,081	7,599,438
Total deposits	11,072,435	10,577,512
Federal funds purchased and securities sold under repurchase agreements	477,891	469,827
Short-term borrowings	186,647	971,049
Long-term Federal Home Loan Bank (FHLB) advances	913	946
Junior subordinated debt securities	61,856	61,856
Other liabilities	141,451	145,062
<b>Total Liabilities</b>	<b>11,941,193</b>	<b>12,226,252</b>
<b>Shareholders' Equity</b>		

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Common stock, no par value:

Authorized: 250,000,000 shares

Issued and outstanding: 67,621,111 shares - 2018; 67,746,094 shares - 2017	14,089	14,115
Capital surplus	361,715	369,124
Retained earnings	1,282,007	1,228,187
Accumulated other comprehensive loss, net of tax	(73,739 )	(39,725 )
Total Shareholders' Equity	1,584,072	1,571,701
Total Liabilities and Shareholders' Equity	\$13,525,265	\$13,797,953

See notes to consolidated financial statements.

## Trustmark Corporation and Subsidiaries

## Consolidated Statements of Income

(\$ in thousands except per share data)

(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30,	2017	June 30,	2017
	2018		2018	2017
<b>Interest Income</b>				
Interest and fees on LHFS & LHFI	\$96,712	\$84,988	\$188,382	\$164,395
Interest and fees on acquired loans	5,022	6,263	9,899	11,452
Interest on securities:				
Taxable	16,894	19,377	34,400	38,574
Tax exempt	579	766	1,230	1,611
Interest on federal funds sold and securities purchased under reverse repurchase agreements	5	11	7	12
Other interest income	1,054	371	1,988	638
<b>Total Interest Income</b>	<b>120,266</b>	<b>111,776</b>	<b>235,906</b>	<b>216,682</b>
<b>Interest Expense</b>				
Interest on deposits	12,139	5,107	21,630	9,052
Interest on federal funds purchased and securities sold under repurchase agreements	1,250	1,037	1,912	1,735
Other interest expense	1,713	3,628	5,107	6,301
<b>Total Interest Expense</b>	<b>15,102</b>	<b>9,772</b>	<b>28,649</b>	<b>17,088</b>
<b>Net Interest Income</b>	<b>105,164</b>	<b>102,004</b>	<b>207,257</b>	<b>199,594</b>
Provision for loan losses, LHFI	3,167	2,921	7,128	5,683
Provision for loan losses, acquired loans	(441 )	(2,564 )	(291 )	(4,169 )
<b>Net Interest Income After Provision for Loan Losses</b>	<b>102,438</b>	<b>101,647</b>	<b>200,420</b>	<b>198,080</b>
<b>Noninterest Income</b>				
Service charges on deposit accounts	10,647	10,755	21,504	21,587
Bank card and other fees	7,070	7,370	13,696	13,870
Mortgage banking, net	9,046	9,008	20,311	19,193
Insurance commissions	10,735	9,745	20,154	18,957
Wealth management	7,478	7,674	15,045	15,087
Other, net	2,415	5,637	3,474	7,528
Security gains (losses), net	—	1	—	1
<b>Total Noninterest Income</b>	<b>47,391</b>	<b>50,190</b>	<b>94,184</b>	<b>96,223</b>
<b>Noninterest Expense</b>				
Salaries and employee benefits	59,975	57,185	118,450	112,574
Defined benefit plan termination	—	17,644	—	17,644
Services and fees	16,322	15,009	32,068	30,341

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Net occupancy - premises	6,550	6,210	13,052	12,448
Equipment expense	6,202	6,162	12,301	12,160
Other real estate expense, net	(93 )	383	773	2,142
FDIC assessment expense	2,538	2,686	5,533	5,326
Other expense	12,306	16,796	24,088	31,497
Total Noninterest Expense	103,800	122,075	206,265	224,132
Income Before Income Taxes	46,029	29,762	88,339	70,171
Income taxes	6,216	5,727	11,696	14,888
Net Income	\$39,813	\$24,035	\$76,643	\$55,283
Earnings Per Share				
Basic	\$0.59	\$0.35	\$1.13	\$0.82
Diluted	\$0.59	\$0.35	\$1.13	\$0.81
Dividends Per Share				
	\$0.23	\$0.23	\$0.46	\$0.46

See notes to consolidated financial statements.

## Trustmark Corporation and Subsidiaries

## Consolidated Statements of Comprehensive Income

(\$ in thousands)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net income per consolidated statements of income	\$39,813	\$24,035	\$76,643	\$55,283
Other comprehensive income (loss), net of tax:				
Net unrealized gains (losses) on available for sale securities and transferred securities:				
Net unrealized holding gains (losses) arising during the period	(6,955 )	2,832	(27,985 )	4,243
Less: adjustment for net (gains) losses realized in net income	—	(1 )	—	(1 )
Change in net unrealized holding loss on securities transferred to held to maturity	728	734	1,452	1,495
Pension and other postretirement benefit plans:				
Net change in prior service costs	46	38	93	77
Recognized net loss due to lump sum settlement	30	—	61	—
Change in net actuarial loss	272	482	548	968
Recognized net loss due to defined benefit plan termination	—	10,492	—	10,492
Derivatives:				
Change in the accumulated gain (loss) on effective cash flow hedge derivatives	99	(129 )	419	(94 )
Less: adjustment for (gain) loss realized in net income	(73 )	48	(78 )	109
Other comprehensive income (loss), net of tax	(5,853 )	14,496	(25,490 )	17,289
Comprehensive income	\$33,960	\$38,531	\$51,153	\$72,572

See notes to consolidated financial statements.



Trustmark Corporation and Subsidiaries

Consolidated Condensed Statements of Changes in Shareholders' Equity

(\$ in thousands)

(Unaudited)

	2018	2017
Balance, January 1,	\$1,571,701	\$1,520,208
Net income per consolidated statements of income	76,643	55,283
Other comprehensive income (loss), net of tax	(25,490 )	17,289
Common stock dividends paid	(31,347 )	(31,397 )
Common stock issued-net, long-term incentive plan	(1,422 )	(1,639 )
Repurchase and retirement of common stock	(7,877 )	—
Compensation expense, long-term incentive plan	1,864	2,174
Balance, June 30,	\$1,584,072	\$1,561,918

See notes to consolidated financial statements.

## Trustmark Corporation and Subsidiaries

## Consolidated Statements of Cash Flows

(\$ in thousands)

(Unaudited)

	Six Months Ended June 30,	
	2018	2017
<b>Operating Activities</b>		
Net income per consolidated statements of income	\$76,643	\$55,283
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses, net	6,837	1,514
Depreciation and amortization	19,534	18,729
Net amortization of securities	5,086	5,375
Securities (gains) losses, net	—	(1 )
Gains on sales of loans, net	(9,999 )	(8,550 )
Deferred income tax provision	4,000	4,200
Proceeds from sales of loans held for sale	525,611	565,150
Purchases and originations of loans held for sale	(534,903 )	(588,773 )
Originations of mortgage servicing rights	(7,719 )	(7,497 )
Earnings on bank-owned life insurance	(2,639 )	(2,487 )
Net change in other assets	7,087	22,130
Net change in other liabilities	(2,658 )	(5,676 )
Other operating activities, net	(9,478 )	2,588
Net cash provided by operating activities	77,402	61,985
<b>Investing Activities</b>		
Proceeds from maturities, prepayments and calls of securities held to maturity	71,817	90,340
Proceeds from maturities, prepayments and calls of securities available for sale	226,479	230,945
Proceeds from sales of securities available for sale	—	26,409
Purchases of securities held to maturity	—	(69,989 )
Purchases of securities available for sale	(4,159 )	(292,170 )
Net proceeds from bank-owned life insurance	1,586	—
Net change in federal funds sold and securities purchased		
under reverse repurchase agreements	615	500
Net change in member bank stock	27,114	474
Net change in loans	(28,727 )	(374,640 )
Purchases of premises and equipment	(6,224 )	(8,142 )
Proceeds from sales of premises and equipment	651	7,696
Proceeds from sales of other real estate	10,681	15,948
Purchases of software	(7,359 )	(2,267 )
Investments in tax credit and other partnerships	(17 )	(2,893 )
Net cash used in business acquisition	—	(19,775 )

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Net cash provided by (used in) investing activities	292,457	(397,564)
<b>Financing Activities</b>		
Net change in deposits	494,923	201,221
Net change in federal funds purchased and securities sold under repurchase agreements	8,064	(31,749 )
Net change in short-term borrowings	(780,816)	192,799
Payments on long-term FHLB advances	(33 )	(33 )
Redemption of junior subordinated debt securities	—	(3,000 )
Common stock dividends	(31,347 )	(31,397 )
Repurchase and retirement of common stock	(7,877 )	—
Shares withheld to pay taxes, long-term incentive plan	(1,422 )	(1,639 )
Net cash provided by (used in) financing activities	(318,508)	326,202
Net change in cash and cash equivalents	51,351	(9,377 )
Cash and cash equivalents at beginning of period	335,768	327,706
Cash and cash equivalents at end of period	\$387,119	\$318,329

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries

Notes to Consolidated Financial Statements

(Unaudited)

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

Trustmark Corporation (Trustmark) is a bank holding company headquartered in Jackson, Mississippi. Through its subsidiaries, Trustmark operates as a financial services organization providing banking and financial solutions to corporate institutions and individual customers through 198 offices at June 30, 2018 in Alabama, Florida, Mississippi, Tennessee and Texas.

The consolidated financial statements include the accounts of Trustmark and all other entities in which Trustmark has a controlling financial interest. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to prior period amounts to conform to the current period presentation.

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements and should be read in conjunction with the consolidated financial statements, and notes thereto, included in Trustmark's 2017 Annual Report on Form 10-K.

Operating results for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year or any future period. In the opinion of Management, all adjustments (consisting of normal recurring accruals) considered necessary for the fair presentation of these consolidated financial statements have been included. The preparation of financial statements in conformity with these accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and income and expense during the reporting periods and the related disclosures. Although Management's estimates contemplate current conditions and how they are expected to change in the future, it is reasonably possible that in 2018 actual conditions could vary from those anticipated, which could affect Trustmark's financial condition and results of operations. Actual results could differ from those estimates.

#### Note 2 – Business Combinations

On April 7, 2017, Trustmark completed its merger with RB Bancorporation (Reliance), the holding company for Reliance Bank, which had seven offices serving the Huntsville, Alabama metropolitan service area (MSA). Reliance Bank was merged into Trustmark National Bank simultaneously with the merger of Trustmark and Reliance. Under the terms of the Merger Agreement dated November 14, 2016, Trustmark paid \$22.00 in cash for each share of Reliance common stock outstanding, which represented payment to Reliance common shareholders of approximately \$23.7 million. In addition, Trustmark paid off Reliance Preferred Stock of \$1.1 million bringing the total consideration paid to \$24.8 million.

The merger with Reliance was consistent with Trustmark's strategic plan to selectively expand the Trustmark franchise and enhance the Trustmark franchise in north Alabama.

This merger was accounted for in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 805, "Business Combinations." Accordingly, the assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the merger date.

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The statement of assets purchased and liabilities assumed in the Reliance merger is presented below at their estimated fair values as of the merger date of April 7, 2017 (\$ in thousands):

Assets:	
Cash and due from banks	\$5,013
Federal funds sold and securities purchased under reverse repurchase agreements	6,900
Securities	54,843
Acquired loans	117,447
Premises and equipment, net	3,700
Identifiable intangible assets	1,850
Other real estate	475
Other assets	6,037
<b>Total assets</b>	<b>196,265</b>
Liabilities:	
Deposits	166,158
Other borrowings	17,469
Other liabilities	1,322
<b>Total liabilities</b>	<b>184,949</b>
<b>Net identifiable assets acquired at fair value</b>	<b>11,316</b>
Goodwill	13,471
<b>Total consideration paid</b>	<b>\$24,787</b>

The excess of the consideration paid over the estimated fair value of the net assets acquired was \$13.5 million, which was recorded as goodwill under FASB ASC Topic 805. The identifiable intangible assets acquired represent the core deposit intangible at fair value at the merger date. The core deposit intangible is being amortized on an accelerated basis over the estimated useful life, currently expected to be approximately ten years.

Loans acquired from Reliance were evaluated under a fair value process. Loans with evidence of deterioration in credit quality and for which it was probable at acquisition that Trustmark would not be able to collect all contractually required payments are referred to as acquired impaired loans and accounted for in accordance with FASB ASC Topic 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality." See Note 5 – Acquired Loans for additional information on acquired loans.

The operations of Reliance are included in Trustmark's operating results from April 7, 2017 and did not have a material impact on Trustmark's results of operations. During the second quarter of 2017, Trustmark included merger transaction expenses in other noninterest expense totaling \$3.2 million (change in control expense of \$1.3 million; professional fees, contract termination and other expenses of \$1.9 million).

#### Fair Value of Acquired Financial Instruments

For financial instruments measured at fair value, Trustmark utilized inputs within Level 2 of the fair value hierarchy to determine the fair value of securities available for sale (included in securities above), time deposits (included in deposits above) and FHLB advances (included in other borrowings above). Level 3 inputs were used to determine the fair value of acquired loans, identifiable intangible assets and other real estate. The methodology and significant assumptions used in estimating the fair values of these financial assets and liabilities are as follows:

Securities Available for Sale

Estimated fair values for securities available for sale are based on quoted market prices where available. If quoted market prices are not available, estimated fair values are based on quoted market prices of comparable instruments.

Acquired Loans

Fair value of acquired loans is determined using a discounted cash flow model based on assumptions regarding the amount and timing of principal and interest payments, estimated prepayments, estimated default rates, estimated loss severity in the event of default and current market rates.

#### Identifiable Intangible Assets

The fair value assigned to the identifiable intangible assets, in this case the core deposit intangible, represents the future economic benefits of the potential cost savings from acquiring core deposits in the merger compared to the cost of obtaining alternative funding from market sources.

#### Other Real Estate

Other real estate was initially recorded at its estimated fair value on the merger date based on independent appraisals less estimated selling costs.

#### Time Deposits

Time deposits were valued by projecting expected cash flows into the future based on each account's contracted rate and then determining the present value of those expected cash flows using current rates for deposits with similar maturities.

#### FHLB Advances

FHLB advances were valued by projecting expected cash flows into the future based on each advance's contracted rate and then determining the present value of those expected cash flows using current rates for advances with similar maturities.

Please refer to Note 17 – Fair Value for more information on Trustmark's classification of financial instruments based on valuation inputs within the fair value hierarchy.



## Note 3 – Securities Available for Sale and Held to Maturity

The following tables are a summary of the amortized cost and estimated fair value of securities available for sale and held to maturity at June 30, 2018 and December 31, 2017 (\$ in thousands):

	Securities Available for Sale				Securities Held to Maturity			
	Amortized Cost	Gross Gains	Gross Losses	Estimated Fair Value	Amortized Cost	Gross Gains	Gross Losses	Estimated Fair Value
June 30, 2018								
U.S. Government agency obligations	\$37,384	\$ 161	\$(1,131 )	\$36,414	\$3,714	\$ 89	\$—	\$3,803
Obligations of states and political subdivisions	64,986	408	(46 )	65,348	42,458	577	(101 )	42,934
Mortgage-backed securities								
Residential mortgage pass-through securities								
Guaranteed by GNMA	62,747	124	(2,626 )	60,245	12,756	39	(291 )	12,504
Issued by FNMA and FHLMC	753,124	192	(25,882 )	727,434	123,377	22	(3,979 )	119,420
Other residential mortgage-backed securities								
Issued or guaranteed by FNMA, FHLMC or GNMA	925,705	166	(28,220 )	897,651	627,470	40	(23,956 )	603,554
Commercial mortgage-backed securities								
Issued or guaranteed by FNMA, FHLMC or GNMA	191,538	200	(4,155 )	187,583	176,070	63	(3,710 )	172,423
Total	\$2,035,484	\$ 1,251	\$(62,060 )	\$1,974,675	\$985,845	\$ 830	\$(32,037 )	\$954,638
December 31, 2017								
	\$45,763	\$ 322	\$(800 )	\$45,285	\$3,692	\$ 182	\$—	\$3,874

U.S. Government agency obligations								
Obligations of states and political subdivisions	78,433	850	(54 )	79,229	46,039	1,044	(59 )	47,024
Mortgage-backed securities								
Residential mortgage pass-through securities								
Guaranteed by GNMA	66,634	215	(1,103 )	65,746	13,539	207	(73 )	13,673
Issued by FNMA and FHLMC	824,872	827	(11,249 )	814,450	133,975	210	(1,559 )	132,626
Other residential mortgage-backed securities								