

INTERNATIONAL BANCSHARES CORP  
Form 10-Q  
May 08, 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 March 31, 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 000-09439

INTERNATIONAL BANCSHARES CORPORATION

(Exact name of registrant as specified in its charter)

Texas

74-2157138

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

1200 San Bernardo Avenue, Laredo, Texas 78042-1359

(Address of principal executive offices)

(Zip Code)

(956) 722-7611

(Registrant's telephone number, including area code)

None

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 if the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a 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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date

Class	Shares Issued and Outstanding
Common Stock, \$1.00 par value	66,111,459 shares outstanding at May 4, 2018

## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Condition (Unaudited)

(Dollars in Thousands)

	March 31, 2018	December 31, 2017
Assets		
Cash and cash equivalents	\$ 254,622	\$ 265,357
Investment securities:		
Held to maturity debt securities (Market value of \$2,400 on March 31, 2018 and \$2,400 on December 31, 2017)	2,400	2,400
Available for sale debt securities (Amortized cost of \$3,955,525 on March 31, 2018 and \$4,196,263 on December 31, 2017)	3,868,173	4,124,185
Equity securities with readily determinable fair values	27,301	27,885
Total investment securities	3,897,874	4,154,470
Loans	6,453,103	6,348,172
Less allowance for probable loan losses	(67,154)	(67,687)
Net loans	6,385,949	6,280,485
Bank premises and equipment, net	511,696	514,454
Accrued interest receivable	32,773	34,456
Other investments	558,410	571,415
Goodwill	282,532	282,532
Other assets	146,756	81,529
Total assets	\$ 12,070,612	\$ 12,184,698

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Condition, continued (Unaudited)

(Dollars in Thousands)

	March 31, 2018	December 31, 2017
Liabilities and Shareholders' Equity		
Liabilities:		
Deposits:		
Demand—non-interest bearing	\$ 3,439,357	\$ 3,243,255
Savings and interest bearing demand	3,393,766	3,245,131
Time	2,021,789	2,056,506
Total deposits	8,854,912	8,544,892
Securities sold under repurchase agreements	258,953	353,805
Other borrowed funds	831,600	1,195,225
Junior subordinated deferrable interest debentures	160,416	160,416
Other liabilities	133,473	91,380
Total liabilities	10,239,354	10,345,718
Shareholders' equity:		
Common shares of \$1.00 par value. Authorized 275,000,000 shares; issued 96,019,028 shares on March 31, 2018 and 95,910,143 shares on December 31, 2017	96,044	96,019
Surplus	172,416	171,816
Retained earnings	1,923,411	1,891,805
Accumulated other comprehensive loss (including \$0 on March 31, 2018 and \$(3,287) on December 31, 2017 of comprehensive loss related to other-than-temporary impairment for non-credit related issues)	(68,350)	(28,397)
	2,123,521	2,131,243
Less cost of shares in treasury, 29,939,545 shares on March 31, 2018 and 29,934,675 on December 31, 2017	(292,263)	(292,263)
Total shareholders' equity	1,831,258	1,838,980
Total liabilities and shareholders' equity	\$ 12,070,612	\$ 12,184,698

See accompanying notes to consolidated financial statements.

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Income (Unaudited)

(Dollars in Thousands, except per share data)

	Three Months Ended March 31,	
	2018	2017
Interest income:		
Loans, including fees	\$ 87,833	\$ 75,401
Investment securities:		
Taxable	21,214	19,006
Tax-exempt	2,195	2,491
Other interest income	165	83
Total interest income	111,407	96,981
Interest expense:		
Savings deposits	2,228	1,289
Time deposits	2,669	2,376
Securities sold under repurchase agreements	1,023	3,068
Other borrowings	4,689	1,263
Junior subordinated deferrable interest debentures	1,526	1,250
Total interest expense	12,135	9,246
Net interest income	99,272	87,735
Provision for probable loan losses	1,662	1,700
Net interest income after provision for probable loan losses	97,610	86,035
Non-interest income:		
Service charges on deposit accounts	17,712	17,906
Other service charges, commissions and fees		
Banking	11,122	10,385
Non-banking	1,360	1,335
Investment securities transactions, net	—	927
Other investments, net	4,726	4,268
Other income	4,055	2,894
Total non-interest income	\$ 38,975	\$ 37,715



## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Income, continued (Unaudited)

(Dollars in Thousands, except per share data)

	Three Months Ended	
	March 31,	
	2018	2017
Non-interest expense:		
Employee compensation and benefits	\$ 34,618	\$ 32,730
Occupancy	6,075	5,991
Depreciation of bank premises and equipment	6,273	6,227
Professional fees	2,572	3,716
Deposit insurance assessments	1,000	390
Net expense, other real estate owned	(271)	914
Amortization of identified intangible assets	—	25
Advertising	1,839	2,268
Early termination fee—securities sold under repurchase agreements	—	5,765
Software and software maintenance	4,072	3,791
Other	12,731	13,809
Total non-interest expense	68,909	75,626
Income before income taxes	67,676	48,124
Provision for income taxes	14,256	16,120
Net income	\$ 53,420	\$ 32,004
Basic earnings per common share:		
Weighted average number of shares outstanding	66,092,379	65,994,201
Net income	\$ 0.81	\$ .48
Fully diluted earnings per common share:		
Weighted average number of shares outstanding	66,863,895	66,747,499
Net income	\$ 0.80	\$ .48



See accompanying notes to consolidated financial statements

4

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## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Comprehensive Income (Unaudited)

(Dollars in Thousands)

	Three Months Ended March 31,	
	2018	2017
Net income	\$ 53,420	\$ 32,004
Other comprehensive income, net of tax:		
Net unrealized holding gains (losses) on securities available for sale arising during period (net of tax effects of \$(9,427) and \$7,198)	(39,953)	13,369
Reclassification adjustment for losses on securities available for sale included in net income (net of tax effects of \$0, and \$(324))	—	(603)
	(39,953)	12,766
Comprehensive income	\$ 13,467	\$ 44,770

See accompanying notes to consolidated financial statements.

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Cash Flows (Unaudited)

(Dollars in Thousands)

	Three Months Ended March 31,	
	2018	2017
Operating activities:		
Net income	\$ 53,420	\$ 32,004
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for probable loan losses	1,662	1,700
Specific reserve, other real estate owned	71	45
Depreciation of bank premises and equipment	6,273	6,227
Gain on sale of bank premises and equipment	(8)	(15)
Gain on sale of other real estate owned	(2)	(4)
Accretion of investment securities discounts	(75)	(120)
Amortization of investment securities premiums	5,700	7,021
Investment securities transactions, net	—	(927)
Unrealized loss on equity securities with readily determinable fair values	774	—
Amortization of identified intangible assets	—	25
Stock based compensation expense	185	268
Earnings from affiliates and other investments	(4,303)	(2,890)
Deferred tax expense	269	229
Increase in accrued interest receivable	1,683	2,047
(Increase) decrease in other assets	(42,473)	3,794
Net increase in other liabilities	30,001	14,990
Net cash provided by operating activities	53,177	64,394
Investing activities:		
Proceeds from maturities of securities	1,075	—
Proceeds from sales and calls of available for sale securities	18,145	121,549
Purchases of available for sale securities	(1,075)	(385,594)
Principal collected on mortgage backed securities	188,893	187,386
Net increase in loans	(107,206)	(46,999)
Purchases of other investments	(17,963)	(2,903)
Distributions from other investments	5,367	4,557
Purchases of bank premises and equipment	(3,519)	(3,962)
Proceeds from sales of bank premises and equipment	12	681

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Proceeds from sales of other real estate owned	376	205
Net cash provided by (used in) investing activities	\$ 84,105	\$ (125,080)

6

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## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

## Consolidated Statements of Cash Flows, continued (Unaudited)

(Dollars in Thousands)

	Three Months Ended March 31,	
	2018	2017
Financing activities:		
Net increase in non-interest bearing demand deposits	\$ 196,102	\$ 197,317
Net increase in savings and interest bearing demand deposits	148,635	82,579
Net decrease in time deposits	(34,717)	(25,667)
Net decrease in securities sold under repurchase agreements	(94,852)	(195,208)
Net (decrease) increase in other borrowed funds	(363,625)	29,625
Purchase of treasury stock	—	(97)
Proceeds from stock transactions	440	744
Net cash (used in) provided by financing activities	(148,017)	89,293
(Decrease ) increase in cash and cash equivalents	(10,735)	28,607
Cash and cash equivalents at beginning of period	265,357	269,198
Cash and cash equivalents at end of period	\$ 254,622	\$ 297,805
Supplemental cash flow information:		
Interest paid	\$ 12,052	\$ 10,411
Income taxes paid	—	—
Non-cash investing and financing activities:		
Net transfers from loans to other real estate owned	80	9
Dividends declared, not yet paid on common stock	\$ 21,814	\$ 21,793

See accompanying notes to consolidated financial statements.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

Note 1 — Basis of Presentation

The accounting and reporting policies of International Bancshares Corporation (the “Corporation”) and Subsidiaries (the Corporation and Subsidiaries collectively referred to herein as the “Company”) conform to accounting principles generally accepted in the United States of America and to general practices within the banking industry. The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiaries, International Bank of Commerce, Laredo (“IBC”), Commerce Bank, International Bank of Commerce, Zapata, International Bank of Commerce, Brownsville, International Bank of Commerce, Oklahoma and the Corporation’s wholly-owned non-bank subsidiaries, IBC Subsidiary Corporation, IBC Trading Company, Premier Tierra Holdings, Inc., IBC Charitable and Community Development Corporation, and IBC Capital Corporation. All significant inter-company balances and transactions have been eliminated in consolidation. The consolidated financial statements are unaudited, but include all adjustments, which, in the opinion of management, are necessary for a fair presentation of the results of the periods presented. All such adjustments were of a normal and recurring nature. These financial statements should be read in conjunction with the financial statements and the notes thereto in the Company’s latest Annual Report on Form 10-K. The consolidated statement of condition at December 31, 2017 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. Certain reclassifications have been made to make prior periods comparable. Operating results for the three months ended March 31, 2018 are not necessarily indicative of the results for the year ending December 31, 2018 or any future period.

The Company operates as one segment. The operating information used by the Company’s chief executive officer for purposes of assessing performance and making operating decisions about the Company is the consolidated statements presented in this report. The Company has five active operating subsidiaries, namely, the bank subsidiaries, known as International Bank of Commerce, Laredo, Commerce Bank, International Bank of Commerce, Zapata, International Bank of Commerce, Brownsville and International Bank of Commerce, Oklahoma. The Company applies the provisions of Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”), FASB ASC 280, “Segment Reporting,” in determining its reportable segments and related disclosures.

The Company has evaluated all events or transactions that occurred through the date the Company issued these financial statements. During this period, the Company did not have any material recognizable or non-recognizable subsequent events.

On January 1, 2018, the Company adopted the provisions of ASU 2016-01, “Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities,” and ASU 2018-03, “Technical Corrections and Improvements to Financial Instruments – Overall,” which affects current US GAAP as it relates to the accounting for equity investments, financial liability under the fair value option, and the presentation and disclosure requirements for financial instruments. ASU 2016-01 also supersedes the guidance that requires: (i) the classification of equity securities with readily determinable fair values into different categories, and (ii) recognition in changes in fair value of available-for-sale securities in other comprehensive income. The main effect resulting from the adoption of the new standards is that beginning on January 1, 2018, equity securities with readily determinable fair values are now reported in a single line item on the face of the Company’s consolidated statement of condition under the caption, “Equity securities with readily determinable fair values.” Additionally, the changes in fair value of the equity securities is now recognized in net income and is included in other non-interest expense on the face of the Company’s consolidated income statement. Prior to January 1, 2018, the equity securities were classified as available-for-sale and stated at fair value with unrealized gains and losses included in accumulated comprehensive income, net of tax and had a net unrealized loss of \$189,000. Other equity securities without readily determinable fair values are recorded at cost less any impairment, if any and included in other investments in the Company’s consolidated financial statements.

On January 1, 2018, the Company adopted the provisions of ASU 2014-09 to ASC 606, “Revenue from Contracts with Customers.” ASC 606 sets a common standard that defines revenue and the principals for recognizing revenue. The core principle of the accounting standards update requires an entity to recognize revenue in a manner that reflects the consideration that an entity is expected to receive in exchange for goods or services as performance obligations are satisfied. The Company’s revenue is primarily comprised of net interest income on financial assets and financial liabilities, which is explicitly excluded from the scope of ASC 606. The Company has evaluated the impact of the accounting standards update on certain other non-interest revenue streams that the provisions of the update apply to and has determined that the adoption of the new provisions to ASC 606 did not have a significant impact to the Company’s consolidated financial statements or operations.

## Note 2 — Fair Value Measurements

ASC Topic 820, “Fair Value Measurements and Disclosures” (“ASC 820”), defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. ASC 820 applies to all financial instruments that are being measured and reported on a fair value basis. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date; it also establishes a fair value hierarchy that prioritizes the inputs used in valuation methodologies into the following three levels:

- Level 1 Inputs - Unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2 Inputs - Observable inputs other than Level 1 inputs, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Inputs - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or other valuation techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy is set forth below.

The following table represents assets and liabilities reported on the consolidated balance sheets at their fair value on a recurring basis as of March 31, 2018 by level within the fair value measurement hierarchy:

Fair Value Measurements at  
Reporting Date Using  
(in Thousands)



	Assets/Liabilities Measured at Fair Value March 31, 2018	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Measured on a recurring basis:				
Assets:				
Available for sale debt securities:				
Residential mortgage-backed securities	\$ 3,656,083	\$ —	\$ 3,656,083	\$ —
States and political subdivisions	212,090	—	212,090	—
Equity securities	27,301	27,301	—	—
	\$ 3,895,474	\$ 27,301	\$ 3,868,173	\$ —

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The following table represents assets and liabilities reported on the consolidated balance sheets at their fair value on a recurring basis as of December 31, 2017 by level within the fair value measurement hierarchy:

	Assets/Liabilities Measured at Fair Value December 31, 2017	Fair Value Measurements at Reporting Date Using (in Thousands)		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Measured on a recurring basis:				
Assets:				
Available for sale securities				
Residential mortgage - backed securities	\$ 3,891,233	\$ —	\$ 3,891,233	\$ —
States and political subdivisions	232,951	—	232,951	—
Equity Securities	27,886	27,886	—	—
	\$ 4,152,070	\$ 27,886	\$ 4,124,184	\$ —

Available-for-sale debt securities are classified within Level 2 of the valuation hierarchy. Equity securities with readily determinable fair values are classified within Level 1. For debt investments classified as Level 2 in the fair value hierarchy, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things.

Certain financial assets and financial liabilities are measured at fair value on a non-recurring basis. The instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

The following table represents financial instruments measured at fair value on a non-recurring basis as of and for the period ended March 31, 2018 by level within the fair value measurement hierarchy:

Fair Value Measurements at Reporting Date Using (in thousands)  
Quoted

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	Assets/Liabilities Measured at	Prices in Active	Significant		Net Provision (Credit) During Period
	Fair Value Period ended March 31, 2018	Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Measured on a non-recurring basis:					
Assets:					
Impaired loans	\$ 23,404	\$ —	\$ —	\$ 23,404	\$ 8,907
Other real estate owned	63	—	—	63	71

10

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The following table represents financial instruments measured at fair value on a non-recurring basis as of and for the period ended December 31, 2017 by level within the fair value measurement hierarchy:

	Assets/Liabilities Measured at	Fair Value Measurements at Reporting Date Using (in thousands)			Net (Credit) Provision During Period
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Measured on a non-recurring basis:	Fair Value Year ended December 31, 2017	Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Net (Credit) Provision During Period
Assets:					
Impaired loans	\$ 11,210	\$ —	\$ —	\$ 11,210	\$ 2,138
Other real estate owned	2,000	—	—	2,000	710

The Company's assets measured at fair value on a non-recurring basis are limited to impaired loans and other real estate owned. Impaired loans are classified within Level 3 of the valuation hierarchy. The fair value of impaired loans is derived in accordance with FASB ASC 310, "Receivables". Impaired loans are primarily comprised of collateral-dependent commercial loans. As the primary sources of loan repayments decline, the secondary repayment source, the collateral, takes on greater significance. Correctly evaluating the fair value becomes even more important. Re-measurement of the impaired loan to fair value is done through a specific valuation allowance included in the allowance for probable loan losses. The fair value of impaired loans is based on the fair value of the collateral, as determined through either an appraisal or evaluation process. The basis for the Company's appraisal and appraisal review process is based on regulatory guidelines and strives to comply with all regulatory appraisal laws, regulations, and the Uniform Standards of Professional Appraisal Practice. All appraisals and evaluations are "as is" (the property's highest and best use) valuations based on the current conditions of the property/project at that point in time. The determination of the fair value of the collateral is based on the net realizable value, which is the appraised value less any closing costs, when applicable. As of March 31, 2018, the Company had \$56,826,000 of impaired commercial collateral dependent loans, of which \$20,687,000 had an appraisal performed within the immediately preceding twelve months, and of which \$29,897,000 had an evaluation performed within the immediately preceding twelve months. As of December 31, 2017, the Company had \$53,267,000 of impaired commercial collateral dependent loans, of which \$18,585,000 had an appraisal performed within the immediately preceding twelve months and of which \$0 had an evaluation performed within the immediately preceding twelve months.

The determination to either seek an appraisal or to perform an evaluation begins in weekly credit quality meetings, where the committee analyzes the existing collateral values of the impaired loans and where obsolete appraisals are identified. In order to determine whether the Company would obtain a new appraisal or perform an internal evaluation to determine the fair value of the collateral, the credit committee reviews the existing appraisal to determine if the collateral value is reasonable in view of the current use of the collateral and the economic environment related to the collateral. If the analysis of the existing appraisal does not find that the collateral value is

reasonable under the current circumstances, the Company would obtain a new appraisal on the collateral or perform an internal evaluation of the collateral. The ultimate decision to get a new appraisal rests with the independent credit administration group. A new appraisal is not required if an internal evaluation, as performed by in-house experts, is able to appropriately update the original appraisal assumptions to reflect current market conditions and provide an estimate of the collateral's market value for impairment analysis. The internal evaluations must be in writing and contain sufficient information detailing the analysis, assumptions and conclusions, and they must support performing an evaluation in lieu of ordering a new appraisal.

Other real estate owned is comprised of real estate acquired by foreclosure and deeds in lieu of foreclosure. Other real estate owned is carried at the lower of the recorded investment in the property or its fair value less estimated costs to sell such property (as determined by independent appraisal) within Level 3 of the fair value hierarchy. Prior to foreclosure, the value of the underlying loan is written down to the fair value of the real estate to be acquired by a charge to the allowance for probable loan losses, if necessary. The fair value is reviewed periodically and subsequent write-

downs are made, accordingly, through a charge to operations. Other real estate owned is included in other assets on the consolidated financial statements. For the three months ended March 31, 2018 and the twelve months ended December 31, 2017, the Company recorded \$24,000 and \$30,000 respectively, in charges to the allowance for probable loan losses in connection with loans transferred to other real estate owned. For the three months ended March 31, 2018 and the twelve months ended December 31, 2017, the Company recorded \$71,000 and \$710,000, respectively, in adjustments to fair value in connection with other real estate owned.

The fair value estimates, methods, and assumptions for the Company's financial instruments at March 31, 2018 and December 31, 2017 are outlined below.

#### Cash and Cash Equivalents

For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

#### Time Deposits with Banks

The carrying amounts of time deposits with banks approximate fair value.

#### Investment Securities Held-to-Maturity

The carrying amounts of investments held-to-maturity approximate fair value.

#### Investment Securities

For investment securities, which include U.S. Treasury securities, obligations of other U.S. government agencies, obligations of states and political subdivisions and mortgage pass through and related securities, fair values are from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things. See disclosures of fair value of investment securities in Note 6.

## Loans

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type, such as commercial, real estate and consumer loans, as outlined by regulatory reporting guidelines. Each category is segmented into fixed and variable interest rate terms and by performing and non-performing categories.

For variable rate performing loans, the carrying amount approximates the fair value. For fixed-rate performing loans, except residential mortgage loans, the fair value is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan. For performing residential mortgage loans, fair value is estimated by discounting contractual cash flows adjusted for prepayment estimates using discount rates based on secondary market sources or the primary origination market. Fixed-rate performing loans are within Level 3 of the fair value hierarchy. At March 31, 2018, and December 31, 2017, the carrying amount of fixed-rate performing loans was \$1,540,426,000 and \$1,505,531,000, respectively, and the estimated fair value was \$1,491,579,000 and \$1,454,434,000, respectively.

## Accrued Interest

The carrying amounts of accrued interest approximate fair value.

## Deposits

The fair value of deposits with no stated maturity, such as non-interest bearing demand deposit accounts, savings accounts and interest bearing demand deposit accounts, was equal to the amount payable on demand as of March

31, 2018 and December 31, 2017. The fair value of time deposits is based on the discounted value of contractual cash flows. The discount rate is based on currently offered rates. Time deposits are within Level 3 of the fair value hierarchy. At March 31, 2018 and December 31, 2017, the carrying amount of time deposits was \$2,021,789,000 and \$2,056,506,000, respectively, and the estimated fair value was \$2,024,312,000 and \$2,058,621,000, respectively.

#### Securities Sold Under Repurchase Agreements

Securities sold under repurchase agreements include short- and long-term maturities. Due to the contractual terms of the short-term instruments, the carrying amounts approximated fair value at March 31, 2018 and December 31, 2017. The fair value of the long-term instruments is based on established market spreads using option adjusted spread methodology. Long-term repurchase agreements are within Level 3 of the fair value hierarchy. The only remaining long-term repurchase agreement outstanding matured in the first quarter of 2018 and was not renewed. At December 31, 2017, the carrying amount of long-term repurchase agreements was \$100,000,000 and the estimated fair value was \$99,504,000.

#### Junior Subordinated Deferrable Interest Debentures

The Company currently has floating-rate junior subordinated deferrable interest debentures outstanding. Due to the contractual terms of the floating-rate junior subordinated deferrable interest debentures, the carrying amounts approximated fair value at March 31, 2018 and December 31, 2017.

#### Other Borrowed Funds

The Company currently has short and long-term borrowings issued from the Federal Home Loan Bank ("FHLB"). Due to the contractual terms of the short-term borrowings, the carrying amounts approximated fair value at March 31, 2018 and December 31, 2017. The long-term borrowings outstanding at March 31, 2018 are fixed-rate borrowings and the fair value is based on established market spreads for similar types of borrowings. The fixed rate long-term borrowings are included in Level 2 of the fair value hierarchy. At March 31, 2018 and December 31, 2017, the carrying amount of the fixed rate long-term FHLB borrowings was \$300,000,000 and \$250,000,000, respectively, and the estimated fair value was \$298,355,900 and \$249,728,000, respectively.

#### Commitments to Extend Credit and Letters of Credit



Commitments to extend credit and fund letters of credit are principally at current interest rates, and, therefore, the carrying amount approximates fair value.

#### Limitations

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

Fair value estimates are based on existing on- and off-statement of condition financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Other significant assets and liabilities that are not considered financial assets or liabilities include the bank premises and equipment and core deposit value. In addition, the tax ramifications related to the effect of fair value estimates have not been considered in the above estimates.

## Note 3 — Loans

A summary of loans, by loan type at March 31, 2018 and December 31, 2017 is as follows:

	March 31, 2018	December 31, 2017
	(Dollars in Thousands)	
Commercial, financial and agricultural	\$ 3,394,251	\$ 3,322,668
Real estate - mortgage	1,128,934	1,133,525
Real estate - construction	1,725,629	1,683,550
Consumer	46,778	49,543
Foreign	157,511	158,886
Total loans	\$ 6,453,103	\$ 6,348,172

## Note 4 — Allowance for Probable Loan Losses

The allowance for probable loan losses primarily consists of the aggregate loan loss allowances of the bank subsidiaries. The allowances are established through charges to operations in the form of provisions for probable loan losses. Loan losses or recoveries are charged or credited directly to the allowances. The allowance for probable loan losses of each bank subsidiary is maintained at a level considered appropriate by management, based on estimated probable losses in the loan portfolio. The allowance for probable loan losses is derived from the following elements: (i) allowances established on specific impaired loans, which are based on a review of the individual characteristics of each loan, including the customer's ability to repay the loan, the underlying collateral values, and the industry in which the customer operates; (ii) allowances based on actual historical loss experience for similar types of loans in the Company's loan portfolio; and (iii) allowances based on general economic conditions, changes in the mix of loans, company resources, border risk and credit quality indicators, among other things. All segments of the loan portfolio continue to be impacted by the prolonged economic recovery. Loans secured by real estate could be impacted negatively by the continued economic environment and resulting decrease in collateral values. Consumer loans may be impacted by continued and prolonged unemployment rates.

The Company's management continually reviews the allowance for loan losses of the bank subsidiaries using the amounts determined from the allowances established on specific impaired loans, the allowance established on quantitative historical loss percentages, and the allowance based on qualitative data to establish an appropriate amount to maintain in the Company's allowance for loan losses. Should any of the factors considered by management in evaluating the adequacy of the allowance for probable loan losses change, the Company's estimate of probable loan losses could also change, which could affect the level of future provisions for probable loan losses. While the calculation of the allowance for probable loan losses utilizes management's best judgment and all information reasonably available, the adequacy of the allowance is dependent on a variety of factors beyond the Company's control, including, among other things, the performance of the entire loan portfolio, the economy, changes in interest

rates and the view of regulatory authorities towards loan classifications.

The loan loss provision is determined using the following methods. On a weekly basis, loan past due reports are reviewed by the credit quality committee to determine if a loan has any potential problems and if a loan should be placed on the Company's internal classified report. Additionally, the Company's credit department reviews the majority of the Company's loans for proper internal classification purposes, regardless of whether they are past due, and segregates any loans with potential problems for further review. The credit department will discuss the potential problem loans with the servicing loan officers to determine any relevant issues that were not discovered in the evaluation. Also, an analysis of loans that is provided through examinations by regulatory authorities is considered in the review process. After the above analysis is completed, the Company determines if a loan should be placed on an internal classified report because of issues related to the analysis of the credit, credit documents, collateral and/or payment history.

A summary of the transactions in the allowance for probable loan losses by loan class is as follows:

Three Months Ended March 31, 2018									
	Domestic							Foreign	
	Commercial Real Estate: Other	Commercial Real Estate: Construction Land	Commercial Real Estate: Farmland & Commercial	Commercial Real Estate: Multifamily	Commercial Real Estate: First Lien	Commercial Real Estate: Residential: Junior Lien	Commercial Real Estate: Residential: Consumer	Commercial Real Estate: Residential: Foreign	Commercial Real Estate: Residential: Total
	Commercial	Development	Commercial	Multifamily	First Lien	Junior Lien	Consumer	Foreign	Total
	(Dollars in Thousands)								
Balance at December 31,	\$ 27,905	\$ 11,675	\$ 16,663	\$ 1,109	\$ 2,950	\$ 6,103	\$ 440	\$ 842	\$ 67,687
Provision charged to allowance	(2,715)	(1)	—	—	(14)	(30)	(117)	—	(2,877)
Recoveries credited to allowance	583	2	18	—	1	66	12	—	682
Net (losses) recoveries charged to allowance	(2,132)	1	18	—	(13)	36	(105)	—	(2,195)
Provision charged to operations	(5,082)	122	8,122	(162)	69	(1,450)	102	(59)	1,662
Balance at March 31,	\$ 20,691	\$ 11,798	\$ 24,803	\$ 947	\$ 3,006	\$ 4,689	\$ 437	\$ 783	\$ 67,154

Three Months Ended March 31, 2017									
	Domestic							Foreign	
	Commercial Real Estate: Other	Commercial Real Estate: Construction Land	Commercial Real Estate: Farmland & Commercial	Commercial Real Estate: Multifamily	Commercial Real Estate: First Lien	Commercial Real Estate: Residential: Junior Lien	Commercial Real Estate: Residential: Consumer	Commercial Real Estate: Residential: Foreign	Commercial Real Estate: Residential: Total
	Commercial	Development	Commercial	Multifamily	First Lien	Junior Lien	Consumer	Foreign	Total
	(Dollars in Thousands)								
Balance at December 31,	\$ 25,649	\$ 13,889	\$ 16,731						