

MBT FINANCIAL CORP
Form 10-Q
August 09, 2016

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2016

Or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission File Number: 000-30973

MBT FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

Michigan **38-3516922**
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

102 E. Front Street

Monroe, Michigan 48161

(Address of principal executive offices)

(Zip Code)

(734) 241-3431

(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

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, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer", and "smaller accelerated filer" in Rule 12b-2 of the Exchange Act (check one).

Large accelerated filer Accelerated Filer
Non-accelerated filer Smaller reporting company

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 August 9, 2016, there were 22,732,586 shares of the Company's Common Stock outstanding.

Part I Financial Information**Item 1. Financial Statements****MBT FINANCIAL CORP.****CONSOLIDATED BALANCE SHEETS**

Dollars in thousands	June 30, 2016	December 31, 2015
	(Unaudited)	
ASSETS		
Cash and Cash Equivalents		
Cash and due from banks		
Non-interest bearing	\$ 15,529	\$ 14,996
Interest bearing	102,839	70,054
Total cash and cash equivalents	118,368	85,050
Securities - Held to Maturity	39,314	41,282
Securities - Available for Sale	429,057	496,859
Federal Home Loan Bank stock - at cost	4,148	4,148
Loans held for sale	919	1,477
Loans	638,280	617,308
Allowance for Loan Losses	(9,903)	(10,896)
Loans - Net	628,377	606,412
Accrued interest receivable and other assets	20,106	23,365
Other Real Estate Owned	1,808	2,383
Bank Owned Life Insurance	53,707	53,093
Premises and Equipment - Net	27,611	28,244
Total assets	\$ 1,323,415	\$ 1,342,313
LIABILITIES		
Deposits:		
Non-interest bearing	\$ 270,391	\$ 253,795
Interest-bearing	893,027	911,598
Total deposits	1,163,418	1,165,393

Repurchase agreements	-	15,000
Interest payable and other liabilities	14,374	14,579
Total liabilities	1,177,792	1,194,972
STOCKHOLDERS' EQUITY		
Common stock (no par value; 50,000,000 shares authorized, 22,728,558 and 22,790,707 shares issued and outstanding)	22,315	23,492
Retained earnings	120,633	126,214
Unearned compensation	(35)	(13)
Accumulated other comprehensive income (loss)	2,710	(2,352)
Total stockholders' equity	145,623	147,341
Total liabilities and stockholders' equity	\$ 1,323,415	\$ 1,342,313

The accompanying notes to consolidated financial statements are an integral part of these statements.

MBT FINANCIAL CORP.**CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME - UNAUDITED**

	Three Months		Six Months	
	Ended June 30,		Ended June 30,	
	2016	2015	2016	2015
Dollars in thousands, except per share data				
Interest Income				
Interest and fees on loans	\$7,179	\$7,154	\$14,214	\$14,586
Interest on investment securities-				
Tax-exempt	303	273	608	548
Taxable	2,218	2,436	4,744	4,864
Interest on balances due from banks	162	14	279	40
Total interest income	9,862	9,877	19,845	20,038
Interest Expense				
Interest on deposits	486	619	1,003	1,264
Interest on borrowed funds	132	177	308	351
Total interest expense	618	796	1,311	1,615
Net Interest Income	9,244	9,081	18,534	18,423
Provision For (Recovery Of) Loan Losses	(200)	-	(500)	(800)
Net Interest Income After Provision For Loan Losses	9,444	9,081	19,034	19,223
Other Income				
Income from wealth management services	1,105	1,191	2,202	2,413
Service charges and other fees	1,016	1,030	2,024	1,924
Debit card income	735	591	1,409	1,155
Net gain on sales and redemptions of securities available for sale	1,752	22	2,072	258
Net loss on sales of Other Real Estate Owned	(1)	(21)	(57)	(284)
Origination fees on mortgage loans sold	136	137	266	266
Bank owned life insurance income	362	362	717	633
Other	450	493	1,036	1,065
Total other income	5,555	3,805	9,669	7,430
Other Expenses				
Salaries and employee benefits	5,399	5,750	11,017	11,624
Occupancy expense	633	606	1,334	1,426
Equipment expense	726	790	1,410	1,524
Marketing expense	286	308	545	554
Professional fees	556	550	1,208	1,126
EFT/ATM Expense	237	118	546	208

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Other Real Estate Owned expenses	30	179	94	305
FDIC Deposit Insurance Assessment	191	429	360	843
Bonding and other insurance expense	214	227	336	457
Telephone expense	91	109	217	204
Other	509	664	1,288	1,278
Total other expenses	8,872	9,730	18,355	19,549
Income Before Income Taxes	6,127	3,156	10,348	7,104
Income Tax Expense	1,888	871	3,112	2,042
Net Income	\$4,239	\$2,285	\$7,236	\$5,062
Other Comprehensive Income - Net of Tax				
Unrealized gains (losses) on securities	2,049	(3,760)	6,376	(819)
Reclassification adjustment for gains included in net income	(1,156)	(15)	(1,367)	(171)
Postretirement benefit liability	26	26	53	53
Total Other Comprehensive Income (Loss) - Net of Tax	919	(3,749)	5,062	(937)
Comprehensive Income (Loss)	\$5,158	\$(1,464)	\$12,298	\$4,125
Basic Earnings Per Common Share	\$0.19	\$0.10	\$0.32	\$0.22
Diluted Earnings Per Common Share	\$0.18	\$0.10	\$0.31	\$0.22
Dividends Declared Per Share of Common Stock	\$0.03	\$-	\$0.56	\$-

The accompanying notes to consolidated financial statements are an integral part of these statements.

MBT FINANCIAL CORP.**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY - UNAUDITED**

Dollars in thousands	Accumulated				Total
	Common Stock	Retained Earnings	Unearned Compensation	Other Comprehensive Income (Loss)	
Balance - January 1, 2016	\$ 23,492	\$ 126,214	(13) \$ (2,352) \$ 147,341
Repurchase of Common Stock (192,080 shares)	(1,414)	-	-	-	(1,414)
Issuance of Common Stock					
SOSARs exercised (105,303 shares)	75	-	-	-	75
Restricted stock awards (5,000 shares)	41	-	(41)	-
Other stock issued (19,628 shares)	156	-	-	-	156
Equity Compensation	(35)	-	19	-	(16)
Dividends declared (\$0.56 per share)	-	(12,817)	-	-	(12,817)
Net income	-	7,236	-	-	7,236
Other comprehensive income - net of tax	-	-	-	5,062	5,062
Balance - June 30, 2016	\$ 22,315	\$ 120,633	(35) \$ 2,710	\$ 145,623

Dollars in thousands	Accumulated				Total
	Common Stock	Retained Earnings	Unearned Compensation	Other Comprehensive Income (Loss)	
Balance - January 1, 2015	\$ 23,037	\$ 114,132	\$ -	(2,633) \$ 134,536
Issuance of Common Stock					
SOSARs exercised (8,301 shares)	-	-	-	-	-
Restricted stock awards (6,000 shares)	35	-	(35)	-
Other stock issued (9,520 shares)	53	-	-	-	53

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Equity Compensation	145	-	5	-	150
Net income	-	5,062	-	-	5,062
Other comprehensive income - net of tax	-	-	-	(937) (937)
Balance - June 30, 2015	\$ 23,270	\$ 119,194	\$ (30) (3,570) \$ 138,864

The accompanying notes to consolidated financial statements are an integral part of these statements.

MBT FINANCIAL CORP.**CONSOLIDATED STATEMENTS OF CASH FLOWS - UNAUDITED**

	Six Months Ended	
	June 30,	
Dollars in thousands	2016	2015
Cash Flows from Operating Activities		
Net Income	\$7,236	\$5,062
Adjustments to reconcile net income to net cash from operating activities		
Recovery of loan losses	(500)	(800)
Depreciation	797	792
Decrease in deferred taxes	1,891	1,711
Net amortization of investment premium and discount	707	651
Writedowns of Other Real Estate Owned	69	369
Net decrease in interest payable and other liabilities	(125)	(270)
Net increase in interest receivable and other assets	(763)	(324)
Equity based compensation expense	59	150
Net gain on sale/settlement of securities	(2,072)	(258)
Increase in cash surrender value of life insurance	(614)	(548)
Net cash provided by operating activities	\$6,685	\$6,535
Cash Flows from Investing Activities		
Proceeds from maturities and redemptions of investment securities held to maturity	\$6,182	\$6,005
Proceeds from maturities and redemptions of investment securities available for sale	240,900	84,584
Proceeds from sales of investment securities available for sale	-	16,672
Net increase in loans	(21,338)	(13,715)
Proceeds from sales of other real estate owned	918	1,412
Proceeds from sales of other assets	171	75
Purchase of investment securities held to maturity	(4,259)	(8,707)
Purchase of investment securities available for sale	(164,098)	(130,248)
Purchase of bank premises and equipment	(793)	(684)
Net cash provided by (used for) investing activities	\$57,683	\$(44,606)
Cash Flows from Financing Activities		
Net increase (decrease) in deposits	\$(1,975)	\$9,469
Repayment of repurchase agreements	(15,000)	-
Proceeds from issuance of common stock	156	53
Repurchase of common stock	(1,414)	-
Dividends paid	(12,817)	-
Net cash provided by (used for) financing activities	\$(31,050)	\$9,522
Net Increase (Decrease) in Cash and Cash Equivalents	\$33,318	\$(28,549)
Cash and Cash Equivalents at Beginning of Period	85,050	52,122
Cash and Cash Equivalents at End of Period	\$118,368	\$23,573

Supplemental Cash Flow Information

Cash paid for interest	\$1,359	\$1,629
Cash paid for federal income taxes	\$1,220	\$331

Supplemental Schedule of Non Cash Investing Activities

Transfer of loans to other real estate owned	\$397	\$40
Transfer of loans to other assets	\$34	\$54

The accompanying notes to consolidated financial statements are an integral part of these statements.

MBT FINANCIAL CORP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. BASIS OF PRESENTATION AND ACCOUNTING POLICIES

The unaudited consolidated financial statements include the accounts of MBT Financial Corp. (the “Company”) and its subsidiary, Monroe Bank & Trust (the “Bank”). The Bank includes the accounts of its wholly owned subsidiary, MB&T Financial Services, Inc. The Bank operates fourteen branches in Monroe County, Michigan, six branches in Wayne County, Michigan, and one loan and wealth management office in each Wayne County and Lenawee County. The Bank’s primary source of revenue is from providing loans to customers, who are predominantly small and middle-market businesses and middle-income individuals. The Company’s sole business segment is community banking.

The accounting and reporting policies of the Bank conform to practice within the banking industry and are in accordance with accounting principles generally accepted in the United States. Preparation of financial statements in conformity with generally accepted accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant changes in the near term are the determination of the allowance for loan losses, the valuation of other real estate owned, and the fair value of investment securities.

The accompanying unaudited consolidated financial statements of the Company have been prepared in accordance with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. However, such information reflects all adjustments (consisting of normal recurring adjustments), which are, in the opinion of Management, necessary for fair statement of results for the interim periods.

The significant accounting policies are as follows:

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its subsidiary. All material intercompany transactions and balances have been eliminated.

COMPREHENSIVE INCOME

Accounting principles generally require that revenue, expenses, gains, and losses be included in net income. Certain changes in assets and liabilities, however, such as unrealized gains and losses on securities available for sale and amounts recognized related to postretirement benefit plans (gains and losses, prior service costs, and transition assets or obligations), are reported as a direct adjustment to the equity section of the balance sheet. Such items, along with net income, are components of comprehensive income.

BUSINESS SEGMENTS

While the Company's chief decision makers monitor the revenue streams of various products and services, operations are managed and financial performance is evaluated on a company wide basis. Accordingly, all of the Company's operations are considered by management to be aggregated in one reportable segment.

FAIR VALUE

The Company measures or monitors many of its assets and liabilities on a fair value basis. Fair value is used on a recurring basis for assets and liabilities that are elected to be accounted for under The Fair Value Option as well as for certain assets and liabilities in which fair value is the primary basis of accounting. Examples of these include derivative instruments and available for sale securities. Additionally, fair value is used on a non-recurring basis to evaluate assets or liabilities for impairment or for disclosure purposes. Examples of these non-recurring uses of fair value include certain loans held for sale accounted for on a lower of cost or market basis. Fair value is defined 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. Depending on the nature of the asset or liability, the Company uses various valuation techniques and assumptions when estimating fair value.

When determining the fair value measurements for assets and liabilities required or permitted to be recorded at and/or marked to fair value, the Company considers the principal or most advantageous market in which it would transact and considers assumptions that market participants would use when pricing the asset or liability. When possible, the Company looks to active and observable markets to price identical assets or liabilities. When identical assets and liabilities are not traded in active markets, the Company looks to market observable data for similar assets or liabilities. Nevertheless, certain assets and liabilities are not actively traded in observable markets and the Company must use alternative valuation techniques to derive a fair value measurement.

ACCOUNTING PRONOUNCEMENTS

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2014-09 (ASU 2014-09), "Revenue from Contracts with Customers (Topic 606)". ASU 2014-09 adopts a standardized approach for revenue recognition and was a joint effort with the International Accounting Standards Board (IASB). The new revenue recognition standard is based on a core principle of recognizing revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 does not apply to financial instruments. ASU 2014-09 is effective for public entities for reporting periods beginning after December 15, 2016 (therefore, for the year ending December 31, 2017 for the Corporation). Early implementation is not allowed for public companies. Management is currently assessing the impact to the Corporation's consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities". The amendments in ASU 2016-01 supersede the guidance to classify equity securities with readily determinable fair values into different categories (that is, trading or available-for-sale) and require equity securities (including other ownership interests, such as partnerships, unincorporated joint ventures, and limited liability companies) to be measured at fair value with changes in the fair value recognized through net income. The amendments allow equity investments that do not have readily determinable fair values to be re-measured at fair value either upon the occurrence of an observable price change or upon identification of an impairment. The amendments also require enhanced disclosures about those investments. The amendments improve financial reporting by providing relevant information about an entity's equity investments and reducing the number of items that are recognized in other comprehensive income. For public business entities, the

amendments in this update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The amendments should be applied by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The adoption of this guidance is not expected to have a material effect on the Company's financial position or results of operations.

In February 2016, the Financial Accounting Standards Board issued ASU 2016-02, "Leases", which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right of use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease footnote guidance will be effective for the Company's year ending December 31, 2019 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The effect of applying the new lease guidance on the financial statements as not yet been determined, however the new lease standard is not expected to have a significant effect on the Company's financial statements.

In June 2016, the Financial Accounting Standards Board issued ASU No. 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income.

ASU 2016-13 requires an entity measure expected credit losses for financial assets over the estimated lifetime of expected credit loss and record an allowance that, when deducted from the amortized cost basis of the financial asset, presents the net amount expected to be collected on the financial asset. The standard includes the following core concepts in determining the expected credit loss estimate: (a) be based on an asset's amortized cost (including premiums or discounts, net deferred fees and costs, foreign exchange and fair value hedge accounting adjustments), (b) reflect losses expected over the remaining contractual life of an asset (considering the effect of voluntary prepayments), (c) consider available relevant information about the estimated collectability of cash flows (including information about past events, current conditions, and reasonable and supportable forecasts), and (d) reflect the risk of loss, even when that risk is remote.

ASU 2016-13 also amends the recording of purchased credit-deteriorated assets. Under the new guidance, an allowance will be recognized at acquisition through a gross-up approach whereby an entity will record as the initial amortized cost the sum of (a) the purchase price and (b) an estimate of credit losses as of the date of acquisition. In addition, the guidance also requires immediate recognition in earnings any subsequent changes, both favorable and unfavorable, in expected cash flows by adjusting this allowance.

ASU 2016-13 amends the impairment model for available-for-sale debt securities and requires entities to determine whether all or a portion of the unrealized loss on an available-for-sale debt security is a credit loss. Management may not use the length of time a security has been in an unrealized loss position as a factor in concluding whether a credit loss exists, as is currently permitted. In addition, an entity will recognize an allowance for credit losses on available-for-sale debt securities as a contra-account to the amortized cost basis rather than as a direct reduction of the amortized cost basis of the investment, as is currently required. As a result, entities will recognize improvements to credit losses on available-for-sale debt securities immediately in earnings rather than as interest income over time under current practice.

New disclosures required by ASU 2016-13 include: (a) for financial assets measured at amortized cost, an entity will be required to disclose information about how it developed its allowance, including changes in the factors that influenced management's estimate of expected credit losses and the reasons for those changes, (b) for financial receivables and net investments in leases measured at amortized cost, an entity will be required to further disaggregate the information it currently discloses about the credit quality of these assets by year of the asset's origination or vintage for as many as five annual periods, and (c) for available-for-sale debt securities, an entity will be required to provide a roll-forward of the allowance for credit losses and an aging analysis for securities that are past due.

Upon adoption of ASU 2016-13, a cumulative-effect adjustment to retained earnings will be recorded as of the beginning of the first reporting period in which the guidance is effective. ASU 2016-13 is effective for public companies for interim and annual periods beginning after December 15, 2019, with early adoption permitted for annual periods beginning after December 15, 2018. The Corporation is currently evaluating the provisions of ASU 2016-13 to determine the potential impact on the Corporation's consolidated financial condition and results of operations.

2. EARNINGS PER SHARE

The calculations of earnings per common share are as follows:

	For the three months ended		For the six months ended	
	June 30, 2016	2015	June 30, 2016	2015
Basic				
Net income	\$4,239,000	\$2,285,000	\$7,236,000	\$5,062,000
Average common shares outstanding	22,884,350	22,733,739	22,869,453	22,727,825
Earnings per common share - basic	\$0.19	\$0.10	\$0.32	\$0.22
Diluted				
Net income	\$4,239,000	\$2,285,000	\$7,236,000	\$5,062,000
Average common shares outstanding	22,884,350	22,733,739	22,869,453	22,727,825
Equity compensation	165,368	197,805	160,385	190,172
Average common shares outstanding - diluted	23,049,718	22,931,544	23,029,838	22,917,997
Earnings per common share - diluted	\$0.18	\$0.10	\$0.31	\$0.22

3. STOCK BASED COMPENSATION

Stock Only Stock Appreciation Rights (SOSARs) - On February 25, 2016, 105,500 Stock Only Stock Appreciation Rights (SOSARs) were awarded to certain officers in accordance with the MBT 2008 Stock Incentive Plan that was approved by shareholders on May 1, 2008 and amended by shareholders on May 7, 2015. The SOSARs have a term of ten years and vest in three equal annual installments beginning on December 31, 2016. The fair value of \$3.08 for the SOSARs was estimated at the date of the grant, using the Black-Scholes option pricing model, with the following assumptions: expected option lives of 7 years, expected volatility of 41.21%, a risk free interest rate of 1.47% and dividend yield of 1.50%. The fair value of the Company's common stock was \$8.26 on the grant date.

SOSARs granted under the plan are structured as fixed grants with the base price equal to the market value of the underlying stock on the date of the grant.

The following table summarizes the SOSARs that have been granted:

SOSARs	Weighted Average
--------	---------------------

		Base Price
SOSARs Outstanding, January 1, 2016	609,275	\$ 4.02
Granted	105,500	8.26
Exercised	(197,723)	2.65
Forfeited	(4,503)	4.93
Expired	-	-
SOSARs Outstanding, June 30, 2016	512,549	\$ 5.41
SOSARs Exercisable, June 30, 2016	227,633	\$ 3.30

The exercise of a SOSAR results in the issuance of a number of shares of common stock of the Company based on the appreciation of the market price of the stock over the base price of the SOSAR. The market value of the Company's common stock on June 30, 2016 was \$8.00. The value of the exercisable SOSARs that are in-the-money as of June 30, 2016 was \$1,100,000, and exercise of those SOSARs on that date would have resulted in the issuance of 133,734 shares of common stock. The plan allows participants to elect to withhold shares from the exercise of SOSARs to cover their tax liability. This may affect the number of shares issued and the value of the common stock account on the balance sheet and the statement of changes in equity.

Restricted Stock Unit Awards – On February 25, 2016, 35,000 performance restricted stock units were awarded to certain key executive officers in accordance with the MBT 2008 Stock Incentive Plan that was approved by shareholders on May 1, 2008 and amended by shareholders on May 7, 2015. Each Restricted Stock Unit (RSU) is equivalent to one share of MBT Financial Corp. common stock. Stock will be issued to the participants following a two year performance period that ends on December 31, 2017 if the defined performance targets are achieved. Earned RSUs vest on December 15, 2018 and as of June 30, 2016 none of the RSUs were vested.

Restricted Stock Awards – On February 25, 2016, 5,000 restricted shares were awarded to certain non-executive members of the board of directors in accordance with the MBT 2008 Stock Incentive Plan that was approved by shareholders on May 1, 2008 and amended by shareholders on May 7, 2015. The restricted shares vest on December 31, 2016. The expense for the restricted stock is based on the grant date value of \$8.26 and is recognized over the vesting period. The unrecognized cost related to the non-vested restricted stock awards was \$28,000 as of June 30, 2016.

The total expense for equity based compensation was \$162,000 in the second quarter of 2016 and \$94,000 in the second quarter of 2015. The total expense for equity based compensation was \$276,000 in the first six months of 2016 and \$177,000 in the first six months of 2015.

4. LOANS

The Bank makes commercial, consumer, and mortgage loans primarily to customers in Monroe County, Michigan, southern and western Wayne County, Michigan, Lenawee County, Michigan, and surrounding areas. Although the Bank has a diversified loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent on the automotive, manufacturing, and real estate development economic sectors.

Loans consist of the following (000s omitted):

June 30,	December
	31,
2016	

	2015	
Residential real estate loans	\$215,236	\$213,989
Commercial and Construction real estate loans	264,126	259,139
Agriculture and agricultural real estate loans	21,164	19,243
Commercial and industrial loans	86,726	84,438
Loans to individuals for household, family, and other personal expenditures	51,028	40,499
Total loans, gross	\$638,280	\$617,308
Less: Allowance for loan losses	9,903	10,896
Net Loans	\$628,377	\$606,412

Loans are placed in a nonaccrual status when, in the opinion of Management, the collection of additional interest is doubtful. All loan relationships over \$250,000 that are classified by Management as nonperforming as well as selected performing accounts and all renegotiated loans are reviewed for impairment each quarter. Allowances for loans determined to be impaired are included in the allowance for loan losses. All cash received on nonaccrual loans is applied to the principal balance. Nonperforming assets consist of nonaccrual loans, loans 90 days or more past due, restructured loans, nonaccrual investment securities, other real estate owned, and other repossessed assets. Other real estate owned includes real estate that has been acquired in full or partial satisfaction of loan obligations or upon foreclosure.

The following table summarizes nonperforming assets (000s omitted):

	June30, 2016	December 31, 2015		
Nonaccrual loans	\$7,522	\$ 8,633		
Loans 90 days past due and accruing	41	4		
Restructured loans	16,701	18,910		
Total nonperforming loans	\$24,264	\$ 27,547		
Other real estate owned	1,808	2,383		
Other assets	10	-		
Total nonperforming assets	\$26,082	\$ 29,930		
Nonperforming assets to total assets	1.97	%	2.23	%
Allowance for loan losses to nonperforming loans	40.81	%	39.55	%

5. ALLOWANCE FOR LOAN LOSSES

The Company separates its loan portfolio into segments to perform the calculation and analysis of the allowance for loan losses. The six segments analyzed are Agriculture and Agricultural Real Estate, Commercial, Commercial Real Estate, Construction Real Estate, Residential Real Estate, and Consumer and Other. The Agriculture and Agricultural Real Estate segment includes all loans to finance agricultural production and all loans secured by agricultural real estate. This segment does not include loans to finance agriculture that are secured by residential real estate, which are included in the Residential Real Estate segment. The Commercial segment includes loans to finance commercial and industrial businesses that are not secured by real estate. The Commercial Real Estate segment includes loans secured by non-farm, non-residential real estate. The Construction Real Estate segment includes loans to finance construction and land development. This includes residential and commercial construction and land development. The Residential Real Estate segment includes all loans, other than construction loans, that are secured by single family and multi family residential real estate properties. The Consumer and Other segment includes all loans not included in any other segment. These are primarily loans to consumers for household, family, and other personal expenditures. The majority of this segment is student loans, and it also includes loans for autos, boats, and recreational vehicles.

Activity in the allowance for loan losses during the three and six months ended June 30, 2016 was as follows (000s omitted):

	Agriculture and Agricultural Real Estate	Commercial Commercial Real Estate	Commercial Real Estate	Construction Real Estate	Residential Real Estate	Consumer and Other	Total
Allowance for loan losses: For the three months ended June 30, 2016							
Beginning Balance	\$ 487	\$ 1,597	\$ 5,018	\$ 475	\$ 1,920	\$ 1,040	\$ 10,537
Charge-offs	(221)	(12)	(296)	-	(65)	(24)	(618)
Recoveries	-	44	46	14	45	35	184
Provision	(66)	(103)	(298)	(29)	(109)	405	(200)
Ending balance	\$ 200	\$ 1,526	\$ 4,470	\$ 460	\$ 1,791	\$ 1,456	\$ 9,903
Allowance for loan losses: For the six months ended June 30, 2016							
Beginning Balance	\$ 389	\$ 2,279	\$ 4,350	\$ 420	\$ 2,235	\$ 1,223	\$ 10,896
Charge-offs	(221)	(12)	(352)	-	(156)	(86)	(827)
Recoveries	-	77	69	27	103	58	334
Provision	32	(818)	403	13	(391)	261	(500)
Ending balance	\$ 200	\$ 1,526	\$ 4,470	\$ 460	\$ 1,791	\$ 1,456	\$ 9,903
Allowance for loan losses as of June 30, 2016							
Ending balance individually evaluated for impairment	\$ 1	\$ 468	\$ 447	\$ 262	\$ 309	\$ 188	\$ 1,675
Ending balance collectively evaluated for impairment	199	1,058	4,023	198	1,482	1,268	8,228
Ending balance	\$ 200	\$ 1,526	\$ 4,470	\$ 460	\$ 1,791	\$ 1,456	\$ 9,903
Loans as of June 30, 2016							
Ending balance individually evaluated for impairment	\$ 1,366	\$ 823	\$ 10,805	\$ 1,779	\$ 7,212	\$ 496	\$ 22,481
Ending balance collectively evaluated for impairment	19,798	85,903	236,551	14,991	208,024	50,532	615,799
Ending balance	\$ 21,164	\$ 86,726	\$ 247,356	\$ 16,770	\$ 215,236	\$ 51,028	\$ 638,280

Activity in the allowance for loan losses during the three and six months ended June 30, 2015 was as follows (000s omitted):

	Agriculture and Agricultural Real Estate	Commercial Commercial Real Estate	Commercial Real Estate	Construction Real Estate	Residential Real Estate	Consumer and Other	Total
Allowance for loan losses: For the three months ended June 30, 2015							
Beginning Balance	\$ 255	\$ 1,380	\$ 5,678	\$ 810	\$ 3,073	\$ 1,995	\$ 13,191
Charge-offs	(75)	(58)	(120)	-	(57)	(97)	(407)
Recoveries	3	97	21	12	133	29	295
Provision	242	62	(142)	(199)	(79)	116	-
Ending balance	\$ 425	\$ 1,481	\$ 5,437	\$ 623	\$ 3,070	\$ 2,043	\$ 13,079
Allowance for loan losses: For the six months ended June 30, 2015							
Beginning Balance	\$ 216	\$ 1,361	\$ 6,179	\$ 803	\$ 3,226	\$ 1,423	\$ 13,208
Charge-offs	(75)	(164)	(120)	-	(253)	(117)	(729)
Recoveries	10	171	182	621	356	60	1,400
Provision	274	113	(804)	(801)	(259)	677	(800)
Ending balance	\$ 425	\$ 1,481	\$ 5,437	\$ 623	\$ 3,070	\$ 2,043	\$ 13,079
Allowance for loan losses as of June 30, 2015							
Ending balance individually evaluated for impairment	\$ 80	\$ 473	\$ 913	\$ 478	\$ 630	\$ 208	\$ 2,782
Ending balance collectively evaluated for impairment	345	1,008	4,524	145	2,440	1,835	10,297
Ending balance	\$ 425	\$ 1,481	\$ 5,437	\$ 623	\$ 3,070	\$ 2,043	\$ 13,079
Loans as of June 30, 2015							
Ending balance individually evaluated for impairment	\$ 892	\$ 1,276	\$ 16,827	\$ 1,819	\$ 12,117	\$ 514	\$ 33,445
Ending balance collectively evaluated for impairment	18,084	82,349	233,178	11,344	205,421	39,749	590,125
Ending balance	\$ 18,976	\$ 83,625	\$ 250,005	\$ 13,163	\$ 217,538	\$ 40,263	\$ 623,570

Each period the provision for loan losses in the income statement results from the combination of an estimate by Management of loan losses that occurred during the current period and the ongoing adjustment of prior estimates of losses occurring in prior periods.

The provision for loan losses increases the allowance for loan losses, a valuation account which appears on the consolidated balance sheets. As the specific customer and amount of a loan loss is confirmed by gathering additional information, taking collateral in full or partial settlement of the loan, bankruptcy of the borrower, etc., the loan is charged off, reducing the allowance for loan losses. If, subsequent to a charge off, the Bank is able to collect additional amounts from the customer or sell collateral worth more than earlier estimated, a recovery is recorded.

To serve as a basis for making this provision, the Bank maintains an extensive credit risk monitoring process that considers several factors including: current economic conditions affecting the Bank's customers, the payment performance of individual loans and pools of homogeneous loans, portfolio seasoning, changes in collateral values, and detailed reviews of specific loan relationships.

The Company utilizes an internal loan grading system to assign a risk grade to all commercial loans, all renegotiated loans, and each commercial credit relationship. Grades 10 through 45 are considered "pass" credits and grades 50 through 65 are considered "watch" credits and are subject to greater scrutiny. Loans with grades 70 through 95 are considered "doubtful" or "loss" and have generally been charged off. A description of the general characteristics of each grade is as follows:

Grade 10– Excellent – Loans secured by marketable collateral, with adequate margin, or supported by strong financial statements, including substantial levels of tangible net worth. Probability of serious financial deterioration is unlikely. Possess a sound repayment source and a secondary source. This classification will also include individual loans backed by liquid personal assets, established history and unquestionable character. High liquidity, minimum risk, strong ratios, and low handling costs are common to these loans.

Grade 20– Above Average – Loans that exhibit less than average risk and clearly demonstrate debt service coverage that is consistently above average as well as a strong capital base. These loans may have some deficiency or vulnerability, but with offsetting features and are considered to be fully collectable.

Grade 30– Satisfactory – Loans that have an acceptable amount of risk but may exhibit vulnerability to deterioration if adverse circumstances are encountered. These loans should demonstrate adequate debt service coverage and adequate levels of capital support but warrant periodic monitoring to ensure that weaknesses do not materialize or advance.

Grades 40 and 45 – Pass – Loans that are considered “pass credits” and typically demonstrate adequate debt service coverage. The level of risk is considered acceptable but these loans warrant ongoing monitoring to ensure that adverse trends or other credit deficiencies have not materialized or advanced. The level of risk is considered acceptable so long as the loan is given adequate and ongoing management supervision.

Grades 50 and 55 – Watch – Loans that possess some credit deficiency or potential weakness that deserves close attention. The primary source of loan repayment is sufficient but may be considered inadequate by the Bank’s standards.

Grade 60– Substandard – Loans that exhibit one or more of the following characteristics: (1) a defined credit weakness, financial deterioration is underway, and uncertainty about the likelihood that the loan will be paid from the primary source of repayment; (2) inadequately protected by the current net worth and paying capacity of the obligor; (3) reliance on secondary source of repayment such as collateral liquidation or guarantees; (4) distinct possibility the Bank will sustain loss if deficiencies are not corrected; (5) unusual courses of action are needed to maintain a high probability of repayment; (6) insufficient cash flow to repay principal but continuing to pay interest; (7) the Bank is subordinated or unsecured due to flaws in documentation; (8) loans are restructured or are on nonaccrual status due to concessions to the borrower when compared to normal loan terms; (9) the Bank is contemplating foreclosure or legal action due to the apparent deterioration in the loan; or (10) there is deterioration in the market conditions and the borrower is highly vulnerable to these conditions.

Grade 70– Doubtful – Loans that exhibit one or more of the following characteristics: (1) loans with all the weaknesses of Substandard loans and collection or liquidation is not probable to result in payment in full; (2) the primary source of repayment is gone and there is considerable doubt as to the quality of the secondary source of repayment; or (3) the possibility of loss is high, but certain important pending factors may strengthen the loan and loss classification is deferred.

Grades 80 and 90 - Loss – Loans are considered uncollectible and of such little value that continuing to carry them on the Bank’s financial statements is not feasible.

The assessment of compensating factors may result in a rating plus or minus one grade from those listed above. These factors include, but are not limited to collateral, guarantors, environmental conditions, history, plan/projection reasonableness, quality of information, and payment delinquency.

The portfolio segments in each credit risk grade as of June 30, 2016 are as follows (000s omitted):

Credit Quality Indicators as of June 30, 2016

Credit Risk by Internally Assigned Grade

	Agriculture		Commercial	Construction	Residential	Consumer	Total
	and	Commercial	Real Estate	Real Estate	Real Estate	and Other	
	Agricultural	Real Estate					
Not Rated	\$ 55	\$ 1,403	\$ 245	\$ 7,834	\$ 133,729	\$ 43,667	\$ 186,933
10	-	5,350	-	-	-	-	5,350
20	551	337	488	-	-	146	1,522
30	609	11,770	9,525	-	228	-	22,132
40	14,786	61,020	186,572	4,956	65,994	7,042	340,370
45	2,301	2,584	11,541	1,453	4,064	-	21,943
50	1,315	2,573	21,143	2,182	3,889	15	31,117
55	180	243	4,094	-	31	-	4,548
60	1,367	1,446	13,748	345	7,301	158	24,365
70	-	-	-	-	-	-	-
80	-	-	-	-	-	-	-
90	-	-	-	-	-	-	-
Total	\$ 21,164	\$ 86,726	\$ 247,356	\$ 16,770	\$ 215,236	\$ 51,028	\$ 638,280
Performing	\$ 20,340	\$ 85,744	\$ 235,130	\$ 14,902	\$ 207,502	\$ 50,398	\$ 614,016
Nonperforming	824	982	12,226	1,868	7,734	630	24,264
Total	\$ 21,164	\$ 86,726	\$ 247,356	\$ 16,770	\$ 215,236	\$ 51,028	\$ 638,280

The portfolio segments in each credit risk grade as of December 31, 2015 are as follows (000s omitted):

Credit Quality Indicators as of December 31, 2015

Credit Risk by Internally Assigned Grade

Agriculture	Commercial	Commercial	Construction	Residential	Consumer	Total
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			Real Estate	Real Estate	Real Estate	and Other	
	and						
	Agricultural						
	Real Estate						
Not Rated	\$ 102	\$ 2,173	\$ 310	\$ 6,789	\$ 136,049	\$ 32,461	\$ 177,884
10	-	2,717	-	-	60	-	2,777
20	306	359	533	-	-	366	1,564
30	432	17,024	7,620	-	373	-	25,449
40	14,413	55,204	184,504	6,548	62,347	7,453	330,469
45	840	1,094	6,506	74	2,957	-	11,471
50	1,340	3,428	23,678	2,163	3,948	18	34,575
55	929	-	3,700	-	-	-	4,629
60	881	2,439	16,369	345	8,255	201	28,490
70	-	-	-	-	-	-	-
80	-	-	-	-	-	-	-
90	-	-	-	-	-	-	-
Total	\$ 19,243	\$ 84,438	\$ 243,220	\$ 15,919	\$ 213,989	\$ 40,499	\$ 617,308
Performing	\$ 18,362	\$ 83,372	\$ 228,624	\$ 14,104	\$ 205,430	\$ 39,869	\$ 589,761
Nonperforming	881	1,066	14,596	1,815	8,559	630	27,547
Total	\$ 19,243	\$ 84,438	\$ 243,220	\$ 15,919	\$ 213,989	\$ 40,499	\$ 617,308

Loans are considered past due when contractually required payment of interest or principal has not been received. The amount classified as past due is the entire principal balance outstanding of the loan, not just the amount of payments that are past due. The following is a summary of past due loans as of June 30, 2016 and December 31, 2015 (000s omitted):

							Recorded
	30-59	60-89	>90	Total		Total	Investment
June 30, 2016	Days	Days	Days	Past	Current	Loans	>90
	Past	Past	Past	Due			Days Past
	Due	Due	Due				Due
							and
							Accruing
Agriculture and Agricultural Real Estate	\$-	\$-	\$213	\$213	\$20,951	\$21,164	\$ -
Commercial	39	1	69	109	86,617	86,726	41
Commercial Real Estate	696	323	1,613	2,632	244,724	247,356	-
Construction Real Estate	-	242	-	242	16,528	16,770	-
Residential Real Estate	1,581	543	909	3,033	212,203	215,236	-
Consumer and Other	140	1	59	200	50,828	51,028	-
Total	\$2,456	\$1,110	\$2,863	\$6,429	\$631,851	\$638,280	\$ 41

							Recorded
	30-59	60-89	>90	Total		Total	Investment
December 31, 2015	Days	Days	Days	Past	Current	Loans	>90
	Past	Past	Past	Due			Days Past
	Due	Due	Due				Due
							and
							Accruing
Agriculture and Agricultural Real Estate	\$136	\$213	\$44	\$393	\$18,850	\$19,243	\$ -
Commercial	10	75	76	161	84,277	84,438	4
Commercial Real Estate	2,194	230	2,123	4,547	238,673	243,220	-
Construction Real Estate	-	-	-	-	15,919	15,919	-
Residential Real Estate	2,252	227	464	2,943	211,046	213,989	-
Consumer and Other	130	81	52	263	40,236	40,499	-
Total	\$4,722	\$826	\$2,759	\$8,307	\$609,001	\$617,308	\$ 4

Loans are placed on non-accrual status when, in the opinion of Management, the collection of additional interest is doubtful. Loans are automatically placed on non-accrual status upon becoming ninety days past due, however, loans may be placed on non-accrual status regardless of whether or not they are past due. All cash received on non-accrual loans is applied to the principal balance. Loans are considered for return to accrual status on an individual basis when all principal and interest amounts contractually due are brought current and future payments are reasonably assured.

The following is a summary of non-accrual loans as of June 30, 2016 and December 31, 2015 (000s omitted):

	June 30, 2016	December 31, 2015
Agriculture and Agricultural Real Estate	\$213	\$ 565
Commercial	159	148
Commercial Real Estate	4,286	4,823
Construction Real Estate	124	46
Residential Real Estate	2,606	2,915
Consumer and Other	134	136
Total	\$7,522	\$ 8,633

For loans deemed to be impaired due to an expectation that all contractual payments will probably not be received, impairment is measured by comparing the Bank's recorded investment in the loan to the present value of expected cash flows discounted at the loan's effective interest rate, the fair value of the collateral, or the loan's observable market price.

The following is a summary of impaired loans as of June 30, 2016 and 2015 (000s omitted):

June 30, 2016	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average	Interest	Average	Interest
				Recorded Investment for the Three Months Ended	Income Recognized in the Three Months Ended	Recorded Investment for the Six Months Ended	Income Recognized in the Six Months Ended
With no related allowance recorded:							
Agriculture and Agricultural Real Estate	\$ 1,017	\$ 1,216	\$ -	\$ 1,026	\$ 10	\$ 1,028	\$ 25
Commercial	142	192	-	146	3	148	5
Commercial Real Estate	6,970	7,555	-	7,217	70	7,255	133
Construction Real Estate	107	139	-	127	2	130	4
Residential Real Estate	4,022	4,367	-	4,292	47	4,335	98
Consumer and Other	33	33	-	34	1	35	1
With an allowance recorded:							
Agriculture and Agricultural Real Estate	349	379	1	352	3	417	3
Commercial	681	756	468	726	8	754	17
Commercial Real Estate	3,835	4,100	447	4,140	44	4,272	98
Construction Real Estate	1,672	1,671	262	1,676	19	1,681	38
Residential Real Estate	3,190	3,238	309	3,269	26	3,292	63
Consumer and Other	463	485	188	467	6	471	11
Total:							
Agriculture and Agricultural Real Estate	\$ 1,366	\$ 1,595	\$ 1	\$ 1,378	\$ 13	\$ 1,445	\$ 28
Commercial	823	948	468	872	11	902	22
Commercial Real Estate	10,805	11,655	447	11,357	114	11,527	231
Construction Real Estate	1,779	1,810	262	1,803	21	1,811	42
Residential Real Estate	7,212	7,605	309	7,561	73	7,627	161
Consumer and Other	496	518	188	501	7	506	12

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	Recorded Investment as of December 31, 2015	Unpaid Principal Balance as of December 31, 2015	Related Allowance as of December 31, 2015	Average Recorded Investment for the Three Months Ended June 30, 2015	Interest Income Recognized in the Three Months Ended June 30, 2015	Average Recorded Investment for the Six Months Ended June 30, 2015	Interest Income Recognized in the Six Months Ended June 30, 2015
With no related allowance recorded:							
Agriculture and Agricultural Real Estate	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial	63	113	-	170	3	174	6
Commercial Real Estate	7,701	8,107	-	8,380	83	8,430	175
Construction Real Estate	200	233	-	211	1	247	3
Residential Real Estate	4,137	4,359	-	7,782	93	7,830	187
Consumer and Other	26	26	-	35	1	36	1
With an allowance recorded:							
Agriculture and Agricultural Real Estate	882	885	240	904	12	911	24
Commercial	895	916	672	1,199	15	1,227	28
Commercial Real Estate	5,697	6,183	634	10,843	105	10,900	207
Construction Real Estate	1,609	1,609	277	1,823	21	1,828	42
Residential Real Estate	3,206	3,310	506	4,985	45	4,988	97
Consumer and Other	470	468	223	483	5	487	11
Total:							
Agriculture and Agricultural Real Estate	\$ 882	\$ 885	\$ 240	\$ 904	\$ 12	\$ 911	\$ 24
Commercial	958	1,029	672	1,369	18	1,401	34
Commercial Real Estate	13,398	14,290	634	19,223	188	19,330	382
Construction Real Estate	1,809	1,842	277	2,034	22	2,075	45
Residential Real Estate	7,343	7,669	506	12,767	138	12,818	284
Consumer and Other	496	494	223	518	6	523	12

The Bank may agree to modify the terms of a loan in order to improve the Bank's ability to collect amounts due. These modifications may include reduction of the interest rate, extension of the loan term, or in some cases, reduction of the principal balance. Modifications that are performed due to the debtor's financial difficulties are considered Troubled Debt Restructurings ("TDRs").

Loans that have been classified as TDRs during the three and six month periods ended June 30, 2016 and June 30, 2015 are as follows (000s omitted from dollar amounts):

	Three months ended		Six months ended			
	June 30, 2016		June 30, 2016			
	Pre-	Post-	Pre-	Post-		
	Modification Number of Recorded Contracts	Modification Recorded Principal	Modification Number of Recorded Contracts	Modification Recorded Principal		
	Balance	Balance	Balance	Balance		
Agriculture and Agricultural Real Estate	1	\$ 362	\$ 362	1	\$ 362	\$ 362
Commercial	-	-	-	-	-	-
Commercial Real Estate	-	-	-	-	-	-
Construction Real Estate	-	-	-	-	-	-
Residential Real Estate	6	251	250	7	451	447
Consumer and Other	1	57	57	1	57	57
Total	8	\$ 670	\$ 669	9	\$ 870	\$ 866

	Three months ended		Six months ended			
	June 30, 2015		June 30, 2015			
	Pre-	Post-	Pre-	Post-		
	Modification Number of Recorded Contracts	Modification Recorded Principal	Modification Number of Recorded Contracts	Modification Recorded Principal		
	Balance	Balance	Balance	Balance		
Agriculture and Agricultural Real Estate	-	\$ -	\$ -	-	\$ -	\$ -
Commercial	1	66	64	1	66	64
Commercial Real Estate	2	352	304	3	684	636
Construction Real Estate	-	-	-	-	-	-
Residential Real Estate	7	581	533	7	581	533
Consumer and Other	-	-	-	-	-	-
Total	10	\$ 999	\$ 901	11	\$ 1,331	\$ 1,233

The Bank considers TDRs that become past due under the modified terms as defaulted. There were no loans that became TDRs during the six month periods ended June 30, 2016 and June 30, 2015 that subsequently defaulted during the six month periods ended June 30, 2016 and June 30, 2015, respectively.

The Company has allocated \$1,644,000 of specific reserves to customers whose loan terms have been modified in troubled debt restructurings at June 30, 2016. In addition, there were no commitments to lend additional amounts to borrowers that are classified as troubled debt restructurings as of June 30, 2016 and June 30, 2015.

6. INVESTMENT SECURITIES

The following is a summary of the Bank's investment securities portfolio as of June 30, 2016 and December 31, 2015 (000s omitted):

	Held to Maturity			
	June 30, 2016			
	Gross	Gross	Estimated	
	Amortized	Unrealized	Unrealized	Market
	Cost	Gains	Losses	Value
Obligations of States and Political Subdivisions	\$38,814	\$ 2,130	\$ (6)	\$ 40,938
Corporate Debt Securities	500	6	-	506
	\$39,314	\$ 2,136	\$ (6)	\$ 41,444

Available for Sale**June 30, 2016**

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Obligations of U.S. Government Agencies	\$219,964	\$ 4,165	\$ -	\$ 224,129
Mortgage Backed Securities issued by U.S. Government Agencies	127,862	932	(423)	128,371
Obligations of States and Political Subdivisions	20,651	329	(2)	20,978
Other Debt Securities	53,285	229	(107)	53,407
Equity Securities	2,044	128	-	2,172
	\$423,806	\$ 5,783	\$ (532)	\$ 429,057

Held to Maturity**December 31, 2015**

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Obligations of States and Political Subdivisions	\$40,782	\$ 1,333	\$ (178)	\$ 41,937
Corporate Debt Securities	500	-	-	500
	\$41,282	\$ 1,333	\$ (178)	\$ 42,437

Available for Sale**December 31, 2015**

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Obligations of U.S. Government Agencies	\$370,469	\$ 1,647	\$ (3,055)	\$ 369,061
Mortgage Backed Securities issued by U.S. Government Agencies	104,472	107	(1,327)	103,252
Obligations of States and Political Subdivisions	17,212	305	(48)	17,469
Corporate Debt Securities	5,000	-	(50)	4,950

Equity Securities	2,044	83	-	2,127
	\$499,197	\$ 2,142	\$ (4,480) \$496,859

The amortized cost and estimated market values of securities by contractual maturity as of June 30, 2016 are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Held to Maturity		Available for Sale	
	Amortized	Estimated	Amortized	Estimated
	Cost	Market	Cost	Market
		Value		Value
Contractual maturity in				
1 year or less	\$5,937	\$ 5,977	\$3,586	\$ 3,593
After 1 year through five years	21,973	22,616	117,682	119,348
After 5 years through 10 years	9,342	10,428	153,808	156,785
After 10 years	2,062	2,423	18,824	18,788
Total	39,314	41,444	293,900	298,514
Mortgage Backed Securities	-	-	127,862	128,371
Securities with no stated maturity	-	-	2,044	2,172
Total	\$39,314	\$ 41,444	\$423,806	\$ 429,057

The investment securities portfolio is evaluated for impairment throughout the year. Impairment is recorded against individual securities, unless the decrease in fair value is attributable to interest rates or the lack of an active market, and Management determines that the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before a recovery of their amortized costs bases, which may be maturity. The following table shows the gross unrealized losses and fair value of the Company's investments with unrealized losses (in thousands), aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at June 30, 2016 and December 31, 2015.

June 30, 2016

	Less than 12 months		12 months or longer		Total	
	Aggregate	Gross	Aggregate	Gross	Aggregate	Gross
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of United States Government Agencies	\$-	\$ -	\$-	\$ -	\$-	\$ -
Mortgage Backed Securities issued by U.S. Government Agencies	19,661	132	31,335	291	50,996	423
Obligations of States and Political Subdivisions	3,354	6	1,806	2	5,160	8
Corporate Debt Securities	29,705	107	-	-	29,705	107
	\$52,720	\$ 245	\$33,141	\$ 293	\$85,861	\$ 538

December 31, 2015

Less than 12 months **Total**

	Aggregate		12 months or longer		Aggregate	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Obligations of United States Government Agencies	\$170,178	\$ 2,367	\$53,497	\$ 688	\$223,675	\$ 3,055
Mortgage Backed Securities issued by U.S. Government Agencies	57,949	633	31,118	694	89,067	1,327
Obligations of States and Political Subdivisions	10,830	165	5,324	61	16,154	226
Corporate Debt Securities	4,950	50	-	-	4,950	50
	\$243,907	\$ 3,215	\$89,939	\$ 1,443	\$333,846	\$ 4,658

The amount of investment securities issued by government agencies, states, and political subdivisions with unrealized losses and the amount of unrealized losses on those investment securities are primarily the result of market interest rates and not the result of the credit quality of the issuers of the securities. Because the Company does not intend to sell the investments and it is not more likely than not that the Company will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, the Company does not consider those investments to be other than temporarily impaired at June 30, 2016. As of June 30, 2016 and December 31, 2015, there were 41 and 146 securities in an unrealized loss position, respectively.

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value, as defined in ASC Topic 820, is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability is not adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for market activities that are usual and customary for transactions involving such assets or liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

The Company utilizes fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. Fair value is used on a recurring basis for Available for Sale Securities. Additionally, fair value is used on a non-recurring basis to evaluate assets or liabilities for impairment or for disclosure purposes. Examples of these non-recurring uses of fair value include certain loans held for sale accounted for on a lower of cost or market basis. Depending on the nature of the asset or liability, the Company uses various valuation techniques and assumptions when estimating fair value.

The Company applied the following fair value hierarchy:

Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets. The Company’s mutual fund investments where quoted prices are available in an active market generally are classified within Level 1 of the fair value hierarchy.

Level 2 – Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. The Company’s borrowed funds and investments in U.S. government agency securities, government sponsored mortgage backed securities, corporate debt securities, bank certificates of deposit, and obligations of states and political subdivisions are generally classified in Level 2 of the fair value hierarchy. Fair values for these instruments are estimated using pricing models, quoted prices of securities with similar characteristics, or discounted cash flows.

Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Private equity investments and certain municipal debt obligations are classified within Level 3 of the fair value hierarchy. Fair values are initially valued based on transaction price and are adjusted to reflect exit values.

The following tables present information about the Company's financial assets and liabilities measured at fair value on a recurring basis at June 30, 2016 and December 31, 2015, and the valuation techniques used by the Company to determine those fair values.

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June 30, 2016	Carrying Value	Level 1	Level 2	Level 3	Total
					Estimated Fair Value
Financial Assets:					
Cash and due from banks	\$ 118,368	\$ 99,172	\$ 19,403	\$ -	\$ 118,575
Securities - Held to Maturity					
Obligations of States and Political Subdivisions	38,814	-	3,489	37,449	40,938
Corporate Debt Securities	500	-	506	-	506
Securities - Available for Sale					
Obligations of U.S. Government Agencies	224,129	-	224,129	-	224,129
MBS issued by U.S. Government Agencies	128,371	-	128,371	-	128,371
Obligations of States and Political Subdivisions	20,978	-	20,978	-	20,978
Other Debt Securities	53,407	-	53,407	-	53,407
Other Securities	2,172	2,172	-	-	2,172
Federal Home Loan Bank Stock	4,148	-	4,148	-	4,148
Loans Held for Sale	919	-	-	938	938
Loans, net	628,377	-	-	634,776	634,776
Accrued Interest Receivable	3,902	-	-	3,902	3,902
Financial Liabilities:					
Noninterest Bearing Deposits	270,391	270,391	-	-	270,391
Interest Bearings Deposits	893,027	-	894,696	-	894,696
Accrued Interest Payable	61	-	-	61	61

December 31, 2015	Carrying Value	Level 1	Level 2	Level 3	Total
					Estimated Fair Value
Financial Assets:					
Cash and due from banks	\$ 85,050	\$ 85,050	\$ -	\$ -	\$ 85,050
Securities - Held to Maturity					
Obligations of States and Political Subdivisions	40,782	-	3,805	38,132	41,937
Corporate Debt Securities	500	-	500	-	500
Securities - Available for Sale					
Obligations of U.S. Government Agencies	369,061	-	369,061	-	369,061

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MBS issued by U.S. Government Agencies	103,252	-	103,252	-	103,252
Obligations of States and Political Subdivisions	17,469	-	17,469	-	17,469
Corporate Debt Securities	4,950	-	4,950	-	4,950
Other Securities	2,127	2,127	-	-	2,127
Federal Home Loan Bank Stock	4,148	-	4,148	-	4,148
Loans Held for Sale	1,477	-	-	1,508	1,508
Loans, net	606,412	-	-	613,397	613,397
Accrued Interest Receivable	4,170	-	-	4,170	4,170
Financial Liabilities:					
Noninterest Bearing Deposits	253,795	253,795	-	-	253,795
Interest Bearings Deposits	911,598	-	913,410	-	913,410
Repurchase Agreements	15,000	-	15,253	-	15,253
Accrued Interest Payable	108	-	-	108	108

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Company's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

The Company did not have any Level 3 assets measured at fair value on a recurring basis as of June 30, 2016 or December 31, 2015. The Company did not have any sales or purchases of Level 3 available for sale securities during the period.

Both observable and unobservable inputs may be used to determine the fair value of positions classified as Level 3 assets. As a result, the unrealized gains and losses for these assets presented in the tables above may include changes in fair value that were attributable to both observable and unobservable inputs.

The Company also has assets that under certain conditions are subject to measurement at fair value on a nonrecurring basis. These assets include loans and Other Real Estate Owned. The Company estimated the fair values of these assets using Level 3 inputs, specifically discounted cash flow projections.

Assets measured at fair value on a nonrecurring basis are as follows (000s omitted):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>June 30, 2016</u>			
Impaired loans	\$ -	\$ -	\$ 20,806
Other Real Estate Owned	\$ -	\$ -	\$ 1,808
<u>December 31, 2015</u>			
Impaired loans	\$ -	\$ -	\$ 22,334
Other Real Estate Owned	\$ -	\$ -	\$ 2,383

Impaired loans categorized as Level 3 assets consist of non-homogenous loans that are considered impaired. The Company estimates the fair value of the loans based on the present value of expected future cash flows using management's best estimate of key assumptions. These assumptions include future payment ability, timing of payment streams, and estimated realizable values of available collateral (typically based on outside appraisals). Other Real Estate Owned (OREO) consists of property received in full or partial satisfaction of a receivable. The Company

utilizes independent appraisals to estimate the fair value of OREO properties.

8. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Bank is a party to 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 commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated statements of condition.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for its other lending activities.

Financial instruments whose contractual amounts represent off-balance sheet credit risk were as follows (000s omitted):

	Contractual Amount	
	June 30, 2016	December 31, 2015
Commitments to extend credit:		
Unused portion of commercial lines of credit	\$72,720	\$ 70,488
Unused portion of credit card lines of credit	4,283	4,396
Unused portion of home equity lines of credit	24,690	23,164
Standby letters of credit and financial guarantees written	1,582	1,555
All other off-balance sheet commitments	-	-

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Most commercial lines of credit are secured by real estate mortgages or other collateral, and generally have fixed expiration dates or other termination clauses. Since the lines of credit may expire without being drawn upon, the total committed amounts do not necessarily represent future cash requirements. Credit card lines of credit have various established expiration dates, but are fundable on demand. Home equity lines of credit are secured by real estate mortgages, a majority of which have ten year expiration dates, but are fundable on demand. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of the collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on Management's credit evaluation of the counterparty.

Standby letters of credit written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements and other business transactions.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Introduction

MBT Financial Corp. (the "Company") is a bank holding company with one commercial bank subsidiary, Monroe Bank & Trust (the "Bank"). The Bank operates 14 branch offices in Monroe County, Michigan and 6 branch offices in Wayne County, Michigan, and 1 loan and wealth management office in each Wayne County and Lenawee County, Michigan.

The Bank's primary source of income is Net Interest Income (interest income on loans and investments less interest expense on deposits and borrowings), and its primary expense is the compensation of its employees. The discussion and analysis should be read in conjunction with the accompanying consolidated statements and footnotes.

Executive Overview

The Bank is operated as a community bank, primarily providing loan, deposit, and wealth management products and services to the people, businesses, and communities in its market area. In addition to our commitment to our mission of serving the needs of our local communities, we are focused on improving asset quality, increasing net interest income, and improving non-interest income and expenses.

The net profit of \$7,236,000 for the first six months of 2016 was an increase of \$2,174,000 or 42.9% compared to the first six months of 2015. The increase was primarily the result of an increase in gains on securities transactions due to par calls of bonds owned at discounts. In addition, net interest income, non-interest income and non-interest expense improved in 2016. These improvements exceeded the decrease in the recovery of loan losses, resulting in increases in income before taxes and federal income tax expense.

The national economic recovery is continuing slowly, and the recovery in southeast Michigan is relatively strong. Local unemployment rates continued to improve, with areas in our market better than the state and national averages. Commercial and residential development property values continue to improve, with some values reaching or exceeding their pre-recession levels. Our total classified assets, which include internal watch list loans, other real estate owned, and nonperforming and watch list investment securities, improved significantly during 2014 and 2015, and this trend of improvement continued through the first half of 2016. Classified assets went down \$4.7 million, or 15.2% during the first half of 2016, and decreased \$20.0 million or 43.3% compared to a year ago. The net charge offs for the six months were \$493,000, or 0.16% of loans, annualized. This is a good result, however, it is an increase compared to the first six months of 2015 when we recorded a net recovery of \$671,000 mainly due to a large recovery on one credit relationship. Due to improving loan quality metrics and lower charge offs, a reduction in our Allowance for Loan and Lease Losses (ALLL) was appropriate, and we recorded a \$500,000 credit to the provision expense, reflecting an increase of \$300,000 when compared to the negative provision of \$800,000 recorded in the first half of 2015. The ALLL as a percent of loans decreased from 1.76% at the end of 2015 to 1.55%. We assess the adequacy of our ALLL each quarter, and adjust it as necessary by debiting or crediting the provision expense. The allowance includes \$1.7 million of specific allocations on \$22.5 million of loans evaluated for impairment and \$8.2 million of general allocations on the remainder of the portfolio. The general allocation is based on the historical charge off experience of the previous 16 quarters. For the last several quarters, we have been replacing high charge off periods with low charge off periods in the calculation of our historical charge off rate, necessitating the negative provisions. If we continue to experience low charge off amounts, further negative provisions may occur, however, if recent loan growth continues or asset quality deteriorates, a provision expense may be required.

Net Interest Income increased \$111,000, or 0.6% compared to the first half of 2015 even though the net interest margin decreased from 3.20% to 3.09% as the average earnings assets increased \$43.1 million and the period was a day longer in 2016. The net interest margin decreased because the yield on earnings assets decreased more than the cost of interest bearing liabilities as interest rates remain at historically low levels. Non-interest income for the six months increased \$2,239,000, due to larger securities gains from bonds that were owned at discounts being called at par in the first half of 2016 than in the first half of 2015. Non-interest expenses decreased \$1,194,000, as salaries, benefits, occupancy expenses, equipment expenses, Other Real Estate expenses, FDIC deposit insurance assessments, and insurance expenses decreased. These decreases were partially offset by increases in professional fees, EFT and ATM expenses, and other expenses that were related to some product changes and enhancements. We completed a branch efficiency initiative that began in the fourth quarter of 2015, which contributed to the decreases in salaries, benefits, and occupancy expenses.

Critical Accounting Policies

The Company's Allowance for Loan Losses, Fair Value of Investment Securities, and Other Real Estate Owned are "critical accounting estimates" because they are estimates that are based on assumptions that are highly uncertain, and if different assumptions were used or if any of the assumptions used were to change, there could be a material impact on the presentation of the Company's financial condition. These assumptions include, but are not limited to, collateral values, the effect of economic conditions on the financial condition of the borrowers, the Company, and the issuers of investment securities, market interest rates, and projected earnings for the Company.

To determine the Allowance for Loan Losses, the Company estimates losses on all loans that are not classified as non accrual or renegotiated by applying historical loss rates, adjusted for current conditions, to those loans. In addition, all non accrual loan relationships over \$250,000 that are classified by Management as nonperforming as well as selected performing accounts and all renegotiated loans are individually tested for impairment. Any amount of monetary impairment is included in the Allowance for Loan Losses.

To determine the fair value of investment securities, the Company utilizes quoted prices in active markets for identical assets, quoted prices for similar assets in active markets, or discounted cash flow calculations for investments where there is little, if any, market activity for the asset.

To determine the fair value of Other Real Estate Owned, the Company utilizes independent appraisals to estimate the fair value of the property.

Financial Condition

The regional economic recovery continued this quarter, with local unemployment and property values steadily improving since 2014. Management efforts are focused on improving asset quality, increasing net interest income, and improving non-interest income and expenses.

With respect to asset quality, our nonperforming assets (“NPAs”) decreased 5.1% during the quarter, from \$27.5 million to \$26.1 million, and total classified assets decreased 7.7% from \$28.4 million to \$26.2 million. Loan delinquencies increased from \$6.3 million 30 days or more past due as of March 31, 2016 to \$6.4 million as of June 30, 2016, but with the portfolio growth, the delinquency percentage was unchanged at 1.0% of the total loans. Over the last twelve months, NPAs decreased \$12.1 million, or 31.7%, with nonperforming loans decreasing 28.3% from \$33.9 million to \$24.3 million, and Other Real Estate Owned (“OREO”) decreasing 57.1% from \$4.2 million to \$1.8 million. Total classified assets, which include internally classified watch list loans, other real estate, and watch list investment securities, decreased \$20.0 million, or 43.3%. The Company’s Allowance for Loan and Lease Losses (“ALLL”) decreased \$3.2 million over the last four quarters because of the improvement in the quality of the assets in the loan portfolio and a decrease in the historical loss rates. The ALLL is now 1.55% of loans, down from 2.09% at June 30, 2015. The ALLL is 40.81% of nonperforming loans (“NPLs”), compared to 39.55% at year end and 38.53% at June 30, 2015. In light of current economic conditions, we believe that this level of ALLL adequately estimates the potential losses in the loan portfolio.

Since December 31, 2015, total loans held for investment increased \$21.0 million as new loan activity exceeded payments received and other reductions in the period. Even with the increase in loans, our pipeline of loans in process remained steady this quarter, and we expect new loan production to continue to exceed run off, resulting in an increase in loans outstanding, in the second half of 2016.

Since December 31, 2015, deposits decreased \$2.0 million, borrowed funds decreased \$15.0 million, and capital decreased \$1.7 million, and as a result our total assets decreased \$18.9 million, or 1.4%. The Company expects minimal deposit funding growth in the third quarter of 2016, as we have adequate liquidity to fund our anticipated loan growth without needing to actively grow deposits. The composition of deposits continues to change as customers move funds from maturing interest bearing time deposit accounts to low or no cost non maturity deposit accounts due to the low interest rate environment. The expected loan growth will be funded by reductions in our cash and investments. The decrease in total capital during the first six months of 2016 was due to stock repurchase activity and the payment of a special \$0.50 per share dividend and regular quarterly dividends of \$0.03 per share in each of the first two quarters. The total dividend payments of \$12.8 million and stock repurchase of \$1.4 million were offset by the profit of \$7.2 million and the \$5.1 million increase in the accumulated other comprehensive income (AOCI). AOCI increased mainly due to an increase in the value of our securities available for sale. Capital decreased at a lower rate than assets, causing the capital to assets ratio to increase from 10.98% at December 31, 2015 to 11.00% at June 30, 2016.

Results of Operations – Second Quarter 2016 vs. Second Quarter 2015

Net Interest Income - A comparison of the income statements for the three months ended June 30, 2016 and 2015 shows an increase of \$163,000, or 1.8%, in Net Interest Income. Interest income on loans increased \$25,000 or 0.3% as the average loans outstanding increased \$4.4 million and the average yield on loans was unchanged at 4.62%. The average loans outstanding increased due to improving economic conditions and purchases of loan participations. The interest income on investments, fed funds sold, and interest bearing balances due from banks decreased \$40,000 even though the average amount of investments, fed funds sold, and interest bearing balances due from banks increased \$30.8 million because the yield decreased from 1.94% to 1.82%. The Company continues to maintain a high level of liquidity by keeping a large amount of funds in low yielding short term investments and deposits in the Federal Reserve Bank. The interest expense on deposits decreased \$133,000 or 21.5% even though the average deposits increased \$52.3 million because the average cost of deposits decreased from 0.22% to 0.17%. The average cost of deposits decreased because maturing time deposits are either resetting at lower rates or customers are moving the funds to non interest bearing demand deposit accounts or low cost non maturity deposits due to the low interest rate environment. The interest expense on borrowed funds decreased \$45,000 as the final remaining borrowed funds were repaid on June 8, 2016. As a result, the interest expense on borrowed funds is expected to decrease \$132,000 in the third quarter of 2016 compared to the second quarter of 2016.

Provision for Loan Losses - The Provision for Loan Losses decreased \$200,000 compared to the second quarter of 2015 as a \$200,000 credit to provision expense was recorded in the second quarter of 2016, compared to no provision expense recorded in the second quarter of 2015. We charged off \$618,000 of principal while recovering \$184,000 of previously charged off loans in the second quarter of 2016, for a net charge off total of \$434,000, or 0.28% of loans, annualized. Each quarter, the Company conducts a review and analysis of its ALLL to determine its adequacy. This analysis involves specific allocations for impaired credits and a general allocation for losses expected based on historical experience adjusted for current conditions. Due to an improvement in portfolio risk indicators and a decrease in the historical charge off percentages, the amount of ALLL required at the end of the second quarter of 2016 decreased from \$10,537,000 at March 31, 2016 to \$9,903,000 as of June 30, 2016. Along with the \$434,000 net charge off, this required us to record a credit to the provision expense. The allowance includes \$1.7 million of specific allocations and \$8.2 million of general allocations. The general allocation is based on the historical charge off experience of the previous 16 quarters. For the last several quarters, we have been replacing high charge off periods with low charge off periods in the calculation of our historical charge off rate, necessitating the negative provisions. If we continue to experience low charge offs, further negative provisions may continue to occur. However, significant growth in loans outstanding or deterioration of asset quality could require a provision expense.

Other Income – Non interest income increased \$1,750,000, or 46.0% compared to the second quarter of 2015. Excluding gains and losses on securities and other real estate owned activity, non-interest income was unchanged at \$3.8 million. Wealth management income decreased \$86,000 or 7.2% as the market value of assets managed decreased. Debit card income increased \$144,000, or 24.4% due to increased non customer surcharge and interchange activity. Gains on securities transactions increased \$1,730,000 due to large gains in the second quarter of 2016 that were the result of the bonds purchased at discounts being called at par. Due to the low interest rates, issuers continued to call and refinance their debt in the second quarter of 2016. We do not expect this activity and these gains to continue beyond the second quarter of 2016. Losses from other real estate activity improved \$20,000 due to smaller losses and write downs of the carrying values properties in the second quarter of 2016 compared to the second quarter of 2015. Other non-interest income decreased \$43,000, or 8.7%, primarily due to lower rental income on Other Real

Estate.

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Other Expenses – Total non-interest expenses decreased \$858,000, or 8.8% compared to the second quarter of 2015. Salaries and Employee Benefits decreased \$351,000, or 6.1%, as the number of full time equivalent employees decreased from 350 to 288 due to various efforts to reduce staffing in 2015, culminating in an efficiency initiative in the fourth quarter that resulted in the closing of 4 branch offices and the reduction of 43 staff positions. Occupancy expense increased \$27,000, or 4.4% as higher maintenance costs exceeded the reduction in depreciation expense. Electronic Funds Transfer and Automated Teller Machine related expenses increased \$119,000 due to increased debit card use and higher card reissuance costs. Other Real Estate Owned expenses decreased \$149,000 or 83.2% due to the decrease in the amount of OREO properties owned. FDIC insurance assessments decreased \$238,000 as the termination of our informal agreement with the FDIC and Michigan Department of Insurance and Financial Services in 2015 resulted in decreases in the assessment rate. Other expense decreased \$155,000, primarily due to an adjustment to the accrual for interest on the recently settled IRS audit.

As a result of the above activity, the Profit Before Income Taxes in the second quarter of 2016 was \$6,127,000, an increase of \$2,971,000 compared to the pre-tax profit of \$3,156,000 in the second quarter of 2015. The Company recorded a federal income tax expense of \$1,888,000 in the second quarter of 2016, reflecting an effective tax rate of 30.8%, compared to the tax expense of \$871,000 in the second quarter of 2015, which reflected an effective rate of 27.6%. The increase in the effective tax rate was the result of the decrease in the percentage of operating income that was from municipal investments and bank owned life insurance. The Net profit for the second quarter of 2016 was \$4,239,000, an increase of 85.5% compared to the net profit of \$2,285,000 in the second quarter of 2015.

Results of Operations – Six Months Ended June 30, 2016 vs. Six Months Ended June 30, 2015

Net Interest Income - A comparison of the income statements for the six months ended June 30, 2016 and 2015 shows an increase of \$111,000, or 0.6%, in Net Interest Income. Interest income on loans decreased \$372,000 or 2.6% as the average loans outstanding increased \$4.2 million while the average yield on loans was decreased from 4.76% to 4.59%. The average loans outstanding increased due to improving economic conditions and purchases of loan participations. The interest income on investments, fed funds sold, and interest bearing balances due from banks increased \$179,000 even though the yield decreased from 1.96% to 1.89% as the average amount of investments, fed funds sold, and interest bearing balances due from banks increased \$38.9 million. The Company continues to maintain a very high liquidity position by keeping a large amount of funds in low yielding short term investments and deposits in the Federal Reserve Bank. The interest expense on deposits decreased \$261,000 or 20.6% even though the average deposits increased \$46.0 million because the average cost of deposits decreased from 0.23% to 0.17%. The average cost of deposits decreased because maturing time deposits are either resetting at lower rates or customers are moving the funds to non interest bearing demand deposit accounts due to the low interest rate environment. The interest expense on borrowed funds decreased \$43,000 as the average amount of borrowed funds decreased \$1.9 million.

Provision for Loan Losses - The Provision for Loan Losses increased \$300,000 compared to the first six months of 2015 as a \$500,000 credit to provision expense was recorded in the first half of 2016, compared to the \$800,000 credit to provision expense recorded in the first two quarters of 2015. We charged off \$827,000 of principal while recovering \$334,000 of previously charged off loans in the first two quarters of 2016, for a net charge off total of \$493,000, or 0.16% of loans, annualized. In the first two quarters of 2015, recoveries exceeded charge offs, resulting in a net recovery of \$671,000, or 0.22% of loans.

Other Income – Non interest income increased \$2,239,000, or 30.1% compared to the first six months of 2015. Excluding gains and losses on securities and other real estate owned activity, non-interest income increased \$198,000, or 2.7%. Wealth management income decreased \$211,000 or 8.7% as the market value of assets managed decreased. Service charges and other fees on deposit accounts increased \$100,000, or 5.2% as we added new features and benefits to our primary checking account product and instituted a monthly service fee. Debit card income increased \$254,000, or 22.0% due to increased activity. Gains on securities transactions increased \$1,814,000 due to large gains in the first six months of 2016 that were the result of the bonds purchased at discounts being called at par. Losses from other real estate activity improved \$227,000 due to smaller losses and write downs of the carrying values properties in the first six months of 2016 compared to the first six months of 2015. Bank Owned Life Insurance income increased \$84,000 due to a non-recurring cash surrender value adjustment in 2015.

Other Expenses – Total non-interest expenses decreased \$1,194,000, or 6.1% compared to the first six months of 2015. Salaries and Employee Benefits decreased \$607,000, or 5.2%, as the number of full time equivalent employees decreased from 352 to 288 due to various efforts to reduce staffing in 2015, culminating in an efficiency initiative in the fourth quarter that resulted in the closing of 4 branch offices and the reduction of 43 staff positions. Occupancy expense decreased \$92,000, or 6.5% due to lower utilities and maintenance costs, resulting from the efficiency initiative and the mild winter weather. Professional fees increased \$82,000 or 7.3% due to increased consulting and legal expenses. Electronic Funds Transfer and Automated Teller Machine related expenses increased \$338,000 due to increased debit card use, the reissuance of all of our debit cards with EMV chip cards in the first quarter of 2016, and an incentive payment received from a vendor in the first quarter of 2015. FDIC insurance assessments decreased \$483,000 and other insurance decreased \$121,000 as the termination of our informal agreement with the FDIC and Michigan Department of Insurance and Financial Services in 2015 resulted in decreases in the rates.

As a result of the above activity, the Profit Before Income Taxes in the first six months of 2016 was \$10,348,000, an increase of \$3,244,000 compared to the pre-tax profit of \$7,104,000 in the first six months of 2015. The Company recorded a federal income tax expense of \$3,112,000 in the first six months of 2016, reflecting an effective tax rate of 30.1%, compared to the tax expense of \$2,042,000 in the first six months of 2015, which reflected an effective rate of 28.7%. The increase in the effective tax rate was the result of the decrease in the percentage of operating income that was from municipal investments and bank owned life insurance. The Net profit for the first six months of 2016 was \$7,236,000, an increase of 42.9% compared to the net profit of \$5,062,000 in the first six months of 2015.

Cash Flows

Cash flows provided by operating activities increased \$150,000 compared to the first six months of 2015 even though the net income was \$2,174,000 higher because most of the improvement in earnings was due to securities gains, which are classified as investing activities for cash flow reporting. Cash flows from investing activities increased by \$102.3 million from \$44.6 million used in the first six months of 2015 to \$57.7 million provided in the first six months of 2016 as more cash was provided by investment security maturities and redemptions and less was invested in securities in the first six months of 2016 than in the first six months of 2015. The increase in cash provided by investing activities was partially offset by an increase in the cash used for loan growth, which was \$7.6 million more in 2016. The amount of cash used for financing activities in the first six months of 2016 was \$31.1 million, due to the repayment of a maturing repurchase agreement of \$15.0 million, the payment of \$12.8 in dividends on the common stock, and the repurchase of 192,080 shares of common stock for \$1.4 million. In the first six months of 2015, \$9.5 million of cash was provided by deposit growth, compared to the \$2.0 million decrease in deposits in the first six months of 2016. In the first six months of 2016, the cash provided by operations and investing activities exceeded the cash used for financing activities, and the amount of cash and cash equivalents increased by \$33.3 million during the period. In the first six months of 2015, the cash used for investing activities exceeded the cash provided by operations and financing activities, resulting in a decrease of \$28.5 million in cash and cash equivalents during the six months. We expect cash flows from redemptions of callable investment securities to decrease in the third quarter of 2016, and we plan to use some of the cash and the cash provided by operations to fund loan growth and investment security purchases, resulting in a reduction in our cash and cash equivalents by the end of the year.

Liquidity and Capital

The Company believes it has sufficient liquidity to fund its lending activity and allow for fluctuations in deposit levels. Internal sources of liquidity include the maturities of loans and securities in the ordinary course of business as well as our available for sale securities portfolio. External sources of liquidity include a line of credit with the Federal Home Loan Bank of Indianapolis, the Federal funds line that has been established with our correspondent bank, and Repurchase Agreements with money center banks that allow us to pledge securities as collateral for borrowings. As of June 30, 2016, the Bank was not utilizing any of its authorized limit of \$255 million with the Federal Home Loan Bank of Indianapolis, or its \$20 million overdraft line of credit with the Federal Home Loan Bank of Indianapolis, or its \$25 million federal funds line with a correspondent bank. The Company periodically draws on its overdraft and fed funds lines to ensure that funding will be available if needed.

The Company's Funds Management Policy includes guidelines for desired amounts of liquidity and capital. The Funds Management Policy also includes contingency plans for liquidity and capital that specify actions to take if liquidity and capital ratios fall below the levels contained in the policy. Throughout the first six months of 2016 the Company was in compliance with its Funds Management Policy regarding liquidity and capital.

Total stockholders' equity of the Company was \$145.6 million at June 30, 2016 and \$147.3 million at December 31, 2015. Common stock decreased \$1.2 million due to the repurchase of 192,080 shares, partially offset by issuance of stock under compensation programs and for our Employee Stock Purchase Plan. Retained earnings decreased \$5.6 million as the year to date profit of \$7.2 million was exceeded by the payment of \$12.8 million in common stock

dividends, and the Accumulated Other Comprehensive Income (AOCI) increased \$5.1 million due to an increase in the value of our securities that are classified as Available For Sale. Total equity decreased \$1.7 million while total assets decreased \$18.9 million, so the ratio of equity to assets increased from 10.98% at December 31, 2015 to 11.00% at June 30, 2016.

Federal bank regulatory agencies have set capital adequacy standards for Total Risk Based Capital, Tier 1 Risk Based Capital, and Leverage Capital. These standards require banks to maintain Leverage and Tier 1 ratios of at least 4% and a Total Capital ratio of at least 8% to be adequately capitalized. The regulatory agencies consider a bank to be well capitalized if its Total Risk Based Capital is at least 10% of Risk Weighted Assets, Tier 1 Capital is at least 8% of Risk Weighted Assets, and the Leverage Capital Ratio is at least 5%. The Basel III capital requirements that began to be phased in the first quarter of 2015 increased the well capitalized requirement for the Tier 1 Capital as a percent of Risk Weighted Assets from 6% to 8%. Basel III also implemented the new Common Equity Tier 1 Capital to Risk Weighted Assets ratio, with a minimum of 6.5% required to be considered well capitalized.

The following table summarizes the capital ratios of the Company and the Bank:

	Actual		Minimum to Qualify as	
	Amount	Ratio	Well Capitalized Amount	Ratio
As of June 30, 2016:				
Total Capital to Risk-Weighted Assets Consolidated	\$ 148,701	18.10 %	\$ 82,144	10.0 %
Monroe Bank & Trust	148,355	18.08 %	82,066	10.0 %
Tier 1 Capital to Risk-Weighted Assets Consolidated	138,405	16.85 %	65,715	8.0 %
Monroe Bank & Trust	138,059	16.82 %	65,653	8.0 %
Common Equity Tier 1 Capital to Risk-Weighted Assets Consolidated	138,405	16.85 %	53,394	6.5 %
Monroe Bank & Trust	138,059	16.82 %	53,343	6.5 %
Tier 1 Capital to Average Assets Consolidated	138,405	10.35 %	66,834	5.0 %
Monroe Bank & Trust	138,059	10.33 %	66,795	5.0 %

	Actual		Minimum to Qualify as	
	Amount	Ratio	Well Capitalized Amount	Ratio
As of December 31, 2015:				
Total Capital to Risk-Weighted Assets Consolidated	\$ 154,718	19.79 %	\$ 78,163	10.0 %
Monroe Bank & Trust	153,026	19.59 %	78,107	10.0 %
Tier 1 Capital to Risk-Weighted Assets Consolidated	144,857	18.53 %	62,531	8.0 %
Monroe Bank & Trust	143,175	18.33 %	62,485	8.0 %
Common Equity Tier 1 Capital to Risk-Weighted Assets Consolidated	144,857	18.53 %	50,806	6.5 %
Monroe Bank & Trust	143,175	18.33 %	50,769	6.5 %
Tier 1 Capital to Average Assets				

Consolidated	144,857	11.04 %	65,625	5.0 %
Monroe Bank & Trust	143,175	10.91 %	65,602	5.0 %

Market risk for the Bank, as is typical for most banks, consists mainly of interest rate risk and market price risk. The Bank's earnings and the economic value of its equity are exposed to interest rate risk and market price risk, and monitoring this risk is the responsibility of the Asset/Liability Management Committee (ALCO) of the Bank. The Bank's market risk is monitored quarterly and it has not changed significantly since year-end 2015.

Forward-Looking Statements

Certain statements contained herein are not based on historical facts and are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements which are based on various assumptions (some of which are beyond the Company's control), may be identified by reference to a future period or periods, or by the use of forward-looking terminology, such as "may," "will," "believe," "expect," "estimate," "anticipate," "continue," or similar terms or variations on those terms, or the negative of these terms. Actual results could differ materially from those set forth in forward-looking statements, due to a variety of factors, including, but not limited to, those related to the economic environment, particularly in the market areas in which the Company operates, competitive products and pricing, fiscal and monetary policies of the U.S. Government, changes in government regulations affecting financial institutions, including regulatory fees and capital requirements, changes in prevailing interest rates, acquisitions and the integration of acquired businesses, credit risk management, asset/liability management, changes in the financial and securities markets, including changes with respect to the market value of our financial assets, the availability of and costs associated with sources of liquidity, and the ability of the Company to resolve or dispose of problem loans.

The Company does not undertake, and specifically disclaims any obligation, to publicly release the result of any revisions which may be made to any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Bank faces market risk to the extent that the fair values of its financial instruments are affected by changes in interest rates. The Bank does not face market risk due to changes in foreign currency exchange rates, commodity prices, or equity prices. The asset and liability management process of the Bank seeks to monitor and manage the amount of interest rate risk. This is accomplished by analyzing the differences in repricing opportunities for assets and liabilities, by simulating operating results under varying interest rate scenarios, and by estimating the change in the net present value of the Bank's assets and liabilities due to interest rate changes.

Each quarter, the Asset and Liability Committee (ALCO), which includes the senior management of the Bank and a non executive member of the board of directors, estimates the effect of interest rate changes on the projected net interest income of the Bank. The sensitivity of the Bank's net interest income to changes in interest rates is measured by using a computer based simulation model to estimate the impact on earnings of increases of 100, 200, 300, and 400 basis points and decreases of 100 and 200 basis points in the interest rates. The net interest income projections are compared to a base case projection, which assumes no changes in interest rates.

The Bank's ALCO has established limits in the acceptable amount of interest rate risk, as measured by the change in the Bank's projected net interest income, in its policy. Throughout the first six months of 2016, the Bank's interest rate risk has remained within its policy limits.

The ALCO also monitors interest rate risk by estimating the effect of changes in interest rates on the economic value of the Bank's equity each quarter. The economic value of the Bank's equity is first determined by subtracting the fair value of the Bank's liabilities from the fair value of the Bank's assets. The Bank estimates the interest rate risk by calculating the effect of market interest rate changes on that economic value of its equity. For this analysis, the Bank assumes immediate parallel shifts of plus 100, 200, 300, and 400 basis points and minus 100 and 200 basis points in interest rates. The discount rates used to determine the present values of the loans and deposits, as well as the prepayment rates for the loans, are based on Management's expectations of the effect of the rate changes on the market for loans and deposits. In addition, each quarter, the Bank conducts additional analyses that utilize other rate scenarios, such as larger shifts in rates and changes in the shape of the yield curve, to assess the Bank's exposure to interest rate risk in stress scenarios.

The Bank's interest rate risk, as measured by the net interest income and economic value of equity simulations, has not changed significantly from December 31, 2015.

Item 4. Controls and Procedures

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of June 30, 2016, pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of June 30, 2016, in alerting them in a timely manner to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic SEC filings.

There was no change in the Company's internal control over financial reporting that occurred during the Company's fiscal quarter ended June 30, 2016, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II Other Information

Item 1. Legal Proceedings

MBT Financial Corp. and its subsidiaries are not a party to, nor is any of their property the subject of any material legal proceedings other than ordinary routine litigation incidental to their respective businesses, nor are any such proceedings known to be contemplated by governmental authorities.

Item 1A. Risk Factors

There have been no material changes in the risk factors disclosed by the Company in its Report on Form 10-K for the fiscal year ended December 31, 2015.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The Company has a stock repurchase program which it publicly announced on January 28, 2016. On that date, the Board of Directors authorized the repurchase of 2 million of the Company's common shares, which authorization commenced on February 1, 2016 and will expire on January 31, 2018. The following table summarizes the open-market and privately negotiated stock repurchase activity of the Company during the three months ended June 30, 2016:

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
April 1, 2016 - April 30, 2016	-	\$ -	-	2,000,000
May 1, 2016 - May 31, 2016	-	\$ -	-	2,000,000
June 1, 2016 - June 30, 2016	192,080	\$ 7.36	192,080	1,807,920

Total	192,080	\$ 7.36	192,080
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Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

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Item 6. Exhibits

- 3.1 Amended and Restated Articles of Incorporation of MBT Financial Corp.
- 3.2 Amended and Restated Bylaws of MBT Financial Corp. Previously filed as Exhibit 3.2 to MBT Financial Corp.'s Form 10-Q for its quarter ended March 31, 2008.
- 31.1 Certification by Chief Executive Officer required by Securities and Exchange Commission Rule 13a-14.
- 31.2 Certification by Chief Financial Officer required by Securities and Exchange Commission Rule 13a-14.
- 32.1 Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as enacted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification by Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as enacted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema Document
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MBT Financial Corp.
(Registrant)

August 9, 2016
Date

By /s/ H. Douglas Chaffin
H. Douglas Chaffin
President &
Chief Executive Officer

August 9, 2016
Date

By /s/ John L. Skibski
John L. Skibski
Executive Vice President and
Chief Financial Officer

Exhibit Index

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