

COMMUNITY TRUST BANCORP INC /KY/  
Form 10-Q  
August 06, 2010

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2010

Or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 0-11129

COMMUNITY TRUST BANCORP, INC.  
(Exact name of registrant as specified in its charter)

|  |                                 |
|--|---------------------------------|
| Kentucky   | 61-0979818                      |
| (State or other jurisdiction of incorporation or organization) | IRS Employer Identification No. |

|  |            |
|--|------------|
| 346 North Mayo Trail                     | 41501      |
| Pikeville, Kentucky                      | (Zip Code) |
| (address of principal executive offices) |            |

(606) 432-1414  
(Registrant's telephone number)

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 <input checked="" type="checkbox"/> | No <input type="checkbox"/> |
|---|-----------------------------|

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.)

Yes

No

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

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

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes

No

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practical date.

Common stock – 15,239,459 shares outstanding at July 31, 2010

PART I - FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

The accompanying information has not been audited by independent registered public accountants; however, in the opinion of management such information reflects all adjustments necessary for a fair presentation of the results for the interim period. All such adjustments are of a normal and recurring nature.

The accompanying condensed consolidated financial statements are presented in accordance with the requirements of Form 10-Q and consequently do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America or those normally made in the Registrant's annual report on Form 10-K. Accordingly, the reader of the Form 10-Q should refer to the Registrant's Form 10-K for the year ended December 31, 2009 for further information in this regard.

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Community Trust Bancorp, Inc.  
Condensed Consolidated Balance Sheets

|  | (unaudited)<br>June 30<br>2010 | December<br>31<br>2009 |
|--|--------------------------------|------------------------|
| (dollars in thousands)   |                                |                        |
| Assets:  |                                |                        |
| Cash and due from banks  | \$71,196                       | \$62,720               |
| Interest bearing deposits  | 38,363                         | 31,814                 |
| Federal funds sold   | 67,006                         | 47,595                 |
| Cash and cash equivalents  | 176,565                        | 142,129                |
| Certificates of deposits in other banks  | 15,508                         | 100                    |
| Securities available-for-sale at fair value<br>(amortized cost of \$344,163 and \$263,756, respectively) | 352,616                        | 270,237                |
| Securities held-to-maturity at amortized cost<br>(fair value of \$1,662 and \$14,435, respectively)      | 1,662                          | 14,336                 |
| Loans held for sale  | 1,466                          | 1,818                  |
| Loans  | 2,441,222                      | 2,435,760              |
| Allowance for loan losses  | (36,156 )                      | (32,643 )              |
| Net loans  | 2,405,066                      | 2,403,117              |
| Premises and equipment, net  | 48,403                         | 49,242                 |
| Federal Reserve Bank and Federal Home Loan Bank stock  | 29,054                         | 29,048                 |
| Goodwill   | 65,059                         | 65,059                 |
| Core deposit intangible (net of accumulated amortization of \$7,174 and<br>\$6,857, respectively)        | 331                            | 648                    |
| Bank owned life insurance  | 38,812                         | 38,117                 |
| Mortgage servicing rights  | 2,692                          | 3,406                  |
| Other real estate owned  | 40,105                         | 37,333                 |
| Other assets   | 31,953                         | 32,069                 |
| Total assets   | \$3,209,292                    | \$3,086,659            |
| Liabilities and shareholders' equity:  |                                |                        |
| Deposits   |                                |                        |
| Noninterest bearing  | \$494,901                      | \$490,809              |
| Interest bearing   | 2,076,226                      | 1,971,400              |
| Total deposits   | 2,571,127                      | 2,462,209              |
| Repurchase agreements  | 183,287                        | 180,471                |
| Federal funds purchased and other short-term borrowings  | 8,465                          | 12,205                 |
| Advances from Federal Home Loan Bank   | 20,059                         | 20,671                 |
| Long-term debt   | 61,341                         | 61,341                 |
| Other liabilities  | 34,682                         | 28,305                 |
| Total liabilities  | 2,878,961                      | 2,765,202              |
| Shareholders' equity:  |                                |                        |
| Preferred stock, 300,000 shares authorized and unissued  | -                              | -                      |

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|   |             |             |
|---|-------------|-------------|
| Common stock, \$5 par value, shares authorized 25,000,000;<br>shares outstanding 2010 – 15,227,945; 2009 – 15,183,987 | 76,140      | 75,920      |
| Capital surplus   | 153,640     | 152,484     |
| Retained earnings   | 95,057      | 88,840      |
| Accumulated other comprehensive income, net of tax  | 5,494       | 4,213       |
| Total shareholders' equity  | 330,331     | 321,457     |
| Total liabilities and shareholders' equity  | \$3,209,292 | \$3,086,659 |

See notes to condensed consolidated financial statements.

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Community Trust Bancorp, Inc.  
Condensed Consolidated Statements of Income and Other Comprehensive Income  
(unaudited)

|   | Three Months Ended |               | Six Months Ended |               |
|---|--------------------|---------------|------------------|---------------|
|   | June 30            |               | June 30          |               |
| (in thousands except per share data)  | 2010               | 2009          | 2010             | 2009          |
| <b>Interest income:</b>   |                    |               |                  |               |
| Interest and fees on loans, including loans held for sale                         | \$35,165           | \$34,434      | \$70,316         | \$68,622      |
| <b>Interest and dividends on securities</b>                                       |                    |               |                  |               |
| Taxable   | 2,394              | 2,499         | 4,608            | 5,098         |
| Tax exempt  | 394                | 498           | 818              | 928           |
| <b>Interest and dividends on Federal Reserve and Federal Home Loan Bank stock</b> |                    |               |                  |               |
| Home Loan Bank stock  | 343                | 340           | 962              | 684           |
| Other, including interest on federal funds sold                                   | 148                | 154           | 237              | 269           |
| <b>Total interest income</b>  | <b>38,444</b>      | <b>37,925</b> | <b>76,941</b>    | <b>75,601</b> |
| <b>Interest expense:</b>  |                    |               |                  |               |
| Interest on deposits  | 7,637              | 10,435        | 15,233           | 21,489        |
| <b>Interest on repurchase agreements and other short-term borrowings</b>          |                    |               |                  |               |
| Interest on advances from Federal Home Loan Bank                                  | 17                 | 482           | 38               | 958           |
| Interest on long-term debt  | 1,000              | 1,000         | 2,000            | 2,000         |
| <b>Total interest expense</b>   | <b>9,166</b>       | <b>12,516</b> | <b>18,318</b>    | <b>25,718</b> |
| <b>Net interest income</b>  | <b>29,278</b>      | <b>25,409</b> | <b>58,623</b>    | <b>49,883</b> |
| Provision for loan losses   | 3,106              | 4,522         | 8,828            | 6,503         |
| <b>Net interest income after provision for loan losses</b>                        | <b>26,172</b>      | <b>20,887</b> | <b>49,795</b>    | <b>43,380</b> |
| <b>Noninterest income:</b>  |                    |               |                  |               |
| Service charges on deposit accounts   | 5,949              | 5,517         | 11,246           | 10,466        |
| Gains on sales of loans, net  | 337                | 1,309         | 779              | 3,240         |
| Trust income  | 1,458              | 1,249         | 2,882            | 2,411         |
| Loan related fees   | 46                 | 1,494         | 886              | 2,242         |
| Bank owned life insurance   | 407                | 287           | 812              | 543           |
| Securities gains (losses)   | 0                  | (4)           | 0                | 515           |
| Other   | 1,345              | 1,103         | 2,678            | 2,291         |
| <b>Total noninterest income</b>   | <b>9,542</b>       | <b>10,955</b> | <b>19,283</b>    | <b>21,708</b> |
| <b>Noninterest expense:</b>   |                    |               |                  |               |
| Salaries and employee benefits  | 11,632             | 10,650        | 23,077           | 21,918        |
| Occupancy, net  | 1,742              | 1,714         | 3,483            | 3,518         |
| Equipment   | 959                | 1,269         | 1,942            | 2,388         |
| Data processing   | 1,697              | 1,514         | 3,283            | 3,001         |
| Bank franchise tax  | 977                | 918           | 1,955            | 1,828         |
| Legal and professional fees   | 1,014              | 924           | 1,838            | 1,994         |
| FDIC insurance  | 1,140              | 2,250         | 2,139            | 3,746         |
| Other real estate owned provision and expense                                     | 606                | 386           | 1,478            | 899           |

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|   |         |         |          |          |
|---|---------|---------|----------|----------|
| Other   | 3,888   | 3,953   | 7,901    | 8,083    |
| Total noninterest expense                                 | 23,655  | 23,578  | 47,096   | 47,375   |
| Income before income taxes                                | 12,059  | 8,264   | 21,982   | 17,713   |
| Income taxes  | 3,506   | 2,327   | 6,638    | 5,196    |
| Net income  | 8,553   | 5,937   | 15,344   | 12,517   |
| Other comprehensive income, net of tax:                   |         |         |          |          |
| Unrealized holding gains on securities available-for-sale | 964     | 56      | 1,281    | 1,142    |
| Comprehensive income                                      | \$9,517 | \$5,993 | \$16,625 | \$13,659 |
| Basic earnings per share                                  | \$0.56  | \$0.39  | \$1.01   | \$0.83   |
| Diluted earnings per share                                | \$0.56  | \$0.39  | \$1.01   | \$0.82   |
| Weighted average shares outstanding-basic                 | 15,228  | 15,127  | 15,215   | 15,101   |
| Weighted average shares outstanding-diluted               | 15,305  | 15,219  | 15,252   | 15,194   |
| Dividends declared per share                              | \$0.30  | \$0.30  | \$0.60   | \$0.60   |

See notes to condensed consolidated financial statements.

Community Trust Bancorp, Inc.  
Condensed Consolidated Statements of Cash Flows  
(unaudited)

|  | Six Months Ended |            |
|--|------------------|------------|
|  | June 30          |            |
| (in thousands)   | 2010             | 2009       |
| <b>Cash flows from operating activities:</b>   |                  |            |
| Net income   | \$15,344         | \$12,517   |
| <b>Adjustments to reconcile net income to net cash provided by operating activities:</b> |                  |            |
| Depreciation and amortization  | 2,326            | 2,712      |
| Deferred taxes   | 0                | 581        |
| Stock based compensation   | 380              | 283        |
| Excess tax benefits of stock-based compensation  | 21               | 313        |
| Provision for loan and other real estate losses  | 9,223            | 7,030      |
| Securities gains   | 0                | (515 )     |
| Gains on sale of mortgage loans held for sale  | (779 )           | (3,240 )   |
| (Gains) losses on sale of assets, net  | 16               | (11 )      |
| Proceeds from sale of mortgage loans held for sale                                       | 36,794           | 162,972    |
| Funding of mortgage loans held for sale  | (35,663 )        | (159,708 ) |
| Amortization of securities premiums, net   | 954              | 929        |
| Change in cash surrender value of bank owned life insurance                              | (695 )           | (444 )     |
| Mortgage servicing rights  |                  |            |
| Fair value adjustments   | 981              | (237 )     |
| New servicing assets created   | (267 )           | (1,002 )   |
| <b>Changes in:</b>   |                  |            |
| Other liabilities  | 5,695            | 8,785      |
| Other assets   | 265              | 467        |
| Net cash provided by operating activities  | 34,595           | 31,432     |
| <b>Cash flows from investing activities:</b>   |                  |            |
| <b>Certificates of deposit in other banks</b>  |                  |            |
| Purchase of certificates of deposit  | (16,363 )        | (29,400 )  |
| Maturity of certificates of deposit  | 955              | 0          |
| <b>Securities available-for-sale:</b>  |                  |            |
| Proceeds from sales  | 43,358           | 37,451     |
| Proceeds from prepayments and maturities   | 5,005            | 51,744     |
| Purchase of securities   | (129,723 )       | (118,454 ) |
| <b>Securities held-to-maturity:</b>  |                  |            |
| Proceeds from prepayments and maturities   | 13,153           | 6,179      |
| Purchase of securities   | (480 )           | (480 )     |
| Change in loans, net   | (17,230 )        | (49,582 )  |
| Purchase of premises and equipment   | (1,170 )         | (1,900 )   |
| Proceeds from sale of premises and equipment   | 2                | 24         |
| Additional investment in equity securities   | (6 )             | (8 )       |
| Proceeds from sale of other real estate and other repossessed assets                     | 3,304            | 2,155      |
| Additional investment in other real estate owned   | (185 )           | (508 )     |
| Additional investment in bank owned life insurance                                       | 0                | (945 )     |



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|  |  |             |              |
|--|--|-------------|--------------|
| Net cash used in investing activities  |  | \$(99,380 ) | \$(103,724 ) |
| <b>Cash flows from financing activities:</b>                                   |  |             |              |
| Change in deposits, net  |  | \$108,918   | \$62,119     |
| Change in repurchase agreements and other short-term borrowings, net           |  | (924 )      | 3,088        |
| Payments on advances from Federal Home Loan Bank                               |  | (612 )      | (31 )        |
| Issuance of common stock   |  | 975         | 1,375        |
| Excess tax benefits of stock-based compensation                                |  | (21 )       | (313 )       |
| Dividends paid   |  | (9,115 )    | (9,045 )     |
| Net cash provided by financing activities                                      |  | 99,221      | 57,193       |
| Net increase (decrease) in cash and cash equivalents                           |  | 34,436      | (15,099 )    |
| Cash and cash equivalents at beginning of period                               |  | 142,129     | 140,878      |
| Cash and cash equivalents at end of period                                     |  | \$176,565   | \$125,779    |
| <b>Supplemental disclosures:</b>   |  |             |              |
| Income taxes paid  |  | \$4,200     | \$3,468      |
| Interest paid  |  | 15,288      | 23,353       |
| <b>Non-cash activities</b>   |  |             |              |
| Loans to facilitate the sale of other real estate and other repossessed assets |  | 146         | 281          |
| Common stock dividends accrued, paid in subsequent quarter                     |  | 4,568       | 4,540        |
| Real estate acquired in settlement of loans                                    |  | 6,599       | 12,357       |

See notes to condensed consolidated financial statements.

Community Trust Bancorp, Inc.  
Notes to Condensed Consolidated Financial Statements (unaudited)

Note 1 - Summary of Significant Accounting Policies

In the opinion of management, the unaudited condensed consolidated financial statements include all adjustments (which consist of normal recurring accruals) necessary, to present fairly the condensed consolidated financial position as of June 30, 2010, the results of operations for the three and six months ended June 30, 2010 and 2009, and the cash flows for the six months ended June 30, 2010 and 2009. In accordance with accounting principles generally accepted in the United States of America for interim financial information, these statements do not include certain information and footnote disclosures required by accounting principles generally accepted in the United States of America for complete annual financial statements. The results of operations for the three and six months ended June 30, 2010 and 2009, and the cash flows for the six months ended June 30, 2010 and 2009, are not necessarily indicative of the results to be expected for the full year. The condensed consolidated balance sheet as of December 31, 2009 has been derived from the audited consolidated financial statements of Community Trust Bancorp, Inc. ("CTBI") for that period. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended December 31, 2009, included in CTBI's Annual Report on Form 10-K.

**Principles of Consolidation** – The unaudited condensed consolidated financial statements include the accounts of CTBI and its separate and distinct, wholly owned subsidiaries Community Trust Bank, Inc. (the "Bank") and Community Trust and Investment Company. All significant intercompany transactions have been eliminated in consolidation.

**Reclassifications** – Certain reclassifications considered to be immaterial have been made in the prior year condensed consolidated financial statements to conform to current year classifications. These reclassifications had no effect on net income.

**New Accounting Standards** –

Ø **Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities** – ASC 260, formerly FASB Staff Position (FSP) EITF 03-6-1, addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing earnings per share under the two-class method described in ASC 260-10-45, formerly paragraphs 60 and 61 of FASB Statement No. 128, Earnings Per Share. This standard was effective January 1, 2009, and did not have a significant impact on our consolidated financial statements.

Ø **Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly** – ASC 820, formerly FSP FAS 157-4, affirms that the objective of fair value when the market for an asset is not active is the price that would be received to sell the asset in an orderly transaction and clarifies and includes additional factors for determining whether there has been a significant decrease in market activity for an asset when the market for that asset is not active. ASC 820 requires an entity to base its conclusion about whether a transaction was not orderly on the weight of the evidence. This standard is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. CTBI did not elect to early adopt. This standard did not have a significant impact on our consolidated financial statements.

Ø **Recognition and Presentation of Other Than Temporary Impairments** – ASC 320, formerly FSP FAS 115-2 and FSP FAS 124-2, (i) changes existing guidance for determining whether an impairment is other than temporary to debt

securities and (ii) replaces the existing requirement that the entity's management assert it has both the intent and ability to hold an impaired security until recovery with a requirement that management assert: (a) it does not have the intent to sell the security; and (b) it is more likely than not it will not have to sell the security before recovery of its cost basis. Under ASC 320, declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of the impairment related to other factors is recognized in other comprehensive income. This standard is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. CTBI did not elect to early adopt. This standard did not have a significant impact on our consolidated financial statements.

Ø Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies – ASC 805, formerly FSP FAS 141(R)-1, requires that assets acquired and liabilities assumed in a business combination that arise from contingencies be recognized at fair value if fair value can be reasonably estimated. If fair value of such an asset or liability cannot be reasonably estimated, the asset or liability would generally be recognized in accordance with ASC 450, formerly FAS 5, Accounting for Contingencies and FASB Interpretation No. (FIN) 14, Reasonable Estimation of the Amount of a Loss. ASC 805 removes subsequent accounting guidance for assets and liabilities arising from contingencies and requires entities to develop a systematic and rational basis for subsequently measuring and accounting for assets and liabilities arising from contingencies. This standard also eliminates the requirement to disclose an estimate of the range of outcomes of recognized contingencies at the acquisition date. For unrecognized contingencies, entities are required to include only the disclosures required by ASC 450, formerly FAS 5. The standard also requires that contingent consideration arrangements of an acquiree assumed by the acquirer in a business combination be treated as contingent consideration of the acquirer and should be initially and subsequently measured at fair value in accordance with the standard. This standard is effective for assets or liabilities arising from contingencies CTBI acquires in business combinations occurring after January 1, 2009.

Ø Accounting for Transfers of Financial Assets – In June 2009, the FASB issued ASC 860, formerly FAS 166, Accounting for Transfers of Financial Assets — An Amendment of FAS 140. ASC 860 removes the concept of a qualifying special-purpose entity and limits the circumstances in which a financial asset, or portion of a financial asset, should be derecognized when the transferor has not transferred the entire financial asset to an entity that is not consolidated with the transferor in the financial statements being presented and/or when the transferor has continuing involvement with the transferred financial asset. The new standard became effective for CTBI on January 1, 2010. The adoption of this standard did not have a material impact on CTBI's consolidated financial position or results of operations.

Ø Determining When to Consolidate Variable Purpose Entities – In June 2009, the FASB issued ASC 810, formerly FAS 167 — Amendments to FASB Interpretation No. 46(R). ASC 810 requires an entity to perform an analysis to determine whether an entity's variable interest or interests give it a controlling financial interest in a variable interest entity. This standard requires ongoing reassessments of whether an entity is the primary beneficiary of a variable interest entity and enhanced disclosures that provide more transparent information about an entity's involvement with a variable interest entity. The new standard became effective for CTBI on January 1, 2010. The adoption of this standard did not have a material impact on CTBI's consolidated financial position or results of operations.

Ø Codification of Authoritative Accounting Principles – In June 2009, the FASB issued ASC 105, formerly FAS 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles. ASC 105 establishes the FASB Accounting Standards Codification as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with generally accepted accounting principles ("GAAP"). Rules and interpretative releases of the Securities and Exchange Commission under federal securities laws are also sources of authoritative GAAP for SEC registrants. The new standard became effective for financial statements issued for interim and annual periods ending after September 15, 2009. The adoption of this standard did not have a material impact on CTBI's consolidated financial position or results of operations.

Ø Disclosures Regarding Postretirement Benefit Plan Assets – In December 2008, the FASB issued ASC 715, formerly FSP FAS 132(R)-1, Employers' Disclosures about Postretirement Benefit Plan Assets. This standard requires disclosure of the fair value of each major category of plan assets for pension plans and other postretirement benefit plans. The new standard became effective for CTBI on January 1, 2010. The adoption of this standard did not have a material impact on CTBI's consolidated financial position or results of operations.

Ø Improving Disclosures about Fair Value Measurements – In January 2010, the FASB released Accounting Standards Update (ASU) 2010-06, Improving Disclosures about Fair Value Measurements. ASU 2010-06 amends ASC Subtopic 820, Fair Value Measurements and Disclosures, and Subtopic 715-20, Compensation—Retirement Benefits—Defined Benefit Plans. The new standard expands the existing fair value disclosures required by these two subtopics. Additional disclosures required by the new standard must be made for each period beginning after the effective date. Expansion of disclosures for prior periods to include those required by the ASU is optional.

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Disclosure changes made by ASU 2010-06 include:

- The amounts of and reasons for significant transfers in and out of Level 1, Level 2 and Level 3 fair value measurements and the accounting policy for the date used to recognize such transfers, e.g., actual transaction date, beginning of reporting period date or end of reporting period date
- Presentation of purchases, sales, issuances and settlements as separate lines, rather than one net number, in the table reconciling activity for assets and liabilities measured at fair value on a recurring basis using Level 3 inputs
- Provision of fair value measurement disclosures for each class of assets and liabilities with a class often being a subset of assets or liabilities within a balance sheet line item. Class should be determined on the basis of the nature and risks of investments in debt and equity securities and generally will not require change from the classifications already employed in disclosures for those investments
- Provision of explanations about the valuation techniques and inputs used to determine fair value for both recurring and nonrecurring fair value measurements falling in either Level 2 or Level 3
- Revision of the existing disclosures made by a plan sponsor about fair value for assets of defined benefit pension and other postretirement benefit plans to require those disclosures be made by asset class instead of asset category

ASU 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009, with early adoption permitted. The one exception involves reporting certain items gross instead of net in the existing activity table for items measured at fair value on a recurring basis using Level 3 inputs, which is effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years and may be adopted earlier if desired. Except for the Level 3 table item, each SEC issuer must apply the ASU starting with its first interim period beginning after December 15, 2009. CTBI did not elect to early adopt the provisions which are effective for years beginning after December 15, 2009 or the December 15, 2010 provisions. ASU 2010-06 has not and is not expected to have a material impact on CTBI's consolidated financial statements.

Ø Effect of a Loan Modification When the Loan is Part of a Pool that is Accounted for as a Single Asset – a consensus of the FASB Emerging Issues Task Force – In April 2010, the FASB issued ASU No. 2010-18, Receivables (Topic 310) – Effect of a Loan Modification When the Loan is Part of a Pool that is Accounted for as a Single Asset – a consensus of the FASB Emerging Issues Task Force. ASU 2010-18 provides guidance on account for acquired loans that have evidence of credit deterioration upon acquisition. It allows acquired assets with common risk characteristics to be accounted for in the aggregate as a pool. ASU 2010-18 is effective for modifications of loans accounted for within pools under Subtopic 310-30 in the first interim or annual reporting period ending on or after July 15, 2010. We do not expect ASU 2010-18 to have an impact on our financial condition, results of operations, or disclosures.

Ø Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses – In July 2010, the FASB released ASU 2010-20, Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. The standard will help investors assess the credit risk of a company's receivables portfolio and the adequacy of its allowance for credit losses held against the portfolios by expanding credit risk disclosures. Companies will be required to provide more information about the credit quality of their financing receivables in the disclosures to financial statements, such as aging information and credit quality indicators. Both new and existing disclosures must be disaggregated by portfolio segment or class. The disaggregation of information is based on how a company develops its allowance for credit losses and how it manages its credit exposure.

The standard will require CTBI to expand disclosures about the credit quality of our loans and the related reserves against them. The additional disclosures will include details on our past due loans, credit quality indicators, and modifications of loans. CTBI will adopt the standard beginning with our December 31, 2010 financial statements.

#### Note 2 – Stock-Based Compensation

CTBI's compensation expense related to stock option grants was \$198 thousand and \$238 thousand, respectively, for the six months ended June 30, 2010 and 2009, respectively. Restricted stock expense for the first six months of 2010 and 2009 was \$182 thousand and \$45 thousand, respectively. As of June 30, 2010, there was a total of \$0.4 million of unrecognized compensation expense related to unvested stock option awards that will be recognized as expense as the awards vest over a weighted average period of 1.9 years.

There were options to purchase 4,525 shares of CTBI common stock and 44,996 shares of restricted stock granted during the six months ended June 30, 2010. The options were granted pursuant to the terms of the 2006 Stock Ownership Incentive Plan, with an exercise price per share of \$25.09 (equal to fair market value on date of grant), a term of 10 years, and vesting in five years. The restrictions on the restricted stock will lapse at the end of five years. However, in the event of a change in control of CTBI or the death of the participant, the restrictions will lapse. In the event of the disability of the participant, the restrictions will lapse on a pro rata basis (with respect to 20% of the participant's restricted stock for each year since the date of award). The Compensation Committee of the Board of Directors will have discretion to review and revise restrictions applicable to a participant's restricted stock in the event of the participant's retirement. There were options to purchase 9,000 shares of CTBI common stock and 5,710 shares of restricted stock granted during the six months ended June 30, 2009.

The fair values of options granted during the six months ended June 30, 2010 and 2009, were established at the date of grant using a Black-Scholes option pricing model with the weighted average assumptions as follows:

|  | Six Months Ended |   |        |   |
|--|------------------|---|--------|---|
|  | 2010             |   | 2009   |   |
|  |                  |   |        |   |
| Expected dividend yield                | 4.78             | % | 4.02   | % |
| Risk-free interest rate                | 3.14             | % | 2.23   | % |
| Expected volatility                    | 39.12            | % | 37.12  | % |
| Expected term (in years)               | 7.5              |   | 7.5    |   |
| Weighted average fair value of options | \$6.53           |   | \$7.69 |   |

#### Note 3 – Securities

Securities are classified into held-to-maturity and available-for-sale categories. Held-to-maturity securities are those that CTBI has the positive intent and ability to hold to maturity and are reported at amortized cost. Available-for-sale securities are those that CTBI may decide to sell if needed for liquidity, asset-liability management or other reasons. Available-for-sale securities are reported at fair value, with unrealized gains or losses included as a separate component of equity, net of tax.

The amortized cost and fair value of securities at June 30, 2010 are summarized as follows:

Available-for-Sale

| (in thousands)                        | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value |
|---------------------------------------|-------------------|------------------------------|-------------------------------|------------|
| U.S. Treasury and government agencies | \$16,989          | \$352                        | \$0                           | \$17,341   |
| State and political subdivisions      | 40,554            | 1,015                        | (38 )                         | 41,531     |
| U.S. government sponsored agencies    | 238,495           | 7,120                        | (111 )                        | 245,504    |
| Collateralized mortgage obligations   | 27,585            | 47                           | (106 )                        | 27,526     |
| Total debt securities                 | 323,623           | 8,534                        | (255 )                        | 331,902    |
| Marketable equity securities          | 20,540            | 357                          | (183 )                        | 20,714     |
| Total available-for-sale securities   | \$344,163         | \$8,891                      | \$(438 )                      | \$352,616  |

Held-to-Maturity

| (in thousands)                    | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value |
|-----------------------------------|-------------------|------------------------------|-------------------------------|------------|
| State and political subdivisions  | \$1,182           | \$0                          | \$0                           | \$1,182    |
| Other debt securities             | 480               | 0                            | 0                             | 480        |
| Total held-to-maturity securities | \$1,662           | \$0                          | \$0                           | \$1,662    |

The amortized cost and fair value of securities as of December 31, 2009 are summarized as follows:

Available-for-Sale

| (in thousands)                        | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value |
|---------------------------------------|-------------------|------------------------------|-------------------------------|------------|
| U.S. Treasury and government agencies | \$16,994          | \$20                         | \$(283 )                      | \$16,731   |
| State and political subdivisions      | 44,529            | 1,222                        | (94 )                         | 45,657     |
| U.S. government sponsored agencies    | 181,693           | 5,787                        | (83 )                         | 187,397    |
| Total debt securities                 | 243,216           | 7,029                        | (460 )                        | 249,785    |
| Marketable equity securities          | 20,540            | 97                           | (185 )                        | 20,452     |
| Total available-for-sale securities   | \$263,756         | \$7,126                      | \$(645 )                      | \$270,237  |

Held-to-Maturity

| (in thousands)                     | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value |
|------------------------------------|-------------------|------------------------------|-------------------------------|------------|
| State and political subdivisions   | \$1,576           | \$6                          | \$0                           | \$1,582    |
| U.S. government sponsored agencies | 12,280            | 93                           | 0                             | 12,373     |
| Other debt securities              | 480               | 0                            | 0                             | 480        |
| Total held-to-maturity securities  | \$14,336          | \$99                         | \$0                           | \$14,435   |

The amortized cost and fair value of securities at June 30, 2010 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations

with or without call or prepayment penalties.

| (in thousands)                      | Available-for-Sale |            | Held-to-Maturity |            |
|-------------------------------------|--------------------|------------|------------------|------------|
|                                     | Amortized Cost     | Fair Value | Amortized Cost   | Fair Value |
| Due in one year or less             | \$5,772            | \$5,825    | \$0              | \$0        |
| Due after one through five years    | 14,667             | 15,207     | 0                | 0          |
| Due after five through ten years    | 24,066             | 24,549     | 0                | 0          |
| Due after ten years                 | 13,038             | 13,291     | 1,182            | 1,182      |
| U.S. government sponsored agencies  | 238,495            | 245,504    | 0                | 0          |
| Collateralized mortgage obligations | 27,585             | 27,526     | 0                | 0          |
| Other securities                    | 0                  | 0          | 480              | 480        |
| Total debt securities               | 323,623            | 331,902    | 1,662            | 1,662      |
| Marketable equity securities        | 20,540             | 20,714     | 0                | 0          |
| Total securities                    | \$344,163          | \$352,616  | \$1,662          | \$1,662    |

There were no pre-tax gains or losses as of June 30, 2010. There was a combined gain of \$519 thousand realized in the first six months of 2009 due to sales of five securities and a loss of \$4 thousand due to a sale of one security in 2009.

The carrying value of securities pledged as collateral, to secure public deposits and for other purposes, was \$104.0 million at June 30, 2010 and \$89.2 million at December 31, 2009.

The book value of securities sold under agreements to repurchase amounted to \$181.1 million at June 30, 2010 and \$179.9 million at December 31, 2009.



CTBI evaluates its investment portfolio on a quarterly basis for impairment. The analysis performed as of June 30, 2010 indicates that all impairment is considered temporary, market driven, and not credit-related. The percentage of total investments with unrealized losses as of June 30, 2010 was 7.6% compared to 8.5% as of December 31, 2009. The following tables provide the amortized cost, gross unrealized losses, and fair market value, aggregated by investment category and length of time the individual securities have been in a continuous unrealized loss position as of June 30, 2010 that are not deemed to be other-than-temporarily impaired.

## Available-for-Sale

| (in thousands)                      | Amortized<br>Cost | Gross<br>Unrealized<br>Losses | Fair Value |
|-------------------------------------|-------------------|-------------------------------|------------|
| <b>Less Than 12 Months</b>          |                   |                               |            |
| States and political subdivision    | \$2,632           | \$(19 )                       | \$2,613    |
| U.S. government sponsored agencies  | 7,890             | (111 )                        | 7,779      |
| Collateralized mortgage obligations | 15,116            | (106 )                        | 15,010     |
| Total debt securities               | 25,638            | (236 )                        | 25,402     |
| Marketable equity securities        | 0                 | 0                             | 0          |
| Total securities                    | 25,638            | (236 )                        | 25,402     |
| <b>12 Months or More</b>            |                   |                               |            |
| States and political subdivision    | 1,385             | (20 )                         | 1,365      |
| U.S. government sponsored agencies  | 0                 | 0                             | 0          |
| Collateralized mortgage obligations | 0                 | 0                             | 0          |
| Total debt securities               | 1,385             | (20 )                         | 1,365      |
| Marketable equity securities        | 329               | (183 )                        | 146        |
| Total securities                    | 1,714             | (203 )                        | 1,511      |
| <b>Total</b>                        |                   |                               |            |
| States and political subdivision    | 4,017             | (38 )                         | 3,978      |
| U.S. government sponsored agencies  | 7,890             | (111 )                        | 7,779      |
| Collateralized mortgage obligations | 15,116            | (106 )                        | 15,010     |
| Total debt securities               | 27,023            | (255 )                        | 26,767     |
| Marketable equity securities        | 329               | (183 )                        | 146        |
| Total securities                    | \$27,352          | \$(438 )                      | \$26,913   |

As of June 30, 2010, there were no held-to-maturity securities with unrealized losses.

The analysis performed as of December 31, 2009 indicated that all impairment was considered temporary, market driven, and not credit-related. The following tables provide the amortized cost, gross unrealized losses, and fair market value, aggregated by investment category and length of time the individual securities have been in a continuous unrealized loss position as of December 31, 2009 that are not deemed to be other-than-temporarily impaired.

## Available-for-Sale

| (in thousands)             | Amortized<br>Cost | Gross<br>Unrealized<br>Losses | Fair Value |
|----------------------------|-------------------|-------------------------------|------------|
| <b>Less Than 12 Months</b> |                   |                               |            |

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|                                       |           |        |   |           |
|---------------------------------------|-----------|--------|---|-----------|
| U.S. Treasury and government agencies | \$ 14,992 | \$(283 | ) | \$ 14,709 |
| States and political subdivision      | 2,567     | (55    | ) | 2,512     |
| U.S. government sponsored agencies    | 5,013     | (83    | ) | 4,930     |
| Total debt securities                 | 22,572    | (421   | ) | 22,151    |
| Marketable equity securities          | 540       | (185   | ) | 355       |
| Total securities                      | 23,112    | (606   | ) | 22,506    |
| 12 Months or More                     |           |        |   |           |
| U.S. Treasury and government agencies | 0         | 0      |   | 0         |
| States and political subdivision      | 1,601     | (39    | ) | 1,562     |
| U.S. government sponsored agencies    | 0         | 0      |   | 0         |
| Total debt securities                 | 1,601     | (39    | ) | 1,562     |
| Marketable equity securities          | 0         | 0      |   | 0         |
| Total securities                      | 1,601     | (39    | ) | 1,562     |
| Total                                 |           |        |   |           |
| U.S. Treasury and government agencies | 14,992    | (283   | ) | 14,709    |
| States and political subdivision      | 4,168     | (94    | ) | 4,074     |
| U.S. government sponsored agencies    | 5,013     | (83    | ) | 4,930     |
| Total debt securities                 | 24,173    | (460   | ) | 23,713    |
| Marketable equity securities          | 540       | (185   | ) | 355       |
| Total securities                      | \$24,713  | \$(645 | ) | \$24,068  |

As of December 31, 2009, there were no held-to-maturity securities with unrealized losses.

## Note 4 – Loans

Major classifications of loans, net of unearned income and deferred loan origination costs, are summarized as follows:

| (in thousands)                    | June 30<br>2010 | December<br>31<br>2009 |
|-----------------------------------|-----------------|------------------------|
| Commercial construction           | \$142,847       | \$141,440              |
| Commercial secured by real estate | 761,646         | 707,500                |
| Commercial other                  | 347,284         | 373,829                |
| Real estate construction          | 47,957          | 51,311                 |
| Real estate mortgage              | 616,618         | 610,727                |
| Consumer                          | 507,724         | 530,905                |
| Equipment lease financing         | 17,146          | 20,048                 |
| Total loans                       | \$2,441,222     | \$2,435,760            |

Not included in the loan balances above were loans held for sale in the amount of \$1.5 million and \$1.8 million at June 30, 2010 and December 31, 2009, respectively. The amount of capitalized fees and costs under ASC 310, formerly SFAS 91, Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases, included in the above loan totals were \$0.7 million at June 30, 2010 and \$0.6 million at December 31, 2009.

Total nonperforming loans were as follows:

| (in thousands)   | June 30<br>2010 | December<br>31<br>2009 |
|--|-----------------|------------------------|
| Homogeneous pools of nonaccrual loans                  | \$7,073         | \$5,643                |
| Nonaccrual loans individually evaluated for impairment | 38,362          | 26,604                 |
| Total nonaccrual loans                                 | 45,435          | 32,247                 |
| Loans greater than 90 days past due                    | 16,857          | 9,067                  |
| Total nonperforming loans                              | \$62,292        | \$41,314               |

Additional interest which would have been recorded for the quarter ended June 30, 2010 was \$0.9 million compared to \$0.4 million and \$0.8 million for quarters ended December 31, 2009 and June 30, 2009, respectively. Any loan greater than 90 days past due must be well secured and in the process of collection to continue accruing interest.

A loan is considered impaired, in accordance with the impairment accounting guidance (ASC 310-10-35-16), when based on current information and events, it is probable CTBI will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming commercial loans but also include loans modified in troubled debt restructurings where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance or other actions intended to maximize collection.

The recorded investments in impaired loans are summarized below:

| (in thousands) | June 30<br>2010 | December<br>31<br>2009 |
|----------------|-----------------|------------------------|
|----------------|-----------------|------------------------|

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|  |          |          |
|--|----------|----------|
| Impaired loans without specific reserves | \$26,143 | \$12,775 |
| Impaired loans with specific reserves    | 28,443   | 19,231   |
| Restructured loans                       | 5,604    | 6        |
| Total impaired loans                     | \$60,190 | \$32,012 |

Specific reserves for impaired loans totaled \$9.3 million at June 30, 2010 compared to \$6.6 million at December 31, 2009. The average investment in impaired loans was \$54.7 million and \$30.2 million at June 30, 2010 and December 31, 2009, respectively.

Cash payments on impaired loans were as follows:

| (in thousands)                       | June 30<br>2010 | June 30<br>2009 |
|--------------------------------------|-----------------|-----------------|
| Interest payments on impaired loans  | \$240           | \$252           |
| Principal payments on impaired loans | 1,159           | 1,523           |
| Total payments                       | \$1,399         | \$1,775         |

Activity in the allowance for loan and lease losses was as follows:

| (in thousands)                                    | Six Months Ended<br>June 30 |          |
|---|-----------------------------|----------|
|   | 2010                        | 2009     |
| Allowance balance at January 1                    | \$32,643                    | \$30,821 |
| Additions to allowance charged against operations | 8,828                       | 6,503    |
| Recoveries credited to allowance                  | 1,618                       | 1,668    |
| Losses charged against allowance                  | (6,933 )                    | (7,570 ) |
| Allowance balance at June 30                      | \$36,156                    | \$31,422 |

## Note 5 – Mortgage Banking and Servicing Rights

Mortgage banking activities primarily include residential mortgage originations and servicing. Mortgage servicing rights (“MSRs”) are carried at fair market value. The fair value is determined quarterly based on an independent third-party valuation using a discounted cash flow analysis and calculated using a computer pricing model. The computer valuation is based on key economic assumptions including the prepayment speeds of the underlying loans, the weighted-average life of the loan, the discount rate, the weighted-average coupon, and the weighted-average default rate, as applicable. Along with the gains received from the sale of loans, fees are received for servicing loans. These fees include late fees, which are recorded in interest income, and ancillary fees and monthly servicing fees, which are recorded in noninterest income. Costs of servicing loans are charged to expense as incurred. Changes in fair market value of the MSRs are reported as an increase or decrease to mortgage banking income.

The following table presents the components of mortgage banking income:

| (in thousands)                          | Three Months Ended |         | Six Months Ended |         |
|---|--------------------|---------|------------------|---------|
|   | June 30            |         | June 30          |         |
|   | 2010               | 2009    | 2010             | 2009    |
| Net gain on sale of loans held for sale | \$337              | \$1,309 | \$779            | \$3,240 |
| Net loan servicing income (loss)        |                    |         |                  |         |
| Servicing fees                          | 275                | 262     | 548              | 500     |
| Late fees                               | 18                 | 15      | 34               | 33      |
| Ancillary fees                          | 57                 | 161     | 123              | 388     |
| Fair value adjustments                  | (855 )             | 511     | (981 )           | 237     |
| Net loan servicing income (loss)        | (505 )             | 949     | (276 )           | 1,158   |
| Mortgage banking income (loss)          | \$(168 )           | \$2,258 | \$503            | \$4,398 |

Mortgage loans serviced for others are not included in the accompanying balance sheets. Mortgage loans serviced for the benefit of others (primarily FHLMC) at June 30, 2010, December 31, 2009, and June 30, 2009, were \$438 million, \$431 million, and \$425 million, respectively. Servicing loans for others generally consists of collecting mortgage payments, maintaining escrow accounts, disbursing payments to investors, and processing foreclosures. Custodial escrow balances maintained in connection with the foregoing loan servicing, and included in demand deposits, were approximately \$1.2 million at June 30, 2010, \$0.6 million at December 31, 2009, and \$1.2 million at June 30, 2009.

Activity for capitalized mortgage servicing rights using the fair value method was as follows:

| (in thousands)                                 | Six Months Ended |         |
|--|------------------|---------|
|  | June 30          |         |
|  | 2010             | 2009    |
| Fair value, beginning of period                | \$3,406          | \$2,168 |
| New servicing assets created                   | 267              | 1,002   |
| Change in fair value during the period due to: |                  |         |
| Time decay (1)                                 | (74 )            | (76 )   |
| Payoffs (2)                                    | (58 )            | (392 )  |
| Changes in valuation inputs or assumptions (3) | (849 )           | 705     |
| Fair value, end of period                      | \$2,692          | \$3,407 |

(1) Represents decrease in value due to regularly scheduled loan principal payments and partial loan paydowns.

(2) Represents decrease in value due to loans that paid off during the period.

(3) Represents change in value resulting from market-driven changes in interest rates and prepayment speeds.

The fair value of capitalized mortgage servicing rights was \$2.7 million at June 30, 2010 compared to \$3.4 million at December 31, 2009 and \$3.4 million at June 30, 2009. Fair values were determined by third-party valuations using a discount rate of 10.0% for the quarters ended June 30, 2010, December 31, 2009 and June 30, 2009, and weighted average default rates of 2.1%, 1.9% and 1.5% respectively. Prepayment speeds generated using the Andrew Davidson Prepayment Model averaged 17.9%, 13.6%, and 13.3% at June 30, 2010, December 31, 2009, and June 30, 2009, respectively. MSR values are very sensitive to movement in interest rates as expected future net servicing income depends on the projected balance of the underlying loans, which can be greatly impacted by the level of prepayments. CTBI does not currently hedge against changes in the fair value of its MSR portfolio.

#### Note 6 – Other Real Estate Owned

Activity for foreclosed properties during the six months ended June 30, 2010 and 2009 was as follows:

| (in thousands)               | 2010     | 2009     |
|------------------------------|----------|----------|
| Beginning balance, January 1 | \$37,333 | \$10,425 |
| New assets acquired          | 6,450    | 12,358   |
| Capitalized costs            | 185      | 508      |
| Fair value adjustments       | (395 )   | (517 )   |
| Sale of assets               | (3,468 ) | (2,405 ) |
| Ending balance, June 30      | \$40,105 | \$20,369 |

Carrying costs and fair value adjustments associated with foreclosed properties at June 30, 2010 and 2009, respectively, were \$1.5 million and \$0.9 million.

#### Note 7 – Borrowings

Short-term debt consists of the following:

| (in thousands)          | June 30<br>2010 | December<br>31<br>2009 |
|-------------------------|-----------------|------------------------|
| Subsidiaries:           |                 |                        |
| Repurchase agreements   | \$183,287       | \$180,471              |
| Federal funds purchased | 8,465           | 12,205                 |
| Total short-term debt   | \$191,752       | \$192,676              |

On October 28, 2009, Community Trust Bancorp, Inc. entered into a revolving credit promissory note for a line of credit in the amount of \$12 million at a floating interest rate of 2.25% in excess of the one-month LIBOR Rate. An unused commitment fee of 0.15% has been established. Currently, all \$12 million remain available for general corporate purposes. The agreement, which was effective October 29, 2009, replaced the agreement dated July 29, 2008, and will mature on October 28, 2010.

All federal funds purchased and the majority of repurchase agreements mature and reprice daily. The average rates paid for federal funds purchased and repurchase agreements on June 30, 2010 were 0.15% and 1.09%, respectively.

The maximum balance for repurchase agreements at any month-end during the second quarter 2010 occurred at May 31, 2010, with a month-end balance of \$191.5 million. The average balance of repurchase agreements for the quarter was \$184.8 million.



Federal Home Loan Bank advances consisted of the following monthly amortizing and term borrowings:

| (in thousands)     | June 30<br>2010 | December<br>31<br>2009 |
|--------------------|-----------------|------------------------|
| Monthly amortizing | \$59            | \$671                  |
| Term               | 20,000          | 20,000                 |
| Total advances     | \$20,059        | \$20,671               |

The advances from the Federal Home Loan Bank that require monthly principal payments were due for repayment as follows:

| (in thousands)   | Principal Payments Due by Period at June 30, 2010 |                  |         |         |         |         |                  |
|--|---|------------------|---------|---------|---------|---------|------------------|
|  | Total   | Within 1<br>Year | 2 Years | 3 Years | 4 Years | 5 Years | After 5<br>Years |
| Outstanding<br>advances,<br>weighted average<br>interest rate –<br>1.40% | \$59  | \$9              | \$8     | \$8     | \$8     | \$7     | \$19             |

The term advances that require the total payment to be made at maturity follow:

| (in thousands)                   | June 30<br>2010 | December<br>31<br>2009 |
|----------------------------------|-----------------|------------------------|
| Advance #156, 0.43%, due 1/29/10 | \$0             | \$20,000               |
| Advance #157, 0.32%, due 7/28/10 | 20,000          | 0                      |
| Total term advances              | \$20,000        | \$20,000               |

Advances totaling \$20.1 million at June 30, 2010 were collateralized by FHLB stock of \$24.7 million and a blanket lien on qualifying first mortgage loans. As of June 30, 2010, CTBI had a \$312.1 million FHLB borrowing capacity with \$20.1 million in advances and \$98.3 million in letters of credit leaving \$193.7 million available for additional advances. The advances had fixed interest rates ranging from 0.32% to 2.00% with a weighted average rate of 0.32%. The advances are subject to restriction or penalties in the event of prepayment.

Long-term debt consists of the following:

| (in thousands)                                    | June 30<br>2010 | December<br>31<br>2009 |
|---|-----------------|------------------------|
| Junior subordinated debentures, 6.52%, due 6/1/37 | \$61,341        | \$61,341               |

On March 31, 2007, CTBI issued \$61.3 million in junior subordinated debentures to a newly formed unconsolidated Delaware statutory trust subsidiary which in turn issued \$59.5 million of capital securities in a private placement to institutional investors. The debentures, which mature in 30 years but are redeemable at par at CTBI's option after five years, were issued at a rate of 6.52% until June 1, 2012, and thereafter at a floating rate based on the three-month LIBOR plus 1.59%. The underlying capital securities were issued at the equivalent rates and terms. The proceeds of the debentures were used to fund the redemption on April 2, 2007 of all CTBI's outstanding 9.0% and 8.25% junior subordinated debentures in the total amount of \$61.3 million.



## Note 8 – Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share:

| (in thousands except per share data) | Three Months Ended |         | Six Months Ended |          |
|--------------------------------------|--------------------|---------|------------------|----------|
|                                      | June 30            |         | June 30          |          |
|                                      | 2010               | 2009    | 2010             | 2009     |
| <b>Numerator:</b>                    |                    |         |                  |          |
| Net income                           | \$8,553            | \$5,937 | \$15,344         | \$12,517 |
| <b>Denominator:</b>                  |                    |         |                  |          |
| <b>Basic earnings per share:</b>     |                    |         |                  |          |
| Weighted average shares              | 15,228             | 15,127  | 15,215           | 15,101   |
| <b>Diluted earnings per share:</b>   |                    |         |                  |          |
| Effect of dilutive stock options     | 77                 | 92      | 37               | 93       |
| Adjusted weighted average shares     | 15,305             | 15,219  | 15,252           | 15,194   |
| <b>Earnings per share:</b>           |                    |         |                  |          |
| Basic earnings per share             | \$0.56             | \$0.39  | \$1.01           | \$0.83   |
| Diluted earnings per share           | \$0.56             | \$0.39  | \$1.01           | \$0.82   |

Options to purchase 385,022 and 422,972 common shares, respectively, were excluded from the diluted calculations above for the three and six months ended June 30, 2010 because the exercise prices on the options were greater than the average market price for the period. Options to purchase 388,024 common shares were excluded from the diluted calculations above for the three and six months ended June 30, 2009.

## Note 9 – Fair Value of Financial Assets and Liabilities

ASC 820, formerly FAS 157, Fair Value Measurements, defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. ASC 820 applies whenever other standards require (or permit) assets or liabilities to be measured at fair value but does not expand the use of fair value in any new circumstances. In this standard, the FASB clarifies the principle that fair value should be based on the assumptions market participants would use when pricing the asset or liability. In support of this principle, ASC 820 establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The fair value hierarchy is as follows:

Level 1 Inputs – Quoted prices in active markets for identical assets or liabilities.

Level 2 Inputs – Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 Inputs – Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

The application of ASC 820 in situations where the market for a financial asset is not active was clarified in October 2008 by the issuance of ASC 820-10-35, formerly FSP FAS 157-3, Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active. This clarification was effective for financial statements issued as of September 30, 2008 and thereafter and did not have a material impact on the methods by which CTBI determines the

fair values of its financial assets. ASC 820 was also clarified in April 2009 effective for the second quarter 2009 by ASC 820-10-65, formerly FSP No. FAS 157-4, Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly. This section clarifies factors that determine whether transactions are orderly or not in evaluating the reliability of market transactions for fair value estimates. ASC 820-10-15, formerly FSP FAS 157-2, deferred the application of ASC 820 for nonfinancial assets and nonfinancial liabilities that are measured at fair value on a nonrecurring basis to fiscal years beginning after November 15, 2008. CTBI adopted the provisions of this standard with respect to nonfinancial assets and nonfinancial liabilities beginning on January 1, 2009.

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## Assets Measured on a Recurring Basis

The following tables present information about CTBI's assets measured at fair value on a recurring basis as of June 30, 2010 and December 31, 2009, and indicates the fair value hierarchy of the valuation techniques utilized by CTBI to determine such fair value.

| (in thousands)  | Fair Value Measurements at<br>June 30, 2010 Using |   |  |  |
|---|---|---|--|--|
|   | Fair Value<br>June 30<br>2010                     | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| Available-for-sale securities:  |   |   |  |  |
| U.S. Treasury and government agencies   | \$17,341  | \$0   | \$17,341                                   | \$ 0   |
| State and political subdivisions  | 41,531  | 0   | 41,531                                     | 0  |
| U.S. government sponsored agencies and mortgage-backed<br>pass through certificates | 273,030   | 0   | 273,030                                    | 0  |
| Marketable equity securities  | 20,714  | 0   | 20,503                                     | 211  |
| Mortgage servicing rights   | 2,692   | 0   | 0  | 2,692  |
| Total recurring assets measured at fair value                                       | \$355,308   | \$0   | \$352,405                                  | \$ 2,903   |

| (in thousands)  | Fair Value Measurements at<br>December 31, 2009 Using |   |  |  |
|---|---|---|--|--|
|   | Fair Value<br>December<br>31<br>2009                  | Quoted<br>Prices in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| Available-for-sale securities:  |   |   |  |  |
| U.S. Treasury and government agencies   | \$16,731  | \$0   | \$16,731                                   | \$ 0   |
| State and political subdivisions  | 45,657  | 0   | 45,657                                     | 0  |
| U.S. government sponsored agencies and mortgage-backed<br>pass through certificates | 187,397   | 0   | 187,397                                    | 0  |
| Marketable equity securities  | 20,452  | 0   | 20,241                                     | 211  |
| Mortgage servicing rights   | 3,406   | 0   | 0  | 3,406  |
| Total recurring assets measured at fair value                                       | \$273,643   | \$0   | \$270,026                                  | \$ 3,617   |

U.S. Treasury and government agencies, State and political subdivision, U.S. government sponsored agencies and mortgage-backed pass through certificates, Marketable equity securities – Level 2 Inputs. For these securities, CTBI obtains fair value measurements from an independent pricing service, which utilizes pricing models to determine fair value measurements. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things.

Marketable equity securities – Level 3 Inputs. The securities owned by CTBI that were measured using Level 3 criteria are auction rate securities issued by FNMA. These securities were valued using an independent third party. For these securities, the valuation methods used were (1) a discounted cash flow model valuation, where the expected cash flows of the securities are discounted to the present using a yield that incorporates compensation for illiquidity and (2) a market comparables method, where the securities are valued based on indications, from the secondary market, of what discounts buyers demand when purchasing similar securities. Using these methods, the auction rate securities are classified as Level 3.

Mortgage Servicing Rights – Level 3 Inputs. CTBI records MSR's at fair value on a recurring basis with subsequent remeasurement of MSR's based on change in fair value. In determining fair value, CTBI utilizes the expertise of an independent third party. An estimate of the fair value of CTBI's MSR's is determined by the independent third party utilizing discounted cash flow models and assumptions about mortgage interest rates, discount rates, mortgage loan prepayment speeds, market trends and industry demand. All of CTBI's MSR's are classified as Level 3.

Following is a reconciliation of the beginning and ending balances of recurring fair value measurements using significant unobservable (Level 3) inputs:

|  | Three Months Ended |       | Six Months Ended |        |
|--|--------------------|-------|------------------|--------|
|  | June 30            |       | June 30          |        |
| Marketable Equity Securities (in thousands)    | 2010               | 2009  | 2010             | 2009   |
| Beginning balance                              | \$211              | \$211 | \$211            | \$540  |
| Total realized and unrealized gains and losses |                    |       |                  |        |
| Included in net income                         | 0                  | 0     | 0                | 0      |
| Transfer of Securities from Level 3 to Level 2 | 0                  | 0     | 0                | 0      |
| Purchases                                      | 0                  | 0     | 0                | 0      |
| Issuances                                      | 0                  | 0     | 0                | 0      |
| Settlements                                    | 0                  | 0     | 0                | (329 ) |
| Ending balance                                 | \$211              | \$211 | \$211            | \$211  |

|  | Three Months Ended |         | Six Months Ended |         |
|--|--------------------|---------|------------------|---------|
|  | June 30            |         | June 30          |         |
| Mortgage Servicing Rights (in thousands)       | 2010               | 2009    | 2010             | 2009    |
| Beginning balance                              | \$3,442            | \$2,475 | \$3,406          | \$2,168 |
| Total realized and unrealized gains and losses |                    |         |                  |         |
| Included in net income                         | (834 )             | 744     | (849 )           | 705     |
| Transfer of Securities from Level 3 to Level 2 | 0                  | 0       | 0                | 0       |
| Purchases                                      | 0                  | 0       | 0                | 0       |
| Issuances                                      | 105                | 420     | 267              | 1,002   |
| Settlements                                    | (21 )              | (232 )  | (132 )           | (468 )  |
| Ending balance                                 | \$2,692            | \$3,407 | \$2,692          | \$3,407 |

## Assets Measured on a Non-Recurring Basis

Assets measured at fair value on a non-recurring basis as of June 30, 2010 and December 31, 2009 are summarized below:

| (in thousands)                 | Fair Value Measurements at<br>June 30, 2010 Using |  |  |  |
|--------------------------------|---|--|--|--|
|                                | Fair Value<br>June 30<br>2010                     | Quoted<br>Prices in<br>Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| Impaired loans                 | \$15,317  | \$0  | \$0  | \$ 15,317  |
| Other real estate/assets owned | 3,898   | 0  | 0  | 3,898  |

| (in thousands)                 | Fair Value Measurements at<br>December 31, 2009 Using |  |  |  |
|--------------------------------|---|--|--|--|
|                                | Fair Value<br>December<br>31<br>2009                  | Quoted<br>Prices in<br>Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
| Impaired loans                 | \$8,387   | \$0  | \$0  | \$ 8,387   |
| Other real estate/assets owned | 8,331   | 0  | 0  | 8,331  |

**Impaired Loans – Level 3 Inputs.** Loans considered impaired under ASC 310, formerly FAS 114, Accounting, Accounting by Creditors for Impairment of a Loan, as amended by SFAS No. 118, Accounting by Creditors for Impairment of a Loan — Income Recognition and Disclosure, are loans for which, based on current information and events, it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans are subject to nonrecurring fair value adjustments to reflect (1) partial write-downs that are based on the observable market price or current appraised value of the collateral less discounts for costs to sell and other estimated discounts or (2) the full charge-off of the loan carrying value. Quarter-to-date fair value adjustments on impaired loans were \$2.1 million at June 30, 2010 compared to \$1.1 million and \$2.4 million for quarters ended December 31, 2009 and June 30, 2009, respectively. Year-to-date fair value adjustments on impaired loans were \$5.6 million for both June 30, 2010 and December 31, 2009.

**Other real estate/assets owned – Level 3 Inputs.** In accordance with the provisions of FASB Codification Topic 360, formerly FAS 144, long-lived assets held for sale with a carrying amount of \$3.9 million were written down to their fair value less costs to sale during the year. Long-lived assets are subject to nonrecurring fair value adjustments to reflect partial write-downs that are based on the observable market price or current appraised value of the collateral. Quarter-to-date fair value adjustments on other real estate/assets owned were \$0.1 million, \$0.7 million, and \$0.2 million for quarters ended June 30, 2010, December 31, 2009, and June 30, 2009, respectively. Year-to-date fair value adjustments on other real estate/assets owned were \$0.4 million as of June 30, 2010 compared to \$1.4 million as of December 31, 2009.

The following table presents the carrying amounts and estimated fair values of financial instruments at June 30, 2010 and December 31, 2009:

| (in thousands)                            | June 30, 2010      |                      | December 31, 2009  |                      |
|---|--------------------|----------------------|--------------------|----------------------|
|   | Carrying Amount    | Estimated Fair Value | Carrying Amount    | Estimated Fair Value |
| <b>Financial assets</b>                   |                    |                      |                    |                      |
| Cash and cash equivalents                 | \$176,565          | \$176,565            | \$142,129          | \$142,129            |
| Certificates of deposits in other banks   | 15,508             | 15,489               | 100                | 100                  |
| Securities available-for-sale             | 352,616            | 352,616              | 270,237            | 270,237              |
| Securities held-to-maturity               | 1,662              | 1,662                | 14,336             | 14,435               |
| Loans, net (including impaired loans)     | 2,405,066          | 2,397,560            | 2,403,117          | 2,407,703            |
| Loans held for sale                       | 1,466              | 1,494                | 1,818              | 1,845                |
| Federal Reserve Bank stock                | 4,354              | 4,354                | 4,348              | 4,348                |
| Federal Home Loan Bank stock              | 24,700             | 24,700               | 24,700             | 24,700               |
| Accrued interest receivable               | 11,769             | 11,769               | 11,936             | 11,936               |
| Capitalized mortgage servicing rights     | 2,692              | 2,692                | 3,406              | 3,406                |
| <b>Total financial assets</b>             | <b>\$2,996,398</b> | <b>\$2,988,901</b>   | <b>\$2,876,127</b> | <b>\$2,880,839</b>   |
| <b>Financial liabilities</b>              |                    |                      |                    |                      |
| Deposits                                  | \$2,571,127        | \$2,572,347          | \$2,462,209        | \$2,462,676          |
| Repurchase agreements                     | 183,287            | 183,385              | 180,471            | 180,776              |
| Federal funds purchased                   | 8,465              | 8,465                | 12,205             | 12,205               |
| Advances from Federal Home Loan Bank      | 20,059             | 20,059               | 20,671             | 20,670               |
| Long-term debt                            | 61,341             | 30,832               | 61,341             | 29,522               |
| Accrued interest payable                  | 6,716              | 6,716                | 3,686              | 3,686                |
| <b>Total financial liabilities</b>        | <b>\$2,850,995</b> | <b>\$2,821,804</b>   | <b>\$2,740,583</b> | <b>\$2,709,535</b>   |
| <b>Unrecognized financial instruments</b> |                    |                      |                    |                      |
| Letters of credit                         | \$0                | \$0                  | \$0                | \$0                  |
| Commitments to extend credit              | 0                  | 0                    | 0                  | 0                    |
|   | \$0                | \$0                  | \$0                | \$0                  |

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and cash equivalents – The carrying amount approximates fair value.

Certificates of deposit in other banks – Fair values are based on quoted market prices or dealer quotes.

Securities – Fair values are based on quoted market prices, if available. If a quoted price is not available, fair value is estimated using quoted prices for similar securities.

Loans (net of the allowance for loan and lease losses and including impaired loans) – The fair value of fixed rate loans and variable rate mortgage loans is estimated by discounting the future cash flows using current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. For other variable rate loans, the carrying amount approximates fair value.

Loans held for sale – The fair value is predetermined at origination based on sale price.

Federal Reserve Bank stock – The carrying value of Federal Reserve Bank stock approximates fair value based on the redemption provisions of the Federal Reserve Bank.

Federal Home Loan Bank stock – The carrying value of Federal Home Loan Bank stock approximates fair value based on the redemption provisions of the Federal Home Loan Bank.

Accrued interest receivable – The carrying amount approximates fair value.

Deposits – The fair value of fixed maturity time deposits is estimated by discounting the future cash flows using the rates currently offered for deposits of similar remaining maturities. For deposits including demand deposits, savings accounts, NOW accounts, and certain money market accounts, the carrying value approximates fair value.

Repurchase agreements – The fair value is estimated by discounting future cash flows using current rates.

Federal funds purchased – The carrying amount approximates fair value.

Advances from Federal Home Loan Bank – The fair value of these fixed-maturity advances is estimated by discounting future cash flows using rates currently offered for advances of similar remaining maturities.

Long-term debt – The fair value is estimated by discounting future cash flows using current rates.

Accrued interest payable – The carrying amount approximates fair value.

Other financial instruments – The estimated fair value for other financial instruments and off-balance sheet loan commitments approximates cost at June 30, 2010 and December 31, 2009. Off-balance sheet loan commitments at June 30, 2010 and December 31, 2009 were \$421.6 million and \$425.1 million, respectively.

Letters of credit – The fair values of letters of credit and lines of credit are based on fees currently charged for similar agreements or on the estimated cost to terminate or otherwise settle the obligations with the counterparties at the reporting date. The fair value of such letters of credit is not material.

Commitments to extend credit – The fair value of commitments to extend credit is based upon the difference between the interest rate at which we are committed to make the loans and the current rates at which similar loans would be

made to borrowers with similar credit ratings and for the same remaining maturities, adjusted for the estimated volume of loan commitments actually expected to close. The fair value of such commitments is not material.

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

Overview

Community Trust Bancorp, Inc. ("CTBI") is a bank holding company headquartered in Pikeville, Kentucky. At June 30, 2010, CTBI owned one commercial bank and one trust company. Through its subsidiaries, CTBI has seventy-six banking locations in eastern, northeastern, central, and south central Kentucky and southern West Virginia, and five trust offices across Kentucky. At June 30, 2010, CTBI had total consolidated assets of \$3.2 billion and total consolidated deposits, including repurchase agreements, of \$2.8 billion, making it the largest depository of Kentucky based deposits of any bank holding company headquartered in the Commonwealth of Kentucky. Total shareholders' equity at June 30, 2010 was \$330.3 million.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires the appropriate application of certain accounting policies, many of which require us to make estimates and assumptions about future events and their impact on amounts reported in our consolidated financial statements and related notes. Since future events and their impact cannot be determined with certainty, the actual results will inevitably differ from our estimates. Such differences could be material to the consolidated financial statements.

We believe the application of our accounting policies and the estimates required therein are reasonable. These accounting policies and estimates are constantly reevaluated, and adjustments are made when facts and circumstances dictate a change. Historically, we have found our application of accounting policies to be appropriate, and actual results have not differed materially from those determined using necessary estimates.

See note 1 to the condensed consolidated financial statements for further information regarding our accounting policies. We have identified the following critical accounting policies:

**Cash and Cash Equivalents** – Cash and cash equivalents include cash on hand, amounts due from banks, interest bearing deposits in other financial institutions, and federal funds sold. Generally, federal funds are sold for one-day periods.

At December 31, 2009, all of the financial institutions holding CTBI's or its subsidiary's cash accounts were participating in the FDIC's Transaction Account Guarantee Program. Under the program, through December 31, 2010, all noninterest-bearing transaction accounts at these institutions are fully guaranteed by the FDIC for the entire amount in the account. Effective January 1, 2010 one correspondent bank opted out of the program leaving CTBI with exposure of \$1.2 million at June 30, 2010. The Dodd-Frank financial reform bill extended the unlimited FDIC insurance on noninterest-bearing transaction accounts through December 31, 2012. Beginning January 1, 2011, this will apply to all insured institutions, including those who opted out of the current rules.

**Investments** – Management determines the classification of securities at purchase. We classify securities into held-to-maturity, trading, or available-for-sale categories. Held-to-maturity securities are those which we have the positive intent and ability to hold to maturity and are reported at amortized cost. In accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 320, formerly Financial Accounting Standard (FAS) 115, Accounting for Certain Investments in Debt and Equity Securities, investments in debt securities that are not classified as held-to-maturity and equity securities that have readily determinable fair values shall be classified in one of the following categories and measured at fair value in the statement of financial position:

a. Trading securities. Securities that are bought and held principally for the purpose of selling them in the near term (thus held for only a short period of time) shall be classified as trading securities. Trading generally reflects active and frequent buying and selling, and trading securities are generally used with the objective of generating profits on short-term differences in price.

b. Available-for-sale securities. Investments not classified as trading securities (nor as held-to-maturity securities) shall be classified as available-for-sale securities.

We do not have any securities that are classified as trading securities. Available-for-sale securities are reported at fair value, with unrealized gains and losses included as a separate component of shareholders' equity, net of tax. If declines in fair value are other than temporary, the carrying value of the securities is written down to fair value as a realized loss.

Gains or losses on disposition of securities are computed by specific identification for all securities except for shares in mutual funds, which are computed by average cost. Interest and dividend income, adjusted by amortization of purchase premium or discount, is included in earnings.

When the fair value of a security is below its amortized cost, and depending on the length of time the condition exists and the extent the fair market value is below amortized cost, additional analysis is performed to determine whether an other than temporary impairment condition exists. Available-for-sale and held-to-maturity securities are analyzed quarterly for possible other than temporary impairment. The analysis considers (i) whether we have the intent to sell our securities prior to recovery and/or maturity and (ii) whether it is more likely than not that we will not have to sell our securities prior to recovery and/or maturity. Often, the information available to conduct these assessments is limited and rapidly changing, making estimates of fair value subject to judgment. If actual information or conditions are different than estimated, the extent of the impairment of the security may be different than previously estimated, which could have a material effect on the CTBI's results of operations and financial condition.

Available-for-Sale Securities – Available-for-sale securities are valued using the following valuation techniques:

U.S. Treasury and government agencies, state and political subdivision, U.S. government sponsored agencies, Marketable equity securities – Level 2 Inputs. For these securities, CTBI obtains fair value measurements from an independent pricing service, which utilizes pricing models to determine fair value measurements. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the bond's terms and conditions, among other things.

Marketable equity securities – Level 3 Inputs. The securities owned by CTBI that were measured using Level 3 criteria are auction rate securities issued by FNMA. These securities were valued using an independent third party. For these securities, the valuation methods used were (1) a discounted cash flow model valuation, where the expected cash flows of the securities are discounted to the present using a yield that incorporates compensation for illiquidity and (2) a market comparables method, where the securities are valued based on indications, from the secondary market, of what discounts buyers demand when purchasing similar securities. Using these methods, the auction rate securities are classified as Level 3.

Loans – Loans with the ability and the intent to be held until maturity and/or payoff are reported at the carrying value of unpaid principal reduced by unearned interest and an allowance for loan and lease losses and unamortized deferred

fees or costs. Income is recorded on the level yield basis. Interest accrual is discontinued when management believes, after considering economic and business conditions, collateral value, and collection efforts, that the borrower's financial condition is such that collection of interest is doubtful. Any loan greater than 90 days past due must be well secured and in the process of collection to continue accruing interest. Cash payments received on nonaccrual loans generally are applied against principal, and interest income is only recorded once principal recovery is reasonably assured. Loans are not reclassified as accruing until principal and interest payments are brought current and future payments appear reasonably certain.

Loan origination and commitment fees and certain direct loan origination costs are deferred and the net amount amortized over the estimated life of the related loans, leases, or commitments as a yield adjustment.

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Allowance for Loan and Lease Losses – We maintain an allowance for loan and lease losses (“ALLL”) at a level that is appropriate to cover estimated credit losses on individually evaluated loans determined to be impaired, as well as estimated credit losses inherent in the remainder of the loan and lease portfolio. Since arriving at an appropriate ALLL involves a high degree of management judgment, we use an ongoing quarterly analysis to develop a range of estimated losses. In accordance with accounting principles generally accepted in the United States, we use our best estimate within the range of potential credit loss to determine the appropriate ALLL. Credit losses are charged and recoveries are credited to the ALLL.

We utilize an internal risk grading system for commercial credits. Those larger commercial credits that exhibit probable or observed credit weaknesses are subject to individual review. The borrower’s cash flow, adequacy of collateral coverage, and other options available to CTBI, including legal remedies, are evaluated. The review of individual loans includes those loans that are impaired as defined by ASC 310, formerly FAS 114, Accounting by Creditors for Impairment of a Loan. We evaluate the collectibility of both principal and interest when assessing the need for loss provision. Historical loss rates are analyzed and applied to other commercial loans not subject to specific allocations. The ALLL allocation for this pool of commercial loans is established based on the historical average, maximum, minimum, and median loss ratios.

A loan is considered impaired when, based on current information and events, it is probable that CTBI will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower’s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan’s effective interest rate, the loan’s obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Homogenous loans, such as consumer installment, residential mortgages, and home equity lines are not individually risk graded. The associated ALLL for these loans is measured under ASC 450, formerly FAS 5, Accounting for Contingencies.

Historical loss rates for commercial and retail loans are adjusted for significant factors that, in management’s judgment, reflect the impact of any current conditions on loss recognition. Factors that we consider include delinquency trends, current economic conditions and trends, strength of supervision and administration of the loan portfolio, levels of underperforming loans, level of recoveries to prior year’s charge offs, trend in loan losses, industry concentrations and their relative strengths, amount of unsecured loans and underwriting exceptions. These factors are reviewed quarterly and a weighted range developed with a “most likely” scenario determined. The total of each of these weighted factors is then applied against the applicable portion of the portfolio and the ALLL is adjusted accordingly.

Loans Held for Sale – Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate. Net unrealized losses, if any, are recognized in a valuation allowance by charges to income.

Premises and Equipment – Premises and equipment are stated at cost less accumulated depreciation and amortization. Capital leases are included in premises and equipment at the capitalized amount less accumulated amortization. Premises and equipment are evaluated for impairment on a quarterly basis.

Depreciation and amortization are computed primarily using the straight-line method. Estimated useful lives range up to 40 years for buildings, 2 to 10 years for furniture, fixtures, and equipment, and up to the lease term for leasehold improvements. Capitalized leased assets are amortized on a straight-line basis over the lives of the respective leases.

Other Real Estate – Real estate acquired by foreclosure is carried at the lower of the investment in the property or its fair value less estimated cost to sell. Periodically, but not less frequently than bi-annually, an updated appraisal is obtained for each property owned and any decline in the fair value is recognized by a charge to income. All revenues and expenses related to the carrying of other real estate owned are recognized by a charge to income.

Goodwill and Core Deposit Intangible – We evaluate total goodwill and core deposit intangible for impairment, based upon ASC 350, formerly FAS 142, Goodwill and Other Intangible Assets and FAS 147, Acquisitions of Certain Financial Institutions, using fair value techniques including multiples of price/equity. Goodwill and core deposit intangible are evaluated for impairment on an annual basis or as other events may warrant.

Amortization of core deposit intangible is estimated at approximately \$0.4 million for year one, approximately \$0.05 million annually in years two through five, and approximately \$0.03 million in year six.

Transfers of Financial Assets -- Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from CTBI—put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) CTBI does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

Income Taxes – Income tax expense is based on the taxes due on the consolidated tax return plus deferred taxes based on the expected future tax benefits and consequences of temporary differences between carrying amounts and tax bases of assets and liabilities, using enacted tax rates.

Earnings Per Share (“EPS”) – Basic EPS is calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding, excluding restricted shares.

Diluted EPS adjusts the number of weighted average shares of common stock outstanding by the dilutive effect of stock options, including restricted shares, as prescribed in ASC 718, formerly FAS 123R.

Segments – Management analyzes the operation of CTBI assuming one operating segment, community banking services. CTBI, through its operating subsidiaries, offers a wide range of consumer and commercial community banking services. These services include: (i) residential and commercial real estate loans; (ii) checking accounts; (iii) regular and term savings accounts and savings certificates; (iv) full service securities brokerage services; (v) consumer loans; (vi) debit cards; (vii) annuity and life insurance products; (viii) Individual Retirement Accounts and Keogh plans; (ix) commercial loans; (x) trust services; and (xi) commercial demand deposit accounts.

Bank Owned Life Insurance – CTBI’s bank owned life insurance policies are carried at their cash surrender value. We recognize tax-free income from the periodic increases in cash surrender value of these policies and from death benefits.

Mortgage Servicing Rights – Mortgage servicing rights (“MSRs”) are carried at fair market value with the implementation of ASC 860, formerly FAS 156, in January 2007. MSRs are valued using Level 3 inputs as defined in ASC 820, formerly FAS 157. The fair value is determined quarterly based on an independent third-party valuation using a discounted cash flow analysis and calculated using a computer pricing model. The computer valuation is based on key economic assumptions including the prepayment speeds of the underlying loans, the weighted-average

life of the loan, the discount rate, the weighted-average coupon, and the weighted-average default rate, as applicable. Along with the gains received from the sale of loans, fees are received for servicing loans. These fees include late fees, which are recorded in interest income, and ancillary fees and monthly servicing fees, which are recorded in noninterest income. Costs of servicing loans are charged to expense as incurred. Changes in fair market value of the MSRs are reported in mortgage banking income.

Stock Options – At June 30, 2010 and December 31, 2009, CTBI had a share-based employee compensation plan, which is described more fully in note 14 to the consolidated financial statements for the year ended December 31, 2009, included in CTBI's Annual Report on Form 10-K. CTBI accounts for this plan under the recognition and measurement principles of ASC 718, formerly FAS 123R, Share-Based Payment.

Comprehensive Income – Comprehensive income consists of net income and other comprehensive income, net of applicable income taxes. Other comprehensive income includes unrealized appreciation (depreciation) on available-for-sale securities and unrealized appreciation (depreciation) on available-for-sale securities for which a portion of an other than temporary impairment has been recognized in income.

Reclassifications – Certain reclassifications considered to be immaterial have been made in the prior year condensed consolidated financial statements to conform to current year classifications. These reclassifications had no effect on net income.

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## Dividends

The following schedule shows the quarterly cash dividends paid for the past six quarters:

| Pay Date        | Record Date        | Amount Per Share |
|-----------------|--------------------|------------------|
| July 1, 2010    | June 15, 2010      | \$0.30           |
| April 1, 2010   | March 15, 2010     | \$0.30           |
| January 1, 2010 | December 15, 2009  | \$0.30           |
| October 1, 2009 | September 15, 2009 | \$0.30           |
| July 1, 2009    | June 15, 2009      | \$0.30           |
| April 1, 2009   | March 15, 2009     | \$0.30           |

On July 27, 2010, CTBI announced an increase in the quarterly cash dividend to \$0.305 per share to be paid on October 1, 2010, to shareholders of record on September 15, 2010.

## Statement of Income Review

CTBI reported earnings for the second quarter 2010 of \$8.6 million or \$0.56 per basic share compared to \$6.8 million or \$0.45 per basic share earned during the quarter ended March 31, 2010 and \$5.9 million or \$0.39 per basic share earned during the second quarter of 2009. Earnings for the six months ended June 30, 2010 were \$15.3 million or \$1.01 per basic share compared to \$12.5 million or \$0.83 per basic share for the six months ended June 30, 2009.

## Earnings Summary

| (in thousands except per share data) | 2Q<br>2010 | 1Q<br>2010 | 2Q<br>2009 | 6 Months<br>2010 | 6 Months<br>2009 |
|--------------------------------------|------------|------------|------------|------------------|------------------|
| Net income                           | \$8,553    | \$6,791    | \$5,937    | \$15,344         | \$12,517         |
| Earnings per share                   | \$0.56     | \$0.45     | \$0.39     | \$1.01           | \$0.83           |
| Earnings per share--diluted          | \$0.56     | \$0.45     | \$0.39     | \$1.01           | \$0.82           |
| Return on average assets             | 1.06       | 0.88       | 0.78       | 0.98             | 0.83             |
| Return on average equity             | 10.40      | 8.47       | 7.54       | 9.44             | 8.02             |
| Efficiency ratio                     | 60.41      | 59.45      | 64.25      | 59.93            | 66.08            |
| Tangible common equity               | 8.43       | 8.36       | 8.38       | 8.43             | 8.38             |
| Dividends declared per share         | \$0.30     | \$0.30     | \$0.30     | \$0.60           | \$0.60           |
| Book value per share                 | \$21.69    | \$21.35    | \$20.80    | \$21.69          | \$20.80          |
| Weighted average shares              | 15,228     | 15,202     | 15,127     | 15,215           | 15,101           |
| Weighted average shares--diluted     | 15,305     | 15,235     | 15,219     | 15,252           | 15,194           |

## Second Quarter 2010 Highlights

- v As announced on June 8, 2010, CTBI has entered into an acquisition agreement and plan of share exchange with LaFollette First National Corporation and First National Bank of LaFollette, the wholly-owned subsidiary of LaFollette Corporation.
- v CTBI's quarterly basic earnings per share increased \$0.11 per share from first quarter 2010 and \$0.17 per share from second quarter 2009. Year-to-date basic earnings per share increased \$0.18 per share from prior year. Year-to-date earnings were positively impacted by increased net interest income; however, this was partially offset by an increased provision for loan losses.

- v CTBI experienced significant improvement in our net interest margin year over year; however, our net interest margin for the quarter decreased 20 basis points from first quarter 2010.
- v Nonperforming loans increased \$7.4 million during the second quarter 2010 to \$62.3 million compared to \$54.9 million at prior quarter end and \$59.6 million at June 30, 2009. The linked quarter increase in nonperforming loans was in the nonaccrual classification. Nonperforming assets increased \$8.7 million from prior quarter-end and \$22.5 million from prior year second quarter.
- v The loan loss provision for the six months ended June 30, 2010 increased \$2.3 million from prior year to support the increase in nonperforming loans year over year per CTBI's robust loan portfolio management process and loan loss reserve analysis. This increase resulted in an increase in the loan loss reserve ratio to 1.48% from 1.32% at June 30, 2009.
- v Net loan charge-offs for the quarter ended June 30, 2010 of \$1.8 million, or 0.30% of average loans annualized, was a reduction from prior quarter's 0.58% and from the 0.63% experienced for the second quarter 2009.
- v Noninterest income decreased for the period ended June 30, 2010 compared to same period 2009 as a result of decreased gains on sales of loans and loan related fees. The decrease in loan related fees resulted from a \$0.7 million decline in the fair value of our mortgage servicing rights portfolio. The decline in these noninterest income sources, however, was partially offset by increases in trust revenue and deposit service charges.
- v Our loan portfolio increased \$12.3 million, an annualized rate of 2.0%, during the quarter with increases in the commercial and residential loan portfolios offset partially by a decline in the consumer loan portfolio.
- v Our investment portfolio increased \$32.9 million during the quarter as deposit growth continued to be stronger than loan demand.
- v Our tangible common equity/tangible assets ratio remains strong at 8.43%.

CTBI had basic weighted average shares outstanding of 15.2 million for both the three and six months ended June 30, 2010 compared to 15.1 million for both the three and six months ended June 30, 2009. The following table sets forth on an annualized basis the return on average assets and return on average shareholders' equity for the three months and six months ended June 30, 2010 and 2009:

|  | Three Months Ended |        | Six Months Ended |        |
|--|--------------------|--------|------------------|--------|
|  | June 30            |        | June 30          |        |
|  | 2010               | 2009   | 2010             | 2009   |
| Return on average shareholders' equity | 10.40              | % 7.54 | % 9.44           | % 8.02 |
| Return on average assets               | 1.06               | % 0.78 | % 0.98           | % 0.83 |



## Net Interest Income

CTBI saw improvement in its net interest margin of 49 basis points for the first six months of 2010 and 38 basis points for the second quarter 2010 compared to 2009; however, we saw a 20 basis point decline from prior quarter due to the increase in deposits during a time of weak loan demand and limited alternative investment opportunities. Net interest income for the quarter decreased 0.2% from prior quarter but increased 15.2% from prior year second quarter with average earning assets increasing 3.6% and 4.2%, respectively, for the same periods. The yield on average earning assets decreased 26 basis points from prior quarter and 14 basis points from prior year second quarter as higher yielding investment opportunities are limited. The cost of interest bearing funds decreased 7 basis points and 68 basis points, respectively, for the same periods. Net interest income for the six months ended June 30, 2010 increased 17.5% from prior year.

The following table summarizes the annualized net interest spread and net interest margin for the three and six months ended June 30, 2010 and 2009.

|                                  | Three Months Ended |        |         |        | Six Months Ended |      |         |      |
|----------------------------------|--------------------|--------|---------|--------|------------------|------|---------|------|
|                                  | June 30            |        | June 30 |        | June 30          |      | June 30 |      |
|                                  | 2010               | 2009   | 2010    | 2009   | 2010             | 2009 | 2010    | 2009 |
| Yield on interest earning assets | 5.24               | % 5.38 | % 5.36  | % 5.45 | %                | %    | %       | %    |
| Cost of interest bearing funds   | 1.56               | 2.25   | 1.60    | 2.34   |                  |      |         |      |
| Net interest spread              | 3.68               | % 3.13 | % 3.76  | % 3.11 | %                | %    | %       | %    |
| Net interest margin              | 4.00               | % 3.62 | % 4.10  | % 3.61 | %                | %    | %       | %    |

## Provision for Loan Losses

The analysis of the changes in the allowance for loan losses and selected ratios is set forth below:

| (in thousands)   | Six Months Ended |             |         |      |
|--|------------------|-------------|---------|------|
|  | June 30          |             | June 30 |      |
|  | 2010             | 2009        | 2010    | 2009 |
| Allowance balance at January 1                                   | \$32,643         | \$30,821    |         |      |
| Additions to allowance charged against operations                | 8,828            | 6,503       |         |      |
| Recoveries credited to allowance                                 | 1,618            | 1,668       |         |      |
| Losses charged against allowance                                 | (6,933)          | (7,570)     |         |      |
| Allowance balance at June 30                                     | \$36,156         | \$31,422    |         |      |
| Allowance for loan losses to period-end loans                    | 1.48             | % 1.32      | %       | %    |
| Average loans, net of unearned income                            | \$2,438,738      | \$2,352,664 |         |      |
| Provision for loan losses to average loans, annualized           | 0.73             | % 0.56      | %       | %    |
| Loan charge-offs net of recoveries, to average loans, annualized | 0.44             | % 0.51      | %       | %    |

Net loan charge-offs for the quarter were \$1.8 million, or 0.30% of average loans annualized, a decline from prior quarter's \$3.5 million or 0.58% and prior year second quarter's \$3.7 million or 0.63%. Of the total net charge-offs for the quarter of \$1.8 million, \$0.6 million was in commercial loans, \$0.5 million was in indirect auto loans, and \$0.4 million was in residential real estate mortgage loans. Specific reserves covered 77.0% of the commercial loan charge-offs. Allocations to loan loss reserves were \$3.1 million for the quarter ended June 30, 2010 compared to \$5.7 million for the quarter ended March 31, 2010 and \$4.5 million for the quarter ended June 30, 2009. Our loan loss reserves as a percentage of total loans outstanding at June 30, 2010 increased to 1.48% from 1.44% at March 31, 2010 and 1.32% at June 30, 2009. The adequacy of our loan loss reserves is analyzed quarterly and adjusted as necessary

with a focus on maintaining appropriate reserves for potential losses. The analysis includes an individual loan review including current valuation of the collateral. Specific reserves are allocated to address any identified shortfalls in collateral while additional reserves address many other considerations, including but not limited to historical losses, loss trends, and current economic conditions, for an adequate reserve coverage.

#### Noninterest Income

Noninterest income for the quarter ended June 30, 2010 decreased 2.0% and 12.9% from prior quarter and prior year second quarter, respectively. Year-to-date noninterest income declined 11.2% from prior year. The decrease in noninterest income was significantly impacted by decreased gains on sales of loans as 2009 was a period of significant refinancing of residential real estate loans, as well as a \$0.7 million decline in the fair value of our mortgage servicing rights. The decline in these noninterest income sources was partially offset by increases in trust and brokerage revenue and deposit service charges.

#### Noninterest Expense

Noninterest expense for the quarter increased 0.9% from prior quarter and 0.3% from prior year second quarter. Noninterest expense for the first six months 2010, however, decreased 0.6% from 2009 as increased personnel expenses were offset by a decrease in FDIC insurance premiums and special assessment.

#### Balance Sheet Review

CTBI continues to experience internal growth of its banking franchise. Total assets at \$3.2 billion increased an annualized 5.1% during the quarter and an annualized 8.0% from December 31, 2009. Loans outstanding at June 30, 2010 were \$2.4 billion with an annualized 2.0% growth from March 31, 2010 and an annualized 0.5% growth from December 31, 2009. CTBI's investment portfolio increased \$32.9 million over prior quarter and \$69.7 million from prior year-end as CTBI continues to experience good growth in its deposit base while loan demand remains weak. Deposits, including repurchase agreements, at \$2.8 billion increased an annualized 5.5% from prior quarter and an annualized 8.5% from December 31, 2009.

Shareholders' equity at June 30, 2010 was \$330.3 million compared to \$324.9 million at March 31, 2010 and \$321.5 million at December 31, 2009. CTBI's annualized dividend yield to shareholders as of June 30, 2010 was 4.78%.

#### Loans

Loan growth during the quarter of \$16.9 million in the commercial loan portfolio and \$6.9 million in the residential loan portfolio was partially offset by a decline in the consumer loan portfolio of \$11.5 million. The commercial and residential loan portfolios increased \$26.1 million and \$2.5 million, respectively, from December 31, 2009, while the consumer loan portfolio decreased \$23.2 million.

The following tables summarize CTBI's nonperforming loans as of June 30, 2010 and December 31, 2009.

| (in thousands)                    | Nonaccrual<br>Loans | As a % of<br>Loan<br>Balances<br>by<br>Category | Accruing<br>Loans Past<br>Due 90<br>Days or<br>More | As a % of<br>Loan<br>Balances<br>by<br>Category | Total Loan<br>Balances |
|-----------------------------------|---------------------|---|---|---|------------------------|
| June 30, 2010                     |                     |   |   |   |                        |
| Commercial construction           | \$ 16,963           | 11.87   | % \$401   | 0.28  | % \$142,847            |
| Commercial secured by real estate | 14,302              | 1.88  | 11,696  | 1.54  | 761,646                |
| Commercial other                  | 8,398               | 2.42  | 1,514   | 0.44  | 347,284                |

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|                                   |          |      |            |      |               |
|-----------------------------------|----------|------|------------|------|---------------|
| Consumer real estate construction | 662      | 1.38 | 20         | 0.04 | 47,957        |
| Consumer real estate secured      | 5,110    | 0.83 | 2,817      | 0.46 | 616,618       |
| Consumer other                    | 0        | 0.00 | 409        | 0.08 | 507,724       |
| Equipment lease financing         | 0        | 0.00 | 0          | 0.00 | 17,146        |
| Total                             | \$45,435 | 1.86 | % \$16,857 | 0.69 | % \$2,441,222 |

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| (in thousands)                    | Nonaccrual<br>Loans | As a % of<br>Loan<br>Balances<br>by<br>Category | Accruing<br>Loans Past<br>Due 90<br>Days or<br>More | As a % of<br>Loan<br>Balances<br>by<br>Category | Total Loan<br>Balances |
|-----------------------------------|---------------------|---|---|---|------------------------|
| December 31, 2009                 |                     |   |   |   |                        |
| Commercial construction           | \$12,312            | 8.70  | % \$865   | 0.61  | % \$141,440            |
| Commercial secured by real estate | 9,803               | 1.39  | 5,640   | 0.80  | 707,500                |
| Commercial other                  | 4,489               | 1.20  | 286   | 0.08  | 373,829                |
| Consumer real estate construction | 1,244               | 2.42  | 0   | 0.00  | 51,311                 |
| Consumer real estate secured      | 4,399               | 0.72  | 1,698   | 0.28  | 610,727                |
| Consumer other                    | 0                   | 0.00  | 578   | 0.11  | 530,905                |
| Equipment lease financing         | 0                   | 0.00  | 0   | 0.00  | 20,048                 |
| Total                             | \$32,247            | 1.32  | % \$9,067   | 0.37  | % \$2,435,760          |

CTBI's total nonperforming loans were \$62.3 million at June 30, 2010, an increase from the \$54.9 million at March 31, 2010 and \$41.3 million at December 31, 2009. The \$7.4 million increase in nonperforming loans during the quarter is primarily attributable to three commercial loan relationships, a \$4.1 million motel loan, and \$2.9 million in two residential real estate development loans in Central Kentucky. Loans 30-89 days past due decreased \$12.5 million during the quarter including the \$7.4 million movement of loans into nonperforming status. Loans past-due 30-89 days at June 30, 2010 were \$23.7 million, a decrease from the \$36.2 million at March 31, 2010 and the \$24.8 million at December 31, 2009. Our loan portfolio management processes focus on the immediate identification, management, and resolution of problem loans to maximize recovery and minimize loss.

Impaired loans increased \$28.2 million during the six months ended June 30, 2010. Of this increase, \$13.4 million or 47.4% was in loans that are impaired for which no specific reserve is required. Management makes this determination of impairment based on the present value of the expected future cash flows, discounted at the loan's effective interest rate. In cases where the loan is collateral-dependent, updated appraisals are obtained and selling costs are considered to arrive at an estimated current fair value. When a loan is determined to have adequate cash flow or in the case of collateral dependent loans, when the collateral is of sufficient value to pay the entire amount of principal and interest due on a loan, no specific reserve is provided.

Our level of foreclosed properties increased to \$40.1 million for the second quarter 2010 compared to the \$38.6 million at March 31, 2010 and \$37.3 million at December 31, 2009. Sales of foreclosed properties for the six months ended June 30, 2010 totaled \$3.5 million while new foreclosed properties totaled \$6.5 million. Our nonperforming loans and foreclosed properties remain primarily concentrated in our Central Kentucky Region.

#### Allowance for Loan Losses

The allowance for loan and lease losses balance is maintained by management at a level considered adequate to cover anticipated probable losses based on past loss experience, general economic conditions, information about specific borrower situations including their financial position and collateral values, and other factors and estimates which are subject to change over time. This analysis is completed quarterly and forms the basis for allocation of the loan loss reserve and what charges to the provision may be required. For further discussion of the allowance for loan losses, see the Critical Accounting Policies and Estimates section presented earlier in Item 2.

#### Securities

CTBI uses its securities held-to-maturity for production of income and to manage cash flow needs through expected maturities. CTBI uses its securities available-for-sale for income and balance sheet liquidity management. Securities

available-for-sale reported at fair value increased from \$270.2 million as of December 31, 2009 to \$352.6 million at June 30, 2010. The excess of market over cost increased from \$6.5 million at December 31, 2009 to \$8.5 million at June 30, 2010. Securities held-to-maturity decreased from \$14.3 million to \$1.7 million during the same period. Total securities as a percentage of total assets were 9.2% as of December 31, 2009 and 11.0% as of June 30, 2010.

### Liquidity and Capital Resources

CTBI's liquidity objectives are to ensure that funds are available for the subsidiary bank to meet deposit withdrawals and credit demands without unduly penalizing profitability. Additionally, CTBI's objectives ensure that funding is available for CTBI to meet ongoing cash needs while maximizing profitability. CTBI continues to identify ways to provide for liquidity on both a current and long-term basis. The subsidiary bank relies mainly on core deposits, certificates of deposits of \$100,000 or more, repayment of principal and interest on loans and securities and federal funds sold and purchased to create long-term liquidity. The subsidiary bank also has available the sale of securities under repurchase agreements, securities available-for-sale, and Federal Home Loan Bank ("FHLB") borrowings as secondary sources of liquidity.

Due to the nature of the markets served by the subsidiary bank, management believes that the majority of its certificates of deposit of \$100,000 or more and its repurchase agreements are no more volatile than its core deposits. During periods of interest rate volatility, these deposit balances have remained stable as a percentage of total deposits. In addition, arrangements have been made with correspondent banks for the purchase of federal funds on an unsecured basis, up to \$20 million, if necessary, to meet CTBI's liquidity needs.

CTBI owns securities with an estimated fair value of \$352.6 million that are designated as available-for-sale and available to meet liquidity needs on a continuing basis. In addition, CTBI has \$15.5 million in other investments consisting of certificates of deposits in other banks. All investments in other banks are made at or below the FDIC insured maximum of \$250 thousand. CTBI also has available Federal Home Loan Bank advances for both liquidity and management of its asset/liability position. FHLB advances decreased slightly from \$20.7 million at December 31, 2009 to \$20.1 million at June 30, 2010. FHLB borrowing capacity at June 30, 2010 was \$193.7 million. Long-term debt remained at \$61.3 million from December 31, 2009 to June 30, 2010. The parent company has a \$12 million line of credit, all of which is currently available for general corporate purposes. At June 30, 2010, federal funds sold were \$67.0 million compared to \$47.6 million at December 31, 2009. Additionally, management projects cash flows from CTBI's investment portfolio to generate additional liquidity over the next 90 days.

CTBI generally relies upon net inflows of cash from financing activities, supplemented by net inflows of cash from operating activities, to provide cash for its investing activities. As is typical of many financial institutions, significant financing activities include deposit gathering, use of short-term borrowing facilities such as federal funds purchased and securities sold under repurchase agreements, and issuance of long-term debt. CTBI's primary investing activities include purchases of securities and loan originations.

The investment portfolio consists of investment grade short-term issues suitable for bank investments. The majority of the investment portfolio is in U.S. government and government sponsored agency issuances. The average life of the portfolio is 3.42 years. At the end of the second quarter 2010, available-for-sale ("AFS") securities comprised approximately 99.5% of the total investment portfolio. The AFS portfolio was approximately 106.7% of equity capital, and 83% of the pledge eligible portfolio was pledged.

CTBI's stock repurchase program began in December 1998 with the authorization to acquire up to 500,000 shares and was increased by an additional 1,000,000 shares in July 2000 and in May 2005. CTBI did not repurchase any shares of its common stock during the first six months of 2010. There are currently 288,519 shares remaining under CTBI's current repurchase authorization. As of June 30, 2010, a total of 2,211,481 shares have been repurchased through this program.



In conjunction with maintaining a satisfactory level of liquidity, management monitors the degree of interest rate risk assumed on the consolidated balance sheet. CTBI monitors its interest rate risk by use of the static gap model and dynamic gap model at the one-year interval. CTBI uses the Sendero system to monitor its interest rate risk. The static gap model monitors the difference in interest rate sensitive assets and interest rate sensitive liabilities as a percentage of total assets that mature within the specified time frame. The dynamic gap model goes further in that it assumes that interest rate sensitive assets and liabilities will be reinvested. CTBI desires an interest sensitivity gap of not more than fifteen percent of total assets at the one-year interval.

CTBI's principal source of funds used to pay dividends to shareholders and service long-term debt is the dividends it receives from the subsidiary bank. Various federal statutory provisions, in addition to regulatory policies and directives, limit the amount of dividends that subsidiary banks can pay without prior regulatory approval. These restrictions have had no major impact on CTBI's dividend policy or its ability to service long-term debt, nor is it anticipated that they would have any major impact in the foreseeable future. During the remainder of 2010, approximately \$20.1 million plus any remaining 2010 net profits can be paid by CTBI's banking subsidiary without prior regulatory approval.

The primary source of capital for CTBI is the retention of earnings. CTBI paid cash dividends of \$0.60 per share during the first six months of 2010. Basic earnings per share for the same period were \$1.01. CTBI retained 41% of earnings for the first six months of 2010. CTBI announced an increase in the quarterly cash dividend to \$0.305 per share beginning with the October 1, 2010 payment.

Under guidelines issued by banking regulators, CTBI and its subsidiary bank are required to maintain a minimum Tier 1 risk-based capital ratio of 4% and a minimum total risk-based ratio of 8%. In order to be considered "well-capitalized" CTBI must maintain ratios of 6% and 10%, respectively. Risk-based capital ratios weight the relative risk factors of all assets and consider the risk associated with off-balance sheet items. CTBI must also maintain a minimum Tier 1 leverage ratio of 4%. The well-capitalized ratio for Tier 1 leverage is 5%. CTBI's Tier 1 leverage, Tier 1 risk-based, and total risk-based ratios were 10.12%, 13.20%, and 14.46%, respectively, as of June 30, 2010, all exceeding the threshold for meeting the definition of well-capitalized.

As of June 30, 2010, management is not aware of any conditions or current recommendations by banking regulatory authorities which, if they were to be implemented, would have, or would be reasonably likely to have, a material adverse impact on CTBI's liquidity, capital resources, or operations.

#### Impact of Inflation and Changing Prices

The majority of CTBI's assets and liabilities are monetary in nature. Therefore, CTBI differs greatly from most commercial and industrial companies that have significant investment in nonmonetary assets, such as fixed assets and inventories. However, inflation does have an important impact on the growth of assets in the banking industry and on the resulting need to increase equity capital at higher than normal rates in order to maintain an appropriate equity to assets ratio. Inflation also affects other expenses, which tend to rise during periods of general inflation.

Management believes one of the most significant impacts on financial and operating results is CTBI's ability to react to changes in interest rates. Management seeks to maintain an essentially balanced position between interest rate sensitive assets and liabilities in order to protect against the effects of wide interest rate fluctuations.

#### Pending Acquisition

On June 8, 2010, CTBI announced that it had entered into an Agreement and Plan of Share Exchange (the "Agreement") with LaFollette First National Corporation, a Tennessee corporation ("LaFollette Corporation") and First National Bank of LaFollette, the wholly-owned subsidiary of LaFollette Corporation ("LaFollette Bank"). The Agreement calls for

CTBI to acquire all outstanding shares of LaFollette Corporation in a share exchange (“Share Exchange”) for \$650 per share, or a total of approximately \$16.1 million. Following the Share Exchange, LaFollette Corporation will be merged into CTBI and LaFollette Bank will be merged into Community Trust Bank, Inc., the wholly-owned subsidiary of CTBI. The Agreement is subject to certain conditions, including the receipt of regulatory approval and the approval of LaFollette Corporation shareholders.

#### FORWARD-LOOKING STATEMENTS

Certain of the statements contained herein that are not historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act. CTBI’s actual results may differ materially from those included in the forward-looking statements. Forward-looking statements are typically identified by words or phrases such as “believe,” “expect,” “anticipate,” “intend,” “estimate,” “may increase,” “may fluctuate,” and similar expressions or conditional verbs such as “will,” “should,” “would,” and “could.” These forward-looking statements involve risks and uncertainties including, but not limited to, economic conditions, portfolio growth, the credit performance of the portfolios, including bankruptcies, and seasonal factors; changes in general economic conditions including the performance of financial markets, prevailing inflation and interest rates, realized gains from sales of investments, gains from asset sales, and losses on commercial lending activities; results of various investment activities; the effects of competitors’ pricing policies, changes in laws and regulations, competition, and demographic changes on target market populations’ savings and financial planning needs; industry changes in information technology systems on which we are highly dependent; failure of acquisitions to produce revenue enhancements or cost savings at levels or within the time frames originally anticipated or unforeseen integration difficulties; the adoption by CTBI of a Federal Financial Institutions Examination Council (FFIEC) policy that provides guidance on the reporting of delinquent consumer loans and the timing of associated credit charge-offs for financial institution subsidiaries; and the resolution of legal proceedings and related matters. In addition, the banking industry in general is subject to various monetary and fiscal policies and regulations, which include those determined by the Federal Reserve Board, the Federal Deposit Insurance Corporation, and state regulators, whose policies and regulations could affect CTBI’s results. These statements are representative only on the date hereof, and CTBI undertakes no obligation to update any forward-looking statements made.

#### Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest rate risk management focuses on maintaining consistent growth in net interest income within Board-approved policy limits. CTBI uses an earnings simulation model to analyze net interest income sensitivity to movements in interest rates. Given a 200 basis point increase to the yield curve used in the simulation model, it is estimated net interest income for CTBI would decrease by 0.23 percent over one year and by 0.48 percent over two years. A 25 basis point decrease in the yield curve would decrease net interest income by an estimated 0.03 percent over one year and by 0.03 percent over two years. For further discussion of CTBI’s market risk, see the Management’s Discussion and Analysis of Financial Condition and Results of Operations--Liquidity and Market Risk included in the Annual Report on Form 10-K for the year ended December 31, 2009.

#### Item 4. Controls and Procedures

#### EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

CTBI’s management is responsible for establishing and maintaining effective disclosure controls and procedures, as defined under Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934. As of the end of the period covered by this report, an evaluation was carried out by CTBI’s management, with the participation of our Chief Executive Officer and the Executive Vice President/Treasurer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, management concluded that disclosure controls and



procedures as of June 30, 2010 were effective in ensuring material information required to be disclosed in this quarterly report on Form 10-Q was recorded, processed, summarized, and reported on a timely basis.

#### CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There were no changes in CTBI's internal control over financial reporting that occurred during the quarter ended June 30, 2010 that have materially affected, or are reasonably likely to materially affect, CTBI's internal control over financial reporting.

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PART II - OTHER INFORMATION

|          |  |                              |
|----------|--|------------------------------|
| Item 1.  | Legal Proceedings  | None                         |
| Item 1A. | Risk Factors   | None                         |
| Item 2.  | Unregistered Sales of Equity Securities and Use of Proceeds  | None                         |
| Item 3.  | Defaults Upon Senior Securities  | None                         |
| Item 4.  | Reserved   | None                         |
| Item 5.  | Other Information:<br>CTBI's Principal Executive Officer and Principal Financial Officer have furnished to the SEC the certifications with respect to this Form 10-Q that are required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002 |                              |
| Item 6.  | a. Exhibits:   |                              |
|          | (1) Certifications Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  | Exhibit 31.1<br>Exhibit 31.2 |
|          | (2) Certifications Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  | Exhibit 32.1<br>Exhibit 32.2 |

SIGNATURES

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

COMMUNITY TRUST BANCORP, INC.

Date: August 6, 2010

By: /s/ Jean R. Hale  
Jean R. Hale  
Chairman, President and Chief Executive Officer

By: /s/ Kevin J. Stumbo  
Kevin J. Stumbo  
Executive Vice President and Treasurer  
(Principal Financial Officer)

