PEOPLES BANCORP INC
Form 10-Q
October 23, 2009
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2009

OR

o 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: 0-16772

PEOPLES BANCORP INC.
(Exact name of Registrant as specified in its charter)

Ohio	31-0987416
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
138 Putnam Street, P. O. Box 738, Marietta, Ohio	45750
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (740) 373-3155

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).Yes oNo o

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

Large accelerated   Accelerated filer x   Non-accelerated filer o

filer o	(Do not check if a smaller reporting company)	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 10,480,835 common shares, without par value, at October 21, 2009.

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As used in this Quarterly Report on Form 10-Q ("Form 10-Q"), "Peoples" refers to Peoples Bancorp Inc. and its consolidated subsidiaries collectively, except where the context indicates the reference relates solely to the registrant, Peoples Bancorp Inc.

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
PEOPLES BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (Unaudited)

(Dollars in thousands)	September 30, 2009	December 31, 2008
Assets		
Cash and cash equivalents:		
Cash and due from banks	$ 29,699	$ 34,389
Interest-bearing deposits in other banks	11,999	1,209
Total cash and cash equivalents	41,698	35,598
Available-for-sale investment securities, at fair value (amortized cost of $704,388 at September 30, 2009 and $696,855 at December 31, 2008)	725,898	684,757
Other investment securities, at cost	24,356	23,996
Total investment securities	750,254	708,753
Loans, net of deferred fees and costs	1,068,039	1,104,032
Allowance for loan losses	(26,249)	(22,931)
Net loans	1,041,790	1,081,101
Loans held for sale	2,591	791
Bank premises and equipment, net	24,952	25,111
Bank owned life insurance	52,679	51,873
Goodwill	62,520	62,520
Other intangible assets	3,285	3,886
Other assets	24,985	32,705
Total assets	$ 2,004,754	$ 2,002,338
Liabilities		
Deposits:		
Non-interest-bearing	$ 187,011	$ 180,040
Interest-bearing	1,206,564	1,186,328
Total deposits	1,393,575	1,366,368
Short-term borrowings	48,344	98,852
Long-term borrowings	277,085	308,297
Junior subordinated notes held by subsidiary trust	22,522	22,495
Accrued expenses and other liabilities	18,865	19,700
Total liabilities	1,760,391	1,815,712

Stockholders' Equity		
Preferred stock, no par value, 50,000 shares authorized, 39,000 shares		
issued at September 30, 2009, and no shares issued at December 31, 2008	38,518	–
Common stock, no par value, 24,000,000 shares authorized,		
11,023,079 shares issued at September 30, 2009 and 10,975,364 shares		
issued at December 31, 2008, including shares in treasury	166,090	164,716
Retained earnings	46,576	50,512
Accumulated comprehensive income (loss), net of deferred income taxes	9,638	(12,288)
Treasury stock, at cost, 651,722 shares at September 30, 2009 and		
641,480 shares at December 31, 2008	(16,459)	(16,314)
Total stockholders' equity	244,363	186,626
Total liabilities and stockholders' equity	$ 2,004,754	$ 2,002,338

See Notes to the Unaudited Consolidated Financial Statements

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PEOPLES BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

(Dollars in thousands, except per share data)	Three Months Ended Sept. 30, 2009	2008	Nine Months Ended Sept. 30, 2009	2008
Interest Income:				
Interest and fees on loans	$ 16,053	$ 18,027	$ 49,021	$ 56,805
Interest and dividends on taxable investment securities	8,716	7,361	26,321	20,929
Interest on tax-exempt investment securities	682	663	2,147	2,115
Other interest income	21	12	62	61
Total interest income	25,472	26,063	77,551	79,910
Interest Expense:				
Interest on deposits	6,490	7,458	20,052	23,704
Interest on short-term borrowings	111	689	388	3,006
Interest on long-term borrowings	2,907	2,819	9,200	7,957
Interest on junior subordinated notes held by subsidiary trust	495	495	1,485	1,481
Total interest expense	10,003	11,461	31,125	36,148
Net interest income	15,469	14,602	46,426	43,762
Provision for loan losses	10,168	5,996	18,965	14,198
Net interest income after provision for loan losses	5,301	8,606	27,461	29,564
Gross impairment losses	(6,395)	–	(6,395)	(260)
Less: Non-credit losses included in other comprehensive income	(465)	–	(465)	–
Net impairment losses	(5,930)	–	(5,930)	(260)
Other Income:				
Deposit account service charges	2,703	2,761	7,718	7,431
Insurance income	2,228	2,439	7,378	7,701
Trust and investment income	1,189	1,266	3,484	3,915
Electronic banking income	986	994	2,929	2,925
Mortgage banking income	276	104	1,384	500
Gain (loss) on investment securities	276	(111)	864	134
Bank owned life insurance	254	391	807	1,220
Loss on asset disposals	(41)	(14)	(103)	(11)
Other non-interest income	150	201	568	581

Total other income	8,021	8,031	25,029	24,396
Other Expenses:				
Salaries and employee benefit costs	7,015	7,035	22,038	21,501
Net occupancy and equipment	1,398	1,344	4,366	4,169
Professional fees	742	528	2,183	1,594
FDIC insurance	687	55	2,782	142
Electronic banking expense	618	638	1,781	1,678
Data processing and software	603	521	1,704	1,622
Franchise tax	466	416	1,293	1,248
Amortization of other intangible assets	307	390	956	1,208
Marketing	279	273	811	1,010
Other non-interest expense	1,972	1,993	6,196	5,807
Total other expenses	14,087	13,193	44,110	39,979
(Loss) income before income taxes	(6,695)	3,444	2,450	13,721
Income tax (benefit) expense	(2,630)	493	(526)	3,169
Net (loss) income	$ (4,065)	$ 2,951	$ 2,976	$ 10,552
Preferred dividends	512	–	1,364	–
Net (loss) income available to common shareholders	$ (4,577)	$ 2,951	$ 1,612	$ 10,552
Earnings per common share - basic	$ (0.44)	$ 0.29	$ 0.16	$ 1.02
Earnings per common share - diluted	$ (0.44)	$ 0.28	$ 0.16	$ 1.02
Weighted-average number of common shares outstanding - basic	10,372,946	10,319,534	10,359,569	10,309,010
Weighted-average number of common shares outstanding - diluted	10,390,275	10,354,522	10,372,630	10,350,008
Cash dividends declared on common shares	$ 1,047	$ 2,397	$ 5,852	$ 7,072
Cash dividends declared per common share	$ 0.10	$ 0.23	$ 0.56	$ 0.68

See Notes to the Unaudited Consolidated Financial Statements

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PEOPLES BANCORP INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (Unaudited)

(Dollars in thousands, except per share data)	Preferred Stock	Common Stock	Retained Earnings	Accumulated Comprehensive Income (Loss)	Treasury Stock	Total
Balance, December 31, 2008	$ –	$ 164,716	$ 50,512	$ (12,288)	$ (16,314)	$ 186,626
Net income			2,976			2,976
Other comprehensive income, net of tax				22,230		22,230
Issuance of preferred shares and common stock warrant	38,454	546				39,000
Accrued dividends on preferred shares			(1,300)			(1,300)
Amortization of discount on preferred shares	64		(64)			–
Cash dividends declared of $0.56 per common share			(5,852)			(5,852)
Tax benefit from exercise of stock options		(9)				(9)
Purchase of treasury stock					(190)	(190)
Common shares issued under dividend reinvestment plan		724				724
Stock-based compensation expense		113				113
Reissuance of treasury stock for deferred compensation plan					45	45
Cumulative effect adjustment for noncredit portion of previously recorded OTTI losses			304	(304)		–

Balance, September 30, 2009	$	38,518	$	166,090	$	46,576	$	9,638	$	(16,459)	$	244,363

See Notes to the Unaudited Consolidated Financial Statements

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PEOPLES BANCORP INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Nine Months Ended September 30,	
(Dollars in thousands)	2009	2008
Net cash provided by operating activities	$ 21,625	$ 25,232
Investing activities		
Available-for-sale securities:		
Purchases	(187,374)	(237,441)
Proceeds from sales	41,521	64,893
Proceeds from maturities, calls and prepayments	135,727	110,127
Net decrease (increase) in loans	19,513	(2,988)
Net expenditures for premises and equipment	(1,853)	(2,904)
Proceeds from sales of other real estate owned	512	272
Investment in limited partnership and tax credit funds	(248)	(249)
Net cash provided by (used in) investing activities	7,798	(68,290)
Financing activities		
Net increase in non-interest-bearing deposits	6,971	9,417
Net increase in interest-bearing deposits	20,159	54,991
Net decrease in short-term borrowings	(50,508)	(82,080)
Proceeds from long-term borrowings	5,000	115,000
Payments on long-term borrowings	(36,211)	(53,413)
Issuance of preferred shares and common stock warrant	39,000	–
Preferred stock dividends	(1,056)	–
Cash dividends paid on common shares	(6,482)	(6,268)
Purchase of treasury stock	(190)	(449)
Proceeds from issuance of common shares	4	203
Excess tax (expense) benefit for stock-based compensation	(10)	15
Net cash (used in) provided by financing activities	(23,323)	37,416
Net increase (decrease) in cash and cash equivalents	6,100	(5,642)
Cash and cash equivalents at beginning of period	35,598	45,200
Cash and cash equivalents at end of period	$ 41,698	$ 39,558

See Notes to the Unaudited Consolidated Financial Statements

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PEOPLES BANCORP INC. AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

Basis of Presentation: The accompanying Unaudited Consolidated Financial Statements of Peoples Bancorp Inc. and its subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States ("US GAAP") for interim financial information and the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, these financial statements do not contain all of the information and footnotes required by US GAAP for annual financial statements and should be read in conjunction with Peoples' Annual Report on Form 10-K for the fiscal year ended December 31, 2008 ("2008 Form 10-K").

The accounting and reporting policies followed in the presentation of the accompanying Unaudited Consolidated Financial Statements are consistent with those described in Note 1 of the Notes to the Consolidated Financial Statements included in Peoples' 2008 Form 10-K, as updated by the information contained in this Form 10-Q. Management has evaluated all significant events and transactions that occurred after September 30, 2009, but prior to October 22, 2009, the date these consolidated financial statements were issued, for potential recognition or disclosure in these consolidated financial statements. In the opinion of management, these consolidated financial statements reflect all adjustments necessary to present fairly such information for the periods and dates indicated. Such adjustments are normal and recurring in nature. All significant intercompany accounts and transactions have been eliminated. The Consolidated Balance Sheet at December 31, 2008, contained herein has been derived from the audited Consolidated Balance Sheets included in Peoples' 2008 Form 10-K.

The preparation of the consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Results of operations for interim periods are not necessarily indicative of the results to be expected for the full year, due in part to seasonal variations and unusual or infrequently occurring items. Peoples' results of operations for the three and nine months ended September 30, 2009, were impacted by the recognition of FDIC insurance expense of $930,000 ($605,000 after-tax) associated with a special assessment imposed on all FDIC-insured depository institutions as of June 30, 2009. This special assessment was collected on September 30, 2009. In addition, Peoples' insurance income includes contingent performance based insurance commissions that are recognized by Peoples when received, which typically occurs during the first quarter of each year.

Preferred Stock and Common Stock Warrant: As more fully described in Note 4, Peoples issued preferred stock and a common stock warrant, which are classified in stockholders' equity on the Consolidated Balance Sheet at September 30, 2009. The outstanding preferred stock has similar characteristics of an "Increasing Rate Security" as described by Securities and Exchange Commission ("SEC") Staff Accounting Bulletin Topic 5Q, Increasing Rate Preferred Stock. The proceeds received in conjunction with the issuance of the preferred stock and common stock warrant were allocated to the preferred stock and common stock warrant based on their relative fair values. Discounts on the increasing rate preferred stock are amortized over the expected life of the preferred stock (5 years), by charging imputed dividend cost against retained earnings and increasing the carrying amount of the preferred stock by a corresponding amount. The discount at the time of issuance is computed as the present value of the difference between dividends that will be payable in future periods and the dividend amount for a corresponding number of periods, discounted at a market rate for dividend yield on comparable securities. The amortization in each period is the amount which, together with the stated dividend in the period, results in a constant rate of effective cost with regard to the carrying amount of the preferred stock.

Common stock warrants are evaluated for liability or equity treatment. The common stock warrant outstanding is carried in stockholders' equity until exercised or expired based on the view of both the SEC and Financial Accounting Standards Board (the "FASB") that they would not object to classification of such warrants as permanent equity. This view is consistent with the objective of the Capital Purchase Program that equity in these securities should be considered part of equity for regulatory reporting purposes. The fair value of the common stock warrant used in allocating total proceeds received was determined based on a binomial model.

New Accounting Pronouncements: On June 29, 2009, the FASB issued an accounting pronouncement establishing the FASB Accounting Standards CodificationTM (the "ASC") as the source of authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities. This pronouncement was effective for financial statements issued for interim and annual periods ending after September 15, 2009, for most entities. On the effective date, all non-SEC accounting and reporting standards will be superceded. Peoples adopted this new accounting pronouncement for the quarterly period ended September 30, 2009, as required, and adoption did not have a material impact on Peoples' financial statements taken as a whole.

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On June 12, 2009, the FASB issued two related accounting pronouncements changing the accounting principles and disclosures requirements related to securitizations and special-purpose entities. Specifically, these pronouncements eliminate the concept of a "qualifying special-purpose entity", change the requirements for derecognizing financial assets and change how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. These pronouncements also expand existing disclosure requirements to include more information about transfers of financial assets, including securitization transactions, and where companies have continuing exposure to the risks related to transferred financial assets. These pronouncements will be effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application is prohibited. The recognition and measurement provisions regarding transfers of financial assets shall be applied to transfers that occur on or after the effective date. Peoples will adopt these new pronouncements on January 1, 2010, as required. Management has not yet determined the impact adoption may have on Peoples' consolidated financial statements.

On May 28, 2009, the FASB issued an accounting pronouncement establishing general standards of accounting for and disclosure of subsequent events, which are events occurring after the balance sheet date but before the date the financial statements are issued or available to be issued. In particular, the pronouncement requires entities to recognize in the financial statements the effect of all subsequent events that provide additional evidence of conditions that existed at the balance sheet date, including the estimates inherent in the financial preparation process. Entities may not recognize the impact of subsequent events that provide evidence about conditions that did not exist at the balance sheet date but arose after that date. This pronouncement also requires entities to disclose the date through which subsequent events have been evaluated. This pronouncement was effective for interim and annual reporting periods ending after June 15, 2009. Peoples adopted the provisions of this pronouncement for the quarter ended June 30, 2009, as required, and adoption did not have a material impact on Peoples' financial statements taken as a whole.

On April 9, 2009, the FASB issued three related accounting pronouncements intended to provide additional application guidance and enhance disclosures regarding fair value measurements and impairments of securities. In particular, these pronouncements: (1) provide guidelines for making fair value measurements more consistent with the existing accounting principles when the volume and level of activity for the asset or liability have decreased significantly; (2) enhance consistency in financial reporting by increasing the frequency of fair value disclosures and (3) modify existing general standards of accounting for and disclosure of other-than-temporary impairment ("OTTI") losses for impaired debt securities.

The fair value measurement guidance of these pronouncements reaffirms the need for entities to use judgment in determining if a formerly active market has become inactive and in determining fair values when markets have become inactive. The changes to fair value disclosures relate to financial instruments that are not currently reflected on the balance sheet at fair value. Prior to these pronouncements, fair value disclosures for these instruments were required for annual statements only. These disclosures now are required to be included in interim financial statements. The general standards of accounting for OTTI losses were changed to require the recognition of an OTTI loss in earnings only when an entity (1) intends to sell the debt security; (2) more likely than not will be required to sell the security before recovery of its amortized cost basis or (3) does not expect to recover the entire amortized cost basis of the security. In situations when an entity intends to sell or more likely than not will be required to sell the security, the entire OTTI loss must be recognized in earnings. In all other situations, only the portion of the OTTI losses representing the credit loss must be recognized in earnings, with the remaining portion being recognized in other comprehensive income, net of deferred taxes.

All three pronouncements were effective for interim and annual periods ending after June 15, 2009. Entities were permitted to early adopt the provisions of these pronouncements for interim and annual periods ending after March 15, 2009, but had to adopt all three concurrently. Peoples adopted these provisions of these pronouncements for the quarterly period ending June 30, 2009, as required. As a result of adoption, Peoples recorded a cumulative effect adjustment on April 1, 2009, which increased retained earnings by $304,000, net of tax, for the non-credit portion of previously recorded OTTI losses, with a corresponding reduction in accumulated comprehensive income (loss) included in stockholders' equity on the Consolidated Balance Sheet. The adoption of the remaining provisions of these pronouncements did not have any material impact on Peoples' financial statements taken as a whole.

Note 2. Fair Value of Financial Instruments

The measurement of fair value under US GAAP uses a hierarchy intended to maximize the use of observable inputs and minimize the use of unobservable inputs. This hierarchy uses three levels of inputs to measure the fair value of assets and liabilities as follows:

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Level 1: Quoted prices in active exchange markets for identical assets or liabilities; also includes certain U.S. Treasury and other U.S. government and agency securities actively traded in over-the-counter markets.

Level 2: Observable inputs other than Level 1 including quoted prices for similar assets or liabilities, quoted prices in less active markets, or other observable inputs that can be corroborated by observable market data; also includes derivative contracts whose value is determined using a pricing model with observable market inputs or can be derived principally from or corroborated by observable market data. This category generally includes certain U.S. government and agency securities, corporate debt securities, derivative instruments, and residential mortgage loans held for sale.

Level 3: Unobservable inputs supported by little or no market activity for financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation; also includes observable inputs for single dealer nonbinding quotes not corroborated by observable market data. This category generally includes certain private equity investments, retained interests from securitizations, and certain collateralized debt obligations.

Assets measured at fair value on a recurring basis comprised the following at September 30, 2009:

		Fair Value Measurements at Reporting Date Using		
(Dollars in thousands)	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale investment securities	$ 725,898	$ 2,900	$ 721,669	$ 1,329

The investment securities measured at fair value utilizing Level 1 and Level 2 inputs are obligations of the U.S. Treasury, agencies and corporations of the U.S. government, including mortgage-backed securities, bank eligible obligations of any state or political subdivision in the U.S., bank eligible corporate obligations, including private-label mortgage-backed securities and common stocks issued by various unrelated banking holding companies. The fair values used by Peoples are obtained from an independent pricing service and represent either quoted market prices for the identical securities (Level 1 inputs) or fair values determined by pricing models that consider observable market data, such as interest rate volatilities, LIBOR yield curve, credit spreads and prices from market makers and live trading systems.

The investment securities measured at fair value using Level 3 inputs are comprised of four collateralized debt obligations, with a total book value of $2.8 million, and a single corporate obligation, with a book value of $1.0 million, for which there is not an active market. Peoples uses multiple input factors to determine the fair value of these securities. Those input factors are discounted cash flow analysis, structure of the security in relation to current level of deferrals and/or defaults, changes in credit ratings, financial condition of the debtors within the underlying securities, broker quotes for securities with similar structure and credit risk, interest rate movements and pricing of new issuances.

The following is a reconciliation of activity for assets measured at fair value based on significant unobservable (non-market) information:

	Investment Securities
Balance, January 1, 2009	$ 5,422
Other-than-temporary impairment loss included in earnings	(1,930)
Unrealized loss included in comprehensive income	(2,630)
Cumulative effect adjustment for noncredit portion of previously recorded OTTI losses	467
Balance, September 30, 2009	$ 1,329

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

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Impaired Loans: Impaired loans are measured and reported at fair value when management believes collection of contractual interest and principal payments is doubtful. Management's determination of the fair value for these loans represents the estimated net proceeds to be received from the sale of the collateral based on observable market prices and market value provided by independent, licensed or certified appraisers (Level 2 Inputs). At September 30, 2009, impaired loans with an aggregate outstanding principal balance of $27.1 million were measured and reported at a fair value of $21.2 million. During the three months and nine months ended September 30, 2009, Peoples recognized losses on impaired loans of $10.0 million and $15.1 million, respectively, through the allowance for loan losses.

The following table presents the fair values of financial assets and liabilities carried on Peoples' consolidated balance sheet, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis:

	September 30, 2009		December 31, 2008	
(Dollars in thousands)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and cash equivalents	$ 41,698	$ 41,698	$ 35,598	$ 35,598
Investment securities	750,254	750,254	708,753	708,753
Loans	1,041,790	1,047,828	1,081,101	1,088,322
Financial liabilities:				
Deposits	$ 1,393,575	$ 1,404,755	$ 1,366,368	$ 1,376,614
Short-term borrowings	48,344	48,344	98,852	98,852
Long-term borrowings	277,085	287,772	308,297	324,809
Junior subordinated notes held by subsidiary trust	22,522	25,983	22,495	26,009

The methodologies for estimating the fair value of financial assets and liabilities that are measured at fair value on a recurring or non-recurring basis are discussed above. For certain financial assets and liabilities, carrying value approximates fair value due to the nature of the financial instrument. These instruments include cash and cash equivalents, demand and other non-maturity deposits and overnight borrowings. Peoples used the following methods and assumptions in estimating the fair value of the following financial instruments:

Loans: The fair value of performing variable rate loans that reprice frequently and performing demand loans, with no significant change in credit risk, is based on carrying value. The fair value of fixed rate performing loans is estimated using discounted cash flow analyses and interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

The fair value of significant nonperforming loans is based on either the estimated fair value of underlying collateral or estimated cash flows, discounted at a rate commensurate with the risk. Assumptions regarding credit risk, cash flows, and discount rates are determined using available market information and specific borrower information.

Deposits: The fair value of fixed maturity certificates of deposit is estimated using a discounted cash flow calculation based on current rates offered for deposits of similar remaining maturities.

Short-term Borrowings: The fair value of term national market repurchase agreements is estimated using a discounted cash flow calculation based on rates currently available to Peoples for repurchase agreements with similar terms.

Long-term Borrowings: The fair value of long-term borrowings is estimated using discounted cash flow analysis based on rates currently available to Peoples for borrowings with similar terms.

Junior Subordinated Notes Held by Subsidiary Trust: The fair value of the junior subordinated notes held by subsidiary trust is estimated using discounted cash flow analysis based on current market rates of securities with similar risk and remaining maturity.

Bank premises and equipment, customer relationships, deposit base, banking center networks, and other information required to compute Peoples' aggregate fair value are not included in the above information. Accordingly, the above fair values are not intended to represent the aggregate fair value of Peoples.

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Note 3. Investment Securities

The following table summarizes Peoples' available-for-sale investment securities:

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Non-Credit Losses included in Other Comprehensive Income	Fair Value
September 30, 2009					
Obligations of U.S. Treasury and government agencies	$ 84	$ –	$ –	$ –	$ 84
Obligations of U.S. government sponsored agencies	7,776	205	–	–	7,981
Obligations of states and political subdivisions	63,292	4,026	–	–	67,318
Residential mortgage-backed securities	532,709	21,990	(5,687)	–	549,012
Commercial mortgage-backed securities	26,988	135	(449)	–	26,674
U.S. government-backed student loan pools	52,803	5,912	(171)	–	58,544
Bank-issued trust preferred securities	16,745	47	(3,910)	–	12,882
Collateralized debt obligations	2,763	–	(1,502)	(932)	329
Equity securities	1,228	1,897	(51)	–	3,074
Total available-for-sale securities	$ 704,388	$ 34,212	$ (11,770)	$ (932)	$ 725,898
December 31, 2008					
Obligations of U.S. Treasury and government agencies	$ 176	$ 1	$ (1)	$ –	$ 176
Obligations of U.S. government sponsored agencies	8,160	282	–	–	8,442
Obligations of states and political	67,830	1,356	(256)	–	68,930

subdivisions					
Residential mortgage-backed securities	519,744	4,618	(13,161)	–	511,201
Commercial mortgage-backed securities	26,835	5	(889)	–	25,951
U.S. government-backed student loan pools	47,915	21	(2,951)	–	44,985
Bank-issued trust preferred securities	20,742	992	(3,846)	–	17,888
Collateralized debt obligations	4,225	198	–	–	4,423
Equity securities	1,228	1,581	(48)	–	2,761
Total available-for-sale securities	$ 696,855	$ 9,054	$ (21,152)	$ –	$ 684,757

Peoples' investment in collateralized debt obligations ("CDOs") at both September 30, 2009 and December 31, 2008, consisted of four separate securities comprised of trust preferred and subordinated debt securities issued by banks, bank holding companies, insurance companies and real estate investment trusts. Two of these securities were lower mezzanine tranches and the remaining two CDOs were equity tranches. The mezzanine tranches had book values of $1.8 million and $3.4 million at September 30, 2009 and December 31, 2008, respectively, and fair values of $0.2 million and $3.4 million, respectively. Peoples' investment in equity securities was comprised entirely of common stocks issued by various unrelated banking holding companies at both September 30, 2009 and December 31, 2008.

At September 30, 2009, there were no securities of a single issuer, other than U.S. Treasury and government agencies and U.S. government sponsored agencies that exceeded 10% of stockholders' equity. Investment securities having a carrying value of $627.4 million and $619.3 million at September 30, 2009 and December 31, 2008, respectively, were pledged to secure public and trust department deposits and repurchase agreements in accordance with federal and state requirements.

The gross gains and gross losses realized by Peoples from sales of available-for-sale securities for the three and nine months ended September 30 were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	2009	2008	2009	2008
Gross gains realized	$ 276	$ 509	$ 878	$ 1,206
Gross losses realized	-	620	14	1,072
Net gain (loss) realized	$ 276	$ (111)	$ 864	$ 134

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The cost of investment securities sold, and any resulting gain or loss, was based on the specific identification method and recognized as of the trade date.

The following table presents a summary of available-for-sale investment securities that had an unrealized loss:

	Less than 12 Months		12 Months or More		Total	
(Dollars in thousands)	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
September 30, 2009						
Obligations of U.S. Treasury and government agencies	$ –	$ –	$ -	$ –	$ -	$ –
Obligations of U.S. government sponsored agencies	–	–	–	–	–	–
Obligations of states and political subdivisions	–	–	–	–	–	–
Residential mortgage-backed securities	34,554	1,332	87,075	4,355	121,629	5,687
Commercial mortgage-backed securities	16,247	449	–	–	16,247	449
U.S. government-backed student loan pools	–	–	7,705	171	7,705	171
Bank-issued trust preferred securities	3,497	568	7,133	3,342	10,630	3,910
Collateralized debt obligations	–	–	329	2,434	329	2,434
Equity securities	–	–	125	51	125	51
Total available-for-sale securities	$ 54,298	$ 2,349	$ 102,367	$ 10,353	$ 156,665	$ 12,702
December 31, 2008						
Obligations of U.S. Treasury and government agencies	$ –	$ –	$ 29	$ 1	$ 29	$ 1
Obligations of U.S. government sponsored agencies	–	–	–	–	–	–

Obligations of states and political subdivisions	10,521	256	–	–	10,521	256
Residential mortgage-backed securities	197,594	10,485	38,318	2,676	235,912	13,161
Commercial mortgage-backed securities	20,283	889	–	–	20,283	889
U.S. government-backed student loan pools	38,261	2,951	–	–	38,261	2,951
Bank-issued trust preferred securities	5,675	1,719	3,342	2,127	9,017	3,846
Collateralized debt obligations	–	–	–	–	–	–
Equity securities	353	48	–	–	353	48
Total available-for-sale securities	$ 272,687	$ 16,348	$ 41,689	$ 4,804	$ 314,376	$ 21,152

The unrealized losses at both September 30, 2009 and December 31, 2008, were attributable to changes in market interest rates since the securities were purchased. Management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. This analysis requires management to consider various factors, which include (1) duration and magnitude of the decline in value, (2) the financial condition of the issuer or issuers, (3) structure of the security and (4) Peoples' intent to sell the security or whether it is more likely than not that Peoples would be required to sell the security before its anticipated recovery in market value.

At September 30, 2009, management concluded an individual bank-issued trust preferred security, with a book value of $4.0 million, and a single mezzanine tranche CDO, with a book value of $2.7 million, were other-than-temporarily impaired. These determinations reflected management's evaluation of the underlying credit quality of the securities and estimations of cash flows expected to be collected from the securities, which indicated it was probable Peoples would not recover the entire amortized cost of the securities. As a result, Peoples recognized a non-cash impairment loss of $5.9 million ($3.9 million after-tax) in earnings for the three months ended September 30, 2009, of which $4.0 million related to the individual bank-issued trust preferred security and $1.9 million related to the mezzanine tranche CDO. This impairment loss represents management's estimate of credit losses incurred during the third quarter of 2009. Since Peoples does not intend to sell, nor is it more likely than not that Peoples will be required to sell, the security prior to recovery, the non-credit component was recognized in other comprehensive income.

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The measurement of the credit loss incurred on the mezzanine tranche CDO was based upon management's estimation of future cash flows versus the cash flows projected previously. In estimating future cash flows, management considers the structure and term of the pool and the financial condition of the underlying issuers. Specifically, the evaluation incorporates factors such as over-collateralization and interest coverage tests, interest rates and appropriate risk premiums, the timing and amount of interest and principal payments and the allocation of payments to the various tranches. Current estimates of cash flows are based on the recent trustee reports, announcements of deferrals or defaults and assumptions regarding expected future default rates, prepayment and recovery rates and other relevant information. Additionally, management considers the impact on future cash flows should institutions identified as possessing a higher probability of default, based upon an evaluation of performance metrics, were to default in the near term. Key assumptions used include: (1) current defaults would have no recovery and (2) current deferrals considered as defaults with no expected recovery.

Management performed its quarterly analysis of the remaining securities with an unrealized loss at September 30, 2009, and concluded no other individual securities were other-than-temporarily impaired.

The following table summarizes the roll-forward of cumulative credit losses on available-for-sale securities for which a portion of an other-than-temporary impairment is recognized in other comprehensive income, including those securities for which a cumulative effect adjustment was recorded:

	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2009
Balance, beginning of period	$ 4,328	$ 4,795
Cumulative effect adjustment for noncredit portion of previously recorded OTTI losses	–	(467)
Credit-related other-than-temporary impairment recorded	1,930	1,930
Balance, end of period	$ 6,258	$ 6,258

The following table presents the amortized costs, fair value and weighted-average yield of securities by contractual maturity at September 30, 2009. The average yields are based on the amortized cost. In some cases, the issuers may have the right to call or prepay obligations without call or prepayment penalties prior to the contractual maturity date. Rates are calculated on a fully tax-equivalent basis using a 35% federal income tax rate.

(Dollars in thousands)	Within 1 Year	1 to 5 Years	5 to 10 Years	Over 10 Years	Total
Amortized cost					
Obligations of U.S. Treasury and government agencies	$ –	$ –	$ 84	$ –	$ 84
Obligations of U.S. government					
	–	3,309	4,467	–	7,776

sponsored agencies					
Obligations of states and					
political subdivisions	1,364	13,181	20,558	28,189	63,292
Residential mortgage-backed securities	–	4,176	105,245	423,288	532,709
Commercial mortgage-backed securities	–	–	–	26,988	26,988
U.S. government-backed student loan pools	–	–	15,806	36,997	52,803
Bank-issued trust preferred securities	–	–	–	16,745	16,745
Collateralized debt obligations	–	–	–	2,763	2,763
Equity securities	–	–	–	1,228	1,228
Total available-for-sale securities	$ 1,364	$ 20,666	$ 146,160	$ 536,198	$ 704,388

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(Dollars in thousands)	Within 1 Year	1 to 5 Years	5 to 10 Years	Over 10 Years	Total
Fair value					
Obligations of U.S. Treasury and government agencies	$ –	$ –	$ 84	$ –	$ 84
Obligations of U.S. government sponsored agencies	–	3,369	4,612	–	7,981
Obligations of states and political subdivisions	1,370	13,599	21,975	30,374	67,318
Residential mortgage-backed securities	–	4,320	106,460	438,232	549,012
Commercial mortgage-backed securities	–	–	–	26,675	26,675
U.S. government-backed student loan pools	–	–	16,928	41,616	58,544
Bank-issued trust preferred securities	–	–	–	12,882	12,882
Collateralized debt obligations	–	–	–	329	329
Equity securities	–	–	–	3,073	3,073
Total available-for-sale securities	$ 1,370	$ 21,288	$ 150,059	$ 553,181	$ 725,898
Total average yield	5.87%	5.81%	5.04%	5.36%	5.31%

Peoples' other investment securities on the Consolidated Balance Sheets consist solely of restricted equity securities of the Federal Home Loan Bank ("FHLB") of Cincinnati and the Federal Reserve Bank of Cleveland. These securities are carried at cost since they do not have readily determinable fair values due to their restricted nature and Peoples does not exercise significant influence.

Note 4. Stockholders' Equity

The following table details the progression in shares of Peoples' preferred, common and treasury stock during the period presented:

	Preferred Stock	Common Stock	Treasury Stock
	–	10,975,364	641,480

Shares at December 31, 2008			
Issuance of preferred shares	39,000		
Changes related to stock-based compensation awards:			
Release of restricted common shares		2,125	
Changes related to deferred compensation plan:			
Purchase of treasury stock			12,451
Reissuance of treasury stock			(2,209)
Common shares issued under dividend reinvestment plan		45,590	
Shares at September 30, 2009	39,000	11,023,079	651,722

Under its Amended Articles of Incorporation, Peoples is authorized to issue up to 50,000 preferred shares, in one or more series, having such voting powers, designations, preferences, rights, qualifications, limitations and restrictions as determined by the Board of Directors. On January 28, 2009, Peoples' Board of Directors created a series of preferred shares designated as Peoples' Fixed Rate Cumulative Perpetual Preferred Shares, Series A, each without par value and having a liquidation preference of $1,000 per share, and fixed 39,000 shares as the authorized number of such shares (the "Series A Preferred Shares").

On January 30, 2009, Peoples issued and sold to the United States Department of the Treasury (the "U.S. Treasury") (i) 39,000 of Peoples' Series A Preferred Shares, and (ii) a ten-year warrant (the "Warrant") to purchase 313,505 Peoples common shares, at an exercise price of $18.66 per share (subject to certain anti-dilution and other adjustments), for an aggregate purchase price of $39 million in cash.

The Series A Preferred Shares accrue cumulative quarterly dividends at a rate of 5% per annum from January 30, 2009 to, but excluding February 15, 2014, and 9% per annum thereafter. These dividends will be paid only if, as and when declared by Peoples' Board of Directors. The Series A Preferred Shares have no maturity date and rank senior to the common shares with respect to the payment of dividends and distributions and amounts payable upon liquidation, dissolution and winding up of Peoples. Peoples has the option to redeem the Series A Preferred Shares at 100% of their liquidation preference plus accrued and unpaid dividends, subject to the approval of the Board of Governors of the Federal Reserve System and the Office of the Comptroller of Currency. The Series A Preferred Shares are generally non-voting.

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The U.S. Treasury may not transfer a portion or portions of the Warrant with respect to, and/or exercise the Warrant for more than one-half of, the 313,505 common shares issuable upon exercise of the Warrant, in the aggregate, until the earlier of (i) the date on which Peoples has received aggregate gross proceeds of not less than $39 million from one or more Qualified Equity Offerings and (ii) December 31, 2009. However, if Peoples were to redeem all of the Series A Preferred Shares as permitted by and in accordance with the provisions of the American Recovery and Reinvestment Act and the documents required to consummate the redemption, Peoples has the option to repurchase the Warrant from the U.S. Treasury. If Peoples declines to repurchase the Warrant, the U.S. Treasury will be permitted, subject to compliance with applicable securities laws, to transfer all or a portion of the Warrant with respect to, and/or exercise the Warrant for, all or a portion of the number of common shares issuable thereunder, at any time and without limitation. In the event Peoples completes one or more Qualified Equity Offerings on or prior to December 31, 2009, that result in Peoples receiving aggregate gross proceeds of not less than $39 million, the number of the common shares underlying the portion of the Warrant then held by the U.S. Treasury will be reduced by one-half of the common shares originally covered by the Warrant. The U.S. Treasury has agreed not to exercise voting power with respect to any common shares issued to it upon exercise of the Warrant. Any common shares issued by Peoples upon exercise of the Warrant will be issued from common shares held in treasury to the extent available. If no treasury shares are available, common shares will be issued from authorized but unissued common shares. At September 30, 2009, there had been no changes to the number of common shares covered by the Warrant nor had the U.S. Treasury exercised any portion of the Warrant.

The proceeds received from the U.S. Treasury were allocated to the Series A Preferred Shares and the Warrant based on relative fair value. The fair value of the Series A Preferred Shares was determined through a discounted future cash flow model at a discount rate of 14%. The fair value of the Warrant was calculated using a binomial option pricing model, which includes assumptions regarding Peoples' dividend yield, stock price volatility, and the risk-free interest rate. The relative fair value of the Series A Preferred Shares and the Warrant on January 30, 2009, was $38.5 million and $0.5 million, respectively.

Peoples calculated a discount on the Series A Preferred Shares in the amount of $0.5 million, which is being amortized over a 5-year period. The effective yield on the amortization of the Series A Preferred Shares is approximately 5.32%. In determining net income available to common shareholders, the periodic amortization and the cash dividend on the preferred stock are subtracted from net income. For the nine months ended September 30, 2009, Peoples accrued dividends and recorded amortization on Series A Preferred Shares for $1,300,000 and $64,000, respectively.

Note 5. Comprehensive Income (Loss)

The following details the change in the components of Peoples' accumulated other comprehensive (loss) income for the nine months ended September 30, 2009:

(Dollars in thousands)	Unrealized (Loss) Gain on Securities	Unrecognized Net Pension and Postretirement Costs	Accumulated Comprehensive (Loss) Income
Balance, December 31, 2008	$ (7,863)	$ (4,425)	$ (12,288)
Current period change, net of tax	22,148	82	22,230
Cumulative effect adjustment for noncredit			

portion of previously recorded OTTI losses		(304)		–		(304)
Balance, September 30, 2009	$	13,981	$	(4,343)	$	9,638

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The components of other comprehensive income (loss) for the three and nine months ended September 30 were as follows:

(Dollars in thousands)	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008
Net (loss) income	$ (4,065)	$ 2,951	$ 2,976	$ 10,552
Other comprehensive income (loss):				
Available-for-sale investment securities:				
Gross unrealized holding gain (loss) arising in the period	12,088	(8,218)	29,939	(15,715)
Related tax (expense) benefit	(4,231)	2,876	(10,479)	5,500
Non-credit losses on securities during the period	(465)	–	(932)	–
Related tax benefit	163	–	326	–
Less: reclassification adjustment for net (loss) included in earnings	(5,654)	(111)	(5,066)	(126)
Related tax benefit	1,979	39	1,773	44
Net effect on other comprehensive income (loss)	11,230	(5,270)	22,148	(10,133)
Defined benefit plans:				
Amortization of unrecognized loss and service cost on pension plan	42	9	126	9