

FIRST MID ILLINOIS BANCSHARES INC
Form 10-Q
May 08, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2008

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 0-13368

FIRST MID-ILLINOIS BANCSHARES, INC.
(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

37-1103704
(I.R.S. employer identification no.)

1515 Charleston Avenue,
Mattoon, Illinois
(Address of principal executive offices)

61938
(Zip code)

(217) 234-7454
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, 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. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a smaller reporting
company)

Smaller reporting company

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

As of May 7, 2008, 6,238,271 common shares, \$4.00 par value, were outstanding.

PART I

ITEM 1. FINANCIAL STATEMENTS

Condensed Consolidated Balance Sheets

(Unaudited)

| | March 31, 2008 | December 31, 2007 |
|---|-------------------|-------------------------|
| (In thousands, except share data) | | |
| Assets | | |
| Cash and due from banks: | | |
| Non-interest bearing | \$ 22,808 | \$ 28,737 |
| Interest bearing | 23,617 | 136 |
| Federal funds sold | 18,288 | 2,250 |
| Cash and cash equivalents | 64,713 | 31,123 |
| Investment securities: | | |
| Available-for-sale, at fair value | 169,783 | 184,033 |
| Held-to-maturity, at amortized cost (estimated fair value of \$1,062 and \$1,194 at March 31, 2008 and December 31, 2007, respectively) | 1,043 | 1,178 |
| Loans held for sale | 3,612 | 1,974 |
| Loans | 734,229 | 746,187 |
| Less allowance for loan losses | (6,251) | (6,118) |
| Net loans | 727,978 | 740,069 |
| Interest receivable | 6,582 | 8,309 |
| Premises and equipment, net | 15,210 | 15,520 |
| Goodwill, net | 17,363 | 17,363 |
| Intangible assets, net | 4,136 | 4,327 |
| Other assets | 10,740 | 12,442 |
| Total assets | \$ 1,021,160 | \$ 1,016,338 |
| Liabilities and Stockholders' Equity | | |
| Deposits: | | |
| Non-interest bearing | \$ 120,775 | \$ 124,486 |
| Interest bearing | 674,932 | 646,097 |
| Total deposits | 795,707 | 770,583 |
| Securities sold under agreements to repurchase | 54,251 | 68,300 |
| Interest payable | 2,604 | 2,264 |
| Other borrowings | 59,250 | 67,250 |
| Junior subordinated debentures | 20,620 | 20,620 |
| Other liabilities | 5,532 | 6,869 |
| Total liabilities | 937,964 | 935,886 |
| Stockholders' Equity | | |
| Common stock, \$4 par value; authorized 18,000,000 shares; issued 7,163,687 shares in 2008 and 7,135,113 shares in 2007 | 28,655 | 28,540 |
| Additional paid-in capital | 23,941 | 23,308 |
| Retained earnings | 52,817 | 49,895 |
| Deferred compensation | 2,629 | 2,568 |
| Accumulated other comprehensive income | 1,815 | 1,096 |
| Less treasury stock at cost, 923,385 shares in 2008 and 858,396 shares in 2007 | (26,661) | (24,955) |
| Total stockholders' equity | 83,196 | 80,452 |
| Total liabilities and stockholders' equity | \$ 1,021,160 | \$ 1,016,338 |

See accompanying notes to unaudited condensed consolidated financial statements.

Condensed Consolidated Statements of Income (unaudited)
(In thousands, except per share data)

| | Three months ended March 31, | |
|---|---------------------------------|-----------|
| | 2008 | 2007 |
| Interest income: | | |
| Interest and fees on loans | \$ 12,354 | \$ 12,172 |
| Interest on investment securities | 2,122 | 2,269 |
| Interest on federal funds sold | 158 | 81 |
| Interest on deposits with other financial institutions | 153 | 4 |
| Total interest income | 14,787 | 14,526 |
| Interest expense: | | |
| Interest on deposits | 4,850 | 5,290 |
| Interest on securities sold under agreements to repurchase | 368 | 577 |
| Interest on other borrowings | 701 | 587 |
| Interest on subordinated debentures | 366 | 395 |
| Total interest expense | 6,285 | 6,849 |
| Net interest income | 8,502 | 7,677 |
| Provision for loan losses | 191 | 186 |
| Net interest income after provision for loan losses | 8,311 | 7,491 |
| Other income: | | |
| Trust revenues | 744 | 717 |
| Brokerage commissions | 99 | 112 |
| Insurance commissions | 709 | 699 |
| Service charges | 1,321 | 1,270 |
| Securities gains, net | 151 | 139 |
| Mortgage banking revenue, net | 108 | 121 |
| Other | 838 | 774 |
| Total other income | 3,970 | 3,832 |
| Other expense: | | |
| Salaries and employee benefits | 4,124 | 4,076 |
| Net occupancy and equipment expense | 1,235 | 1,217 |
| Amortization of intangible assets | 191 | 217 |
| Stationery and supplies | 143 | 145 |
| Legal and professional | 479 | 474 |
| Marketing and promotion | 176 | 206 |
| Other | 1,437 | 1,196 |
| Total other expense | 7,785 | 7,531 |
| Income before income taxes | 4,496 | 3,792 |
| Income taxes | 1,574 | 1,198 |
| Net income | \$ 2,922 | \$ 2,594 |
| Per share data: | | |
| Basic earnings per share | \$ 0.47 | \$ 0.40 |
| Diluted earnings per share | \$ 0.46 | \$ 0.40 |
| Cash dividends per share | \$ - | \$ - |

See accompanying notes to unaudited condensed consolidated financial statements.

| Condensed Consolidated Statements of Cash Flows (unaudited) (In thousands) | Three months ended March 31, | |
|---|---------------------------------|-----------|
| | 2008 | 2007 |
| Cash flows from operating activities: | | |
| Net income | \$ 2,922 | \$ 2,594 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | 191 | 186 |
| Depreciation, amortization and accretion, net | 516 | 450 |
| Stock-based compensation expense | 16 | 8 |
| Gains on sale of securities, net | (151) | (139) |
| (Gains) losses on sale of other real property owned, net | 44 | (19) |
| Loss on write down of fixed assets | 132 | - |
| Gains on sale of loans held for sale, net | (121) | (130) |
| Origination of loans held for sale | (12,134) | (11,556) |
| Proceeds from sale of loans held for sale | 10,617 | 12,616 |
| Decrease in other assets | 2,662 | 1,211 |
| Increase (decrease) in other liabilities | 197 | (715) |
| Net cash provided by operating activities | 4,891 | 4,506 |
| Cash flows from investing activities: | | |
| Proceeds from sales of securities available-for-sale | - | 7,567 |
| Proceeds from maturities of securities available-for-sale | 56,914 | 11,738 |
| Proceeds from maturities of securities held-to-maturity | 135 | 125 |
| Purchases of securities available-for-sale | (41,263) | (12,572) |
| Net decrease in loans | 11,900 | 13,434 |
| Purchases of premises and equipment | (85) | (158) |
| Proceeds from sales of other real property owned | 186 | 152 |
| Net cash provided by investing activities | 27,787 | 20,286 |
| Cash flows from financing activities: | | |
| Net increase in deposits | 25,124 | 7,657 |
| Decrease in federal funds purchased | - | (6,800) |
| Decrease in repurchase agreements | (14,049) | (18,393) |
| Proceeds from short term FHLB advances | - | 7,000 |
| Repayment of short term FHLB advances | (10,000) | (7,000) |
| Proceeds from long term FHLB advances | - | 10,000 |
| Proceeds from long term debt | 2,000 | 4,000 |
| Repayment of long term debt | - | (500) |
| Proceeds from issuance of common stock | 262 | 444 |
| Purchase of treasury stock | (1,646) | (3,008) |
| Dividends paid on common stock | (779) | (732) |
| Net cash provided by (used in) financing activities | 912 | (7,332) |
| Increase in cash and cash equivalents | 33,590 | 17,460 |
| Cash and cash equivalents at beginning of period | 31,123 | 21,836 |
| Cash and cash equivalents at end of period | \$ 64,713 | \$ 39,296 |

Supplemental disclosures of cash flow information

Cash paid during the period for:

| | | |
|--|----------|----------|
| Interest | \$ 5,945 | \$ 6,732 |
| Income taxes | 450 | 232 |
| Supplemental disclosures of noncash investing and financing activities | | |
| Loans transferred to real estate owned | 135 | 18 |
| Dividends reinvested in common stock | 414 | 383 |
| Net tax benefit related to option and deferred compensation plans | 55 | 166 |

See accompanying notes to unaudited condensed consolidated financial statements.

Notes to Consolidated Financial Statements
(unaudited)

Basis of Accounting and Consolidation

The unaudited condensed consolidated financial statements include the accounts of First Mid-Illinois Bancshares, Inc. (“Company”) and the following wholly-owned subsidiaries: Mid-Illinois Data Services, Inc. (“MIDS”), The Checkley Agency, Inc. (“Checkley”), and First Mid-Illinois Bank & Trust, N.A. (“First Mid Bank”). All significant intercompany balances and transactions have been eliminated in consolidation. The financial information reflects all adjustments which, in the opinion of management, are necessary for a fair presentation of the results of the interim periods ended March 31, 2008 and 2007, and all such adjustments are of a normal recurring nature. Certain amounts in the prior year’s consolidated financial statements have been reclassified to conform to the March 31, 2008 presentation and there was no impact on net income or stockholders’ equity. The results of the interim period ended March 31, 2008 are not necessarily indicative of the results expected for the year ending December 31, 2008. The Company operates as a one-segment entity for financial reporting purposes.

The 2007 year-end consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by generally accepted accounting principles.

The unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X and do not include all of the information required by U.S. generally accepted accounting principles for complete financial statements and related footnote disclosures although the Company believes that the disclosures made are adequate to make the information not misleading. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s 2007 Annual Report on Form 10-K.

Stock Plans

At the Annual Meeting of Stockholders held May 23, 2007, the stockholders approved the First Mid-Illinois Bancshares, Inc. 2007 Stock Incentive Plan (“SI Plan”). The SI Plan was implemented to succeed the Company’s 1997 Stock Incentive Plan, which had a ten-year term that expired October 21, 2007. The SI Plan is intended to provide a means whereby directors, employees, consultants and advisors of the Company and its subsidiaries may sustain a sense of proprietorship and personal involvement in the continued development and financial success of the Company and its subsidiaries, thereby advancing the interests of the Company and its stockholders. Accordingly, directors and selected employees, consultants and advisors may be provided the opportunity to acquire shares of common stock of the Company on the terms and conditions established herein in the SI Plan.

A maximum of 300,000 shares of common stock may be issued under the SI Plan. As of December 31, 2007, the Company had awarded 32,000 shares under the plan. There were no shares awarded during the first quarter of 2008.

Stock Split

On June 29, 2007, the Company effected a three-for-two stock split in the form of a 50% stock dividend for all shareholders of record as of June 18, 2007. Accordingly, an entry was made for \$9,493,000 to increase the common stock account and decrease the retained earnings account. Par value remained at \$4 per share. All current and prior period share and per share amounts have been restated giving retroactive recognition to the stock split.

Treasury Stock

On May 23, 2007, the Company retired 1,500,000 shares of its treasury stock (after adjustment for stock split), the cost of which was determined using the first-in, first-out method. Accordingly, an entry was made to decrease the treasury stock account for \$21,021,000, the common stock account for \$4,000,000 and the retained earnings account for \$17,021,000.

Website

The Company maintains a website at www.firstmid.com. All periodic and current reports of the Company and amendments to these reports filed with the Securities and Exchange Commission (“SEC”) can be accessed, free of charge, through this website as soon as reasonably practicable after these materials are filed with the SEC.

Comprehensive Income

The Company's comprehensive income for the three-month periods ended March 31, 2008 and 2007 was as follows (in thousands):

| | Three months ended | |
|---------------------------------------|--------------------|----------|
| | March 31, | |
| | 2008 | 2007 |
| Net income | \$ 2,922 | \$ 2,594 |
| Other comprehensive income: | | |
| Unrealized gains during the period | 1,330 | 300 |
| Less realized gains during the period | (151) | (139) |
| Tax effect | (460) | (62) |
| Total other comprehensive income | 719 | 99 |
| Comprehensive income | \$ 3,641 | \$ 2,693 |

New Accounting Pronouncements

In March 2008, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 161 (FAS 161), "Disclosures About Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133." FAS 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. FAS 161 is effective for fiscal years beginning after November 15, 2008. The Company does not expect the implementation of FAS 161 to have a material impact on its consolidated financial statements.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160 (FAS 160), "Noncontrolling Interests in Consolidated Financial Statements -- an amendment of ARB No.51." FAS 160 requires that a noncontrolling interest in a subsidiary be reported separately within equity and the amount of consolidated net income specifically attributable to the noncontrolling interest be identified in the consolidated financial statements. It also calls for consistency in the manner of reporting changes in the parent's ownership interest and requires fair value measurement of any noncontrolling equity investment retained in deconsolidation. FAS 160 is effective for fiscal years beginning after December 15, 2008. The Company does not expect the implementation of FAS 160 to have a material impact on its consolidated financial statements.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141(R) (FAS 141(R)), "Business Combinations." FAS 141(R) will significantly change the financial accounting and reporting of business combination transactions. FAS 141(R) establishes principles for how an acquirer recognizes and measures the identifiable assets acquired, liabilities assumed, and any noncontrolling interest in the acquiree; recognizes and measures goodwill acquired in the business combination or a gain from a bargain purchase; and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. FAS 141(R) is effective for acquisition dates in fiscal years beginning after December 15, 2008. The Company does not expect the implementation of FAS 141(R) to have a material impact on its consolidated financial statements.

Earnings Per Share

A three-for-two common stock split was effected on June 29, 2007, in the form of a 50% stock dividend for the stockholders of record at the close of business on June 18, 2007. Accordingly, information with respect to shares of common stock and earnings per share has been restated for current and prior periods presented to fully reflect the stock split. Basic earnings per share ("EPS") is calculated as net income divided by the weighted average number of common shares outstanding. Diluted EPS is computed using the weighted average number of common shares outstanding, increased by the assumed conversion of the Company's stock options, unless anti-dilutive.

The components of basic and diluted earnings per common share for the three-month periods ended March 31, 2008 and 2007 were as follows:

| | Three months ended March 31, | |
|--|---------------------------------|--------------|
| | 2008 | 2007 |
| Basic Earnings per Share: | | |
| Net income | \$ 2,922,000 | \$ 2,594,000 |
| Weighted average common shares outstanding | 6,278,128 | 6,421,397 |
| Basic earnings per common share | \$.47 | \$.40 |
| Diluted Earnings per Share: | | |
| Weighted average common shares outstanding | 6,278,128 | 6,421,397 |
| Assumed conversion of stock options | 115,427 | 144,561 |
| Diluted weighted average common shares outstanding | 6,393,555 | 6,565,958 |
| Diluted earnings per common share | \$.46 | \$.40 |

Stock options for 124,813 shares of common stock were not considered in computing diluted earnings per share for 2008 because they were anti-dilutive.

Goodwill and Intangible Assets

The Company has goodwill from business combinations, intangible assets from branch acquisitions, and identifiable intangible assets assigned to core deposit relationships and customer lists of Checkley.

The following table presents gross carrying value and accumulated amortization by major intangible asset class as of March 31, 2008 and December 31, 2007 (in thousands):

| | March 31, 2008 | | December 31, 2007 | |
|---|----------------------------|-----------------------------|----------------------------|-----------------------------|
| | Gross Carrying Value | Accumulated Amortization | Gross Carrying Value | Accumulated Amortization |
| Goodwill not subject to amortization (effective 1/1/02) | \$ 21,123 | \$ 3,760 | \$ 21,123 | \$ 3,760 |
| Intangibles from branch acquisition | 3,015 | 2,212 | 3,015 | 2,161 |
| Core deposit intangibles | 5,936 | 3,333 | 5,936 | 3,241 |
| Customer list intangibles | 1,904 | 1,174 | 1,904 | 1,126 |
| | \$ 31,978 | \$ 10,479 | \$ 31,978 | \$ 10,288 |

Total amortization expense for the three months ended March 31, 2008 and 2007 was as follows (in thousands):

| | March 31, | |
|-------------------------------------|-----------|-------|
| | 2008 | 2007 |
| Intangibles from branch acquisition | \$ 51 | \$ 50 |
| Core deposit intangibles | 92 | 119 |

| | | | | |
|---------------------------|----|-----|----|-----|
| Customer list intangibles | | 48 | | 48 |
| | \$ | 191 | \$ | 217 |

Aggregate amortization expense for the current year and estimated amortization expense for each of the five succeeding years is shown in the table below (in thousands):

| | |
|---------------------------------|--------|
| Aggregate amortization expense: | |
| For period 01/01/08-3/31/08 | \$ 191 |
| Estimated amortization expense: | |
| For period 04/01/08-12/31/08 | \$ 574 |
| For year ended 12/31/09 | \$ 730 |
| For year ended 12/31/10 | \$ 704 |
| For year ended 12/31/11 | \$ 704 |
| For year ended 12/31/12 | \$ 380 |
| For year ended 12/31/13 | \$ 313 |

In accordance with the provisions of SFAS 142, the Company performed testing of goodwill for impairment as of September 30, 2007 and determined that, as of that date, goodwill was not impaired. Management also concluded that the remaining amounts and amortization periods were appropriate for all intangible assets.

Other Assets

The Company owns approximately \$3.7 million of Federal Home Loan Bank stock included in other assets. During the third quarter of 2007, the Federal Home Loan Bank of Chicago received a Cease and Desist Order from its regulator, the Federal Housing Finance Board. The Federal Home Loan Bank will continue to provide liquidity and funding through advances; however, the draft order prohibits capital stock repurchases and redemptions until a time to be determined by the Federal Housing Finance Board. The Board of Directors and management of the Federal Home Loan Bank of Chicago have recently announced it will no longer fund mortgage loan purchases through its MPF Program after July 31, 2008. With regard to dividends, the Federal Home Loan Bank continues to assess its dividend capacity each quarter and make appropriate request for approval. There were no dividends paid by the Federal Home Loan Bank of Chicago during the first quarter of 2008.

Repurchase Agreements and Other Borrowings

Securities sold under agreements to repurchase had seasonal declines of \$14 million during the first three months of 2008. Other borrowings decreased \$8 million during the three-month period ended March 31, 2008. This decrease was primarily due to a decrease of \$10 million in Federal Home Loan Bank advances partially offset by an increase in borrowing on our revolving credit line with The Northern Trust Company.

Fair Value of Assets and Liabilities

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards No. 157 (FAS 157), "Fair Value Measurements." FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 has been applied prospectively as of the beginning of the period.

FAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. FAS 157 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

In accordance with FAS 157, the Company groups its financial assets and financial liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock

1 Exchange. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from

2 third party pricing services for identical or comparable assets or liabilities which use observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level Unobservable inputs that are supported by little or no market activity and that are significant to the fair value

3 of the assets or liabilities.

Following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying balance sheet.

Available-for-Sale Securities

The fair value of available-for-sale securities are determined by various valuation methodologies. Where quoted market prices are available in an active market, securities are classified within Level 1. Level 1 securities include exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models or quoted prices of securities with similar characteristics. Level 2 securities include U.S. Treasury securities, obligations of U.S. government corporations and agencies, obligations of states and political subdivisions, mortgage-backed securities, collateralized mortgage obligations and corporate bonds. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy and include subordinated tranches of collateralized mortgage obligations and investments in financial institution trust preferred securities.

The following table presents the Company's assets that are measured at fair value on a recurring basis and the level within the FAS 157 hierarchy in which the fair value measurements fall as of March 31, 2008 (in thousands):

| | Fair Value | Fair Value Measurements Using | | |
|-------------------------------|------------|---|---|--|
| | | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Available-for-sale securities | \$ 169,783 | \$ 42 | \$ 161,282 | \$ 8,459 |

The change in fair value of assets measured using significant unobservable (Level 3) inputs on a recurring basis is summarized as follows (in thousands): :

| | Available-for-sale Securities |
|---|----------------------------------|
| Balance, December 31, 2007 | \$ 9,491 |
| Total realized and unrealized gains and losses: | |
| Included in net income | 1 |
| Included in other comprehensive income | (828) |
| Purchases, issuances and settlements | (205) |
| Transfers in and/or out of Level 3 | - |
| Balance, March 31, 2008 | \$ 8,459 |
| Total gains or losses for the period included in net income attributable to the change in unrealized gains or losses related to assets and liabilities still held at the reporting date | \$ - |

The Company may be required, from time to time, to measure certain other financial assets and liabilities at fair value on a nonrecurring basis. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis in the first

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three months of 2008 that were still held in the balance sheet at March 31, 2008, the following table provides the level of valuation assumptions used to determine each adjustment and the fair value of the assets at March 31, 2008 (in thousands).

| | Carrying value at March 31, 2008 | | | |
|----------------|----------------------------------|---|---|--|
| | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Impaired loans | \$ 4,190 | \$ - | \$ - | \$ 4,190 |

Impaired Loans

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment in accordance with the provisions of Financial Accounting Standard No. 114 (“FAS 114”) “Accounting by Creditors for Impairment of a Loan.” Allowable methods for estimating fair value include using the fair value of the collateral for collateral dependent loans or, where a loan is determined not to be collateral dependent, using the discounted cash flow method.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value based on First Mid’s loan review policy and procedures.

If the impaired loan is determined not to be collateral dependent, then the discounted cash flow method is used. This method requires the impaired loan to be recorded at the present value of expected future cash flows discounted at the loan’s effective interest rate. The effective interest rate of a loan is the contractual interest rate adjusted for any net deferred loan fees or costs, premiums, or discount existing at origination or acquisition of the loan.

Management establishes a specific reserve for loans that have an estimated fair value that is below the carrying value. Impaired loans for which the specific reserve was adjusted in accordance with FAS 114 during the first quarter of 2008 had a carrying amount of \$4.9 million with specific loss exposures of \$712,000, an increase of \$492,000 from December 31, 2007. The increase in specific loss exposures was the result of several loans added to substandard classifications which had impairments and management’s change in the discount factor used to value real estate collateral to more accurately reflect the Company’s experience in liquidating foreclosed real estate.

When there is little prospect of collecting either principal or interest, loans, or portions of loans, may be charged-off to the allowance for loan losses. Losses are recognized in the period an obligation becomes uncollectible. The recognition of a loss does not mean that the loan has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off the loan even though partial recovery may be effected in the future. During the first quarter of 2008, the Company charged-off \$113,000 of impaired loans to the allowance for loan losses

New Accounting Principles

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159 (FAS 159), “The Fair Value Option for Financial Assets and Financial Liabilities – Including amendment of FASB Statement No. 115.” FAS 159 allows companies to report selected financial assets and liabilities at fair value. The changes in fair value are recognized in earnings and the assets and liabilities measured under this methodology are required to be displayed separately in the balance sheet. The main intent of FAS 159 is to mitigate the difficulty in determining reported earnings caused by a “mixed-attribute model” (that is, reporting some assets at fair value and others using a different valuation method such as amortized cost). The project is separated into two phases. This first phase addresses the creation of a fair value option for financial assets and liabilities. A second phase will address creating a fair value option for selected non-financial items. FAS 159 is effective for all financial statements issued for fiscal years beginning after November 15, 2007. The Company has not elected the fair value option for any financial assets or liabilities at March 31, 2008.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis is intended to provide a better understanding of the consolidated financial condition and results of operations of the Company and its subsidiaries as of, and for the three month periods ended, March 31, 2008 and 2007. This discussion and analysis should be read in conjunction with the consolidated financial statements, related notes and selected financial data appearing elsewhere in this report.

Forward-Looking Statements

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), such as discussions of the Company's pricing and fee trends, credit quality and outlook, liquidity, new business results, expansion plans, anticipated expenses and planned schedules. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and is including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of the Company, are identified by use of the words "believe", "expect", "intend", "anticipate", "estimate", "project", or similar expressions. Actual results could differ materially from the results indicated by these statements because the realization of those results is subject to many risks and uncertainties including: changes in interest rates, general economic conditions, legislative/regulatory changes, monetary and fiscal policies of the U.S. government, including policies of the U.S. Treasury and the Federal Reserve Board, the quality or composition of the loan or investment portfolios, demand for loan products, deposit flows, competition, demand for financial services in the Company's market area and accounting principles, policies and guidelines. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Further information concerning the Company and its business, including a discussion of these and additional factors that could materially affect the Company's financial results, is included in the Company's 2007 Annual Report on Form 10-K under the headings "Item 1. Business" and "Item 1A. Risk Factors."

New Accounting Standards Adopted

The Company adopted the provisions of FAS 157 on January 1, 2008. The implementation of FAS 157 did not have a material impact on the Company's financial statements. FAS 157 has been applied prospectively as of the beginning of the period. See "Fair Value of Assets and Liabilities" in the notes to consolidated financial statements for more detailed information regarding the adoption of FAS 157.

Properties

On September 29, 2007, the Company closed its facilities located at 435 South Hamilton, Sullivan, Illinois in the IGA and at 220 North Highway Avenue, DeLand, Illinois. The customers and operations of both of these facilities were moved to other facilities in Sullivan and Monticello, Illinois. The Company did not expect the closing or moving of these facilities to have a material impact on its other operations.

During the first quarter of 2008, the Company obtained an independent appraisal of the DeLand property in anticipation of possibly donating or selling this property. Subsequently, the Company adjusted its carrying value of the property to the appraised value which resulted in a loss of \$132,000 in the consolidated financial statements.

Overview

This overview of management's discussion and analysis highlights selected information in this document and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources, and critical accounting estimates which have an impact on the Company's financial condition and results of operations you should carefully read this entire document.

Net income was \$2,922,000 and \$2,594,000 and diluted earnings per share was \$.46 and \$.40 for the three months ended March 31, 2008 and 2007, respectively. The following table shows the Company's annualized performance ratios for the three months ended March 31, 2008 and 2007, compared to the performance ratios for the year ended December 31, 2007:

| | Three months ended | | Year ended |
|----------------------------------|--------------------|-------------------|-------------------------|
| | March 31, 2008 | March 31, 2007 | December 31, 2007 |
| Return on average assets | 1.15% | 1.07% | 1.03% |
| Return on average equity | 14.16% | 13.53% | 13.06% |
| Average equity to average assets | 8.15% | 7.90% | 7.90% |

Total assets at March 31, 2008 and December 31, 2007 were \$1,021.2 million and \$1,016.3 million, respectively. The increase in net assets was primarily due to an increase in interest-bearing deposits and federal funds sold, offset by decreases in available-for-sale securities and net loans. Available-for-sale securities decreased by \$14.3 million during the first three months of 2008 due to securities that were called or matured and were not immediately replaced. Net loan balances were \$728 million at March 31, 2008, a decrease of \$12.1 million, or 1.6%, from \$740.1 million at December 31, 2007 due to seasonal pay downs on agricultural operating loans. Total deposit balances increased to \$795.7 million at March 31, 2008 from \$770.6 million at December 31, 2007 due to increased balances in certificates of deposit.

Net interest margin, defined as net interest income divided by average interest-earning assets, was 3.55% for the three months ended March 31, 2008, up from 3.41% for the same period in 2007. The increase in the net interest margin is attributable to a greater decrease in borrowing and deposit rates compared to the decrease in interest-earning asset rates. Net interest income before the provision for loan losses was \$8.5 million compared to net interest income of \$7.7 million for the same period in 2007. The increase was due to improvement in the net interest margin and growth in average earning assets of \$43.8 million for the three months ended March 31, 2008 compared to the same period in 2007.

Noninterest income increased \$.2 million or 3.6%, to \$4 million for the three months ended March 31, 2008 compared to \$3.8 million for the three months ended March 31, 2007. The increase in noninterest income was due to increases in fees received on overdrafts and fees on ATM and debit cards.

Noninterest expense increased 3.4%, or \$.3 million, to \$7.8 million for the three months ended March 31, 2008 compared to \$7.5 million during the same period in 2007. The increase in noninterest expense was due to the write down of the DeLand property and increases in loan collection expenses.

Following is a summary of the factors that contributed to the changes in net income (in thousands):

| | Change in Net Income 2008 vs. 2007 Three months ended March 31 |
|---|---|
| Net interest income | \$ 825 |
| Provision for loan losses | (5) |
| Other income, including securities transactions | 138 |
| Other expenses | (254) |
| Income taxes | (376) |
| Increase in net income | \$ 328 |

Credit quality is an area of importance to the Company. Total nonperforming loans were \$8.3 million at March 31, 2008, compared to \$4 million at March 31, 2007 and \$7.5 million at December 31, 2007. This increase was primarily due to insufficient cash flow on commercial real estate loans to one borrower which totaled \$2.9 million and on a residential construction loan to one borrower which totaled \$.7 million. The Company's provision for loan losses for the three months ended March 31, 2008 and 2007 was \$191,000 and \$186,000, respectively. At March 31, 2008, the composition of the loan portfolio remained similar to the same period last year. During the three months ended March 31, 2008, annualized net charge-offs were .03% of average loans compared to .02% for the same period in 2007. Loans secured by both commercial and residential real estate comprised 70% and 71% of the loan portfolio as of March 31, 2008 and 2007, respectively.

The Company owns approximately \$3.7 million of Federal Home Loan Bank stock included in other assets. During the third quarter of 2007, the Federal Home Loan Bank of Chicago received a Cease and Desist Order from their regulator, the Federal Housing Finance Board. The Federal Home Loan Bank will continue to provide liquidity and funding through advances; however, the draft order prohibits capital stock repurchases and redemptions until a time to be determined by the Federal Housing Finance Board. The Board of Directors and management of the Federal Home Loan Bank of Chicago have recently announced it will no longer fund mortgage loan purchases through its MPF Program after July 31, 2008. With regard to dividends, the Federal Home Loan Bank continues to assess its dividend capacity each quarter and make appropriate request for approval. There were no dividends paid by the Federal Home Loan Bank of Chicago during the first quarter of 2008.

The Company's capital position remains strong and the Company has consistently maintained regulatory capital ratios above the "well-capitalized" standards. The Company's Tier 1 capital to risk weighted assets ratio calculated under the regulatory risk-based capital requirements at March 31, 2008 and 2007 was 10.8% and 10.4%, respectively. The Company's total capital to risk weighted assets ratio calculated under the regulatory risk-based capital requirements at March 31, 2008 and 2007 was 11.6% and 11.2%, respectively.

The Company's liquidity position remains sufficient to fund operations and meet the requirements of borrowers, depositors, and creditors. The Company maintains various sources of liquidity to fund its cash needs. See discussion under the heading "Liquidity" for a full listing of sources and anticipated significant contractual obligations. The Company enters into financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include lines of credit, letters of credit and other

commitments to extend credit. The total outstanding commitments at March 31, 2008 and 2007 were \$167.1 million and \$149.3 million, respectively. This increase is primarily attributable to increases in commercial operating lines of credit.

Critical Accounting Policies

The Company has established various accounting policies that govern the application of U.S. generally accepted accounting principles in the preparation of the Company's financial statements. The significant accounting policies of the Company are described in the footnotes to the consolidated financial statements included in the Company's 2007 Annual Report on Form 10-K. Certain accounting policies involve significant judgments and assumptions by management that have a material impact on the carrying value of certain assets and liabilities; management considers such accounting policies to be critical accounting policies. The judgments and assumptions used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and assumptions made by management, actual results could differ from these judgments and assumptions, which could have a material impact on the carrying values of assets and liabilities and the results of operations of the Company.

The Company believes the allowance for loan losses is the critical accounting policy that requires the most significant judgments and assumptions used in the preparation of its consolidated financial statements. In estimating the allowance for loan losses, management utilizes historical experience, as well as other factors, including the effect of changes in the local real estate market on collateral values, the effect on the loan portfolio of current economic indicators and their probable impact on borrowers, and increases or decreases in nonperforming and impaired loans. Changes in these factors may cause management's estimate of the allowance for loan losses to increase or decrease and result in adjustments to the Company's provision for loan losses. See heading "Loan Quality and Allowance for Loan Losses" for a more detailed description of the Company's estimation process and methodology related to the allowance for loan losses.

Results of Operations

Net Interest Income

The largest source of revenue for the Company is net interest income. Net interest income represents the difference between total interest income earned on earning assets and total interest expense paid on interest-bearing liabilities. The amount of interest income is dependent upon many factors, including the volume and mix of earning assets, the general level of interest rates and the dynamics of changes in interest rates. The cost of funds necessary to support earning assets varies with the volume and mix of interest-bearing liabilities and the rates paid to attract and retain such funds. The Company's average balances, interest income and expense and rates earned or paid for major balance sheet categories are set forth in the following table (dollars in thousands):

| | Three months ended March 31, 2008 | | | Three months ended March 31, 2007 | | |
|---|--------------------------------------|----------|-----------------|--------------------------------------|----------|-----------------|
| | Average Balance | Interest | Average Rate | Average Balance | Interest | Average Rate |
| ASSETS | | | | | | |
| Interest-bearing deposits | \$ 21,660 | \$ 153 | 2.84% | \$ 321 | \$ 4 | 5.05% |
| Federal funds sold | 20,532 | 158 | 3.11% | 6,362 | 81 | 5.16% |
| Investment securities | | | | | | |
| Taxable | 152,715 | 1,938 | 5.07% | 169,948 | 2,103 | 4.95% |
| Tax-exempt (1) | 18,323 | 184 | 4.02% | 16,208 | 166 | 4.10% |
| Loans (2)(3) | 735,088 | 12,354 | 6.76% | 711,647 | 12,172 | 6.94% |
| Total earning assets | 948,318 | 14,787 | 6.25% | 904,486 | 14,526 | 6.51% |
| Cash and due from banks | 21,454 | | | 19,276 | | |
| Premises and equipment | 15,421 | | | 16,167 | | |
| Other assets | 33,703 | | | 36,630 | | |
| Allowance for loan losses | (6,212) | | | (5,962) | | |
| Total assets | \$ 1,012,684 | | | \$ 970,597 | | |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | | | | |
| Interest-bearing deposits | | | | | | |
| Demand deposits | \$ 287,772 | \$ 1,174 | 1.64% | \$ 261,649 | \$ 1,509 | 2.34% |
| Savings deposits | 59,004 | 85 | .58% | 61,612 | 83 | .55% |
| Time deposits | 322,184 | 3,591 | 4.48% | 332,812 | 3,698 | 4.51% |
| Securities sold under | | | | | | |
| agreements to repurchase | 57,342 | 368 | 2.58% | 50,601 | 577 | 4.62% |
| FHLB advances | 43,519 | 536 | 4.95% | 28,778 | 338 | 4.76% |
| Federal funds purchased | - | - | .00% | 3,345 | 45 | 5.46% |
| Junior subordinated debt | 20,620 | 366 | 7.14% | 20,620 | 395 | 7.77% |
| Other debt | 14,819 | 165 | 4.49% | 12,322 | 204 | 6.71% |
| Total interest-bearing liabilities | 805,260 | 6,285 | 3.14% | 771,739 | 6,849 | 3.60% |
| Non interest-bearing demand | | | | | | |
| deposits | 119,108 | | | 115,279 | | |
| Other liabilities | 5,790 | | | 6,887 | | |
| Stockholders' equity | 82,526 | | | 76,692 | | |
| Total liabilities & equity | \$ 1,012,684 | | | \$ 970,597 | | |
| Net interest income | | \$ 8,502 | | | \$ 7,677 | |
| Net interest spread | | | 3.11% | | | 2.91% |

| | | |
|---------------------------------------|-------|-------|
| Impact of non-interest bearing funds | .44% | .50% |
| Net yield on interest- earning assets | 3.55% | 3.41% |

(1) The tax-exempt income is not recorded on a tax equivalent basis.

(2) Nonaccrual loans have been included in the average balances.

(3) Includes loans held for sale.

Changes in net interest income may also be analyzed by segregating the volume and rate components of interest income and interest expense. The following table summarizes the approximate relative contribution of changes in average volume and interest rates to changes in net interest income for the three months ended March 31, 2008, compared to the same period in 2007 (in thousands):

| | For the three months ended March 31, 2008 compared to 2007 Increase / (Decrease) | | |
|---|--|------------|----------|
| | Total Change | Volume (1) | Rate (1) |
| Earning Assets: | | | |
| Interest-bearing deposits | \$ 149 | \$ 162 | \$ (13) |
| Federal funds sold | 77 | 289 | (212) |
| Investment securities: | | | |
| Taxable | (165) | (482) | 317 |
| Tax-exempt (2) | 18 | 21 | (3) |
| Loans (3) | 182 | 1,535 | (1,353) |
| Total interest income | 261 | 1,525 | (1,264) |
| Interest-Bearing Liabilities: | | | |
| Interest-bearing deposits | | | |
| Demand deposits | (335) | 833 | (1,168) |
| Savings deposits | 2 | (15) | 17 |
| Time deposits | (107) | (89) | (18) |
| Securities sold under agreements to repurchase | | | |
| FHLB advances | 198 | 184 | 14 |
| Federal funds purchased | (45) | (23) | (22) |
| Junior subordinated debt | (29) | - | (29) |
| Other debt | (39) | 193 | (232) |
| Total interest expense | (564) | 1,513 | (2,077) |
| Net interest income | \$ 825 | \$ 12 | \$ 813 |

(1) Changes attributable to the combined impact of volume and rate have been allocated proportionately to the change due to volume and the change due to rate.

(2) The tax-exempt income is not recorded on a tax-equivalent basis.

(3) Nonaccrual loans have been included in the average balances.

Net interest income increased \$.8 million, or 10.7%, to \$8.5 million for the three months ended March 31, 2008, from \$7.7 million for the same period in 2007. The increase in net interest income was due to improvement in the Company's net interest margin and growth in earning assets.

For the three months ended March 31, 2008, average earning assets increased by \$44 million, or 4.8%, and average interest-bearing liabilities increased \$33.5 million, or 4.3%, compared with average balances for the same period in 2007. The changes in average balances for these periods are shown below:

- Average interest-bearing deposits increased \$21.3 million or 6635.5%
- Average federal funds sold increased \$14.2 million or 223.2%

- Average loans increased by \$23.4 million or 3.3%.
 - Average securities decreased by \$15.1 million or 8.1%.
 - Average deposits increased by \$12.9 million or 2%.
 - Average securities sold under agreements to repurchase increased by \$6.7 million or 13.2%.
 - Average borrowings and other debt increased by \$13.9 million or 21.4%.
 - Net interest margin increased to 3.55% for the first three months of 2008 from 3.41% for the first three months of 2007.
-

To compare the tax-exempt yields on interest-earning assets to taxable yields, the Company also computes non-GAAP net interest income on a tax equivalent basis (TE) where the interest earned on tax-exempt securities is adjusted to an amount comparable to interest subject to normal income taxes assuming a federal tax rate of 34% (referred to as the tax equivalent adjustment). The net yield on interest-earning assets (TE) was 3.64% for the first three months of 2008 and 3.45% for the first three months of 2007. The TE adjustments to net interest income for March 31, 2008 and 2007 were \$94,000 and \$86,000, respectively.

Provision for Loan Losses

The provision for loan losses for the three months ended March 31, 2008 and 2007 was \$191,000 and \$186,000, respectively. Nonperforming loans were \$8.3 million and \$4.0 million as of March 31, 2008 and 2007, respectively. Net charge-offs were \$58,000 for the three months ended March 31, 2008 compared to \$31,000 during the same period in 2007. For information on loan loss experience and nonperforming loans, see discussion under the “Nonperforming Loans” and “Loan Quality and Allowance for Loan Losses” sections below.

Other Income

An important source of the Company’s revenue is derived from other income. The following table sets forth the major components of other income for the three months ended March 31, 2008 and 2007 (in thousands):

| | Three months ended March 31, | | |
|-----------------------|------------------------------|----------|-----------|
| | 2008 | 2007 | \$ Change |
| Trust | \$ 744 | \$ 717 | \$ 27 |
| Brokerage | 99 | 112 | (13) |
| Insurance commissions | 709 | 699 | 10 |
| Service charges | 1,321 | 1,270 | 51 |
| Security gains | 151 | 139 | 12 |
| Mortgage banking | 108 | 121 | (13) |
| Other | 838 | 774 | 64 |
| Total other income | \$ 3,970 | \$ 3,832 | \$ 138 |

Following are explanations of the changes in these other income categories for the three months ended March 31, 2008 compared to the same period in 2007:

- Trust revenues increased \$27,000 or 3.8% to \$744,000 from \$717,000. Trust assets, at market value, were \$446.9 million at March 31, 2008 compared to \$446.6 million at March 31, 2007.
- Revenues from brokerage decreased \$13,000 or 11.6% to \$99,000 from \$112,000 due to a reduction in commissions received from the sale of annuities.
- Insurance commissions increased \$10,000 or 1.4% to \$709,000 from \$699,000 due to the increase in commissions received on sales of business property and casualty insurance in the first quarter of 2008 compared to the same period in 2007.
- Fees from service charges increased \$51,000 or 4% to \$1,321,000 from \$1,270,000. This was primarily the result of an increase in the number of overdrafts during the first quarter of 2008 compared to the same period in 2007.

- The sale of securities during the three months ended March 31, 2008 resulted in net securities gains of \$151,000 compared to the three months ended March 31, 2007 which resulted in net securities gains of \$139,000.
- Mortgage banking income decreased \$13,000 or 10.7% to \$108,000 from \$121,000. This decrease was primarily due to a decrease in the volume of fixed rate loans originated and sold by First Mid Bank. Loans sold balances were as follows:
 - \$10.5 million (representing 80 loans) for the first quarter of 2008.
 - \$12.5 million (representing 101 loans) for the first quarter of 2007.

First Mid Bank generally releases the servicing rights on loans sold into the secondary market.

- Other income increased \$64,000 or 8.3% to \$838,000 from \$774,000. This increase was primarily due to increased ATM and debit card service fees.
-

Other Expense

The major categories of other expense include salaries and employee benefits, occupancy and equipment expenses and other operating expenses associated with day-to-day operations. The following table sets forth the major components of other expense for the three months ended March 31, 2008 and 2007 (in thousands):

| | Three months ended March 31, | | |
|-----------------------------|------------------------------|----------|-----------|
| | 2008 | 2007 | \$ Change |
| Salaries and benefits | \$ 4,124 | \$ 4,076 | \$ 48 |
| Occupancy and equipment | 1,235 | 1,217 | 18 |
| Amortization of intangibles | 191 | 217 | (26) |
| Stationery and supplies | 143 | 145 | (2) |
| Legal and professional fees | 479 | 474 | 5 |
| Marketing and promotion | 176 | 206 | (30) |
| Other operating expenses | 1,437 | 1,196 | 241 |
| Total other expense | \$ 7,785 | \$ 7,531 | \$ 254 |

Following are explanations for the changes in these other expense categories for the three months ended March 31, 2008 compared to the same period in 2007:

- Salaries and employee benefits, the largest component of other expense, increased \$48,000 or 1.2% to \$4,124,000 from \$4,076,000. This increase is primarily due to merit increases for continuing employees. There were 350 full-time equivalent employees at March 31, 2008 compared to 348 at March 31, 2007.
- Occupancy and equipment expense increased \$18,000 or 1.5% to \$1,235,000 from \$1,217,000.
- Expense for amortization of intangible assets decreased \$26,000 or 12% to \$191,000 from \$217,000 due to complete amortization of one core deposit intangible in July 2007.
- Other operating expenses increased \$241,000 or 20.2% to \$1,437,000 in 2008 from \$1,196,000 in 2007. This increase was due to the write down of property in DeLand, Illinois to its appraised value, losses on foreclosed real estate sales and product training for all personnel during the first quarter of 2008.
- All other categories of operating expenses decreased a net of \$27,000 or 3.3% to \$798,000 from \$825,000. The decrease was primarily due to decreases in marketing and promotion expenses.

Income Taxes

Total income tax expense amounted to \$1,574,000 (35% effective tax rate) for the three months ended March 31, 2008, compared to \$1,198,000 (31.6% effective tax rate) for the same period in 2007. The change in effective rate from 2007 to 2008 is primarily due to a \$142,000 reduction in the state tax expense accrual during 2007 as a result of amending the 2003 and 2002 state income tax returns for a greater deduction in enterprise zone interest. This resulted in a \$93,000 net reduction in tax expense for 2007 that did not occur in 2008.

The Company adopted the provisions of FASB Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes," on January 1, 2007. The implementation of FIN 48 did not impact the Company's financial statements.

The Company files U.S. federal and state of Illinois income tax returns. The Company is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2003.

Analysis of Balance Sheets

Loans

The loan portfolio (net of unearned interest) is the largest category of the Company's earning assets. The following table summarizes the composition of the loan portfolio, including loans held for sale, as of March 31, 2008 and December 31, 2007 (in thousands):

| | March 31, 2008 | December 31, 2007 |
|------------------------------|-------------------|-------------------------|
| Real estate – residential | \$ 139,050 | \$ 138,765 |
| Real estate – agricultural | 62,035 | 61,825 |
| Real estate – commercial | 318,686 | 317,302 |
| Total real estate – mortgage | 519,771 | 517,892 |
| Commercial and agricultural | 160,241 | 172,294 |
| Installment | 51,825 | 52,875 |
| Other | 6,004 | 5,100 |
| Total loans | \$ 737,841 | \$ 748,161 |

Overall loans decreased \$10.3 million, or 1.4%. The decrease was primarily a result of decreases in commercial and agricultural operating loans. Total real estate mortgage loans have averaged approximately 70% of the Company's total loan portfolio for the past several years. This is the result of the Company's focus on commercial real estate lending and long-term commitment to residential real estate lending. The balance of real estate loans held for sale amounted to \$3,612,000 and 1,974,000 as of March 31, 2008 and December 31, 2007, respectively.

At March 31, 2008, the Company had loan concentrations in agricultural industries of \$101 million, or 13.7%, of outstanding loans and \$114.2 million, or 15.3%, at December 31, 2007. In addition, the Company had loan concentrations in the following industries as of March 31, 2008 compared to December 31, 2007 (dollars in thousands):

| | March 31, 2008 | | December 31, 2007 | |
|--|----------------------|---------------------------|----------------------|---------------------------|
| | Principal balance | Outstanding loans % | Principal Balance | Outstanding loans % |
| Lessors of non-residential buildings | \$ 65,371 | 8.86% | \$ 68,322 | 9.13% |
| Lessors of residential buildings & dwellings | 49,496 | 6.71% | 49,517 | 6.62% |
| Hotels and motels | 35,569 | 4.82% | 30,841 | 4.12% |

The Company had no further loan concentrations in excess of 25% of total risk-based capital.

The following table presents the balance of loans outstanding as of March 31, 2008, by maturities (in thousands):

| | Maturity (1) | | | Total |
|--|-------------------------|------------------------------|-----------------|-------|
| | One year or less (2) | Over 1 through 5 years | Over 5 years | |
| | | | | |

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| | | | | |
|-------------------------------|------------|------------|-----------|------------|
| Real estate – residential | \$ 62,747 | \$ 58,885 | \$ 17,418 | \$ 139,050 |
| Real estate -- agricultural | 15,992 | 37,057 | 8,986 | 62,035 |
| Real estate – commercial | 160,649 | 143,510 | 14,527 | 318,686 |
| Total real estate -- mortgage | 239,388 | 239,452 | 40,931 | 519,771 |
| Commercial and agricultural | 113,140 | 42,181 | 4,920 | 160,241 |
| Installment | 23,452 | 28,129 | 244 | 51,825 |
| Other | 1,594 | 2,954 | 1,456 | 6,004 |
| Total loans | \$ 377,574 | \$ 312,716 | \$ 47,551 | \$ 737,841 |

(1) Based on scheduled principal repayments.

(2) Includes demand loans, past due loans and overdrafts.

As of March 31, 2008, loans with maturities over one year consisted of approximately \$315 million in fixed rate loans and \$46 million in variable rate loans. The loan maturities noted above are based on the contractual provisions of the individual loans. Rollovers and borrower requests are handled on a case-by-case basis.

Nonperforming Loans

Nonperforming loans are defined as: (a) loans accounted for on a nonaccrual basis; (b) accruing loans contractually past due ninety days or more as to interest or principal payments; and (c) loans not included in (a) and (b) above which are defined as "renegotiated loans". The Company's policy is to cease accrual of interest on all loans that become ninety days past due as to principal or interest. Nonaccrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal.

The following table presents information concerning the aggregate amount of nonperforming loans at March 31, 2008 and December 31, 2007 (in thousands):

| | March 31, 2008 | December 31, 2007 |
|---|-------------------|-------------------------|
| Nonaccrual loans | \$ 8,247 | \$ 7,460 |
| Renegotiated loans which are performing in accordance with revised terms | 19 | 21 |
| Total nonperforming loans | \$ 8,266 | \$ 7,481 |

The \$787,000 increase in nonaccrual loans during the three months ended March 31, 2008 resulted from the net of \$1,674,000 of additional loans put on nonaccrual status, \$637,000 of loans brought current or paid-off, \$135,000 of loans transferred to other real estate owned and \$115,000 of loans charged-off.

Interest income that would have been reported if nonaccrual and renegotiated loans had been performing totaled \$113,700 and \$70,600 for the three-month periods ended March 31, 2008 and 2007, respectively.

Loan Quality and Allowance for Loan Losses

The allowance for loan losses represents management's estimate of the reserve necessary to adequately account for probable losses attributable to current loan exposures. The provision for loan losses is the charge against current earnings that is determined by management as the amount needed to maintain an adequate allowance for loan losses. In determining the adequacy of the allowance for loan losses, and therefore the provision to be charged to current earnings, management relies predominantly on a disciplined credit review and approval process that extends to the full range of the Company's credit exposure. The review process is directed by overall lending policy and is intended to identify, at the earliest possible stage, borrowers who might be facing financial difficulty. Once identified, the magnitude of exposure to individual borrowers is quantified in the form of specific allocations of the allowance for loan losses. Management considers collateral values and guarantees in the determination of such specific allocations. Additional factors considered by management in evaluating the overall adequacy of the allowance include historical net loan losses, the level and composition of nonaccrual, past due and renegotiated loans, trends in volumes and terms of loans, effects of changes in risk selection and underwriting standards or lending practices, lending staff changes, concentrations of credit, industry conditions and the current economic conditions in the region

where the Company operates. Management considers the allowance for loan losses a critical accounting policy.

Management recognizes there are risk factors that are inherent in the Company's loan portfolio. All financial institutions face risk factors in their loan portfolios because risk exposure is a function of the business. The Company's operations (and therefore its loans) are concentrated in east central Illinois, an area where agriculture is the dominant industry. Accordingly, lending and other business relationships with agriculture-based businesses are critical to the Company's success. At March 31, 2008, the Company's loan portfolio included \$101 million of loans to borrowers whose businesses are directly related to agriculture. The balance decreased \$13.2 million from \$114.2 million at December 31, 2007. While the Company adheres to sound underwriting practices, including collateralization of loans, any extended period of low commodity prices, significantly reduced yields on crops and/or reduced levels of government assistance to the agricultural industry could result in an increase in the level of problem agriculture loans and potentially result in loan losses within the agricultural portfolio.

In addition, the Company has \$35.6 million of loans to motels, hotels and tourist courts. The performance of these loans is dependent on borrower specific issues as well as the general level of business and personal travel within the region. While the Company adheres to sound underwriting standards, a prolonged period of reduced business or personal travel could result in an increase in nonperforming loans to this business segment and potentially in loan losses. The Company also has \$65.4 million of loans to lessors of non-residential buildings and \$49.5 million of loans to lessors of residential buildings and dwellings. A significant widespread decline in real estate values could result in an increase in nonperforming loans to this segment and potentially in loan losses.

Analysis of the allowance for loan losses as of March 31, 2008 and 2007, and of changes in the allowance for the three-month periods ended March 31, 2008 and 2007, is as follows (dollars in thousands):

| | Three months ended March | |
|--|--------------------------|------------|
| | 2008 | 2007 |
| Average loans outstanding, net of unearned income | \$ 735,088 | \$ 711,647 |
| Allowance-beginning of period | 6,118 | \$ 5,876 |
| Charge-offs: | | |
| Real estate-mortgage | 33 | 4 |
| Commercial, financial & agricultural | 71 | 15 |
| Installment | 14 | 30 |
| Other | 36 | 34 |
| Total charge-offs | 154 | 83 |
| Recoveries: | | |
| Real estate-mortgage | 51 | 1 |
| Commercial, financial & agricultural | 3 | 2 |
| Installment | 8 | 13 |
| Other | 34 | 36 |
| Total recoveries | 96 | 52 |
| Net charge-offs (recoveries) | 58 | 31 |
| Provision for loan losses | 191 | 186 |
| Allowance-end of period | \$ 6,251 | \$ 6,031 |
| Ratio of annualized net charge-offs to average loans | .03% | .02% |
| Ratio of allowance for loan losses to loans outstanding (less unearned interest at end of period) | .85% | .85% |
| Ratio of allowance for loan losses to nonperforming loans | 75.6% | 150.3% |

The ratio of the allowance for loan losses to nonperforming loans is 75.6% as of March 31, 2008 compared to 150.3% as of March 31, 2007. The increase in total nonperforming loans is the primary factor in the decline in the ratio. The increase in nonperforming loans is primarily due to the addition of commercial real estate loans to one borrower that totaled \$2.9 million. The commercial real estate loans are secured by one commercial building that is partially leased, one commercial building under construction, one subdivision development, and four residential properties. Management recognized charge-offs of \$33,000 and \$200,000 on these loans during 2008 and 2007, respectively. Also a residential construction loan to one borrower which totaled \$.7 million was classified during the first quarter of 2008. Based upon market real estate comparable information, the Company estimates that the probable remaining collateral shortfall on these loans is not material and management believes that the overall estimate of the allowance for loan losses adequately accounts for probable losses attributable to current exposures.

The Company minimizes credit risk by adhering to sound underwriting and credit review policies. Management and the board of directors of the Company review these policies at least annually. Senior management is actively involved in business development efforts and the maintenance and monitoring of credit underwriting and approval. The loan review system and controls are designed to identify, monitor and address asset quality problems in an accurate and timely manner. On a quarterly basis, the board of directors and management review the status of problem loans and determine a best estimate of the allowance. In addition to internal policies and controls, regulatory authorities periodically review asset quality and the overall adequacy of the allowance for loan losses.

Securities

The Company's overall investment objectives are to insulate the investment portfolio from undue credit risk, maintain adequate liquidity, insulate capital against changes in market value and control excessive changes in earnings while optimizing investment performance. The types and maturities of securities purchased are primarily based on the Company's current and projected liquidity and interest rate sensitivity positions.

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The following table sets forth the amortized cost of the securities as of March 31, 2008 and December 31, 2007 (dollars in thousands):

| | March 31, 2008 | | December 31, 2007 | |
|--|----------------|------------------------|-------------------|------------------------|
| | Amortized Cost | Weighted Average Yield | Amortized Cost | Weighted Average Yield |
| U.S. Treasury securities and obligations of | | | | |
| U.S. government corporations and agencies | \$ 76,573 | 4.79% | \$ 106,175 | 4.82% |
| Obligations of states and political subdivisions | 19,745 | 4.09% | 17,820 | 4.15% |
| Mortgage-backed securities | 55,908 | 5.31% | 49,798 | 5.33% |
| Other securities | 15,625 | 5.84% | 9,622 | 6.30% |
| Total securities | \$ 167,851 | 4.98% | \$ 183,415 | 4.96% |

At March 31, 2008, the Company's investment portfolio showed a decrease of \$15.6 million from December 31, 2007 primarily due to U.S. Treasury and obligations of U.S. government corporations and agencies securities that matured and were not immediately replaced offset by additional purchases of mortgage-backed securities. The amortized cost, gross unrealized gains and losses and estimated fair values for available-for-sale and held-to-maturity securities by major security type at March 31, 2008 and December 31, 2007 were as follows (in thousands):

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Estimated Fair Value |
|--|----------------|------------------------|---------------------------|----------------------|
| March 31, 2008 | | | | |
| Available-for-sale: | | | | |
| U.S. Treasury securities and obligations | | | | |
| of U.S. government corporations & agencies | \$ 76,573 | \$ 2,184 | \$ (12) | \$ 78,745 |
| Obligations of states and political subdivisions | 18,702 | 314 | (47) | 18,969 |
| Mortgage-backed securities | 55,908 | 1,678 | - | 57,586 |
| Other securities | 15,625 | 7 | (1,149) | 14,483 |
| Total available-for-sale | \$ 166,808 | \$ 4,183 | \$ (1,208) | \$ 169,783 |
| Held-to-maturity: | | | | |
| Obligations of states and political subdivisions | \$ 1,043 | \$ 19 | \$ - | \$ 1,062 |
| December 31, 2007 | | | | |
| Available-for-sale: | | | | |
| U.S. Treasury securities and obligations | | | | |
| of U.S. government corporations & agencies | \$ 106,175 | \$ 1,496 | \$ (73) | \$ 107,598 |
| Obligations of states and political subdivisions | 16,642 | 182 | (15) | 16,809 |
| Mortgage-backed securities | 49,798 | 502 | (116) | 50,184 |
| Other securities | 9,622 | 222 | (402) | 9,442 |
| Total available-for-sale | \$ 182,237 | \$ 2,402 | \$ (606) | \$ 184,033 |
| Held-to-maturity: | | | | |
| Obligations of states and political subdivisions | \$ 1,178 | \$ 16 | \$ - | \$ 1,194 |

At March 31, 2008, there were two obligations of U.S. government agencies with a fair value of \$10,923,000 and an unrealized loss of \$6,091, in a continuous unrealized loss position for twelve months or more. At March 31, 2007, there were five obligations of states and political subdivisions with a fair value of \$1,590,000 and an unrealized loss of \$13,000, six mortgage-backed securities with a fair value of \$12,740,000 and an unrealized loss of \$273,000, and eleven obligations of U.S. government agencies with a fair value of \$56,801,000 and an unrealized loss of \$619,000, in a continuous unrealized loss position for twelve months or more. This position was due to short-term and intermediate rates increasing since the purchase of these securities resulting in the market value of the security being lower than book value. Management does not believe any individual unrealized loss as of March 31, 2008 or 2007 represents an other than temporary impairment.

The following table indicates the expected maturities of investment securities classified as available-for-sale and held-to-maturity, presented at amortized cost, at March 31, 2008 and the weighted average yield for each range of maturities. Mortgage-backed securities are included based on their weighted average life. All other securities are shown at their contractual maturity (dollars in thousands).

| | One year or less | After 1 through 5 years | After 5 through 10 years | After ten years | Total |
|---|---------------------|-------------------------------|--------------------------------|--------------------|-------------------|
| Available-for-sale: | | | | | |
| U.S. Treasury securities and obligations of | | | | | |
| U.S. government corporations and agencies | \$ 16,245 | \$ 10,173 | \$ 50,155 | \$ - | \$ 76,573 |
| Obligations of state and political subdivisions | 1,370 | 3,837 | 4,643 | 8,852 | 18,702 |
| Mortgage-backed securities | 1 | 30,911 | 24,996 | - | 55,908 |
| Other securities | - | 6,554 | 4,747 | 4,324 | 15,625 |
| Total investments | \$ 17,616 | \$ 51,475 | \$ 84,541 | \$ 13,176 | \$ 166,808 |
| Weighted average yield | 3.66% | 5.07% | 5.07% | 5.81% | 4.98% |
| Full tax-equivalent yield | 3.79% | 5.21% | 5.18% | 7.01% | 5.19% |
| Held-to-maturity: | | | | | |
| Obligations of state and political subdivisions | | | | | |
| | \$ 20 | \$ 431 | \$ 423 | \$ 169 | \$ 1,043 |
| Weighted average yield | 5.75% | 5.50% | 5.28% | 5.75% | 5.46% |
| Full tax-equivalent yield | 8.41% | 7.89% | 7.70% | 8.41% | 7.91% |

The weighted average yields are calculated on the basis of the amortized cost and effective yields weighted for the scheduled maturity of each security. Tax-equivalent yields have been calculated using a 34% tax rate. With the exception of obligations of the U.S. Treasury and other U.S. government agencies and corporations, there were no investment securities of any single issuer, the book value of which exceeded 10% of stockholders' equity at March 31, 2008.

Investment securities carried at approximately \$132,868,000 and \$163,872,000 at March 31, 2008 and December 31, 2007, respectively, were pledged to secure public deposits and repurchase agreements and for other purposes as permitted or required by law.

Deposits

Funding of the Company's earning assets is substantially provided by a combination of consumer, commercial and public fund deposits. The Company continues to focus its strategies and emphasis on retail core deposits, the major component of funding sources. The following table sets forth the average deposits and weighted average rates for the three months ended March 31, 2008 and for the year ended December 31, 2007 (dollars in thousands):

| | March 31, 2008 | | December 31, 2007 | |
|------------------------|-----------------|-----------------------|-------------------|-----------------------|
| | Average Balance | Weighted Average Rate | Average Balance | Weighted Average Rate |
| Demand deposits: | | | | |
| Non-interest-bearing | \$ 119,108 | - | \$ 114,393 | - |
| Interest-bearing | 287,772 | 1.64% | 271,117 | 1.98% |
| Savings | 59,004 | .59% | 60,654 | .58% |
| Time deposits | 322,184 | 4.48% | 325,397 | 4.54% |
| Total average deposits | \$ 788,068 | 2.48% | \$ 771,561 | 2.66% |

The following table sets forth the high and low month-end balances for the three months ended March 31, 2008 and for the year ended December 31, 2007 (in thousands):

| | March 31, 2008 | December 31, 2007 |
|---|-------------------|-------------------------|
| High month-end balances of total deposits | \$ 796,742 | \$ 784,597 |
| Low month-end balances of total deposits | 777,389 | 756,222 |

The following table sets forth the maturity of time deposits of \$100,000 or more at March 31, 2008 and December 31, 2007 (in thousands):

| | March 31, 2008 | December 31, 2007 |
|--------------------------|-------------------|-------------------------|
| 3 months or less | \$ 34,077 | \$ 17,883 |
| Over 3 through 6 months | 48,436 | 25,339 |
| Over 6 through 12 months | 13,449 | 47,160 |
| Over 12 months | 7,976 | 7,670 |
| Total | \$ 103,938 | \$ 98,052 |

During the first three months of 2008, the balance of time deposits of \$100,000 or more increased by approximately \$5.9 million. The increase in balances was primarily attributable to an increase in consumer time deposits.

Balances of time deposits of \$100,000 or more include time deposits maintained for public fund entities and consumer time deposits. The Company also maintained time deposits for the State of Illinois with balances of \$3.0 million as of March 31, 2008 and December 31, 2007. The State of Illinois deposits are subject to bid annually and could increase

or decrease in any given year.

Repurchase Agreements and Other Borrowings

Securities sold under agreements to repurchase are short-term obligations of First Mid Bank. First Mid Bank collateralizes these obligations with certain government securities that are direct obligations of the United States or one of its agencies. First Mid Bank offers these retail repurchase agreements as a cash management service to its corporate customers. Other borrowings consist of Federal Home Loan Bank (“FHLB”) advances, federal funds purchased and loans (short-term or long-term debt) that the Company has outstanding and junior subordinated debentures.

Information relating to securities sold under agreements to repurchase and other borrowings as of March 31, 2008 and December 31, 2007 is presented below (dollars in thousands):

| | March 31, 2008 | December 31, 2007 |
|--|-------------------|-------------------------|
| Securities sold under agreements to repurchase | \$ 54,251 | \$ 68,300 |
| Federal Home Loan Bank advances: | | |
| Fixed term – due in one year or less | 5,000 | 15,000 |
| Fixed term – due after one year | 37,750 | 37,750 |
| Debt: | | |
| Loans due after one year | 16,500 | 14,500 |
| Junior subordinated debentures | 20,620 | 20,620 |
| Total | \$ 134,121 | \$ 156,170 |
| Average interest rate at end of period | 3.67% | 3.96% |
| Maximum outstanding at any month-end | | |
| Federal funds purchased | \$ - | \$ 14,100 |
| Securities sold under agreements to repurchase | 59,137 | 68,300 |
| Federal Home Loan Bank advances: | | |
| Overnight | - | 7,000 |
| Fixed term – due in one year or less | 5,000 | 20,000 |
| Fixed term – due after one year | 37,750 | 37,750 |
| Debt: | | |
| Loans due after one year | 16,500 | 16,500 |
| Junior subordinated debentures | 20,620 | 20,620 |
| Averages for the period (YTD) | | |
| Federal funds purchased | \$ - | \$ 3,907 |
| Securities sold under agreements to repurchase | 57,342 | 54,962 |
| Federal Home Loan Bank advances: | | |
| Overnight | - | 58 |
| Fixed term – due in one year or less | 5,385 | 8,905 |
| Fixed term – due after one year | 38,135 | 25,950 |
| Debt: | | |
| Loans due after one year | 14,819 | 14,345 |
| Junior subordinated debentures | 20,620 | 20,620 |
| Total | \$ 136,301 | \$ 128,747 |
| Average interest rate during the period | 4.21% | 5.31% |

Securities sold under agreements to repurchase had seasonal declines of \$14 million during the first three months of 2008. FHLB advances decreased \$10 million during the three-month period ended March 31, 2008 due to an advance that matured and was not replaced given the Company's federal funds sold position.

FHLB advances represent borrowings by First Mid Bank to economically fund loan demand. At March 31, 2008 the fixed term advances consisted of \$42.75 million as follows:

- \$5 million advance at 5.03% with a 1-year maturity, due September 8, 2008
- \$5 million advance at 4.82% with a 2-year maturity, due September 8, 2009
 - \$5 million advance at 4.58% with a 5-year maturity, due March 22, 2010
 - \$2.5 million advance at 5.46% with a 3-year maturity, due June 12, 2010
- \$2.5 million advance at 5.12% with a 3-year maturity, due June 12, 2010, one year lockout, callable quarterly beginning June, 2008
 - \$3 million advance at 5.98% with a 10-year maturity, due March 1, 2011
- \$5 million advance at 4.82% with a 5-year maturity, due January 19, 2012, two year lockout, callable quarterly beginning January, 2009
- \$5 million advance at 4.69% with a 5-year maturity, due February 23, 2012, two year lockout, callable quarterly beginning February, 2009
 - \$4.75 million advance at 4.75% with a 5-year maturity, due December 24, 2012
- \$5 million advance at 4.58% with a 10-year maturity, due July 14, 2016, one year lockout, callable quarterly beginning July, 2007

At March 31, 2008, outstanding debt balances include \$16,500,000 on a revolving credit agreement with The Northern Trust Company. This loan was renegotiated on April 24, 2006 in conjunction with obtaining financing for the acquisition of Mansfield Bancorp, Inc. (“Mansfield”), and its wholly owned subsidiary, Peoples State Bank of Mansfield, in May 2006. The revolving credit agreement has a maximum available balance of \$22.5 million with a term of three years from the date of closing. The interest rate (3.52% as of March 31, 2008) is floating at 1.25% over the federal funds rate when the ratio of senior debt to Tier 1 capital is equal to or below 35% as of the end of the previous quarter and 1.50% over the federal funds rate when the ratio of senior debt to Tier 1 capital is above 35%. Currently senior debt to Tier 1 capital is below 35%. The loan is secured by the common stock of First Mid Bank and subject to a borrowing agreement containing requirements for the Company and First Mid Bank similar to those of the prior agreement including requirements for operating and capital ratios. The Company and its subsidiary bank were in compliance with the existing covenants at March 31, 2008 and 2007 and December 31, 2007.

On February 27, 2004, the Company completed the issuance and sale of \$10 million of floating rate trust preferred securities through First Mid-Illinois Statutory Trust I (“Trust I”), a statutory business trust and wholly-owned unconsolidated subsidiary of the Company, as part of a pooled offering. The Company established Trust I for the purpose of issuing the trust preferred securities. The \$10 million in proceeds from the trust preferred issuance and an additional \$310,000 for the Company’s investment in common equity of Trust I, a total of \$10,310 000, was invested in junior subordinated debentures of the Company. The underlying junior subordinated debentures issued by the Company to Trust I mature in 2034, bear interest at three-month London Interbank Offered Rate (“LIBOR”) plus 280 basis points (7.21% and 8.24% at March 31, 2008 and December 31, 2007, respectively), reset quarterly, and are callable, at the option of the Company, at par on or after April 7, 2009. The Company used the proceeds of the offering for general corporate purposes.

On April 26, 2006, the Company completed the issuance and sale of \$10 million of fixed/floating rate trust preferred securities through First Mid-Illinois Statutory Trust II (“Trust II”), a statutory business trust and wholly-owned unconsolidated subsidiary of the Company, as part of a pooled offering. The Company established Trust II for the purpose of issuing the trust preferred securities. The \$10 million in proceeds from the trust preferred issuance and an additional \$310,000 for the Company’s investment in common equity of Trust II, a total of \$10,310 000, was invested in junior subordinated debentures of the Company. The underlying junior subordinated debentures issued by the Company to Trust II mature in 2036, bear interest at a fixed rate of 6.98% (three-month LIBOR plus 160 basis points) paid quarterly and converts to floating rate (LIBOR plus 160 basis points) after June 15, 2011. The net proceeds to the

Company were used for general corporate purposes, including the Company's acquisition of Mansfield.

The trust preferred securities issued by Trust I and Trust II are included as Tier 1 capital of the Company for regulatory capital purposes. On March 1, 2005, the Federal Reserve Board adopted a final rule that allows the continued limited inclusion of trust preferred securities in the calculation of Tier 1 capital for regulatory purposes. The final rule provides a five-year transition period, ending September 30, 2009, for application of the revised quantitative limits. The Company does not expect the application of the revised quantitative limits to have a significant impact on its calculation of Tier 1 capital for regulatory purposes or its classification as well-capitalized.

Interest Rate Sensitivity

The Company seeks to maximize its net interest margin while maintaining an acceptable level of interest rate risk. Interest rate risk can be defined as the amount of forecasted net interest income that may be gained or lost due to changes in the interest rate environment, a variable over which management has no control. Interest rate risk, or sensitivity, arises when the maturity or repricing characteristics of interest-bearing assets differ significantly from the maturity or repricing characteristics of interest-bearing liabilities.

The Company monitors its interest rate sensitivity position to maintain a balance between rate sensitive assets and rate sensitive liabilities. This balance serves to limit the adverse effects of changes in interest rates. The Company's asset liability management committee (ALCO) oversees the interest rate sensitivity position and directs the overall allocation of funds.

In the banking industry, a traditional way to measure potential net interest income exposure to changes in interest rates is through a technique known as "static GAP" analysis which measures the cumulative differences between the amounts of assets and liabilities maturing or repricing at various intervals. By comparing the volumes of interest-bearing assets and liabilities that have contractual maturities and repricing points at various times in the future, management can gain insight into the amount of interest rate risk embedded in the balance sheet.

The following table sets forth the Company's interest rate repricing GAP for selected maturity periods at March 31, 2008 (dollars in thousands):

| | 1 year | 1-2 years | Rate Sensitive Within | | | Thereafter | Total | Fair Value |
|--|-------------------|-------------------|-----------------------|------------------|------------------|-------------------|-------------------|-------------------|
| | | | 2-3 years | 3-4 years | 4-5 years | | | |
| Interest-earning assets: | | | | | | | | |
| Federal funds sold and other interest-bearing deposits | \$ 41,905 | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 41,905 | \$ 41,905 |
| Taxable investment securities | 16,379 | 1,027 | 501 | - | 8,071 | 124,836 | 150,814 | 150,814 |
| Nontaxable investment securities | 1,541 | 942 | 1,346 | 1,190 | 708 | 14,285 | 20,012 | 20,031 |
| Loans | 411,267 | 133,638 | 98,003 | 44,972 | 23,118 | 26,843 | 737,841 | 749,318 |
| Total | \$ 471,092 | \$ 135,607 | \$ 99,850 | \$ 46,162 | \$ 31,897 | \$ 165,964 | \$ 950,572 | \$ 962,068 |
| Interest-bearing liabilities: | | | | | | | | |
| Savings and N.O.W. accounts | \$ 60,924 | \$ 10,440 | 10,896 | \$ 15,912 | \$ 16,451 | \$ 98,579 | \$ 213,202 | \$ 213,202 |
| Money market accounts | 121,407 | 990 | 1,017 | 1,320 | 1,347 | 7,120 | 133,201 | 133,201 |
| Other time deposits | 292,786 | 14,817 | 8,607 | 3,954 | 8,300 | 65 | 328,529 | 334,886 |
| Short-term borrowings/debt | 59,251 | - | - | - | - | - | 59,251 | 59,327 |
| Long-term borrowings/debt | - | 36,810 | 8,000 | 20,310 | 4,750 | 5,000 | 74,870 | 77,361 |
| Total | \$ 534,368 | \$ 63,057 | \$ 28,520 | \$ 41,496 | \$ 30,848 | \$ 110,764 | \$ 809,053 | \$ 817,977 |
| Rate sensitive assets - | \$ (63,276) | \$ 72,550 | \$ 71,330 | \$ 4,666 | \$ 1,049 | \$ 55,200 | \$ 141,519 | |

rate sensitive
liabilities

| | | | | | | |
|----------------|-------------|----------|-----------|-----------|-----------|------------|
| Cumulative GAP | \$ (63,276) | \$ 9,274 | \$ 80,604 | \$ 85,270 | \$ 86,319 | \$ 141,519 |
|----------------|-------------|----------|-----------|-----------|-----------|------------|

Cumulative
amounts as % of
total

rate sensitive

| | | | | | | |
|--------|-------|------|------|------|------|------|
| assets | -6.7% | 7.6% | 7.5% | 0.5% | 0.1% | 5.8% |
|--------|-------|------|------|------|------|------|

| | | | | | | |
|------------------|-------|------|------|------|------|-------|
| Cumulative Ratio | -6.7% | 1.0% | 8.5% | 9.0% | 9.1% | 14.9% |
|------------------|-------|------|------|------|------|-------|

The static GAP analysis shows that at March 31, 2008, the Company was liability sensitive, on a cumulative basis, through the twelve-month time horizon. This indicates that future increases in interest rates, if any, could have an adverse effect on net interest income. Conversely, future decreases in interest rates could have a positive effect on net interest income.

There are several ways the Company measures and manages the exposure to interest rate sensitivity, including static GAP analysis. The Company's ALCO also uses other financial models to project interest income under various rate scenarios and prepayment/extension assumptions consistent with First Mid Bank's historical experience and with known industry trends. ALCO meets at least monthly to review the Company's exposure to interest rate changes as indicated by the various techniques and to make necessary changes in the composition terms and/or rates of the assets and liabilities. Based on all information available, management does not believe that changes in interest rates, which might reasonably be expected to occur in the next twelve months, will have a material adverse effect on the Company's net interest income.

Capital Resources

At March 31, 2008, the Company's stockholders' equity had increased \$2,744,000, or 3.4%, to \$83,196,000 from \$80,452,000 as of December 31, 2007. During the first three months of 2008, net income contributed \$2,922,000 to equity before the payment of dividends to common stockholders. The change in market value of available-for-sale investment securities increased stockholders' equity by \$719,000, net of tax. Additional purchases of treasury stock (64,989 shares at an average cost of \$25.32 per share) decreased stockholders' equity by approximately \$1,645,000.

The Company is subject to various regulatory capital requirements administered by the federal banking agencies. Bank holding companies follow minimum regulatory requirements established by the Board of Governors of the Federal Reserve System ("Federal Reserve System"), and First Mid Bank follows similar minimum regulatory requirements established for national banks by the Office of the Comptroller of the Currency ("OCC"). Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary action by regulators that, if undertaken, could have a direct material effect on the Company's financial statements.

Quantitative measures established by each regulatory agency to ensure capital adequacy require the reporting institutions to maintain a minimum total risk-based capital ratio of 8%, a minimum Tier 1 risk-based capital ratio of 4% and a minimum leverage ratio of 3% for the most highly rated banks that do not expect significant growth. All other institutions are required to maintain a minimum leverage ratio of 4%. Management believes that, as of March 31, 2008 and December 31, 2007, the Company and First Mid Bank met all capital adequacy requirements.

As of March 31, 2008, both the Company and First Mid Bank had capital ratios above the required minimums for regulatory capital adequacy and that qualified them for treatment as well-capitalized under the regulatory framework for prompt corrective action. To be categorized as well-capitalized, total risk-based, Tier 1 risk-based and Tier 1 leverage ratios must be maintained as set forth in the following table (dollars in thousands).

| | Actual | | Required Minimum | | To Be Well-Capitalized Under Prompt Corrective Action Provisions | |
|---|-----------|--------|------------------|---------|--|---------|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| March 31, 2008 | | | | | | |
| Total Capital (to risk-weighted assets) | | | | | | |
| Company | \$ 86,133 | 11.64% | \$ 59,176 | > 8.00% | N/A | N/A |
| First Mid Bank | 95,815 | 13.05% | 58,756 | > 8.00% | \$ 73,445 | >10.00% |
| Tier 1 Capital (to risk-weighted assets) | | | | | | |
| Company | 79,882 | 10.80% | 29,588 | > 4.00% | N/A | N/A |
| First Mid Bank | 89,564 | 12.19% | 29,378 | > 4.00% | 44,067 | 6.00% |
| Tier 1 Capital (to average assets) | | | | | | |
| Company | 79,882 | 8.06% | 39,647 | > 4.00% | N/A | N/A |
| First Mid Bank | 89,564 | 9.08% | 39,448 | > 4.00% | 49,310 | 5.00% |
| December 31, 2007 | | | | | | |
| Total Capital (to risk-weighted assets) | | | | | | |
| Company | \$ 83,783 | 11.13% | \$ 60,228 | > 8.00% | N/A | N/A |
| First Mid Bank | 92,290 | 12.36 | 59,727 | > 8.00% | \$ 74,659 | >10.00% |
| Tier 1 Capital (to risk-weighted assets) | | | | | | |
| Company | 77,665 | 10.32 | 30,114 | > 4.00% | N/A | N/A |
| First Mid Bank | 86,172 | 11.54 | 29,864 | > 4.00% | 44,795 | 6.00% |
| Tier 1 Capital (to average assets) | | | | | | |
| Company | 77,665 | 7.89 | 39,389 | > 4.00% | N/A | N/A |
| First Mid Bank | 86,172 | 8.80 | 39,169 | > 4.00% | 48,961 | 5.00% |

These ratios allow the Company to operate without capital adequacy concerns.

Stock Plans

Participants may purchase Company stock under the following four plans of the Company: the Deferred Compensation Plan, the First Retirement and Savings Plan, the Dividend Reinvestment Plan, and the SI Plan. For more detailed information on these plans, refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

At the Annual Meeting of Stockholders held May 23, 2007, the stockholders approved the SI Plan. The SI Plan was implemented to succeed the Company's 1997 Stock Incentive Plan, which has a ten-year term that expires October 21, 2007. The SI Plan is intended to provide a means whereby directors, employees, consultants and advisors of the Company and its Subsidiaries may sustain a sense of proprietorship and personal involvement in the continued development and financial success of the Company and its Subsidiaries, thereby advancing the interests of the Company and its stockholders. Accordingly, directors and selected employees, consultants and advisors may be provided the opportunity to acquire shares of Common Stock of the Company on the terms and conditions established herein. A maximum of 300,000 shares may be issued under the SI Plan. During the fourth quarter of 2007, 32,000 shares were awarded under the plan. There were no shares awarded in the first quarter of 2008.

Stock Split

On June 29, 2007, the Company effected a three-for-two stock split in the form of a 50% stock dividend for all shareholders of record as of June 18, 2007. Accordingly, an entry was made for \$9,493,000 to increase the common stock account and decrease the retained earnings account. Par value remained at \$4 per share. All current and prior period share and per share amounts have been restated giving retroactive recognition to the stock split.

Stock Repurchase Program

Since August 5, 1998, the Board of Directors has approved repurchase programs pursuant to which the Company may repurchase a total of approximately \$44.2 million of the Company's common stock. The repurchase programs approved by the Board of Directors are as follows:

- On August 5, 1998, repurchases of up to 3%, or \$2 million, of the Company's common stock.
- In March 2000, repurchases up to an additional 5%, or \$4.2 million of the Company's common stock.
- In September 2001, repurchases of \$3 million of additional shares of the Company's common stock.
 - In August 2002, repurchases of \$5 million of additional shares of the Company's common stock.
- In September 2003, repurchases of \$10 million of additional shares of the Company's common stock.
- On April 27, 2004, repurchases of \$5 million of additional shares of the Company's common stock.
- On August 23, 2005, repurchases of \$5 million of additional shares of the Company's common stock.
- On August 22, 2006, repurchases of \$5 million of additional shares of the Company's common stock.
- On February 27, 2007, repurchases of \$5 million of additional shares of the Company's common stock.
- On November 13, 2007, repurchases of \$5 million of additional shares of the Company's common stock.

During the three-month period ending March 31, 2008, the Company repurchased 64,989 shares at a total cost of approximately \$1,646,000. Since 1998, the Company has repurchased a total of 2,416,635 shares at a total price of approximately \$45,029,000. As of March 31, 2008, the Company was authorized per all repurchase programs to purchase \$4,177,000 in additional shares.

Treasury Stock

On May 23, 2007, the Company retired 1,500,000 shares of its treasury stock (after adjustment for stock split), the cost of which was determined using the first-in, first-out method. Accordingly, an entry was made to decrease the treasury stock account for \$21,021,000, the common stock account for \$4,000,000 and the retained earnings account for \$17,021,000.

Liquidity

Liquidity represents the ability of the Company and its subsidiaries to meet all present and future financial obligations arising in the daily operations of the business. Financial obligations consist of the need for funds to meet extensions of credit, deposit withdrawals and debt servicing. The Company's liquidity management focuses on the ability to obtain funds economically through assets that may be converted into cash at minimal costs or through other sources. The Company's other sources of cash include overnight federal fund lines, Federal Home Loan Bank advances, deposits of the State of Illinois, the ability to borrow at the Federal Reserve Bank of Chicago, and the Company's operating line of credit with The Northern Trust Company. Details for the sources include:

- First Mid Bank has \$25 million available in overnight federal fund lines, including \$10 million from Harris Trust and Savings Bank of Chicago and \$15 million from The Northern Trust Company. Availability of the funds is subject to First Mid Bank meeting minimum regulatory capital requirements for total capital to risk-weighted assets and Tier 1 capital to total average assets. As of March 31, 2008, First Mid Bank met these regulatory requirements.
 - First Mid Bank can also borrow from the Federal Home Loan Bank as a source of liquidity. Availability of the funds is subject to the pledging of collateral to the Federal Home Loan Bank. Collateral that can be pledged includes one-to-four family residential real estate loans and securities. At March 31, 2008, the excess collateral at the FHLB would support approximately \$64.6 million of additional advances.
-

- First Mid Bank also receives deposits from the State of Illinois. The receipt of these funds is subject to competitive bid and requires collateral to be pledged at the time of placement.
- First Mid Bank is also a member of the Federal Reserve System and can borrow funds provided that sufficient collateral is pledged.
- In addition, as of March 31, 2008, the Company had a revolving credit agreement in the amount of \$22.5 million with The Northern Trust Company with an outstanding balance of \$16.5 million and \$6 million in available funds.

Management monitors its expected liquidity requirements carefully, focusing primarily on cash flows from:

- lending activities, including loan commitments, letters of credit and mortgage prepayment assumptions;
 - deposit activities, including seasonal demand of private and public funds;
- investing activities, including prepayments of mortgage-backed securities and call provisions on U.S. Treasury and government agency securities; and
 - operating activities, including scheduled debt repayments and dividends to stockholders.

The following table summarizes significant contractual obligations and other commitments at March 31, 2008 (in thousands):

| | Total | Less than 1 year | 1-3 years | 3-5 years | More than 5 years |
|-------------------------|------------|---------------------|-----------|-----------|----------------------|
| Time deposits | \$ 328,529 | \$ 292,444 | \$ 23,587 | \$ 12,433 | \$ 65 |
| Debt | 37,120 | - | 16,500 | - | 20,620 |
| Other borrowings | 97,001 | 76,751 | 15,500 | 4,750 | - |
| Operating leases | 3,165 | 463 | 854 | 685 | 1,163 |
| Supplemental retirement | 863 | 50 | 100 | 100 | 613 |
| | \$ 466,678 | \$ 369,708 | \$ 56,541 | \$ 17,968 | \$ 22,461 |

For the three-month period ended March 31, 2008, net cash of \$4.9 million, \$27.8 million and \$.9 million was provided from operating activities, investing activities and financing activities, respectively. In total, cash and cash equivalents increased by \$33.6 million since year-end 2007.

Off-Balance Sheet Arrangements

First Mid Bank enters into financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include lines of credit, letters of credit and other commitments to extend credit. Each of these instruments involves, to varying degrees, elements of credit, interest rate and liquidity risk in excess of the amounts recognized in the consolidated balance sheets. The Company uses the same credit policies and requires similar collateral in approving lines of credit and commitments and issuing letters of

credit as it does in making loans. The exposure to credit losses on financial instruments is represented by the contractual amount of these instruments. However, the Company does not anticipate any losses from these instruments.

The off-balance sheet financial instruments whose contract amounts represent credit risk at March 31, 2008 and December 31, 2007 were as follows (in thousands):

| | March 31, 2008 | December 31, 2007 |
|--|-------------------|-------------------------|
| Unused commitments and lines of credit: | | |
| Commercial real estate | \$ 43,636 | \$ 42,215 |
| Commercial operating | 64,472 | 60,468 |
| Home equity | 19,619 | 18,492 |
| Other | 34,373 | 26,552 |
| Total | \$ 162,100 | \$ 147,727 |
| Standby letters of credit | \$ 4,998 | \$ 4,996 |

Commitments to originate credit represent approved commercial, residential real estate and home equity loans that generally are expected to be funded within ninety days. Lines of credit are agreements by which the Company agrees to provide a borrowing accommodation up to a stated amount as long as there is no violation of any condition established in the loan agreement. Both commitments to originate credit and lines of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the lines and some commitments are expected to expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The increase in commercial real estate unused commitments and lines of credit are primarily due to seasonal increases in construction loan commitments and lines of credit.

Standby letters of credit are conditional commitments issued by the Company to guarantee the financial performance of customers to third parties. Standby letters of credit are primarily issued to facilitate trade or support borrowing arrangements and generally expire in one year or less. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending credit facilities to customers. The maximum amount of credit that would be extended under letters of credit is equal to the total off-balance sheet contract amount of such instrument.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There has been no material change in the market risk faced by the Company since December 31, 2007. For information regarding the Company's market risk, refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

ITEM 4. CONTROLS AND PROCEDURES

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's "disclosure controls and procedures" (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act), as of the end of the period covered by this report. Based on such evaluation, such officers have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures are effective in bringing to their attention on a timely basis material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic

filings under the Exchange Act. Further, there have been no changes in the Company's internal control over financial reporting during the last fiscal quarter that have materially affected or that are reasonably likely to affect materially the Company's internal control over financial reporting.

PART II

ITEM 1. LEGAL PROCEEDINGS

Since First Mid Bank acts as a depository of funds, it is named from time to time as a defendant in lawsuits (such as garnishment proceedings) involving claims as to the ownership of funds in particular accounts. Management believes that all such litigation as well as other pending legal proceedings in which the Company is involved constitute ordinary, routine litigation incidental to the business of the Company and that such litigation will not materially adversely affect the Company's consolidated financial condition.

ITEM 1A. RISK FACTORS

Various risks and uncertainties, some of which are difficult to predict and beyond the Company's control, could negatively impact the Company. As a financial institution, the Company is exposed to interest rate risk, liquidity risk, credit risk, operational risk, risks from economic or market conditions, and general business risks among others. Adverse experience with these or other risks could have a material impact on the Company's financial condition and results of operations, as well as the value of its common stock. There has been no material change to the risk factors described in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

ISSUER PURCHASES OF EQUITY SECURITIES

| Period | (a) Total Number of Shares Purchased | (b) Average Price Paid per Share | (c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | (d) Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs |
|---------------------------------------|---|---|--|--|
| January 1, 2008 -- January 31, 2008 | - | \$ - | - | \$ 5,823,000 |
| February 1, 2008 -- February 29, 2008 | 17,706 | \$ 25.25 | 17,706 | \$ 5,376,000 |
| March 1, 2008 -- March 31, 2008 | 47,283 | \$ 25.35 | 47,283 | \$ 4,177,000 |
| Total | 64,989 | \$ 25.32 | 64,989 | \$ 4,177,000 |

See heading "Stock Repurchase Program" for more information regarding stock purchases.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5.

OTHER INFORMATION

None.

ITEM 6.

EXHIBITS

The exhibits required by Item 601 of Regulation S-K and filed herewith are listed in the Exhibit Index that follows the Signature Page and that immediately precedes the exhibits filed.

SIGNATURES

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

FIRST MID-ILLINOIS BANCSHARES, INC.
(Registrant)

Date: May 7, 2008

/s/ William S. Rowland

William S. Rowland
President and Chief Executive Officer

/s/ Michael L. Taylor

Michael L. Taylor
Chief Financial Officer

Exhibit Index to Quarterly Report on Form 10-Q

| Exhibit Number | Description and Filing or Incorporation Reference |
|-------------------|--|
| 4.1 | The Registrant agrees to furnish to the Commission, upon request, a copy of each instrument with respect to issues of long-term debt involving a total amount which does not exceed 10% of the total assets of the Registrant and its subsidiaries on a consolidated basis |
| 11.1 | Statement re: Computation of Earnings Per Share (Filed herewith on page 8) |
| 31.1 | Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.1 | Certification pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002 |
| 32.2 | Certification pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002 |