S&T BANCORP INC
Form 10-Q
August 05, 2011
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2011

OR

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

For the transition period from To

Commission file number 000-12508

S&T BANCORP, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania	**25-1434426**
(State or other jurisdiction of	**(IRS Employer**
incorporation or organization)	**Identification No.)**
800 Philadelphia Street, Indiana, PA	**15701**
(Address of principal executive offices)	**(zip code)**

800-325-2265

(Registrant s telephone number, including area code)

Not Applicable

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

Large accelerated filer ¨	Accelerated filer x
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 Exchange Act). Yes ¨ No x

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

Common Stock, $2.50 Par Value - 28,081,091 shares as of July 31, 2011

Table of Contents

INDEX

S&T BANCORP, INC. AND SUBSIDIARIES

		Page No.
PART I. FINANCIAL INFORMATION		
Item 1.	Financial Statements	
	Consolidated Balance Sheets June 30, 2011 and December 31, 2010	3
	Consolidated Statements of Income Three and Six Months Ended June 30, 2011 and 2010	4
	Consolidated Statements of Changes in Shareholders Equity Six Months Ended June 30, 2011 and 2010	5
	Consolidated Statements of Cash Flows Six Months Ended June 30, 2011 and 2010	6
	Notes to Consolidated Financial Statements	7-28
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	29-44
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	45-46
Item 4.	Controls and Procedures	46
PART II. OTHER INFORMATION		
Item 1.	Legal Proceedings	47
Item 1A.	Risk Factors	47
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	
Item 3.	Defaults Upon Senior Securities	47
Item 4.	Removed and Reserved	47
Item 5.	Other Information	47
Item 6.	Exhibits	47
	Signatures	48

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)	000000000 **June 30, 2011 (Unaudited)**	000000000 **December 31, 2010 (Audited)**
ASSETS		
Cash and due from banks, including interest-bearing amounts of $114,985 and $61,260, respectively	$ 170,826	$ 108,196
Securities available-for-sale, at fair value	337,566	288,025
Federal Home Loan Bank stock, at cost	20,184	22,365
Loans held for sale	10,960	8,337
Portfolio loans, net of unearned income	3,191,877	3,355,590
Allowance for loan losses	(58,004)	(51,387)
Portfolio loans, net	3,133,873	3,304,203
Premises and equipment, net	39,434	39,954
Goodwill	165,273	165,273
Other intangibles, net	6,556	7,465
Bank owned life insurance	55,727	54,924
Other assets	117,891	115,597
Total Assets	**$ 4,058,290**	**$ 4,114,339**
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$ 801,504	$ 765,812
Interest-bearing demand	284,488	295,246
Money market	236,514	262,683
Savings	753,304	753,813
Certificates of deposit	1,178,173	1,239,970
Total Deposits	**3,253,983**	**3,317,524**
Securities sold under repurchase agreements	41,112	40,653
Long-term borrowings	32,759	29,365
Junior subordinated debt securities	90,619	90,619
Other liabilities	47,280	57,513
Total Liabilities	**3,465,753**	**3,535,674**
SHAREHOLDERS EQUITY		
Fixed Rate Cumulative Perpetual Preferred Stock, Series A, no par value $1,000 per share liquidation price 10,000,000 shares authorized in 2011 and 2010 108,676 shares issued and outstanding in 2011 and 2010	106,532	106,137
Common stock, $2.50 par value 50,000,000 shares authorized in 2011 and 2010 29,714,038 shares issued in 2011 and 2010 28,078,849 shares and 27,951,689 shares outstanding at June 30, 2011 and December 31, 2010, respectively	74,285	74,285

Additional paid-in capital	52,104	51,570
Retained earnings	408,868	401,734
Accumulated other comprehensive loss	(4,048)	(6,334)
Treasury stock (1,635,189 shares and 1,762,349 shares at June 30, 2011 and December 31, 2010, respectively, at cost)	(45,204)	(48,727)
Total Shareholders Equity	**592,537**	**578,665**
Total Liabilities and Shareholders Equity	**$ 4,058,290**	**$ 4,114,339**

See Notes to Consolidated Financial Statements

3

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(in thousands, except per share data)	Three Months Ended June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
INTEREST INCOME				
Loans, including fees	$ 38,968	$ 42,662	$ 78,617	$ 84,881
Investment securities:				
Taxable	2,078	2,061	3,890	4,238
Tax-exempt	555	725	1,153	1,521
Dividends	182	113	315	245
Total Interest Income	**41,783**	**45,561**	**83,975**	**90,885**
INTEREST EXPENSE				
Deposits	5,957	7,440	12,019	15,047
Short-term borrowings and securities sold under repurchase agreements	15	95	30	212
Long-term borrowings and junior subordinated debt securities	1,273	1,401	2,516	3,086
Total Interest Expense	**7,245**	**8,936**	**14,565**	**18,345**
NET INTEREST INCOME	**34,538**	**36,625**	**69,410**	**72,540**
Provision for loan losses	1,097	9,127	11,737	13,557
Net Interest Income After Provision for Loan Losses	**33,441**	**27,498**	**57,673**	**58,983**
NONINTEREST INCOME				
Service charges on deposit accounts	2,389	3,027	4,673	5,864
Insurance fees	2,181	1,964	4,313	4,332
Wealth management fees	2,144	1,916	4,194	3,900
Debit and credit card fees	2,077	2,283	4,089	3,664
Mortgage banking	246	166	871	577
Securities (losses) gains, net	(56)	103	(43)	257
Other	2,133	2,070	4,043	4,278
Total Noninterest Income	**11,114**	**11,529**	**22,140**	**22,872**
NONINTEREST EXPENSE				
Salaries and employee benefits	12,571	11,811	25,891	24,376
Occupancy, net	1,738	1,659	3,595	3,643
Data processing	1,681	1,451	3,185	3,054
Furniture and equipment	1,365	1,313	2,542	2,386
FDIC assessment	917	1,398	2,143	2,699
Other taxes	903	942	1,805	1,887
Joint venture amortization	849	709	1,589	1,337

Legal	751	989	1,217	3,204
Amortization of intangibles	446	496	909	1,019
Other	4,373	4,967	10,167	10,061
Total Noninterest Expense	**25,594**	**25,735**	**53,043**	**53,666**
Income Before Provision for Income Taxes	**18,961**	**13,292**	**26,770**	**28,189**
Provision for Income Taxes	4,051	3,888	5,565	7,481
Net Income	**14,910**	**9,404**	**21,205**	**20,708**
Preferred stock dividends and discount amortization	1,558	1,549	3,113	3,096
Net Income Available to Common Shareholders	**$ 13,352**	**$ 7,855**	**$ 18,092**	**$ 17,612**
Common earnings per share basic	$ 0.48	$ 0.28	$ 0.65	$ 0.63
Common earnings per share diluted	$ 0.48	$ 0.28	$ 0.65	$ 0.63
Dividends declared per common share	$ 0.15	$ 0.15	$ 0.30	$ 0.30
Average common shares outstanding basic	27,968	27,770	27,923	27,750
Average common shares outstanding diluted	27,984	27,797	27,941	27,780

See Notes to Consolidated Financial Statements

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

(Unaudited)

(in thousands, except per share data)	Comprehensive Income	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance at January 1, 2010		**$ 105,370**	**$ 74,285**	**$ 51,158**	**$ 383,118**	**$ (6,214)**	**$ (54,399)**	**$ 553,318**
Net income for six months ended June 30, 2010	$ 20,708				20,708			20,708
Other Comprehensive Income								
Change in unrealized gains on available-for-sale securities, net of tax of $1,000	1,858					1,858		1,858
Reclassification adjustment for gains on securities available-for-sale included in net income, net of tax of $90	(167)					(167)		(167)
Adjustment to funded status of employee benefit plans, net of tax of $162	301					301		301
Total Comprehensive Income	**$ 22,700**							
Preferred stock dividends and discount amortization		379			(3,096)			(2,717)
Cash dividends declared ($0.30 per share)					(8,332)			(8,332)
Treasury stock issued (73,203 shares)					(904)		2,025	1,121
Recognition of restricted stock compensation expense				213				213
Tax benefits from stock-based compensation				4				4
Forfeitures of nonstatutory stock options				(104)				(104)
Balance at June 30, 2010		**$ 105,749**	**$ 74,285**	**$ 51,271**	**$ 391,494**	**$ (4,222)**	**$ (52,374)**	**$ 566,203**
Balance at January 1, 2011		**$ 106,137**	**$ 74,285**	**$ 51,570**	**$ 401,734**	**$ (6,334)**	**$ (48,727)**	**$ 578,665**
Net income for six months ended June 30, 2011	$ 21,205				21,205			21,205
Other Comprehensive Income								
Change in unrealized gains on available-for-sale securities, net of tax of $1,069	1,986					1,986		1,986
Reclassification adjustment for losses on securities available-for-sale included in net income, net of tax of $15	28					28		28
Adjustment to funded status of employee benefit plans, net of tax of $147	272					272		272
Total Comprehensive Income	**$ 23,491**							
Preferred stock dividends and discount amortization		395			(3,113)			(2,718)
Cash dividends declared ($0.30 per share)					(8,401)			(8,401)

Treasury stock issued (128,697 shares)			(10)	(2,557)		3,559	992
Recognition of restricted stock compensation expense			534				534
Forfeitures of restricted stock (1,537 shares)			10			(36)	(26)
Balance at June 30, 2011	**$ 106,532**	**$ 74,285**	**$ 52,104**	**$ 408,868**	**$ (4,048)**	**$ (45,204)**	**$ 592,537**

See Notes to Consolidated Financial Statements

5

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)	**Six Months Ended June 30, 2011**	**2010**
OPERATING ACTIVITIES		
Net income	$ 21,205	$ 20,708
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	11,737	13,557
Provision for unfunded loan commitments	188	(671)
Depreciation and amortization	3,328	3,366
Net amortization (accretion) of discounts and premiums	580	391
Stock-based compensation expense	383	163
Securities losses (gains), net	43	(257)
Deferred income taxes	(1,366)	(2,670)
Tax benefits from stock-based compensation	0	(4)
Mortgage loans originated for sale	(43,733)	(41,468)
Proceeds from the sale of loans	41,660	43,704
Gain on the sale of loans, net	(550)	(293)
Net decrease in interest receivable	421	1,582
Net decrease in interest payable	(262)	(827)
Net decrease (increase) in other assets	6,631	(8,290)
Net (decrease) increase in other liabilities	(9,589)	10,689
Net Cash Provided by Operating Activities	**30,676**	**39,680**
INVESTING ACTIVITIES		
Proceeds from maturities, prepayments and calls of securities available-for-sale	30,480	79,331
Proceeds from sales of securities available-for-sale	70	2,369
Purchases of securities available-for-sale	(77,616)	(40,568)
Proceeds from the redemption of Federal Home Loan Bank stock	2,181	0
Net decrease (increase) in loans	148,263	(15,082)
Purchases of premises and equipment	(1,780)	(863)
Proceeds from the sale of premises and equipment	258	27
Net Cash Provided by Investing Activities	**101,856**	**25,214**
FINANCING ACTIVITIES		
Net decrease in core deposits	(1,744)	(26,901)
Net (decrease) increase in certificates of deposit	(61,858)	19,484
Net increase in short-term borrowings	0	450
Net increase (decrease) in securities sold under repurchase agreements	459	(439)
Proceeds from long-term borrowings	4,192	9,663
Repayments of long-term borrowings	(798)	(55,229)
Purchase of treasury shares	(26)	0
Sale of treasury shares	992	1,121
Cash dividends paid to preferred shareholder	(2,718)	(2,717)
Cash dividends paid to common shareholders	(8,401)	(8,332)
Tax benefits from stock-based compensation	0	4

Net Cash Used in Financing Activities	**(69,902)**	**(62,896)**
Net increase in cash and cash equivalents	62,630	1,998
Cash and cash equivalents at beginning of period	108,196	69,152
Cash and Cash Equivalents at End of Period	**$ 170,826**	**$ 71,150**
Supplemental Disclosures		
Loans transferred to held for sale	$ 8,753	$ 0
Transfers of other real estate owned and other repossessed assets	$ 6,124	$ 5,049
Interest paid	$ 14,827	$ 19,173
Income taxes paid	$ 6,100	$ 7,848

See Notes to Consolidated Financial Statements

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. BASIS OF PRESENTATION

Principals of Consolidation

The interim Consolidated Financial Statements include the accounts of S&T Bancorp, Inc. and subsidiaries (S&T) and its wholly owned subsidiaries. All significant intercompany transactions have been eliminated in consolidation. Investments of 20 percent to 50 percent of the outstanding common stock of investees are accounted for using the equity method of accounting.

Basis of Presentation

The accompanying unaudited interim Consolidated Financial Statements of S&T have been prepared in accordance with generally accepted accounting principles (GAAP) in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements and should be read in conjunction with our annual report on Form 10-K for the year ended December 31, 2010, filed with the SEC on March 16, 2011. In the opinion of management, the accompanying interim financial information reflects all adjustments, including normal recurring adjustments, necessary to present fairly S&T s financial position and results of operations for each of the interim periods presented. Results of operations for interim periods are not necessarily indicative of the results of operations that may be expected for a full year or any future period.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current year s presentation. These reclassifications did not have a material impact on S&T s consolidated financial condition or results of operations.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

Recently Adopted Accounting Standards Updates

When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts

In December 2010, the FASB issued ASU No. 2010-28, which reflects the decision reached in EITF Issue No. 10-A. This ASU modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that impairment may exist. The qualitative factors are consistent with the existing guidance and examples, which require that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. For public entities, this ASU was effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. The adoption of this ASU did not have a material impact on S&T s results of operations or financial position.

Recently Issued Accounting Standards Updates

Presentation of Comprehensive Income

In June 2011, the FASB issued ASU No. 2011-05, the provisions of which allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. Under both options, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. ASU 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders equity. ASU 2011-05 does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. ASU 2011-05 should be applied retrospectively and is effective for public companies for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this ASU is not expected to have a material impact on S&T s results of operations or financial position.

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued

Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs

In May 2011, the FASB issued ASU No. 2011-04, which represents the convergence of the FASB s and the IASB s guidance on fair value measurement. ASU 2011-04 reflects the common requirements under U.S. GAAP and IFRS for measuring fair value and for disclosing information about fair value measurements, including a consistent meaning for the term fair value. The new guidance does not extend the use of fair value but, rather, provides guidance about how fair value should be applied where it is already required or permitted under IFRS or U.S. GAAP. For U.S. GAAP, most of the changes are clarifications of existing guidance or wording changes to align with IFRS 13. A public company is required to apply the ASU prospectively for interim and annual periods beginning after December 15, 2011. Early adoption is not permitted for a public company. The adoption of this ASU is not expected to have a material impact on S&T s results of operations or financial position.

Reconsideration of Effective Control for Repurchase Agreements

In April 2011, the FASB issued ASU No. 2011-03, which is intended to improve financial reporting of repurchase agreements (repos) and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. When an entity enters into a typical repo arrangement, it transfers financial assets to a counterparty in exchange for cash with an agreement for the counterparty to return the same or equivalent financial assets for a fixed price in the future. Current guidance prescribes when an entity may or may not recognize a sale upon the transfer of financial assets subject to a repo agreement. That determination is based, in part, on whether the entity has maintained effective control over the transferred financial assets. This ASU improves the accounting for these transactions by removing from the assessment of effective control the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets and focuses the assessment on the transferor s contractual rights. This guidance is effective for the first interim or annual period beginning on or after December 15, 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. The adoption of this ASU is not expected to have a material impact on S&T s results of operations or financial position.

A Creditor s Determination of Whether a Restructuring Is a Troubled Debt Restructuring

In April 2011, the FASB issued ASU No. 2011-02, which amends the guidance for evaluating whether the restructuring of a receivable by a creditor is a troubled debt restructuring (TDR). In evaluating whether a restructuring constitutes a TDR both for purposes of recording an impairment loss and for disclosure purposes, a creditor must separately conclude that both of the following exist: (*a*) the restructuring constitutes a concession; and (*b*) the debtor is experiencing financial difficulties. For public companies, the new guidance is effective for interim and annual periods beginning on or after June 15, 2011, and applies retrospectively to restructurings occurring on or after the beginning of the fiscal year of adoption. However, an entity should apply prospectively changes in the method used to calculate impairment. At the same time a public entity adopts ASU 2011-02, it will be required to disclose the activity based information that was previously deferred by ASU No. 2011-01. Early adoption is permitted. The adoption of this ASU is not expected to have a material impact on S&T s results of operations or financial position.

Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20

In January 2011, the FASB issued ASU No. 2011-01, which temporarily delayed the effective date of the disclosures about troubled debt restructurings in ASU No. 2010-20 for public entities. The delay was intended to allow the FASB time to complete its deliberations on what constitutes a troubled debt restructuring. The deferral in ASU 2011-01 was effective January 19, 2011. Refer to the discussion of ASU No. 2011-02 above, which lifted the temporary delay and now requires disclosures about troubled debt restructurings at the same time ASU 2011-02 is adopted.

NOTE 2. CAPITAL PURCHASE PROGRAM

On January 16, 2009, S&T, as a participant in the U.S. Treasury Capital Purchase Program (CPP), issued to the U.S. Treasury 108,676 shares of its Series A Preferred Stock and a Warrant to purchase 517,012 shares of common stock at an exercise price of $31.53 per share, in exchange for proceeds of $108.7 million. The Series A Preferred Stock pays cumulative dividends at a rate of five percent per year for the first five years and thereafter at a rate of nine percent per year. The Warrant provides for the adjustment of the exercise price and the number of shares of S&T s common stock issuable upon exercise pursuant to customary anti-dilution provisions, such as upon stock splits or distributions of securities or other assets to holders of S&T s common stock and upon certain issuances of S&T s common stock at or below a specified price relative to the initial exercise price. The U.S. Treasury has agreed not to exercise voting power with respect to any shares of common stock issued upon exercise of the Warrant. The Warrant expires ten years from date of issuance.

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued

Under changes made to the CPP by the American Recovery and Reinvestment Act of 2009 (ARRA), S&T can redeem the Series A Preferred Stock, plus any accrued and unpaid dividends, subject to approval by banking regulatory agencies, at any time. If S&T only redeems part of the CPP investment, then it must pay a minimum of 25 percent of the issuance price, or $27.2 million. The consent of the U.S. Treasury will be required for S&T to increase its common stock dividend (above the dividend amount prior to S&T s participation in the CPP) or repurchase its common stock or other equity or capital securities, other than in connection with benefit plans consistent with past practice and certain other circumstances through January 16, 2012. The consent of the U.S. Treasury will not be required if S&T has redeemed the Series A Preferred Stock or the U.S. Treasury has transferred the Series A Preferred Stock to a third party. In addition, the Series A Preferred Stock issuance includes certain restrictions on executive compensation that could limit the tax deductibility of compensation S&T pays to executive management.

NOTE 3. FAIR VALUE MEASUREMENTS

S&T uses fair value measurements to record fair value adjustments to certain financial assets and liabilities and to determine fair value disclosures. Securities available-for-sale, trading assets and derivatives are recorded at fair value on a recurring basis. Additionally, from time to time, S&T may be required to record other assets at fair value on a nonrecurring basis, such as loans held for sale, impaired loans, other real estate owned (OREO), mortgage servicing rights (MSR) and certain other assets.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants at the measurement date. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities; it is not a forced transaction. In determining fair value, S&T uses various valuation approaches, including market, income and cost approaches. The fair value standard establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing an asset or liability, which are developed, based on market data obtained from sources independent of S&T. Unobservable inputs reflect S&T s estimate of assumptions that market participants would use in pricing an asset or liability, which are developed based on the best information available in the circumstances.

The fair value hierarchy gives the highest priority to unadjusted quoted market prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). The fair value hierarchy is broken down into three levels based on the reliability of inputs as follows:

Level 1: valuation is based upon unadjusted quoted market prices for identical instruments traded in active markets.

Level 2: valuation is based upon quoted market prices for similar instruments traded in active markets, quoted market prices for identical or similar instruments traded in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by market data.

Level 3: valuation is derived from other valuation methodologies including discounted cash flow models and similar techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in determining fair value.

A financial instrument s level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. S&T s policy is to recognize transfers between any of the fair value hierarchy levels at the end of the reporting period in which the transfer occurred.

The following is a description of the valuation methodologies that S&T uses for financial instruments recorded at fair value on either a recurring or nonrecurring basis:

Recurring Basis

Securities Available-for-Sale

Securities available-for-sale include both debt and equity securities.

S&T obtains estimated fair values for debt securities from a third-party pricing service, which utilizes several sources for valuing fixed-income securities. The market evaluation sources for debt securities include observable inputs rather than significant unobservable inputs and are classified as Level 2. The service provider utilizes evaluated pricing models that vary by asset class and include available trade, bid and other market information. Generally, the methodologies include broker quotes, proprietary models, vast descriptive terms and conditions databases, as well as extensive quality control programs.

Marketable equity securities that have an active, quotable market are classified in Level 1. Marketable equity securities that are quotable, but are thinly traded or inactive, are classified as Level 2 and securities that are not readily traded and do not have a quotable market are classified as Level 3.

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued

Trading Assets

S&T uses quoted market prices to determine the fair value of its trading assets. S&T s trading assets are held in a Rabbi Trust under a deferred compensation plan and are invested in two readily quoted mutual funds. Accordingly, these assets are classified as Level 1.

Derivative Financial Instruments

S&T calculates the fair value for derivatives using widely accepted valuation techniques including discounted cash flow analysis on the expected cash flows of each derivative. Each valuation considers the contractual terms of the derivative, including the period to maturity and uses observable market based inputs, such as interest rate curves and implied volatilities. Accordingly, derivatives are classified as Level 2.

S&T incorporates credit valuation adjustments into the valuation models to appropriately reflect both its own nonperformance risk and the respective counterparty s nonperformance risk in calculating fair value measurements. In adjusting the fair value of its derivative contracts for the effect of nonperformance risk, S&T has considered the impact of netting and any applicable credit enhancements and collateral postings.

Nonrecurring Basis

Loans Held for Sale

Loans held for sale consist of 1-4 family residential loans originated for sale in the secondary market and from time to time, certain loans transferred from the loan portfolio to loans held for sale, all of which are carried at the lower of cost or fair value. The fair value of 1-4 family residential loans is based on the price secondary markets are currently offering for similar loans using observable market data. The fair values of the loans transferred from the loan portfolio are based on the amounts offered for these loans in currently pending sales transactions. Loans held for sale carried at fair value are classified as Level 2.

Impaired Loans

Impaired loans are carried at the lower of carrying value or fair value. Fair value is determined as the recorded investment balance less any specific reserve. S&T establishes a specific reserve based on the following three impairment methods: 1) the present value of expected future cash flows discounted at the loan s effective interest rate, 2) the loan s observable market price or 3) the fair value of the collateral less estimated selling costs when the loan is collateral dependent. Collateral values are generally based upon appraisals from approved, independent state certified appraisers.

Appraisals may be discounted based on management s historical knowledge, changes in market conditions from the time of valuation or management s knowledge of the borrower and the borrower s business. Because not all valuation inputs are observable, impaired loans are classified as Level 2 or Level 3 based on the lowest level of input that is significant to the fair value measurement.

OREO and Other Repossessed Assets

OREO and other repossessed assets obtained in partial or total satisfaction of a loan are recorded at the lower of recorded investment in the loan or fair value less cost to sell. Subsequent to foreclosure, these assets are carried at the lower of the amount recorded at acquisition date or estimated fair value less cost to sell. Accordingly, it may be necessary to record nonrecurring fair value adjustments. Fair value, when recorded, is generally based upon appraisals by approved, independent state certified appraisers. OREO and other repossessed assets are classified as Level 2.

Mortgage Servicing Rights

The fair value of MSR is determined by calculating the present value of estimated future net servicing cash flows, considering expected mortgage loan prepayment rates, discount rates, servicing costs and other economic factors, which are determined based on current market conditions. The expected rate of mortgage loan prepayments is the most significant factor driving the value of MSR. As the valuation model includes significant unobservable inputs, MSR are classified as Level 3. If the carrying value of MSR exceeds fair value, they are considered impaired. As a result, they are carried at fair value and classified within Level 3 of the fair value hierarchy.

S&T BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued

Other Assets

In accordance with GAAP, S&T measures certain other assets at fair value on a nonrecurring basis. Fair value is based on the application of lower of cost or fair value accounting, or write downs of individual assets. Valuation methodologies used to measure fair value are consistent with overall principles of fair value accounting and consistent with those described above.

Financial Instruments

In addition to financial instruments recorded at fair value in S&T s financial statements, fair value accounting guidance requires disclosure of the fair value of all of an entity s assets and liabilities that are considered financial instruments. The majority of S&T s assets and liabilities are considered financial instruments as defined in the guidance. Many of these instruments lack an available trading market as characterized by a willing buyer and willing seller engaged in an exchange transaction. Also, it is S&T s general practice and intent to hold its financial instruments to maturity and to not engage in trading or sales activities. For fair value disclosure purposes, S&T substantially utilized the fair value measurement criteria as required and explained above. In cases where quoted fair values are not available, S&T uses present value methods to determine the fair value of its financial instruments.

Cash and Cash Equivalents and Other Short-Term Assets

The carrying amounts reported in the Consolidated Balance Sheets for cash and due from banks and interest-bearing deposits with banks approximates fair value.

Loans

The fair values of variable rate performing loans is based on carrying values adjusted for credit risk. The fair values of fixed rate performing loans is estimated using discounted cash flow analyses, utilizing interest rates currently being offered for loans with similar terms, adjusted for credit risk. The fair values of nonperforming loans is based on their carrying values less any specific reserve. The carrying amount of accrued interest approximates fair value.

Bank Owned Life Insurance

Fair value approximates net cash surrender value.

Deposits

The fair values disclosed for deposits without defined maturities (e.g., noninterest and interest-bearing demand, money market and savings accounts) are by definition equal to the amounts payable on demand. The carrying amounts for variable rate, fixed-term time deposits approximate their fair values. Estimated fair values for fixed rate and other time deposits are based on discounted cash flow analysis, using interest rates currently offered for time deposits with similar terms. The carrying amount of accrued interest approximates its estimated fair value.

Short-Term Borrowings

The carrying amounts of federal funds purchased, securities sold under repurchase agreements and other short-term borrowings approximate their fair values.

Long-Term Borrowings

The fair values disclosed for fixed-rate long-term borrowings are determined by discounting their contractual cash flows using current interest rates for long-term borrowings of similar remaining maturities. The carrying amounts of variable rate long-term borrowings approximate their fair values.

Junior Subordinated Debt Securities

For the variable rate junior subordinated debt securities that reprice quarterly, fair values are based on carrying values. For the $25.0 million junior subordinated debt issued with a fixed rate period of five years which then converts to a variable rate, fair valued is based on discounted cash flows at current interest rates during the fixed rate period.

Loan Commitments and Standby Letters of Credit

Off-balance sheet financial instruments consist of commitments to extend credit and letters of credit. Except for interest rate lock commitments, estimates of the fair value of these off-balance sheet items were not made because of the short-term nature of these arrangements and the credit standing of the counterparties.

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued

The following tables present assets and liabilities that are measured at fair value on a recurring basis by fair value hierarchy level at June 30, 2011 and December 31, 2010. There were no transfers between Level 1 and Level 2 during the periods presented.

	June 30, 2011			
(in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
ASSETS				
Securities available-for-sale:				
Obligations of U.S. government corporations and agencies	$ 0	$ 141,453	$ 0	$ 141,453
Collateralized mortgage obligations of U.S. government corporations and agencies	0	71,146	0	71,146
Mortgage-backed securities of U.S. government corporations and agencies	0	54,781	0	54,781
Obligations of states and political subdivisions	0	57,889	0	57,889
Marketable equity securities	2,940	7,688	1,669	12,297
Total securities available-for-sale	2,940	332,957	1,669	337,566
Trading securities held in a Rabbi Trust under a deferred compensation plan	2,005	0	0	2,005
Total securities	4,945	332,957	1,669	339,571
Derivative financial assets:				
Interest rate swaps	0	17,955	0	17,955
Interest rate lock commitments	0	237	0	237
Total Assets	**$ 4,945**	**$ 351,149**	**$ 1,669**	**$ 357,763**
LIABILITIES				
Derivative financial liabilities:				
Interest rate swaps	$ 0	$ 17,858	$ 0	$ 17,858
Forward sale contracts	0	13	0	13
Total Liabilities	**$ 0**	**$ 17,871**	**$ 0**	**$ 17,871**

Table of Contents

S&T BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS continued

(in thousands)	December 31, 2010 Level 1	Level 2	Level 3	Total
ASSETS				
Securities available-for-sale:				
Obligations of U.S. government corporations and agencies	$ 0	$ 125,675	$ 0	$ 125,675
Collateralized mortgage obligations of U.S. government corporations and agencies	0	41,491	0	41,491
Mortgage-backed securities of U.S. government corporations and agencies	0	43,991	0	43,991
Obligations of states and political subdivisions	0	65,772	0	65,772
Marketable equity securities	1,528	7,980	1,588	11,096
Total securities available-for-sale	1,528	284,909	1,588	288,025
Trading securities held in a Rabbi Trust under a deferred compensation plan	2,089	0	0	2,089
Total securities	3,617	284,909	1,588	290,114
Derivative financial assets:				
Interest rate swaps	0	17,518	0	17,518
Interest rate lock commitments	0	217	0	217
Forward sale contracts	0	412	0	412
Total Assets	**$ 3,617**	**$ 303,056**	**$ 1,588**	**$ 308,261**