S&T BANCORP INC
Form 10-K
February 25, 2013
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the fiscal year ended December 31, 2012

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 0-12508

S&T BANCORP, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania	**25-1434426**
(State or other jurisdiction of incorporation of organization)	(I.R.S. Employer Identification No.)
800 Philadelphia Street, Indiana, PA	**15701**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code (800) 325-2265

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, par value $2.50 per share	The NASDAQ Stock Market LLC (NASDAQ Global Select Market)

Securities registered pursuant to Section 12(g) of the Act: **None**

(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes ¨ No x

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (229.405 of this chapter) is not contained herein and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this form 10-K or any amendment to this form 10-K. ¨

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

Yes x No ¨

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

Large accelerated 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 Act).

Yes ¨ No x

The aggregate estimated fair value of the voting and non-voting common equity held by non-affiliates of the registrant as of June 30, 2012:

Common Stock, $2.50 par value $520,833,295

The number of shares outstanding of the issuer s classes of common stock as of January 31, 2013:

Common Stock, $2.50 par value 29,728,005 shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the proxy statement to be filed with the Securities and Exchange Commission for the annual shareholders meeting to be held May 20, 2013 are incorporated by reference into Part III.

Table of Contents

Part I		
Item 1.	Business	3
Item 1A.	Risk Factors	13
Item 1B.	Unresolved Staff Comments	19
Item 2.	Properties	19
Item 3.	Legal Proceedings	20
Item 4.	Mine Safety Disclosures	20
Part II		
Item 5.	Market for Registrant s Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities	21
Item 6.	Selected Financial Data	23
Item 7.	Management s Discussion and Analysis of Financial Condition and Results of Operations	24
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	61
Item 8.	Financial Statements and Supplementary Data	63
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosures	129
Item 9A.	Controls and Procedures	129
Item 9B.	Other Information	129
Part III		
Item 10.	Directors, Executive Officers and Corporate Governance	130
Item 11.	Executive Compensation	130
Item 12.	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	130
Item 13.	Certain Relationships and Related Transactions, and Director Independence	130
Item 14.	Principal Accountant Fees and Services	130
Part IV		
Item 15.	Exhibits and Financial Statement Schedules	131
	Signatures	134

Table of Contents

PART I

Item 1. BUSINESS

General

S&T Bancorp, Inc., or S&T, (also referred to below as we , us or our), including on a consolidated basis with our subsidiaries where appropriate, was incorporated on March 17, 1983 under the laws of the Commonwealth of Pennsylvania as a bank holding company and has three wholly owned subsidiaries, S&T Bank, 9th Street Holdings, Inc. and STBA Capital Trust I. We also own a one-half interest in Commonwealth Trust Credit Life Insurance Company, or CTCLIC. We are registered as a financial holding company with the Board of Governors of the Federal Reserve System, or the Federal Reserve Board, under the Bank Holding Company Act of 1956, as amended, or the BHCA. As of December 31, 2012, we had approximately $4.5 billion in assets, $3.4 billion in loans, $3.6 billion in deposits and $537.4 million in shareholder s equity.

S&T Bank is a full service bank with its Main Office at 800 Philadelphia Street, Indiana, Pennsylvania, providing services to its customers through offices located in Allegheny, Armstrong, Blair, Butler, Cambria, Clarion, Clearfield, Indiana, Jefferson, Washington and Westmoreland counties of Pennsylvania. S&T Bank deposits are insured by the Federal Deposit Insurance Corporation, or FDIC, to the maximum extent provided by law.

S&T Bank has three wholly owned operating subsidiaries: S&T Insurance Group, LLC, S&T Bancholdings, Inc. and Stewart Capital Advisors, LLC. S&T Insurance Group, LLC, through its subsidiaries, offers a variety of insurance products. S&T Bancholdings, Inc. is an investment company. Stewart Capital Advisors, LLC, is a registered investment advisor that manages private investment accounts for individuals and institutions and advises the Stewart Capital Mid Cap Fund.

We operate three reportable operating segments including Community Banking, Wealth Management and Insurance. Our Community Banking segment offers services which include accepting time and demand deposits, originating commercial and consumer loans, and providing letters of credit and credit card services. We believe that we have a relatively stable deposit base and no material amount of deposits is obtained from a single depositor or group of depositors (including federal, state and local governments). Our core deposit base remained stable in 2012.

The Wealth Management segment offers discount brokerage services, services as executor and trustee under wills and deeds, guardian and custodian of employee benefits and other trust and brokerage services, as well as a registered investment advisor that manages private investment accounts for individuals and institutions. Total Wealth Management assets under management and administration were approximately $1.7 billion at December 31, 2012.

The Insurance segment includes a full-service insurance agency offering commercial property and casualty insurance, group life and health coverage, employee benefit solutions and personal insurance lines.

Refer to the financial statements and Note 25 of this Form 10-K for further details pertaining to our operating segments.

Recent Developments

On March 9, 2012, we completed the acquisition and conversion of Mainline Bancorp, Inc., or Mainline, a bank holding company based in Ebensburg, Pennsylvania. Mainline had one subsidiary, Mainline National Bank, with eight branches and $129.5 million in loans and $206.0 million in deposits. The acquisition expanded our market share and footprint throughout Cambria and Blair counties of Western Pennsylvania.

The total acquisition cost of Mainline was $27.8 million.

On August 13, 2012, we completed the acquisition of Gateway Bank of Pennsylvania, a bank with $99.1 million in loans and $105.4 million in deposits, headquartered in McMurray, Pennsylvania. The total acquisition cost of Gateway Bank was $19.8 million. As of December 31, 2012, Gateway was operating as a separate wholly-owned subsidiary of S&T, with all transactions since the acquisition

Table of Contents

Item 1. BUSINESS continued

date consolidated in our financial statements. On February 8, 2013, Gateway Bank was merged into S&T Bank, and their two branches are now fully operational branches of S&T Bank.

In August 2012, we expanded our commercial lending footprint into Northeastern Ohio through the opening of a loan production office in Akron.

Employees

As of December 31, 2012, we had 1,027 full-time equivalent employees.

Access to United States Securities and Exchange Commission Filings

All of our reports filed electronically with the United States Securities and Exchange Commission, or the SEC, including this Annual Report on Form 10-K for the fiscal year ended December 31, 2012, or the Report, our prior annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and our annual proxy statements, as well as any amendments to those reports are accessible at no cost on our website at www.stbancorp.com under Financial Information, SEC Filings. These filings are also accessible on the SEC s website at www.sec.gov. You may read and copy any material we file with the SEC at the SEC s Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Our charters of the Audit Committee, the Compensation and Benefits Committee, the Nominating and Corporate Governance Committee, the Wealth Management Oversight Committee, Complaints Regarding Accounting, Internal Accounting Controls or Auditing Matters, or the Whistleblower Policy, the Code of Conduct for the CEO and CFO, the General Code of Conduct, the Shareholder Communications Policy, and S&T Excessive and Luxury Expenditure Policy are also available at www.stbancorp.com under Corporate Governance.

Supervision and Regulation

General

S&T and S&T Bank are each extensively regulated under federal and state law. The following describes certain aspects of that regulation and does not purport to be a complete description of all regulations that affect S&T and S&T Bank or all aspects of any regulation discussed here.

To the extent statutory or regulatory provisions are described, the description is qualified in its entirety by reference to the particular statutory or regulatory provisions. Proposals to change the laws and regulations governing the banking industry are frequently raised in Congress, in state legislatures and before the various bank regulatory agencies. The likelihood and timing of any changes and the impact such changes might have on S&T or S&T Bank is impossible to determine with any certainty.

Any change in applicable laws or regulations, or in the way such laws or regulations are interpreted by regulatory agencies or courts, may have a material impact on our business, operations and earnings.

S&T

We are a bank holding company subject to regulation under the BHCA and the examination and reporting requirements of the Federal Reserve Board. Under the BHCA, a bank holding company may not directly or indirectly acquire ownership or control of more than five percent of the voting shares or substantially all of the assets of any additional bank, or merge or consolidate with another bank holding company, without the prior approval of the Federal Reserve Board. We have received approval from the Federal Reserve Board for a passive ownership position in Allegheny Valley Bancorp, Inc. (14.4 percent).

As a bank holding company, we are expected under statutory and regulatory provisions to serve as a source of financial and managerial strength to our subsidiary bank. A bank holding company is also expected to commit resources, including capital and other funds, to support its subsidiary bank.

Table of Contents

Item 1. BUSINESS continued

We elected to become a financial holding company under the BHCA in 2001 and thereby engage in a broader range of financial and other activities than are permissible for traditional bank holding companies. In order to maintain our status as a financial holding company, we must remain well-capitalized and well-managed and the depository institutions controlled by us must remain well-capitalized, well-managed (as defined in federal law) and have at least a satisfactory Community Reinvestment Act, or CRA rating. Refer to Item 8, Note 23 Regulatory Matters, of this Report for information concerning the current capital ratios of S&T and S&T Bank. No prior regulatory approval is required for a financial holding company with total consolidated assets less than $50 billion to acquire a company, other than a bank or savings association, engaged in activities that are financial in nature or incidental to activities that are financial in nature, as determined by the Federal Reserve Board, unless the total consolidated assets to be acquired exceed $10 billion. The BHCA identifies several activities as financial in nature including, among others, securities underwriting, dealing and market making; sponsoring mutual funds and investment companies; insurance underwriting and sales agency; investment advisory activities; merchant banking activities; and activities that the Federal Reserve Board has determined to be closely related to banking or a proper incident thereto. Banks may also engage, subject to limitations on investment, in activities that are financial in nature, other than insurance underwriting, insurance company portfolio investment, real estate development and real estate investment, through a financial subsidiary of the bank, if the bank is well-capitalized, well-managed and has at least a satisfactory CRA rating.

If S&T or S&T Bank ceases to be well-capitalized or well-managed, we will not be in compliance with the requirements of the BHCA regarding financial holding companies. If a financial holding company is notified by the Federal Reserve Board of such a change in the ratings of any of its subsidiary banks, it must take certain corrective actions within specified time frames. Furthermore, if S&T Bank was to receive a CRA rating of less than satisfactory, then we would be prohibited from engaging in new activities or acquiring companies engaged in certain financial activities until the rating is raised to satisfactory or better.

We are presently engaged in nonbanking activities through the following five entities:

- 9th Street Holdings, Inc. was formed in June 1988 to hold and manage a group of investments previously owned by S&T Bank and to give us additional latitude to purchase other investments.
- S&T Bancholdings, Inc. was formed in August 2002 to hold and manage a group of investments previously owned by S&T Bank and to give us additional latitude to purchase other investments.
- CTCLIC is a joint venture with another financial institution, acting as a reinsurer of credit life, accident and health insurance policies sold by S&T Bank and the other institution.
- S&T Insurance Group, LLC distributes life insurance and long-term disability income insurance products. During 2001, S&T Insurance Group, LLC and Attorneys Abstract Company, Inc. entered into an agreement to form S&T Settlement Services, LLC or STSS, with respective ownership interests of 55 percent and 45 percent. STSS is a title insurance agency servicing commercial customers. During 2002, S&T Insurance Group, LLC expanded into the property and casualty insurance business with the acquisition of S&T-Evergreen Insurance LLC.
- Stewart Capital Advisors, LLC was formed in August 2005 and is a registered investment advisor that manages private investment accounts for individuals and institutions and advises the Stewart Capital Mid Cap Fund.

S&T Bank

As a state-chartered, commercial bank, the deposits of which are insured by the FDIC, S&T Bank is subject to the supervision and regulation of the Pennsylvania Department of Banking and

Table of Contents

Item 1. BUSINESS continued

Securities, or PADB and the FDIC. We are also subject to various requirements and restrictions under federal and state law, including requirements to maintain reserves against deposits, restrictions on the types, amount and terms and conditions of loans that may be granted and limits on the type of other activities in which S&T Bank may engage and the investments it may make.

In addition, S&T Bank is subject to affiliate transaction rules in Sections 23A and 23B of the Federal Reserve Act that limit the amount of transactions between itself and S&T or S&T s nonbank subsidiaries. Under these provisions, transactions between a bank and its parent company or any single nonbank affiliate generally are limited to 10 percent of the bank subsidiary s capital and surplus, and with respect to all transactions with affiliates, are limited to 20 percent of the bank subsidiary s capital and surplus. Loans and extensions of credit from a bank to an affiliate generally are required to be secured by eligible collateral in specified amounts. The Dodd-Frank Act Wall Street Reform and Consumer Protection Act, or Dodd-Frank Act, expands the affiliate transaction rules to broaden the definition of affiliate and to apply to securities lending, repurchase agreements and derivatives activities that we may have with an affiliate, as well as to strengthen collateral requirements and limit Federal Reserve exemptive authority. Also, the definition of extension of credit for transactions with executive officers, directors and principal shareholders is being expanded to include credit exposure arising from a derivative transaction, a repurchase or reverse repurchase agreement and a securities lending or borrowing transaction. These expansions became effective July 21, 2012. These provisions have not had a material effect on S&T or S&T Bank.

Insurance of Accounts; Depositor Preference

The deposits of S&T Bank are insured up to applicable limits per insured depositor by the FDIC. The Dodd-Frank Act codified FDIC deposit insurance coverage per separately insured depositor for all account types at $250,000. The Dodd-Frank Act also maintained federal deposit insurance coverage for noninterest-bearing transaction accounts at an unlimited amount from December 31, 2010 until this part of the Act expired on December 31, 2012. Deposits held in noninterest-bearing transaction accounts are now aggregated with any interest-bearing deposits the owner may hold in the same ownership category, and the combined total insured up to at least $250,000.

As an FDIC-insured bank, S&T Bank is also subject to FDIC insurance assessments, which are imposed based upon the risk the institution poses to the Deposit Insurance Fund, or DIF. Under this assessment system, risk is defined and measured using an institution s supervisory ratings with other risk measures, including financial ratios. The current total base assessment rates on an annualized basis range from 2.5 basis points for certain well-capitalized, well-managed banks, with the highest ratings, to 45 basis points for institutions posing the most risk to the DIF. The FDIC may raise or lower these assessment rates on a quarterly basis based on various factors to achieve a reserve ratio, which the Dodd-Frank Act has mandated to be no less than 1.35 percent of insured deposits.

In February 2011, the FDIC Board of Directors adopted a final rule, Deposit Insurance Assessment Base, Assessment Rate Adjustments, Dividends, Assessment Rates and Large Bank Pricing Methodology. This final rule redefined the deposit insurance assessment base to equal average consolidated total assets minus average tangible equity as required by the Dodd-Frank Act, altered assessment rates, implemented the Dodd-Frank Act s DIF dividend provisions and revised the risk-based assessment system for all large insured depository institutions (those with at least $10.0 billion in total assets). Many of the changes were made as a result of provisions of the Dodd-Frank Act that were intended to shift more of the cost of raising the reserve ratio from institutions with less than $10.0 billion in assets (such as S&T Bank) to the larger banks. Except for the future assessment rate schedules, all changes went into effect April 1, 2011 which lowered our FDIC expense in 2012 compared to 2011 and 2010. In addition to DIF assessments, the FDIC assesses all insured deposits a special assessment to fund the repayment of debt obligations of the Financing Corporation, or FICO. FICO is a government-sponsored entity that was formed to borrow the money necessary to carry out

Table of Contents

Item 1. BUSINESS continued

the closing and ultimate disposition of failed thrift institutions by the Resolution Trust Corporation in the 1990s. For the first quarter of 2013, the annualized rate established by the FDIC for the FICO assessment is 0.64 basis points.

Under federal law, deposits and certain claims for administrative expenses and employee compensation against insured depository institutions are afforded a priority over other general unsecured claims against such an institution, including federal funds and letters of credit, in the liquidation or other resolution of such an institution by a receiver. Such priority creditors would include the FDIC.

Capital

The Federal Reserve Board and FDIC have issued substantially similar risk-based and leverage capital guidelines applicable to banking organizations they supervise. Under current capital guidelines, S&T and S&T Bank are required to maintain certain capital standards based on ratios of capital to assets and capital to risk weighted assets. The guidelines define a bank s total qualifying capital as having two components. Tier 1 capital, which must be at least 50 percent of total qualifying capital, is mainly comprised of common equity, retained earnings and qualifying preferred stock, less certain intangibles. Tier 2 capital may include the allowance for loan losses, or ALL, up to a maximum of 1.25 percent of risk weighted assets, qualifying subordinated debt, qualifying preferred stock, hybrid capital instruments and up to 45 percent of net unrealized gains on available-for-sale equity securities. The guideline also defines the weights assigned to assets and off-balance sheet items to determine the risk weighted asset component of the risk-based capital ratios.

The Federal Reserve Board and FDIC have established minimum and well-capitalized standards for banks and bank holding companies. The minimum capital standards are defined as a Tier 1 ratio of at least 4.00 percent, a Total capital ratio of at least 8.00 percent and a Leverage ratio of at least 3.00 percent. The Leverage ratio of 3.00 percent is for those bank and bank holding companies that meet certain specified criteria, including having received the highest regulatory rating and are not experiencing significant growth or expansion. All other banks and bank holding companies generally are required to maintain a leverage ratio of at least 4 percent. S&T and S&T Bank maintain capital levels to meet the well-capitalized regulatory standards, which are defined as a Tier 1 ratio of at least 6.00 percent, Total capital ratio of at least 10.00 percent and a Leverage ratio of at least 5.00 percent. At December 31, 2012 S&T s Tier 1 capital, Total capital and Leverage ratios were 11.98 percent, 15.39 percent and 9.31 percent, respectively. S&T Bank s Tier 1, Total capital and Leverage ratios were 10.88 percent, 14.35 percent, and 8.45 percent, respectively.

Both the Federal Reserve Board and the FDIC s risk-based capital standards explicitly identify concentrations of credit risk and the risk arising from non-traditional activities, as well as an institution s ability to manage these risks, as important factors to be taken into account by the agency in assessing an institution s overall capital adequacy. The capital guidelines also provide that an institution s exposure to a decline in the economic value of its capital due to changes in interest rates be considered by the agency as a factor in evaluating a bank s capital adequacy. The Federal Reserve Board has also issued additional capital guidelines for certain bank holding companies that engage in trading activities. We do not believe that consideration of these additional factors will affect the regulators assessment of the capital position of S&T or S&T Bank. The Dodd-Frank Act contains a number of provisions intended to strengthen capital, including requiring minimum leverage and risk-based capital that are at least as stringent as those currently in effect. Also, the Dodd-Frank Act requires the Federal Reserve Board to implement capital regulations that are countercyclical so that the amount of capital required to be maintained by us would increase in times of economic expansion and decrease in times of economic contraction, consistent with the safety and soundness of the company. In addition to the Dodd-Frank Act, the international oversight body of the Basel Committee on Banking Supervision, or Basel III, reached agreements in July, 2010 to introduce a minimum

Item 1. BUSINESS continued

common equity tier 1 capital requirement of 4.50 percent, along with a capital conservation buffer of 2.50 percent to bring total common equity capital requirements to 7.00 percent. The federal banking agencies issued proposed rules in June 2012 to implement Basel III and certain other recent revisions to the Basel capital framework, as well as the minimum leverage and risk-based capital requirements of the Dodd Frank Act, but they have yet to issue any final rules. Federal regulators periodically propose amendments to the risk-based capital guidelines and the related regulatory framework and consider changes to the capital standards that could significantly increase the amount of capital needed to meet applicable standards. The timing of adoption, ultimate form and effect of any such proposed amendments cannot be predicted.

Capital Purchase Program

On December 7, 2011, we redeemed all of the preferred stock that we sold to the federal government as part of the Capital Purchase Program, or CPP. As a participant in the CPP, we completed the $108.7 million capital raise on January 16, 2009.

In connection with the issuance of the preferred stock to the U.S. Treasury in 2009, we also issued the U.S. Treasury a warrant to purchase 517,012 shares of our common stock at an initial per share exercise price of $31.53, with an estimated fair value of $4.0 million on the date of issuance. The warrant remains outstanding as of the date of the filing of this Annual Report on Form 10-K. The warrant provides for the adjustment of the exercise price and the number of shares of our common stock issuable upon exercise pursuant to customary anti-dilution provisions. The U.S. Treasury agreed not to exercise voting power with respect to any shares of common stock issued upon exercise of the warrant. We did not repurchase the warrant concurrently with the redemption of the preferred stock. Unless we repurchase the warrant, it will remain outstanding and will expire 10 years from the issuance date.

Payment of Dividends

S&T is a legal entity separate and distinct from its banking and other subsidiaries. A substantial portion of our revenues consist of dividend payments we receive from S&T Bank. S&T Bank, in turn, is subject to state laws and regulations that limit the amount of dividends it can pay to S&T. In addition, both S&T and S&T Bank are subject to various general regulatory policies relating to the payment of dividends, including requirements to maintain adequate capital above regulatory minimums. The Federal Reserve Board has indicated that banking organizations should generally pay dividends only if (i) the organization s net income available to common shareholders over the past year has been sufficient to fully fund the dividends and (ii) the prospective rate of earnings retention appears consistent with the organization s capital needs, asset quality and overall financial condition. Thus, under certain circumstances based upon our financial condition, our ability to declare and pay quarterly dividends may require consultation with the Federal Reserve Board and may be prohibited by applicable Federal Reserve Board regulations. If we were to pay a dividend in contravention of Federal Reserve regulations, the Federal Reserve could raise supervisory concerns. During the year ended December 31, 2012, S&T Bank paid $17.4 million in cash dividends to us for dividends paid to common shareholders.

Other Safety and Soundness Regulations

There are a number of obligations and restrictions imposed on bank holding companies such as us and our depository institution subsidiary by federal law and regulatory policy. These obligations and restrictions are designed to reduce potential loss exposure to the FDIC s deposit

insurance fund in the event an insured depository institution becomes in danger of default or is in default. Under current federal law for example, the federal banking agencies possess broad powers to take prompt corrective

Table of Contents

Item 1. BUSINESS continued

action to resolve problems of insured depository institutions. The extent of these powers depends upon whether the institution in question is well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized or critically undercapitalized, as defined by the law. Under regulations established by the federal banking agencies, a well-capitalized institution must have a Tier 1 capital ratio of at least 6.00 percent, a Total capital ratio of at least 10.00 percent and a leverage ratio of at least 5.00 percent and must not be subject to a capital directive or order. An adequately capitalized institution must have a Tier 1 capital ratio of at least 4.00 percent, a Total capital ratio of at least 8.00 percent and a leverage ratio of at least 4.00 percent. The most highly-rated financial institutions minimum requirement for the leverage ratio is 3.00 percent. In the proposed rules to implement Basel III and the minimum leverage and risk-based capital requirements of the Dodd-Frank Act, the federal banking agencies have also proposed changes to the definition of these categories, including the introduction of a common equity tier 1 capital ratio in each definition. As of December 31, 2012, S&T and S&T Bank were classified as well-capitalized. The classification of depository institutions is primarily for the purpose of applying the federal banking agencies prompt corrective action provisions and is not intended to be and should not be interpreted as a representation of overall financial condition or prospects of any financial institution.

The federal banking agencies prompt corrective action powers (which increase depending upon the degree to which an institution is undercapitalized) can include, among other things, requiring an insured depository institution to adopt a capital restoration plan which cannot be approved unless guaranteed by the institution s parent company; placing limits on asset growth and restrictions on activities, including restrictions on transactions with affiliates; restricting the interest rates the institution may pay on deposits; prohibiting the payment of principal or interest on subordinated debt; prohibiting the holding company from making capital distributions without prior regulatory approval; and, ultimately, appointing a receiver for the institution. For example, only a well-capitalized depository institution may accept brokered deposits without prior regulatory approval.

The federal banking agencies have also adopted guidelines prescribing safety and soundness standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth and compensation, fees and benefits. In general, the guidelines require appropriate systems and practices to identify and manage specified risks and exposures. The guidelines prohibit excessive compensation as an unsafe and unsound practice and characterize compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director or principal shareholder. In addition, the agencies have adopted regulations that authorize, but do not require an agency to order an institution that has been given notice by an agency that it is not in compliance with any of such safety and soundness standards to submit a compliance plan. If, after being so notified, an institution fails to submit an acceptable compliance plan, the agency must issue an order directing action to correct the deficiency and may issue an order directing other actions of the types to which an undercapitalized institution is subject under the prompt corrective action provisions described above.

Regulatory Enforcement Authority

The enforcement powers available to federal banking agencies are substantial and include, among other things and in addition to other powers described herein, the ability to assess civil money penalties, to issue cease-and-desist or removal orders and to initiate injunctive actions against banks and bank holding companies and institution affiliated parties, as defined in the Federal Deposit Insurance Act. In general, these enforcement actions may be initiated for violations of laws and regulations, as well as engagement in unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities.

Item 1. BUSINESS continued

At the state level, the PADB also has broad enforcement powers over S&T Bank, including the power to impose fines and other civil and criminal penalties and to appoint a conservator or receiver.

Interstate Banking and Branching

The BHCA currently permits bank holding companies from any state to acquire banks and bank holding companies located in any other state, subject to certain conditions, including certain nationwide and state-imposed deposit concentration limits. In addition, because of changes to law made by the Dodd-Frank Act, S&T Bank may now establish de novo interstate branches in any state to the same extent that a bank chartered in that state could establish a branch.

Community Reinvestment and Consumer Protection Laws

In connection with its lending activities, S&T Bank is subject to a number of federal laws designed to protect borrowers and promote lending to various sectors of the economy and population. These include, among other laws, the Equal Credit Opportunity Act, the Truth-in-Lending Act, the Home Mortgage Disclosure Act, the Real Estate Settlement Procedures Act, the Fair Credit Reporting Act and the CRA. In addition, rules developed by the federal banking agencies pursuant to federal law require disclosure of privacy policies to consumers and in some circumstances, allow consumers to prevent the disclosure of certain personal information to nonaffiliated third parties.

The CRA requires the appropriate federal banking agency, in connection with its examination of a bank, to assess the bank s record in meeting the credit needs of the communities served by the bank, including low and moderate-income neighborhoods. Furthermore, such assessment is required of any bank that has applied, among other things, to merge or consolidate with or acquire the assets or assume the liabilities of an insured depository institution, or to open or relocate a branch office. In the case of a bank holding company (including a financial holding company) applying for approval to acquire a bank or bank holding company, the Federal Reserve Board will assess the record of each subsidiary bank of the applicant bank holding company in considering the application. Under the CRA, institutions are assigned a rating of outstanding, satisfactory, needs to improve or unsatisfactory. S&T Bank was rated satisfactory in its most recent CRA evaluation.

Anti-Money Laundering Rules

S&T Bank is subject to the Bank Secrecy Act, its implementing regulations and other anti-money laundering laws and regulations, including the USA Patriot Act of 2001. Among other things, these laws and regulations require S&T Bank to take steps to prevent the bank from being used to facilitate the flow of illegal or illicit money, to report large currency transactions and to file suspicious activity reports. S&T Bank is also required to develop and implement a comprehensive anti-money laundering compliance program. Banks must also have in place appropriate know your customer policies and procedures. Violations of these requirements can result in substantial civil and criminal sanctions. In addition, provisions of the USA Patriot Act of 2001 require the federal financial institution regulatory agencies to consider the effectiveness of a financial institution s anti-money laundering activities when reviewing bank mergers and bank holding company acquisitions.

Government Actions and Legislation

The Dodd-Frank Act is significantly changing the current bank regulatory structure and affecting the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies, including S&T and S&T Bank. The Dodd-Frank Act contains a number of provisions intended to strengthen capital. Refer to Capital within Item 1 for additional information. For example, the federal banking agencies are directed to establish minimum leverage and risk-based capital that are at least as stringent as those currently in effect.

Item 1. BUSINESS continued

The Dodd-Frank Act requires various federal agencies to adopt a broad range of new rules and regulations, and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and consequently, many of the details and much of the impact of the Act may not be known for many years. The Dodd-Frank Act also contains provisions that expand the insurance assessment base and increase the scope of deposit insurance coverage.

Among other provisions, the SEC has enacted rules, required by the Dodd-Frank Act, giving stockholders a non-binding vote on executive compensation and so-called golden parachute payments. The Dodd-Frank Act also authorizes the SEC to promulgate rules that would allow stockholders to nominate their own candidates for election as directors using a company s proxy materials. The legislation also directs the federal financial institution regulatory agencies to promulgate rules prohibiting excessive compensation being paid to financial institution executives.

The Dodd-Frank Act also created the Consumer Financial Protection Bureau, or CFPB that took over rulemaking responsibility on July 21, 2011 for the principal federal consumer protection laws, such as the Truth in Lending Act, the Equal Credit Opportunity Act, the Real Estate Settlement Procedures Act and the Truth in Saving Act, among others. Institutions that have assets of $10.0 billion or less, such as S&T Bank, will continue to be supervised in this area by their state and primary federal regulators (in the case of S&T Bank, the FDIC). The Act also gives the CFPB expanded data collection powers for fair lending purposes for both small business and mortgage loans, as well as expanded authority to prevent unfair, deceptive and abusive practices. The consumer complaint function also has been consolidated into the CFPB with respect to the institutions it supervises. The CFPB established an Office for Community Banks and Credit Unions, with a mission to ensure that the CFPB incorporates the perspectives of small depository institutions into the policy-making process, communicate relevant policy initiatives to community banks and credit unions and work with community banks and credit unions to identify potential areas for regulatory simplification. In addition, the Dodd-Frank Act required the Federal Reserve Board to adopt a rule addressing interchange fees applicable to debit card transactions. This rule, Regulation II, effective October 1, 2011, does not apply to banks with less than $10.0 billion in assets.

There have been delays in the rulemaking processes of the various federal agencies responsible for enacting the provisions of the Dodd-Frank Act. A substantial number of rules required to implement the Dodd-Frank Act have not been finalized, and many have not even been proposed. Not all of the Dodd-Frank Act provisions remaining to be finalized apply to banks the size of S&T Bank. As a result, we cannot predict the ultimate impact of the Act on S&T or S&T Bank at this time, including the extent to which it could increase costs or limit our ability to pursue business opportunities in an efficient manner, or otherwise adversely affect our business, financial condition and results of operations. Nor can we predict the impact or substance of other future legislation or regulation. However, it is expected that they, at a minimum, will increase our operating and compliance costs.

In 2012, Pennsylvania enacted three bills known as the Banking Law Modernization Package. The bills became effective on December 24, 2012. The overall goal of the Banking Law Modernization Package was to modernize the banking laws of Pennsylvania and reduce regulatory burden at the state level.

Federal and state regulatory agencies consistently propose and adopt changes to their regulations or change the manner in which existing regulations are applied. We cannot predict the substance or impact of pending or future legislation or regulation, or the application thereof, although enactment of the proposed legislation could affect how S&T and S&T Bank operate and could significantly increase costs, impede the efficiency of internal business processes, or limit our ability to pursue business opportunities in an efficient manner, any of which could materially and adversely affect our business, financial condition and results of operations.

Table of Contents

Item 1. BUSINESS continued

Competition

S&T Bank competes with other local, regional and national financial service providers, such as other financial holding companies, commercial banks, savings associations, credit unions, finance companies and brokerage and insurance firms. Some of our competitors are not subject to the same level of regulation and oversight that is required of banks and bank holding companies, and are thus able to operate under lower cost structures.

Changes in bank regulation, such as changes in the products and services banks can offer and involvement in non-banking activities by bank holding companies, as well as bank mergers and acquisitions, can affect our ability to compete successfully. Legislation and regulations have also expanded the activities in which depository institutions may engage. Our ability to compete successfully will depend upon how successfully we can respond to the evolving competitive, regulatory, technological and demographic developments affecting our operations.

We face significant competition in both originating loans and attracting deposits. The western Pennsylvania area has a high density of financial institutions, some of which are significantly larger institutions with greater financial resources than us, and many of which are our competitors to varying degrees. Our competition for loans comes principally from commercial banks, savings associations, mortgage banking companies, credit unions and other financial service companies. Our most direct competition for deposits has historically come from commercial banks, savings banks and credit unions. We face additional competition for deposits from non-depository competitors such as the mutual fund industry, securities and brokerage firms and insurance companies. Because larger competitors have advantages in attracting business from larger corporations, we do not generally compete for that business. Instead, we concentrate our efforts on attracting the business of individuals and small and medium-size businesses. We generally compete on the basis of customer service and responsiveness to customer needs, the convenience of banking offices and hours, and the availability and pricing of our products and services. We emphasize personalized banking and the advantage of local decision-making in our banking business and this strategy appears to have been well received in our market area.

The financial service industry is likely to become more competitive as further technological advances enable more companies to provide financial services on a more efficient and convenient basis. Technological innovations have lowered traditional barriers of entry and enabled many of these companies to compete in financial services markets. Many customers now expect a choice of banking options for the delivery of services, including traditional banking offices, telephone, mail, internet, mobile banking, ATMs, self-service branches, and/or in-store branches. These products are offered by traditional banks and savings associations, as well as credit unions, brokerage firms, asset management groups, finance and insurance companies, internet-based companies, and mortgage banking firms. We believe that our current market area, consisting primarily of western Pennsylvania, provides long-term opportunity for growth in deposits and commercial lending. Commercial and residential real estate values in our market appear to have stabilized. Nevertheless, the national and local economies still remain fragile with high unemployment rates while business conditions remain subdued, with uncertainty that seems to limit both consumer and corporate spending in our area.

Table of Contents

Item 1A. RISK FACTORS

Investments in our common stock involve risk. The following discussion highlights the risks that we believe are material to our company, but does not necessarily include all risks that we may face.

The market price of our common stock may fluctuate significantly in response to a number of factors.

Our quarterly and annual operating results have varied significantly in the past and could vary significantly in the future, which makes it difficult for us to predict our future operating results. Our operating results may fluctuate due to a variety of factors, many of which are outside of our control, including the changing and recently volatile U.S. economic environment and changes in the commercial and residential real estate market, any of which may cause our stock price to fluctuate. If our operating results fall below the expectations of investors or securities analysts, the price of our common stock could decline substantially. Our stock price can fluctuate significantly in response to a variety of factors including, among other things:

- volatility of stock market prices and volumes in general;
- changes in market valuations of similar companies;
- changes in conditions in credit markets;
- changes in accounting policies or procedures as required by the Financial Accounting Standards Board, or FASB, or other regulatory agencies;
- legislative and regulatory actions (including the impact of the Dodd-Frank Act and related regulations) subjecting us to additional regulatory oversight which may result in increased compliance costs and/or require us to change our business model;
- government intervention in the U.S. financial system and the effects of and changes in trade and monetary and fiscal policies and laws, including the interest rate policies of the Federal Reserve Board;
- additions or departures of key members of management;
- fluctuations in our quarterly or annual operating results; and
- changes in analysts estimates of our financial performance.

Risks Related to Credit

Our ability to assess the credit-worthiness of our customers may diminish, which may adversely affect our results of operations.

We take credit risk by virtue of making loans and extending loan commitments and letters of credit. Our exposure to credit risk is managed through the use of consistent underwriting standards that emphasize in-market lending while avoiding highly leveraged transactions as well as excessive industry and other concentrations. Our credit administration function employs risk management techniques to ensure that loans adhere to corporate policy and problem loans are promptly identified. There can be no assurance that such measures will be effective in avoiding undue credit risk. If the models and approaches we use to select, manage and underwrite our consumer and commercial customers become less predictive of future charge-offs (due, for example, to rapid changes in the economy, including the unemployment rate), our credit losses may increase.

The value of the collateral used to secure our loans may not be sufficient to compensate for the amount of an unpaid loan and we may be unsuccessful in recovering the remaining balance from our customers.

Decreases in real estate values, particularly with respect to our commercial lending and mortgage activities, could adversely affect the value of property used as collateral for our loans and our customers ability to repay these loans, which in turn could impact our profitability. Repayment of our commercial loans is often dependent on the cash flow of the borrower, which may become

Table of Contents

Item 1A. RISK FACTORS continued

unpredictable in the current economy. If the value of the assets, such as real estate, serving as collateral for the loan portfolio were to decline materially, a significant part of the loan portfolio could become under-collateralized. If the loans that are secured by real estate become troubled when real estate market conditions are declining or have declined, in the event of foreclosure, we may not be able to realize the amount of collateral that was anticipated at the time of originating the loan. This could result in higher charge-offs which could have a material adverse effect on our operating results and financial condition.

Changes in the overall credit quality of our portfolio can have a significant impact on our earnings.

Like other lenders, we face the risk that our customers will not repay their loans. We reserve for losses in our loan portfolio based on our assessment of inherent credit losses. This process, which is critical to our financial results and condition, requires complex judgments, including our assessment of economic conditions, which are difficult to predict. Through a periodic review of the loan portfolio, management determines the amount of the allowance for loan loss, or ALL, by considering historical losses combined with qualitative factors including general and regional economic conditions, asset quality trends, loan policy and underwriting and changes in loan concentrations and collateral values. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates, which may be beyond our control. We may underestimate our inherent losses and fail to hold an ALL sufficient to account for these losses. Incorrect assumptions could lead to material underestimates of inherent losses and inadequate ALL. As our assessment of inherent losses changes, we may need to increase or decrease our ALL, which could adversely impact our financial results and profitability.

Our loan portfolio is concentrated in western Pennsylvania, and our lack of geographic diversification increases our risk profile.

The regional economic conditions in western Pennsylvania affects the demand for our products and services as well as the ability of our customers to repay their loans and the value of the collateral securing these loans. We are less able than a larger institution to spread the risks of unfavorable local economic conditions across a large number of diversified economies. A significant decline in the regional economy caused by inflation, recession, unemployment or other factors could adversely affect our customers, the quality of our loan portfolio and the demand for our products and services. Any sustained period of increased payment delinquencies, foreclosures or losses caused by adverse market or economic conditions in our market area could adversely affect the value of our assets, revenues, results of operations and financial condition. Moreover, we cannot give any assurance we will benefit from any market growth or favorable economic conditions in our primary market area.

A significant portion of our loan portfolio includes commercial real estate loans that have higher risks, and we may experience higher credit losses.

The majority of our loans are to commercial borrowers. The commercial real estate segment of our loan portfolio has been more adversely impacted by the continuing economic downturn. Commercial real estate lending typically involves higher loan principal amounts, and the repayment of these loans generally are dependent, in large part, on sufficient income from the properties securing the loans to cover operating expenses and debt service. Because payments on loans secured by commercial real estate often depend upon the successful operating and management of the properties, repayment of these loans may be affected by factors outside the borrower s control, including adverse conditions in the real estate market or the economy. Additionally, we have a number of significant credit exposures to commercial borrowers, and while the majority of these borrowers have numerous projects that

make up the total aggregate exposure, if one or more of these borrowers default or have financial difficulties, we could experience higher credit losses, which could adversely impact our results of operations.

Risks Related to Our Operations

An interruption or breach in security of our information systems may result in financial losses or in a loss of customers.

We depend upon data processing, communication and information exchange on a variety of computing platforms and networks, including the internet. We have experienced cybersecurity incidents in the past, which we did not deem material, and may experience them in the future. We believe that we have implemented appropriate measures to mitigate potential risks to our technology and our operations from these information technology disruptions. However, we cannot be certain that all of our systems are entirely free from vulnerability to attack, despite safeguards we have instituted. The occurrence of any failures, interruptions or security breaches of our information systems could result in a material adverse impact to our business, financial condition and results of operations through damage to our reputation, loss of customer business, additional regulatory scrutiny or exposure to civil litigation and possible financial liability. Losses arising from such a breach could materially exceed the amount of insurance coverage we have, which could adversely affect our results of operation.

We rely on third-party providers and other suppliers for a number of services that are important to our business. An interruption or cessation of an important service by any third party could have a material adverse effect on our business.

We are dependent for the majority of our technology, including our core operating system, on third party providers. If these companies were to discontinue providing services to us, we may experience significant disruption to our business. If any of our third party service providers experience financial, operational or technological difficulties, or if there is any other disruption in our relationships with them, we may be required to locate alternative sources of such services. Assurance cannot be provided that we could negotiate terms with alternative service sources that are as favorable or could obtain services with similar functionality as found in existing systems without the need to expend substantial resources, if at all, thereby resulting in a material adverse impact on our business and results of operations.

Risks Related to Interest Rates and Investments

Our net interest income could be negatively affected by interest rate changes or by significant loan prepayments, which may adversely affect our financial condition.

Our results of operations are largely dependent on net interest income, which is the difference between the interest and fees earned on interest-earning assets and the interest paid on interest-bearing liabilities. There may be mismatches between the maturity and repricing of our

assets and liabilities that could cause the net interest rate spread to compress, depending on the level and type of changes in the interest rate environment. Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions and the policies of various governmental agencies. In addition, some of our customers often have the ability to prepay loans or redeem deposits with either no penalties, or penalties that are insufficient to compensate us for the lost income. If customers continue to prepay loans at a higher rate, we may not be able to recover the lost revenues, which may affect our results of operations. A significant reduction in our net interest income will adversely affect our business and results of operations. If we are unable to manage interest rate risk effectively, our business, financial condition and results of operations could be materially harmed.

Table of Contents

Item 1A. RISK FACTORS continued

Declines in the value of investment securities held by us could require write-downs, which would reduce our earnings.

In order to diversify earnings and enhance liquidity, we own both debt and equity instruments of government agencies, municipalities and other companies. We may be required to record impairment charges on our investment securities if they suffer a decline in value that is considered other-than-temporary. Additionally, the value of these investments may fluctuate depending on the interest rate environment, general economic conditions and circumstances specific to the issuer. Volatile market conditions may detrimentally affect the value of these securities, such as through reduced valuations due to the perception of heightened credit or liquidity risks. Changes in the value of these instruments may result in a reduction to earnings and/or capital, which may adversely affect our results of operations.

Risks Related to Liquidity

We rely on a stable core deposit base and high quality unpledged liquid assets as our primary sources of liquidity.

We are dependent for our funding on a stable base of core deposits and high quality unpledged assets including cash held on deposit at the Federal Reserve. Our ability to maintain a stable core deposit base is a function of our financial performance, our reputation and the security provided by FDIC insurance, which combined, gives customers confidence in us. If any of these items are damaged or come into question, the stability of our core deposits could be harmed. If our high quality unpledged liquid assets lose value or can not be sold in an orderly fashion, it could harm our ability to meet our obligations.

Our ability to meet contingency funding needs, in the event of a crisis that causes a disruption to our core deposit base, is dependent on access to wholesale markets, including funds provided by the FHLB of Pittsburgh.

We own common stock of the FHLB in order to qualify for membership in the FHLB system, which enables us to borrow on our line of credit with the FHLB that is secured by a blanket lien on a significant portion of our loan portfolio. Changes or disruptions to the FHLB or the FHLB system in general may materially impact our ability to meet short and long-term liquidity needs or meet growth plans. Additionally, we cannot be assured that the FHLB will be able to provide funding to us when needed, nor can we be certain that the FHLB will provide funds specifically to us, should our financial condition and/or our regulators prevent access to our line of credit. The inability to access this source of funds could have a materially adverse effect on our ability to meet our customer s needs. Our financial flexibility could be severely constrained if we were unable to maintain our access to funding or if adequate financing is not available at acceptable interest rates.

Risks Related to Regulatory Compliance and Legal Matters

Recent legislation enacted in response to market and economic conditions may significantly affect our operations, financial condition and earnings.

Disruptions in the financial system during the past several years have resulted in significantly reduced business activity throughout the global and U.S. economies, which have the potential to significantly affect financial institutions. The Dodd-Frank Act was enacted as a major reform in response to this financial crisis. The Dodd-Frank Act increases regulation and oversight of the financial services industry, and imposes restrictions on the ability of institutions within the industry to conduct business consistent with historical practices, including aspects such as capital requirements, affiliate transactions, compensation, consumer protection regulations and mortgage

Table of Contents

Item 1A. RISK FACTORS continued

regulation, among others. It is not clear what impact the Dodd-Frank Act and the numerous implementing regulations will ultimately have on the financial markets or on the U.S. banking and financial services industries and the broader U.S. and global economies. They may increase our costs of regulatory compliance and of doing business and otherwise affect our operations, and will likely result in additional costs and a diversion of management s time from other business activities, any of which may adversely impact our results of operations, liquidity or financial condition. They also may significantly affect the markets in which we do business, the markets for and value of our investments and our ongoing operations, costs and profitability.

Our deposit insurance premiums have decreased but may increase in the future, which could have a material adverse impact on our future earnings and financial condition.

The FDIC insures deposits at FDIC-insured financial institutions, including S&T Bank. The FDIC charges insured financial institutions premiums to maintain the DIF at a specific level. The Bank s FDIC insurance premiums recently decreased after substantial increases beginning in 2009, but we may pay significantly higher premiums in the future. Current economic conditions have increased bank failures and additional failures are expected, all of which decrease the DIF. The Dodd-Frank Act increased the minimum target DIF ratio from 1.15 percent of estimated insured deposits to 1.35 percent of estimated insured deposits. The FDIC must seek to achieve the 1.35 percent ratio by September 30, 2020. Insured institutions with assets of $10 billion or more are supposed to fund the increase. The FDIC has issued regulations to implement these provisions of the Dodd-Frank Act. It has, in addition, established a higher reserve ratio of 2 percent as a long-term goal beyond what is required by statute. There is no implementation deadline for the 2 percent ratio. The FDIC may increase the assessment rates or impose additional special assessments in the future to keep the DIF at or above the statutory minimum target. Any increase in our FDIC premiums could have an adverse effect on the Bank s profits and financial condition. Refer to Supervision and Regulation within Item 1 of this report for additional information.

Future governmental regulation and legislation could limit our growth.

We are subject to extensive state and federal regulation, supervision and legislation that govern nearly every aspect of our operations. The regulations are primarily intended to protect depositors, customers and the banking system as a whole, not shareholders. Failure to comply with applicable regulations could lead to penalties and damage to our reputation. Furthermore, as shown through the Dodd-Frank Act, the regulatory environment is constantly undergoing change and the impact of changes to laws, the rapid implementation of regulations, the interpretation of such laws or regulations or other actions by existing or new regulatory agencies could make regulatory compliance more difficult or expensive, and thus could affect our ability to deliver or expand services, or it could diminish the value of our business. The ramifications and uncertainties of the recent increase in government intervention in the U.S. financial system could also adversely affect us. Refer to Supervision and Regulation within Item 1 of this report for additional information.

Negative public opinion could damage our reputation and adversely impact our earnings and liquidity.

Reputational risk, or the risk to our business, earnings, liquidity and capital from negative public opinion, could result from our actual or alleged conduct in a variety of areas, including legal and regulatory compliance, lending practices, corporate governance, litigation, ethical issues or inadequate protection of customer information. We expend significant resources to comply with regulatory requirements, and the failure to

comply with such regulations could result in reputational harm or significant legal or remedial costs. Damage to our reputation could adversely affect our ability to retain and attract new customers and adversely impact our earnings and liquidity.

Table of Contents

Item 1A. RISK FACTORS continued

We may be a defendant from time to time in a variety of litigation and other actions, which could have a material adverse effect on our financial condition and results of operations.

From time to time, customers and others make claims and take legal action pertaining to the performance of our responsibilities. Additionally, the current economic downturn has resulted in higher customer defaults and a resultant increase in litigation. Whether customer claims and legal action related to the performance of our responsibilities are founded or unfounded, if such claims and legal actions are not resolved in a manner favorable to us, they may result in significant expenses, attention from management and financial liability. Any financial liability or reputational damage could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations.

Risks Related to Our Business Strategy

Our strategy includes growth plans through organic growth and acquisitions. Our financial condition and results of operations could be negatively affected if we fail to grow or fail to manage our growth effectively.

We intend to continue pursuing a growth strategy, which may include organic growth, expansion or acquisitions. We cannot assure you that we will be able to expand our market presence in our existing markets or successfully enter new markets or that any such expansion will not adversely affect our results of operations. Failure to manage our growth effectively could have a material adverse effect on our business, future prospects, financial condition or results of operations and could adversely affect our ability to successfully implement our business strategy.

Our failure to find suitable acquisition candidates, or successfully bid against other competitors for acquisitions, could adversely affect our ability to successfully implement our business strategy. If we are successful in acquiring other entities, the process of integrating such entities will divert significant management time and resources. We may not be able to integrate successfully or operate profitably any entity we may acquire. We may experience disruption and incur unexpected expenses in integrating acquisitions. These failures could adversely impact our future prospects and results of operation.

We are subject to competition from both banks and non-banking companies.

The financial services industry is highly competitive, and we encounter strong competition for deposits, loans and other financial services in our market area. Our principal competitors include commercial banks of all types, finance companies, credit unions, mortgage brokers, insurance agencies, trust companies and various sellers of investments and investment advice. Many of our non-bank competitors are not subject to the same degree of regulation as we are and have advantages over us in providing certain services. Additionally, many of our competitors are significantly larger than we are and have greater access to capital and other resources. Failure to compete effectively for deposit, loan and other banking customers in our markets could cause us to lose market share, slow our growth rate and may have an adverse effect on our financial condition and results of operations.

We may be required to raise capital in the future, but that capital may not be available or may not be on acceptable terms when it is needed.

We are required by federal regulatory authorities to maintain adequate capital levels to support operations. Our ability to raise additional capital is dependent on capital market conditions at that time and on our financial performance and outlook. Pending regulatory changes, such as regulations to implement Basel III and the Dodd-Frank Act, may require us to have more capital than was

Table of Contents

Item 1A. RISK FACTORS continued

previously required. If we cannot raise additional capital when needed, we may not be able to meet these requirements, and our ability to further expand our operations through organic growth or through acquisitions may be adversely affected.

The Warrant we issued to the U.S. Treasury may be dilutive to holders of our common stock.

The ownership interest of the existing holders of our common stock may be diluted to the extent the warrant we issued to the U.S. Treasury in connection with the sale to the U.S. Treasury of the Series A Preferred Stock is exercised. Although we redeemed all of the outstanding preferred stock previously issued to the U.S. Treasury, we did not repurchase the outstanding warrant and it will remain outstanding until 2019 or until we repurchase it. The shares of common stock underlying the warrant represent approximately 1.70 percent of the shares of our common stock outstanding as of January 31, 2013 (including the shares issuable upon exercise of the warrant in total shares outstanding). Although the U.S. Treasury has agreed not to vote any of the shares of common stock it receives upon exercise of the warrant, a purchaser of any portion of the warrant or of any shares of common stock acquired upon exercise of the warrant is not bound by this restriction.

Our ability to pay dividends on our common stock may be limited.

Holders of our common stock will be entitled to receive only such dividends as our Board of Directors may declare out of funds legally available for such payments. Although we have historically declared cash dividends on our common stock, we are not required to do so and our Board of Directors could reduce, suspend or eliminate our dividend at any time. Any decrease or elimination to the dividends on our common stock could adversely affect the market price of our common stock.

Item 1B. UNRESOLVED STAFF COMMENTS

There are no unresolved SEC staff comments.

Item 2. PROPERTIES

We own a four-story building in Indiana, Pennsylvania, located at 800 Philadelphia Street, which serves as our headquarters, executive and administrative offices. Our Community Banking and Wealth Management segments are also located at our headquarters. The executive office of

our Insurance segment is located in a leased building in Ebensburg, Pennsylvania which is in Cambria County. Additionally, we lease a building in Indiana, Pennsylvania that serves as our data processing and technology center and we own a two-story building directly behind it that serves as additional administrative offices. Community Banking has 63 locations, including 59 branches located in eleven counties in Pennsylvania, of which 37 are owned and 22 are leased, as well as three separate drive up facilities and one loan production office in Akron, Ohio. Community Banking leases an office in Akron, Ohio, that is staffed by three commercial lenders. Community Banking also leases two offices to Insurance. Wealth Management leases two offices, one in Allegheny County, Pennsylvania and one in Westmoreland County, Pennsylvania. Wealth Management also has several staff located within the Community Banking offices to provide their services to retail customers. Insurance leases three offices located in three counties in Pennsylvania. Insurance also has staff located within the Community Banking offices in Jefferson and Blair counties. The operating and capital leases for Community Banking, Wealth Management and Insurance expire at various dates through the year 2054 and generally include options to renew. For additional information regarding the lease commitments, refer to Note 10 Premises and Equipment in the Notes to Consolidated Financial Statements, which is included in Item 8 of this Report.

Table of Contents

Item 3. LEGAL PROCEEDINGS

The nature of our business generates a certain amount of litigation involving matters arising in the ordinary course of business. However, in management s opinion, there are no proceedings pending to which we are a party or to which our property is subject, which, if determined adversely to us, would be material in relation to our shareholders equity or financial condition. In addition, no material proceedings are pending nor are known to be threatened or contemplated against us by governmental authorities or other parties.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

Table of Contents

PART II

Item 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Stock Prices and Dividend Information

Our common stock is listed on the NASDAQ Global Select Market System or NASDAQ under the symbol STBA. The range of sale prices for the years 2012 and 2011 is set forth in the table below and is based upon information obtained from NASDAQ. As of the close of business on January 31, 2013, we had 3,277 shareholders of record. Dividends paid by S&T are primarily provided from S&T Bank s dividends to S&T. The payment of dividends by S&T Bank to S&T is subject to the restrictions described in Item 8, Note 6, Dividend and Loan Restrictions of this Report. The cash dividends declared per share are shown below.

	Price Range of Common Stock		Cash Dividends
2012	**Low**	**High**	**Declared**
Fourth quarter	$ 16.32	$ 18.50	$ 0.15
Third quarter	15.68	19.40	0.15
Second quarter	16.41	21.98	0.15
First quarter	19.65	23.34	0.15
2011			
Fourth quarter	$ 15.21	$ 20.67	$ 0.15
Third quarter	15.21	19.46	0.15
Second quarter	16.65	22.23	0.15
First quarter	20.90	23.86	0.15

Table of Contents

Item 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES continued

Five-Year Cumulative Total Return

The following chart compares the cumulative total shareholder return on our common stock with the cumulative total shareholder return of the NASDAQ Composite Index and NASDAQ Bank Index[1] assuming a $100 investment in each on December 31, 2007.

	Period Ending					
Index	**12/31/07**	**12/31/08**	**12/31/09**	**12/31/10**	**12/31/11**	**12/31/12**
S&T Bancorp, Inc.	$ 100.00	$ 133.37	$ 66.36	$ 90.74	$ 80.94	$ 77.27
NASDAQ Composite	100.00	60.02	87.24	103.08	102.26	120.42
NASDAQ Bank	100.00	78.46	65.67	74.97	67.10	79.64

(1) The NASDAQ Bank Index contains securities of NASDAQ-listed companies classified according to the Industry Classification Benchmark as Banks. These companies include banks providing a broad range of financial services, including retail banking, loans and money transmissions.

Table of Contents

Item 6. SELECTED FINANCIAL DATA

The tables below summarize selected consolidated financial data as of the dates or for the periods indicated and should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations in Item 7 and the Consolidated Financial Statements and Notes in Item 8 of this report.

CONSOLIDATED BALANCE SHEETS

December 31 *(in thousands)*	**2012**	**2011**	**2010**	**2009**	**2008**
Total assets	$ 4,526,702	$ 4,119,994	$ 4,114,339	$ 4,170,475	$ 4,438,368
Securities available-for-sale	453,096	357,596	288,025	354,860	452,713
Goodwill	175,733	165,273	165,273	165,167	163,546
Net loans and loans held for sale	3,322,637	3,083,768	3,312,540	3,344,827	3,526,027
Total deposits	3,638,428	3,335,859	3,317,524	3,304,541	3,228,416
Securities sold under repurchase agreements and federal funds purchased	62,582	30,370	40,653	44,935	113,419
Short-term borrowings	75,000	75,000		51,300	308,475
Long-term borrowings	34,101	31,874	29,365	85,894	180,331
Junior subordinated debt securities	90,619	90,619	90,619	90,619	90,619
Preferred stock, series A			106,137	105,370	
Total shareholders equity	537,422	490,526	578,665	553,318	448,694

CONSOLIDATED STATEMENTS OF NET INCOME

Years Ended December 31 *(in thousands, except per share data)*	**2012**	**2011**	**2010**	**2009**	**2008**
Interest income	$ 156,251	$ 165,079	$ 180,419	$ 195,087	$ 216,118
Interest expense	21,024	27,733	34,573	49,105	72,171
Provision for loan losses	22,815	15,609	29,511	72,354	12,878
Net Interest Income After Provision for Loan Losses	**112,412**	**121,737**	**116,335**	**73,628**	**131,069**
Noninterest income	51,912	44,057	47,210	38,580	37,452
Noninterest expense	122,863	103,908	105,633	108,126	83,801
Net Income Before Taxes	**41,461**	**61,886**	**57,912**	**4,082**	**84,720**
Provision (benefit) for income taxes	7,261	14,622	14,432	(3,869)	24,517
Net Income	**34,200**	**47,264**	**43,480**	**7,951**	**60,203**
Preferred stock dividends and discount amortization		7,611	6,201	5,913	
Net Income Available to Common Shareholders	**$ 34,200**	**$ 39,653**	**$ 37,279**	**$ 2,038**	**$ 60,203**
Per Share Data					
Earnings per common share basic	$ 1.18	$ 1.41	$ 1.34	$ 0.07	$ 2.30
Earnings per common share diluted	1.18	1.41	1.34	0.07	2.28
Dividends declared per common share	0.60	0.60	0.60	0.61	1.24
Common book value	18.08	17.44	16.91	16.14	16.24

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This section reviews our financial condition and results of operations for each of the past three years. Certain reclassifications have been made to prior periods to place them on a basis comparable with the current period presentation. Some tables may include additional time periods to illustrate trends within our financial statements. The results of operations reported in the accompanying Consolidated Financial Statements are not necessarily indicative of results to be expected in future periods.

Important Note Regarding Forward-Looking Statements

This Report on Form 10-K contains or incorporates statements that we believe are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements generally relate to our financial condition, results of operations, plans, objectives, future performance or business. They usually can be identified by the use of forward-looking language such as will likely result, may, are expected to, is anticipated, estimate, forecast, projected, intends to or other similar words. You should not place undue reliance on these statements, as they are subject to risks and uncertainties, including but not limited to, those identified under Risk Factors in Item 1A of this report, the documents incorporated by reference or other important factors disclosed in this report and from time to time in our other filings with the Securities and Exchange Commission, or SEC. When considering these forward-looking statements, you should keep in mind these risks and uncertainties, as well as any cautionary statements we may make. Moreover, you should treat these statements as speaking only as of the date they are made and based only on information actually known to us at that time. We undertake no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

These forward-looking statements are based on current expectations, estimates and projections about our business and beliefs and assumptions made by management. These Future Factors, are not guarantees of our future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in these forward-looking statements.

Future Factors include:

- changes in interest rates, spreads on interest-earning assets and interest-bearing liabilities, the shape of the yield curve and interest rate sensitivity;
- a prolonged period of low interest rates;
- credit losses;
- access to capital in the amounts, at the times and on the terms required to support our future businesses;
- legislation affecting the financial services industry as a whole, and/or S&T Bancorp, Inc., or S&T, in particular, including the effects of the Dodd-Frank Act;
- regulatory supervision and oversight, including required capital levels, and public policy changes, including environmental regulations;
- increasing price and product/service competition, including new entrants;
- rapid technological developments and changes;
- the ability to continue to introduce competitive new products and services on a timely, cost-effective basis;
- deterioration of the housing market and reduced demand for mortgages;
- containing costs and expenses;
- reliance on large customers;
- the outcome of pending and future litigation and governmental proceedings;
- managing our internal growth and acquisitions;

the possibility that the anticipated benefits from our acquisitions cannot be fully realized in a timely manner or at all, or that integrating the acquired operations will be more difficult, disruptive or costly than anticipated;

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

- general economic or business conditions, either nationally or regionally in Western Pennsylvania, may be less favorable than expected, resulting in among other things, a reduced demand for credit and other services;
- a decline in market capitalization to common book value, which could warrant further analysis of the carrying value of goodwill and could result in an adjustment to its carrying value resulting in a non-cash charge to net income; and
- a continuation of recent turbulence in significant portions of the global financial and real estate markets could impact our performance, both directly, by affecting our revenues and the value of our assets and liabilities and indirectly, by affecting the economy generally.

These are representative of the Future Factors that could affect the outcome of the forward-looking statements. In addition, such statements could be affected by general industry and market conditions and growth rates, general economic conditions, including interest rate and currency exchange rate fluctuations and other Future Factors.

Critical Accounting Policies and Estimates

Our financial statements are prepared in accordance with U.S. generally accepted accounting principles, or GAAP. Application of these principles requires management to make estimates, assumptions and judgments that affect the amounts reported in the Consolidated Financial Statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the Consolidated Financial Statements; accordingly, as this information changes, the Consolidated Financial Statements could reflect different estimates, assumptions and judgments. Certain policies inherently are based to a greater extent on estimates, assumptions and judgments of management and, as such, have a greater possibility of producing results that could be materially different than originally reported.

Our most significant accounting policies are presented in Note 1 Summary of Significant Accounting Policies in the Notes to Consolidated Financial Statements, which are included in Item 8 of this report. These policies, along with the disclosures presented in the Notes to Consolidated Financial Statements, provide information on how significant assets and liabilities are valued in the Consolidated Financial Statements and how those values are determined.

We view critical accounting policies to be those which are highly dependent on subjective or complex estimates, assumptions and judgments and where changes in those estimates and assumptions could have a significant impact on the Consolidated Financial Statements. We currently view the determination of the allowance for loan losses, or ALL, income taxes, securities valuation and goodwill and other intangible assets to be critical accounting policies. During 2012, we did not significantly change the manner in which we applied our critical accounting policies or developed related assumptions or estimates. We have reviewed these related critical accounting estimates and related disclosures with the Audit Committee.

Allowance for Loan Losses

Our loan portfolio is our largest category of assets on our Consolidated Balance Sheets. Accordingly, we have designed a systematic ALL methodology which is used to determine our provision for loan losses and ALL on a quarterly basis. The ALL represents management s estimate of probable losses inherent in the loan portfolio at the balance sheet date and is presented as a reserve against loans in the Consolidated Balance Sheets. The ALL is increased by a provision charged to expense and reduced by charge-offs, net of recoveries. Determination of an adequate ALL is inherently subjective, as it requires estimations of the occurrence of future events, as well as the timing of such events. The ALL may be subject to significant changes from period to period.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

The methodology for determining the ALL has two main components: evaluation and impairment tests of individual loans and evaluation and impairment tests of certain groups of homogeneous loans with similar risk characteristics.

We individually evaluate all substandard, doubtful and nonaccrual commercial loans greater than $0.5 million for impairment. A loan is impaired when, based on current information and events, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. For all troubled debt restructurings, or TDRs, regardless of size, as well as all other impaired loans, we conduct further analysis to determine the probable loss and assign a specific reserve to the loan if deemed appropriate. Specific reserves are established based upon 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 estimated fair value of the collateral if the loan is collateral dependent. These analyses involve a high degree of judgment in estimating the amount of loss associated with specific impaired loans, including estimating the amount and timing of future cash flows, current estimated fair value of the loan and collateral values. Our impairment evaluations consist primarily of the fair value of collateral method since most loans are collateral dependent.

The ALL methodology for groups of homogeneous loans, known as the general reserve, is comprised of both a quantitative and qualitative analysis. We first apply historical loss rates to pools of loans with similar risk characteristics. Loss rates are calculated by historical charge-offs that have occurred within each pool of loans over the loss emergence period. Loss emergence refers to the length of time between a loss event and a charge-off of the loan. We estimate the loss emergence period to be two years for commercial real estate, or CRE, loans and one year for all other loan classes. We use a one year look back period that results, when considering our loss emergence periods, in capturing historic losses for three years for CRE and two years for our other portfolio segments. After consideration of the loss calculations, management applies additional qualitative adjustments so that the ALL is reflective of the inherent losses that exist in the loan portfolio at the balance sheet date. Qualitative adjustments are made based upon changes in economic conditions, loan portfolio and asset quality data and credit process changes, such as credit policies or underwriting standards. The evaluation of the various components of the ALL requires considerable judgment in order to estimate inherent loss exposures.

We enhanced our ALL model in the fourth quarter of 2010 to better align it with regulatory guidance. The calculation of the base historical loss utilizing an average method over the prior five years was shortened to include a one to two year loss emergence period depending on the loan category over a rolling four quarter average. With the volatility in the credit cycle at that time, the shorter time horizon was more indicative of the loss emergence periods we were experiencing in our portfolio. We believe this shorter time horizon provides a better indication of inherent losses in the loan portfolio given the recent economic downturn. We also refined the qualitative factors beginning in the fourth quarter of 2010 to better align with regulatory guidance. Qualitative factors became a basis point adjustment applied to the historical base loss. The combination of the enhancements to the average method and the qualitative factors did not materially change the ALL at December 31, 2010, resulting in an increase in the ALL and provision of less than $0.5 million. Since December 31, 2010, there have been no further enhancements to the ALL methodology.

Our ALL Committee meets quarterly to verify the overall adequacy of the ALL. Additionally, on an annual basis, the Committee meets to validate certain aspects of our ALL model. This validation includes reviewing the pools of loans to ensure the segmentation results in relevant homogeneous pools of loans. The Committee reviews the historical loss emergence period and look back periods used to calculate the loss rates. Further, the Committee reviews the qualitative factors for reasonableness. As a result of this ongoing monitoring process, we may make changes to our ALL methodology to be responsive to the economic environment.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

At December 31, 2012, approximately 87 percent of the ALL related to the commercial loan portfolio. Commercial loans represent 72 percent of total portfolio loans. Commercial loans have been more impacted by the economic slowdown in our markets. The ability of customers to repay commercial loans is more dependent upon the success of their businesses, continuing income and general economic conditions. The risk of loss is higher on such loans compared to consumer loans, which have incurred lower losses in our market.

There are many factors affecting the ALL; some are quantitative, while others require qualitative judgment. Although we believe our process for determining the ALL adequately considers all of the factors that would likely result in credit losses, the process includes subjective elements and may be susceptible to significant change. To the extent actual outcomes differ from management estimates, additional provisions for loan losses could be required and could adversely affect our earnings or financial position in future periods.

Income Taxes

We estimate income tax expense based on amounts expected to be owed to the tax jurisdictions where we conduct business. The laws are complex and subject to different interpretations by us and various taxing authorities. On a quarterly basis, we assess the reasonableness of our effective tax rate based upon our current estimate of the amount and components of pre-tax income, tax credits and the applicable statutory tax rates expected for the full year.

Deferred income tax assets and liabilities are determined using the asset and liability method and are reported in other assets or other liabilities, as appropriate, in the Consolidated Balance Sheets. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities and recognizes enacted changes in tax rate and laws. When deferred tax assets are recognized, they are subject to a valuation allowance based on management s judgment as to whether realization is more likely than not.

Accrued taxes represent the net estimated amount due to taxing jurisdictions and are reported in other assets or other liabilities, as appropriate, in the Consolidated Balance Sheets. We evaluate and assess the relative risks and appropriate tax treatment of transactions and filing positions after considering statutes, regulations, judicial precedent and other information and maintain tax accruals consistent with the evaluation of these relative risks and merits. Changes to the estimate of accrued taxes occur periodically due to changes in tax rates, interpretations of tax laws, the status of examinations being conducted by taxing authorities and changes to statutory, judicial and regulatory guidance. These changes, when they occur, can affect deferred taxes and accrued taxes, as well as the current period s income tax expense and can be significant to our operating results.

Tax positions are recognized as a benefit only if it is more likely than not that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50 percent likely of being realized on examination. For tax positions not meeting the more likely than not test, no tax benefit is recorded.

Securities Valuation

We determine the appropriate classification of securities at the time of purchase. All securities, including both debt and equity securities, are classified as available-for-sale. These securities are carried at fair value with net unrealized gains and losses deemed to be temporary reported separately as a component of other comprehensive income, net of tax. Realized gains and losses on the sale of

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

available-for-sale securities and other-than-temporary impairment, or OTTI, charges are recorded within noninterest income in the Consolidated Statements of Net Income. Realized gains and losses on the sale of securities are determined using the specific-identification method.

We perform a quarterly review of our securities to identify those that may indicate an OTTI. Our policy for OTTI within the marketable equity securities portfolio generally requires an impairment charge when the security is in a loss position for 12 consecutive months, unless facts and circumstances would suggest the need for an OTTI prior to that time. Our policy for OTTI within the debt securities portfolio is based upon a number of factors, including but not limited to, the length of time and extent to which the estimated fair value has been less than cost, the financial condition of the underlying issuer, the ability of the issuer to meet contractual obligations, the best estimate of impairment charge representing credit losses, the likelihood of the security s ability to recover any decline in its estimated fair value and whether we intend to sell the investment security or if it is more likely than not that we will be required to sell the security prior to the security s recovery. If the financial markets experience deterioration, charges to income could occur in future periods.

Goodwill and Other Intangible Assets

As a result of acquisitions, we have recorded goodwill and identifiable intangible assets on our Consolidated Balance Sheets. Goodwill represents the excess of the purchase price over the fair value of net assets purchased.

Goodwill relates to value inherent in the Community Banking and Insurance reporting units and the value is dependent upon our ability to provide quality, cost-effective services in the face of competition from other market participants. This ability relies upon continuing investments in processing systems, the development of value-added service features and the ease of use of our services. As such, goodwill value is supported ultimately by profitability that is driven by the volume of business transacted. A decline in earnings as a result of a lack of growth or the inability to deliver cost-effective services over sustained periods can lead to impairment of goodwill, which could adversely impact earnings in future periods.

We have three reporting units including: Community Banking, Wealth Management and Insurance. The carrying value of goodwill is tested annually for impairment each October 1 or more frequently if it is determined that we should do so. We first assess qualitatively whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. Our qualitative assessment considers such factors as macroeconomic conditions, market conditions specifically related to the banking industry, our overall financial performance and various other factors. If we determine that it is more likely than not that the fair value is less than the carrying amount, we proceed to test for impairment. The evaluation for impairment involves comparing the current estimated fair value of each reporting unit to its carrying value, including goodwill. If the current estimated fair value of a reporting unit exceeds its carrying value, no additional testing is required and impairment loss is not recorded. If the estimated fair value of a reporting unit is less than the carrying value, further valuation procedures are performed and could result in impairment of goodwill being recorded. Further valuation procedures would include allocating the estimated fair value to all assets and liabilities of the reporting unit to determine an implied goodwill value. If the implied value of goodwill of a reporting unit is less than the carrying amount of that goodwill, an impairment loss is recognized in an amount equal to that excess. We completed the annual goodwill impairment assessment as required in 2012, 2011 and 2010; the results indicated that the fair value of each reporting unit exceeded the carrying value.

Based upon our qualitative assessment performed for our annual impairment analysis, we concluded that it is more likely than not that the fair value of the reporting units exceeds the carrying value. Both the national economy and the local western Pennsylvania economy where our business is concentrated showed signs of stabilization over the past year. General economic activity

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

and key indicators such as housing and unemployment showed modest improvement. While still challenging, the banking environment also improved with fewer bank failures, better asset quality, improved earnings and generally better stock prices. Activity in mergers and acquisition demonstrated that there is premium value of banking franchises and a number of banks of our size have been able to access the capital markets over the past year. While our stock price declined slightly over the course of the year after increasing in the first quarter, it has been fairly consistent for the past three quarters. Additionally, our overall performance has not significantly deteriorated and we did not identify any other facts or circumstances that would cause us to conclude that it is more likely than not that the fair value of the reporting units would be less than the carrying value.

We determine the amount of identifiable intangible assets based upon independent core deposit and insurance contract analyses at the time of acquisition. Intangible assets with finite useful lives, consisting primarily of core deposit and customer list intangibles, are amortized using straight-line or accelerated methods over their estimated weighted average useful lives, ranging from 10 to 16 years. Intangible assets with finite useful lives are evaluated for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. No events or changes in circumstances occurred during the years ended December 31, 2012, 2011 and 2010.

The financial services industry and securities markets can be adversely affected by declining values. Although the economic weakness of recent years appears to be stabilizing, if economic conditions result in a prolonged period of economic weakness in the future, our business segments, including the Community Banking segment, may be adversely affected. In the event that we determine that either our goodwill or finite lived intangible assets are impaired, recognition of an impairment charge could have a significant adverse impact on our financial position or results of operations in the period in which the impairment occurs.

Recent Accounting Pronouncements and Developments

Note 1 Summary of Significant Accounting Policies, Recently Adopted Accounting Standards Updates and Recently Issued Accounting Standards Updates in the Notes to the Consolidated Financial Statements, which is included in Item 8 of this report, discusses new accounting pronouncements that we adopted and the expected impact of accounting pronouncements recently issued or proposed, but not yet required to be adopted.

Executive Overview

We are a bank holding company headquartered in Indiana, Pennsylvania with assets of $4.5 billion at December 31, 2012. We provide a full range of financial services through offices located in Allegheny, Armstrong, Blair, Butler, Cambria, Clarion, Clearfield, Indiana, Jefferson, Washington and Westmoreland counties of Pennsylvania. We provide full service retail and commercial banking products as well as cash management services, insurance, estate planning and administration, employee benefit plan investment management and administration, corporate services and other fiduciary services. Our common stock trades on the Nasdaq Global Select Market under the symbol STBA.

We earn revenue primarily from interest on loans and securities and fees charged for financial services provided to our customers. Offsetting these revenues are the cost of deposits and other funding sources, provision for loan losses and other operating costs such as: salaries and employee benefits, occupancy, data processing and tax expense.

Our mission is to become the financial services provider of choice in Western Pennsylvania by delivering exceptional service and value, one customer at a time. Our strategic plan focuses on growth through de novo expansion, acquisition or organic growth. Our strategic plan includes a collaborative model that combines expertise from all of our business segments and focuses on satisfying each customer s individual financial objectives.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

During 2012, we grew primarily through acquisition and successfully completed two mergers adding approximately $368 million in assets. On March 9, 2012, we completed our acquisition and conversion of Mainline Bancorp, Inc., or Mainline, a bank holding company located in Ebensburg, Pennsylvania. Mainline had one bank subsidiary, Mainline National Bank, with eight branches located throughout Cambria and Blair counties in Western Pennsylvania, adding $129.5 million in loans and $206.0 million in deposits. The total acquisition cost of Mainline was $27.8 million. On August 13, 2012, we further expanded our community banking network with the completion of our acquisition of Gateway Bank of Pennsylvania, a two branch bank with $99.1 million in loans and $105.4 million in deposits. The total acquisition cost of Gateway Bank was $19.8 million. As of December 31, 2012, Gateway was operating as a separate wholly-owned subsidiary of S&T, with all transactions since the acquisition date consolidated in our financial statements. On February 8, 2013, Gateway Bank was merged into S&T Bank, and their two branches are now fully operational branches of S&T Bank.

As a result of these acquisitions, our earnings were impacted by one-time merger related expenses of $6.0 million.

Organic loan growth remained a challenge for a majority of 2012, however, we did experience positive trends in the later part of the year. An important strategic initiative as we move in to 2013 is loan growth. In August 2012, we expanded our commercial lending footprint into Northeastern Ohio through the opening of a loan production office in Akron. We are retaining 10, 15 and 20 year residential real estate loans in our portfolio, rather than selling these loans in the secondary market. Additionally, we are hiring seasoned lenders in both our commercial and residential real estate areas to improve organic loan growth.

Asset quality remained a challenge for us throughout 2012, especially in the first half of the year. The provision for loan losses increased $7.2 million to $22.8 million for 2012 compared to $15.6 million in 2011. Net loan charge-offs increased to $25.2 million compared to $18.2 million in 2011. During the first half of 2012, we experienced increased charge-offs primarily in our commercial construction loan portfolio as projects in this portfolio slowed due to the economic environment and as a result, appraised values declined. Asset quality stabilized in the second half of the year resulting in a lower provision for loan losses. Our nonperforming assets are at their lowest level since 2008 at $55.0 million at December 31, 2012. Additionally, we have been actively managing our substandard loans resulting in a decrease of $49.1 million, or 26.0 percent at December 31, 2012 compared to December 31, 2011.

Our capital ratios increased slightly from 2011 and remain significantly above the well capitalized thresholds of federal bank regulatory agencies with a leverage ratio of 9.31 percent, tier 1 risk-based capital ratio of 11.98 percent and total risk based capital ratio of 15.39 percent.

In 2013, our performance will be influenced by asset quality. If the economy improves, we should expect to see progress in reducing net charge-offs, nonperforming loans and provision for loan losses. However, a return of the economic slowdown, regionally or nationally, could cause deterioration in our asset quality. We recognize a greater dependence on commercial loans may expose us to credit risk and that we may have more volatility in nonperforming loans and loan charge-offs when problems do occur. We will mitigate this risk through our disciplined credit risk management practices, the review of such loans by our Criticized Asset Committee and continued sound underwriting practices. Because the majority of our revenue comes from net interest income, net loan and deposit growth, combined with the relative pricing and mix of that growth are major factors that affect our operations and financial condition. Our net interest margin will be a challenge as we move into 2013, especially if the low interest rate environment persists.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Results of Operations

Year Ended December 31, 2012

Net Income

Our net income available to common shareholders decreased $5.5 million to $34.2 million or $1.18 per share in 2012 compared to $39.7 million or $1.41 per share in the previous year. The decrease in net income was primarily a result of an increase of $19.0 million in noninterest expense, which includes $6.0 million in one-time merger related expenses. Additionally, our provision for loan losses increased $7.2 million. We also experienced a decline in our net interest income of $2.1 million compared to the prior year, due to lack of organic loan growth and the low interest rate environment. These decreases were partially offset by a $7.9 million increase in noninterest income primarily due to increased mortgage banking and wealth management fees and gains on security sales, and a decrease of $7.4 million in provision for income taxes. Additionally, we did not have preferred dividend payments due to the redemption of $108.7 million of preferred stock from the U.S. Department of Treasury s Capital Purchase Program in December of 2011.

Return on Equity and Assets

The table below presents our consolidated profitability and common equity to assets ratio for each of the last three years:

Years Ended December 31	2012	2011	2010
Common return on average assets	0.79%	0.97%	0.90%
Common return on average equity	6.62%	6.78%	6.58%
Dividend payout ratio	50.75%	42.44%	44.75%
Common equity to asset ratio	11.87%	11.91%	11.48%

Net Interest Income

Our principal source of revenue is net interest income. Net interest income represents the difference between the interest and fees earned on interest-earning assets and the interest paid on interest-bearing liabilities. Net interest income is affected by changes in the average balance of interest-earning assets and interest-bearing liabilities and changes in interest rates and spreads. Maintaining consistent spreads between interest-earning assets and interest-bearing liabilities is significant to our financial performance because net interest income comprised 73 percent of operating revenue (net interest income plus noninterest income, excluding security gains/losses) in 2012 and 76 percent of operating revenue in 2011. Refer to page 57 Explanation of Use of Non-GAAP Financial Measures for a discussion of operating revenue as a non-GAAP financial measure. The level and mix of interest-earning assets and interest-bearing liabilities are managed by our Asset and Liability Committee, or ALCO, in order to mitigate interest rate and liquidity risks of the balance sheet. A variety of ALCO strategies were implemented,

within prescribed ALCO risk parameters, to maintain an acceptable net yield on interest-earning assets (net interest margin) given the challenges of the current interest rate environment.

The interest income on interest-earning assets and the net interest margin are presented on a fully taxable-equivalent basis. The fully taxable-equivalent basis adjusts for the tax benefit of income on certain tax-exempt loans and investments using the federal statutory tax rate of 35 percent for each period. We believe this measure to be the preferred industry measurement of net interest income that provides a relevant comparison between taxable and non-taxable amounts.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

The following table reconciles interest income per the Consolidated Statements of Net Income to net interest income adjusted to a fully taxable-equivalent basis:

Years Ended December 31 *(in thousands)*	**2012**	**2011**	**2010**
Interest income per Consolidated Statements of Net Income	$ 156,251	$ 165,079	$ 180,419
Adjustment to fully taxable-equivalent basis	4,471	4,154	4,627
Interest income adjusted to fully taxable-equivalent basis	160,722	169,233	185,046
Interest expense per Consolidated Statements of Net Income	21,024	27,733	34,573
Net Interest Income Adjusted to Fully Taxable-equivalent Basis (non-GAAP)	**$ 139,698**	**$ 141,500**	**$ 150,473**

32

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Average Balance Sheet and Net Interest Income Analysis

The following table provides information regarding the average balances, interest and yields earned on interest-earning assets and the average balances, interest and rates paid on interest-bearing liabilities:

	2012			2011			2010		
December 31	**Average Balance**	**Interest**	**Yield/ Rate**	**Average Balance**	**Interest**	**Yield/ Rate**	**Average Balance**	**Interest**	**Yield/ Rate**
(dollars in thousands)									
ASSETS									
Loans[1][2]	$ 3,213,018	$ 147,819	4.59%	$ 3,216,856	$ 156,845	4.88%	$ 3,386,103	$ 172,319	5.09%
Taxable investment securities	297,168	7,351	2.47%	273,320	8,475	3.10%	226,714	8,373	3.69%
Tax-exempt investment securities[2]	90,527	4,801	5.30%	62,607	3,611	5.77%	76,707	4,354	5.68%
Federal Home Loan Bank stock	17,115	33	0.19%	20,091		%	23,336		%
Interest-bearing balance with banks	289,947	718	0.25%	123,714	302	0.24%	49		0.34%
Total Interest-earning Assets	**3,907,775**	**160,722**	**4.10%**	**3,696,588**	**169,233**	**4.58%**	**3,712,909**	**185,046**	**4.98%**
Noninterest-earning assets:									
Cash and due from banks	53,517			50,458			90,462		
Premises and equipment, net	38,460			38,425			39,142		
Other assets	361,982			344,378			340,234		
Less allowance for loan losses	(49,196)			(57,241)			(59,292)		
Total Assets	**$ 4,312,538**			**$ 4,072,608**			**$ 4,123,455**		
LIABILITIES AND SHAREHOLDERS EQUITY									
Interest-bearing liabilities:									
Interest-bearing demand and money market	$ 615,713	$ 674	0.11%	$ 536,085	$ 739	0.14%	$ 518,383	$ 1 220	0.24%
Savings	902,889	2,356	0.26%	761,274	1,267	0.17%	749,325	2,127	0.28%
Certificates of deposit	1,104,262	13,766	1.24%	1,181,823	20,946	1.77%	1,300,803	25,370	1.95%
Securities sold under repurchase agreements	47,388	82	0.17%	41,584	53	0.13%	46,490	64	0.14%
Short-term borrowings	50,212	123	0.24%	551	2	0.32%	32,473	146	0.45%
Long-term borrowings	33,841	1,107	3.26%	31,651	1,091	3.45%	42,920	1,643	3.83%
Junior subordinated debt securities	90,619	2,916	3.21%	90,619	3,635	4.01%	90,619	4,003	4.42%
Total Interest-bearing Liabilities	**2,844,924**	**21,024**	**0.74%**	**2,643,587**	**27,733**	**1.05%**	**2,781,013**	**34,573**	**1.24%**
Noninterest-bearing liabilities:									
Noninterest-bearing demand	877,056			792,911			728,708		
Other liabilities	73,746			50,924			47,064		
Shareholders equity	516,812			585,186			566,670		
Total Liabilities and Shareholders Equity	**$ 4,312,538**			**$ 4,072,608**			**$ 4,123,455**		
Net Interest Income		**$ 139,698**			**$ 141,500**			**$ 150,473**	
Net Yield on Interest-earning Assets			**3.57%**			**3.83%**			**4.05%**

(1) *For the purpose of these computations, nonaccruing loans are included in the daily average loan amounts outstanding.*

(2) *Tax-exempt income is on a fully taxable-equivalent basis, including the dividend-received deduction for equity securities, using the statutory federal corporate income tax rate of 35 percent for 2012, 2011 and 2010.*

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

The following table presents a summary of the changes in interest earned and interest paid resulting from changes in average balances and changes in rates:

	2012 Compared to 2011 Increase (Decrease) Due to*(1)*			2011 Compared to 2010 Increase (Decrease) Due to*(1)*		
(in thousands)	**Volume**	**Rate**	**Net**	**Volume**	**Rate**	**Net**
Interest earned on:						
Loans*(2)*	$ (187)	$ (8,839)	$ (9,026)	$ (8,613)	$ (6,861)	$ (15,474)
Taxable investment securities	739	(1,863)	(1,124)	1,722	(1,620)	102
Tax-exempt investment securities*(2)*	1,612	(420)	1,192	(800)	57	(743)
Federal Home Loan Bank Stock		33	33			
Interest-bearing balance with bank	406	9	415	419	(117)	302
Total Interest-earning Assets	**2,570**	**(11,080)**	**(8,510)**	**(7,272)**	**(8,541)**	**(15,813)**
Interest paid on:						
Interest-bearing demand and money market	$ 110	$ (175)	$ (65)	$ 42	$ (523)	$ (481)
Savings	236	853	1,089	34	(894)	(860)
Certificates of deposit	(1,374)	(5,806)	(7,180)	(2,321)	(2,103)	(4,424)
Securities sold under repurchase agreements	7	22	29	(7)	(4)	(11)
Short-term borrowings	157	(36)	121	(143)	(1)	(144)
Long-term borrowings	75	(58)	17	(431)	(121)	(552)
Junior subordinated debt securities		(719)	(719)		(368)	(368)
Total Interest-bearing Liabilities	**(789)**	**(5,919)**	**(6,708)**	**(2,826)**	**(4,014)**	**(6,840)**
Change in Net Interest Income	**$ 3,359**	**$ (5,161)**	**$ (1,802)**	**$ (4,446)**	**$ (4,527)**	**$ (8,973)**

(1) *The change in interest due to both volume and rate has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.*

(2) *Tax-exempt income is on a fully taxable-equivalent basis, including the dividend-received deduction for equity securities, using the statutory federal corporate income tax rate of 35 percent for 2012, 2011 and 2010.*

Net interest income and net interest margin decreased by $1.8 million or 26 basis points compared to 2011. The low interest rate environment was a challenge to our net interest income in 2012, as earning assets rates reset faster than our ability to offset those decreases on the funding side.

Interest income decreased $8.5 million to $160.7 million in 2012 compared to $169.2 million in 2011. Rates decreased on almost all earning asset categories due to the low interest rate environment. The decrease in net interest income was primarily driven by a 29 basis point decrease in average loan yields to 4.59 percent compared to 4.88 percent in 2011. Average loan balances were relatively unchanged with a decline of $3.8 million despite the addition of approximately $143.0 million of average loans related to the acquisitions of Mainline and Gateway. Loans from acquisitions were offset by significant loan payoffs throughout the past two years, primarily in our commercial loan portfolio. We retained more residential mortgage loans in the portfolio during the year, rather than selling them in the secondary market. Average investments increased $51.8 million compared to the prior year; however, due to declining yields interest income was essentially unchanged. The interest-bearing balance with banks is primarily funds held at the Federal Reserve and increased $166.2 million, or 134.4 percent, during 2012 due to a lack of organic loan growth. Overall, the fully taxable-equivalent yield on total interest-earning assets decreased 48 basis points to 4.10 percent in 2012 as compared to 4.58 percent in 2011.

Interest expense decreased $6.7 million to $21.0 million for 2012 compared to $27.7 million for 2011. The primary driver of the decrease in interest expense was the maturities of higher costing CDs. For 2012, average interest-bearing deposits increased by $143.7 million to $2.6 billion as compared to $2.5 billion 2011. The increase in average interest-bearing deposits is attributed to a

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

$141.6 million average balance increase in savings deposits and a $79.6 million average balance increase in interest-bearing demand and money market accounts, partially offset by an average balance decrease of $77.6 million in CDs. The increase in deposits includes the addition of $171.0 million in average deposits related to the acquisitions of Mainline and Gateway. The cost of deposits was 0.48 percent, a decrease of 22 basis points from 2011 primarily due to CDs maturing and being replaced by demand and other lower interest rate deposits. The cost of long-term borrowed funds decreased 64 basis points, to 3.23 percent from 3.87 percent in 2011. However, the cost of securities sold under repurchase agreements, or REPOs, and other short-term borrowed funds increased 8 basis points to 0.21 percent as a result of increased utilization of more expensive short-term borrowings compared to customer repos. Overall, the yield on interest-bearing liabilities decreased 31 basis points to 0.74 percent for 2012 as compared to 2011.

Provision for Loan Losses

The provision for loan losses is the amount to be added to the ALL after adjusting for charge-offs and recoveries to bring the ALL to a level considered appropriate to absorb probable losses inherent in the loan portfolio. The provision for loan losses increased $7.2 million to $22.8 million for 2012 compared to $15.6 million for 2011. Net charge-offs were $25.2 million or 0.78 percent of average loans in 2012, compared to $18.2 million or 0.56 percent of average loans in 2011. During the first half of 2012, we experienced elevated charge-offs primarily in our commercial construction loan portfolio as projects in this portfolio slowed due to the economic environment and as a result, appraised values declined. Refer to the Allowance for Loan Losses section of this Management s Discussion and Analysis of Financial Condition and Results of Operations, or MD&A, for further details.

Noninterest Income

Years Ended December 31 *(in thousands)*	**2012**	**2011**	**$ Change**
Security gains (losses), net	$ 3,016	$ (124)	$ 3,140
Debit and credit card fees	11,134	10,889	245
Service charges on deposit accounts	9,992	9,978	14
Wealth management fees	9,808	8,180	1,628
Insurance fees	8,448	8,314	134
Mortgage banking	2,878	1,199	1,679
Other Income:			
Interest rate swap fees	1,036		1,036
Other	5,600	5,621	(21)
Total Other Noninterest Income	6,636	5,621	1,015
Total Noninterest Income	**$ 51,912**	**$ 44,057**	**$ 7,855**

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Noninterest income increased $7.9 million in 2012 compared to 2011, with increases in almost all noninterest income categories. The primary drivers were gains on sales of securities, as well as increased fees from wealth management, mortgage banking and interest rate swap fee income.

The $3.1 million increase in security gains relates to the sales of two equity positions during the year as a result of increases in value after merger announcements. Mortgage interest rates remained at very attractive levels throughout 2012 driving strong customer demand. As a result, we experienced an increase of $1.7 million in mortgage banking fee activity in 2012 compared to the prior year. During 2012, we sold $82.9 million of 1-4 family mortgage loans to Fannie Mae compared to $67.9 million in 2011 which increased fees by $0.5 million. Additionally, in 2011 we recorded an impairment charge related to mortgage servicing rights of $0.4 million that reflected a decline in the remaining value of the mortgage servicing asset compared to no impairment in 2012. The remaining increase in mortgage banking activity primarily related to a net gain on our mortgage derivative due to a strong mortgage pipeline at the end of 2012 compared to a decrease in 2011. During the fourth quarter of 2012, we began to retain 20 year mortgages within the loan portfolio which were previously priced and underwritten using secondary market terms and guidelines. This retention of 20 year mortgages is in addition to the 10 and 15 year mortgages which we have been retaining in the portfolio since the second quarter of 2011.

Wealth management fees increased $1.6 million due to improved brokerage business of $0.8 million as a result of adding new producers and our trust income increased $0.6 million due to an increase in assets under management of $201.0 million compared to the prior year.

Interest rate swap fees have increased $1.0 million compared to the prior year as our customers have opted to lock in low interest rates for longer terms.

Noninterest Expense

Years Ended December 31 *(in thousands)*	**2012**	**2011**	**$ Change**
Salaries and employee benefits[(1)]	$ 57,920	$ 51,078	$ 6,842
Data processing[(1)]	7,326	6,853	473
Net occupancy[(1)]	7,603	6,943	660
Professional services and legal[(1)]	4,610	5,437	(827)
Furniture and equipment	5,262	4,941	321
Marketing[(1)]	3,206	3,019	187
Other taxes	3,200	3,381	(181)
FDIC assessment	2,926	3,570	(644)
Merger related expense	5,968		5,968
Other expenses:			
Joint venture amortization	4,199	3,302	897
Other real estate owned	2,166	1,518	648
Unfunded loan commitments	1,811	(1,474)	3,285
Amortization of intangibles	1,709	1,737	(28)
Other[(1)]	14,957	13,603	1,354
Total Other Noninterest Expense	24,842	18,686	6,156
Total Noninterest Expense	**$ 122,863**	**$ 103,908**	**$ 18,955**

(1) *Excludes one-time merger related expenses for 2012.*

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

We had an increase of $19.0 million in noninterest expense in 2012, compared to 2011, with the largest increases in salaries and employee benefits and one-time merger related expenses.

During the first quarter of 2012, we acquired Mainline Bancorp, Inc., an eight branch institution headquartered in Ebensburg, Pennsylvania and during the third quarter of 2012, we acquired Gateway Bank, a two branch institution headquartered in McMurray, Pennsylvania. In 2012, we incurred one-time merger related expenses of $2.3 million of change in control, severance and other employee costs, $2.3 million in data processing contract termination fees, $1.0 million for professional and legal fees and $0.4 million of other expenses. We expect to incur approximately $1.2 million of additional merger related expenses related to the conversion of Gateway Bank into S&T Bank on February 8, 2013.

Excluding one-time merger related expenses, salaries and employee benefits increased by $6.8 million, or 13.4 percent, compared to 2011. Approximately $2.3 million of the increase related to additional employees added as a result of the acquisitions. We added 53 former Mainline employees to our staff in March 2012 and 19 former Gateway employees in August 2012. Further increasing salary expenses in 2012 were annual merit increases of approximately $1.7 million. Our pension expense increased $2.0 million in 2012 due to an increase in our pension liability as a result of a significant decrease of 100 basis points in our discount rate from the prior year. Payroll incentives and commissions increased $0.4 million due to increased production in areas including wealth management and mortgage banking.

Excluding one-time merger related expenses, data processing expenses increased by $0.5 million, primarily due to $0.3 million related to an increased customer processing base due to the acquisitions and an additional $0.2 million related to an upgrade to our Wealth Management data processing system. Net occupancy expenses increased by $0.7 million due to the addition of 10 branches from the acquisitions.

We invest in partnerships that provide federal income tax benefits through tax credits. The partnerships are amortized over the life of the expected tax credits. Joint venture amortization increased by $0.9 million year over year due to three new projects going into service during 2012. Further, we recorded impairment charges of $0.3 million during the year where the benefit of the tax credits had been fully utilized and no future benefits were expected to be realized.

We did see decreases in several expense categories. Excluding one-time merger related expenses, legal and professional expense decreased by $0.8 million, due in part to one-time legal and accounting fees incurred in early 2011. FDIC expense decreased by $0.6 million as we benefited from a lower FDIC assessment based on the revisions made by the FDIC that went into effect April 1, 2011.

Within other noninterest expense, the reserve for unfunded loan commitments increased $3.3 million as a result of increased volume in our construction commitments coupled with higher historical loss rates. In the prior year we had a reversal of $1.5 million of unfunded loan commitments. The reversal in 2011 was primarily attributable to the decline in commitments at that time. Additionally, $0.8 million of the reserve reversal in 2011 related to an expense recognized in 2008 for a letter of credit that we were contractually obligated to fulfill. During 2011, the letter of credit was drawn upon and funded and a corresponding loan charge-off was recorded. We also had an increase of $0.6 million in other real estate owned, or OREO, expense, primarily due to two properties that were sold during 2012 at values significantly below the appraised values, as well as increases in selling expenses pertaining to these properties.

Our efficiency ratio, which measures noninterest expense as a percent of noninterest income plus net interest income, on a fully taxable-equivalent basis, excluding security gains/losses, was 65 percent for 2012, including the one-time merger related expenses of $6.0 million, and 56 percent for 2011. Refer to page 57 Explanation of Use of Non-GAAP Financial Measures for a discussion of this non-GAAP financial measure.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Federal Income Taxes

We recorded a federal income tax provision of $7.3 million in 2012 compared to $14.6 million in 2011. The effective tax rate, which is the provision for income taxes as a percentage of pretax income was 17.5 percent in 2012 compared to 23.6 percent in 2011. The effective tax rate decreased due to tax-exempt income and tax credits remaining relatively constant on a declining pre-tax income. We ordinarily generate an annual effective tax rate that is less than the statutory rate of 35 percent due to benefits resulting from tax-exempt interest, excludable dividend income, tax-exempt interest on bank owned life insurance, or BOLI and tax benefits associated with Low Income Housing Tax Credits, or LIHTC, and Federal Historic Tax Credit Projects.

Results of Operations

Year Ended December 31, 2011

Net Income

Net income available to common shareholders for 2011 was $39.7 million resulting in diluted earnings per common share of $1.41 compared to $37.3 million or $1.34 diluted earnings per common share in 2010. The increase in net income was primarily a result of a reduction of $13.9 million in provision for loan losses, partially offset with decreases of $8.5 million in net interest income and $3.2 million in noninterest income.

Return on Equity and Assets

The table below presents our consolidated profitability and common equity to asset ratio for each of the last three years:

Years Ended December 31	**2011**	**2010**	**2009**
Common return on average assets	0.97%	0.90%	0.05%
Common return on average equity	6.78%	6.58%	0.37%
Dividend payout ratio	42.44%	44.75%	1247.64%
Common equity to asset ratio	11.91%	11.48%	10.74%

Net Interest Income

The interest income on interest-earning assets and the net interest margin are presented on a fully taxable-equivalent basis. The fully taxable-equivalent basis adjusts for the tax benefit of income on certain tax-exempt loans and investments using the federal statutory tax rate of 35 percent for each period. We believe this measure to be the preferred industry measurement of net interest income that provides a relevant comparison between taxable and non-taxable amounts.

The following table reconciles interest income per the Consolidated Statements of Net Income to net interest income adjusted to a fully taxable-equivalent basis:

Years Ended December 31 *(in thousands)*	**2011**	**2010**	**2009**
Interest income per Consolidated Statements of Net Income	$ 165,079	$ 180,419	$ 195,087
Adjustment to fully taxable-equivalent basis	4,154	4,627	5, 202
Interest income adjusted to fully taxable-equivalent basis	169,233	185,046	200,289
Interest expense per Consolidated Statements of Net Income	27,733	34,573	49,105
Net Interest Income Adjusted to Fully Taxable-equivalent Basis (non-GAAP)	**$ 141,500**	**$ 150,473**	**$ 151,184**

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Average Balance Sheet and Net Interest Income Analysis

The following table provides information regarding the average balances, interest and yields earned on interest-earning assets and the average balances, interest and rates paid on interest-bearing liabilities:

December 31 *(dollars in thousands)*	2011 Average Balance	2011 Interest	2011 Yield/ Rate	2010 Average Balance	2010 Interest	2010 Yield/ Rate	2009 Average Balance	2009 Interest	2009 Yield/ Rate
ASSETS									
Loans*(1)(2)*	$ 3,216,856	$ 156,845	4.88%	$ 3,386,103	$ 172,319	5.09%	$ 3,473,169	$ 182,767	5.26%
Taxable investment securities	273,320	8,475	3.10%	226,714	8,373	3.69%	286,295	11,897	4.16%
Tax-exempt investment securities[2]	62,607	3,611	5.77%	76,707	4,354	5.68%	103,832	5,624	5.42%
Federal Home Loan Bank stock	20,091		%	23,336		%	23,542		%
Interest-bearing balance with banks	123,714	302	0.24%	49		0.34%	54		0.17%
Federal funds sold			%			%	258	1	0.25%
Total Interest-earning Assets	**3,696,588**	**169,233**	**4.58%**	**3,712,909**	**185,046**	**4.98%**	**3,887,150**	**200,289**	**5.15%**
Noninterest-earning assets:									
Cash and due from banks	50,458			90,462			67,405		
Premises and equipment, net	38,425			39,142			41,915		
Other assets	344,378			340,234			320,803		
Less allowance for loan losses	(57,241)			(59,292)			(57,985)		
Total Assets	**$ 4,072,608**			**$ 4,123,455**			**$ 4,259,288**		
LIABILITIES AND SHAREHOLDERS EQUITY									
Interest-bearing liabilities:									
Interest-bearing demand and money market	$ 536,085	$ 739	0.14%	$ 518,383	$ 1,220	0.24%	$ 485,742	$ 1,616	0.33%
Savings	761,274	1,267	0.17%	749,325	2,127	0.28%	758,216	3,465	0.46%
Certificates of deposit	1,181,823	20,946	1.77%	1,300,803	25,370	1.95%	1,367,372	33,358	2.44%
Federal funds purchased			%			%	115	1	0.79%
Securities sold under repurchase agreements	41,584	53	0.13%	46,490	64	0.14%	86,616	140	0.16%
Short-term borrowings	551	2	0.32%	32,473	146	0.45%	104,217	544	0.52%
Long-term borrowings	31,651	1,091	3.45%	42,920	1,643	3.83%	127,045	5,568	4.38%
Junior subordinated debt securities	90,619	3,635	4.01%	90,619	4,003	4.42%	90,619	4,413	4.38%
Total Interest-bearing Liabilities	**2,643,587**	**27,733**	**1.05%**	**2,781,013**	**34,573**	**1.24%**	**3,019,942**	**49,105**	**1.63%**
Noninterest-bearing liabilities:									
Noninterest-bearing demand	792,911			728,708			637,434		
Other liabilities	50,924			47,064			57,377		
Shareholders equity	585,186			566,670			544,535		
Total Liabilities and Shareholders Equity	**$ 4,072,608**			**$ 4,123,455**			**$ 4,259,288**		
Net Interest Income		**$ 141,500**			**$ 150,473**			**$ 151,184**	
Net Yield on Interest-earning Assets			**3.83%**			**4.05%**			**3.89%**

(1) *For the purpose of these computations, nonaccruing loans are included in the daily average loan amounts outstanding.*

(2) *Tax-exempt income is on a fully taxable-equivalent basis, including the dividend-received deduction for equity securities, using the statutory federal corporate income tax rate of 35 percent for 2011, 2010 and 2009.*

39

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

The following table presents a summary of the changes in interest earned and interest paid resulting from changes in average balance and changes in rates:

	2011 Compared to 2010 Increase (Decrease) Due to(1)			2010 Compared to 2009 Increase (Decrease) Due to(1)		
(in thousands)	Volume	Rate	Net	Volume	Rate	Net
Interest earned on:						
Loans(2)	$ (8,613)	$ (6,861)	$ (15,474)	$ (4,581)	$ (5,867)	$ (10,448)
Taxable investment securities	1,722	(1,620)	102	(2,476)	(1,048)	(3,524)
Tax-exempt investment securities(2)	(800)	57	(743)	(1,469)	199	(1,270)
Interest bearing balance with bank	419	(117)	302			
Other investments						
Federal funds sold				(1)		(1)
Total Interest-earning Assets	**(7,272)**	**(8,541)**	**(15,815)**	**(8,527)**	**(6,716)**	**(15,243)**
Interest paid on:						
Interest-bearing demand and money market	$ 42	$ (523)	$ (481)	$ 109	$ (505)	$ (396)
Savings deposits	34	(894)	(860)	(41)	(1,297)	(1,338)
Certificates of deposit	(2,321)	(2,103)	(4,424)	(1,624)	(6,364)	(7,988)
Federal funds purchased				(1)		(1)
Securities sold under repurchase agreements	(7)	(4)	(11)	(65)	(11)	(76)
Short-term borrowings	(143)	(1)	(144)	(374)	(24)	(398)
Long-term borrowings	(431)	(121)	(552)	(3,687)	(238)	(3,925)
Junior subordinated debt securities		(368)	(368)		(410)	(410)
Total Interest-bearing Liabilities	**(2,826)**	**(4,014)**	**(6,840)**	**(5,683)**	**(8,849)**	**(14,532)**
Change in Net Interest Income	**$ (4,446)**	**$ (4,527)**	**$ (8,973)**	**$ (2,844)**	**$ 2,133**	**$ (711)**

(1) *The change in interest due to both volume and rate has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.*

(2) *Tax-exempt income is on a fully taxable-equivalent basis, including the dividend-received deduction for equity securities, using the statutory federal corporate income tax rate of 35 percent for 2011, 2010 and 2009.*

On a fully taxable-equivalent basis, net interest income decreased by $9.0 million in 2011 compared to 2010. The decline in the net interest margin from 4.05 percent in 2010 to 3.83 percent in 2011 is a result of loan repricing and replacement volume at lower rates and an unfavorable shift in asset mix, offset in part by lower rates paid on deposits and a better funding mix between deposits, including noninterest-bearing demand deposits and borrowings.

The shift in asset mix during 2011 is primarily reflected by the $169.2 million decrease in average loans and an increase in average interest-bearing balance with banks of $123.7 million. The interest-bearing balance with banks is primarily funds held at the Federal Reserve and had increased during 2011 as a result of loan pay downs and weak demand for new loans. The yield on average loans and taxable investment securities decreased 21 basis points and 59 basis points, respectively. Overall, the fully taxable-equivalent yield on total interest-earning assets decreased 40 basis points to 4.58 percent in 2011 as compared to 4.98 percent in 2010.

For 2011, average interest-bearing deposits decreased by $89.3 million to $2.5 billion as compared to $2.6 billion in 2010. The decrease in average interest-bearing deposits is attributed to a $119.0 million average balance decrease in CDs, primarily in brokered CDs. The cost of deposits totaled 0.93 percent, a decrease of 19 basis points from 2010 due to lower rates paid on deposits. The cost of securities sold under repurchase agreements, or REPOs, and other short-term borrowed funds decreased 14 basis points to 0.13 percent as a result of lower short-term rates as compared to 2010. Overall, the yield on interest-bearing liabilities decreased 19 basis points to 1.05 percent for 2011 as compared to 2010.

40

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Positively affecting net interest income was a $121.2 million increase in average net free funds during 2011, as compared to 2010. Average net free funds are the excess of noninterest-bearing demand deposits, other noninterest-bearing liabilities and shareholders equity over noninterest-earning assets. The largest driver of the increase in net free funds was an increase in noninterest-bearing demand deposit average balances, which is a result of limited investment options available to our customers in the low rate environment.

Provision for Loan Losses

The provision for loan losses is the amount to be added to the ALL after adjusting for charge-offs and recoveries to bring the ALL to a level considered appropriate to absorb probable losses inherent in our loan portfolio. The provision for loan losses decreased to $15.6 million for 2011 compared to $29.5 million for 2010. The substantial decrease in provision for loan losses was a result of the overall improving economic conditions from the prior year and a significant decrease in net charge-offs. Net charge-offs decreased to $18.2 million, 0.56 percent of average loans in 2011 from $37.7 million or 1.11 percent of average loans in 2010 as overall asset quality improved during 2011. Refer to the Allowance for Loan Losses section of this MD&A for further details.

Noninterest Income

Years Ended December 31 *(in thousands)*	**2011**	**2010**	**$ Change**
Security gains (losses), net	$ (124)	$ 274	$ (398)
Debit and credit card fees	10,889	9,954	935
Service charges on deposit accounts	9,978	11,178	(1,200)
Insurance fees	8,314	8,312	2
Wealth management fees	8,180	7,808	372
Mortgage banking	1,199	3,403	(2,204)
Other income:			
Commercial rate swap	(38)	96	(134)
Rabbi trust	(41)	200	(241)
Derivative fee income		136	(136)
Other	5,700	5,849	(149)
Total Other Noninterest Income	5,621	6,281	(660)
Total Noninterest Income	**$ 44,057**	**$ 47,210**	**$ (3,153)**

We experienced a decline of $3.2 million in our noninterest income in 2011 primarily as a result of regulatory changes and declining volumes in our mortgage banking area.

Service charges on deposit accounts decreased $1.2 million primarily relating to the impacts of Regulation E, which requires customers with existing accounts to opt in for overdraft coverage of certain types of electronic banking activities. Regulation E caused service charge income to decrease by $1.8 million in 2011, which we offset in part by the introduction of a new paper statement fee in August 2011. Paper statement fees generated $0.5 million in revenue in 2011. We expect customers to continue to elect to receive electronic bank statements; therefore it is expected that paper statement fee income will decline in future periods.

Mortgage banking includes fee income related to loans sold in the secondary market, mortgage servicing income and fair value adjustments associated with valuing mortgage derivatives. Although interest rates continue to be low, the volume of loan sales in the secondary market have decreased

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

resulting in a $2.2 million decrease in mortgage banking income. During 2011, we sold $67.9 million of 1-4 family mortgage loans to Fannie Mae compared to $109.3 million in 2010 which resulted in a fee reduction of $0.9 million. In the second quarter of 2011, we began to retain within the loan portfolio 10 and 15 year mortgages which had previously been priced and underwritten using secondary market terms and guidelines. Additionally, we recorded higher impairment charges on our mortgage servicing asset in 2011 compared to 2010. This impairment charge reflects a decline in the value of the remaining mortgage servicing rights due to increased prepayment speeds resulting from decreases in interest rates.

We recognized $0.1 million in security losses in 2011 related to OTTI on two equity securities compared to realized gains of $0.3 million in the prior year. In the prior year, OTTI was not significant and we experienced gains as we sold several of our equity positions.

The decreases in noninterest income are partially offset by increases of $0.9 million in debit and credit card fees and $0.4 million in wealth management fees. Debit and credit card fees have increased $0.9 million in 2011 as a result of increased volume and successful marketing campaigns around signature based debit card transactions throughout 2011. Our wealth management fees increased $0.4 million from the prior year. We experienced increased fee income of $0.2 million as our customers moved to fixed annuities in this low interest rate environment. Additionally, wealth management fees were positively impacted by improving market conditions in 2011.

Noninterest Expense

Years Ended December 31 *(in thousands)*	**2011**	**2010**	**$ Change**
Salaries and employee benefits	$ 51,078	$ 48,715	$ 2,363
Net Occupancy	6,943	6,928	15
Data processing	6,853	6,145	708
Professional services and legal	5,437	6,889	(1,452)
Furniture and equipment	4,941	5,054	(113)
FDIC assessment	3,570	5,426	(1,856)
Other taxes	3,381	3,432	(51)
Joint venture amortization	3,302	2,573	729
Marketing	3,019	2,795	224
Other expenses:			
Amortization of intangibles	1,737	1,943	(206)
Other real estate owned	1,518	1,921	(403)
Loan collection fees	624	1,770	(1,146)
Unfunded loan commitments	(1,474)	(1,555)	81
Other	12,979	13,597	(618)
Total Other Noninterest Expense	15,384	17,676	(2,292)
Total Noninterest Expense	**$ 103,908**	**$ 105,633**	**$ (1,725)**

We had a slight decline in noninterest expense of $1.7 million during 2011. This was primarily a result of certain one-time expenses in 2010 and a significant decrease in our FDIC assessment in 2011.

The decrease in professional services and legal expense is due to $2.3 million of legal settlement costs that occurred in the first and second quarters of 2010. The decrease in the FDIC assessment of $1.9 million is the result of the FDIC changing the methodology used to calculate the assessment as of

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

April 1, 2011 and the expiration of the FDIC s Transaction Account Guarantee Program on December 31, 2010. Asset quality improved throughout 2011 resulting in $1.1 million less in loan collection fees. While these expenses have declined from the prior year, we expect to continue to experience elevated costs in this area as our criticized and classified loans remain above historic averages. For the year ended December 31, 2011, $1.5 million of unfunded loan commitments was reversed compared to $1.6 million for the year ended December 31, 2010. The reversal of the reserve is primarily attributable to the decline in available commitments. Additionally, $0.8 million of the reserve reversal in 2011 related to an expense recognized in 2008 for a letter of credit that we were contractually obligated to fulfill. During the third quarter of 2011, the letter of credit was drawn upon and funded and a corresponding loan charge-off was recorded. Other noninterest expense decreased $0.6 million primarily related to a $1.2 million write-off of an uncollectible receivable in the third quarter of 2010. The receivable related to expenses for a mutual fund advised by an affiliate.

We had a $2.4 million increase in salaries and employee benefits primarily due to the full year impact of our annual merit increase resulting in additional salary expense of $1.0 million for 2011. Additionally, restricted stock expense increased $0.7 million related to the 2010 incentive plan and a newly implemented long-term incentive plan. Incentive plans were re-instituted in 2010 which impacted the 2011 expense. Deferred loan origination costs are down by $0.9 million from 2010, which increases salaries and employee benefits in the current period since we are deferring less costs. These increases were offset by a decrease in the pension plan expense of $0.3 million due to a change in the number of participants in the plan. We do not expect to see a similar decrease in pension expense in 2012 as a result of a significant increase in our pension liability due to a decline in the discount rate of 100 basis points to 4.75%.

The $0.7 million in additional data processing costs relate to one-time charges for the implementation of mobile banking and other system conversion fees. The increase of $0.7 million in joint venture amortization reflects the addition of two low income housing projects that were completed in 2011.

Our efficiency ratio, which measures noninterest expense as a percent of noninterest income plus net interest income, on a fully taxable-equivalent basis, excluding security gains/losses, was 56 percent for 2011 and 54 percent for 2010. Refer to page 57 Explanation of Use of Non-GAAP Financial Measures for a discussion of this non-GAAP financial measure.

Federal Income Taxes

We recorded a federal income tax provision of $14.6 million in 2011 compared to $14.4 million in 2010. The effective tax rate, which is the provision for income taxes as a percentage of pre-tax income was 23.6 percent compared to 25.0 percent in 2010. We ordinarily generate an annual effective tax rate that is less than the statutory rate of 35 percent due to benefits resulting from tax-exempt interest, excludable dividend income, tax-exempt interest on BOLI and tax benefits associated with LIHTC, and Federal Historic Tax Credit Projects, which are relatively consistent regardless of the level of pretax income.

Financial Condition

December 31, 2012

Our total assets of $4.5 billion have increased by $406.7 million since December 31, 2011. The acquisition of Mainline and Gateway added $368.5 million in assets. Total gross loans increased $216.9 million to $3.3 billion at December 31, 2012 compared to $3.1 billion at

December 31, 2011. Our commercial loan portfolio has grown by $121.8 million to $2.4 billion or by 5.3 percent and our consumer loan portfolio has increased by $95.1 million to $935.0 million or by 11.3 percent, due primarily to the two acquisitions. We did begin to see organic loan growth in the later part of

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

2012. Our loan pay downs were significant throughout 2012, primarily in our commercial loan portfolio. Due to lack of loan growth, we increased our securities by $95.5 million and excess cash held at the Federal Reserve by $42.5 million. Our core deposit base remains strong with total deposits of $3.6 billion at December 31, 2012, a $302.6 million, or 9.1 percent increase since December 31, 2011. Our acquisitions added $311.4 million of deposits. We did see an improvement in our mix of deposits throughout 2012, with a decrease in CDs offset by increases in demand, money market and savings accounts.

Securities Activity

December 31 *(in thousands)*	**2012**	**2011**	**2010**
Obligations of U.S. government corporations and agencies	$ 212,066	$ 142,786	$ 125,675
Collateralized mortgage obligations of U.S. government corporations and agencies	57,896	65,395	41,491
Mortgage-backed securities of U.S. government corporations and agencies	60,781	48,752	43,991
Obligations of states and political subdivisions	112,767	88,805	65,772
Marketable equity securities	9,586	11,858	11,096
Total Securities Available-for-Sale	**$ 453,096**	**$ 357,596**	**$ 288,025**

We invest in various securities in order to provide a source of liquidity, to satisfy various pledging requirements, increase net interest income and as a tool of the ALCO to reposition the balance sheet for interest rate risk purposes. Securities are subject to market risks that could negatively affect the level of liquidity available to us. Risks associated with various securities portfolios are managed and monitored through investment policies which are annually approved by our Board of Directors and administered through ALCO and our treasury function.

The securities portfolio increased $95.5 million, or 26.7 percent, from December 31, 2011. The increase is due to the redeployment of deposits at banks which increased substantially as a result of our acquisitions and lack of organic growth. Additionally, we sold $5.7 million of equity securities since December 31, 2011 that resulted in a $3.0 million gain.

During 2012, 2011 and 2010, we did not record any significant OTTI. The performance of the debt and equity securities markets could generate impairment in future periods requiring realized losses to be reported.

At December 31, 2012, net unrealized gains on securities classified as available-for-sale were approximately $16.0 million as compared to $14.9 million at December 31, 2011. Net unrealized gains related to our debt securities portfolio totaled $14.9 million at December 31, 2012 and $13.2 million at December 31, 2011. The increase in unrealized gains related to debt securities is due to decreases in interest rates. The marketable equity securities portfolio had net unrealized gains of $1.1 million at December 31, 2012 compared to net unrealized gains of $1.7 million at December 31, 2011. At December 31, 2012, we had no securities that were in an unrealized loss position for greater than 12 months. We do not intend to sell and it is not likely that we will be required to sell any of the securities in an unrealized loss position before recovery of its amortized cost.

At December 31, 2012 and 2011, we held Federal Home Loan Bank, or FHLB, stock of $14.5 million and $18.2 million, respectively. This investment is carried at cost and evaluated for impairment based on the ultimate recoverability of the par value. We hold FHLB stock because we are a member of the FHLB of Pittsburgh. The FHLB requires members to purchase and hold a specified level of FHLB stock based upon on the members asset value, level of borrowings and participation in other programs offered. Stock in the FHLB is non-marketable and is redeemable at the discretion of

44

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

the FHLB. Members do not purchase stock in the FHLB for the same reasons that traditional equity investors acquire stock in an investor-owned enterprise. Rather, members purchase stock to obtain access to the low-cost products and services offered by the FHLB. Unlike equity securities of traditional for-profit enterprises, the stock of the FHLB does not provide its holders with an opportunity for capital appreciation because, by regulation, FHLB stock can only be purchased, redeemed and transferred at par value.

On February 22, 2012, the FHLB of Pittsburgh announced that it would pay a dividend on the average capital stock balance held during the three month period ended December 31, 2011 at an annualized rate of 0.10% for the first time since late 2008. The FHLB noted future dividend payments and capital stock repurchases will continue to be reviewed on a quarterly basis. We had $5.7 million of redemptions from the FHLB throughout 2012. We reviewed and evaluated the FHLB capital stock for OTTI at December 31, 2012. Based upon our review of the FHLB s current financial position, they reported improved earnings throughout 2012 compared to 2011 and continue to exceed all capital ratios required. Additionally, we considered that the FHLB began paying dividends and redeeming excess stock during 2012. Accordingly, we believe sufficient evidence exists to conclude that no OTTI exists at December 31, 2012.

The following table sets forth the maturities of securities at December 31, 2012 and the weighted average yields of such securities. Taxable-equivalent adjustments (using a 35 percent federal income tax rate) for 2012 have been made in calculating yields on obligations of state and political subdivisions.

	Maturing								
	Within One Year		After One But Within Five Years		After Five But Within Ten Years		After Ten Years		No Fixed Maturity
(dollars in thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount
Available-for-Sale									
Obligations of U.S. government corporations and agencies	$ 30,562	2.00%	$ 125,266	1.62%	$ 52,644	1.47%	$ 3,594	0.72%	$
Collateralized mortgage obligations of U.S. government corporations and agencies		%	5,040	4.61%		%	52,856	2.52%	
Mortgage-backed securities of U.S. government corporations and agencies		%	149	4.19%	17,747	2.66%	42,885	3.41%	
Obligations of states and political subdivisions	8,408	5.38%	8,926	5.70%	13,863	3.94%	81,571	4.59%	
Marketable equity securities		%		%		%		%	9,585
Total	**$ 38,970**		**$ 139,381**		**$ 84,254**		**$ 180,906**		**$ 9,585**
Weighted Average Rate		**2.73%**		**1.99%**		**2.13%**		**3.63%**	

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Lending Activity

The following table summarizes our loan distribution at the end of each of the last five years:

	2012		2011		2010		2009		2008	
December 31 *(dollars in thousands)*	**Amount**	**% of Total**	**Amount**	**% of Total**	**Amount**	**% of Total**	**Amount**	**% of Total**	**Amount**	**% of Total**
Commercial										
Commercial real estate	$ 1,452,133	43.39%	$ 1,415,333	45.22%	$ 1,494,202	44.53%	$ 1,428,329	42.03%	$ 1,440,200	40.36%
Commercial and industrial	791,396	23.65%	685,753	21.91%	722,359	21.52%	701,650	20.65%	822,543	23.05%
Commercial construction	168,143	5.02%	188,852	6.04%	259,598	7.74%	359,342	10.57%	361,910	10.14%
Total Commercial Loans	**2,411,672**	**72.06%**	**2,289,938**	**73.17%**	**2,476,159**	**73.79%**	**2,489,321**	**73.25%**	**2,624,653**	**73.55%**
Consumer										
Home equity	431,335	12.89%	411,404	13.14%	441,096	13.15%	458,643	13.49%	438,380	12.28%
Residential mortgage	427,303	12.77%	358,846	11.47%	359,536	10.71%	357,393	10.52%	408,603	11.45%
Installment and other consumer	73,875	2.21%	67,131	2.14%	74,780	2.23%	81,141	2.39%	84,065	2.36%
Consumer construction	2,437	0.07%	2,440	0.08%	4,019	0.12%	11,836	0.35%	13,014	0.36%
Total Consumer Loans	**934,950**	**27.94%**	**839,821**	**26.83%**	**879,431**	**26.21%**	**909,013**	**26.75%**	**944,062**	**26.45%**
Total Portfolio Loans	**$ 3,346,622**	**100%**	**$ 3,129,759**	**100%**	**$ 3,355,590**	**100%**	**$ 3,398,334**	**100%**	**$ 3,568,715**	**100%**

The loan portfolio represents the most significant source of interest income for us. The risk that borrowers will be unable to pay such obligations is inherent in the loan portfolio. Other conditions such as the overall economic climate can significantly impact the borrower s ability to pay.

At December 31, 2012 our total loans were $3.3 billion, a $216.9 million increase compared to the prior year. The overall composition of the loan portfolio did not change significantly from the prior year. The Mainline and Gateway acquisitions added $228.6 million in loans during 2012, which was a mix of both consumer and commercial loans. Organic loan growth was challenging during the year and we did experience significant loan pay downs, primarily in our commercial loan portfolio. We did see positive trends in our loan portfolio in the later part of 2012 with increased customer demand.

In August 2012, we expanded our commercial lending footprint into Northeastern Ohio through the opening of a loan production office in Akron. We are retaining 10, 15 and 20 year residential real estate loans in our portfolio, rather than selling these loans in the secondary market. Additionally, we are hiring seasoned lenders in both our commercial and residential real estate areas to improve organic loan growth.

Commercial loans, including commercial real estate, or CRE, commercial and industrial, or C&I, and commercial construction, comprised 72 percent and 73 percent of total portfolio loans at December 31, 2012 and 2011, respectively. Although commercial loans can have a relatively higher risk profile, management believes these risks are mitigated through active portfolio management, conservative underwriting standards and continuous portfolio review. The loan-to-value policy guidelines for CRE loans are generally 65-85 percent. At December 31, 2012, variable rate commercial loans were 78 percent of the commercial loan portfolio as compared to 79 percent at December 31, 2011.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Home equity and residential mortgage loans comprised 26 percent of the loan portfolio in 2012 and 25 percent in 2011. Residential mortgage lending continues to be a strategic focus through a centralized mortgage origination department, ongoing product redesign, secondary market activities and the utilization of commission compensated originators. Management believes that continued adherence to our conservative mortgage lending policies for portfolio loans will be as important in a gradually growing economy as it was during the downturn in recent years. The loan-to-value policy guideline is 80 percent for residential first lien mortgages. Higher loan-to-value loans may be approved with the appropriate private mortgage insurance coverage. Portfolio loans permit a maximum term of 20 years for traditional mortgages. Balloon payment mortgages are also offered in the portfolio. The maximum balloon term is 15 years with a maximum amortization term of 30 years. Balloon mortgages with terms of 10 years or less may have a maximum amortization term for up to 40 years. Combo mortgage loans consisting of our residential first mortgage and home equity second mortgage are also available to credit-worthy borrowers. Second lien positions are assumed with home equity loans, but normally only to the extent that the combined credit exposure for both the first and second liens does not exceed 100 percent of the fair value of the property.

We also originate and price loans for sale into the secondary market, primarily to Fannie Mae. The rationale for these sales is to mitigate interest-rate risk associated with holding lower rate, long-term residential mortgages in the loan portfolio, generate fee revenue from sales and servicing and maintain the primary customer relationship. In 2011, we began to retain 10 and 15 year mortgages in our portfolio and just recently we began retaining the 20 year mortgages that had been priced and underwritten using secondary market terms and guidelines. During 2012 and 2011, we sold $82.9 million and $67.9 million, respectively, of 1 4 family mortgages to Fannie Mae and currently service $329.2 million of secondary market mortgage loans at December 31, 2012 compared to $332.6 million at December 31, 2011. Loans sold to Fannie Mae increased from the prior year due to the low interest rate environment and economic stabilization in our markets. We intend to continue to sell 30 year loans to Fannie Mae in the future, especially during periods of lower interest rates.

We offer a variety of unsecured and secured consumer loan and credit card products. Loan-to-value policy guidelines for direct loans are 90 100 percent of invoice for new automobiles and 80 90 percent of National Automobile Dealer Association, or NADA, value for used automobiles.

We maintain a General Lending Policy to control the quality of our loan portfolio. The policy delegates the authority to extend loans under specific guidelines and underwriting standards. The General Lending Policy is formulated by management and reviewed and ratified annually by the Board of Directors. Any exception to the General Lending Policy must be approved by the Senior Loan Committee or the Regional Loan Committee.

The following table presents the maturity of consumer and commercial loans outstanding as of December 31, 2012.

	Maturing			
(in thousands)	**Within One Year**	**After One But Within Five Years**	**After Five Years**	**Total**
Fixed interest rates	$ 121,611	$ 286,041	$ 122,421	$ 530,073
Variable interest rates	497,811	618,200	765,588	1,881,599
Total Commercial Loans	**$ 619,422**	**$ 904,241**	**$ 888,009**	**$ 2,411,672**
Fixed interest rates	69,390	253,681	301,491	624,562
Variable interest rates	217,794	25,844	66,750	310,388
Total Consumer Loans	**$ 287,184**	**$ 279,525**	**$ 368,241**	**$ 934,950**
Total Portfolio Loans	**$ 906,606**	**$ 1,183,766**	**$ 1,256,250**	**$ 3,346,622**

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Credit Quality

We have a Criticized Asset Committee that meets quarterly and monitors all special mention loans greater than $1.0 million and substandard loans greater than $0.5 million. Additional credit risk management practices include periodic review and updates to lending policies and procedures regarding sound underwriting practices and portfolio management expectations; a portfolio and loan stress testing initiative; and an independent loan review program developed to review underwriting decisions and adherence to policy, proper risk rating methodology and a review of all of our credit related business units. There can be no assurance that we will be successful in controlling the risk with these loans and consequently they could result in losses for us.

We determine loans to be impaired when based upon current information and events it is probable that we will be unable to collect all principal and interest payments due according to the original contractual terms of the loan agreement. All TDRs are classified as impaired loans. Impaired loans are continually monitored by our Managed Assets Division.

Nonperforming assets consist of nonaccrual loans, TDRs and OREO. The following represents nonperforming assets for the periods presented:

(dollars in thousands)	**2012**	**2011**	**2010**	**2009**	**2008**
Nonaccrual Loans					
Commercial real estate	$ 20,972	$ 20,777	$ 14,674	$ 52,380	$ 19,386
Commercial and industrial	5,496	7,570	2,567	7,489	3,341
Commercial construction	1,454	3,604	5,844	21,674	13,848
Home equity	3,312	2,936	1,433	2,252	174
Residential mortgage	4,526	2,859	5,996	5,583	5,624
Installment and other consumer	40	4	65	20	73
Consumer construction	218	181	525		
Total Nonaccrual Loans	**36,018**	**37,931**	**31,104**	**89,398**	**42,446**
Nonaccrual Troubled Debt Restructurings					
Commercial real estate	9,584	10,871	29,636	1,409	
Commercial and industrial	939		1,000		
Commercial construction	5,324	2,943	2,143		
Home Equity	341				
Residential mortgage	2,752	4,370			
Total Nonaccrual Troubled Debt Restructurings	**18,940**	**18,184**	**32,779**	**1,409**	
Total Nonperforming Loans	**54,958**	**56,115**	**63,883**	**90,807**	**42,446**
OREO	911	3,967	5,820	4,607	851
Total Nonperforming Assets	**$ 55,869**	**$ 60,082**	**$ 69,703**	**$ 95,414**	**$ 43,297**
Nonperforming loans as a percent of total loans	1.63%	1.79%	1.90%	2.67%	1.19%
Nonperforming assets as a percent of total loans plus OREO	1.66%	1.92%	2.07%	2.80%	1.21%

Nonperforming assets decreased 7.0 percent from the prior year as a result of resolution of several credits either through the foreclosure process and subsequent sale of the property or pay downs or payoffs of the loans. Additionally, our nonperforming loan formation was significantly less than the

48

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

prior year with encouraging trends in the second half of 2012. Our CRE portfolio continues to represent a significant amount of our nonperforming loans at 55% of our total nonperforming loans. There are no loans 90 days or more past due and still accruing.

TDRs are loans where we, for economic or legal reasons related to a borrower s financial difficulties, grant a concession to the borrower that we would not otherwise consider. Modifications to loans classified as TDR generally include reductions in contractual interest rates, principal deferment and extensions of maturity dates at a stated interest rate lower than the current market rate for a new loan with similar risk characteristics. Generally these concessions are for a period of at least six months. While unusual, there may be instances of loan principal forgiveness.

TDRs can be returned to accruing status if the following criteria are met: 1) the ultimate collectability of all contractual amounts due, according to the restructured agreement, is not in doubt and 2) there is a period of a minimum of six months of satisfactory payment performance by the borrower either immediately before or after the restructuring. We did not return any TDRs to accruing status during 2012.

All TDRs are considered to be impaired loans and will be reported as impaired loans for their remaining lives, unless the restructuring agreement specifies an interest rate equal to or greater than the rate that would be accepted at the time of the restructuring for a new loan with comparable risk and we fully expected that the remaining principal and interest will be collected according to the restructured agreement. All impaired loans are reported as nonaccrual loans unless the loan is a TDR that has met the requirements noted above to be returned to accruing status.

As an example consider a substandard commercial construction loan that is currently 90 days past due where the loan is restructured to extend the maturity date for a period longer than would be considered an insignificant period of time. The post-modification interest rate is not increased to correspond with the current credit risk of the borrower, and all other terms remain the same according to the original loan agreement. This loan will be considered a TDR as the borrower is experiencing financial difficulty and a concession has been granted. The loan will be reported as nonaccrual status and as an impaired loan and a TDR. In addition, the loan could be charged down to the fair value of the collateral if a confirmed loss exists. If the loan subsequently performs, by means of making on-time principal and interest payments according to the newly restructured terms for a period of six months, and it is expected that all remaining principal and interest will be collected according to the terms of the restructured agreement, the loan will be returned to accrual status and reported as an accruing TDR. The loan will remain an impaired loan for the remaining life of the loan since the interest rate was not adjusted to be equal to or greater than the rate that would be accepted at the time of the restructuring for a new loan with the comparable risk of a longer term.

As of December 31, 2012, we had $60.4 million in TDRs of which $41.5 million were accruing and $18.9 were in nonaccrual status. This compared to $67.9 million at December 31, 2011 of which $49.7 million were accruing and $18.2 million were in nonaccrual status. During 2012, none of the TDRs met the above requirements for being placed back into accrual status. The decrease in total TDRs from prior year is due to loan pay downs or pay offs and loan charge-offs. We did have $6.9 million of new TDRs related to our consumer loan portfolio for borrowers who had their debt discharged and not reaffirmed through Chapter 7 bankruptcy. These loans are being reported as accruing TDRs as the borrowers are current on their payments and have no history of delinquency.

During the year ended December 31, 2012, we modified $6.6 million of C&I loans, $3.6 million of CRE loans and $1.2 million of commercial construction loans for financially troubled borrowers that were not considered to be TDRs. These borrowers received modifications that represented insignificant delays in the timing of payments that were not considered to be concessions or we concluded that the bank was adequately compensated through loan pay downs or additional collateral.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

OREO and other repossessed assets are comprised of properties acquired through foreclosure proceedings or acceptance of a deed in lieu of a foreclosure. At December 31, 2012, OREO consists of 13 properties, none of which had a balance greater than $0.2 million. All OREO properties have current appraisals. It is our policy to obtain appraisals annually or sooner if indications of impairment exist. Foreclosures decreased to 22 in 2012 compared to 41 in 2011.

The following represents delinquency for the periods presented:

	2012		2011		2010		2009		2008	
December 31 *(dollars in thousands)*	**Amount**	**% of Loans**	**Amount**	**% of Loans**	**Amount**	**% of Loans**	**Amount**	**% of Loans**	**Amount**	**% of Loans**
90 days or more:										
Commercial real estate	$ 30,556	2.10%	$ 31,648	2.24%	$ 44,310	2.97%	$ 53,789	3.77%	$ 19,386	1.35%
Commercial and Industrial	6,435	0.81%	7,570	1.10%	3,567	0.49%	7,489	1.07%	3,341	0.41%
Commercial construction	6,778	4.03%	6,547	3.47%	7,987	3.08%	21,674	6.03%	13,848	3.83%
Home equity	3,653	0.85%	2,936	0.71%	1,433	0.32%	2,252	0.49%	174	0.04%
Residential mortgage	7,278	1.70%	7,229	2.01%	5,996	1.67%	5,583	1.56%	5,624	1.38%
Installment and other consumer	40	0.05%	4	0.01%	65	0.09%	20	0.02%	73	0.09%
Consumer construction	218	8.95%	181	7.42%	525	13.06%		%		%
Total Loans	**$ 54,958**	**1.64%**	**$ 56,115**	**1.79%**	**$ 63,883**	**1.90%**	**$ 90,807**	**2.67%**	**$ 42,446**	**1.19%**
30 to 89 days:										
Commercial real estate	$ 2,643	0.18%	$ 9,105	0.64%	$ 4,371	0.29%	$ 22,923	1.60%	$ 9,603	0.67%
Commercial and industrial	4,646	0.59%	5,284	0.77%	1,714	0.24%	1,241	0.18%	3,689	0.45%
Commercial construction	10,542	6.27%		%	835	0.32%	899	0.25%	10,446	2.89%
Home equity	3,197	0.74%	2,890	0.70%	2,451	0.56%	2,106	0.46%	356	0.08%
Residential mortgage	3,661	0.86%	2,403	0.67%	1,346	0.37%	5,151	1.44%	5,093	1.25%
Installment and other consumer	501	0.68%	452	0.67%	342	0.46%	852	1.05%	449	0.53%
Consumer construction		%		%		%		%		%
Total Loans	**$ 25,190**	**0.75%**	**$ 20,134**	**0.64%**	**$ 11,059**	**0.33%**	**$ 33,172**	**0.98%**	**$ 29,636**	**0.83%**

Closed-end installment loans, amortizing loans secured by real estate and any other loans with payments scheduled monthly are reported past due when the borrower is in arrears two or more monthly payments. Other multi-payment obligations with payments scheduled other than monthly are reported past due when one scheduled payment is due and unpaid for 30 days or more. We monitor delinquency on a monthly basis, including early stage delinquencies in the 30 to 89 days past due for early identification of potential problem loans.

Allowance for Loan Losses

We maintain an ALL at a level determined to be adequate to absorb estimated probable credit losses inherent within the loan portfolio as of the balance sheet date. Determination of an adequate ALL is inherently subjective, as it requires estimations of the occurrence of future events, as well as the timing of such events, and it may be subject to significant changes from period to period. The methodology for determining the ALL has two main components: evaluation and impairment tests of individual loans and impairment tests of certain groups of homogeneous loans with similar risk characteristics.

We enhanced our ALL model in the fourth quarter of 2010 to better align it with regulatory guidance. The calculation of the base historical loss utilizing an average method over the prior five years was shortened to include a one to two year loss emergence period depending on the loan category over a rolling four quarter average. Loss emergence refers to the length of time between a loss event and a charge-off of the loan. With the volatility in the credit cycle at that time, the shorter

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

time horizon was more responsive to the loss emergence periods we were experiencing in our portfolio. We believe this shorter time horizon provides a better indication of inherent losses in the loan portfolio given the recent economic downturn. We also refined the qualitative factors beginning in the fourth quarter of 2010 to better align with regulatory guidance. Qualitative factors became a basis point adjustment applied to the historical base loss. The combination of the enhancements to the average method and the qualitative factors did not materially change the ALL at December 31, 2010, resulting in an increase in the ALL of less than $0.5 million. Since December 31, 2010, there have been no further enhancements to the ALL methodology.

We develop and document a systematic ALL methodology based on the following portfolio segments: 1) CRE, 2) C&I, 3) Commercial Construction, 4) Consumer Real Estate and 5) Other Consumer. The following is the ALL for the past 5 years by portfolio segment:

	2012		2011		2010		2009		2008	
December 31	**Amount**	**% of Total**	**Amount**	**% of Total**	**Amount**	**% of Total**	**Amount**	**% of Total**	**Amount**	**% of Total**
(dollars in thousands)										
Commercial real estate	$ 25,246	54%	$ 29,804	61%	$ 30,424	59%	$ 27,322	46%	$ 18,781	44%
Commercial and industrial	7,759	17%	11,274	23%	9,777	19%	21,393	36%	20,170	47%
Commercial construction	7,500	16%	3,703	8%	5,905	11%	8,008	13%	73	%
Consumer real estate	5,058	11%	3,166	6%	3,962	8%	2,143	4%	2,750	7%
Other consumer	921	2%	894	2%	1,319	3%	714	1%	915	2%
Total	**$ 46,484**	**100%**	**$ 48,841**	**100%**	**$ 51,387**	**100%**	**$ 59,580**	**100%**	**$ 42,689**	**100%**

An inherent risk to the loan portfolio as a whole is the condition of the local economy. In addition, each loan segment carries with it risks specific to the segment.

CRE loans are secured by commercial purpose real estate, including both owner occupied properties and investment properties for various purposes such as hotels, strip malls and apartments. Individual project cash flows, as well as global cash flows, are generally the sources of repayment for these loans. Besides cash flow risks, CRE loans have collateral risk and risks based upon the business prospects of the lessee, if the project is not owner occupied.

C&I loans are made to operating companies or manufacturers for the purpose of production, operating capacity, accounts receivable, inventory or equipment financing. Collateral for these types of loans often do not have sufficient value in a distressed or liquidation scenario to satisfy the outstanding debt. Cash flow from the operations of the company is the primary source of repayment for these loans and the cash flow depends not only on the economy as a whole, but also on the health of the company s industry.

Commercial construction loans are made to finance construction of buildings or other structures, as well as to finance the acquisition and development of raw land for various purposes. While the risk is generally confined to the construction period, if there are problems, the project may not be completed, and as such, may not provide sufficient cash flow on its own to service the debt or have sufficient value in a liquidation to cover the outstanding principal. There are also various risks depending on the type of project and the experience and resources of the developer.

Consumer real estate loans are secured by 1-4 family residences, including purchase money mortgages, first and second lien home equity loans and home equity lines of credit. The primary source of repayment for these loans is the income and assets of the borrower. The unemployment rate, as well as the state of the local housing markets have a significant impact on the risk determination, since low demand and/or declining home values can limit the ability of borrowers to sell a property and satisfy the debt.

Other consumer loans are made to individuals and may be secured by assets other than 1-4 family residences, or may be unsecured. This class of loans includes auto loans, unsecured lines and credit cards. The primary source of repayment for these loans is the income and assets of the borrower so

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

the local unemployment rate is an important indicator of risk. The value of the collateral, if there is any, is less likely to be a source of repayment due to less certain collateral values.

Significant to the ALL is a higher mix of commercial loans. At December 31, 2012, approximately 87 percent of the ALL related to the commercial loan portfolio, while commercial loans comprise 72 percent of our loan portfolio. Our commercial loans, and more specifically, our CRE and construction loan portfolio, had been more impacted by the economic slowdown in our markets within the past few years. The ability of customers to repay commercial loans is more dependent upon the success of their business, continuing income and general economic conditions. Accordingly, the risk of loss is higher on such loans compared to consumer loans, which have incurred lower losses in our market.

The following table summarizes the ALL for each of the last five years as indicated:

December 31 *(in thousands)*	**2012**	**2011**	**2010**	**2009**	**2008**
General reserves	$ 44,253	$ 43,296	$ 47,756	$ 42,577	$ 35,574
Specific reserves	2,231	5,545	3,631	17,003	7,115
Total Allowance for Loan Losses	**$ 46,484**	**$ 48,841**	**$ 51,387**	**$ 59,580**	**$ 42,689**

The balance in the ALL decreased to $46.5 million or 1.38 percent of total loans at December 31, 2012 as compared to $48.8 million or 1.56 percent of total loans at December 31, 2011. The decrease in the ALL is due to a decrease of $3.3 million in specific reserves associated with loans individually evaluated for impairment offset by an increase of $1.0 million in the general reserve. The December 31, 2012 ALL includes $2.2 million that was specifically allocated for impaired loans of $82.6 million at December 31, 2012, compared to $5.5 million that was allocated for impaired loans of $94.0 million at December 31, 2011. The overall composition of the reserve has changed from 2011 with reserves decreasing in both the CRE and C&I portfolios and increasing in the commercial construction portfolio. We have experienced stress in our commercial construction portfolio during the year, with net charge-offs of $9.6 million compared to net recoveries of $0.7 million during 2011. The losses are primarily related to land development and construction projects that had slowed during the economic downturn, resulting in significant reductions in the appraised values. Many of these loans have been extended resulting in the loan becoming a TDR, and consequently an impaired loan. As a result of these losses the reserve allocated to commercial construction loans has increased $3.8 million to $7.5 million at December 31, 2012 compared to $3.7 million at December 31, 2011. The allowances for both the CRE and the C&I portfolios have decreased as loans evaluated individually for impairment and substandard loans have declined. Further, we have seen a decline in historic loss rates in both the CRE and C&I portfolios. The CRE reserve decreased $4.6 million from $29.8 million at December 31, 2011 to $25.2 million at December 31, 2012, while the C&I reserve decreased $3.5 million, from $11.3 million at December 31, 2011 to $7.8 million at December 31, 2012. Our acquired loans through the acquisition of Mainline and Gateway were recorded at fair value with no carryover of the related ALL.

Consumer unsecured loans and secured loans that are not real estate secured are evaluated for charge-off after the loan becomes 90 days past due. At that time, unsecured loans are fully charged-off and secured loans are charged-off to the estimated fair value of the collateral less the cost to sell. Consumer loans secured by real estate are evaluated for charge-off after the loan balance becomes 90 days past due and are charged down to the estimated fair value of the collateral less cost to sell.

Our charge-off policy for commercial loans requires that loans and other obligations that are not collectible be promptly charged-off when a confirmed loss exists, regardless of the delinquency status of the loan. We may elect to recognize a partial charge-off when management has determined that the

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

value of collateral is less than the remaining investment in the loan. A loan or obligation does not need to be charged-off, regardless of delinquency status, if (i) management has determined there exists sufficient collateral to protect the remaining loan balance and (ii) there exists a strategy to liquidate the collateral. Management may also consider a number of other factors to determine when a charge-off is appropriate. These factors may include, but are not limited to:

- The status of a bankruptcy proceeding;
- The value of collateral and probability of successful liquidation; and/or
- The status of adverse proceedings or litigation that may result in collection.

The following summarizes our loan loss experience for each of the five years presented below:

Years Ended December 31 *(in thousands)*	**2012**	**2011**	**2010**	**2009**	**2008**
ALL Balance at Beginning of Year:	$ 48,841	$ 51,387	$ 59,580	$ 42,689	$ 34,345
Charge-offs:					
Commercial real estate	(9,627)	(8,824)	(23,925)	(8,795)	(828)
Commercial and industrial	(5,278)	(8,971)	(7,277)	(29,350)	(4,681)
Commercial construction	(10,521)	(1,720)	(6,353)	(12,397)	(1,869)
Consumer real estate	(2,509)	(2,617)	(2,210)	(4,558)	(3,217)
Other consumer	(1,078)	(1,013)	(1,262)	(1,762)	(1,575)
Total	(29,013)	(23,145)	(41,027)	(56,862)	(12,170)
Recoveries:					
Commercial real estate	1,259	780	576	70	523
Commercial and industrial	1,153	357	328	532	1,035
Commercial construction	891	2,463	1,748		
Consumer real estate	197	1,030	202	276	157
Other consumer	341	360	469	521	501
Total	3,841	4,990	3,323	1,399	2,216
Net Charge-offs	**(25,172)**	**(18,155)**	**(37,704)**	**(55,463)**	**(9,954)**
Provision for loan losses	22,815	15,609	29,511	72,354	12,878
Acquired loan loss reserve					5,420
ALL Balance at End of Year:	**$ 46,484**	**$ 48,841**	**$ 51,387**	**$ 59,580**	**$ 42,689**

Net loan charge-offs increased $7.0 million to $25.2 million or 0.78 percent of average loans for 2012 as compared to $18.2 million or 0.56 percent of average loans for 2011. The significant increase is primarily due to an increase of $10.4 in net loan charge-offs in the commercial construction portfolio. The commercial construction portfolio had $9.6 million of net loan charge-offs in 2012 compared to a net loan recovery of $0.7 million in 2011. The losses are primarily related to land development and construction projects that had slowed during the economic downturn, resulting in significant reductions in the appraised values. Many of these loans have been extended resulting in the loan becoming a TDR, and consequently an impaired loan.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

The following table summarizes net charge-offs as a percentage of average loans and other ratios:

December 31	2012	2011	2010	2009	2008
Commercial real estate	0.59%	0.55%	1.42%	3.42%	0.52%
Commercial and industrial	0.57%	1.24%	1.62%	0.62%	0.03%
Commercial construction	5.94%	(0.34)%	0.96%	3.74%	0.43%
Consumer real estate	0.28%	0.20%	0.24%	0.50%	0.40%
Other consumer	0.91%	0.94%	1.04%	1.52%	1.35%
Ratio of net charge-offs to average loans outstanding	0.78%	0.56%	1.11%	1.60%	0.31%
Allowance for loan losses as a percentage of total loans	1.38%	1.56%	1.53%	1.75%	1.20%
Allowance for loan losses to total nonperforming loans	85%	87%	80%	66%	101%
Provision for loan losses as a percentage of net loan charge-offs	91%	86%	78%	130%	184%

Deposits

The following table presents the composition of deposits at December 31:

December 31 *(in thousands)*	2012	2011	$ Change
Noninterest-bearing demand	$ 960,980	$ 818,686	$ 142,294
Interest-bearing demand	316,760	283,611	33,149
Money market	361,233	278,092	83,141
Savings	965,571	802,942	162,629
Certificates of deposit	1,033,884	1,152,528	(118,644)
Total	**$ 3,638,428**	**$ 3,335,859**	**$ 302,569**

Deposits are the primary source of funds for us. We believe that our deposit base is stable and that we have the ability to attract new deposits, mitigating a funding dependency on other more volatile sources. During 2012, our demand, money market and savings deposit balances increased by $421.2 million as a result of our two acquisitions and a shift from our certificate of deposit balances due to the low rate environment. Additionally, savings have increased as a result of our preferred savings account which offers an attractive rate in the current low interest rate environment.

Certificates of deposit of $100,000 and over were ten percent of total deposits at December 31, 2012 and eleven percent of total deposits at December 31, 2011, and primarily represent deposit relationships with local customers in our market area. Maturities of certificates of deposit of $100,000 or more outstanding at December 31 are summarized as follows:

December 31 *(in thousands)*	2012

Three months or less	$ 124,799
Over three through six months	59,157
Over six through twelve months	85,393
Over twelve months	98,774
Total	**$ 368,123**

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Through the Promontory Interfinancial Network, LLC, we participate in the Certificate of Deposit Account Registry Services, or CDARS, reciprocal and One-Way Buy programs. We have been a member of Promontory and have utilized CDARS since 2009. Reciprocal deposits provide a stable and cost-effective source of funds with rates generally lower than traditional brokered deposits. Although reciprocal deposits are considered brokered under existing law, they tend to act more like core deposits. Reciprocal deposits are customer funds exchanged among insured depository institutions that are members of the CDARS deposit placement service. Through the exchange, we benefit from large, local customer deposits, while providing our customers with access to FDIC insurance protection beyond the maximum deposit insurance amount. Reciprocal deposits address the need to attract and retain valuable customer relationships. As of December 31, 2012 we had $9.8 million in CDARS reciprocal deposits. We also participate in the CDARS One-Way Buy program which allows us to obtain large blocks of wholesale funding. Through the One-Way Buy program, funding is effectively purchased from insured depository institutions that are member of the CDARS deposit placement service. As of December 31, 2012 we had $1.9 million in the CDARS One-Way Buy program.

The daily average amount of deposits and rates paid on deposits are summarized for the periods indicated in the following table:

Years Ended December 31	2012 Amount	Rate	2011 Amount	Rate	2010 Amount	Rate
(dollars in thousands)						
Noninterest-bearing demand	$ 877,056		$ 792,911		$ 728,708	
Interest-bearing demand	306,994	0.05%	286,588	0.13%	267,291	0.21%
Money market	308,719	0.17%	249,497	0.15%	251,092	0.26%
Savings	902,889	0.26%	761,274	0.17%	749,325	0.28%
Certificates of deposit	1,104,262	1.24%	1,181,822	1.77%	1,300,803	1.95%
Total	**$ 3,499,920**	**0.48%**	**$ 3,272,092**	**0.70%**	**$ 3,297,219**	**0.87%**

Borrowings

The following table represents the composition of borrowings at December 31:

Years Ended December 31	2012	2011	$ Change
(in thousands)			
Securities sold under repurchase agreements, retail	$ 62,582	$ 30,370	$ 32,212
Short-term borrowings	75,000	75,000	
Long-term borrowings	34,101	31,874	2,227
Junior subordinated debt securities	90,619	90,619	
Total Borrowings	**$ 262,302**	**$ 227,863**	**$ 34,439**

Borrowings are an additional source of funding for us. Short-term borrowings are for terms under one year and were comprised of REPOs and FHLB advances. We define repurchase agreements with our local retail customers as retail REPO. Securities pledged as collateral under these REPO financing arrangements cannot be sold or repledged by the secured party and are therefore accounted for as a secured borrowing. FHLB advances are for various terms secured by a blanket lien on residential mortgages and other real estate secured loans. The purpose of long-term borrowings is to match-fund selected new loan originations, to mitigate interest rate sensitivity risks and to take advantage of discounted borrowing rates through the FHLB for community investment projects. The increase in borrowings of $34.4 million is primarily within our retail

REPOs and is primarily due to the expiration of the unlimited FDIC insurance on noninterest-bearing demand deposits.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Information pertaining to REPOs is summarized in the table below:

(dollars in thousands)	2012	2011	2010
Balance at December 31	$ 62,582	$ 30,370	$ 40,653
Average balance during the year	47,388	41,584	46,489
Average interest rate during the year	0.17%	0.13%	0.14%
Maximum month-end balance during the year	$ 62,582	$ 42,409	$ 52,046
Average interest rate at December 31	0.20%	0.11%	0.07%

Information pertaining to short-term FHLB advances is summarized in the table below:

(dollars in thousands)	2012	2011	2010
Balance at December 31	$ 75,000	$ 75,000	$
Average balance during the year	50,212	551	32,473
Average interest rate during the year	0.24%	0.32%	0.45%
Maximum month-end balance during the year	$ 75,000	$ 75,000	$ 141,800
Average interest rate at December 31	0.19%	0.18%	%

During 2012, long-term borrowings increased $2.2 million as compared to December 31, 2011. At December 31, 2012, our long-term borrowings outstanding of $34.1 million included $31.0 million that were at a fixed rate and $3.1 million at a variable rate.

During the third quarter of 2006, we issued $25.0 million of junior subordinated debentures through a pooled transaction at an initial fixed rate of 6.78 percent. Beginning September 15, 2011 and quarterly thereafter, we have had the option to redeem the subordinated debt, subject to a 30 day written notice and prior approval by the FDIC. We chose not to exercise the option for early redemption in either 2011 or 2012 and the subordinated debt converted to a variable rate of 3-month LIBOR plus 160 basis points. The subordinated debt qualifies as Tier 2 capital under regulatory guidelines and will mature on December 15, 2036.

During the first quarter of 2008, we completed a private placement to a financial institution of $20.0 million of floating rate trust preferred securities. The trust preferred securities mature in March 2038, are callable at our option after five years, bear interest initially at a rate of 6.44 percent per annum and quarterly adjust with the three-month LIBOR plus 350 basis points. We began making interest payments to the trustee on June 15, 2008 and quarterly thereafter. The trust

preferred securities qualify as Tier 1 capital under regulatory guidelines. To issue these trust preferred securities, we formed STBA Capital Trust I, or the Trust, with $0.6 million of equity, which is owned 100 percent by us. The proceeds from the sale of the trust preferred securities and the issuance of common equity were invested in junior subordinated debt, which is the sole asset of the Trust. The Trust pays dividends on the trust preferred securities at the same rate as the interest we pay on the junior subordinate debt held by the Trust. Since the third-party investors are the primary beneficiaries, the Trust qualifies as a variable interest entity, or VIE, but is not consolidated in our financial statements.

During the second quarter of 2008, we issued $20.0 million of junior subordinated debt through a private placement with three financial institutions at an initial rate of 6.40 percent that floats quarterly with 3-month LIBOR plus 350 basis points. If all or any portion of the

subordinated debt ceases to be deemed Tier 2 Capital due to a change in applicable capital regulations, we will have the right to redeem, on any interest payment date, subject to a 30 day written notice and prior approval

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

by the FDIC, the subordinated debt at the applicable redemption rate. The redemption rate starts at a high of 102.82 percent at June 15, 2009 and decreases yearly to 100 percent on June 15, 2013 and thereafter and can be called after five years. The subordinated debt qualifies as Tier 2 capital under regulatory guidelines and will mature on June 15, 2018.

Also during the second quarter of 2008, we issued $25.0 million of junior subordinated debt through a private placement with a financial institution at an initial rate of 5.15 percent that floats quarterly with 3-month LIBOR plus 250 basis points. At any time after May 30, 2013, we will have the right to redeem all or a portion of the subordinated debt, subject to a 30-day written notice and prior approval by the FDIC. The subordinated debt qualifies as Tier 2 capital under regulatory guidelines and will mature on May 30, 2018.

Wealth Management Assets

As of December 31, 2012, the fair value of the S&T Bank wealth management assets under management and administration, or AUM, which are not accounted for as part of our assets, increased to $1.7 billion from $1.5 billion as of December 31, 2011. AUM consist of $1.1 billion in S&T Trust and $0.6 billion in S&T Financial Services. The increase in 2012 is primarily attributable to the improved performance of the U.S. and global capital markets.

Explanation of Use of Non-GAAP Financial Measures

In addition to the results of operations presented in accordance with GAAP, our management uses and this Annual Report contains or references, certain non-GAAP financial measures, such as net interest income on a fully taxable-equivalent basis, operating revenue and the efficiency ratio. We believe these non-GAAP financial measures provide information useful to investors in understanding our underlying operational performance and our business and performance trends as they facilitate comparisons with the performance of other companies in the financial services industry. Although we believe that these non-GAAP financial measures enhance investors understanding of our business and performance, these non-GAAP financial measures should not be considered an alternative to GAAP or considered to be more important than financial results determined in accordance with GAAP, nor is it necessarily comparable with non-GAAP measures which may be presented by other companies.

We believe the presentation of net interest income on a fully taxable-equivalent basis ensures comparability of net interest income arising from both taxable and tax-exempt sources and is consistent with industry practice. Interest income per the Consolidated Statements of Net Income is reconciled to net interest income adjusted to a fully taxable-equivalent basis on pages 32 and 38.

Operating revenue is the sum of net interest income and noninterest income less security gains/losses. In order to understand the significance of net interest income to our business and operating results, we believe it is appropriate to evaluate the significance of net interest income as a component of operating revenue.

The efficiency ratio is recurring noninterest expense divided by recurring noninterest income plus net interest income, on a fully taxable-equivalent basis, which ensures comparability of net interest income arising from both taxable and tax-exempt sources and is consistent with industry practice.

Capital Resources

Shareholders equity increased $46.9 million to $537.4 million at December 31, 2012 compared to $490.5 million at December 31, 2011. The increase in shareholders equity is primarily due to the issuance of 1.5 million shares of common stock of $27.6 million, for the two acquisitions consummated in 2012, and the addition of $14.6 million in retained earnings, primarily comprised of

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

net income of $34.2 million reduced by common stock dividends of $17.4 million. Included in other comprehensive income was an increase of $4.1 million in unrealized gains on securities available-for-sale due to the continued low interest rate environment.

We continue to maintain a strong capital position with a leverage ratio of 9.31 percent as compared to the regulatory guideline of 5.00 percent to be well capitalized. Our risk-based Tier 1 and Total capital ratios were 11.98 percent and 15.39 percent, respectively, at December 31, 2012, which places us significantly above the Federal Reserve s well capitalized guidelines of 6.00 percent and 10.00 percent for Tier 1 and Total capital. We believe that we have sufficient cash flow, on balance sheet liquidity and borrowing capacity to fund all outstanding commitments and letters of credit, while maintaining proper levels of liquidity. We believe that we have the ability to raise additional capital, if necessary.

In October 2012, we filed a shelf registration statement on Form S-3 under the Securities Act of 1933 as amended, with the SEC for the issuance of up to $300.0 million of a variety of securities including, debt and capital securities, preferred and common stock and warrants. We may use the proceeds from the issuance of any securities for general corporate purposes, which could include investments at the holding company level, investing in, or extending credit to, our subsidiaries, possible acquisitions and stock repurchases. As of December 31, 2012, we had not issued any securities pursuant to the shelf registration statement.

Contractual Obligations

Contractual obligations represent future cash commitments and liabilities under agreements with third parties and exclude contingent contractual liabilities for which we cannot reasonably predict future payments. We have various financial obligations, including contractual obligations and commitments that may require future cash payments.

The following table presents as of December 31, 2012, significant fixed and determinable contractual obligations to third parties by payment date:

	Payments Due In				
(in thousands)	**2013**	**2014-2015**	**2016-2017**	**Later Years**	**Total**
Deposits without a stated maturity[1]	$ 2,604,544	$	$	$	$ 2,604,544
Certificates of deposit[1]	643,635	248,792	131,071	10,386	1,033,884
Securities sold under repurchase agreements[1]	62,582				62,582
Short-term borrowings[1]	75,000				75,000
Long-term borrowings[1]	12,291	4,767	4,742	12,301	34,101
Junior subordinated debt securities[1]				90,619	90,619
Operating and capital leases	2,164	4,335	4,112	43,953	54,564
Purchase obligations	7,388	14,204	7,524		29,116
Total	**$ 3,407,604**	**$ 272,098**	**$ 147,449**	**$ 157,259**	**$ 3,984,410**

[1] *Excludes interest*

Operating lease obligations represent short and long-term lease arrangements as described in Item 8, Note 10 Premises and Equipment, in the Consolidated Financial Statements. Purchase obligations primarily represent obligations under agreement with our third party data processing servicer and communications charges as described in Item 8, Note 17 Commitments and Contingencies.

58

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Off-Balance Sheet Arrangements

In the normal course of business, we offer off-balance sheet credit arrangements to enable our customers to meet their financing objectives. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the financial statements. Our exposure to credit loss, in the event the customer does not satisfy the terms of the agreement, equals the contractual amount of the obligation less the value of any collateral. We apply the same credit policies in making commitments and standby letters of credit that are used for the underwriting of loans to customers. Commitments generally have fixed expiration dates, annual renewals or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The allowance for unfunded commitments is included in other liabilities in the Consolidated Balance Sheets.

The following table sets forth the commitments and letters of credit for the periods stated:

December 31 *(in thousands)*	**2012**	**2011**
Commitments to extend credit	$ 874,137	$ 816,160
Standby letters of credit	95,399	119,576
Total	**$ 969,536**	**$ 935,736**

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.

Our allowance for unfunded commitments is determined using a methodology similar to that used to determine the ALL. Amounts are added to the allowance for unfunded commitments through a charge to current earnings in noninterest expense. The balance in the allowance for unfunded commitments increased by $1.8 million to $3.0 million a December 31, 2012 as compared to $1.2 million at December 31, 2011 due to increases in both the volume of construction commitments and higher historic loss rates.

Liquidity

Liquidity is defined as a financial institution s ability to meet its cash and collateral obligations at a reasonable cost. This includes the ability to satisfy the financial needs of depositors who want to withdraw funds or of borrowers needing to access funds to meet their credit needs. Liquidity risk management involves monitoring and maintaining sufficient levels of a diverse set of funding sources that are available for normal operations and for unanticipated stress events. In order to manage liquidity risk our Board of Directors has delegated authority to the ALCO, for formulation, implementation and oversight of liquidity risk management. ALCO s goal is to maintain adequate levels of liquidity to meet our funding needs in both a normal operating environment and for potential liquidity stress events.

Our primary funding and liquidity source is a stable deposit base. We believe that S&T bank has the ability to retain existing and attract new deposits, mitigating a funding dependency on other more volatile sources. Although deposits are the primary source of funds, we have identified various funding sources that can be used as part of our normal funding program when either a structure or cost efficiency has been identified.

These funding sources include a cushion of highly liquid assets, borrowing availability at the FHLB, Federal Funds lines with other financial institutions and access to the brokered certificates of deposit market including CDARs.

Table of Contents

Item 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS continued

Since the beginning of the financial industry crisis in 2008, monitoring and maintaining appropriate liquidity levels has been a focus of regulators, bankers and investors. ALCO has enhanced the measurement, monitoring and reporting systems for liquidity risk management for potential liquidity stress events. Specific focus has been on maintaining an adequate level of asset liquidity, performing short-term and long-term stress tests and developing a more detailed contingency funding plan. We also work to ensure that access to various wholesale funding sources is available, even in a stress event.

ALCO uses a variety of ratios and reports to monitor our liquidity position. The ratios and reports include an asset liquidity ratio, a liquidity coverage ratio, a loan to deposit ratio, a noncore funding ratio, and a cash flow projections report. ALCO policy guidelines are in place for each ratio that defines graduated risk tolerance levels. If a ratio moves to high risk, specific actions are defined, such as increased monitoring or the development of an action plan to reduce the risk position. As of December 31, 2012 there were no liquidity ratios in the high risk tolerance level.

Inflation

Management is aware of the significant effect inflation has on interest rates and can have on financial performance. Our ability to cope with this is best determined by analyzing our capability to respond to changing interest rates and our ability to manage noninterest income and expense. We monitor the mix of interest-rate sensitive assets and liabilities through ALCO in order to reduce the impact of inflation on net interest income. We also control the effects of inflation by reviewing the prices of our products and services, by introducing new products and services and by controlling overhead expenses.

Table of Contents

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is defined as the degree to which changes in interest rates, foreign exchange rates, commodity prices or equity prices can adversely affect a financial institution s earnings or capital. For most financial institutions, including S&T, market risk primarily reflects exposures to changes in interest rates. Interest rate fluctuations affect earnings by changing net interest income and other interest-sensitive income and expense levels. Interest rate changes affect capital by changing the net present value of a bank s future cash flows, and the cash flows themselves, as rates change. Accepting this risk is a normal part of banking and can be an important source of profitability and shareholder value. However, excessive interest rate risk can threaten banks earnings, capital, liquidity and solvency. Our sensitivity to changes in interest rate movements are continually monitored by the ALCO. ALCO monitors and manages market risk through rate shock analyses, economic value of equity, or EVE analysis and simulations in order to avoid unacceptable earnings and market value fluctuations due to changes in interest rates.

Rate shock analyses are performed on a static balance sheet to estimate the effect that specific interest rate changes would have on 12 months of pre-tax net interest income. Rate shock analyses assume an immediate parallel shift in market interest rates. Assumptions are modified in the decreasing rate shock analyses due to the very low level of interest rates. Rate shock analyses also incorporate management assumptions regarding the level of interest rate changes on non-maturity deposit products (noninterest-bearing demand, interest-bearing demand, money market and savings) and changes in the prepayment behavior of fixed rate loans and securities with optionality. S&T policy guidelines limit the change in pre-tax net interest income over a 12 month horizon using rate shocks of +/- 300 basis points. Policy guidelines define the percent change in pre-tax net interest income by graduated risk tolerance levels of minimal, moderate and high. The table below reflects the rate shock analyses results, which are in the minimal risk tolerance level.

In order to monitor interest rate risk beyond the 12 month time horizon of rate shocks, we also perform EVE analysis. EVE represents the present value of all asset cash flows minus the present value of all liability cash flows. As with rate shock analysis, EVE incorporates management assumptions regarding prepayment behavior of fixed rate loans and securities with optionality and core deposit behavior and value. S&T policy guidelines limit the change in EVE given changes in rates of +/- 300 basis points. Policy guidelines define the percent change in EVE by graduated risk tolerance levels of minimal, moderate and high.

The table below reflects the rate shock and EVE results, which are in the minimal risk tolerance level.

	December 31, 2012		December 31, 2011	
Change in Interest Rate (basis points)	% Change in Pretax Net Interest Income	% Change in Economic Value of Equity	% Change in Pretax Net Interest Income	% Change in Economic Value of Equity
+300	8.2	23.2	11.3	20.9
+200	5.0	16.8	7.3	15.9
+100	2.0	9.1	3.5	9.1
-100	(2.4)	(9.7)	(3.9)	(12.9)
-200	(5.1)	(7.5)	(6.9)	(15.2)
-300	(6.7)	(6.8)	(8.9)	(15.1)

In addition to rate shocks and EVE, simulations are performed periodically to assess the sensitivity of scenario assumptions on pre-tax net interest income. Simulation analyses most often test for sensitivity to yield curve shape and slope changes, severe rate shocks, changes in prepayment assumptions and significant balance mix changes.

The results from the rate shock and EVE analyses are consistent with having an asset sensitive balance sheet. Having an asset sensitive balance sheet means more assets than liabilities will reprice during the measured time frames. The implications of an asset sensitive balance sheet will differ

Table of Contents

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK continued

depending upon the change in market interest rates. For example, with an asset sensitive balance sheet in a declining interest rate environment, more assets than liabilities will decrease in rate. This situation could result in a decrease in net interest income and operating income. Conversely, with an asset sensitive balance sheet in a rising interest rate environment, more assets than liabilities will increase in rate. This situation could result in an increase in net interest income and operating income. When comparing the results of December 31, 2012 to December 31, 2011 the percent changes are a result of the balance sheet becoming less asset sensitive. The Consolidated Balance Sheet became less asset sensitive during 2012 mainly as a result of slower prepayment behavior of fixed rate loans and customer preference for short term deposit products.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Consolidated Financial Statements

Consolidated Balance Sheets	64
Consolidated Statements of Net Income	65
Consolidated Statements of Comprehensive Income	66
Consolidated Statements of Changes in Shareholders Equity	67
Consolidated Statements of Cash Flows	68
Notes to Consolidated Financial Statements	69
Report of KPMG LLP, Independent Registered Public Accounting Firm on Effectiveness of Internal Control Over Financial Reporting	127
Report of KPMG LLP, Independent Registered Public Accounting Firm on Consolidated Financial Statements	128

Table of Contents

CONSOLIDATED BALANCE SHEETS

S&T Bancorp, Inc. and Subsidiaries

(in thousands, except share and per share data)	**December 31, 2012**	**2011**
ASSETS		
Cash and due from banks, including interest-bearing deposits of $257,116 and $208,854 at December 31, 2012 and 2011, respectively	$ 337,711	$ 270,526
Securities available-for-sale, at fair value	453,096	357,596
Loans held for sale	22,499	2,850
Portfolio loans, net of unearned income of $216 and $715 at December 31, 2012 and 2011, respectively	3,346,622	3,129,759
Allowance for loan losses	(46,484)	(48,841)
Portfolio loans, net	3,300,138	3,080,918
Bank owned life insurance	58,619	56,755
Premises and equipment, net	38,676	37,755
Federal Home Loan Bank stock, at cost	14,485	18,216
Goodwill	175,733	165,273
Other intangibles, net	5,350	5,728
Other assets	120,395	124,377
Total Assets	**$ 4,526,702**	**$ 4,119,994**
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$ 960,980	$ 818,686
Interest-bearing demand	316,760	283,611
Money market	361,233	278,092
Savings	965,571	802,942
Certificates of deposit	1,033,884	1,152,528
Total Deposits	**3,638,428**	**3,335,859**
Securities sold under repurchase agreements	62,582	30,370
Short-term borrowings	75,000	75,000
Long-term borrowings	34,101	31,874
Junior subordinated debt securities	90,619	90,619
Other liabilities	88,550	65,746
Total Liabilities	**3,989,280**	**3,629,468**
SHAREHOLDERS EQUITY		
Common stock ($2.50 par value)		
Authorized 50,000,000 shares		
Issued 31,197,365 shares and 29,714,038 shares at December 31, 2012 and 2011, respectively		
Outstanding 29,732,209 shares and 28,131,249 shares at December 31, 2012 and 2011, respectively	77,993	74,285
Additional paid-in capital	77,458	52,637
Retained earnings	436,039	421,468
Accumulated other comprehensive loss	(13,582)	(14,108)
Treasury stock (1,465,156 shares and 1,582,789 shares, at December 31, 2012 and 2011, respectively, at cost)	(40,486)	(43,756)
Total Shareholders Equity	**537,422**	**490,526**
Total Liabilities and Shareholders Equity	**$ 4,526,702**	**$ 4,119,994**

See Notes to Consolidated Financial Statements

64

Table of Contents

CONSOLIDATED STATEMENTS OF NET INCOME

S&T Bancorp, Inc. and Subsidiaries

(in thousands, except per share data)	Years ended December 31, 2012	2011	2010
INTEREST INCOME			
Loans, including fees	$ 145,181	$ 154,121	$ 169,404
Investment Securities:			
Taxable	7,544	8,169	7,685
Tax-exempt	3,121	2,347	2,830
Dividends	405	442	500
Total Interest Income	**156,251**	**165,079**	**180,419**
INTEREST EXPENSE			
Deposits	16,796	22,952	28,717
Borrowings and junior subordinated debt securities	4,228	4,781	5,856
Total Interest Expense	**21,024**	**27,733**	**34,573**
NET INTEREST INCOME	**135,227**	**137,346**	**145,846**
Provision for loan losses	22,815	15,609	29,511
Net Interest Income After Provision for Loan Losses	**112,412**	**121,737**	**116,335**
NONINTEREST INCOME			
Debit and credit card fees	11,134	10,889	9,954
Service charges on deposit accounts	9,992	9,978	11,178
Wealth management fees	9,808	8,180	7,808
Insurance fees	8,448	8,314	8,312
Securities gains (losses), net	3,016	(124)	274
Mortgage banking	2,878	1,199	3,403
Other	6,636	5,621	6,281
Total Noninterest Income	**51,912**	**44,057**	**47,210**
NONINTEREST EXPENSE			
Salaries and employee benefits	60,256	51,078	48,715
Data processing	9,620	6,853	6,145
Net occupancy	7,605	6,943	6,928
Professional services and legal	5,659	5,437	6,889
Furniture and equipment	5,262	4,941	5,054
Marketing	3,302	3,019	2,795
Other taxes	3,200	3,381	3,432
FDIC assessment	2,926	3,570	5,426
Other	25,033	18,686	20,249
Total Noninterest Expense	**122,863**	**103,908**	**105,633**
Income Before Taxes	**41,461**	**61,886**	**57,912**
Provision for income taxes	7,261	14,622	14,432
Net Income	**34,200**	**47,264**	**43,480**
Preferred stock dividends and discount amortization		7,611	6,201
Net Income Available to Common Shareholders	**$ 34,200**	**$ 39,653**	**$ 37,279**
Earnings per common share basic	$ 1.18	$ 1.41	$ 1.34
Earnings per common share diluted	1.18	1.41	1.34
Dividends declared per common share	0.60	0.60	0.60

See Notes to Consolidated Financial Statements

Table of Contents

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

S&T Bancorp, Inc. and Subsidiaries

	Years ended December 31,		
(in thousands)	**2012**	**2011**	**2010**
Net Income	**$ 34,200**	**$ 47,264**	**$ 43,480**
Other Comprehensive Income (Loss), Before Tax and Net of Reclassifications into Net Income:			
Change in unrealized gains on securities available-for-sale	4,097	6,702	695
Reclassification adjustment for net (gains) losses on securities available-for-sale included in net income	(3,016)	124	(274)
Adjustment to funded status of employee benefit plans	(271)	(18,787)	(606)
Other Comprehensive Income (Loss), Before Tax and Net of Reclassifications into Net Income	**810**	**(11,961)**	**(185)**
Income tax (expense) benefit related to items of other comprehensive income	(284)	4,187	65
Other Comprehensive Income (Loss), After Tax and Net of Reclassifications into Net Income	**526**	**(7,774)**	**(120)**
Comprehensive Income	**$ 34,726**	**$ 39,490**	**$ 43,360**

See Notes to Consolidated Financial Statements

Table of Contents

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

S&T Bancorp, Inc. and Subsidiaries

(thousands, except share and per share data)	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Balance at December 31, 2009	**$ 105,370**	**$ 74,285**	**$ 51,158**	**$ 383,118**	**$ (6,214)**	**$ (54,399)**	**$ 553,318**
Net income for 2010				43,480			43,480
Other comprehensive income (loss), net of tax					(120)		(120)
Preferred stock dividends and discount amortization	767			(6,201)			(5,434)
Cash dividends declared ($0.60 per share)				(16,683)			(16,683)
Treasury stock issued (205,135 shares)				(1,980)		5,672	3,692
Recognition of restricted stock compensation expense			470				470
Tax benefit from stock-based compensation			46				46
Forfeitures of nonstatutory stock options (11,000 shares)			(104)				(104)
Balance at December 31, 2010	**$ 106,137**	**$ 74,285**	**$ 51,570**	**$ 401,734**	**$ (6,334)**	**$ (48,727)**	**$ 578,665**
Net income for 2011				47,264			47,264
Other comprehensive income (loss), net of tax					(7,774)		(7,774)
Redemption of preferred stock	(108,676)						(108,676)
Preferred stock dividends and discount amortization	2,539			(7,611)			(5,072)
Cash dividends declared ($0.60 per share)				(16,830)			(16,830)
Treasury stock issued (182,507 shares, net)				(3,089)		4,971	1,882
Recognition of restricted stock compensation expense			1,133				1,133
Tax expense from stock-based compensation			(66)				(66)
Balance at December 31, 2011	**$**	**$ 74,285**	**$ 52,637**	**$ 421,468**	**$ (14,108)**	**$ (43,756)**	**$ 490,526**
Net income for 2012				34,200			34,200
Other comprehensive income (loss), net of tax					526		526
Cash dividends declared ($0.60 per share)				(17,357)			(17,357)
Common stock issued in acquisition (1,483,327 shares)		3,708	23,902				27,610
Treasury stock issued (117,633 shares, net)				(2,272)		3,270	998
Recognition of restricted stock compensation expense			949				949
Tax expense from stock-based compensation			(30)				(30)
Balance at December 31, 2012	**$**	**$ 77,993**	**$ 77,458**	**$ 436,039**	**$ (13,582)**	**$ (40,486)**	**$ 537,422**

See Notes to Consolidated Financial Statements

Table of Contents

CONSOLIDATED STATEMENTS OF CASH FLOWS

S&T Bancorp, Inc. and Subsidiaries

	Years Ended December 31,		
(in thousands)	**2012**	**2011**	**2010**
OPERATING ACTIVITIES			
Net Income	$ 34,200	$ 47,264	$ 43,480
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	22,815	15,609	29,511
Provision for unfunded loan commitments	1,811	(1,474)	(1,555)
Depreciation and amortization	7,000	6,323	6,587
Net amortization of discounts and premiums	2,280	1,191	881
Stock-based compensation expense	913	960	513
Securities (gains) losses, net	(3,016)	124	(274)
Deferred income taxes	1,038	2,448	(4,537)
Tax expense (benefit) from stock-based compensation	30	66	(46)
Mortgage loans originated for sale	(104,924)	(68,261)	(121,883)
Proceeds from the sale of loans	86,886	74,780	119,617
Gain on the sale of loans, net	(1,612)	(875)	(1,809)
Net decrease in interest receivable	973	589	2,752
Net decrease in interest payable	(1,376)	(443)	(1,678)
Net decrease (increase) in other assets	18,815	4,132	(2,745)
Net increase (decrease) increase in other liabilities	18,057	(8,531)	20,170
Net Cash Provided by Operating Activities	**83,890**	**73,902**	**88,984**
INVESTING ACTIVITIES			
Purchases of securities available-for-sale	(166,786)	(135,447)	(82,890)
Proceeds from maturities, prepayments and calls of securities available-for-sale	87,604	71,318	146,960
Proceeds from sales of securities available-for-sale	66,575	70	2,579
Proceeds from the redemption of Federal Home Loan Bank stock	5,700	4,149	1,177
Net (increase) decrease in loans	(21,892)	185,182	3,236
Proceeds from the sale of loans not originated for resale	3,874	8,595	
Purchases of premises and equipment	(2,179)	(2,531)	(3,469)
Proceeds from the sale of premises and equipment	142	404	60
Net cash acquired from bank acquisitions	18,639		
Net Cash (Used in) Provided by Investing Activities	**(8,323)**	**131,740**	**67,653**
FINANCING ACTIVITIES			
Net increase in core deposits	207,653	105,776	63,383
Net decrease in certificates of deposit	(217,311)	(87,553)	(50,536)
Net increase (decrease) in securities sold under repurchase agreements and federal funds purchased	28,442	(10,283)	(4,281)
Net (decrease) increase in short-term borrowings		75,000	(51,300)
Proceeds from long-term borrowings	4,311	4,192	9,241
Repayments of long-term borrowings	(15,088)	(1,682)	(65,770)
Redemption of preferred stock		(108,676)	
Purchase of treasury shares	(49)	(64)	
Sale of treasury shares	1,047	1,946	3,692
Preferred stock dividends		(5,072)	(5,434)
Cash dividends paid to common shareholders	(17,357)	(16,830)	(16,683)
Tax (expense) benefit from stock-based compensation	(30)	(66)	46
Net Cash Used in Financing Activities	**(8,382)**	**(43,312)**	**(117,642)**
Net increase in cash and cash equivalents	67,185	162,330	38,995
Cash and cash equivalents at beginning of year	270,526	108,196	69,201
Cash and Cash Equivalents at End of Year	**$ 337,711**	**$ 270,526**	**$ 108,196**
Supplemental Disclosures			
Interest paid	$ 22,329	$ 27,733	$ 36,251
Income taxes paid, net of refunds	4,063	15,100	14,818
Loans transferred to held for sale	19,255	8,753	
Net assets (liabilities) from acquisitions, excluding cash and cash equivalents	(683)		
Transfers to other real estate owned and other repossessed assets	1,915	8,472	11,308

See Notes to Consolidated Financial Statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

S&T Bancorp, Inc. and Subsidiaries

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

S&T Bancorp, Inc., or S&T, was incorporated on March 17, 1983 under the laws of the Commonwealth of Pennsylvania as a bank holding company and has three wholly owned subsidiaries, S&T Bank, 9th Street Holdings, Inc. and STBA Capital Trust I. We own a one-half interest in Commonwealth Trust Credit Life Insurance Company, or CTCLIC.

We are presently engaged in nonbanking activities through the following five entities: 9th Street Holdings, Inc.; S&T Bancholdings, Inc.; CTCLIC; S&T Insurance Group, LLC and Stewart Capital Advisors, LLC. 9th Street Holdings, Inc. and S&T Bancholdings, Inc. are investment holding companies. CTCLIC, which is a joint venture with another financial institution, acts as a reinsurer of credit life, accident and health insurance policies sold by S&T Bank and the other institution. S&T Insurance Group, LLC, through its subsidiaries, offers a variety of insurance products. Stewart Capital Advisors, LLC is a registered investment advisor that manages private investment accounts for individuals and institutions and advises the Stewart Capital Mid Cap Fund.

On March 9, 2012, we completed the acquisition and conversion of Mainline Bancorp, Inc., or Mainline, a bank holding company based in Ebensburg, Pennsylvania. Mainline had one subsidiary, Mainline National Bank, with eight branches and $129.5 million in loans and $206.0 million in deposits. The acquisition expanded our market share and footprint throughout Cambria and Blair counties of Western Pennsylvania. The total acquisition cost of Mainline was $27.8 million.

On August 13, 2012, we completed the acquisition of Gateway Bank of Pennsylvania, a bank with $99.1 million in loans and $105.4 million in deposits, headquartered in McMurray, Pennsylvania. The total acquisition cost of Gateway Bank was $19.8 million. As of December 31, 2012, Gateway was operating as a separate wholly-owned subsidiary of S&T, with all transactions since the acquisition date consolidated in our financial statements. On February 8, 2013, Gateway Bank was merged into S&T Bank, and their two branches are now fully operational branches of S&T Bank.

Accounting Policies

Our financial statements have been prepared in accordance with U. S. generally accepted accounting principles, or GAAP. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the balance sheets and revenues and expenses for the periods then ended. Actual results could differ from those estimates. Our significant accounting policies are described below.

Principals of Consolidation

The Consolidated Financial Statements include the accounts of 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.

Reclassification

Certain amounts in prior years financial statements have been reclassified to conform to the current year s presentation. The reclassifications had no significant effect on our results of operations or financial condition.

69

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Business Combinations

We account for business combinations using the acquisition method of accounting. Under this method of accounting, the acquired company s net assets are recorded at fair value at the date of acquisition, and the results of operations of the acquired company are combined with our results from that date forward. Acquisition costs are expensed when incurred. The difference between the purchase price and the fair value of the net assets acquired (including identified intangibles) is recorded as goodwill.

Fair Value Measurements

We use fair value measurements when recording and disclosing certain financial assets and liabilities. Securities available-for-sale, trading assets and derivatives are recorded at fair value on a recurring basis. Additionally, from time to time, we 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, or OREO, mortgage servicing rights, or MSRs, 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, we use 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 is developed, based on market data we have obtained from independent sources. Unobservable inputs reflect our 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. Our 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 are descriptions of the valuation methodologies that we use for financial instruments recorded at fair value on either a recurring or nonrecurring basis.

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Recurring Basis

Securities Available-for-Sale

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

We obtain 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 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 as 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.

Trading Assets

We use quoted market prices to determine the fair value of our trading assets. Our trading assets are held in a Rabbi Trust under a deferred compensation plan and are invested in readily quoted mutual funds. Accordingly, these assets are classified as Level 1. Trading assets are recorded in other assets in the Consolidated Balance Sheets.

Derivative Financial Instruments

We use derivative instruments, including interest rate swaps for commercial loans with our customers, and we sell mortgage loans in the secondary market and enter into interest rate lock commitments. We calculate 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.

We incorporate credit valuation adjustments into the valuation models to appropriately reflect both our own nonperformance risk and the respective counterparty s nonperformance risk in calculating fair value measurements. In adjusting the fair value of our derivative contracts for the effect of nonperformance risk, we have 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 principal or most advantageous market currently offered for similar loans using observable market data. The fair value of the loans transferred from the loan portfolio is 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 3.

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. We establish a specific reserve based on the following three impairment methods: 1) the present value of expected future cash flows discounted at

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

the loan s original 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 and we expect to liquidate the collateral. However, if repayment is expected to come from the operation of the collateral, rather than liquidation, then we do not consider estimated selling costs in determining the fair value of the collateral. Collateral values are generally based upon appraisals by approved, independent state certified appraisers.

Appraisals may be discounted based on our historical knowledge, changes in market conditions from the time of appraisal or our knowledge of the borrower and the borrower s business. Impaired loans carried at fair value are classified as Level 3.

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 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. Like impaired loans, appraisals on OREO may be discounted based on our historical knowledge, changes in market conditions from the time of appraisal or other information available to us. OREO and other repossessed assets are classified as Level 3.

Mortgage Servicing Rights

The fair value of MSRs 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 MSRs. If the carrying value of MSRs exceeds fair value, they are considered impaired. As the valuation model includes significant unobservable inputs, MSRs are classified as Level 3 within the fair value hierarchy.

Other Assets

We measure 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 our 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 our assets and liabilities are considered financial instruments. 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 our general practice and intent to hold our financial instruments to maturity and to not engage in trading or sales activities. For fair value disclosure purposes, we substantially utilize the fair value measurement criteria as required and explained above. In cases where quoted fair values are not available, we use present value methods to determine the fair value of our 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, including interest-bearing deposits, approximate fair value.

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Loans

The fair value of variable rate performing loans is based on carrying values adjusted for credit risk. The fair value 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 value 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 fair value.

Short-Term Borrowings

The carrying amounts of securities sold under repurchase agreements, federal funds purchased 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

The variable rate junior subordinated debt securities reprice quarterly and fair values are based on carrying values.

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 are not made because of the short-term nature of these arrangements and the credit standing of the counterparties.

Other

Estimates of fair value are not made for items that are not defined as financial instruments, including such items as our core deposit intangibles and the value of our trust operations.

Cash and Cash Equivalents

We consider cash and due from banks, interest-bearing deposits with banks and federal funds sold as cash and cash equivalents.

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Securities

We determine the appropriate classification of securities at the time of purchase. All securities, including both debt and equity securities, are classified as available-for-sale. These are securities that we intend to hold for an indefinite period of time, but that may be sold in response to changes in interest rates, prepayment risk, liquidity needs or other factors. Such securities are carried at fair value with net unrealized gains and losses deemed to be temporary, reported as a component of other comprehensive income, net of tax. Realized gains and losses on the sale of available-for-sale securities and other-than-temporary impairment, or OTTI, charges are recorded within noninterest income in the Consolidated Statements of Net Income. Realized gains and losses on the sale of securities are determined using the specific-identification method. Bond premiums are amortized to the call date and bond discounts are accreted to the maturity date, both on a level yield basis.

We perform a quarterly review of our securities to identify those that may indicate an OTTI. Our policy for OTTI within the marketable equity securities portfolio generally requires an impairment charge when the security is in a loss position for 12 consecutive months, unless facts and circumstances would suggest the need for an OTTI prior to that time. Our policy for OTTI within the debt securities portfolio is based upon a number of factors, including but not limited to, the length of time and extent to which the estimated fair value has been less than cost, the financial condition of the underlying issuer, the ability of the issuer to meet contractual obligations, the best estimate of impairment charge representing credit losses, the likelihood of the security s ability to recover any decline in its estimated fair value and whether management intends to sell the security or if it is more likely than not that management will be required to sell the investment security prior to the security s recovery.

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. If a loan is transferred from the loan portfolio to the held-for-sale category, any write-down in the carrying amount of the loan at the date of transfer is recorded as a charge-off against the allowance for loan loss, or ALL. Subsequent declines in fair value are recognized as a charge to noninterest income. When a loan is placed in the held-for-sale category, we stop amortizing the related deferred fees and costs. The remaining unamortized fees and costs are recognized as part of the cost basis of the loan at the time it is sold. Gains and losses on sales of loans held for sale are included in other noninterest income in the Consolidated Statements of Net Income.

Loans

Loans are reported at the principal amount outstanding net of unearned income, unamortized premiums or discounts and deferred origination fees and costs. We defer certain nonrefundable loan origination and commitment fees. Accretion of discounts and amortization of premiums on loans are included in interest income in the Consolidated Statements of Net Income. Loan origination fees and direct loan origination costs are deferred and amortized as an adjustment of loan yield over the respective lives of the loans without consideration of anticipated prepayments. If a loan is paid off, the remaining unaccreted or unamortized net origination fees and costs are immediately recognized into income or expense. Interest is accrued on loans as earned. Interest income is recognized on loans as earned.

Closed-end installment loans, amortizing loans secured by real estate and any other loans with payments scheduled monthly are reported past due when the borrower is in arrears two or more monthly payments. Other multi-payment obligations with payments scheduled other than monthly are reported past due when one scheduled payment is due and unpaid for 30 days or more.

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Generally, consumer loans are charged off against the ALL upon the loan reaching 90 days past due. Commercial loans are charged off as management becomes aware of facts and circumstances that raise doubt as to the collectability of all or a portion of the principal and when we believe a confirmed loss exists.

Nonaccrual Loans

We stop accruing interest on a loan (nonaccrual loan) when the borrower s payment is 90 days past due. Loans are also placed on nonaccrual status when payment is not past due, but we have doubt about the borrower s ability to comply with existing repayment terms. When the interest accrual is discontinued, all unpaid accrued interest is reversed against interest income. Interest income is recognized on nonaccrual loans on a cash basis if recovery of the remaining principal is reasonably assured. As a general rule, a nonaccrual loan may be restored to accrual status when its principal and interest is paid current and the bank expects repayment of the remaining contractual principal and interest, or when the loan otherwise becomes well secured and in the process of collection.

Allowance for Loan Losses

The ALL reflects our estimates of probable losses inherent in the loan portfolio at the balance sheet date. The methodology for determining the ALL has two main components: evaluation and impairment tests of individual loans and evaluation and impairment tests of certain groups of homogeneous loans with similar risk characteristics.

A loan is considered impaired when it is probable that we will be unable to collect all principal and interest payments due according to the original contractual terms of the loan agreement. We individually evaluate all substandard, doubtful and nonaccrual commercial loans greater than $0.5 million for impairment. All troubled debt restructurings, or TDRs, are considered to be impaired loans and will be reported as an impaired loan for the remaining life of the loan, unless the restructuring agreement specifies an interest rate equal to or greater than the rate that would be accepted at the time of the restructuring for a new loan with comparable risk and it is fully expected that the remaining principal and interest will be collected according to the restructured agreement. For all TDRs, regardless of size, as well as all other impaired loans, we conduct further analysis to determine the probable loss and assign a specific reserve to the loan if deemed appropriate. Specific reserves are established based upon the following three impairment methods: 1) the present value of expected future cash flows discounted at the loan s original effective interest rate, 2) the loan s observable market price or 3) the estimated fair value of the collateral if the loan is collateral dependent. Our impairment evaluations consist primarily of the fair value of collateral method since most loans are collateral dependent. Collateral values are discounted to consider disposition costs when appropriate. A specific reserve is established or a charge-off is taken if the fair value of the impaired loan is less than the recorded investment in the loan balance.

The ALL for homogeneous loans is calculated using a systematic methodology that is applied on a quarterly basis. The ALL model is comprised of five distinct portfolio segments: 1) Commercial Real Estate, or CRE, 2) Commercial and Industrial, or C&I, 3) Commercial Construction, 4) Consumer Real Estate and 5) Other Consumer. Each segment has a distinct set of risk characteristics monitored by management. We further assess and monitor risk and performance at a more disaggregated level which includes our internal risk rating system for the commercial segments and collateral position and loan-to-value, or LTV, for the consumer segments.

Historical loss rate calculations are performed whereby past losses from each pool of loans are aggregated over the respective loss emergence period. The loss emergence period is defined as the average time between the occurrence of a credit event (deterioration in the borrower s financial condition) and the confirmation of a loss. Currently, we have estimated the loss emergence period to

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

be two years for CRE loans and one year for all other loan classes. We use a one year look back period that results, when considering our loss emergence periods, in capturing historic losses for three years for CRE and two years for our other portfolio segments. These historic loss calculations are then aggregated and applied to each loan segment to determine the component of the ALL based upon historic losses. Since the losses captured in the historical loss analysis may not accurately represent the losses inherent in the loan portfolio at the balance sheet date, qualitative adjustments are then applied to loan segments to determine the total ALL. Qualitative adjustments are aggregated into five categories, including process, economic conditions, loan portfolio, asset quality and other external factors.

Within the five aforementioned categories, the following qualitative factors are considered:

1) Changes in our lending policies and procedures, including underwriting standards, collection, charge-off and recovery practices not considered elsewhere in estimating credit losses;
2) Changes in national, regional, and local economic and business conditions and developments that affect the collectability of the portfolio, including the condition of various market segments;
3) Changes in the nature and volume of our loan portfolio and terms of loans;
4) Changes in the experience, ability and depth of our lending management and staff;
5) Changes in the volume and severity of past due loans, the volume of non accrual loans, and the volume and severity of adversely classified or graded loans;
6) Changes in the quality of our loan review system;
7) Changes in the value of the underlying collateral for collateral-dependent loans;
8) The existence and effect of any concentrations of credit and changes in the level of such concentrations; and
9) The effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in our current loan portfolio.

Bank Owned Life Insurance

We have purchased life insurance policies on certain executive officers and employees. We receive the cash surrender value of each policy upon its termination or benefits are payable upon the death of the insured. Changes in net cash surrender value are recognized in noninterest income or expense in the Consolidated Statements of Net Income.

Premises and Equipment

Premises and equipment, including leasehold improvements, are stated at cost less accumulated depreciation. Maintenance and repairs are charged to expense as incurred, while improvements that extend an asset s useful life are capitalized and depreciated over the estimated remaining life of the asset. Depreciation expense is computed generally by the straight-line method for financial reporting purposes and accelerated methods for income tax purposes. Leasehold improvements are amortized over the shorter of the asset s useful life or the remaining lease term, including renewal periods when reasonably assured.

Restricted Investment in Bank Stock

Federal Home Loan Bank, or FHLB, stock is carried at cost and evaluated for impairment based on the ultimate recoverability of the par value. We hold FHLB stock because we are a member of the FHLB of Pittsburgh. The FHLB requires members to purchase and hold a specified level of FHLB stock based upon on the members asset value, level of borrowings and participation in other programs offered. Stock in the FHLB is non-marketable and is redeemable at the discretion of the FHLB. Members do not purchase stock in the FHLB for the same reasons that traditional equity investors acquire stock in an investor-owned enterprise. Rather, members purchase stock to obtain access to

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

the low-cost products and services offered by the FHLB. Unlike equity securities of traditional for-profit enterprises, the stock of the FHLB does not provide its holders with an opportunity for capital appreciation because, by regulation, FHLB stock can only be purchased, redeemed and transferred at par value. Both cash and stock dividends are reported as income in taxable investment securities in the Consolidated Statements of Net Income.

On February 22, 2012, the FHLB of Pittsburgh announced that it would pay a dividend on the average capital stock balance held during the three month period ended December 31, 2011 at an annualized rate of 0.10% for the first time since late 2008. The FHLB noted future dividend payments and capital stock repurchases will continue to be reviewed on a quarterly basis. We had $5.7 million of redemptions from the FHLB throughout 2012. We reviewed and evaluated the FHLB capital stock for OTTI at December 31, 2012. Based upon our review of the FHLB s current financial position, they reported improved earnings throughout 2012 compared to 2011 and continue to exceed all capital ratios required. Additionally, we considered that the FHLB began paying dividends and redeeming excess stock during 2012. Accordingly, we believe sufficient evidence exists to conclude that no OTTI exists at December 31, 2012.

Goodwill and Other Intangible Assets

We have three reporting units: Community Banking, Wealth Management and Insurance. At December 31, 2012, we had goodwill of $175.7 million, including $171.5 million in Community Banking, representing 98 percent of total goodwill and $4.2 million in Insurance, representing two percent of total goodwill. The carrying value of goodwill is tested annually for impairment each October 1 or more frequently if it is determined that we should do so. We first assess qualitatively whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. Our qualitative assessment considers such factors as macroeconomic conditions, market conditions specifically related to the banking industry, our overall financial performance and various other factors. If we determine that it is more likely than not that the fair value is less than the carrying amount, we proceed to test for impairment. The evaluation for impairment involves comparing the current estimated fair value of each reporting unit to its carrying value, including goodwill. If the current estimated fair value of a reporting unit exceeds its carrying value, no additional testing is required and impairment loss is not recorded. If the estimated fair value of a reporting unit is less than the carrying value, further valuation procedures are performed and could result in impairment of goodwill being recorded. Further valuation procedures would include allocating the estimated fair value to all assets and liabilities of the reporting unit to determine an implied goodwill value. If the implied value of goodwill of a reporting unit is less than the carrying amount of that goodwill, an impairment loss is recognized in an amount equal to that excess.

We have core deposit and other intangible assets resulting from acquisitions which are subject to amortization. We determine the amount of identifiable intangible assets based upon independent core deposit and insurance contract analyses at the time of the acquisition. Intangible assets with finite useful lives are evaluated for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. No events or changes in circumstances that would indicate that the carrying amount of any identifiable intangible assets may not be recoverable had occurred during the years ended December 31, 2012, 2011 and 2010.

Joint Ventures

We have made investments directly in Low Income Housing Tax Credit, or LIHTC, partnerships formed with third parties. As a limited partner in these operating partnerships, we receive tax credits and tax deductions for losses incurred by the underlying properties. These investments are amortized

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

over a maximum of 10 years, which represents the period that the tax credits will be utilized. We have determined that we are not the primary beneficiary of these investments because the general partners have the power to direct the activities that most significantly impact the economic performance of the partnership and have the obligation to absorb expected losses and the right to receive benefits.

OREO and Other Repossessed Assets

OREO and other repossessed assets are included in other assets in the Consolidated Balance Sheets and are comprised of properties acquired through foreclosure proceedings or acceptance of a deed in lieu of a foreclosure. At the time of foreclosure, these properties are recorded at the lower of the recorded investment in the loan or fair value less cost to sell. Loan losses arising from the acquisition of such property initially are charged against the ALL. Subsequently, these assets are carried at the lower of carrying value or current fair value less cost to sell. Gains or losses realized subsequent to acquisition are recorded in other expenses in the Consolidated Statements of Net Income.

Mortgage Servicing Rights

MSRs are recognized as separate assets when commitments to fund a loan to be sold are made. Upon commitment, the MSR is established, which represents the then current estimated fair value of future net cash flows expected to be realized for performing the servicing activities. The estimated fair value of the MSRs is estimated 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 MSRs. Increases in mortgage loan prepayments reduce estimated future net servicing cash flows because the life of the underlying loan is reduced. In determining the estimated fair value of MSRs, mortgage interest rates, which are used to determine prepayment rates, are held constant over the estimated life of the portfolio. MSRs are reported in other assets in the Consolidated Balance Sheets and are amortized into noninterest income in the Consolidated Statements of Net Income in proportion to, and over the period of, the estimated future net servicing income of the underlying mortgage loans.

MSRs are regularly evaluated for impairment based on the estimated fair value of those rights. The MSRs are stratified by certain risk characteristics, primarily loan term and note rate. If temporary impairment exists within a risk stratification tranche, a valuation allowance is established through a charge to income equal to the amount by which the carrying value exceeds the estimated fair value. If it is later determined all or a portion of the temporary impairment no longer exists for a particular tranche, the valuation allowance is reduced.

MSRs are also reviewed for OTTI. OTTI exists when the recoverability of a recorded valuation allowance is determined to be remote, taking into consideration historical and projected interest rates and loan pay-off activity. When this situation occurs, the unrecoverable portion of the valuation allowance is applied as a direct write-down to the carrying value of the MSR. Unlike a valuation allowance, a direct write-down permanently reduces the carrying value of the MSR and the valuation allowance, precluding subsequent recoveries.

Derivative Financial Instruments

Interest Rate Swaps

In accordance with applicable accounting guidance for derivatives and hedging, all derivatives are recognized as either assets or liabilities on the balance sheet at fair value. Interest rate swaps are contracts in which a series of interest rate flows (fixed and variable) are exchanged over a prescribed period. The notional amounts on which the interest payments are based are not exchanged. We

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

utilize interest rate swaps for commercial loans. These derivative positions relate to transactions in which we enter into an interest rate swap with a customer while at the same time entering into an offsetting interest rate swap with another financial institution. In connection with each transaction, we agree to pay interest to the customer on a notional amount at a variable interest rate and receive interest from the customer on a same notional amount at a fixed rate. At the same time, we agree to pay another financial institution the same fixed interest rate on the same notional amount and receive the same variable interest rate on the same notional amount. The transaction allows our customer to effectively convert a variable rate loan to a fixed rate loan with us receiving a variable yield. These agreements could have floors or caps on the contracted interest rates.

Pursuant to our agreements with various financial institutions, we may receive collateral or may be required to post collateral based upon mark-to-market positions. Beyond unsecured threshold levels, collateral in the form of cash or securities may be made available to counterparties of interest rate swap transactions. Based upon our current positions and related future collateral requirements relating to them, we believe any effect on our cash flow or liquidity position to be immaterial. Derivatives contain an element of credit risk, the possibility that we will incur a loss because a counterparty, which may be a financial institution or a customer, fails to meet its contractual obligations. All derivative contracts with financial institutions may be executed only with counterparties approved by our Asset and Liability Committee, or ALCO, and derivatives with customers may only be executed with customers within credit exposure limits approved by our Senior Loan Committee. Interest rate swaps are considered derivatives, but are not accounted for using hedge accounting. As such, changes in the estimated fair value of the derivatives are recorded in current earnings and included in other noninterest income in the Consolidated Statements of Net Income.

Interest Rate Lock Commitments and Forward Sale Contracts

In the normal course of business, we sell originated mortgage loans into the secondary mortgage loan market. We also offer interest rate lock commitments to potential borrowers. The commitments are generally for 60 days and guarantee a specified interest rate for a loan if underwriting standards are met, but the commitment does not obligate the potential borrower to close on the loan. Accordingly, some commitments expire prior to becoming loans. We can encounter pricing risks if interest rates increase significantly before the loan can be closed and sold. We may utilize forward sale contracts in order to mitigate this pricing risk. Whenever a customer desires these products, a mortgage originator quotes a secondary market rate guaranteed for that day by the investor. The rate lock is executed between the mortgagee and us and in turn a forward sale contract may be executed between us and the investor. Both the rate lock commitment and the corresponding forward sale contract for each customer are considered derivatives, but are not accounted for using hedge accounting. As such, changes in the estimated fair value of the derivatives during the commitment period are recorded in current earnings and included in mortgage banking in the Consolidated Statements of Net Income.

Allowance for Unfunded Commitments

In the normal course of business, we offer off-balance sheet credit arrangements to enable our customers to meet their financing objectives. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the financial statements. Our exposure to credit loss, in the event the customer does not satisfy the terms of the agreement, equals the contractual amount of the obligation less the value of any collateral. We apply the same credit policies in making commitments and standby letters of credit that are used for the underwriting of loans to customers. Commitments generally have fixed expiration dates, annual renewals or other termination clauses and may require payment of a fee. Since many of the commitments are expected

79

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The allowance for unfunded commitments is included in other liabilities in the Consolidated Balance Sheets. The allowance for unfunded commitments is determined using a similar methodology as our ALL. The reserve is calculated by applying historical loss rates from our ALL model to the estimated future utilization of our unfunded commitments.

Treasury Stock

The repurchase of our common stock is recorded at cost. At the time of reissuance, the treasury stock account is reduced using the average cost method. Gains and losses on the reissuance of common stock are recorded in additional paid-in capital, to the extent additional paid-in capital from previous treasury share transactions exists. Any deficiency is charged to retained earnings.

Wealth Management Fees

Assets held in a fiduciary capacity by the subsidiary bank, S&T Bank, are not our assets and are therefore not included in our Consolidated Financial Statements. Wealth management fee income is reported in the Consolidated Statements of Net Income on the accrual basis.

Stock-Based Compensation

Stock-based compensation may include stock options and restricted stock which is measured using the fair value method of accounting. The grant date fair value is recognized over the period during which the recipient is required to provide service in exchange for the award. Stock option expense is determined utilizing the Black-Scholes model. Restricted stock expense is determined using the grant date fair value. We estimate expected forfeitures when stock-based awards are granted and record compensation expense only for awards that are expected to vest.

Pensions

Pension expense for S&T Bank s defined benefit pension plan is actuarially determined using the projected unit credit actuarial cost method. The funding policy for the plan is to contribute amounts to the plan sufficient to meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974, or ERISA, plus such additional amounts as may be appropriate, subject to federal income tax limitation.

Marketing Costs

We expense all marketing-related costs, including advertising costs, as incurred.

Income Taxes

We estimate income tax expense based on amounts expected to be owed to the tax jurisdictions where we conduct business. On a quarterly basis, management assesses the reasonableness of our effective tax rate based upon our current estimate of the amount and components of net income, tax credits and the applicable statutory tax rates expected for the full year.

Deferred income tax assets and liabilities are determined using the asset and liability method and are reported in other assets or other liabilities, as appropriate, in the Consolidated Balance Sheets. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax basis of assets and liabilities and recognizes enacted changes in tax rate and laws. When deferred tax assets are recognized, they are subject to a valuation allowance based on management s judgment as to whether realization is more likely than not.

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Accrued taxes represent the net estimated amount due to taxing jurisdictions and are reported in other assets or other liabilities, as appropriate, in the Consolidated Balance Sheets. We evaluate and assess the relative risks and appropriate tax treatment of transactions and filing positions after considering statutes, regulations, judicial precedent and other information and maintain tax accruals consistent with the evaluation of these relative risks and merits. Changes to the estimate of accrued taxes occur periodically due to changes in tax rates, interpretations of tax laws, the status of examinations being conducted by taxing authorities and changes to statutory, judicial and regulatory guidance. These changes, when they occur, can affect deferred taxes and accrued taxes, as well as the current period s income tax expense and can be significant to our operating results.

Tax positions are recognized as a benefit only if it is more likely than not that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50 percent likely of being realized on examination. For tax positions not meeting the more likely than not test, no tax benefit is recorded.

Earnings Per Share

Basic earnings per share, or EPS, is calculated using the two-class method to determine income allocated to common shareholders. Unvested share-based payment awards that contain nonforfeitable rights to dividends are considered participating securities under the two-class method. Income allocated to common shareholders is then divided by the weighted average number of common shares outstanding during the period. Potentially dilutive securities are excluded from the basic EPS calculation.

Diluted earnings per share is calculated under the more dilutive of either the treasury stock method or the two-class method. Under the treasury stock method, the weighted average number of common shares outstanding is increased by the potentially dilutive common shares. For the two-class method, diluted earnings per share is calculated for each class of shareholders using the weighted average number of shares attributed to each class. Potentially dilutive common shares are common stock equivalents relating to our outstanding warrants, stock options and restricted stock.

Recently Adopted Accounting Standards Updates

Technical Corrections and Improvements

In October 2012, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update, or ASU, No. 2012-04, Technical Corrections and Improvements, which was meant to correct minor technical errors in the codification and to conform terminology and clarify certain guidance in various topics of the codification to fully reflect the fair value measurement and disclosure requirements of Topic 820. Since this includes minor corrections, terminology conformation and guidance clarification only of previously issued accounting guidance, it was adopted at December 31, 2012, and did not have an impact on our results of operations or financial position.

Technical Amendments and Corrections to SEC Sections

In August 2012, the FASB issued ASU No. 2012-03, Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 114, Technical Amendments Pursuant to SEC Release No. 33-9250, and Corrections Related to FASB Accounting Standards Update 2010-22 (SEC Update), which were meant to codify various amendments and corrections included in these previously issued bulletins and releases. Since this is codification only of previously issued accounting guidance, it was adopted at September 30, 2012, and did not have an impact on our results of operations or financial position.

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

Presentation of Comprehensive Income

In December 2011, the FASB issued ASU No. 2011-12, which superseded certain pending paragraphs in ASU No. 2011-05, which had been issued in June 2011. ASU No. 2011-05 allowed 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 but permits companies to present in the annual period the comprehensive income components in a single continuous statement or two consecutive statements and to present in the interim periods only the total for comprehensive income in a single continuous statement or two consecutive statements. ASU No. 2011-12 effectively defers changes that relate to the presentation of reclassification adjustments out of accumulated other comprehensive income. The amendments will be temporary to allow the FASB time to redeliberate the presentation requirements for reclassifications out of accumulated other comprehensive income for annual and interim financial statements. The two amendments became effective at the same time. These ASUs should be applied retrospectively and were effective for public companies for fiscal years, and interim periods within those years, beginning after December 15, 2011. We have elected the option of a single continuous statement format for interim periods, and two separate but consecutive statements for annual periods. The adoption of both ASU 2011-05 and 2011-12 impacted only our presentation of comprehensive income and did not have an impact on our results of operations or financial position.

Testing Goodwill for Impairment

In September 2011, the FASB issued ASU No. 2011-08, which permits an entity to make a qualitative assessment of whether it is more likely than not that a reporting unit s fair value is less than its carrying amount before applying the two-step goodwill impairment test. If an entity concludes it is not more likely than not that its fair value is less than its carrying amount, it need not perform the two-step impairment test. This ASU is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted. The adoption of this ASU did not have a material impact on our results of operations or financial position.

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

In May 2011, the FASB issued ASU No. 2011-04, which represents the convergence of the FASB s and the International Accounting Standard Board s, or IASB, guidance on fair value measurement. ASU 2011-04 reflects the common requirements under U.S. GAAP and international financial reporting standards, or 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 U.S. GAAP or IFRS. For U.S. GAAP, most of the changes are clarifications of existing guidance or wording changes to align with IFRS 13 Fair Value Measurement. 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 impacted only disclosure requirements and did not have a material impact on our results of operations or financial position.

82

Table of Contents

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

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, or 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 did not have a material impact on our results of operations or financial position.

Recently Issued Accounting Standards Updates not yet Adopted

Disclosures About Offsetting Assets and Liabilities

In December 2011, the FASB issued ASU, No. 2011-11, in conjunction with the issuance by the IASB, of amendments to Disclosures Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7). The disclosure requirements apply to recognized financial instruments and derivative instruments that are offset or subject to an enforceable master netting arrangement. An entity shall disclose information to enable users of its financial statements to evaluate the effect or potential effect of netting arrangements on its financial position, including the effect or potential effect of rights of setoff associated with recognized assets and recognized liabilities. While both the FASB and the IASB retained the existing offsetting models under U.S. GAAP and IFRS, the new standards require disclosures to allow investors to better compare financial statements prepared under U.S. GAAP with financial statements prepared under IFRS. The new standards are effective for annual periods beginning January 1, 2013, and interim periods within those annual periods. Retrospective application is required. The adoption of this ASU is expected to impact only our disclosure requirements and is not expected to have a material impact on our results of operations or financial position.

NOTE 2. BUSINESS COMBINATIONS

During 2012, we completed two acquisitions, Mainline Bancorp, Inc., or Mainline and Gateway Bank of Pennsylvania, or Gateway. Goodwill was calculated as the excess of the consideration exchanged over the net identifiable assets acquired from each acquisition and will not be deductible for tax purposes. Goodwill from both acquisitions was assigned to our Community Banking segment.

On March 9, 2012, we acquired 100 percent of the voting shares of Mainline, located in Ebensburg, Pennsylvania, which was the holding company and sole shareholder of Mainline National Bank. The acquisition expanded our market share and footprint throughout Cambria and

Blair Counties of Western Pennsylvania. Mainline shareholders were entitled to elect to receive for each share of Mainline common stock either $69.00 in cash or 3.6316 shares of S&T common stock. We also purchased Mainline s preferred stock issued under the U.S. Treasury Capital Purchase Program, or CPP, for $4.7 million on March 9, 2012. The preferred stock was purchased and retired as part of the merger transaction. Purchase accounting guidance allows for a reasonable period of time following an acquisition for the acquirer to obtain the information necessary to complete the accounting for a

Table of Contents

NOTE 2. BUSINESS COMBINATIONS continued

business combination. This period, known as the measurement period, shall not exceed one year from the acquisition date. The measurement period for the Mainline acquisition ends March 9, 2013. Based on new information received about facts and circumstances that existed as of the acquisition date one measurement period adjustment for $0.5 million was recorded relating to a contingent liability for an IRS proposed penalty for tax year 2010. Cash paid to former Mainline shareholders was $8.2 million and the fair value of common shares issued was $14.8 million. As of December 31, 2012, S&T recognized Goodwill of $6.7 million from the Mainline acquisition.

On August 13, 2012, we acquired 100 percent of the voting shares of Gateway, located in McMurray, Pennsylvania. The acquisition expanded our market share and footprint into Washington and Butler counties in Pennsylvania. Gateway shareholders were entitled to receive $3.08 in cash and 0.4657 shares of S&T common stock in exchange for one share of Gateway common stock. As of December 31, 2012, Gateway was operating as a separate wholly-owned subsidiary of S&T. On February 8, 2013, Gateway Bank was merged into S&T Bank, and their two branches are now fully operational branches of S&T Bank. Cash paid to former Gateway shareholders was $5.2 million and the fair value of common shares issued was $13.3 million. We also settled outstanding equity awards for $1.0 million. As of December 31, 2012, S&T recognized Goodwill of $3.8 million from the Gateway acquisition.

The following table summarizes total consideration paid, assets acquired and liabilities assumed as of December 31, 2012 for both the Mainline and Gateway acquisitions:

(in thousands)	**Mainline**	**Gateway**	**Combined**
Consideration Paid			
Cash	$ 12,904	$ 6,238	$ 19,142
Common stock	14,786	13,284	28,070
Fair value of previously held equity interest	74	272	346
Fair Value of Total Consideration	**$ 27,764**	**$ 19,794**	**$ 47,558**
Fair Value of Assets Acquired			
Cash and cash equivalents	$ 17,763	$ 20,018	$ 37,781
Securities and other investments	73,328	9,564	82,892
Loans	129,501	99,090	228,591
Premises and other equipment	2,280	495	2,775
Core deposit intangible	900	431	1,331
Other assets	12,438	2,665	15,103
Total Assets Acquired	**$ 236,210**	**$ 132,263**	**$ 368,473**
Fair Value of Liabilities Assumed			
Deposits	205,989	105,400	311,389
Borrowings	6,997	9,777	16,774
Other liabilities	2,144	1,068	3,212
Total Liabilities Assumed	**$ 215,130**	**$ 116,245**	**$ 331,375**
Total Fair Value of Identifiable Net Assets	**21,080**	**16,018**	**37,098**
Goodwill	**$ 6,684**	**$ 3,776**	**$ 10,460**

Acquired loans were recorded at fair value with no carryover of the related allowance for loan losses. Determining the fair value of the loans involved estimating the amount and timing of principal and interest cash flows expected to be collected on the loans and discounting those cash flows at a market rate of interest. Loans acquired with evidence of credit quality deterioration were not significant. We acquired $231.9 million of gross loans and recognized a net combined yield and credit mark of $3.3 million.

Table of Contents

NOTE 2. BUSINESS COMBINATIONS continued

Direct costs related to the acquisitions were expensed as incurred. As of December 31, 2012, we recognized a combined total of $6.0 million of one-time merger related expenses. For the Gateway acquisition, we recognized $1.5 million of one-time merger related expenses; consisting primarily of legal, professional and other expenses of $0.6 million, $0.6 million in change in control, severance and other employee costs and $0.3 million in data processing contract termination and conversion costs. For the Mainline acquisition, we recognized $4.5 million of one-time merger related expenses; including $1.8 million in change in control, severance and other employee costs, $2.0 million in data processing contract termination and conversion costs and $0.7 million in legal, professional and other expenses.

NOTE 3. EARNINGS PER SHARE

The following table reconciles the numerators and denominators of basic EPS with that of diluted EPS:

	Years ended December 31,		
(in thousands, except share and per share data)	**2012**	**2011**	**2010**
Numerator for Earnings per Common Share Basic:			
Net income	$ 34,200	$ 47,264	$ 43,480
Less: Preferred stock dividends and discount amortization		7,611	6,201
Less: Income allocated to participating shares	126	130	42
Net Income Allocated to Common Shareholders	**$ 34,074**	**$ 39,523**	**$ 37,237**
Numerator for Earnings per Common Share Diluted:			
Net income	$ 34,200	$ 47,264	$ 43,480
Less: Preferred stock dividends and discount amortization		7,611	6,201
Net Income Available to Common Shareholders	**$ 34,200**	**$ 39,653**	**$ 37,279**
Denominators:			
Weighted Average Common Shares Outstanding Basic	**28,976,619**	**27,966,981**	**27,791,145**
Add: Potentially dilutive common shares	32,261	23,169	22,261
Denominator for Treasury Stock Method Diluted	**29,008,880**	**27,990,150**	**27,813,406**
Weighted Average Common Shares Outstanding Basic	**28,976,619**	**27,966,981**	**27,791,145**
Add: Average participating shares outstanding	107,274	92,212	33,899
Denominator for Two-Class Method Diluted	**29,083,893**	**28,059,193**	**27,825,044**
Earnings per common share basic	$ 1.18	$ 1.41	$ 1.34
Earnings per common share diluted	$ 1.18	$ 1.41	$ 1.34
Warrants considered anti-dilutive excluded from dilutive potential common shares	517,012	517,012	517,012
Stock options considered anti-dilutive excluded from dilutive potential common shares	747,443	757,580	930,969
Restricted stock considered anti-dilutive excluded from dilutive potential common shares	75,012	69,043	11,638

85

Table of Contents

NOTE 4. FAIR VALUE MEASUREMENTS

Refer to Note 1 Summary of Significant Accounting Policies under Fair Value Measurements for our accounting policy including details of the valuation methods used to determine the fair values of our assets and liabilities.

The following tables present our assets and liabilities that are measured at fair value on a recurring basis by fair value hierarchy level at December 31, 2012 and 2011. There were no transfers between Level 1 and Level 2 for items measured at fair value on a recurring basis during the periods presented.

	December 31, 2012			
(in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
ASSETS				
Securities available-for-sale:				
Obligations of U.S. government corporations and agencies	$	$ 212,066	$	$ 212,066
Collateralized mortgage obligations of U.S. government corporations and agencies		57,896		57,896
Mortgage-backed securities of U.S. government corporations and agencies		60,781		60,781
Obligations of states and political subdivisions		112,767		112,767
Marketable equity securities	140	8,316	1,130	9,586
Total securities available-for-sale	**140**	**451,826**	**1,130**	**453,096**
Trading securities held in a Rabbi Trust	2,223			2,223
Total securities	**2,363**	**451,826**	**1,130**	**455,319**
Derivative financial assets:				
Interest rate swaps		23,748		23,748
Interest rate lock commitments		467		467
Total Assets	**$ 2,363**	**$ 476,041**	**$ 1,130**	**$ 479,534**
LIABILITIES				
Derivative financial liabilities:				
Interest rate swaps	$	$ 23,522	$	$ 23,522
Forward sale contracts		48		48
Total Liabilities	**$**	**$ 23,570**	**$**	**$ 23,570**

Table of Contents

NOTE 4. FAIR VALUE MEASUREMENTS continued

(in thousands)	December 31, 2011 Level 1	Level 2	Level 3	Total
ASSETS				
Securities available-for-sale:				
Obligations of U.S. government corporations and agencies	$	$ 142,786	$	$ 142,786
Collateralized mortgage obligations of U.S. government corporations and agencies		65,395		65,395
Mortgage-backed securities of U.S. government corporations and agencies		48,752		48,752
Obligations of states and political subdivisions		88,805		88,805
Marketable equity securities	2,855	7,316	1,687	11,858
Total securities available-for-sale	**2,855**	**353,054**	**1,687**	**357,596**
Trading securities held in a Rabbi Trust	1,949			1,949
Total securities	**4,804**	**353,054**	**1,687**	**359,545**
Derivative financial assets:				
Interest rate swaps		23,764		23,764
Interest rate lock commitments		244		244
Total Assets	**$ 4,804**	**$ 377,062**	**$ 1,687**	**$ 383,553**
LIABILITIES				
Derivative financial liabilities:				
Interest rate swaps	$	$ 23,639	$	$ 23,639
Forward sale contracts	$	$ 95	$	$ 95
Total Liabilities	**$**	**$ 23,734**	**$**	**$ 23,734**

We classify financial instruments as Level 3 when valuation models are used because significant inputs are not observable in the market. The following tables present the changes in assets measured at fair value on a recurring basis for which we have utilized Level 3 inputs to determine the fair value:

(in thousands)	Years Ended December 31, 2012	2011
Balance at beginning of year	$ 1,687	$ 1,588
Total (losses) gains included in other comprehensive income/loss[(1)]	(350)	99
Net purchases, sales, issuances and settlements	(207)	
Transfers out of Level 3		
Balance at end of year	**$ 1,130**	**$ 1,687**

[(1)] *Changes in estimated fair value of available-for-sale investments are recorded in accumulated other comprehensive income/loss, while gains and losses from sales are recorded in security gains (losses), net in the Consolidated Statements of Net Income.*

Table of Contents

NOTE 4. FAIR VALUE MEASUREMENTS continued

We may be required to measure certain assets and liabilities on a nonrecurring basis. The following tables present our assets that are measured at estimated fair value on a nonrecurring basis by the fair value hierarchy level at December 31, 2012 and 2011. There were no liabilities measured at estimated fair value on a nonrecurring basis during these periods. Loans held for sale are recorded at the lower of cost or fair value. At December 31, 2012 and 2011, we had no loans held for sale that were recorded at fair value.

	December 31, 2012			
(in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
ASSETS				
Impaired Loans	$	$	$ 44,059	$ 44,059
Other real estate owned			585	585
Mortgage servicing rights			2,106	2,106
Total Assets	**$**	**$**	**$ 46,750**	**$ 46,750**

	December 31, 2011			
(in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
ASSETS				
Impaired Loans	$	$	$ 36,500	$ 36,500
Other real estate owned			3,739	3,739
Mortgage servicing rights			2,153	2,153
Total Assets	**$**	**$**	**$ 42,392**	**$ 42,392**

The carrying values and fair values of our financial instruments at December 31, 2012 and 2011 are presented in the following tables:

		Fair Value Measurements at December 31, 2012			
(in thousands)	**Carrying Value***(1)*	**Total**	**Level 1**	**Level 2**	**Level 3**
ASSETS					
Cash and due from banks, including interest-bearing deposits	$ 337,711	$ 337,711	$ 337,711	$	