HORIZON BANCORP /IN/
Form 10-Q
August 14, 2009

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HORIZON BANCORP
FORM 10-Q
United States
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2009
Commission file number 0-10792
HORIZON BANCORP
(Exact name of registrant as specified in its charter)

Indiana	**35-1562417**
(State or other jurisdiction of incorporation or organization)	(I.R. S. Employer Identification No.)
515 Franklin Square, Michigan City, Indiana	**46360**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(219) 879-0211**

Former name, former address and former fiscal year, if changed since last report: **N/A**

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 þ No o

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

Yes o No o

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

Large Accelerated Filer o	Accelerated Filer o	Non-accelerated Filer o	Smaller Reporting Company þ

(Do not check if a smaller reporting company)

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

Yes o No þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 3,271,631 at August 14, 2009.

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PART 1 FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

HORIZON BANCORP AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(Dollar Amounts in Thousands)

	June 30 2009 (Unaudited)	December 31 2008
Assets		
Cash and due from banks	**$ 13,885**	$ 36,001
Federal Reserve and fed funds sold	**2,695**	
Cash and cash equivalents	**16,580**	36,001
Interest-bearing deposits	**10,418**	2,679
Investment securities, available for sale	**319,066**	301,638
Investment securities, held to maturity	**12,875**	1,630
Loans held for sale	**9,793**	5,955
Loans, net of allowance for loan losses of $12,649 and $11,410	**882,781**	870,557
Premises and equipment	**30,210**	28,280
Federal Reserve and Federal Home Loan Bank stock	**13,225**	12,625
Goodwill	**5,787**	5,787
Other intangible assets	**1,597**	1,751
Interest receivable	**6,051**	5,708
Cash value life insurance	**22,792**	22,451
Deferred tax asset	**2,520**	2,580
Other assets	**9,601**	9,215
Total assets	**$1,343,296**	$1,306,857
Liabilities		
Deposits		
Non-interest bearing	**$ 83,940**	$ 83,642
Interest bearing	**764,210**	757,527
Total deposits	**848,150**	841,169
Borrowings	**349,499**	324,383
Subordinated debentures	**27,837**	27,837
Interest payable	**1,657**	1,910
Other liabilities	**8,959**	8,208
Total liabilities	**1,236,102**	1,203,507
Commitments and contingent liabilities		
Stockholders Equity		
Preferred stock, no par value, $1,000 liquidation value		
Authorized, 1,000,000 shares		
Issued 25,000 shares		

Common stock, $.2222 stated value	**24,229**	24,154
Authorized, 22,500,000 shares		
Issued, 3,266,611 and 3,254,482 shares	**1,114**	1,114
Additional paid-in capital	**9,785**	9,650
Retained earnings	**70,807**	67,804
Accumulated other comprehensive income	**1,259**	628
Total stockholders equity	**107,194**	103,350
Total liabilities and stockholders equity	**$1,343,296**	$1,306,857

See notes to condensed consolidated financial statements

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HORIZON BANCORP AND SUBSIDIARIES
Condensed Consolidated Statements of Income
(Dollar Amounts in Thousands, Except Per Share Data)

	Three Months Ended June 30		Six Months Ended June 30	
	2009 (Unaudited)	2008 (Unaudited)	2009 (Unaudited)	2008 (Unaudited)
Interest Income				
Loans receivable	**$15,091**	$14,194	**$29,996**	$29,561
Investment securities				
Taxable	**2,811**	2,214	**5,660**	4,762
Tax exempt	**947**	862	**1,867**	1,699
Total interest income	**18,849**	17,270	**37,523**	36,022
Interest Expense				
Deposits	**3,993**	4,697	**7,989**	11,291
Borrowed funds	**3,222**	2,846	**6,114**	5,674
Subordinated debentures	**371**	392	**741**	799
Total interest expense	**7,586**	7,935	**14,844**	17,764
Net Interest Income	**11,263**	9,335	**22,679**	18,258
Provision for loan losses	**3,290**	1,490	**6,487**	2,268
Net Interest Income after Provision for Loan Losses	**7,973**	7,845	**16,192**	15,990
Other Income				
Service charges on deposit accounts	**974**	989	**1,908**	1,910
Wire transfer fees	**261**	122	**508**	227
Interchange fees	**456**	214	**844**	402
Fiduciary activities	**824**	1,021	**1,741**	1,906
Gain on sale of loans	**1,671**	661	**3,584**	1,465
Mortgage servicing net of impairment	**(32)**	29	**(166)**	5
Increase in cash surrender value of bank owned life insurance	**185**	221	**341**	449
Death benefit on officer life insurance		538		538
Loss on sale of securities		(15)		(15)
Other income	**177**	118	**250**	224
Total other income	**4,516**	3,898	**9,010**	7,111

Other Expenses				
Salaries and employee benefits	**4,894**	4,220	**9,725**	8,495
Net occupancy expenses	**899**	918	**1,931**	1,890
Data processing	**396**	350	**775**	682
Professional fees	**310**	291	**705**	540
Outside services and consultants	**351**	308	**677**	612
Loan expense	**644**	552	**1,210**	1,010
FDIC deposit expense	**1,059**	142	**1,351**	258
Other losses	**82**	141	**467**	242
Other Expenses	**1,293**	1,317	**2,484**	2,537
Total other expenses	**9,928**	8,239	**19,325**	16,266
Income Before Income Tax	**2,561**	3,504	**5,877**	6,835
Income tax expense	**497**	514	**1,178**	1,317
Net Income	**2,064**	2,990	**4,699**	5,518
Preferred stock dividend and discount accretion	**(350)**		**(700)**	
Net Income Available to Common Shareholders	**$ 1,714**	$ 2,990	**$ 3,999**	$ 5,518
Basic Earnings Per Share	**$ 0.53**	$ 0.93	**$ 1.25**	$ 1.72
Diluted Earnings Per Share	**$ 0.52**	$ 0.92	**$ 1.22**	$ 1.70

See notes to condensed consolidated financial statements

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Horizon Bancorp and Subsidiaries
Condensed Consolidated Statement of Stockholders Equity
(Unaudited)
(Table Dollar Amounts in Thousands, Except Per Share Data)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Comprehensive Income	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balances, December 31, 2008	$ 24,154	$ 1,114	$ 9,650		$ 67,804	$ 628	$ 103,350
Net income				$ 4,699	4,699		4,699
Amortization of discount on preferred stock	75				(75)		
Other comprehensive income (loss), net of tax							
Unrealized gain on securities				552		552	552
Unrealized gain on derivative instruments				79		79	79
Comprehensive income				$ 5,330			
Amortization of unearned compensation			116				116
Stock option expense			19				19
Cash dividends on preferred stock (5.00%)					(508)		(508)
Cash dividends on common stock ($.34 per share)					(1,113)		(1,113)
Balances, June 30, 2009	**$ 24,229**	**$ 1,114**	**$ 9,785**		**$ 70,807**	**$ 1,259**	**$ 107,194**

See notes to condensed consolidated financial statements

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HORIZON BANCORP AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Dollar Amounts in Thousands)

	Six Months Ended June 30 2009 (Unaudited)	Six Months Ended June 30 2008 (Unaudited)
Operating Activities		
Net income	**$ 4,699**	$ 5,518
Items not requiring (providing) cash		
Provision for loan losses	**6,487**	2,268
Depreciation and amortization	**1,167**	1,164
Share based compensation	**19**	19
Mortgage servicing rights impairment	**158**	7
Deferred income tax	**(278)**	(596)
Premium amortization on securities available for sale, net	**249**	147
Gain on sale of loans	**(3,584)**	(1,272)
Loss on sale of Investment securities		15
Proceeds from sales of loans	**204,229**	72,071
Loans originated for sale	**(206,503)**	(72,419)
Increase in cash surrender value of life insurance	**(341)**	(22)
Loss on sale of other real estate owned	**92**	
Net change in		
Interest receivable	**(343)**	9
Interest payable	**(253)**	(473)
Other assets	**1,063**	851
Other liabilities	**1,137**	(85)
Net cash provided by operating activities	**7,998**	7,202
Investing Activities		
Net change in interest-bearing deposits	**(7,739)**	(1,129)
Purchases of securities available for sale	**(53,019)**	(33,159)
Proceeds from sales, maturities, calls, and principal repayments of securities available for sale	**36,190**	13,080
Purchase of securities held to maturity	**(11,245)**	(815)
Purchases of FRB Stock	**(600)**	
Net change in loans	**(24,014)**	10,245
Proceeds on sale of OREO and repossessed assets	**5,359**	
Recoveries on loans previously charged-off		444
Purchases of premises and equipment	**(2,827)**	(1,856)
Proceeds from sale of loans transferred to held for sale		37,695
Gain on sale of loans transferred to held for sale		(193)
Net cash provided by (used in) investing activities	**(57,895)**	24,312
Financing Activities		

Net change in		
Deposits	**6,981**	(101,408)
Borrowings	**25,116**	34,571
Proceeds from issuance of stock		35
Dividends paid on preferred shares	**(508)**	
Dividends paid on common shares	**(1,113)**	(1,040)
Net cash provided (used) by financing activities	**30,476**	(67,842)
Net Change in Cash and Cash Equivalent	**(19,421)**	(36,328)
Cash and Cash Equivalents, Beginning of Period	**36,001**	55,029
Cash and Cash Equivalents, End of Period	**$ 16,580**	$ 18,701
Additional Cash Flows Information		
Interest paid	**$ 15,097**	$ 18,237
Income taxes paid	**1,165**	1,050

See notes to condensed consolidated financial statements

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HORIZON BANCORP AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Table Dollar Amounts in Thousands, Except Per Share Data)

Note 1 Accounting Policies

The accompanying consolidated financial statements include the accounts of Horizon Bancorp (Horizon or the Company) and its wholly-owned subsidiaries, including Horizon Bank, N.A. (Bank). All inter-company balances and transactions have been eliminated. The results of operations for the periods ended June 30, 2009 and June 30, 2008 are not necessarily indicative of the operating results for the full year of 2009 or 2008. The accompanying unaudited condensed consolidated financial statements reflect all adjustments that are, in the opinion of Horizon s management, necessary to fairly present the financial position, results of operations and cash flows of Horizon for the periods presented. Those adjustments consist only of normal recurring adjustments.

Certain information and note disclosures normally included in Horizon s annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Horizon s Annual Report on Form 10-K for 2008 filed with the Securities and Exchange Commission. The consolidated balance sheet of Horizon as of December 31, 2008 has been derived from the audited balance sheet of Horizon as of that date.

Basic earnings per share is computed by dividing net income available to common shareholders (net income less dividend requirements for preferred stock and accretion of preferred stock discount) by the weighted-average number of common shares outstanding. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. In August 2002, substantially all of the participants in Horizon s Stock Option and Stock Appreciation Rights Plans voluntarily entered into an agreement with Horizon to cap the value of their stock appreciation rights (SARS) at $14.67 per share and cease any future vesting of the SARS. These agreements with option holders make it more advantageous to exercise an option rather than a SAR whenever Horizon s stock price exceeds $14.67 per share, therefore the option becomes potentially dilutive at $14.67 per share or higher. The following table shows computation of basic and diluted earnings per share.

	Three months ended June 30		Six months ended June 30	
	2009 (Unaudited)	**2008 (Unaudited)**	**2009 (Unaudited)**	**2008 (Unaudited)**
Basic earnings per share				
Net income	**$ 2,064**	$ 2,990	**$ 4,699**	$ 5,518
Less: Preferred stock dividends and accretion of discount	**350**		**700**	
Net income available to common shareholders	**$ 1,714**	$ 2,990	**$ 3,999**	$ 5,518
Weighted average common shares outstanding	**3,209,482**	3,208,419	**3,209,482**	3,207,825
Basic earnings per share	**$ 0.53**	$ 0.93	**$ 1.25**	$ 1.72
Diluted earnings per share				
Net income available to common shareholders	**$ 1,714**	$ 2,990	**$ 3,999**	$ 5,518

Weighted average common shares outstanding	**3,209,482**	3,208,419	**3,209,482**	3,207,825
Effect of dilutive securities:				
Restricted stock	**52,179**	17,762	**51,394**	22,607
Stock options	**8,517**	12,150	**6,438**	11,224
Weighted average shares outstanding	**3,270,178**	3,238,331	**3,267,314**	3,241,656
Diluted earnings per share	**$ 0.52**	$ 0.92	**$ 1.22**	$ 1.70

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HORIZON BANCORP AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Table Dollar Amounts in Thousands, Except Per Share Data)

At June 30, 2009 and 2008 there were 35,050 shares and 27,190 shares that were not included in the computation of diluted earnings per share because they were non-dilutive. Warrants to purchase 212,104 shares at June 30, 2009 were not included in the computation of diluted earnings per share because the effect would be non-dilutive.

Horizon has share-based employee compensation plans, which are described in the notes to the financial statements included in the December 31, 2008 Annual Report on Form 10-K.

Reclassifications

Certain reclassifications have been made to the 2008 consolidated financial statements to be comparable to 2009. These reclassifications had no effect on net income.

Note 2 Securities

The fair value of securities is as follows:

June 30, 2009 (Unaudited)	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Available for sale				
U.S. Treasury and federal agencies	$ 19,880	$ 268	$ (3)	$ 20,145
State and municipal	95,175	961	(1,764)	94,372
Federal agency collateralized mortgage obligations	17,521	304	(543)	17,282
Federal agency mortgage-backed pools	183,237	3,941	(292)	186,886
Corporate notes	587		(206)	381
Total available for sale investment securities	$316,400	$5,474	$(2,808)	$319,066
Held to maturity, State and Municipal	$ 12,875	$ 103	$	$ 12,978

December 31, 2008	**Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Available for sale				
U.S. Treasury and federal agencies	$ 23,661	$1,253	$	$ 24,914
State and municipal	88,282	804	(2,101)	86,985
Federal agency collateralized mortgage obligations	13,063	223	(335)	12,951
Federal agency mortgage-backed pools	174,227	2,374	(212)	176,389
Corporate notes	587		(188)	399
Total available for sale investment securities	$299,820	$4,654	$(2,836)	$301,638
Held to maturity, State and Municipal	$ 1,630	$ 4	$	$ 1,634

Based on evaluation of available evidence, including recent changes in market interest rates, credit rating information, and information obtained from regulatory filings, management believes the declines in fair value for these securities are temporary. While these securities are held in the available for sale portfolio, Horizon intends and has the ability to hold them until the earlier of a recovery in fair value or maturity.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period the other-than-temporary impairment is identified. At June 30, 2009, no individual investment security had an unrealized loss that was determined to be other-than-temporary.

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HORIZON BANCORP AND SUBSIDIARIES
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The unrealized losses on the Company s investments in securities of state and political subdivisions were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before recovery of their amortized cost basis, which may be maturity, the Company did not consider those investments to be other-than-temporarily impaired at June 30, 2009.

The amortized cost and fair value of securities available for sale and held to maturity at June 30, 2009 and December 31, 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or perpay obligations with or without call or prepayment penalties.

	June 30, 2009 (Unaudited)		December 31, 2008	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale				
Within one year	**$ 1,907**	**$ 1,931**	$ 1,182	$ 1,190
One to five years	**21,605**	**21,868**	10,569	10,926
Five to ten years	**23,159**	**23,207**	28,701	28,664
After ten years	**68,971**	**67,892**	72,078	71,518
	115,642	**114,898**	112,530	112,298
Federal agency collateralized mortgage obligations	**17,521**	**17,282**	13,063	12,951
Federal agency mortgage-backed pools	**183,237**	**186,886**	174,227	176,389
Total available for sale investment securities	**$316,400**	**$319,066**	$299,820	$301,638
Held to maturity				
Within one year	**$ 12,585**	**$ 12,680**	$ 90	$ 91
One to five years	**290**	**298**	1,540	1,543
Total held to maturity investment securities	**$ 12,875**	**$ 12,978**	$ 1,630	$ 1,634

The following table shows investments gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at June 30, 2009:

	Less than 12 Months		12 Months or More		Total	
June 30, 2009 (Unaudited)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Treasury and federal agencies	$ 1,499	$ (3)	$	$	$ 1,499	$ (3)
State and municipal	37,548	(931)	13,185	(833)	50,733	(1,764)
	5,613	(337)	3,458	(206)	9,071	(543)

Federal agency collateralized mortgage obligations						
Federal agency mortgage-backed pools	14,969	(291)	46	(1)	15,015	(292)
Corporate notes			381	(206)	381	(206)
Total temporarily impaired securities	$59,629	$(1,562)	$17,070	$(1,246)	$76,699	$(2,808)

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HORIZON BANCORP AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Table Dollar Amounts in Thousands, Except Per Share Data)

Note 3 Loans

	June 30, 2009 (Unaudited)	December 31, 2008
Commercial loans	**$313,857**	$310,842
Mortgage warehouse	**163,083**	123,287
Real estate loans	**146,096**	167,766
Installment loans	**272,394**	280,072
	895,430	881,967
Allowance for loan losses	**(12,649)**	(11,410)
Total loans	**$882,781**	$870,557

Note 4 Allowance for Loan Losses

	June 30, 2009 (Unaudited)	June 30, 2008 (Unaudited)
Balances, beginning of period	**$11,410**	$ 9,791
Provision for losses	**6,487**	2,268
Recoveries on loans	**543**	444
Loans charged off	**(5,791)**	(2,691)
Balances, end of period	**$12,649**	$ 9,812

Note 5 Non-performing Assets

	June 30, 2009 (Unaudited)	December 31, 2008
Non-performing loans		
Commercial	**$ 7,959**	$ 5,167
Real estate	**3,764**	1,904
Mortgage warehouse		
Installment	**1,754**	792
Total non-performing loans	**13,477**	7,863
Other real estate owned and repossessed collateral		
Commercial		
Real estate	**2,212**	2,874
Mortgage warehouse		

Installment	**115**	207
Total other real estate owned and repossessed collateral	**2,327**	3,081
Total non-performing assets	**$15,804**	$ 10,944

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HORIZON BANCORP AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Table Dollar Amounts in Thousands, Except Per Share Data)

Note 6 Derivative financial instruments

The Company adopted SFAS No. 161 as of January 1, 2009, which expands the disclosure requirements of SFAS No. 133 as follows.

Cash Flow Hedges

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flow due to interest rate fluctuations, the Company entered into interest rate swap agreements for a portion of its floating rate debt. The agreements provide for the Company to receive interest from the counterparty at three month LIBOR and to pay interest to the counterparty at a weighted average fixed rate of 5.38% on a notional amount of $22.0 million at June 30, 2009. Under the agreements, the Company pays or receives the net interest amount monthly, with the monthly settlements included in interest expense.

Management has designated the interest rate swap agreement as a cash flow hedging instrument. For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of the other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. At June 30, 2009 the Company s cash flow hedge was effective and is not expected to have a significant impact the Company s net income over the next 12 months.

Fair Value Hedges

Fair value hedges are intended to reduce the interest rate risk associated with the underlying hedged item. The Company enters into fixed rate loan agreements as part of its lending policy. To mitigate the risk of changes in fair value based on fluctuations in interest rates, the Company has entered into interest rate swap agreements on individual loans, converting the fixed rate loans to a variable rate. For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current earnings. At June 30, 2009 the Company s fair value hedges were effective and are not expected to have a significant impact the Company s net income over the next 12 months.

The change in fair value of both the hedge instruments and the underlying loan agreements are recorded as gains or losses in interest income. The fair value hedges are considered to be highly effective and any hedge ineffectiveness was deemed not material. The notional amounts of the loan agreements being hedged were $25.9 million at June 30, 2009.

Other Derivative Instruments

The Company enters into non-hedging derivative in the form of mortgage loan forward sale commitments with investors and commitments to originate mortgage loans as part of its mortgage banking business. At June 30, 2009 the Company s fair value of these derivatives were recorded and over the next 12 months are not expected to have a significant impact the Company s net income.

The change in fair value of both the forward sale commitments and commitments to originate mortgage loans were recorded and the net gains or losses included in the Company s gain on sale of loans.

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HORIZON BANCORP AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Table Dollar Amounts in Thousands, Except Per Share Data)

The following tables summarize the fair value of derivative financial instruments utilized by Horizon Bancorp:

	Asset Derivative June 30, 2009 (Unaudited)		Liability Derivatives June 30, 2009 (Unaudited)	
Derivatives designated as hedging instruments under Statement 133	**Balance Sheet Location**	**Fair Value**	**Balance Sheet Location**	**Fair Value**
Interest rate contracts	Loans	$ 1,146	Other liabilities	$ 1,146
Interest rate contracts			Other liabilities	730
Total derivatives designated as hedging instruments under Statement 133		1,146		1,876
Derivatives not designated as hedging instruments under Statement 133				
Mortgage loan contracts	Other assets	230	Other liabilities	143
Total derivatives not designated as hedging instruments under Statement 133		230		143
Total derivatives		$ 1,376		$ 2,019

The effect of the derivative instruments on the consolidated statement of income for the three and six-month periods ended is as follows:

	Amount of Gain Recognized in Other Comprehensive Income on Derivative (Effective Portion)	
	Three Months Ended June 30,	**Six Months Ended June 30,**

Derivative in Statement 133 cash flow hedging relationship	**2009 (Unaudited)**	**2009 (Unaudited)**
Interest rate contracts	$ 126	$ 79
Total	$ 126	$ 79

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HORIZON BANCORP AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
(Table Dollar Amounts in Thousands, Except Per Share Data)

Note 7 Disclosures about fair value of assets and liabilities

Derivative in Statement 133 fair value hedging relationship	Location of Gain (Loss) Recognized on Derivative	Amount of Gain (Loss) Recognized on Derivative Three Months Ended June 30, 2009 (Unaudited)	Six Months Ended June 30, 2009 (Unaudited)
Interest rate contracts	Interest income loans	$ (584)	$ (560)
Interest rate contracts	Interest income loans	584	560
Total		$	$

Derivative in Statement 133 fair value hedging under Statement 133	Location of Gain (Loss) Recognized on Derivative	Amount of Gain (Loss) Recognized on Derivative Three Months Ended June 30, 2009 (Unaudited)	Six Months Ended June 30, 2009 (Unaudited)
Mortgage contracts	Other income gain on sale of loans	$ (177)	$ (145)
Total		$ (177)	$ (145)

Effective January 1, 2008 Horizon adopted Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The standard describes three levels of inputs that may be used to measure fair value:

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

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying financial statements, as well as the general classification of such instruments pursuant to the valuation hierarchy.

Available for sale securities

When quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Level 2 securities include U.S. Treasury and federal agency securities, state and municipal securities, federal agency mortgage obligations and mortgage-backed pools and corporate notes. Level 2 securities are valued by a third party pricing service commonly used in the banking industry utilizing observable inputs. The pricing provider utilizes evaluated pricing models that vary based on asset class. These models incorporate available market information including quoted prices of securities with similar characteristics and, because many fixed-income securities do not trade on a daily basis, apply available information through processes such as benchmark curves, benchmarking of like securities, sector grouping and matrix pricing. In addition, model processes, such as an option adjusted spread model is used to develop prepayment and interest rate scenarios for securities with prepayment features.

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Hedged loans

Certain fixed rate loans have been converted to variable rate loans through entering into interest rate swap agreements. Fair value of those fixed rate loans is based on discounting estimated cash flows using interest rates determined by a respective interest rate swap agreement. Loans are classified within Level 3 of the valuation hierarchy based on the unobservable inputs used.

Interest rate swap agreements

The fair value is estimated by a third party using inputs that are primarily unobservable and cannot be corroborated by observable market data and, therefore, are classified within Level 3 of the valuation hierarchy.

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying financial statements measured at fair value on a recurring basis and the level within the FAS 157 fair value hierarchy in which the fair value measurements fall at the following:

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2009 (Unaudited)				
Available-for-sale securities				
U.S. Treasury and federal agencies	$ 20,145	$	$ 20,145	$
State and municipal	94,372		94,372	
Federal agency collateralized mortgage obligations	17,282		17,282	
Federal agency mortgage-backed pools	186,886		186,886	
Corporate notes	381		381	
Hedged loans	27,017			27,017
Forward sale commitments	230			230
Interest rate swap agreements	(1,876)			(1,876)
Commitments to originate loans	(143)			(143)
December 31, 2008				
Available-for-sale securities	$301,638	$	$301,638	$
Hedged loans	25,033			25,033
Forward sale commitments	670			670
Interest rate swap agreements	(2,557)			(2,557)
Commitments to originate loans	(438)			(438)
June 30, 2008 (Unaudited)				
Available-for-sale securities	$251,976	$ 1,464	$250,512	$
Hedged loans	16,269			16,269
Interest rate swap agreements	258			258

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The following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying condensed consolidated balance sheet using significant unobservable (level 3) inputs (Unaudited):

	Hedged Loans	Forward Sale Commitments	Interest Rate Swaps	Commitments to Originate Loans
Beginning balance December 31, 2008	$25,033	$ 670	$(2,557)	$ (438)
Total realized and unrealized gains and losses				
Included in net income	24	(226)	(24)	258
Included in other comprehensive income, gross			(73)	
Purchases, issuances, and settlements	2,901			
Principal payments	(167)			
Ending balance March 31, 2009	27,791	444	(2,654)	(180)
Total realized and unrealized gains and losses				
Included in net income	(584)	(214)	584	37
Included in other comprehensive income, gross			194	
Purchases, issuances, and settlements				
Principal payments	(190)			
Ending balance June 30, 2009	$27,017	$ 230	$(1,876)	$ (143)

	Hedged Loans	Forward Sale Commitments	Interest Rate Swaps	Commitments to Originate Loans
Beginning balance December 31, 2007	$	$	$	$
Total realized and unrealized gains and losses				
Included in net income	195		(195)	
Included in other comprehensive income, gross			(584)	
Purchases, issuances, and settlements	11,437			
Principal payments	(31)			
Ending balance March 31, 2008	11,601		(779)	
Total realized and unrealized gains and losses				
Included in net income	(436)		436	
Included in other comprehensive income, gross			601	
Purchases, issuances, and settlements	5,166			
Principal payments	(62)			

Ending balance June 30, 2008	$16,269	$	$ 258	$

Realized gains and losses included in net income for the periods are reported in the condensed consolidated statements of income as follows (Unaudited):

	Six Months Ended June 30,	
Non Interest Income	**2009**	**2008**
Total gains and losses from:		
Hedged loans	$ (560)	$ (241)
Fair value interest rate swap agreements	560	241
Derivative loan commitments	(145)	
	$ (145)	$

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Certain other assets and liabilities are measured at fair value on a nonrecurring basis in the course of business and are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment):

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2009 (Unaudited)				
Impaired and non-accrual loans	$9,063	$	$	$ 9,063
Other real estate owned	2,212			2,212
December 31, 2008				
Impaired and non-accrual loans	$4,685	$	$	$ 4,685
Other real estate owned	2,874			2,874

Impaired, non-accrual loans, and other real estate owned: Fair value adjustments for impaired and non-accrual loans typically occur when there is evidence of impairment. Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due according to the contractual terms of the loan agreement will not be collected. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan or the fair value of the collateral. The Company measures fair value based on the value of the collateral securing the loans. Collateral may be in the form of real estate or personal property including equipment and inventory. The value of the collateral is determined based on internal estimates as well as third party appraisals or non-binding broker quotes. These measurements were classified as Level 3. The fair value of the Company s other real estate owned is determined using Level 3 inputs, which include current and prior appraisals and estimated costs to sell.

Note 8 Fair Value of Financial Instruments

The estimated fair value amounts were determined using available market information, current pricing information applicable to Horizon and various valuation methodologies. Where market quotations were not available, considerable management judgment was involved in the determination of estimated fair values. Therefore, the estimated fair value of financial instruments shown below may not be representative of the amounts at which they could be exchanged in a current or future transaction. Due to the inherent uncertainties of expected cash flows of financial instruments, the use of alternate valuation assumptions and methods could have a significant effect on the derived estimated fair value amounts.

The estimated fair values of financial instruments, as shown below, are not intended to reflect the estimated liquidation or market value of Horizon taken as a whole. The disclosed fair value estimates are limited to Horizon s significant financial instruments at June 30, 3009 and December 31, 2008. These include financial instruments recognized as assets and liabilities on the consolidated balance sheet as well as certain off-balance sheet financial instruments. The estimated fair values shown below do not include any valuation of assets and liabilities, which are not financial instruments as defined by SFAS No. 107, *Disclosures About Fair Value of Financial Instruments*.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

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Cash and Cash Equivalents The carrying amounts approximate fair value.

Interest-Bearing Deposits The carrying amounts approximate fair value.

Investment Securities For debt securities held to maturity, fair values are based on quoted market prices or dealer quotes. For those securities where a quoted market price is not available, carrying amount is a reasonable estimate of fair value based upon comparison with similar securities.

Loans Held for Sale The carrying amounts approximate fair value.

Net Loans The fair value of portfolio loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The carrying amounts of loans held for sale approximate fair value.

Interest Receivable/Payable The carrying amounts approximate fair value.

FHLB and FRB Stock Fair value of FHLB and FRB stock is based on the price at which it may be resold to the FHLB and FRB.

Deposits The fair value of demand deposits, savings accounts, interest-bearing checking accounts and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated by discounting the future cash flows using rates currently offered for deposits of similar remaining maturity.

Borrowings Rates currently available to Horizon for debt with similar terms and remaining maturities are used to estimate fair values of existing borrowings.

Subordinated Debentures Rates currently available for debentures with similar terms and remaining maturities are used to estimate fair values of existing debentures.

Commitments to Extend Credit and Standby Letter of Credit The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date. Due to the short-term nature of th