

CENTRUE FINANCIAL CORP  
Form 10-Q  
November 13, 2012

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

**QUARTERLY REPORT**

**Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended September 30, 2012

Commission File Number: 0-28846

**Centrue Financial Corporation**

(Exact name of Registrant as specified in its charter)

Delaware                                      36-3145350  
(State or other jurisdiction of      (I.R.S. Employer Identification  
incorporation or organization)      Number)

**7700 Bonhomme Avenue, St. Louis, Missouri 63105**

(Address of principal executive offices including zip code)

**(314) 505-5500**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant 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  No

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

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

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

Class	Shares outstanding at November 13, 2012
Common Stock, Par Value \$1.00	6,063,441

**Centrue Financial Corporation**

**Form 10-Q Index**

**September 30, 2012**

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**Centrue Financial Corporation****Part I Financial Information****Item 1. Financial Statements****Unaudited Consolidated Balance Sheets****September 30, 2012 and December 31, 2011 (In Thousands, Except Share Data)**

	September 30, 2012	December 31, 2011
<b>ASSETS</b>		
Cash and cash equivalents	\$ 79,423	\$ 69,735
Securities available-for-sale	181,496	228,836
Restricted securities	7,028	9,150
Loans	561,476	582,395
Allowance for loan losses	(21,070 )	(21,232 )
Net loans	540,406	561,163
Bank-owned life insurance	32,146	31,412
Mortgage servicing rights	1,997	2,089
Premises and equipment, net	23,098	23,754
Other intangible assets, net	4,551	5,264
Other real estate owned	28,601	29,667
Other assets	6,079	6,914
<b>Total assets</b>	<b>\$ 904,825</b>	<b>\$ 967,984</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Liabilities</b>		
<b>Deposits:</b>		
Non-interest-bearing	\$ 118,733	\$ 134,137
Interest-bearing	663,864	714,501
<b>Total deposits</b>	<b>782,597</b>	<b>848,638</b>
Federal funds purchased and securities sold under agreements to repurchase	16,669	18,036
Federal Home Loan Bank advances	30,057	23,058
Notes payable	10,345	10,440
Series B mandatory redeemable preferred stock	268	268
Subordinated debentures	20,620	20,620
Other liabilities	15,562	14,355
<b>Total liabilities</b>	<b>876,118</b>	<b>935,415</b>
<b>Commitments and contingent liabilities</b>	<b>—</b>	<b>—</b>
<b>Stockholders' equity</b>		

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Series A Convertible Preferred Stock (aggregate liquidation preference of \$2,762)	500	500
Series C Fixed Rate, Cumulative Perpetual Preferred Stock (aggregate liquidation preference of \$32,668)	31,894	31,429
Common stock, \$1 par value, 15,000,000 shares authorized; 7,453,555 shares issued at September 30, 2012 and December 31, 2011	7,454	7,454
Surplus	74,581	74,558
Accumulated deficit	(65,834 )	(60,064 )
Accumulated other comprehensive income	1,989	569
	50,584	54,446
Treasury stock, at cost, 1,390,114 shares at September 30, 2012 and December 31, 2011	(21,877 )	(21,877 )
Total stockholders' equity	28,707	32,569
Total liabilities and stockholders' equity	\$ 904,825	\$ 967,984

See Accompanying Notes to Unaudited Financial Statements

1.

**Centrue Financial Corporation**

Unaudited Consolidated Statements Of Income (Loss)

And Comprehensive Income (Loss)

**Three Months and Nine Months Ended September 30, 2012 and 2011****(In Thousands, Except Per Share Data)**

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
Interest income				
Loans	\$6,850	\$8,297	\$20,839	\$26,414
Securities				
Taxable	748	1,047	2,432	3,132
Exempt from federal income taxes	105	158	344	550
Federal funds sold and other	23	40	99	108
Total interest income	7,726	9,542	23,714	30,204
Interest expense				
Deposits	973	1,937	3,515	6,637
Federal funds purchased and securities sold under agreements to repurchase	10	11	31	32
Federal Home Loan Bank advances	192	347	568	1,114
Series B mandatory redeemable preferred stock	4	4	12	12
Subordinated debentures	157	277	745	821
Notes payable	92	89	280	270
Total interest expense	1,428	2,665	5,151	8,886
Net interest income	6,298	6,877	18,563	21,318
Provision for loan losses	5,750	2,400	8,475	9,900
Net interest income after provision for loan losses	548	4,477	10,088	11,418
Noninterest income				
Service charges	1,128	1,232	3,217	3,483
Mortgage banking income	777	341	1,719	1,050
Electronic banking services	550	552	1,640	1,644
Bank-owned life insurance	246	256	734	755
Securities gains	684	—	1,398	379
Total other-than-temporary impairment losses	—	—	—	(499 )
Portion of loss recognized in other comprehensive income (before taxes)	—	—	—	—
Net impairment on securities	—	—	—	(499 )
Gain (loss) on sale of OREO	40	(12 )	465	(60 )

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Gain (loss) on sale of other assets	—	(16 )	—	47
Other income	404	213	1,520	575
	3,829	2,566	10,693	7,374

See Accompanying Notes to Unaudited Financial Statements

2.



**Centrue Financial Corporation**

Unaudited Consolidated Statements Of Income (Loss)

And Comprehensive Income (Loss)

**Three Months and Nine Months Ended September 30, 2012 and 2011****(In Thousands, Except Per Share Data)**

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
Noninterest expense				
Salaries and employee benefits	3,697	3,505	10,981	10,598
Occupancy, net	681	712	1,965	2,136
Furniture and equipment	235	407	902	1,267
Marketing	115	56	284	183
Supplies and printing	67	67	200	208
Telephone	180	229	534	637
Data processing	396	381	1,063	1,120
FDIC insurance	515	323	1,544	1,997
Loan processing and collection costs	337	495	1,427	1,597
OREO valuation adjustment	640	4,473	1,435	5,770
Amortization of intangible assets	238	250	713	789
Other expenses	1,383	1,499	4,257	4,472
	8,484	12,397	25,305	30,774
Income (loss) before income taxes	\$(4,107)	\$(5,354)	\$(4,524)	\$(11,982)
Income tax expense (benefit)	(788)	(606)	(788)	(1,352)
Net income (loss)	\$(3,319)	\$(4,748)	\$(3,736)	\$(10,630)
Preferred stock dividends	529	505	1,569	1,500
Net income (loss) for common stockholders	\$(3,848)	\$(5,253)	\$(5,305)	\$(12,130)
Basic earnings (loss) per common share	\$(0.63)	\$(0.87)	\$(0.87)	\$(2.01)
Diluted earnings (loss) per common share	\$(0.63)	\$(0.87)	\$(0.87)	\$(2.01)
Total comprehensive income (loss):				
Net income (loss)	\$(3,319)	\$(4,748)	\$(3,736)	\$(10,630)
Change in unrealized gains (losses) on available for sale securities for which a portion of an other-than-temporary impairment has been recognized in earnings	—	—	—	(80)
Change in unrealized gains (losses) on other securities available for sale	1,727	1,075	3,718	3,411

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Reclassification adjustment:

Net impairment loss recognized in earnings	—	—	—	499
(Gains) recognized in earnings	(684 )	—	(1,398 )	(379 )
Net unrealized gains (loss)	1,043	1,075	2,320	3,451
Tax expense (benefit)	900	416	900	919
Other comprehensive income (loss)	143	659	1,420	2,532
Total comprehensive income (loss)	\$(3,176)	\$(4,089 )	\$(2,316 )	\$(8,098 )

See Accompanying Notes to Unaudited Financial Statements

3.

**Centrue Financial Corporation**

## Unaudited Consolidated Statements Of Cash Flows

**Nine Months Ended September 30, 2012 and 2011 (In Thousands)**

	Nine Months Ended September 30,	
	2012	2011
Cash flows from operating activities		
Net income (loss)	\$(3,736 )	\$(10,630)
Adjustments to reconcile net income (loss) to net cash provided by operating activities		
Depreciation	1,042	1,406
Amortization of intangible assets	713	789
Amortization of mortgage servicing rights, net	470	341
Amortization of bond premiums, net	2,071	1,666
Mortgage servicing rights valuation adjustment	—	89
Income tax valuation adjustment	1,369	3,896
Share based compensation	23	54
Provision for loan losses	8,475	9,900
Provision for deferred income taxes	(1,369 )	(3,896 )
Earnings on bank-owned life insurance	(734 )	(755 )
Other than temporary impairment, securities	—	499
OREO valuation allowance	1,435	5,770
Securities sale (gains), net	(1,398 )	(379 )
(Gain) on sale of other assets, net	—	(47 )
(Gain) loss on sale of OREO	(465 )	60
(Gain) on sale of loans	(1,562 )	(787 )
Proceeds from sales of loans held for sale	63,119	31,651
Origination of loans held for sale	(61,025)	(31,149)
Change in assets and liabilities		
(Increase) decrease in other assets	373	4,166
Increase (decrease) in other liabilities	(1,026 )	(2,227 )
Net cash provided by operating activities	7,775	10,417
Cash flows from investing activities		
Proceeds from paydowns of securities available for sale	38,536	31,946
Proceeds from calls and maturities of securities available for sale	10,310	18,000
Proceeds from sales of securities available for sale	48,381	18,419
Purchases of securities available for sale	(48,189)	(83,212)
Redemption of Federal Home Loan Bank stock	2,088	—
Redemption of Federal Reserve Bank stock	110	1,319
Purchase of Federal Reserve Bank stock	(76 )	—
Net decrease (increase) in loans	3,738	64,458
(Purchase) disposal of premises and equipment	(386 )	(245 )
Proceeds from sale of OREO	7,905	6,152
Net cash from investing activities	62,417	56,837

See Accompanying Notes to Unaudited Financial Statements

4.

**Centrue Financial Corporation**

## Unaudited Consolidated Statements Of Cash Flows

**Nine Months Ended September 30, 2012 and 2011 (In Thousands)**

	Nine Months Ended September 30,	
	2012	2011
Cash flows from financing activities		
Net increase (decrease) in deposits	(66,041)	(68,988)
Net increase (decrease) in federal funds purchased and securities sold under agreements to repurchase	(1,367 )	5,176
Repayment of advances from the Federal Home Loan Bank	(67,001)	(33,001)
Proceeds from advances from the Federal Home Loan Bank	74,000	10,000
Payments on notes payable	(95 )	(90 )
Net cash used in financing activities	(60,504)	(86,903)
Net increase (decrease) in cash and cash equivalents	9,688	(19,649)
Cash and cash equivalents		
Beginning of period	69,735	82,945
End of period	\$79,423	\$63,296
Supplemental disclosures of cash flow information		
Cash payments for		
Interest	\$5,003	\$9,018
Income taxes	10	19
Transfers from loans to other real estate owned	8,011	19,151

See Accompanying Notes to Unaudited Financial Statements

5.

## **Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)**

### **Note 1. Summary of Significant Accounting Policies**

Centrue Financial Corporation is a bank holding company organized under the laws of the State of Delaware. When we use the terms “Centrue,” the “Company,” “we,” “us,” and “our,” we mean Centrue Financial Corporation, a Delaware corporation, and its consolidated subsidiaries. When we use the term the “Bank,” we are referring to our wholly owned banking subsidiary, Centrue Bank. The Company and the Bank provide a full range of banking services to individual and corporate customers located in markets extending from the far western and southern suburbs of the Chicago metropolitan area across Central Illinois down to the metropolitan St. Louis area. These services include demand, time, and savings deposits; business and consumer lending; and mortgage banking. Additionally, brokerage, asset management, and trust services are provided to our customers on a referral basis to third party providers. The Company is subject to competition from other financial institutions and nonfinancial institutions providing financial services. Additionally, the Company and the Bank are subject to regulations of certain regulatory agencies and undergo periodic examinations by those regulatory agencies.

#### Basis of presentation

The accounting and reporting policies of the Company and its subsidiaries conform to U.S. generally accepted accounting principles (“GAAP”) and general practice within the banking industry. The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. Material estimates which are particularly susceptible to significant change in the near term relate to the fair value of investment securities and other-than-temporary impairment of securities, the determination of the allowance for loan losses and valuation of other real estate owned.

For further information with respect to significant accounting policies followed by the Company in the preparation of its consolidated financial statements, refer to the Company’s Annual Report on Form 10-K for the year ended December 31, 2011. The consolidated financial statements include the accounts of the Company and Centrue Bank. Intercompany balances and transactions have been eliminated in consolidation and certain 2011 amounts have been reclassified to conform to the 2012 presentation. The annualized results of operations during the three and nine months ended September 30, 2012 are not necessarily indicative of the results expected for the year ending December 31, 2012. All financial information in the following tables is in thousands (000s), except share and per share data. In the opinion of management, all normal and recurring adjustments which are necessary to fairly present the results for

the interim periods presented have been included.

**Note 2. Earnings Per Share**

Basic earnings per share for the three and nine months ended September 30, 2012 and 2011 were computed by dividing net income by the weighted average number of shares outstanding. Diluted earnings per share for the same periods were computed by dividing net income by the weighted average number of shares outstanding, adjusted for the dilutive effect of the stock options and warrants. Computations for basic and diluted earnings per share are provided as follows:

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 2. Earnings Per Share (Continued)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Basic Earnings (Loss) Per Common Share				
Net income (loss) for common shareholders	\$(3,848)	\$(5,253)	\$(5,305)	\$(12,130)
Weighted average common shares outstanding	6,063	6,048	6,063	6,048
Basic earnings per common share	\$(0.63 )	\$(0.87 )	\$(0.87 )	\$(2.01 )
Diluted Earnings Per Common Share				
Weighted average common shares outstanding	6,063	6,048	6,063	6,048
Add: dilutive effect of assumed exercised stock options	—	—	—	—
Add: dilutive effect of assumed exercised common stock warrants	—	—	—	—
Weighted average common and dilutive potential shares outstanding	6,063	6,048	6,063	6,048
Diluted earnings (loss) per common share	\$(0.63 )	\$(0.87 )	\$(0.87 )	\$(2.01 )

There were 274,927 options and 508,320 warrants outstanding for the three and nine months ended September 30, 2012 and 464,038 options and 508,320 warrants outstanding for the three and nine months ended September 30, 2011 that were not included in the computation of diluted earnings per share because the exercise price was greater than the average market price and therefore, were anti-dilutive. In addition, the Company's convertible preferred stock was not included in the computation of diluted earnings per share as it was anti-dilutive.

**Note 3. Securities**

The primary strategic objective related to the Company's securities portfolio is to assist with liquidity and interest rate risk management. The fair value of securities classified as available-for-sale was \$181.5 million at September 30, 2012 compared to \$228.8 million at December 31, 2011. The carrying value of securities classified as restricted (Federal Reserve and Federal Home Loan Bank stock) was \$7.0 million at September 30, 2012 compared to \$9.2 million at December 31, 2011. The Company does not have any securities classified as trading or held-to-maturity.



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The following tables represent the fair value of available-for-sale securities and the related, gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) at September 30, 2012 and December 31, 2011:

	September 30, 2012			Amortized Cost
	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	
U.S. government agencies	\$7,069	\$ 73	\$ —	\$ 6,996
States and political subdivisions	16,243	764	—	15,479
U.S. government agency residential mortgage-backed securities	119,130	3,145	—	115,985
Collateralized residential mortgage obligations:				
Agency	23,336	234	—	23,102
Private label	1,083	69	—	1,014
Equity securities	2,683	242	—	2,441
Collateralized debt obligations:				
Single issue	2,064	—	—	2,064
Pooled	7,888	1,172	(1,165 )	7,881
Corporate	2,000	—	—	2,000
	\$181,496	\$ 5,699	\$ (1,165 )	\$ 176,962

7.

**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 3. Securities (Continued)**

	December 31, 2011			
	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	Amortized Cost
U.S. government agencies	\$3,019	\$ 88	\$ —	\$2,931
States and political subdivisions	18,125	649	(1 )	17,477
U.S. government agency residential mortgage-backed securities	177,539	2,790	(101 )	174,850
Collateralized residential mortgage obligations:	15,527	229	—	15,298
Agency	1,550	72	(7 )	1,485
Private label	2,530	134	—	2,396
Equity securities				
Collateralized debt obligations:				
Single issue	2,064	—	—	2,064
Pooled	6,600	53	(1,574 )	8,121
Corporate	1,882	—	(118 )	2,000
	\$228,836	\$ 4,015	\$ (1,801 )	\$226,622

The amounts below include the activity for available-for-sale securities related to sales, maturities and calls:

	Three Months Ended		Nine Months Ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
Proceeds from calls and maturities	\$8,000	\$6,080	\$10,310	\$18,000
Proceeds from sales	30,312	—	48,381	18,419
Realized gains	686	—	1,400	379
Realized losses	(2 )	—	(2 )	—
Net impairment loss recognized in earnings	—	—	—	(499 )
Tax benefit (provision) related to net realized gains and losses	(265 )	—	(542 )	46

The following table represents securities with unrealized losses not recognized in income presented by the length of time individual securities have been in a continuous unrealized loss position:

September 30, 2012

	Less than 12 Months	12 Months or More	Total
	Fair Value	Fair Value	Fair Value
	Unrealized Loss	Unrealized Loss	Unrealized Loss
Collateralized debt obligations: pooled	\$—	\$2,206	\$2,206
	\$—	\$ (1,165)	\$ (1,165)
Total temporarily impaired	\$—	\$2,206	\$2,206
	\$—	\$ (1,165)	\$ (1,165)

8.

**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 3. Securities (Continued)**

	December 31, 2011					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
State and political subdivisions	\$524	\$ (1 )	\$—	\$ —	\$524	\$ (1 )
U.S. government agency residential mortgage-backed securities	30,895	(101 )	—	—	30,895	(101 )
Collateralized residential mortgage obligations: private label	731	(7 )	—	—	731	(7 )
Collateralized debt obligations: pooled Corporate	—	—	6,497	(1,574 )	6,497	(1,574 )
Corporate	1,882	(118 )	—	—	1,882	(118 )
Total temporarily impaired	\$34,032	\$ (227 )	\$6,497	\$ (1,574 )	\$40,529	\$ (1,801 )

The fair values of securities classified as available-for-sale at September 30, 2012, by contractual maturity, are shown as follows. Securities not due at a single maturity date, including mortgage-backed securities, collateralized mortgage obligations, and equity securities are shown separately.

	Amortized Cost	Fair Value
Due in one year or less	\$2,156	\$2,167
Due after one year through five years	16,204	16,653
Due after five years through ten years	5,488	5,847
Due after ten years	10,572	10,597
U.S. government agency residential mortgage-backed securities	115,985	119,130
Collateralized residential mortgage obligations	24,116	24,419
Equity	2,441	2,683
	\$176,962	\$181,496

The following table presents a rollforward of the credit losses recognized in earnings for the three month period ended September 30, 2012 and 2011:

	2012	2011
Beginning balance, July 1,	\$20,597	\$20,861
Amounts related to credit loss for which an other-than-temporary impairment was not previously recognized	—	—
Additions/Subtractions		
Amounts realized for securities sold during the period	—	—
Amounts related to securities for which the company intends to sell or that it will be more likely than not that the company will be required to sell prior to recovery of amortized cost basis	—	—
Reductions for increase in cash flows expected to be collected that are recognized over the remaining life of the security	—	—
Increases to the amount related to the credit loss for which other-than-temporary was previously recognized	—	—
Ending balance, September 30,	\$20,597	\$20,861

9.

**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 3. Securities (Continued)**

The following table presents a rollforward of the credit losses recognized in earnings for the nine month period ended September 30, 2012 and 2011:

	2012	2011
Beginning balance, January 1,	\$20,597	\$20,362
Amounts related to credit loss for which an other-than-temporary impairment was not previously recognized	—	—
Additions/Subtractions		
Amounts realized for securities sold during the period	—	—
Amounts related to securities for which the company intends to sell or that it will be more likely than not that the company will be required to sell prior to recovery of amortized cost basis	—	—
Reductions for increase in cash flows expected to be collected that are recognized over the remaining life of the security	—	—
Increases to the amount related to the credit loss for which other-than-temporary was previously recognized	—	499
Ending balance, September 30,	\$20,597	\$20,861

See Note 9 on Fair Value for additional information about our analysis on the security portfolio related to the fair value and other-than-temporary impairment disclosures of these instruments.

**Note 4. Loans**

The major classifications of loans follow:

Aggregate Principal  
Amount

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	September 30, 2012	December 31, 2011
Commercial	\$58,444	\$63,982
Agricultural & AGRE	42,371	39,128
Construction, land & development	32,431	42,008
Commercial RE	296,495	288,068
1-4 family mortgages	129,245	146,767
Consumer	2,490	2,442
Total Loans	\$561,476	\$582,395
Allowance for loan losses	(21,070 )	(21,232 )
Loans, net	\$540,406	\$561,163

There were \$0.2 million and \$1.8 million of loans held for sale at September 30, 2012 and December 31, 2011, respectively.

The credit quality indicator utilized by the Company to internally analyze the loan portfolio is the internal risk rating. Internal risk ratings of 0 to 5 are considered pass credits, a risk rating of a 6 is special mention, a risk rating of a 7 is substandard, and a risk rating of an 8 is doubtful. Loans classified as pass credits have no identified material weaknesses and are performing as agreed. Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 4. Loans (Continued)**

The following table presents the commercial loan portfolio by internal risk rating:

**September 30, 2012**

Internal Risk Rating	Commercial				Commercial Real Estate		Total
	Closed-end	Lines of Credit	Agriculture & AG RE	Construction, Land & Development	Owner-Occupied	Non-Owner Occupied	
1-2	\$1,019	\$288	\$ 4,498	\$ 116	\$3,230	\$ 625	\$9,776
3	2,610	8,914	14,682	1,064	10,248	13,687	51,205
4	7,871	10,613	15,463	2,306	78,495	62,581	177,329
5	9,051	8,813	7,602	11,494	18,726	54,822	110,508
6	461	3,864	—	2,050	7,060	13,943	27,378
7	3,704	1,236	126	14,476	15,954	17,124	52,620
8	—	—	—	925	—	—	925
Total	\$24,716	\$33,728	\$ 42,371	\$ 32,431	\$133,713	\$ 162,782	\$429,741

**December 31, 2011**

Internal Risk Rating	Commercial				Commercial Real Estate		Total
	Closed-end	Lines of Credit	Agriculture & AG RE	Construction, Land & Development	Owner-Occupied	Non-Owner Occupied	
1-2	\$716	\$449	\$ 4,833	\$ 3,649	\$3,489	\$ 647	\$13,783
3	2,938	7,708	15,649	1,034	8,971	17,168	53,468
4	12,989	13,533	14,323	1,566	68,045	44,665	155,121
5	10,405	5,322	3,517	6,200	20,518	51,580	97,542
6	3,374	3,892	741	5,497	10,868	19,900	44,272
7	1,434	1,222	65	24,062	19,720	22,497	69,000



8	—	—	—	—	—	—	—
Total	\$31,856	\$32,126	\$39,128	\$42,008	\$131,611	\$156,457	\$433,186

The retail residential loan portfolio is generally unrated. Delinquency is a typical factor in adversely risk rating a credit to a special mention or substandard. The following table presents the retail residential loan portfolio by internal risk rating:

	Residential -- 1-4 family		
	Senior Lien	Jr. Lien & Lines of Credit	Total
September 30, 2012			
Unrated	\$68,285	\$47,917	\$116,202
Special mention	2,580	943	3,523
Substandard	8,831	689	9,520
Doubtful	—	—	—
Total	\$79,696	\$49,549	\$129,245

11.

**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 4. Loans (Continued)**

	Residential -- 1-4 family		
	Senior Lien	Jr. Lien & Lines of Credit	Total
December 31, 2011			
Unrated	\$83,969	\$49,498	\$133,467
Special mention	907	904	1,811
Substandard	10,013	1,161	11,174
Doubtful	315	—	315
Total	\$95,204	\$51,563	\$146,767

An analysis of the activity in the allowance for loan losses for the three months ended September 30, 2012 and 2011 follows:

	Commercial	Agriculture & AG RE	Construction, Land & Development	Commercial RE	1-4 Family Residential	Consumer	Total
September 30, 2012							
Beginning Balance	\$ 1,478	\$ 267	\$ 3,793	\$ 9,765	\$ 2,883	\$ 48	\$18,234
Charge-offs	—	(128 )	(2,150)	(191 )	(714)	—	(3,183)
Recoveries	1	19	2	239	7	1	269
Provision	503	(48 )	2,234	1,264	1,792	5	5,750
Ending Balance	\$ 1,982	\$ 110	\$ 3,879	\$ 11,077	\$ 3,968	\$ 54	\$21,070

	Commercial	Agriculture & AG RE	Construction, Land & Development	Commercial RE	1-4 Family Residential	Consumer	Total
September 30, 2011							
Beginning Balance	\$ 1,751	\$ 386	\$ 6,310	\$ 13,009	\$ 2,867	\$ 35	\$24,358
Charge-offs	(151 )	(21 )	(3,018)	(961 )	(194)	(9 )	(4,354)
Recoveries	17	3	451	12	426	1	910

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Provision	509	(362 )	1,372	702	170	9	2,400
Ending Balance	\$ 2,126	\$ 6	\$ 5,115	\$ 12,762	\$ 3,269	\$ 36	\$23,314

An analysis of the activity in the allowance for loan losses for the nine months ended September 30, 2012 and 2011 follows:

	Commercial	Agriculture & AG RE	Construction, Land & Development	Commercial RE	1-4 Family Residential	Consumer	Total
September 30, 2012							
Beginning Balance	\$ 1,590	\$ 5	\$ 4,811	\$ 11,680	\$ 3,090	\$ 56	\$21,232
Charge-offs	—	(215 )	(3,243)	(4,120 )	(1,792)	(6 )	(9,376)
Recoveries	1	62	288	370	14	4	739
Provision	391	258	2,023	3,147	2,656	—	8,475
Ending Balance	\$ 1,982	\$ 110	\$ 3,879	\$ 11,077	\$ 3,968	\$ 54	\$21,070

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**Centrue Financial Corporation**

## Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

**Note 4. Loans (Continued)**

	Commercial	Agriculture & AG RE	Construction, Land & Development	Commercial RE	1-4 Family Residential	Consumer	Total
September 30, 2011							
Beginning Balance	\$ 1,634	\$ 337	\$ 12,500	\$ 13,721	\$ 3,273	\$ 46	\$31,511
Charge-offs	(391 )	(674 )	(9,852)	(6,975 )	(1,489)	(35 )	(19,416)
Recoveries	35	6	551	243	462	22	1,319
Provision	848	337	1,916	5,773	1,023	3	9,900
Ending Balance	\$ 2,126	\$ 6	\$ 5,115	\$ 12,762	\$ 3,269	\$ 36	\$23,314

The following is an analysis on the balance in the allowance for loan losses and the recorded investment in impaired loans by portfolio segment based on impairment method as of September 30, 2012 and December 31, 2011:

September 30, 2012	Commercial	Agriculture & AG RE	Construction, Land & Development	Commercial RE	1-4 Family Residential	Consumer	Total
Allowance for loan losses:							
Loans individually evaluated for impairment	\$ 1,510	\$ 41	\$ 2,744	\$ 6,852	\$ 2,327	\$ 2	\$13,476
Loans collectively evaluated for impairment	472	69	1,135	4,225	1,641	52	7,594
Total ending allowance balance:	\$ 1,982	\$ 110	\$ 3,879	\$ 11,077	\$ 3,968	\$ 54	\$21,070
Loan balances:							
Loans individually evaluated for impairment	\$ 4,712	\$ 126	\$ 15,401	\$ 29,746	\$ 9,510	\$ 4	\$59,499
Loans collectively evaluated for impairment	53,732	42,245	17,030	266,749	119,735	2,486	501,977
Loans with an allowance recorded:	\$ 58,444	\$ 42,371	\$ 32,431	\$ 296,495	\$ 129,245	\$ 2,490	\$561,476

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December 31, 2011	Commercial	Agriculture & AG RE	Construction, Land & Development	Commercial RE	1-4 Family Residential	Consumer Total	
Allowance for loan losses:							
Loans individually evaluated for impairment	\$ 715	\$ —	\$ 2,228	\$ 5,211	\$ 1,591	\$ 5	\$9,750
Loans collectively evaluated for impairment	875	5	2,583	6,469	1,499	51	11,482
Total ending allowance balance:	\$ 1,590	\$ 5	\$ 4,811	\$ 11,680	\$ 3,090	\$ 56	\$21,232
Loan balances:							
Loans individually evaluated for impairment	\$ 2,463	\$ 65	\$ 24,062	\$ 36,141	\$ 10,563	\$ 5	\$73,299
Loans collectively evaluated for impairment	61,519	39,063	17,946	251,927	136,204	2,437	509,096
Loans with an allowance recorded:	\$ 63,982	\$ 39,128	\$ 42,008	\$ 288,068	\$ 146,767	\$ 2,442	\$582,395

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)**

**Note 4. Loans (Continued)**

**Troubled Debt Restructurings:**

The Company had troubled debt restructurings (“TDRs”) of \$3.9 million and \$7.1 million as of September 30, 2012 and December 31, 2011, respectively. Specific reserves of \$0.1 million and \$0.95 million were allocated to TDRs as of September 30, 2012 and December 31, 2011, respectively. At September 30, 2012, nonaccrual TDR loans were \$3.8 million, as compared to \$6.0 million at December 31, 2011. September 30, 2012 there were \$0.1 million of TDRs on accrual status compared to December 31, 2011, when \$1.1 million was on accrual. The Company has not committed to lend any additional amounts to customers with outstanding loans that are classified as TDRs as of September 30, 2012.

At September 30, 2012, the Company held loans whose terms had been modified as troubled debt restructuring. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan to a below market rate or the payment modification to interest only. Modifications involving a reduction of the stated interest rate of the loan were for periods ranging from 6 months to 16 months. During the nine month period ending September 30, 2012, there was one TDR added in the amount of \$0.9 million during the first quarter and two TDRs added in the third quarter in the amount \$0.1 million. The TDR from the first quarter was subsequently removed in the second quarter as the collateral was sold, specific provision charged-off and the remaining loan balance paid-off. The TDRs added during the three month period ending September 30, 2012, have specific reserves of \$0.02 million allocated to them.

A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms. There were no loans modified as troubled debt restructurings for which there was a payment default within twelve months following the modification during the three or nine month period ending September 30, 2012.

The Company evaluates loan modifications to determine if the modification constitutes a troubled debt restructure. A loan modification constitutes a troubled debt restructure if the borrower is experiencing financial difficulty and the Company grants a concession it would not otherwise consider. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment

default on any of its loans with the Company's debt in the foreseeable future without the modification. This evaluation is performed under the Company's internal underwriting guidelines. TDRs are separately identified for impairment disclosures. If a loan is considered to be collateral dependent loan, the TDR is reported, net, at the fair value of the collateral.

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**Centrue Financial Corporation**

## Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

**Note 4. Loans (Continued)**

The following tables present data on impaired loans:

September 30, 2012	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
Loans with no related allowance recorded:						
Commercial						
Closed-end	\$ 181	\$ 195	\$ —	\$ 87	\$ 2	\$ 2
Line of credit	65	328	—	39	1	1
Agricultural & AG RE	—	—	—	39	—	—
Construction, land & development	2,721	8,472	—	4,120	—	—
CRE - all other						
Owner occupied	4,755	4,857	—	4,655	26	23
Non-owner occupied	4,532	4,532	—	5,466	224	200
1-4 family residential						
Senior lien	1,113	1,568	—	1,214	5	4
Jr. lien & lines of credit	261	337	—	358	7	7
Consumer	2	2	—	1	—	—
Subtotal	13,630	20,291	—	15,979	265	237
Loans with an allowance recorded:						
Commercial						
Closed-end	\$ 3,295	\$ 3,423	\$ 1,510	\$ 2,105	\$ 104	\$ 98
Line of credit	1,171	1,171	—	1,185	—	(10 )
Agricultural & AG RE	126	126	41	62	1	1
Construction, land & development	12,680	24,763	2,744	15,367	16	14
CRE - all other						
Owner occupied	11,075	11,608	4,496	11,970	448	355
Non-owner occupied	9,384	9,608	2,356	10,099	129	104
1-4 family residential						
Senior lien	7,708	8,362	2,001	7,779	184	173
Jr. lien & lines of credit	428	575	326	488	8	8
Consumer	2	2	2	3	—	—



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Subtotal	45,869	59,638	13,476	49,058	890	743
Total	\$ 59,499	\$ 79,929	\$ 13,476	\$ 65,037	\$ 1,155	\$ 980
Commercial	\$ 49,985	\$ 69,083	\$ 11,147	\$ 55,194	\$ 951	\$ 788
Residential	\$ 9,510	\$ 10,842	\$ 2,327	\$ 9,839	\$ 204	\$ 192
Consumer	\$ 4	\$ 4	\$ 2	\$ 4	\$ —	\$ —

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**Centrue Financial Corporation**

## Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

**Note 4. Loans (Continued)**

December 31, 2011	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized	
Loans with no related allowance recorded:							
Commercial							
Closed-end	\$ 28	\$ 28	\$ —	\$ 53	\$ 1	\$ 1	
Line of credit	45	308	—	550	—	—	
Agricultural & AG RE	65	682	—	62	3	3	
Construction, land & development	4,453	14,583	—	10,066	58	58	
CRE - all other							
Owner occupied	4,738	5,417	—	6,284	44	41	
Non-owner occupied	7,749	8,656	—	11,933	442	416	
1-4 family residential							
Senior lien	1,108	1,576	—	2,198	37	37	
Jr. lien & lines of credit	683	799	—	697	17	16	
Consumer	—	—	—	—	—	—	
Subtotal	18,869	32,049	—	31,843	602	572	
Loans with an allowance recorded:							
Commercial							
Closed-end	\$ 1,213	\$ 1,213	\$ 449	\$ 1,380	\$ 84	\$ 84	
Line of credit	1,177	1,177	266	2,337	25	14	
Agricultural & AG RE	—	—	—	1,039	—	—	
Construction, land & development	19,609	30,053	2,228	19,749	(26	) (27	)
CRE - all other							
Owner occupied	14,851	15,204	3,678	13,152	850	773	
Non-owner occupied	8,803	11,142	1,533	11,632	383	353	
1-4 family residential							
Senior lien	8,396	8,580	1,391	8,062	693	677	
Jr. lien & lines of credit	375	482	200	386	9	9	
Consumer	6	6	5	4	—	—	
Subtotal	54,430	67,857	9,750	57,741	2,018	1,883	
Total	\$ 73,299	\$ 99,906	\$ 9,750	\$ 89,584	\$ 2,620	\$ 2,455	
Commercial	\$ 62,731	\$ 88,463	\$ 8,154	\$ 78,237	\$ 1,864	\$ 1,716	

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Residential	\$ 10,562	\$ 11,437	\$ 1,591	\$ 11,343	\$ 756	\$ 739
Consumer	\$ 6	\$ 6	\$ 5	\$ 4	\$ —	\$ —

Due to the economic conditions facing many of its customers, the Company determined that there were \$12.8 million and \$28.6 million of loans that were classified as impaired but were considered to be performing loans at September 30, 2012 and December 31, 2011, respectively.

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**Centrue Financial Corporation**

## Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 4. Loans (Continued)**

The following tables represent activity related to loan portfolio aging:

September 30, 2012	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days Past Due or Nonaccrual	Total Past Due	Current	Total Loans
Commercial						
Closed-end	\$39	\$—	\$ 1,974	\$2,013	\$22,703	\$24,716
Line of credit	81	—	1,216	1,297	32,431	33,728
Agricultural & AG RE	70	—	126	196	42,175	42,371
Construction, land & development	145	—	15,083	15,228	17,203	32,431
CRE - all other						
Owner occupied	1,110	839	13,661	15,610	118,103	133,713
Non-owner occupied	752	—	6,232	6,984	155,798	162,782
1-4 family residential						
Senior lien	854	624	7,820	9,298	70,398	79,696
Jr. lien & lines of credit	349	21	558	928	48,621	49,549
Consumer	3	—	—	3	2,487	2,490
Total	\$3,403	\$1,484	\$ 46,670	\$51,557	\$509,919	\$561,476

December 31, 2011	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days Past Due or Nonaccrual	Total Past Due	Current	Total Loans
Commercial						
Closed-end	\$1,183	\$—	\$ 95	\$1,278	\$30,578	\$31,856
Line of credit	—	43	1,222	1,265	30,861	32,126
Agricultural & AG RE	—	—	65	65	39,063	39,128
Construction, land & development	—	472	23,738	24,210	17,798	42,008
CRE - all other					—	
Owner occupied	2,477	1,357	8,633	12,467	119,144	131,611
Non-owner occupied	3,207	3,000	6,572	12,779	143,678	156,457
1-4 family residential					—	

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Senior lien	2,832	691	3,588	7,111	88,093	95,204
Jr. lien & lines of credit	738	151	806	1,695	49,868	51,563
Consumer	10	—	4	14	2,428	2,442
Total	\$10,447	\$5,714	\$ 44,723	\$60,884	\$521,511	\$582,395

The Company did not hold any loans as of September 30, 2012 or December 31, 2011 that were ninety or more days past due and still on accrual status.

17.

**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 4. Loans (Continued)**

The following table represents data for nonaccrual loans:

	For the period ended	
	September 30, 2012	December 31, 2011
Commercial		
Closed-end	\$1,974	\$ 95
Line of credit	1,216	1,222
Agricultural & AG RE	126	65
Construction, land & development	15,083	23,738
CRE - all other		
Owner occupied	13,661	8,633
Non-owner occupied	6,232	6,572
1-4 family residential		
Senior lien	7,820	3,588
Jr. lien & lines of credit	558	806
Consumer	—	4
Total	\$46,670	\$ 44,723

Nonaccrual loans include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

**Note 5. Share Based Compensation**

In April 2003, the Company adopted the 2003 Option Plan. Under the 2003 Option Plan, as amended on April 24, 2007, nonqualified options, incentive stock options, restricted stock and/or stock appreciation rights may be granted to employees and outside directors of the Company and its subsidiaries to purchase the Company's common stock at an

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exercise price to be determined by the Executive and Compensation committee. Pursuant to the 2003 Option Plan, 570,000 shares of the Company's unissued common stock have been reserved and are available for issuance upon the exercise of options and rights granted under the 2003 Option Plan. The options have an exercise period of seven to ten years from the date of grant. There are 66,000 shares available to grant under this plan.

A summary of the status of the option plans as of September 30, 2012, and changes during the period ended on those dates is presented below:

	September 30, 2012				
	Shares	Weighted-Average Exercise Price	Weighted-Average Life	Remaining Contractual	Aggregate Intrinsic Value
Outstanding at January 1, 2012	328,438	\$ 16.17			
Granted	—	—			
Exercised	—	—			
Forfeited	(53,511 )	16.96			
Outstanding at end of period	274,927	\$ 16.01	2.5 years		\$ —
Vested or expected to vest	273,820	\$ 16.03	2.5 years		\$ —
Options exercisable at period end	250,327	\$ 16.42	2.5 years		\$ —

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**Centrue Financial Corporation**

## Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)**

## Note 5. Share Based Compensation (Continued)

Options outstanding at September 30, 2012 and December 31, 2011 were as follows:

Range of Exercise Prices	Outstanding			Exercisable	
	Number	Weighted-Average	Remaining Contractual Life	Number	Weighted-Average Exercise Price
September 30, 2012:					
\$ 5.24 - \$ 13.00	73,500	3.4 years		56,100	\$ 7.18
13.24 - 18.63	92,327	1.8 years		85,127	17.25
19.03 - 23.31	109,100	2.6 years		109,100	20.53
	274,927	2.5 years		250,327	\$ 16.42
December 31, 2011:					
\$ 5.24 - \$ 13.00	75,500	4.2 years		49,400	\$ 6.89
13.24 - 18.63	124,838	2.0 years		110,438	16.43
19.03 - 23.31	128,100	3.0 years		124,500	20.77
	328,438	2.9 years		284,338	\$ 16.67

There were no options exercised for the periods ended September 30, 2012 and 2011. The compensation cost that has been charged against income for the stock options portion of the Option Plans was \$0.01 million and \$(0.005) million for the three months ended September 30, 2012 and 2011, and \$0.02 million and \$0.05 million for the nine months ended September 30, 2012 and 2011, respectively.

There were no stock options granted during the 2012 and 2011 periods.

Unrecognized stock option compensation expense related to unvested awards (net of estimated forfeitures) for the remainder of 2012 and beyond is estimated as follows:



	Amount
October, 2012 - December, 2012	\$ 10
2013	18
2014	—
Total	\$ 28

#### **Note 6. Contingent Liabilities and Other Matters**

Neither the Company nor its subsidiary is involved in any pending legal proceedings other than routine legal proceedings occurring in the normal course of business, which, in the opinion of management, in the aggregate, are not material to the Company's consolidated financial condition.

#### **Note 7. Segment Information**

The Company's segment information provided below focuses on its three primary lines of business (Segment(s)): Retail Banking, Commercial Banking and Treasury. The financial information presented was derived from the Company's internal profitability reporting system that is used by management to monitor and manage the financial performance of the Company. This information is based on internal management accounting policies which have been developed to reflect the underlying economics of the Segments and, to the extent practicable, to portray each Segment as if it operated on a stand-alone basis. Thus, each Segment, in addition to its direct revenues, expenses, assets and liabilities, includes an allocation of shared support function expenses and corporate overhead. All Segments also include funds transfer adjustments to appropriately reflect the cost of funds on loans made, funding credits on deposits generated, and the cost of maintaining adequate liquidity. Apart from these adjustments, the accounting policies used are similar to those described in Note 1 of our financial statements from the December 31, 2011 10-K.

**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 7. Segment Information (Continued)**

Since there are no comprehensive standards for management accounting that are equivalent to accounting principles generally accepted in the United States of America, the information presented may not necessarily be comparable with similar information from other financial institutions. In addition, methodologies used to measure, assign, and allocate certain items may change from time-to-time to reflect, among other things, accounting estimate refinements, changes in risk profiles, changes in customers or product lines, and changes in management structure.

The Retail Banking Segment provides retail banking services including direct and indirect lending, checking, savings, money market and certificate of deposit ("CD") accounts, safe deposit rental, automated teller machines and other traditional and electronic commerce retail banking services to individual customers through the Bank's branch locations. The Retail Banking Segment also provides a variety of mortgage lending products to meet customer needs. The majority of the mortgage loans it originates are sold to a third party mortgage services company, which provides private label loan processing and servicing support for both loans sold and loans retained by the Bank.

The Commercial Banking Segment provides commercial banking services including lending, business checking and deposits, treasury management and other traditional as well as electronic commerce commercial banking services to middle market and small business customers through the Bank's branch locations.

The Treasury segment is responsible for managing the investment portfolio, acquiring wholesale funding for loan activity and assisting in the management of the Company's liquidity and interest rate risk. Information reported internally for performance assessment follows:

	Three Months Ended September 30, 2012				
	Retail Segment	Commercial Segment	Treasury Segment	Other Operations	Total Company
Net interest income (loss)	\$ 1,786	\$ 4,894	\$(495)	) \$ 113	\$6,298
Other revenue	2,396	362	684	387	3,829
Other expense	2,577	1,450	44	3,899	7,970

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Noncash items					
Depreciation	216	1	—	59	276
Provision for loan losses	1,797	3,953	—	—	5,750
Other intangibles	238	—	—	—	238
Net allocations	815	2,443	200	(3,458 )	—
Income tax benefit	(29 )	(846 )	87	—	(788 )
Segment profit (loss)	\$(1,432 )	\$(1,745 )	\$(142 )	\$ —	\$(3,319 )
Segment assets	\$ 153,649	\$ 459,138	\$ 205,319	\$ 86,719	\$ 904,825

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**Centrue Financial Corporation**

## Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

**Note 7. Segment Information (Continued)**

	Three Months Ended September 30, 2011				
	Retail Segment	Commercial Segment	Treasury Segment	Other Operations	Total Company
Net interest income (loss)	\$ 1,918	\$ 5,476	\$(411 )	\$ (106 )	\$ 6,877
Other revenue	2,111	229	—	226	2,566
Other expense	2,607	5,129	45	3,906	11,687
Noncash items					
Depreciation	270	—	—	190	460
Provision for loan losses	179	2,221	—	—	2,400
Other intangibles	250	—	—	—	250
Net allocations	1,200	2,489	287	(3,976 )	—
Income tax benefit	13	(597 )	(22 )	—	(606 )
Segment profit (loss)	\$(490 )	\$(3,537 )	\$(721 )	\$ —	\$(4,748 )
Segment assets	\$ 178,774	\$ 496,275	\$ 267,110	\$ 66,794	\$ 1,008,953
	Nine Months Ended September 30, 2012				
	Retail Segment	Commercial Segment	Treasury Segment	Other Operations	Total Company
Net interest income (loss)	\$ 5,485	\$ 14,492	\$(1,362 )	\$ (52 )	\$ 18,563
Other revenue	6,386	1,797	1,398	1,112	10,693
Other expense	7,590	4,009	132	11,819	23,550
Noncash items					
Depreciation	689	1	—	352	1,042
Provision for loan losses	2,656	5,819	—	—	8,475
Other intangibles	713	—	—	—	713
Net allocations	2,969	7,413	729	(11,111 )	—
Income tax benefit	(29 )	(846 )	87	—	(788 )
Segment profit (loss)	\$(2,717 )	\$(107 )	\$(912 )	\$ —	\$(3,736 )
Segment assets	\$ 153,649	\$ 459,138	\$ 205,319	\$ 86,719	\$ 904,825

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Nine Months Ended  
September 30, 2011

	Retail Segment	Commercial Segment	Treasury Segment	Other Operations	Total Company
Net interest income (loss)	\$5,922	\$ 17,293	\$(1,537 )	\$(360 )	\$21,318
Other revenue	6,008	681	(120 )	805	7,374
Other expense	7,960	7,555	132	12,932	28,579
Noncash items					
Depreciation	818	1	—	587	1,406
Provision for loan losses	1,024	8,876	—	—	9,900
Other intangibles	789	—	—	—	789
Net allocations	3,976	8,096	1,002	(13,074 )	—
Income tax benefit	(14 )	(1,181 )	(157 )	—	(1,352 )
Segment profit (loss)	\$(2,623 )	\$(5,373 )	\$(2,634 )	\$—	\$(10,630 )
Segment assets	\$178,774	\$ 496,275	\$267,110	\$ 66,794	\$1,008,953

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## Centrue Financial Corporation

Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

### Note 8. Borrowed Funds and Debt Obligations

As of September 30, 2012, the Company has \$10.3 million outstanding per a loan agreement dated March 31, 2008. This original agreement was entered into with Bank of America and consisted of three credit facilities: a secured revolving line of credit, a secured term facility, and a subordinated debt. In February 2009, the loan agreement on the revolving line of credit was amended resulting in an aggregate principal amount of \$20.3 million. The first credit facility consisted of a \$10.0 million secured revolving line of credit which matured on June 30, 2009 and was not renewed by Bank of America. The second credit facility consists of a \$0.3 million secured term facility, which will mature in March 31, 2015. The third credit facility consists of \$10.0 million in subordinated debt, which also matures in March 31, 2015. On December 14, 2009, Bank of America transferred to Cole Taylor Bank all rights, title, interest in to and under the loan agreements dated March 31, 2008. Repayment of each of the remaining two credit facilities is interest only on a quarterly basis, with the principal amount of the loan due at maturity. The term credit facility is secured by a pledge of the stock of the Bank. The subordinated debt credit facility is unsecured and is intended to qualify as Tier II capital for regulatory purposes. However, the amount included in Tier II capital has been reduced by 60% as of September 30, 2012 due to a sub-debt phase-out provision and will be further reduced by 20% in each of the next two years. The outstanding balance of the debt agreements was \$10.3 million as of September 30, 2012 and December 31, 2011. The Company requires regulatory approval in order to make the quarterly interest payments under our debt agreements as described in Note 13.

On March 7, 2011, the Company entered into an amendment with the lender, which modified the covenant relating to capitalization at the Company and Bank level so that the Company returned to full compliance with the terms of its credit agreement as of December 31, 2010. The amendment contains customary covenants, including but not limited to, the Company and the Bank's maintenance of its status as adequately capitalized and the Bank's minimum loan loss reserves to total loans of 3.00%. As of December 31, 2011, the Company was in compliance with all covenants, with the exception of the Tier 1 leverage ratio, and all payments remain current. A covenant waiver was received from the lender as of December 31, 2011; the loan covenants were revised through an amendment effective quarter-end March 31, 2012 and each quarter thereafter to maintain the adequately capitalized levels for the Bank and remove the holding company capital requirements. As of September 30, 2012, the Company and Bank are in compliance with the covenants of the amended agreement.

Additionally, the Company has a note outstanding to an individual with an imputed interest rate of 5.25% maturing October 24, 2012 from a prior acquisition. The balance as of September 30, 2012 and December 31, 2011 was \$0.1 million and \$0.2 million, respectively.

## Note 9. Fair Value

The Company measures, monitors, and discloses certain of its assets and liabilities on a fair value basis. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Company maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Fair value guidance establishes a fair value hierarchy that prioritizes the inputs used to measure fair value into three broad levels based on the reliability of the input assumptions. The hierarchy gives the highest priority to Level 1 measurements and the lowest priority to Level 3 measurements and the categorization of where an asset or liability falls within the hierarchy is based on the lowest level of input that is significant to the fair value measurement. The three levels of the fair value hierarchy are defined as follows:

Level 1 – Unadjusted quoted prices for identical assets or liabilities traded in active markets.

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar instruments; 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 asset or liability.

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.

The Company used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

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## Centrue Financial Corporation

Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

### Note 9. Fair Value (Continued)

#### Securities

*Available for Sale Securities.* The fair value of securities available for sale is determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). If the securities could not be priced using quoted market prices, observable market activity or comparable trades, the financial market was considered not active and the assets were classified as Level 3. The fair values of Level 3 investment securities are determined by the Finance group who provide default and scenario assumptions to the Company's Chief Investment Officer (CIO) who performs the modeling for the analysis and submits for review by the Chief Financial Officer (CFO). Discounted cash flows are calculated using spread to swap and LIBOR curves that are updated to incorporate loss severities, volatility, credit spread and optionality. During times when trading is more liquid, broker quotes are used (if available) to validate the model. Ratings agency and industry research reports as well as defaults and deferrals on individual securities are reviewed and incorporated into the calculations.

*Pooled Trust Preferred Collateralized Debt Obligations ("CDO").* The assets included in Level 3 are CDOs. Over the past few years, the decline in the level of observable inputs and market activity for trust preferred CDOs by the measurement date was significant and resulted in unreliable external pricing. As such, the Company uses an internal other-than-temporary impairment ("OTTI") evaluation model to compare the present value of expected cash flows to the previous estimate to ensure there are no adverse changes in cash flows during the quarter. The OTTI model considers the structure and term of each CDO and the financial condition of the underlying issuers. Specifically, the model details interest rates, principal balances of note classes and underlying issuers, the timing and amount of interest and principal payments of the underlying issuers, and the allocation of the payments to the note classes. The current estimate of expected cash flows is based on the most recent trustee reports and any other relevant market information including announcements of interest payment deferrals or defaults of underlying trust-preferred securities. Assumptions used in the model include expected future default rates and prepayments.

The Company assumes no recoveries on defaults and treats all interest payment deferrals as defaults. In addition, we use the model to "stress" each CDO, or make assumptions more severe than expected activity, to determine the degree to which assumptions could deteriorate before the CDO could no longer fully support repayment of the Company's note



class.

Each issuer in the tranche was analyzed using the Fitch ratings for the quarter and key financial data so that the issuer in each tranche can be divided between a pool of “performing” companies and “under-performing” companies. A factor is applied to the under-performing company for each quarter to project additional defaults and deferrals to be factored into the cash flow model. Three internal scenarios were developed that had different assumptions regarding the impact of the economic environment on additional defaults and deferrals for the upcoming quarters. On average, the additional deferrals for a specific CDO that were factored in to our calculation were approximately 8% of the performing balance of the instrument across the three scenarios. All of the additional deferrals for the three scenarios are factored in to the cash flow for each tranche. A discount factor to be applied to the London Interbank Offered Rate (“LIBOR”) was developed for each specific tranche and incorporated to arrive at the discount rate for the CDO. The factor applied ranged from 200 basis points to 600 basis points based on the rating of the CDO and its gross-up factor for risk based capital. These rates were applied to calculate the net present value of the cash flows. The results of the three net present value calculations were weighted based on their likelihood of occurring. The scenarios were weighted 35%, 47% and 18%.

Finally, an independent valuation of our portfolio was obtained. This was weighted as the final overall step to arrive at our valuation for September 30, 2012 using 55% for the internal weighting and 45% for the external one. Due to market conditions as well as the limited trading activity of these securities, the market value of the securities is highly sensitive to assumption changes and market volatility.

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## Centrue Financial Corporation

Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

### Note 9. Fair Value (Continued)

At September 30, 2012, the Company held five pooled trust preferred CDOs with an amortized cost of \$7.9 million. These securities were rated high quality (A3 and above) at inception, but at September 30, 2012, these securities were rated as Ca, which are defined as highly speculative and/or default, with some recovery; and C, which is the lowest rating. The issuers in these securities are primarily banks, but some of the pools do include a limited number of insurance companies.

The Company performed an analysis including evaluation for OTTI for each of the five CDOs. During the third quarter of 2012, our model indicated no OTTI was needed for credit impairment. Management has determined that the remaining CDOs are deemed to be only temporarily impaired at quarter-end due to the projected cash flows adjusted for the possible further deterioration is sufficient to return the outstanding principal balance with interest at the stated rate.

*Private Label CMOs.* Private label CMOs were also evaluated using management's internal analysis process. These securities were rated high quality (A3 and above) at inception and are primarily supported by prime collateral, although the RAST Series security has some alt-a collateral support. During the third quarter of 2012, our model indicated no OTTI on these CMOs, with an aggregate cost basis of \$1.0 million.

*Single Issue Trust Preferred.* During the third quarter of 2010, the Company purchased \$3.8 million of single-issue trust preferred securities that are classified as available for sale. With respect to these securities, the Company looks at rating agency actions, payment history, the capital levels of the banks and the financial performance as filed in regulatory reports. As of September 30, 2012, the aggregate cost basis on these securities was \$2.1 million as there have been calls on these securities in previous quarters.

The Company's unrealized losses on other securities relate primarily to its investment in CDO securities. The decline in fair value is primarily attributable to temporary illiquidity and the financial crisis affecting these markets and not necessarily the expected cash flows of the individual securities. Due to the illiquidity in the market, it is unlikely that the Company would be able to recover its investment in these securities if the Company sold the securities at this time. The Company does not intend to sell these securities nor is it more likely than not the Company will be required to

sell these securities before its anticipated recovery.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table summarizes, by measurement hierarchy, the various assets and liabilities of the Company that are measured at fair value on a recurring basis:

	Carrying Amount	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2012				
U.S. government agencies	\$7,069	\$ —	\$ 7,069	\$ —
State and political subdivisions	16,243	—	16,243	—
U.S. government agency residential mortgage-backed securities	119,130	—	119,130	—
Collateralized mortgage obligations:				
Agency	23,336	—	23,336	—
Private Label	1,083	—	—	1,083
Equities	2,683	—	2,683	—
Collateralized debt obligations:				
Single Issue	2,064	—	2,064	—
Pooled	7,888	—	—	7,888
Corporate	2,000	—	2,000	—
Available-for-sale securities	\$181,496	\$ —	\$ 172,525	\$ 8,971

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 9. Fair Value (Continued)**

	Carrying Amount	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2011				
U.S. government agencies	\$3,019	\$ —	\$ 3,019	\$ —
State and political subdivisions	18,125	—	18,125	—
U.S. government agency residential mortgage-backed securities	177,539	—	177,539	—
Collateralized mortgage obligations:				
Agency	15,527	—	15,527	—
Private Label	1,550	—	—	1,550
Equities	2,530	—	2,530	—
Collateralized debt obligations:				
Single Issue	2,064	—	2,064	—
Pooled	6,600	—	—	6,600
Corporate	1,882	—	1,882	—
Available-for-sale securities	\$228,836	\$ —	\$ 220,686	\$ 8,150

There were no transfers between Level 1 and Level 2 during the nine months ended 2012 or all of 2011.

Assets and Liabilities Measured at Fair Value on a Recurring Basis Using Significant Unobservable Inputs

The following table reconciles the beginning and ending balances of the assets of the Company that are measured at fair value on a recurring basis using significant unobservable inputs. There currently are no liabilities of the Company that are measured at fair value on a recurring basis using significant unobservable inputs.

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	Securities Available for Sale			
	2012		2011	
	CDOs	CMOs	CDOs	CMOs
Beginning balance, July 1	\$6,977	\$1,280	\$5,470	\$3,004
Transfers into Level 3	—	—	—	—
Total gains or losses (realized/unrealized) included in earnings	—	—	—	—
Security impairment	—	—	—	—
Payment received	(75 )	(155 )	(1 )	(955 )
Other changes in fair value	—	—	—	1
Included in other comprehensive income	986	(42 )	294	128
Ending Balance, September 30	\$7,888	1,083	5,763	2,178

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 9. Fair Value (Continued)**

	Securities Available for Sale			
	2012		2011	
	CDOs	CMOs	CDOs	CMOs
Beginning balance, January 1	\$6,600	\$1,550	\$4,422	\$4,936
Transfers into Level 3	—	—	—	—
Total gains or losses (realized/unrealized) included in earnings				
Security impairment	—	—	(499 )	—
Payment received	(240 )	(472 )	14	(3,117)
Other changes in fair value	1	1	3	2
Included in other comprehensive income	1,527	4	1,823	357
Ending Balance, September 30	\$7,888	\$1,083	\$5,763	\$2,178

The following table presents quantitative information about recurring Level 3 fair value measurements at September 30, 2012.

	Fair Value	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
Collateralized mortgage obligations	\$1,083	Collateral coverage	Probability of loss Coverage ratio	0% - 40% (34%) 5x - 5x (5x)
Collateralized debt obligations	\$7,888	Discounted cash flow	Collateral default rate Discount rate	4% - 30% (8%) 3% - 5% (3%)

The significant unobservable inputs used in the fair value measurement of the Company's collateralized mortgage obligations are probability of loss and a specified coverage ratio. Significant increases/(decreases) in any of the those inputs in isolation would result in a significantly lower/(higher) fair value measurement.

The significant unobservable inputs used in the fair value measurement of the Company's collateralized debt obligations are probabilities of specific-issuer defaults and deferrals. Significant increases in specific-issuer default assumptions would result in a significantly lower fair value measurement. Conversely, decreases in specific-issuer default and deferral assumptions would result in a higher fair value measurement.

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 9. Fair Value (Continued)**Assets Measured at Fair Value on a Non-Recurring Basis

The following table summarizes, by measurement hierarchy, financial assets of the Company that are measured at fair value on a non-recurring basis:

	Carrying Amount	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2012				
Impaired loans				
Commercial				
Closed end	\$ 1,785	\$ —	\$ —	—\$ 1,785
Line of credit	1,171	—	—	1,171
Agricultural & AGRE	85	—	—	85
CRE - construction, land & development	9,936	—	—	9,936
CRE - all other				
Owner occupied	6,579	—	—	6,579
Non-owner occupied	7,028	—	—	7,028
1-4 family residential				
Senior lien	5,707	—	—	5,707
Junior lien & lines of credit	102	—	—	102
Consumer	—	—	—	—
	Carrying	Quoted	Significant	Significant
	Amount	Prices in	Other	Unobservable
		Active	Observable	Inputs



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	Amount	Markets For Identical Assets (Level 1)	Inputs (Level 2)	(Level 3)
OREO property				
Commercial				
Closed end	\$ —	\$ —	\$ —	—\$ —
Line of credit	—	—	—	—
Agricultural & AGRE	261	—	—	261
CRE - construction, land & development	7,963	—	—	7,963
CRE - all other				
Owner occupied	2,100	—	—	2,100
Non-owner occupied	3,755	—	—	3,755
1-4 family residential				
Senior lien	72	—	—	72
Junior lien & lines of credit	—	—	—	—
Consumer	—	—	—	—

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 9. Fair Value (Continued)**

	Carrying Amount	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2011				
Impaired loans				
Commercial				
Closed end	\$ 764	\$ —	\$ —	—\$ 764
Line of credit	911	—	—	911
Agricultural & AGRE	—	—	—	—
CRE - construction, land & development	17,381	—	—	17,381
CRE - all other				
Owner occupied	11,173	—	—	11,173
Non-owner occupied	7,270	—	—	7,270
1-4 family residential				
Senior lien	7,005	—	—	7,005
Junior lien & lines of credit	175	—	—	175
Consumer	1	—	—	1

	Carrying Amount	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
OREO property				
Commercial				

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Closed end	\$ —	\$ —	\$ —	—\$ —
Line of credit	—	—	—	—
Agricultural & AGRE	261	—	—	261
CRE - construction, land & development	3,312	—	—	3,312
CRE - all other				
Owner occupied	4,082	—	—	4,082
Non-owner occupied	829	—	—	829
1-4 family residential				
Senior lien	285	—	—	285
Junior lien & lines of credit	81	—	—	81
Consumer	—	—	—	—

At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach.

Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 9. Fair Value (Continued)**

Impaired loans had a carrying amount of \$45.9 million with specific loan loss allocations of \$13.5 million in third quarter 2012, resulting in additional provision for loan losses of \$8.9 million for the period. At December 31, 2011, impaired loans had a carrying amount of \$54.4 million with a specific loan loss allocation of \$9.7 million resulting in an additional provision for loan losses of \$9.8 million for the year ended December 31, 2011. The majority of our impaired loans are collateralized by real estate.

Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

OREO properties measured at fair value, less costs to sell, had a net carrying amount of \$14.2 million which is made up of the outstanding balance of \$22.8 million, net of a valuation allowance of \$8.6 million at September 30, 2012, resulting in a write-down of \$0.6 million for the third quarter of 2012 and a write-down of \$1.4 million for the nine month period ending September 30, 2012. This compares to 2011 when OREO properties with a carrying value of \$16.6 million were written down to their fair value of \$8.8 million, which resulted in a charge to earnings of \$7.8 million during the year.

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at September 30, 2012:

Fair Value	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
---------------	---------------------	---------------------	--------------------------------

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Impaired loans	Sales comparison approach	Adjustment for differences between comparable sales
Commercial		
Closed End	\$1,785	20% - 100% (30%)
Line of Credit	1,171	20% - 100% (30%)
Agricultural & AGRE	85	10% - 55% (12%)
CRE - Construction, land & development	9,936	10% - 55% (14%)
CRE - all other		
Owner occupied	6,579	10% - 55% (18%)
Non-owner occupied	7,028	10% - 55% (18%)
1-4 family residential		
Senior lien	5,707	10% - 50% (16%)
Junior lien & lines of credit	102	20% - 100% (51%)
Consumer	—	0% - 60% (0%)

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 9. Fair Value (Continued)**

	Fair Value	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
OREO property		Sales comparison approach	Adjustment for differences between comparable sales	
Commercial				
Closed End	\$—			—
Line of Credit	—			—
Agricultural & AGRE	261			10% (10%)
CRE - Construction, land & development	7,963			8% - 55% (17%)
CRE - all other				
Owner occupied	2,100			15% - 55% (15%)
Non-owner occupied	3,755			10% - 55% (13%)
1-4 family residential				
Senior lien	72			6% - 55% (12%)
Junior lien & lines of credit	—			—
Consumer	—			—

**The Methods and Assumptions Used to Estimate Fair Value of Financial Instruments**

The carrying amount is the estimated fair value for cash, cash equivalents, due from banks, federal funds sold, short-term borrowings, accrued interest receivable and payable, demand deposits, short-term debt, and variable rate loans or deposits that repriced frequently and fully. Security fair values are based on the methods described above.

The carrying value and fair value of the subordinated debentures issued to capital trusts are estimated using market data for similarly risk weighted items to value them. For fixed rate loans or deposits and for variable rate loans or

deposits with infrequent repricing or repricing limits, the fair value is based on discounted cash flows using current market rates applied to the estimated life and credit risk. Fair values for impaired loans are estimated using discounted cash flow analysis or underlying collateral values. The fair value of loans held for sale is based on market quotes. The fair value of debt and redeemable stock is based on current rates for similar financing. It was not practicable to determine the fair value of the restricted securities due to restrictions placed on its transferability. The fair value of off-balance-sheet items is based on the current fees or cost that would be charged to enter into or terminate such arrangements.

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**Centrue Financial Corporation**

## Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)**

## Note 9. Fair Value (Continued)

	Carrying Value	Fair Value measurements at September 30, 2012 Using			Total
		Level 1	Level 2	Level 3	
Financial assets					
Cash and cash equivalents	\$79,423	\$74,423	\$5,000	\$—	\$79,423
Securities	181,496	—	172,525	8,971	181,496
Restricted securities	7,028	—	—	—	NA
Net loans	540,406	—	—	527,836	527,836
Accrued interest receivable	3,003	—	813	2,190	3,003
Financial liabilities					
Deposits	\$782,597	\$—	\$784,872	\$—	\$784,872
Federal funds purchased and securities sold under agreements to repurchase	16,669	—	16,669	—	16,669
Federal Home Loan Bank advances	30,057	—	31,333	—	31,333
Notes payable	10,345	—	—	10,375	10,375
Subordinated debentures	20,620	—	—	12,792	12,792
Series B mandatorily redeemable preferred stock	268	—	268	—	268
Accrued interest payable	4,189	—	762	3,427	4,189

The estimated fair values of the Company's financial instruments at December 31, 2011 are as follows:

	December 31, 2011 Carrying Value	Fair Value
Financial assets		
Cash and cash equivalents	\$ 69,735	\$ 69,735
Securities	228,836	228,836
Restricted securities	9,150	NA
Net loans	561,163	540,612
	3,123	3,123



Accrued interest receivable		
Financial liabilities		
Deposits	\$ 848,638	\$ 849,141
Federal funds purchased and securities sold under agreements to repurchase	18,036	18,036
Federal Home Loan Bank advances	23,058	24,604
Notes payable	10,440	9,321
Subordinated debentures	20,620	14,023
Series B mandatorily redeemable preferred stock	268	268
Accrued interest payable	4,041	4,041

Other assets and liabilities of the Company that are not defined as financial instruments are not included in the above disclosures, such as property and equipment. In addition, nonfinancial instruments typically not recognized in financial statements nevertheless may have value but are not included in the above disclosures.

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)**

**Note 9. Fair Value (Continued)**

These include, among other items, the estimated earning potential of core deposit accounts, the earnings potential of loan servicing rights, customer goodwill and similar items.

The methods and assumptions, not previously presented, used to estimate fair values are described as follows:

***(a) Cash and Cash Equivalents***

The carrying amounts of cash and short-term instruments approximate fair values and are classified as either Level 1 or Level 2.

***(b) Loans***

Fair values of loans, excluding loans held for sale, are estimated as follows: Fair values for loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Impaired loans are valued at the lower of cost or fair value as described previously and carry a Level 3 classification. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

***(c) Deposits***

The fair values disclosed for demand deposits (e.g., interest and non-interest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e.,

their carrying amount) resulting in a Level 2 classification. Fair values for fixed rate certificates of deposit are estimated using a discounted cash flows calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.

***(d) Short-term Borrowings***

The carrying amounts of federal funds purchased, borrowings under repurchase agreements, and other short-term borrowings, generally maturing within ninety days, approximate their fair values resulting in a Level 2 classification.

***(e) Other Borrowings***

The fair values of the Company's long-term borrowings are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 or Level 3 classification.

The fair values of the Company's Subordinated Debentures are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 3 classification.

***(f) Accrued Interest Receivable/Payable***

The carrying amounts of accrued interest approximate fair value resulting in a Level 1, 2 or 3 classification depending on the level its associated asset/liability is classified at.

***(g) Off-balance Sheet Instruments***

Fair values for off-balance sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of commitments is not material.

## Centrue Financial Corporation

Notes to Unaudited Consolidated Financial Statements

(Table Amounts In Thousands, Except Share Data)

### Note 10. Participation in the Treasury Capital Purchase Program

On January 9, 2009, as part of the Troubled Asset Relief Program (“TARP”) Capital Purchase Program, the Company entered into a Letter Agreement and Securities Purchase Agreement (collectively, the “Purchase Agreement”) with the United States Department of the Treasury (“U.S. Treasury”), pursuant to which the Company sold 32,668 shares of newly authorized Fixed Rate Cumulative Perpetual Preferred Stock, Series C, par value \$1.00 per share and liquidation value \$1,000 per share (the “Series C Preferred Stock”) and also issued warrants (the “Warrants”) to the U.S. Treasury to acquire an additional 508,320 shares of the Company’s common stock at an exercise price of \$9.64 per share.

The Series C Preferred Stock qualifies as Tier 1 capital and will pay cumulative dividends at a rate of 5% per annum for the first five years, and 9% per annum thereafter. The Series C Preferred Stock may be redeemed by the Company at any time subject to consultation with the Federal Reserve. The Series C Preferred Stock is not subject to any contractual restrictions on transfer.

Pursuant to the terms of the Purchase Agreement, the ability of the Company to declare or pay dividends or distributions on, or purchase, redeem or otherwise acquire for consideration, shares of its Common Stock will be subject to restrictions, including a restriction against increasing dividends from the last quarterly cash dividend per share \$0.14 declared on the Common Stock prior to October 28, 2008. The redemption, purchase or other acquisition of trust preferred securities of the Company or its affiliates also will be restricted. These restrictions will terminate on the earlier of (a) the third anniversary of the date of issuance of the Preferred Stock and (b) the date on which the Preferred Stock has been redeemed in whole or the U.S. Treasury has transferred all of the Preferred Stock to third parties.

On August 10, 2009, the Company announced that it would defer scheduled dividend payments on the Series C, fixed rate cumulative, perpetual preferred stock. Under the Securities Purchase Agreement entered into with the U.S. Treasury under the TARP program, if a company defers six dividend payments payable to the U.S. Treasury, the U.S. Treasury has the right to appoint up to two directors to its board of directors. As of June 30, 2012 the two directors had been appointed. The Company is accruing the dividends in accordance to GAAP and the terms of the program. At September 30, 2012 and December 31, 2011 the amounts accrued are \$6.0 million and \$4.6 million, respectively. The Company may, at its option with regulatory concurrence, redeem the deferred securities at their liquidation preference plus accrued and unpaid dividends at any time.

Both the preferred securities and the warrant are accounted for as components of regulatory Tier I capital. Per accounting guidelines, the Company is accreting the discount for this instrument.

The U.S. Treasury has notified the Company that the preferred securities and the warrant may be placed into pooled “Dutch Auctions” after October 9, 2012.

**Note 11. Intangible Assets**

Acquired intangible assets were as follows as of the quarter ending:

	September 30, 2012		December 31, 2011	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Core deposit intangibles	\$ 14,124	\$ 10,154	\$ 14,124	\$ 9,441
Missouri charter	581	—	581	—
Total	\$ 14,705	\$ 10,154	\$ 14,705	\$ 9,441

Aggregate amortization expense was \$0.2 million and \$0.3 million for the three months ended September 30, 2012 and 2011. Aggregate amortization expense was \$0.7 million and \$0.8 million for the nine months ended September 30, 2012 and 2011.

**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 11. Intangible Assets (Continued)**

Estimated amortization expense for subsequent periods is as follows:

Remaining quarters in 2012	\$238
2013	951
2014	951
2015	951
2016	879
Thereafter	—

**Note 12. Income Taxes**

In accordance with current income tax accounting guidance, the Company assessed whether a valuation allowance should be established against their deferred tax assets (“DTAs”) based on consideration of all available evidence using a “more likely than not” standard. The most significant portions of the deductible temporary differences relate to (1) net operating loss carryforwards (2) the allowance for loan losses and (3) fair value adjustments or impairment write-downs related to securities.

In assessing the need for a valuation allowance, both the positive and negative evidence about the realization of DTAs were evaluated. The ultimate realization of DTAs is based on the Company’s ability to carryback net operating losses to prior tax periods, tax planning strategies that are prudent and feasible, and the reversal of deductible temporary differences that can be offset by taxable temporary differences and future taxable income.

After evaluating all of the factors previously summarized and considering the weight of the positive evidence compared to the negative evidence, the Company determined a full valuation adjustment was necessary as of December 31, 2011 and September 30, 2012. A three year cumulative loss position and continued near-term losses represent negative evidence that cannot be overcome with future taxable income.

Below is a summary of items included in the deferred tax inventory as of September 30, 2012 and December 31, 2011:

	Balance at 9/30/2012	Balance at 12/31/2011	Change
Allowance for loan loss	\$ 8,177	\$ 8,239	\$(62 )
Impairment on securities portfolio	8,095	8,095	—
Net operating loss carryforwards	21,160	19,388	1,772
Valuation adjustments on OREO property	3,348	3,020	328
Basis adjustment form merger	(1,281 )	(1,467 )	186
Mortgage servicing rights	(775 )	(810 )	35
Securities available-for-sale	(1,760 )	(859 )	(901 )
All other	(46 )	(57 )	11
Net deferred tax before allowance	\$ 36,918	\$ 35,549	\$ 1,369
Valuation allowance	(36,918 )	(35,549 )	(1,369)
Net deferred tax assets	\$ —	\$ —	\$ —

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)****Note 13. Regulatory Matters**

	Actual		To Be Adequately Capitalized		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of September 30, 2012						
Total capital (to risk-weighted assets)						
Centrue Financial	\$54,209	8.4 %	\$51,720	8.0%	N/A	N/A
Centrue Bank	66,378	10.5	50,789	8.0	63,486	10.0
Tier I capital (to risk-weighted assets)						
Centrue Financial	\$30,873	4.8	\$25,860	4.0	N/A	N/A
Centrue Bank	58,280	9.2	25,395	4.0	38,092	6.0
Tier I leverage ratio (to average assets)						
Centrue Financial	\$30,873	3.4	\$36,500	4.0	N/A	N/A
Centrue Bank	58,280	6.4	36,412	4.0	45,515	5.0

	Actual		To Be Adequately Capitalized		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2011						
Total capital (to risk-weighted assets)						
Centrue Financial	\$61,151	9.0 %	\$54,184	8.0%	N/A	N/A
Centrue Bank	68,637	10.3	53,409	8.0	66,762	10.0
Tier I capital (to risk-weighted assets)						
Centrue Financial	\$37,194	5.5	\$27,092	4.0	N/A	N/A
Centrue Bank	60,133	9.0	26,705	4.0	40,057	6.0
Tier I leverage ratio (to average assets)						
Centrue Financial	\$37,194	3.7	\$39,768	4.0	N/A	N/A
Centrue Bank	60,133	6.1	39,681	4.0	49,602	5.0



On December 18, 2009, the Bank entered into an Agreement with the Federal Reserve Bank of Chicago (“FRB”) and the Illinois Department of Financial & Professional Regulation (“IDFPR”). The Agreement describes commitments made by the Bank to address and strengthen banking practices relating to credit risk management practices; improving loan underwriting and loan administration; improving asset quality by enhancing the Bank’s position on problem loans through repayment, additional collateral or other means; reviewing and revising as necessary the Bank’s allowance for loan and lease losses policy; maintaining sufficient capital at the Bank, implementing an earnings plan and comprehensive budget to improve and sustain the Bank’s earnings; and improving the Bank’s liquidity position and funds management practices. The Bank has implemented enhancements to its processes to address the matters identified by the FRB and the IDFPR. The Company is in compliance with all the requirements specified in the agreement except for the Capital Plan. Management continues to aggressively pursue capital raising initiatives to comply with this provision; however, until a more definitive capital raise initiative is developed, the Company will continue to be held in noncompliance with this provision. In the meantime, the Agreement results in the Bank’s ineligibility for certain actions and expedited approvals without the prior written consent and approval of the FRB and the IDFPR. These actions include, among other things, the payment of dividends by the Bank to the Company, the Company cannot pay dividends on its common or preferred shares, payments of interest or principal on subordinated debentures, note payable to Cole Taylor, and Trust Preferred securities, the Company may not increase its debt level and the Company cannot redeem or purchase any shares of its stock.

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**Centrue Financial Corporation**

Notes to Unaudited Consolidated Financial Statements

**(Table Amounts In Thousands, Except Share Data)**

**Note 13. Regulatory Matters (Continued)**

The Company has incurred net losses of \$3.7 million for the first nine months of 2012 and \$10.6 million for the full year 2011 due to loan losses and reduced net interest income. The Company is subject to ongoing monitoring by its regulatory agencies and requires regulatory approval in order to make the quarterly interest payments to Cole Taylor under our debt agreements. The Company has sufficient cash at September 30, 2012 and management believes regulatory approval will be obtained for the remaining interest payments due in 2012. Should the Company and/or its bank subsidiary capital levels fall below “adequately capitalized”, regulatory actions may be taken including requiring us to have higher capital requirements than those required by Prompt Corrective Action regulations. At September 30, 2012 and December 31, 2011, the Company had a Tier 1 leverage ratio of 3.4% and 3.7% which is below the “adequately-capitalized” threshold for that ratio. Management is not aware of any further regulatory actions at this time.

**Note 14. Recent Accounting Developments**

In May, 2011, the FASB issued an amendment to achieve common fair value measurement and disclosure requirements between U.S. and International accounting principles. Overall, the guidance is consistent with existing U.S. accounting principles; however, there are some amendments that change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. The amendments in this guidance are effective for interim and annual reporting periods beginning after December 15, 2011. The adoption of this guidance is included in this filing and included disclosure only.

In June 2011, the FASB amended existing guidance and eliminated the option to present the components of other comprehensive income as part of the statement of changes in shareholder’s equity. The amendment requires that comprehensive income be presented in either a single continuous statement or in two separate consecutive statements. Public Companies: The amendments in this guidance are effective as of the beginning of a fiscal reporting year, and interim periods within that year, that begins after December 15, 2011. Early adoption is permitted. The adoption of this amendment is included in this filing.

## Centrue Financial Corporation

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

#### (Table Amounts In Thousands, Except Share Data)

The following management discussion and analysis ("MD&A") is intended to address the significant factors affecting the Company's results of operations and financial condition for the nine months ended September 30, 2012 as compared to the same period in 2011. In the opinion of management, all normal and recurring adjustments which are necessary to fairly present the results for the interim periods presented have been included. The preparation of financial statements requires management to make estimates and assumptions that affect the recorded amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. When we use the terms "Centrue," the "Company," "we," "us," and "our," we mean Centrue Financial Corporation, a Delaware corporation, and its consolidated subsidiaries. When we use the term the "Bank," we are referring to our wholly owned banking subsidiary, Centrue Bank.

The MD&A should be read in conjunction with the consolidated financial statements of the Company, and the accompanying notes thereto. Actual results could differ from those estimates. All financial information in the following tables is displayed in thousands (000s), except per share data.

#### Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. By their nature, changes in these assumptions and estimates could significantly affect the Company's financial position or results of operations. Actual results could differ from those estimates. Those critical accounting policies that are of particular significance to the Company are discussed in Note 1 of the Company's 2011 Annual Report on Form 10-K.

**Securities:** Securities are classified as available-for-sale when the Company may decide to sell those securities due to changes in market interest rates, liquidity needs, changes in yields on alternative investments, and for other reasons. They are carried at fair value with unrealized gains and losses, net of taxes, reported in other comprehensive income. All of the Company's securities are classified as available-for-sale. For all securities, we obtain fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things. Due to the limited nature of the market for certain securities, the fair value and potential sale proceeds could be materially different in the event of a sale.

Realized securities gains or losses are reported in securities gains (losses), net in the Consolidated Statements of Income. The cost of securities sold is based on the specific identification method. Declines in the fair value of available for sale securities below their amortized cost are evaluated to determine whether the loss is temporary or other-than-temporary. If the Company (a) has the intent to sell a debt security or (b) is more likely than not will be required to sell the debt security before its anticipated recovery, then the Company recognizes the entire unrealized loss in earnings as an other-than-temporary loss. If neither of these conditions are met, the Company evaluates whether a credit loss exists. The impairment is separated into (a) the amount of the total impairment related to the credit loss and (b) the amount of total impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings and the amount related to all other factors is recognized in other comprehensive income.

The Company also evaluates whether the decline in fair value of an equity security is temporary or other-than-temporary. In determining whether an unrealized loss on an equity security is temporary or other-than-temporary, management considers various factors including the magnitude and duration of the impairment, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to hold the equity security to forecasted recovery.

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## Centrue Financial Corporation

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

#### (Table Amounts In Thousands, Except Share Data)

**Allowance for Loan Losses:** The allowance for loan losses is a reserve established through a provision for probable loan losses charged to expense, which represents management's estimate of probable credit losses inherent in the loan portfolio. Estimating the amount of the allowance for loan losses requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. Loan losses are charged off against the allowance, while recoveries of amounts previously charged off are credited to the allowance. A provision for loan losses is charged to operations based on management's periodic evaluation of the factors previously mentioned, as well as other pertinent factors.

The allowance for loan losses is based on an estimation computed pursuant to the requirements of Financial Accounting Standards Board guidance and rules stating that the analysis of the allowance for loan losses consists of three components:

**Specific Component.** The specific credit allocation component is based on an analysis of individual impaired loans over a fixed-dollar amount where the internal credit rating is at or below a predetermined classification for which the recorded investment in the loan exceeds its fair value. The fair value of the loan is determined based on either the present value of expected future cash flows discounted at the loan's effective interest rate, the market price of the loan, or, if the loan is collateral dependent, the fair value of the underlying collateral less cost of sale. These analyses involve a high degree of judgment in estimating the amount of loss associated with specific loans, including estimating the amount and timing of future cash flows and collateral values;

**Historical Loss Component.** The historical loss component is mathematically based using a modified loss migration analysis that examines historical loan loss experience for each loan category. The loss migration is performed quarterly and loss factors are updated regularly based on actual experience. The general portfolio allocation element of the allowance for loan losses also includes consideration of the amounts necessary for concentrations and changes in portfolio mix and volume. The methodology utilized by management to calculate the historical loss portion of the allowance adequacy analysis is based on historical losses. This historical loss period is based on a weighted twelve-quarter average (3 years); and

**Qualitative Component.** The qualitative component requires qualitative judgment and estimates reserves based on general economic conditions as well as specific economic factors believed to be relevant to the markets in which the Company operates. The process for determining the allowance (which management believes adequately considers all of the potential factors which might possibly result in credit losses) includes subjective elements and, therefore, may be susceptible to significant change.

To the extent actual outcomes differs from management estimates, additional provision for credit losses could be required that could adversely affect the Company's earnings or financial position in future periods.

**Other Real Estate Owned:** Other real estate owned includes properties acquired in partial or total satisfaction of certain loans. Properties are recorded at fair value less costs to sell when acquired, establishing a new cost basis. Any write-downs in the carrying value of a property at the time of acquisition are charged against the allowance for loan losses. Management periodically reviews the carrying value of other real estate owned. Any write-downs of the properties subsequent to acquisition, as well as gains or losses on disposition and income or expense from the operations of other real estate owned, are recognized in operating results in the period they are realized.

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## **Centrue Financial Corporation**

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

**(Table Amounts In Thousands, Except Share Data)**

#### **General**

Centrue Financial Corporation is a bank holding company organized under the laws of the State of Delaware. The Company provides a full range of products and services to individual and corporate customers extending from the far western and southern suburbs of the Chicago metropolitan area across Central Illinois down to the metropolitan St. Louis area. These products and services include demand, time, and savings deposits; lending; mortgage banking, brokerage, asset management, and trust services. Brokerage, asset management, and trust services are provided to our customers on a referral basis to third party providers. The Company is subject to competition from other financial institutions, including banks, thrifts and credit unions, as well as nonfinancial institutions providing financial services. Additionally, the Company and its subsidiary, Centrue Bank, are subject to regulations of certain regulatory agencies and undergo periodic examinations by those regulatory agencies.

#### **Results of Operations**

##### ***Net Income (Loss)***

Net loss for the three months ended September 30, 2012 equaled \$3.3 million or a loss of \$0.63 per common diluted share as compared to a net loss of \$4.7 million or a loss of \$0.87 per common diluted share in the third quarter of 2011. For the first nine months of 2012, the Company had a net loss \$3.7 million or a loss of \$0.87 per common diluted share as compared to a loss of \$10.6 million or a loss of \$2.01 per common diluted share for the same period in 2011.

The results for the third quarter 2012 were adversely impacted by a \$5.8 million provision for loan losses and OREO valuation adjustment of \$0.6 million largely related to asset quality deterioration in the Company's commercial and residential real estate portfolios and declining collateral values. During the third quarter of 2011, the Company recorded a \$2.4 million provision for loan losses and a \$4.5 million OREO valuation adjustment.

##### ***Net Interest Income/ Margin***

The Company's net interest income is affected by changes in the amount and mix of interest-earning assets and interest-bearing liabilities, referred to as "volume change." It is also affected by changes in yields earned on interest-earning assets and rates paid on interest-bearing deposits and other borrowed funds referred to as "rate change." The following table details each category of average amounts outstanding for interest-earning assets and interest-bearing liabilities, average rate earned on all interest-earning assets, average rate paid on all interest-bearing liabilities and the net yield on average interest-earning assets. In addition, the table reflects the changes in net interest income stemming from changes in interest rates and from asset and liability volume, including mix. The change in interest attributable to both rate and volume has been allocated to the changes in the rate and the volume on a pro rata basis.

Fully tax equivalent net interest income for the third quarter 2012 decreased 8.6% to \$6.4 million as compared to \$7.0 million for the same period in 2011. The decrease in net interest income from 2011 was primarily due to average loan volume decline, increased rate competition for loan renewals and higher premium amortization due to increased prepayments and lower coupon income with adjustable resets in the security portfolio. Positively impacting net interest income were lower cost of funds led by a 43 basis points reduction in the yield on time deposits and a 42 basis point yield reduction on money market accounts.

The net interest margin was 3.20% for the third quarter of 2012, representing an increase of 6 basis points from the 3.14% recorded at third quarter of 2011. The Bank's net interest margin was 3.33% for the third quarter of 2012, representing an increase of 2 basis points from 3.31% recorded at both the second quarter of 2012 and the third quarter of 2011. Due largely to the protracted economic downturn, the lost interest income on nonaccrual loans and the Company's interest rate sensitivity, the margin will likely remain under pressure throughout 2012.

Fully tax equivalent net interest income for the nine months ended September 30, 2012 totaled \$18.8 million, representing a decrease of \$2.9 million or 13.4% compared to the \$21.7 million earned during the same period in 2011. The net interest margin was 3.11% for the nine months ended September 30, 2012, representing a decrease of 1 basis point from 3.12% recorded in the same period of 2011. The decrease of net interest income and the net interest margin was driven by the same factors impacting the third quarter.



**Centrue Financial Corporation**

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

(Table Amounts In Thousands, Except Share Data)

**AVERAGE BALANCE SHEET****AND ANALYSIS OF NET INTEREST INCOME**

	For the Three Months Ended September 30,									
	2012				2011				Change Due To:	
	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate	Volume	Rate	Net	
<b>ASSETS</b>										
Interest-earning assets										
Interest-earning deposits	\$2,853	\$ 12	1.78 %	\$2,803	\$ 18	2.59 %	\$3	\$(9 )	\$(6 )	
Securities										
Taxable	206,752	749	1.44	209,010	1,044	1.98	33	(328)	(295 )	
Non-taxable	10,897	159	5.82	17,526	243	5.50	(94 )	10	(84 )	
Total securities (tax equivalent)	217,649	908	1.66	226,536	1,287	2.26	(61 )	(318)	(379 )	
Federal funds sold	5,620	11	0.83	10,675	22	0.80	(4 )	(7 )	(11 )	
Loans										
Commercial	87,564	1,071	4.87	115,924	1,598	5.47	(347)	(180)	(527 )	
Real estate	474,224	5,733	4.81	524,050	6,649	5.03	(586)	(330)	(916 )	
Installment and other	3,167	58	7.20	2,710	70	10.21	20	(32 )	(12 )	
Gross loans (tax equivalent)	564,955	6,862	4.83	642,684	8,317	5.13	(913)	(542)	(1,455)	
Total interest-earnings assets	791,077	7,793	3.92	882,698	9,644	4.34	(975)	(876)	(1,851)	
Noninterest-earning assets										
Cash and cash equivalents	46,668			55,275						
	23,152			24,766						

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Premises and equipment, net									
Other assets	56,925			58,230					
Total nonearning assets	126,745			138,271					
Total assets	\$917,822			\$1,020,969					
<b>LIABILITIES &amp; STOCKHOLDERS' EQUITY</b>									
Interest-bearing liabilities									
NOW accounts	91,951	15	0.07	85,456	50	0.23	12	(47 )	(35 )
Money market accounts	124,014	69	0.22	127,554	205	0.64	28	(164)	(136 )
Savings deposits	102,681	5	0.02	95,764	36	0.15	10	(41 )	(31 )
Time deposits	344,319	884	1.02	450,130	1,646	1.45	(341)	(421)	(762 )
Federal funds purchased and repurchase									
Agreements	16,685	10	0.25	17,732	11	0.24	(1 )	—	(1 )
Advances from FHLB	39,089	192	1.95	49,417	347	2.79	(46 )	(109)	(155 )
Notes payable	31,509	253	3.21	31,944	370	4.61	28	(145)	(117 )
Total interest-bearing liabilities	750,248	1,428	0.76	857,997	2,665	1.23	(310)	(927)	(1,237)
Noninterest-bearing liabilities									
Noninterest-bearing deposits	119,642			112,384					
Other liabilities	15,676			13,643					
Total noninterest-bearing liabilities	135,318			126,027					
Stockholders' equity	32,256			36,945					
Total liabilities and stockholders' equity	\$917,822			\$1,020,969					
Net interest income (tax equivalent)		\$6,365			\$6,979			\$(665)	\$51
									\$(614 )
Net interest income (tax equivalent) to total earning assets			3.20 %			3.14 %			
Interest-bearing liabilities to earning assets			94.84 %			97.20 %			

(1)

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Average balance and average rate on securities classified as available-for-sale is based on historical amortized cost balances.

- (2) Interest income and average rate on non-taxable securities are reflected on a tax equivalent basis based upon a statutory federal income tax rate of 34%.
- (3) Nonaccrual loans are included in the average balances; overdraft loans are excluded in the balances.
- (4) Loan fees are included in the specific loan category.

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**Centrue Financial Corporation**

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

(Table Amounts In Thousands, Except Share Data)

**AVERAGE BALANCE SHEET****AND ANALYSIS OF NET INTEREST INCOME**

	For the Nine Months Ended September 30,									
	2012	2011								
	Average Balance	Interest Income/Expense	Average Rate	Average Balance	Interest Income/Expense	Average Rate	Change Due To:		Net	
							Volume	Rate		
<b>ASSETS</b>										
Interest-earning assets										
Interest-earning deposits	\$2,794	\$56	2.68 %	\$2,922	\$60	2.75 %	\$10	\$(14 )	\$(4 )	
Securities										
Taxable	219,543	2,430	1.48	210,283	3,117	1.98	542	(1,229)	(687 )	
Non-taxable	11,957	524	5.85	20,815	849	5.46	(352 )	27	(325 )	
Total securities (tax equivalent)	231,500	2,954	1.70	231,098	3,966	2.29	190	(1,202)	(1,012)	
Federal funds sold	5,620	43	1.03	7,424	48	0.86	7	(12 )	(5 )	
Loans										
Commercial	90,128	3,433	5.09	133,022	5,392	5.42	(1,497)	(462 )	(1,959)	
Real estate	474,001	17,282	4.87	551,817	20,881	5.06	(2,463)	(1,136)	(3,599)	
Installment and other	2,477	165	8.89	2,552	206	10.77	(18 )	(23 )	(41 )	
Gross loans (tax equivalent)	566,606	20,880	4.92	687,391	26,479	5.15	(3,978)	(1,621)	(5,599)	
Total interest-earnings assets	806,520	23,933	3.96	928,835	30,553	4.40	(3,771)	(2,849)	(6,620)	

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Noninterest-earning assets									
Cash and cash equivalents	52,915			55,630					
Premises and equipment, net	23,313			25,106					
Other assets	57,085			50,308					
Total nonearning assets	133,313			131,044					
Total assets	\$939,833			\$1,059,879					
<b>LIABILITIES &amp; STOCKHOLDERS' EQUITY</b>									
Interest-bearing liabilities									
NOW accounts	88,373	48	0.07	85,188	141	0.22	27	(120 )	(93 )
Money market accounts	119,987	226	0.25	129,658	695	0.72	59	(528 )	(469 )
Savings deposits	102,597	25	0.03	97,706	109	0.15	25	(109 )	(84 )
Time deposits	376,512	3,216	1.14	474,692	5,692	1.60	(870 )	(1,606)	(2,476)
Federal funds purchased and repurchase agreements	16,777	31	0.25	17,707	32	0.24	(2 )	1	(1 )
Advances from FHLB	31,981	568	2.37	51,586	1,114	2.89	(343 )	(203 )	(546 )
Notes payable	31,404	1,037	4.41	31,824	1,103	4.64	18	(84 )	(66 )
Total interest-bearing liabilities	767,631	5,151	0.90	888,361	8,886	1.34	(1,086)	(2,649)	(3,735)
Noninterest-bearing liabilities									
Noninterest-bearing deposits	124,373			118,038					
Other liabilities	15,423			14,361					
Total noninterest-bearing liabilities	139,796			132,399					
Stockholders' equity	32,406			39,119					
Total liabilities and stockholders' equity	\$939,833			\$1,059,879					
Net interest income (tax equivalent)	\$18,782			\$21,667			\$(2,685)	\$(200 )	\$(2,885)

Net interest income (tax equivalent) to total earning assets	3.11 %	3.12 %
Interest-bearing liabilities to earning assets	95.18 %	95.64 %

(1) Average balance and average rate on securities classified as available-for-sale is based on historical amortized cost balances.

(2) Interest income and average rate on non-taxable securities are reflected on a tax equivalent basis based upon a statutory federal income tax rate of 34%.

(3) Nonaccrual loans are included in the average balances; overdraft loans are excluded in the balances.

(4) Loan fees are included in the specific loan category.

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## **Centrue Financial Corporation**

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#### **(Table Amounts In Thousands, Except Share Data)**

#### ***Provision for Loan Losses***

The amount of the provision for loan losses is based on management's evaluations of the loan portfolio, with particular attention directed toward nonperforming, impaired and other potential problem loans. During these evaluations, consideration is also given to such factors as management's evaluation of specific loans, the level and composition of impaired loans, other nonperforming loans, other identified potential problem loans, historical loss experience, results of examinations by regulatory agencies, results of the independent asset quality review process, the market value of collateral, the estimate of discounted cash flows, the strength and availability of guarantees, concentrations of credits and various other factors, including concentration of credit risk in various industries and current economic conditions.

The provision for loan losses for third quarter 2012 was \$5.8 million, compared to \$1.4 million and \$2.4 million for second quarter 2012 and third quarter 2011, respectively. The increase in provision expense from the prior year was warranted based on an increase in the level of nonperforming mainly due to the further deterioration of three credits previously identified that migrated to nonperforming status during the period.

Management continues to diligently monitor the loan portfolio, paying particular attention to borrowers with land development, residential, agricultural and commercial real estate, and commercial development exposures. Many of these relationships continued to show duress due to the ongoing economic downturn being experienced for this industry that existed throughout the third quarter 2012 and is projected to continue through the remainder of the year. Should the economic climate deteriorate from current levels, more borrowers may experience repayment difficulty, and the level of nonperforming loans, charge-offs and delinquencies will rise requiring further increases in the provision for loan losses. Management believes that the allowance for loan losses at September 30, 2012 represented probable incurred credit losses inherent in the loan portfolio.

#### ***Noninterest Income***

Noninterest income consists of a wide variety of fee-based revenues from bank-related service charges on deposits, mortgage revenues and increases in cash surrender value on bank-owned life insurance. The following table summarizes the Company's noninterest income:

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
	2012	2011	2012	2011
Service charges	\$1,128	\$1,232	\$3,217	\$3,483
Mortgage banking income	777	341	1,719	1,050
Electronic banking services	550	552	1,640	1,644
Bank owned life insurance	246	256	734	755
Other Income	404	213	1,520	575
Subtotal recurring noninterest income	3,105	2,594	8,830	7,507
Securities gains	684	—	1,398	379
Net impairment on securities	—	—	—	(499 )
Gain (loss) on sale of Oreo	40	(12 )	465	(60 )
Gain (loss) on sale of other assets	—	(16 )	—	47
Total noninterest income	\$3,829	\$2,566	\$10,693	\$7,374

Noninterest income totaled \$3.8 million for the three months ended September 30, 2012, compared to \$2.6 million for the same period in 2011. Excluding credit impairment charges on CDO securities and gains related to the sale of OREO, securities and other assets from both periods, noninterest income increased by \$0.5 million or 19.2%. This \$0.5 million increase was derived mainly from an increase in mortgage banking.



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For the nine months ended September 30, 2012 noninterest income saw a dramatic improvement to \$10.7 million during the period compared to \$7.4 million the prior year. Excluding the above referenced nonrecurring items, the 2012 period saw an increase of \$1.3 million or 14.8% in noninterest income compared to the same period in 2011. This increase was driven by improvements in mortgage banking revenue and increased rental income on real estate. Partially offsetting these improvements was a decrease in service charges.

***Noninterest Expense***

Noninterest expense is comprised primarily of compensation and employee benefits, occupancy and other operating expense. The following table summarizes the Company's noninterest expense:

	Three Months Ended September 30, 2012		Nine Months Ended September 30, 2011	
Salaries and employee benefits	\$3,697	\$3,505	\$10,981	\$10,598
Occupancy expense, net	681	712	1,965	2,136
Furniture and equipment expense	235	407	902	1,267
Marketing	115	56	284	183
Supplies and printing	67	67	200	208
Telephone	180	229	534	637
Data processing	396	381	1,063	1,120
FDIC Insurance	515	323	1,544	1,997
Loan processing and collection costs	337	495	1,427	1,597
Amortization of intangibles assets	238	250	713	789
Other expenses	1,383	1,499	4,257	4,472
Subtotal recurring noninterest expenses	7,844	7,924	23,870	25,004
OREO valuation adjustments	640	4,473	1,435	5,770
Total noninterest expense	\$8,484	\$12,397	\$25,305	\$30,774

Total noninterest expense for the third quarter of 2012 was \$8.5 million, compared to \$12.4 million recorded during the same period in 2011. Excluding OREO valuation adjustments from both periods, noninterest expense levels decreased by \$0.1 million, or 1.3%. This \$0.1 million decline in expenses was spread over various categories, including net occupancy costs, furniture and equipment, telephone, amortization of intangibles and loan processing and collection costs. Adversely impacting expense levels were increases in salaries and employee benefits, marketing, data processing and FDIC Insurance.

For the nine month period ending September 30, 2012, noninterest expense improved to \$25.3 million during the period compared to \$30.8 million for the prior year. Excluding OREO valuation adjustments for both periods, noninterest expense still improved by \$1.1 million. Most expense categories were down across the board with the exception of salaries and employee benefits and marketing.

### ***Applicable Income Taxes***

Income tax expense for the periods included benefits for tax-exempt income, tax-advantaged investments and general business tax credits offset by the effect of nondeductible expenses. The following table shows the Company's income before income taxes, as well as applicable income taxes and the effective tax rates for the three and nine months ended September 30, 2012 and 2011:

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**(Table Amounts In Thousands, Except Share Data)**

	Three Months Ended		Nine Months Ended	
	September 30, 2012	September 30, 2011	September 30, 2012	September 30, 2011
Income (loss) before income taxes	\$(4,107)	\$(5,354)	\$(4,524)	\$(11,982)
Applicable income taxes	(788 )	(606 )	(788 )	(1,352 )
Effective tax rates	19.2 %	11.3 %	17.4 %	11.3 %

The Company recorded income tax benefits of \$(788) and \$(606) for the three months ended September 30, 2012 and 2011, respectively. Effective tax rates equaled 19.2% and 11.3% respectively, for such periods. The Company recorded tax benefits of \$(788) and \$(1,352) for the nine months ended September 30, 2012 and 2011, respectively. Effective tax rates equaled 17.4% and 11.3% respectively, for such periods.

The tax benefits recorded in the third quarter of 2012 and 2011 and on a year-to-date basis for both years were allocated to the loss from continuing operations due to the following GAAP application: The calculation for the income tax provision or benefit generally does not consider the tax effects of changes in other comprehensive income, or OCI, which is a component of shareholders' equity on the balance sheet. However, an exception is provided in certain circumstances, such as when there is a full valuation allowance against net deferred tax assets, there is a loss from continuing operations and income in other components of the financial statements. In such a case, pre-tax income from other categories, such as changes in OCI, must be considered in determining a tax benefit to be allocated to the loss from continuing operations. Excluding this benefit, no tax benefits were recorded for the quarter and year-to-date periods due to the full deferred tax valuation allowance established as of December 31, 2010.

**Earnings Review by Business Segment**

The Company's internal reporting and planning process focuses on three primary lines of business: Retail, Commercial and Treasury. See Note 7 of the Notes to Unaudited Consolidated Financial Statements for the presentation of the condensed income statement and total assets for each Segment.

The financial information presented was derived from the Company's internal profitability reporting system that is used by management to monitor and manage the financial performance of the Company. This information is based on

internal management accounting policies which have been developed to reflect the underlying economics of the Segments and, to the extent practicable, to portray the Segment as if it operated on a stand-alone basis. Thus, each Segment, in addition to its direct revenues and expenses, assets and liabilities, includes an allocation of shared support function expenses. The Retail, Commercial and Treasury Segments also include funds transfer pricing adjustments to appropriately reflect the cost of funds on loans made and funding credits on deposits generated. Apart from these adjustments, the accounting policies used are similar to those described in Note 1 of the Notes to Consolidated Financial Statements.

Since there are no comprehensive authorities for management accounting equivalent to GAAP, the information presented is not necessarily comparable with similar information from other financial institutions. In addition, methodologies used to measure, assign and allocate certain items may change from time-to-time to reflect, among other things, accounting estimate refinements, changes in risk profiles, changes in customers or product lines and changes in management structure.

***Retail Segment.*** The Retail Segment (“Retail”) provides retail banking services including direct lending, checking, savings, money market and certificate of deposit (“CD”) accounts, safe deposit rental, automated teller machines and other traditional and electronic commerce retail banking services to individual customers through the Bank’s branch locations in Illinois and Missouri. The Retail Segment also provides a variety of mortgage lending products to meet customer needs. The majority of the mortgage loans originated are sold to a third party mortgage services company, which provides private label loan processing and servicing support for both loans sold and loans retained by the Bank.

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Retail generated a net loss of \$1.4 million in the third quarter 2012 as compared to a net loss of \$1.3 million during the same period in 2011. During the nine month period in 2012, the Retail segment had a net loss of \$2.7 million compared to \$2.6 million during the prior year. Retail assets were \$153.6 million at September 30, 2012, \$165.9 million at December 31, 2011 and \$178.8 million as of September 30, 2011. This represented 17.0%, 17.1% and 17.7% of total consolidated assets, respectively.

Earnings results for the third quarter of 2012, when compared to the same period of 2011, were positively impacted by lower expenses and higher mortgage banking revenue which was offset by a decline in net interest margin due to lower loan balances, reduced servicing fees, push-back losses on sold loans and higher provision expense. Year to date results were impacted by the same items listed above.

**Commercial Segment.** The Commercial Segment ("Commercial") provides commercial banking services including lending, business checking and deposits, and other traditional as well as electronic commerce commercial banking services to middle market and small business customers through the Bank's branch locations located in Illinois and Missouri.

Commercial generated a loss of \$1.8 million in the third quarter 2012 as compared to a loss of \$7.0 million during the same period in 2011. During the nine month period in 2012, the Commercial segment had a loss of \$0.1 million compared to a net loss of \$5.4 million during the prior year. Commercial assets were \$459.1 million at September 30, 2012, \$470.1 million at December 31, 2011 and \$496.3 million as of September 30, 2011. This represented 50.7%, 48.6% and 49.2% of total consolidated assets, respectively.

Net income results for the third quarter of 2012, when compared to the same period of 2011, were positively impacted by lower provision for loan losses, higher rental and gain income related to OREO and lower OREO valuation adjustments. Offsetting these positive developments were lower net interest income due to average loan volume decline, the impact of nonaccrual loan interest reversals and higher salary expense. Year to date results were impacted by the same items listed above, with the addition of year to date loan related expenses being significantly higher than the prior year for the same period.

**Treasury Segment.** The Treasury Segment (“Treasury”) is responsible for managing the investment portfolio, acquiring wholesale funding for loan activity and assisting in the management of the Company’s liquidity and interest rate risk.

Treasury generated a loss of \$0.1 million in the third quarter 2012 as compared to a net loss of \$1.9 million, during the same period in 2011. During the nine month period in 2012, the Treasury segment had a net loss of \$0.9 million compared to a loss \$2.6 million during the prior year. Treasury assets were \$205.3 million at September 30, 2012, \$250.7 million at December 31, 2011 and \$267.1 million at September 30, 2011. This represented 22.7%, 25.9% and 26.5% of total consolidated assets, respectively.

Earnings results for the third quarter of 2012, when compared to the same period of 2011, were positively impacted by improved interest expense due to decreased balances on borrowed funds and gains on sale of securities during the period. These positives were partially offset with a significant drop in yield on the security portfolio as higher yielding securities have been sold and replaced with lower yielding instruments with higher premium amortization since September 30, 2011. Year to date results were impacted by the same items listed above along with no impairment charges on the CDO portfolio in 2012.

## **Financial Condition**

### ***General***

Following are highlights of the September 30, 2012 balance sheet when compared to December 31, 2011:

**Securities.** The primary strategic objective of the Company’s securities portfolio is to assist with liquidity and interest rate risk management. In managing the securities portfolio, the Company seeks to minimize credit risk and avoid investments in sophisticated and complex investment products. The Company does not hold any securities containing sub-prime mortgages or any Fannie Mae or Freddie Mac equities.

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Securities at September 30, 2012 totaled \$188.5 million as compared to \$238.0 million recorded at December 31, 2011. The \$49.5 million, or 20.8%, net decrease from year-end 2011 was related to a strategy to enhance the Company's liquidity position.

At September 30, 2012, the Company held five pooled trust preferred collateralized debt obligations ("CDOs") involving three hundred issuers with a total book value of \$7.9 million and fair value of \$7.9 million. The investments in trust-preferred securities receive principal and interest payments from several pools of subordinated capital debentures with each pool containing issuances by banks and bank holding companies or, in a few instances, capital notes from insurance companies. The Company did not record an other-than-temporary impairment charge during the quarter, which marks the fifth consecutive quarter without an impairment charge. Should the economic climate deteriorate from current levels, the underlying credits may experience repayment difficulty, and the level of deferrals and defaults could increase requiring additional impairment charges in future quarters.

**Loans.** Total loans equaled \$561.5 million, representing decreases of \$20.9 million, or 3.6% and \$59.0 million or 9.5%, from December 31, 2011 and September 30, 2011, respectively. The net decrease from year-end 2011 was related to a combination of normal attrition, pay-downs, loan charge-offs, transfers to OREO and strategic initiatives to reduce balance sheet risk. Due to economic conditions, we have also experienced a decrease in loan demand as many borrowers continue to reduce their debt.

**Deposits.** Total deposits equaled \$782.6 million at September 30, 2012 compared to \$848.6 million recorded at December 31, 2011 and \$862.1 million on record at September 30, 2011. The September 30, 2012 deposit balance represents a decrease of \$66.0 million or 7.8% from December 31, 2011 and \$79.5 million or 9.2% from September 30, 2011. The net decrease from year-end 2011 was largely related to strategic initiatives to reduce higher costing time deposits and collateralized local public agency deposits. Wholesale funding decreased \$27.0 million, as \$34.1 million in brokered deposits have matured since year-end 2011 and were not replaced. Partially offsetting this decrease was an increase in FHLB advances.

#### *Nonperforming Assets*

The Company's financial statements are prepared on the accrual basis of accounting, including the recognition of interest income on its loan portfolio, unless a loan is placed on nonaccrual status. Loans are placed on nonaccrual status when there are serious doubts regarding the collectibility of all principal and interest due under the terms of the loans. If a loan is placed on nonaccrual status, the loan does not generate current period income for the Company and any amounts received are generally applied first to principal and then to interest. It is the policy of the Company not to renegotiate the terms of a loan because of a delinquent status. Rather, a loan is generally transferred to nonaccrual status if it is not in the process of collection and is delinquent in payment of either principal or interest beyond 90 days.

The classification of a loan as nonaccrual does not necessarily indicate that the principal is uncollectible, in whole or in part. The Bank makes a determination as to collectability on a case-by-case basis and considers both the adequacy of the collateral and the other resources of the borrower in determining the steps to be taken to collect nonaccrual loans. The final determination as to the steps taken is made based upon the specific facts of each situation. Alternatives that are typically considered to collect nonaccrual loans are foreclosure, collection under guarantees, loan restructuring, or judicial collection actions.

Each of the Company's commercial loans is assigned a rating based upon an internally developed grading system. A separate credit administration department also reviews grade assignments on a quarterly basis. Management continuously monitors nonperforming, impaired, and past due loans in an effort to prevent further deterioration of these loans. The Company has an independent loan review function which is separate from the lending function and is responsible for the review of new and existing loans.



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The following table summarizes nonperforming assets and loans past due 90 days or more for the previous five quarters:

	2012			2011		
	Sep 30,	Jun 30,	Mar 31,	Dec 31,	Sep 30,	
Nonaccrual loans	\$42,855	\$35,475	\$37,538	\$38,688	\$40,665	
Troubled debt restructurings	3,884	4,348	6,366	7,147	7,317	
Loans 90 days past due and still accruing interest	—	—	—	—	—	
Total nonperforming loans	46,739	39,823	43,904	45,835	47,982	
Other real estate owned	28,601	27,890	33,501	29,667	32,912	
Total nonperforming assets	\$75,340	\$67,713	\$77,405	\$75,502	\$80,894	
End of period loans	561,476	567,908	563,732	582,395	620,450	
Nonperforming loans to total end of period loans	8.32	% 7.01	% 7.79	% 7.87	% 7.73	%
Nonperforming assets to total end of period loans	13.42	% 11.92	% 13.73	% 12.96	% 13.04	%
Nonperforming assets to total end of period assets	8.33	% 7.31	% 8.05	% 7.80	% 8.02	%

Total nonperforming assets were \$75.3 million, or 8.3% of total assets, at September 30, 2012. This included \$3.9 million in troubled debt restructurings, \$28.6 million of OREO and \$42.8 million of nonaccrual loans. The majority of the OREO is comprised of eleven parcels (land development and commercial real estate) which account for 70.6% of the balance. The Company updates these appraisals quarterly to ensure that they are properly carried at their fair market value. Approximately 32.3% of total nonaccrual loans at September 30, 2012 were concentrated in land development and construction credits. Additionally, 72.0% of total nonaccrual loans represented loans to 10 borrowers.

The level of nonperforming loans (nonaccrual, 90 days past due, and troubled debt restructurings) at September 30, 2012 increased \$0.9 million, or 2.0%, from December 31, 2011 levels and decreased \$1.3 million, or 2.7%, from the \$48.0 million that existed at September 30, 2011. The increase in nonperforming loans was mainly due to the further deterioration of two credits previously identified as impaired. The level of nonperforming loans to total end of period loans was 8.3% at September 30, 2012, as compared to 7.9% at December 31, 2011 and 7.7% at September 30, 2011. The coverage ratio (allowance to nonperforming loans) was reported at 45.1% as of September 30, 2012 as compared to 46.3% as of December 31, 2011.

***Other Potential Problem Loans***

The Company has other potential problem loans that are currently performing, but where some concerns exist regarding the nature of the borrowers' projects in our current economic environment. Through the end of the third quarter of 2012, \$12.8 million of loans had been identified by management that are currently performing but due to the economic environment facing these borrowers were classified by management as impaired. Impaired loans that are performing account for 21.6% of the loans deemed impaired as of the September 30, 2012, whereas, 38.99% of impaired loans were performing at December 31, 2011. Excluding nonperforming loans and loans that management has classified as impaired, there are other potential problem loans that totaled \$8.4 million at September 30, 2012 as compared to \$12.4 million at December 31, 2011. The classification of these loans, however, does not imply that management expects losses on each of these loans, but believes that a higher level of scrutiny and closer monitoring is prudent under the circumstances. Such classifications relate to specific concerns for each individual borrower and do not relate to any concentration risk common to all loans in this group.

***Allowance for Loan Losses***

At September 30, 2012, the allowance for loan losses was \$21.1 million, or 3.8% of total loans, as compared to \$21.2 million, or 3.7%, at December 31, 2011 and \$23.3 million, or 3.8%, of total loans at September 30, 2011.

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The Company recorded a provision of \$5.8 million to the allowance for loan losses in the third quarter 2012 which represents an increase from the same quarter in 2011. The increase in provision expense from the prior year was warranted based on the level of previously identified credits that migrated to nonperforming status.

Net loan charge-offs for the third quarter of 2012 were \$2.9 million, or 0.5% of average loans, compared with \$3.6 million, or 0.6% of average loans, for the fourth quarter of 2011 and \$3.4 million, or 0.5% of average loans, for the third quarter of 2011. Loan charge-offs during the third quarter of 2012 were largely influenced by the credit performance of the Company's commercial and residential real estate portfolios. These charge-offs reflect management's continuing efforts to align the carrying value of these assets with the value of underlying collateral based upon more aggressive disposition strategies and recognizing falling property values. Because these loans are collateralized by real estate, losses occur more frequently when property values are declining and borrowers are losing equity in the underlying collateral. Management believes we are recognizing losses in our portfolio through provisions and charge-offs as credit developments warrant.

#### *Liquidity*

Due to continued uncertainty in the financial markets, liquidity strategies are conservatively postured in an effort to mitigate adverse pressure on liquidity levels. The Company continues to remain in a liquid position by reducing reliance on wholesale funding sources and a reduction in the loan portfolio, net of gross charge-offs and transfers to OREO. Total deposits equaled \$782.6 million, representing decreases of \$66.0 million, or 7.8%, from December 31, 2011 and \$79.5 million, or 9.2%, from September 30, 2011. During the quarter, in-market deposits increased \$14.6 million or 2.0%, primarily as the result of an increase in public funds and money market funds. Wholesale funding (brokered deposits and FHLB advances) decreased \$27.0 million or 29.1%, as \$34.1 million in brokered deposits have matured since year-end 2011 and were not replaced. Partially offsetting this decrease was an increase in FHLB advances.

The Company manages its liquidity position with the objective of maintaining sufficient funds to respond to the needs of depositors and borrowers and to take advantage of earnings enhancement opportunities. In addition to the normal inflow of funds from core-deposit growth together with repayments and maturities of loans and investments, the Company utilizes other short-term funding sources such as securities sold under agreements to repurchase, overnight federal funds purchased from correspondent banks and the acceptance of short-term deposits from public entities.

The Company can borrow from the Federal Reserve Bank of Chicago's discount window to meet short-term liquidity requirements. These borrowings are secured by commercial loans. At September 30, 2012, the Company maintained borrowing capacity of \$16.7 million from the Federal Reserve Bank discount window.

The Company is also a member of the Federal Home Loan Bank-Chicago (FHLB) and as such has advances from FHLB secured generally by residential mortgage loans with a remaining borrowing capacity of \$33.4 million as of September 30, 2012.

The Company monitors and manages its liquidity position on several bases, which vary depending upon the time period. As the time period is expanded, other data is factored in, including estimated loan funding requirements, estimated loan payoffs, investment portfolio maturities or calls and anticipated depository buildups or runoffs.

The Company classifies all of its securities as available-for-sale, thereby maintaining significant liquidity. The Company's liquidity position is further enhanced by structuring its loan portfolio interest payments as monthly and by the significant representation of retail credit and residential mortgage loans in the Company's loan portfolio, resulting in a steady stream of loan repayments. In managing its investment portfolio, the Company provides for staggered maturities so that cash flows are provided as such investments mature.

The Company's cash flows are comprised of three classifications: cash flows from operating activities, cash flows from investing activities and cash flows from financing activities. Cash flows provided by operating activities and investing activities offset by those used in financing activities, resulted in a net increase in cash and cash equivalents of \$9.7 million from December 31, 2011 to September 30, 2012.

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During the first nine months of 2012, the Company experienced net cash inflows of \$7.8 million in operating activities and \$62.4 million in investing activities. In contrast, net cash outflows of \$60.5 million were used in financing activities largely due to decreases in deposits.

At December 31, 2011, the parent Company had \$2.0 million in cash and cash equivalents. During the first nine months of 2012, the parent Company experienced net cash outflow of \$0.7 million leaving \$1.3 million in cash and cash equivalents available at September 30, 2012. The parent Company's primary use of cash is for quarterly debt payments. These payments are estimated to be \$0.3 million for the remainder of the year and are more fully described in Notes 8 & 13 of the Unaudited Consolidated Financial Statements of the Company.

**Contractual Obligations, Commitments, Contingencies, and Off-Balance Sheet Financial Instruments**

The Company has entered into contractual obligations and commitments and off-balance sheet financial instruments. The following tables summarize the Company's contractual cash obligations and other commitments and off balance sheet instruments as of September 30, 2012:

	Payments Due by Period				Total
	Within 1 Year	1-3 Years	4-5 Years	After 5 Years	
Contractual Obligations					
Short-term debt	\$—	\$250	\$—	\$—	\$250
Long-term debt	95	10,000	—	—	10,095
Certificates of deposit	237,772	75,029	24,983	—	337,784
Operating leases	251	504	504	252	1,511
Series B mandatory redeemable preferred stock	—	268	—	—	268
Subordinated debentures	—	—	—	20,620	20,620
FHLB advances	10,000	15,057	5,000	—	30,057
Total contractual cash obligations	\$248,118	\$101,108	\$30,487	\$20,872	\$400,585

	Amount of Commitment Expiration Per Period				
	Within 1 Year	1-3 Years	4-5 Years	After 5 Years	Total
<b>Off-Balance Sheet Financial Instruments</b>					
Lines of credit	\$80,698	\$3,630	\$3,660	\$21,517	\$109,505
Standby letters of credit	1,076	1,076	—	—	2,152
Total contractual cash obligations	\$81,774	\$4,706	\$3,660	\$21,517	\$111,657

## Capital Resources

### *Stockholders' Equity*

Stockholders' equity at September 30, 2012 was \$28.7 million, a decrease of \$3.9 million, or 12.0%, from \$32.6 million at December 31, 2011. The change in stockholders' equity was largely related to the operating loss incurred during 2012.

### *Stock Repurchase*

Restrictions set forth in the U.S. Treasury CPP program prohibit the Company from repurchasing its common stock until the CPP proceeds are paid back.

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**(Table Amounts In Thousands, Except Share Data)***Capital Measurements*

As reflected in the following table, the Bank was considered "well-capitalized" under regulatory defined capital ratios as of September 30, 2012, however the Company was "less than adequately-capitalized" due to the Tier 1 leverage ratio which was 3.4% being below the threshold for "adequately-capitalized" of 4%. See Note 13 to the Unaudited Consolidated Financial Statements for additional disclosure on the capital threshold levels:

	Centrue Financial		Centrue Bank		Well- Capitalized	
	Sep 30, 2012	Dec 31, 2011	Sep 30, 2012	Dec 31, 2011	Thresholds	
Carrying amounts (\$ millions):						
Total risk-based capital	\$54.2	\$61.2	\$66.4	\$68.6		
Tier 1 risk-based capital	\$30.9	\$37.2	\$58.3	\$60.1		
Tangible common equity	\$(9.0)	\$(5.9)	\$61.4	\$62.0		
Capital ratios:						
Total risk-based capital	8.4 %	9.0 %	10.5 %	10.3 %	10.0	%
Tier 1 risk-based capital	4.8 %	5.5 %	9.2 %	9.0 %	6.0	%
Tier 1 leverage ratio	3.4 %	3.7 %	6.4 %	6.1 %	5.0	%

Total capital and some corresponding capital ratios decreased during 2012 for the Company due to a net operating loss and a continued reduction in Tier II capital caused by a sub-debt phase-out provision. The Bank had a slight increase in capital ratios from a reduction in risk-weighted assets in several areas.

The Company is in compliance with all the requirements specified in the agreement with the FRB and IDFPFR except for the Capital Plan. Management continues to aggressively pursue capital raising initiatives to comply with this provision; however, until a more definitive capital raise initiative is developed, the Company will continue to be held in noncompliance with this provision.

The Company's Series C Preferred Stock was issued January 9, 2009, as part of the Troubled Asset Relief Program ("TARP") Capital Purchase Program. At September 30, 2012 this preferred stock totaled \$31.9 million, with \$5.9 million of deferred dividends. The U.S. Treasury has notified the Company that the preferred securities and the warrant may be placed into pooled "Dutch Auctions" after October 9, 2012.

The Company is reviewing proposed rules for Basel III that the FRB released and will continue to monitor during the commenting process before final rules are released.

### **Subsequent Events**

Under the recently passed Jumpstart Our Business Startups (JOBS) Act, banks and bank holding companies may now go private and deregister their shares from the Securities and Exchange Commission (SEC) if they have less than 1,200 shareholders. This is done by filing Form 15 with the SEC, which becomes effective ninety days after the filing date. The Company filed Form 15 in order to reduce the costs of remaining an SEC registrant. It should be noted that the Company's stock will still be traded on the OTCQB Marketplace under the symbol "TRUE.PK" following the deregistration.

### **Recent Accounting Developments**

See Note 14 to the Unaudited Consolidated Financial Statements for information concerning recent accounting developments.



## Centrue Financial Corporation

### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

(Table Amounts In Thousands, Except Share Data)

#### Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Act of 1934 as amended. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and is including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies, and expectations of the Company, are generally identified by the use of words such as "believe," "expect," "intend," "anticipate," "estimate," "project," "planned" or "potential" or similar expressions.

In connection with the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, the Company is hereby identifying important factors that could affect the Company's financial performance and could cause the Company's actual results for future periods to differ materially from any opinions or statements expressed with respect to future periods in any forward-looking statements.

Among the factors that could have an impact on the Company's ability to achieve operating results and the growth plan goals are as follows:

- management's ability to reduce and effectively manage interest rate risk and the impact of interest rates in general on the volatility of the Company's net interest income;
- fluctuations in the value of the Company's investment securities;
- the Company's ability to ultimately collect on any downgraded loan relationships;
- the Company's ability to respond and adapt to economic conditions in our geographic market;
- the Company's ability to adapt successfully to technological changes to compete effectively in the marketplace;
- credit risks and risks from concentrations (by geographic area and by industry) within the Company's loan portfolio and individual large loans;
- volatility of rate sensitive deposits;
- operational risks, including data processing system failures or fraud;
- asset/liability matching risks and liquidity risks;
- the ability to successfully acquire low cost deposits or funding;
- the ability to successfully execute strategies to increase noninterest income;
- the ability to successfully grow non-commercial real estate loans;

- the ability of the Company to continue to realize cost savings and revenue generation opportunities in connection with the synergies of centralizing operations;
- the ability to adopt and implement new regulatory requirements as dictated by the SEC, FASB or other rule-making bodies which govern our industry;
- changes in the general economic or industry conditions, nationally or in the communities in which the Company conducts business;
- the Company's ability to raise additional capital, if available, to sustain growth or operating results;
- the Company's ability to dispose of other real estate owned ("OREO") at reasonable values in a market that is very volatile.

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**Centrue Financial Corporation**

## Item 3. Quantitative and Qualitative Disclosures About Market Risk

(Table Amounts In Thousands, Except Share Data)

**Item 3. Quantitative and Qualitative Disclosures About Market Risk****Interest Rate Sensitivity Management**

The Company performs a net interest income analysis as part of its asset/liability management practices. The net interest income analysis measures the change in net interest income in the event of hypothetical changes in interest rates. This analysis assesses the risk of changes in net interest income in the event of a sudden and sustained 50, 100, 200 and 300 basis point increase in market interest rates or a 50 basis point decrease in market rates. The interest rates scenarios are used for analytical purposes and do not necessarily represent management's view of future market movements. The tables below present the Company's projected changes in net interest income for the various rate shock levels at September 30, 2012 and December 31, 2011, respectively:

	Change in Net Interest Income Over One Year Horizon			
	September 30, 2012		December 31, 2011	
	Change		Change	
	\$	%	\$	%
+ 300 bp	\$182	0.78 %	\$1,442	5.45 %
+ 200 bp	165	0.71	743	2.81
+ 100 bp	111	0.48	174	0.66
+ 50 bp	90	0.39	107	0.41
Base	—	—	—	—
- 50 bp	(181)	(0.78)	(299 )	(1.13)

As shown above, the effect of an immediate 200 basis point increase in interest rates as of September 30, 2012 would increase the Company's net interest income by \$0.2 million or 0.7%. The effect of an immediate 50 basis point decrease in rates would decrease the Company's net interest income by \$0.2 million or 0.8%.

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**Centrue Financial Corporation**

**Item 4. Controls and Procedures**

**Item 4. Controls and Procedures**

As of the end of the period covered by this report, the Company carried out an evaluation under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended). Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective in timely alerting them to material information relating to the Company required to be included in the Company's periodic filings with the Securities and Exchange Commission. It should be noted that in designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. The Company has designed its disclosure controls and procedures to reach a level of reasonable assurance of achieving the desired control objectives and, based on the evaluation described above, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective at reaching that level of reasonable assurance.

There was no change in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) during the Company's most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II - OTHER INFORMATION**

### **Item 1. Legal Proceedings**

In the normal course of business the Company may be involved in various legal proceedings from time to time. The Company does not believe it is currently involved in any claim or action the ultimate disposition of which would have a material adverse effect on the Company's financial statements.

### **Item 1A. Risk Factors**

The Company did not experience any material changes in the Risk Factors during the Company's most recently completed fiscal quarter. For specific information about the risks facing the Company refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

### **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.

### **Item 3. Defaults Upon Senior Securities**

As previously disclosed, in the third quarter of 2009, the Company elected to defer regularly scheduled quarterly interest payments on its outstanding junior subordinated debentures relating to its trust preferred securities and to suspend quarterly cash dividend payments on its Series A convertible preferred stock, Series B mandatory redeemable preferred stock and Series C fixed rate, cumulative perpetual preferred stock issued to the U.S. Treasury. Therefore, the Company is currently in arrears with the dividend payments on the preferred stock and interest payments on the subordinated debentures, as permitted by the related documentation. As of September 30, 2012, the amount of the arrearages on the various instruments was as follows: Junior subordinated debentures: \$3.4 million; Series A convertible preferred stock: \$0.7 million; Series B mandatory redeemable preferred stock: \$0.05 million; and Series C fixed rate, cumulative perpetual preferred stock: \$5.9 million.

**Item 4. Mine Safety Disclosures**

None.

**Item 5. Other Information**

None.

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**Item 6. Exhibits**

Exhibits:

- 31.1 Certification of Kurt R. Stevenson, President and Principal Executive Officer, required by Rule 13a – 14(a).
  - 31.2 Certification of Daniel R. Kadolph, Executive Vice President and Principal Financial and Accounting Officer required by Rule 13a – 14(a).
  - 32.1<sup>(1)</sup> Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, from the Company’s President and Principal Executive Officer.
  - 32.2<sup>(1)</sup> Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, from the Company’s Executive Vice President and Principal Financial and Accounting Officer
- 101<sup>(2)</sup> Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Income, (iii) the Condensed Consolidated Statements of Changes in Equity, (iv) the Condensed Consolidated Statements of Cash Flows, and (v) the Notes to Condensed Consolidated Financial Statements tagged as blocks of text.

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This certification is not “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or

<sup>(1)</sup>incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.

<sup>(2)</sup>As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.



**SIGNATURES**

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

CENTRUE FINANCIAL CORPORATION

Date: November 13, 2012 By: /s/ Kurt R. Stevenson  
Kurt R. Stevenson  
President and Principal Executive Officer

Date: November 13, 2012 By: /s/ Daniel R. Kadolph  
Daniel R. Kadolph  
Executive Vice President and Principal  
Financial and Accounting Officer

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