

Stock Yards Bancorp, Inc.
Form 10-Q
August 05, 2016
Table Of Contents

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 June 30, 2016

OR

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

For the transition period from _____ to _____.

Commission file number 1-13661

STOCK YARDS BANCORP, INC.

(Exact name of registrant as specified in its charter)

Kentucky
(State or other jurisdiction of incorporation or organization)

61-1137529
(I.R.S. Employer Identification No.)

1040 East Main Street, Louisville, Kentucky 40206

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

(Address of principal executive offices including zip code)

(502) 582-2571

(Registrant's telephone number, including area code)

Not Applicable

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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 (Do not check if a smaller reporting company)

Smaller reporting company

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

Yes No ___

The number of shares of the registrant's Common Stock, no par value, outstanding as of July 28, 2016, was

22,513,507.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Index

<u>Item</u>	<u>Page</u>
PART I – FINANCIAL INFORMATION	
Item 1.	Financial Statements
The following consolidated financial statements of Stock Yards Bancorp, Inc. and Subsidiary are submitted herewith:	
	<u>Consolidated Balance Sheets June 30, 2016 (Unaudited) and December 31, 2015</u> 3
	<u>Consolidated Statements of Income (Unaudited) for the three and six months ended June 30, 2016 and 2015</u> 4
	<u>Consolidated Statements of Comprehensive Income (Unaudited) for the three and six months ended June 30, 2016 and 2015</u> 5
	<u>Consolidated Statements of Changes in Stockholders' Equity (Unaudited) for the six months ended June 30, 2016 and 2015</u> 6
	<u>Consolidated Statements of Cash Flows (Unaudited) for the six months ended June 30, 2016 and 2015</u> 7
	<u>Notes to Consolidated Financial Statements (Unaudited)</u> 8
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 40
Item 3.	<u>Quantitative and Qualitative Disclosures about Market Risk</u> 58
Item 4.	<u>Controls and Procedures</u> 58
PART II – OTHER INFORMATION	
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u> 59
Item 6.	<u>Exhibits</u> 59

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

PART I – FINANCIAL INFORMATION

Glossary of Acronyms and Terms

The following listing provides a comprehensive reference of common acronyms and terms used throughout the document:

ASU	Accounting Standards Update
Bancorp	Stock Yards Bancorp, Inc.
Bank	Stock Yards Bank & Trust Company
BOLI	Bank Owned Life Insurance
BP	Basis Point = 1/100 th of one percent
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act
FASB	Financial Accounting Standards Board
FDIC	Federal Deposit Insurance Corporation
FHA	Federal Housing Administration
FHLB	Federal Home Loan Bank
FHLMC	Federal Home Loan Mortgage Corporation
FNMA	Federal National Mortgage Association
GNMA	Government National Mortgage Association
IM&T	Investment Management and Trust
LIBOR	London Interbank Offered Rate

MSR	Mortgage Servicing Right
OAEM	Other Assets Especially Mentioned
OREO	Other Real Estate Owned
PSU	Performance Stock Unit
RSU	Restricted Stock Unit
SAR	Stock Appreciation Right
SEC	Securities and Exchange Commission
TDR	Troubled Debt Restructuring
US GAAP	United States Generally Accepted Accounting Principles
VA	U.S. Department of Veterans Affairs

Table Of ContentsItem 1. Financial Statements**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Consolidated Balance Sheets

June 30, 2016 and December 31, 2015

(In thousands, except share data)

	June 30, 2016 (Unaudited)	December 31, 2015
Assets		
Cash and due from banks	\$ 40,618	\$ 35,895
Federal funds sold	9,616	67,938
Cash and cash equivalents	50,234	103,833
Mortgage loans held for sale	6,405	6,800
Securities available-for-sale (amortized cost of \$557,735 in 2016 and \$564,391 in 2015)	567,307	565,876
Federal Home Loan Bank stock and other securities	6,347	6,347
Loans	2,175,551	2,033,007
Less allowance for loan losses	23,141	22,441
Net loans	2,152,410	2,010,566
Premises and equipment, net	42,718	39,557
Bank owned life insurance	31,437	30,996
Accrued interest receivable	6,799	6,610
Other assets	45,862	46,216
Total assets	\$ 2,909,519	\$ 2,816,801
Liabilities and Stockholders' Equity		
Deposits:		
Non-interest bearing	\$ 637,812	\$ 583,768
Interest bearing	1,712,136	1,787,934
Total deposits	2,349,948	2,371,702
Securities sold under agreements to repurchase	57,437	64,526
Federal funds purchased and other short-term borrowing	114,154	22,477
Federal Home Loan Bank advances	43,002	43,468
Accrued interest payable	132	127
Other liabilities	39,795	27,982
Total liabilities	2,604,468	2,530,282
Stockholders' equity:		
Preferred stock, no par value. Authorized 1,000,000 shares; no shares issued or outstanding	—	—
Common stock, no par value. Authorized 40,000,000 shares; issued and outstanding 22,510,205 and 14,919,351 shares in 2016 and 2015, respectively	35,894	10,616
Additional paid-in capital	21,962	44,180
Retained earnings	241,745	231,091
Accumulated other comprehensive income	5,450	632
Total stockholders' equity	305,051	286,519

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Total liabilities and stockholders' equity	\$2,909,519	\$2,816,801
--------------------------------------------	-------------	-------------

See accompanying notes to unaudited consolidated financial statements.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Consolidated Statements of Income (Unaudited)

For the three and six months ended June 30, 2016 and 2015

(In thousands, except per share data)

	For three months ended June 30,		For six months ended June 30,	
	2016	2015	2016	2015
Interest income:				
Loans	\$22,563	\$20,612	\$44,556	\$41,027
Federal funds sold	111	51	300	119
Mortgage loans held for sale	59	74	119	113
Securities – taxable	2,123	1,969	4,278	4,003
Securities – tax-exempt	306	294	609	585
Total interest income	25,162	23,000	49,862	45,847
Interest expense:				
Deposits	979	938	1,975	1,911
Federal funds purchased and other short-term borrowing	23	5	38	12
Securities sold under agreements to repurchase	29	32	62	69
Federal Home Loan Bank advances	181	224	368	440
Total interest expense	1,212	1,199	2,443	2,432
Net interest income	23,950	21,801	47,419	43,415
Provision for loan losses	750	—	1,250	—
Net interest income after provision for loan losses	23,200	21,801	46,169	43,415
Non-interest income:				
Investment management and trust services	4,807	4,651	9,419	9,203
Service charges on deposit accounts	2,262	2,199	4,408	4,279
Bankcard transaction revenue	1,433	1,246	2,743	2,368
Mortgage banking revenue	1,030	913	1,824	1,741
Brokerage commissions and fees	538	499	981	960
Bank owned life insurance income	220	226	441	448
Other	488	485	1,044	893
Total non-interest income	10,778	10,219	20,860	19,892
Non-interest expenses:				
Salaries and employee benefits	11,971	11,383	24,166	22,483
Net occupancy expense	1,546	1,450	3,070	2,919
Data processing expense	1,881	1,756	3,425	3,210
Furniture and equipment expense	291	260	576	507
FDIC insurance expense	351	317	679	614
Amortization of investment in tax credit partnerships	1,016	159	2,031	317
Other	3,137	3,542	5,786	6,596
Total non-interest expenses	20,193	18,867	39,733	36,646
Income before income taxes	13,785	13,153	27,296	26,661
Income tax expense	3,676	4,151	7,352	8,404
Net income	10,109	9,002	19,944	18,257

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Net income per share:

Basic	\$0.45	\$0.41	\$0.89	\$0.83
Diluted	\$0.45	\$0.40	\$0.88	\$0.82
Average common shares:				
Basic	22,336	22,065	22,295	22,018
Diluted	22,704	22,404	22,658	22,353

See accompanying notes to unaudited consolidated financial statements.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Consolidated Statements of Comprehensive Income (Unaudited)

For the three and six months ended June 30, 2016 and 2015

(In thousands)

	Three months ended		Six months ended	
	June 30,		June 30,	
	2016	2015	2016	2015
Net income	\$10,109	\$9,002	\$19,944	\$18,257
Other comprehensive income, net of tax:				
Unrealized gains (losses) on securities available for sale:				
Unrealized gains (losses) arising during the period (net of tax of \$863, (\$1,417), \$2,831 and (\$405), respectively)	1,603	(2,631)	5,256	(751)
Unrealized losses on hedging instruments:				
Unrealized losses arising during the period (net of tax of (\$53), (\$1), (\$236) and (\$11), respectively)	(99)	(2)	(438)	(21)
Other comprehensive income (loss), net of tax	1,504	(2,633)	4,818	(772)
Comprehensive income	\$11,613	\$6,369	\$24,762	\$17,485

See accompanying notes to unaudited consolidated financial statements.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Consolidated Statements of Changes in Stockholders' Equity (Unaudited)

For the six months ended June 30, 2016 and 2015

(In thousands, except per share data)

	Common stock		Additional	Retained	Accumulated	
	Number	Amount	paid-in	earnings	comprehensive	
	of		capital		income (loss)	Total
	shares					
Balance December 31, 2014	14,745	\$ 10,035	\$ 38,191	\$ 209,584	\$ 2,085	\$ 259,895
Net income	—	—	—	18,257	—	18,257
Other comprehensive loss, net of tax	—	—	—	—	(772)	(772)
Stock compensation expense	—	—	995	—	—	995
Stock issued for share-based awards, net of withholdings to satisfy employee tax obligations upon award	127	422	2,608	(1,507)	—	1,523
Cash dividends, \$0.31 per share	—	—	—	(6,952)	—	(6,952)
Shares repurchased or cancelled	(20)	(67)	(581)	84	—	(564)
Balance June 30, 2015	14,852	\$ 10,390	\$ 41,213	\$ 219,466	\$ 1,313	\$ 272,382
Balance December 31, 2015	14,919	\$ 10,616	\$ 44,180	\$ 231,091	\$ 632	\$ 286,519
Net income	—	—	—	19,944	—	19,944
Other comprehensive income, net of tax	—	—	—	—	4,818	4,818
Stock compensation expense	—	—	1,073	—	—	1,073
Stock issued for share-based awards, net of withholdings to satisfy employee tax obligations upon award	103	342	1,829	(1,689)	—	482
3 for 2 stock split	7,494	24,956	(24,956)	—	—	—
Cash dividends, \$0.35 per share	—	—	—	(7,785)	—	(7,785)

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Shares repurchased or cancelled	(6)	(20)	(164)	184	—	—
Balance June 30, 2016	22,510	\$35,894	\$21,962	\$241,745	\$5,450	\$305,051

See accompanying notes to unaudited consolidated financial statements.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Consolidated Statements of Cash Flows (Unaudited)

For the six months ended June 30, 2016 and 2015

(In thousands)

	2016	2015
Operating activities:		
Net income	\$ 19,944	\$ 18,257
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,250	—
Depreciation, amortization and accretion, net	5,292	3,374
Deferred income tax expense	447	1,171
Gain on sales of mortgage loans held for sale	(1,103)	(1,133)
Origination of mortgage loans held for sale	(57,433)	(63,461)
Proceeds from sale of mortgage loans held for sale	58,931	60,104
Bank owned life insurance income	(441)	(448)
Gain on the disposal of premises and equipment	-	(5)
Loss (gain) on the sale of other real estate	(443)	165
Stock compensation expense	1,073	995
Excess tax benefits from share-based compensation arrangements	(520)	(293)
Decrease (increase) in accrued interest receivable and other assets	(5,246)	386
Increase (decrease) in accrued interest payable and other liabilities	12,321	(4,303)
Net cash provided by operating activities	34,072	14,809
Investing activities:		
Purchases of securities available for sale	(227,714)	(92,730)
Proceeds from sale of securities available for sale	—	5,934
Proceeds from maturities of securities available for sale	232,825	184,878
Net increase in loans	(144,605)	(32,596)
Purchases of premises and equipment	(4,660)	(2,615)
Proceeds from sale of foreclosed assets	1,401	1,820
Net cash provided by (used in) investing activities	(142,753)	64,691
Financing activities:		
Net decrease in deposits	(21,754)	(51,862)
Net increase (decrease) in securities sold under agreements to repurchase and federal funds purchased	84,588	(39,241)
Proceeds from Federal Home Loan Bank advances	160,000	63,200
Repayments of Federal Home Loan Bank advances	(160,466)	(61,177)
Issuance of common stock for options and performance stock units	1,045	1,566
Excess tax benefits from share-based compensation arrangements	520	293
Common stock repurchases	(1,083)	(900)
Cash dividends paid	(7,768)	(6,944)
Net cash provided by (used in) financing activities	55,082	(95,065)
Net decrease in cash and cash equivalents	(53,599)	(15,565)
Cash and cash equivalents at beginning of period	103,833	74,241
Cash and cash equivalents at end of period	\$ 50,234	\$ 58,676
Supplemental cash flow information:		

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Income tax payments	\$5,490	\$6,774
Cash paid for interest	2,438	2,438
Supplemental non-cash activity:		
Transfers from loans to other real estate owned	\$1,511	\$232

See accompanying notes to unaudited consolidated financial statements.

7

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Unaudited)

(1) Summary of Significant Accounting Policies

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all information and footnotes required by U.S. generally accepted accounting principles (US GAAP) for complete financial statements. The consolidated unaudited financial statements of Stock Yards Bancorp, Inc. (“Bancorp”) and its subsidiary reflect all adjustments (consisting only of adjustments of a normal recurring nature) which are, in the opinion of management, necessary for a fair presentation of financial condition and results of operations for the interim periods.

The unaudited consolidated financial statements include the accounts of Stock Yards Bancorp, Inc. and its wholly-owned subsidiary, Stock Yards Bank & Trust Company (“Bank”). Significant intercompany transactions and accounts have been eliminated in consolidation. In preparing the unaudited consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of related revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, valuation of available-for sale securities, other real estate owned and income tax assets, and estimated liabilities and expense.

A description of other significant accounting policies is presented in the notes to Consolidated Financial Statements for the year ended December 31, 2015 included in Stock Yards Bancorp, Inc.’s Annual Report on Form 10-K. Certain reclassifications have been made in the prior year financial statements to conform to current year classifications.

Interim results for the three and six month periods ended June 30, 2016 are not necessarily indicative of the results for the entire year.

Critical Accounting Policies

Management has identified the accounting policy related to the allowance and provision for loan losses as critical to the understanding of Bancorp's results of operations and discussed this conclusion with the Audit Committee of the Board of Directors. Since the application of this policy requires significant management assumptions and estimates, it could result in materially different amounts to be reported if conditions or underlying circumstances were to change. The provision reflects an allowance methodology that is driven by risk ratings, historical losses, and qualitative factors. Assumptions include many factors such as changes in borrowers' financial condition which can change quickly or historical loss ratios related to certain loan portfolios which may or may not be indicative of future losses. In the second quarter of 2015, Bancorp extended the historical period used to capture Bancorp's historical loss ratios from 12 quarters to 24 quarters. Management believes the extension of the look-back period is appropriate to capture the impact of a full economic cycle and more accurately represents the current level of risk inherent in the loan portfolio. To the extent that management's assumptions prove incorrect, the results from operations could be materially affected by a higher or lower provision for loan losses. The accounting policy related to the allowance for loan losses is applicable to the commercial banking segment of Bancorp.

The allowance for loan losses is management's estimate of probable losses inherent in the loan portfolio as of the balance sheet date. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Bancorp's allowance calculation includes allocations to loan portfolio segments at June 30, 2016 for qualitative factors including, among other factors, economic and business conditions in each of our primary markets, the quality and experience of lending staff and management, exceptions to lending policies, levels of and trends in past due loans and loan classifications, concentrations of credit such as collateral type, trends in portfolio growth, dependency upon the value of underlying collateral for collateral-dependent loans, effect of other external factors such as the national economic and business trends, and the quality and depth of the loan review function. Bancorp utilizes the sum of all allowance amounts derived as described above as the appropriate level of allowance for loan and lease losses. Changes in the criteria used in this evaluation or the availability of new information could cause the allowance to be increased or decreased in future periods. In addition, bank regulatory agencies, as part of their examination process, may require adjustments to the allowance for loan and lease losses based on their judgments and estimates.

(2)Securities

The amortized cost, unrealized gains and losses, and fair value of securities available-for-sale follow:

(in thousands) June 30, 2016	Amortized cost	Unrealized Gains	Losses	Fair value
Government sponsored enterprise obligations	\$ 329,128	\$4,760	\$62	\$333,826
Mortgage-backed securities - government agencies	167,512	3,331	140	170,703
Obligations of states and political subdivisions	60,442	1,594	15	62,021
Corporate equity securities	653	104	-	757
Total securities available for sale	\$ 557,735	\$9,789	\$217	\$567,307
December 31, 2015				
U.S. Treasury and other U.S. Government obligations	\$ 79,999	\$1	\$-	\$80,000
Government sponsored enterprise obligations	251,190	1,468	765	251,893
Mortgage-backed securities - government agencies	170,139	1,143	1,654	169,628
Obligations of states and political subdivisions	62,410	1,342	50	63,702
Corporate equity securities	653	-	-	653
Total securities available for sale	\$ 564,391	\$3,954	\$2,469	\$565,876

Corporate equity securities consist of common stock in a publicly-traded business development company.

There were no securities classified as held to maturity as of June 30, 2016 or December 31, 2015.

No securities were sold in 2016. In 2015, Bancorp sold securities with total fair market value of \$5.9 million, generating no gain or loss. These securities consisted of mortgage-backed securities with small remaining balances and agency securities. These sales were made in the ordinary course of portfolio management. Management has the intent and ability to hold all remaining investment securities available-for-sale for the foreseeable future.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

A summary of the available-for-sale investment securities by contractual maturity groupings as of June 30, 2016 is shown below.

(in thousands)	Amortized cost	Fair value
Securities available-for-sale		
Due within 1 year	\$ 134,681	\$ 134,811
Due after 1 but within 5 years	120,813	122,843
Due after 5 but within 10 years	21,231	21,724
Due after 10 years	112,845	116,469
Mortgage-backed securities	167,512	170,703
Corporate equity securities	653	757
Total securities available-for-sale	\$ 557,735	\$ 567,307

Actual maturities may differ from contractual maturities because some issuers have the right to call or prepay obligations. In addition to equity securities, the investment portfolio includes agency mortgage-backed securities, which are guaranteed by agencies such as the FHLMC, FNMA, and GNMA. These securities differ from traditional debt securities primarily in that they may have uncertain principal payment dates and are priced based on estimated prepayment rates on the underlying collateral.

Securities with a carrying value of approximately \$319.5 million at June 30, 2016 and \$380.7 million at December 31, 2015 were pledged to secure accounts of commercial depositors in cash management accounts, public deposits, and cash balances for certain investment management and trust accounts.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Securities with unrealized losses at June 30, 2016 and December 31, 2015, not recognized in the statements of income are as follows:

(in thousands)	Less than 12 months		12 months or more		Total	
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized
June 30, 2016	value	losses	value	losses	value	losses
Government sponsored enterprise obligations	\$109,829	\$ 34	\$3,842	\$ 28	\$113,671	\$ 62
Mortgage-backed securities - government agencies	1,343	2	18,589	138	19,932	140
Obligations of states and political subdivisions	2,556	8	1,338	7	3,894	15
Total temporarily impaired securities	\$113,728	\$ 44	\$23,769	\$ 173	\$137,497	\$ 217
December 31, 2015						
Government sponsored enterprise obligations	\$102,098	\$ 500	\$8,469	\$ 265	\$110,567	\$ 765
Mortgage-backed securities - government agencies	49,774	662	29,936	992	79,710	1,654
Obligations of states and political subdivisions	13,225	31	1,955	19	15,180	50
Total temporarily impaired securities	\$165,097	\$ 1,193	\$40,360	\$ 1,276	\$205,457	\$ 2,469

Applicable dates for determining when securities are in an unrealized loss position are June 30, 2016 and December 31, 2015. As such, it is possible that a security had a market value lower than its amortized cost on other days during the past twelve months, but is not in the "Investments with an Unrealized Loss of less than 12 months" category above.

Unrealized losses on Bancorp's investment securities portfolio have not been recognized as an expense because the securities are of high credit quality, and the decline in fair values is due to changes in the prevailing interest rate environment since the purchase date. Fair value is expected to recover as securities reach their maturity date and/or the interest rate environment returns to conditions similar to when these securities were purchased. These investments consist of 23 and 70 separate investment positions as of June 30, 2016 and December 31, 2015, respectively. Because management does not intend to sell the investments, and it is not likely that Bancorp will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, Bancorp does not consider these securities to be other-than-temporarily impaired at June 30, 2016.

FHLB stock and other securities are investments held by Bancorp which are not readily marketable and are carried at cost. This category includes holdings of Federal Home Loan Bank of Cincinnati (FHLB) stock which are required for access to FHLB borrowing, and are classified as restricted securities.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****(3)Loans**

Composition of loans, net of deferred fees and costs, by primary loan portfolio class follows:

(in thousands)	June 30, 2016	December 31, 2015
Commercial and industrial	\$721,956	\$644,398
Construction and development, excluding undeveloped land	136,029	134,482
Undeveloped land	20,342	21,185
Real estate mortgage:		
Commercial investment	572,438	528,290
Owner occupied commercial	333,862	329,365
1-4 family residential	240,770	226,575
Home equity - first lien	52,360	50,115
Home equity - junior lien	65,999	63,066
Subtotal: Real estate mortgage	1,265,429	1,197,411
Consumer	31,795	35,531
Total loans	\$2,175,551	\$2,033,007

Allowance for loans individually evaluated
for impairment

Allowance for loans acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
------------------------------------------------------------------	------	------	------	------	------	------

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

(in thousands)	Type of loan					
	Construction and development		Commercial excluding undeveloped		Real estate	
December 31, 2015	and industrial	land	land	mortgage	Consumer	Total
Loans	\$644,398	\$ 134,482	\$ 21,185	\$ 1,197,411	\$ 35,531	\$ 2,033,007
Loans collectively evaluated for impairment	\$639,760	\$ 134,160	\$ 21,185	\$ 1,192,864	\$ 35,463	\$ 2,023,432
Loans individually evaluated for impairment	\$4,635	\$ -	\$ -	\$4,050	\$ 68	\$ 8,753
Loans acquired with deteriorated credit quality	\$3	\$ 322	\$ -	\$497	\$ -	\$ 822

	Construction and development		Commercial excluding undeveloped		Real estate	
	and industrial	land	land	mortgage	Consumer	Total
Allowance for loan losses						
At December 31, 2014	\$ 11,819	\$ 721	\$ 1,545	\$ 10,541	\$ 294	\$ 24,920
Provision (credit)	793	1,065	(2,131)	872	151	750
Charge-offs	(4,065)	(26)	-	(693)	(597)	(5,381)
Recoveries	98	-	1,400	155	499	2,152
At December 31, 2015	\$ 8,645	\$ 1,760	\$ 814	\$ 10,875	\$ 347	\$ 22,441
Allowance for loans collectively evaluated for impairment	\$ 8,377	\$ 1,760	\$ 814	\$ 10,667	\$ 279	\$ 21,897
Allowance for loans individually evaluated for impairment	\$ 268	\$ -	\$ -	\$ 208	\$ 68	\$ 544
Allowance for loans acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

The considerations by Bancorp in computing its allowance for loan losses are determined based on the various risk characteristics of each loan segment. Relevant risk characteristics are as follows:

Commercial and industrial loans: Loans in this category are made to businesses. Generally these loans are secured by assets of the business and repayment is expected from the cash flows of the business. A decline in the strength of the business or a weakened economy and resultant decreased consumer and/or business spending may have an effect on the credit quality in this loan category.

Construction and development, excluding undeveloped land: Loans in this category primarily include owner-occupied and investment construction loans and commercial development projects. In most cases, construction loans require only interest to be paid during construction. Upon completion or stabilization, the construction loan may convert to permanent financing in the real estate mortgage segment, requiring principal amortization. Repayment of development loans is derived from sale of lots or units including any pre-sold units. Credit risk is affected by construction delays, cost overruns, market conditions and availability of permanent financing, to the extent such permanent financing is not being provided by Bancorp.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Undeveloped land: Loans in this category are secured by land acquired for development by the borrower, but for which no development has yet taken place. Credit risk is affected by market conditions and time to sell lots at an adequate price. Credit risk is also affected by availability of permanent financing, to the extent such permanent financing is not being provided by Bancorp.

Real estate mortgage: Loans in this category are made to and secured by owner-occupied residential real estate, owner-occupied real estate used for business purposes, and income-producing investment properties. For owner occupied residential and commercial real estate, repayment is dependent on financial strength of the borrower. For income-producing investment properties, repayment is dependent on financial strength of tenants in addition to the borrower. Underlying properties are generally located in Bancorp's primary market area. Cash flows of income producing investment properties may be adversely impacted by a downturn in the economy as evidenced by increased vacancy rates, which in turn, could have an effect on credit quality. Overall health of the economy, including unemployment rates and real estate prices, has an effect on credit quality in this loan category.

Consumer: Loans in this category may be either secured or unsecured and repayment is dependent on credit quality of the individual borrower and, if applicable, adequacy of collateral securing the loan. Therefore, overall health of the economy, including unemployment rates and stock prices, will have a significant effect on credit quality in this loan category.

Bancorp has loans that were acquired in the 2013 acquisition, for which there was, at acquisition, evidence of deterioration of credit quality since origination and for which it was probable that all contractually required payments would not be collected. The carrying amount of those loans is included in the balance sheet amounts of loans at June 30, 2016 and December 31, 2015. Changes in the fair value adjustment for acquired impaired loans are shown in the following table:

(in thousands)	Accretable discount	Non-accretable discount
Balance at December 31, 2014	\$ 62	\$ 266
Accretion	(59)	(77)
Reclassifications from (to) non-accretable discount	-	-
Disposals	-	-
Balance at December 31, 2015	\$ 3	\$ 189
Accretion	(3)	-
Reclassifications from (to) non-accretable discount	-	-
Disposals	-	-
Balance at June 30, 2016	\$ -	\$ 189

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

The following table presents loans individually evaluated for impairment as of June 30, 2016 and December 31, 2015.

(in thousands)	Recorded investment	Unpaid principal balance	Related allowance	Average recorded investment
June 30, 2016				
Loans with no related allowance recorded:				
Commercial and industrial	\$ 1,753	\$ 2,321	\$ -	\$ 2,805
Construction and development, excluding undeveloped land	-	-	-	-
Undeveloped land	-	-	-	-
Real estate mortgage				
Commercial investment	280	280	-	254
Owner occupied commercial	1,241	1,678	-	1,559
1-4 family residential	977	977	-	999
Home equity - first lien	-	-	-	4
Home equity - junior lien	253	253	-	211
Subtotal: Real estate mortgage	2,751	3,188	-	3,027
Consumer	31	31	-	21
Subtotal	\$ 4,535	\$ 5,540	\$ -	\$ 5,853
Loans with an allowance recorded:				
Commercial and industrial	\$ 998	\$ 1,473	\$ 286	\$ 1,206
Construction and development, excluding undeveloped land	-	-	-	-
Undeveloped land	-	-	-	-
Real estate mortgage				
Commercial investment	-	-	-	-
Owner occupied commercial	394	394	7	761
1-4 family residential	-	-	-	-
Home equity - first lien	-	-	-	-
Home equity - junior lien	-	-	-	-
Subtotal: Real estate mortgage	394	394	7	761
Consumer	63	63	63	66
Subtotal	\$ 1,455	\$ 1,930	\$ 356	\$ 2,033
Total:				
Commercial and industrial	\$ 2,751	\$ 3,794	\$ 286	\$ 4,011
Construction and development, excluding undeveloped land	-	-	-	-

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Undeveloped land	-	-	-	-
Real estate mortgage	-	-	-	-
Commercial investment	280	280	-	254
Owner occupied commercial	1,635	2,072	7	2,320
1-4 family residential	977	977	-	999
Home equity - first lien	-	-	-	4
Home equity - junior lien	253	253	-	211
Subtotal: Real estate mortgage	3,145	3,582	7	3,788
Consumer	94	94	63	87
Total	\$ 5,990	\$ 7,470	\$ 356	\$ 7,886

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

(in thousands)				
December 31, 2015	Recorded investment	Unpaid principal balance	Related allowance	Average recorded investment
Loans with no related allowance recorded:				
Commercial and industrial	\$ 3,119	\$ 3,859	\$ -	\$ 1,414
Construction and development, excluding undeveloped land	-	151	-	21
Undeveloped land	-	-	-	-
Real estate mortgage				
Commercial investment	278	278	-	178
Owner occupied commercial	1,743	2,713	-	1,622
1-4 family residential	906	906	-	661
Home equity - first lien	13	13	-	37
Home equity - junior lien	92	92	-	69
Subtotal: Real estate mortgage	3,032	4,002	-	2,567
Consumer	-	-	-	3
Subtotal	\$ 6,151	\$ 8,012	\$ -	\$ 4,005
Loans with an allowance recorded:				
Commercial and industrial	\$ 1,516	\$ 3,087	\$ 268	\$ 4,612
Construction and development, excluding undeveloped land	-	-	-	368
Undeveloped land	-	-	-	-
Real estate mortgage				
Commercial investment	-	-	-	92
Owner occupied commercial	1,018	1,018	208	1,266
1-4 family residential	-	-	-	188
Home equity - first lien	-	-	-	-
Home equity - junior lien	-	-	-	-
Subtotal: Real estate mortgage	1,018	1,018	208	1,546
Consumer	68	68	68	72
Subtotal	\$ 2,602	\$ 4,173	\$ 544	\$ 6,598
Total:				
Commercial and industrial	\$ 4,635	\$ 6,946	\$ 268	\$ 6,026
Construction and development, excluding undeveloped land	-	151	-	389
Undeveloped land	-	-	-	-
Real estate mortgage				
Commercial investment	278	278	-	270

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Owner occupied commercial	2,761	3,731	208	2,888
1-4 family residential	906	906	-	849
Home equity - first lien	13	13	-	37
Home equity - junior lien	92	92	-	69
Subtotal: Real estate mortgage	4,050	5,020	208	4,113
Consumer	68	68	68	75
Total	\$ 8,753	\$ 12,185	\$ 544	\$ 10,603

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Differences between recorded investment amounts and unpaid principal balance amounts less related allowance are due to partial charge-offs which have occurred over the life of loans.

Impaired loans include non-accrual loans and accruing loans accounted for as troubled debt restructurings (TDR), which continue to accrue interest. Non-performing loans include the balance of impaired loans plus any loans over 90 days past due and still accruing interest. Bancorp had loans past due more than 90 days and still accruing interest totaling \$410 thousand at June 30, 2016, compared with \$176 thousand at December 31, 2015.

The following table presents the recorded investment in non-accrual loans as of June 30, 2016 and December 31, 2015.

(in thousands)	June 30, 2016	December 31, 2015
Commercial and industrial	\$1,794	\$ 3,643
Construction and development, excluding undeveloped land	-	-
Undeveloped land	-	-
Real estate mortgage		
Commercial investment	280	278
Owner occupied commercial	1,635	2,761
1-4 family residential	977	906
Home equity - first lien	-	13
Home equity - junior lien	253	92
Subtotal: Real estate mortgage	3,145	4,050
Consumer	31	-
Total	\$4,970	\$ 7,693

At June 30, 2016 and December 31, 2015, Bancorp had \$1.0 million and \$1.1 million of accruing loans classified as TDR, respectively. Bancorp did not modify and classify any additional loans as TDR during the three or six month periods ended June 30, 2016 or 2015.

Bancorp did not have any loans accounted for as TDR that were restructured and experienced a subsequent payment default during the three and twelve month periods ended June 30, 2016 or 2015. Loans accounted for as TDR include modifications from original terms such as those due to bankruptcy proceedings, certain modifications of amortization periods or extended suspension of principal payments due to customer financial difficulties. Loans accounted for as TDR, which have not defaulted, are individually evaluated for impairment and, at June 30, 2016, had a total allowance allocation of \$319 thousand, compared with \$177 thousand at December 31, 2015.

At June 30, 2016 and December 31, 2015, Bancorp did not have any outstanding commitments to lend additional funds to borrowers whose loans have been modified as TDR.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

The following table presents the aging of the recorded investment in loans as of June 30, 2016 and December 31, 2015.

(in thousands)	30-59 days past due	60-89 days past due	90 or more days past due (includes non-accrual)	Total past due	Current	Total loans	Recorded investment > 90 days and accruing
June 30, 2016							
Commercial and industrial	\$587	\$96	\$ 1,794	\$2,477	\$719,479	\$721,956	\$ -
Construction and development, excluding undeveloped land	-	-	-	-	136,029	136,029	-
Undeveloped land	-	-	-	-	20,342	20,342	-
Real estate mortgage							
Commercial investment	-	200	420	620	571,818	572,438	140
Owner occupied commercial	1,367	734	1,836	3,937	329,925	333,862	201
1-4 family residential	1,428	227	1,046	2,701	238,069	240,770	69
Home equity - first lien	78	25	-	103	52,257	52,360	-
Home equity - junior lien	79	259	253	591	65,408	65,999	-
Subtotal: Real estate mortgage	2,952	1,445	3,555	7,952	1,257,477	1,265,429	410
Consumer	-	-	31	31	31,764	31,795	-
Total	\$3,539	\$1,541	\$ 5,380	\$10,460	\$2,165,091	\$2,175,551	\$ 410
December 31, 2015							
Commercial and industrial	\$238	\$327	\$ 3,643	\$4,208	\$640,190	\$644,398	\$ -
Construction and development, excluding undeveloped land	-	-	-	-	134,482	134,482	-
Undeveloped land	-	-	-	-	21,185	21,185	-
Real estate mortgage							
Commercial investment	290	140	278	708	527,582	528,290	-
Owner occupied commercial	-	-	2,761	2,761	326,604	329,365	-
1-4 family residential	1,147	94	1,082	2,323	224,252	226,575	176
Home equity - first lien	35	51	13	99	50,016	50,115	-
Home equity - junior lien	285	173	92	550	62,516	63,066	-

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Subtotal: Real estate mortgage	1,757	458	4,226	6,441	1,190,970	1,197,411	176
Consumer	343	8	-	351	35,180	35,531	-
Total	\$2,338	\$793	\$ 7,869	\$11,000	\$2,022,007	\$2,033,007	\$ 176

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Consistent with regulatory guidance, Bancorp categorizes loans into credit risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information and current economic trends. Pass-rated loans included all risk-rated loans other than those classified as other assets especially mentioned, substandard, and doubtful, which are defined below:

Other assets especially mentioned (“OAEM”): Loans classified as OAEM have potential weaknesses that deserve management's close attention. These potential weaknesses may result in deterioration of repayment prospects for the loan or of Bancorp's credit position at some future date.

Substandard: Loans classified as substandard are inadequately protected by the paying capacity of the obligor or of collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize repayment of the debt. Default is a distinct possibility if the deficiencies are not corrected.

Substandard non-performing: Loans classified as substandard non-performing have all the characteristics of substandard loans and have been placed on non-accrual status or have been accounted for as troubled debt restructurings. Loans are placed on non-accrual status when prospects for recovering both principal and accrued interest are considered doubtful or when a default of principal or interest has existed for 90 days or more.

Doubtful: Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or repayment in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

As of June 30, 2016 and December 31, 2015, the internally assigned risk grades of loans by category were as follows:

(in thousands)	Substandard					Total
June 30, 2016	Pass	OAEM	Substandard	non-performing	Doubtful	loans
Commercial and industrial	\$693,830	\$18,929	\$6,446	\$2,751	\$-	\$721,956
Construction and development, excluding undeveloped land	134,823	-	1,206	-	-	136,029
Undeveloped land	19,681	-	661	-	-	20,342
Real estate mortgage						
Commercial investment	570,100	1,918	-	420	-	572,438
Owner occupied commercial	321,684	8,452	1,890	1,836	-	333,862
1-4 family residential	239,429	295	-	1,046	-	240,770
Home equity - first lien	52,360	-	-	-	-	52,360
Home equity - junior lien	65,696	50	-	253	-	65,999
Subtotal: Real estate mortgage	1,249,269	10,715	1,890	3,555	-	1,265,429
Consumer	31,701	-	-	94	-	31,795
Total	\$2,129,304	\$29,644	\$10,203	\$6,400	\$-	\$2,175,551
December 31, 2015						
Commercial and industrial	\$612,853	\$19,672	\$7,238	\$4,635	\$-	\$644,398
Construction and development, excluding undeveloped land	133,342	773	367	-	-	134,482
Undeveloped land	20,513	517	155	-	-	21,185
Real estate mortgage						
Commercial investment	525,829	2,183	-	278	-	528,290
Owner occupied commercial	306,056	17,135	3,413	2,761	-	329,365
1-4 family residential	224,645	848	-	1,082	-	226,575
Home equity - first lien	50,102	-	-	13	-	50,115
Home equity - junior lien	62,924	50	-	92	-	63,066
Subtotal: Real estate mortgage	1,169,556	20,216	3,413	4,226	-	1,197,411
Consumer	35,463	-	-	68	-	35,531
Total	\$1,971,727	\$41,178	\$11,173	\$8,929	\$-	\$2,033,007

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****(4) Securities Sold Under Agreements to Repurchase**

Securities sold under agreements to repurchase, which represent excess funds from commercial customers as part of a cash management service, totaled \$57.4 million and \$64.5 million at June 30, 2016 and December 31, 2015, respectively. Bancorp enters into sales of securities under agreement to repurchase at a specified future date. At June 30, 2016, all of these financing arrangements had overnight maturities and were secured by government sponsored enterprise obligations and government agency mortgage-backed securities which were owned and under the control of Bancorp.

(5) Federal Home Loan Bank Advances

Bancorp had outstanding borrowings totaling of \$43.0 million and \$43.5 million at June 30, 2016 and December 31, 2015, respectively, via 12 separate fixed-rate advances. For two advances totaling \$30 million, both of which are non-callable, interest payments are due monthly, with principal due at maturity. For the remaining advances totaling \$13.0 million, principal and interest payments are due monthly based on an amortization schedule.

The following is a summary of the contractual maturities and average effective rates of outstanding advances:

Year	June 30, 2016		December 31, 2015	
	Advance	Fixed Rate	Advance	Fixed Rate
2016	\$30,000	0.67 %	\$30,000	0.55 %
2020	1,814	2.23	1,838	2.23
2021	394	2.12	429	2.12
2024	2,764	2.36	2,865	2.36
2025	6,705	2.44	6,991	2.44
2028	1,325	1.48	1,345	1.48
Total	\$43,002	1.16 %	\$43,468	1.09 %

In addition to the fixed-rate advances listed above, Bancorp had a \$60 million cash management advance from the FHLB. This advance matured in the first week of July and was utilized to manage Bancorp's overall cash position. Due to the short nature of the advance, it was recorded within Federal fund purchased and other short-term borrowings.

Advances from the FHLB are collateralized by certain commercial and residential real estate mortgage loans totaling \$627.7 million under a blanket mortgage collateral agreement and FHLB stock. Bancorp believes these borrowings to be an effective alternative to higher cost time deposits to manage interest rate risk associated with long-term fixed rate loans. At June 30, 2016, the amount of available credit from the FHLB totaled \$306.9 million.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****(6) Other Comprehensive Income (Loss)**

The following table illustrates activity within the balances in accumulated other comprehensive income (loss) by component, and is shown for the six months ended June 30, 2016 and 2015.

(in thousands)	Net unrealized gains on securities available-for-sale	Net unrealized gains (losses) on cash flow hedges	Minimum pension liability adjustment	Total
Balance at December 31, 2014	\$ 2,456	\$ 16	\$ (387)	\$2,085
Net current period other comprehensive loss	(751)	(21)	-	(772)
Balance at June 30, 2015	\$ 1,705	\$ (5)	\$ (387)	\$1,313
Balance at December 31, 2015	\$ 965	\$ (60)	\$ (273)	\$632
Net current period other comprehensive income (loss)	5,256	(438)	-	4,818
Balance at June 30, 2016	\$ 6,221	\$ (498)	\$ (273)	\$5,450

(7) Derivative Financial Instruments

Occasionally, Bancorp enters into free-standing interest rate swaps for the benefit of its commercial customers who desire to hedge their exposure to changing interest rates. Bancorp offsets its interest rate exposure on these transactions by entering into offsetting swap agreements with substantially matching terms with approved reputable independent counterparties. These undesignated derivative instruments are recognized on the consolidated balance sheet at fair value. Because of matching terms of offsetting contracts and collateral provisions mitigating any non-performance risk, changes in fair value subsequent to initial recognition are expected to have an insignificant effect on earnings. Exchanges of cash flows related to the undesignated interest rate swap agreements for the first six months of 2016 were offsetting and therefore had no net effect on Bancorp's earnings or cash flows.

Interest rate swap agreements derive their value from underlying interest rates. These transactions involve both credit and market risk. Notional amounts are amounts on which calculations, payments, and the value of the derivative are

based. Notional amounts do not represent direct credit exposures. Direct credit exposure is limited to the net difference between the calculated amounts to be received and paid, if any. Bancorp is exposed to credit-related losses in the event of nonperformance by counterparties to these agreements. Bancorp mitigates the credit risk of its financial contracts through credit approvals, limits and monitoring procedures, and does not expect any counterparties to fail their obligations.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

At June 30, 2016 and December 31, 2015, Bancorp had outstanding undesignated interest rate swap contracts as follows:

(dollar amounts in thousands)	Receiving		Paying	
	June 30, 2016	December 31, 2015	June 30, 2016	December 31, 2015
Notional amount	\$25,657	\$ 10,788	\$25,657	\$ 10,788
Weighted average maturity (years)	7.4	6.9	7.4	6.9
Fair value	\$ (1,282)		\$ (461)	

In 2013, Bancorp entered into an interest rate swap to hedge cash flows of a \$10 million rolling fixed-rate three-month FHLB borrowing. The swap began December 6, 2013 and ends December 6, 2016. In 2015, Bancorp entered into an interest rate swap to hedge cash flows of a \$20 million rolling fixed-rate three-month FHLB borrowing. The swap began December 9, 2015 and matures December 6, 2020. For purposes of hedging, the rolling fixed rate advances are considered to be floating rate liabilities. The interest rate swaps involve exchange of Bancorp's floating rate interest payments for fixed rate swap payments on underlying principal amounts. These swaps were designated, and qualified, for cash-flow hedge accounting. For derivative instruments that are designated and qualify as cash flow hedging instruments, the effective portion of gains or losses is reported as a component of other comprehensive income, and is subsequently reclassified into earnings as an adjustment to interest expense in periods in which the hedged forecasted transaction affects earnings.

The following table details Bancorp's derivative position designated as a cash flow hedge, and the fair values as of June 30, 2016 and December 31, 2015.

(dollars in thousands)

Notional amount	Maturity date	Receive (variable) index	Pay fixed swap rate	Fair value June 30, 2016	Fair value December 31, 2015
\$ 10,000	12/6/2016	US 3 Month LIBOR	0.72 %	\$-	\$ 8
20,000	12/6/2020	US 3 Month LIBOR	1.79 %	(766)	(101)

\$ 30,000

1.43 % \$(766) \$ (93)

(8) Goodwill and Intangible Assets

US GAAP requires that goodwill and intangible assets with indefinite useful lives not be amortized, but instead be tested for impairment at least annually. Annual evaluations have resulted in no indication of impairment. Bancorp currently has goodwill in the amount of \$682 thousand from the 1996 acquisition of an Indiana bank. This goodwill is assigned to the commercial banking segment of Bancorp.

Bancorp recorded a core deposit intangible totaling \$2.5 million as a result of its 2013 acquisition of THE BANCORP, Inc. This intangible is being amortized over the expected life of the underlying deposits to which the intangible is attributable. At June 30, 2016, the unamortized core deposit intangible was \$1.5 million.

Mortgage servicing rights (MSRs) are initially recognized at fair value when mortgage loans are sold with servicing retained. The MSRs are amortized in proportion to and over the period of estimated net servicing income, considering appropriate prepayment assumptions. MSRs are evaluated quarterly for impairment by comparing carrying value to fair value. Estimated fair values of MSRs at June 30, 2016 and December 31, 2015 were \$2.4 million and \$3.1 million, respectively. Total outstanding principal balances of loans serviced for others were \$388.7 million and \$410.8 million at June 30, 2016, and December 31, 2015, respectively.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Changes in the net carrying amount of MSRs for the six months ended June 30, 2016 and 2015 are shown in the following table:

(in thousands)	For six months ended June 30,	
	2016	2015
Balance at beginning of period	\$1,018	\$1,131
Additions for mortgage loans sold	70	216
Amortization	(118)	(370)
Balance at June 30	\$970	\$977

(9) Defined Benefit Retirement Plan

Bancorp sponsors an unfunded, non-qualified, defined benefit retirement plan for three key officers (two current and one retired), and has no plans to increase the number of or benefits to participants. Benefits vest based on 25 years of service. The retired officer and one current officer are fully vested, and one current officer will be fully vested in 2017. Actuarially determined pension costs are expensed and accrued over the service period, and benefits are paid from Bancorp's assets. Net periodic benefits costs, which include interest cost and amortization of net losses, totaled \$34 thousand and \$36 thousand, for the three months ended June 30, 2016 and 2015, respectively. For the six months ended June 30, 2016 and 2015, the net periodic benefit costs totaled \$67 thousand and \$71 thousand, respectively.

(10) Commitments and Contingent Liabilities

As of June 30, 2016, Bancorp had various commitments outstanding that arose in the normal course of business, including standby letters of credit and commitments to extend credit, which are properly not reflected in the consolidated financial statements. In management's opinion, commitments to extend credit of \$628.6 million including standby letters of credit of \$11.6 million represent normal banking transactions. Commitments to extend credit were \$636.9 million, including letters of credit of \$12.8 million, as of December 31, 2015. Commitments to extend credit are agreements to lend to a customer as long as collateral is available and there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses. Commitments to extend credit are mainly comprised of commercial lines of credit, construction and home equity credit lines and credit cards issued to commercial customers. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Bancorp uses the same credit and collateral policies in making commitments and conditional guarantees as for on-balance sheet instruments. Bancorp evaluates each customer's creditworthiness on a case by case basis. The amount

of collateral obtained is based on management's credit evaluation of the customer. Collateral held varies but may include accounts receivable, inventory, equipment, and real estate. However, should the commitments be drawn upon and should our customers default on their resulting obligation to us, our maximum exposure to credit loss, without consideration of collateral, is represented by the contractual amount of those instruments. At June 30, 2016, Bancorp has accrued \$387 thousand in other liabilities for inherent risks related to unfunded credit commitments.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Standby letters of credit and financial guarantees written are conditional commitments issued by Bancorp to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support private commercial transactions. Standby letters of credit generally have maturities of one to two years.

Also, as of June 30, 2016, in the normal course of business, there were pending legal actions and proceedings in which claims for damages are asserted. Management, after discussion with legal counsel, believes the ultimate result of these legal actions and proceedings will not have a material adverse effect on the consolidated financial position or results of operations of Bancorp.

(11) Preferred Stock

Bancorp has a class of preferred stock (no par value; 1,000,000 shares authorized), the relative rights, preferences and other terms of which or any series within the class will be determined by the Board of Directors prior to any issuance. None of this stock has been issued to date.

(12) Stock Split

On April 29, 2016 Bancorp declared a 3 for 2 stock split to be effected as a 50% stock dividend to shareholders of record on May 13, 2016, payable May 27, 2016. Share and per share information has been adjusted for this split.

(13) Stock-Based Compensation

The fair value of all awards granted, net of estimated forfeitures, is recognized as compensation expense over the respective service period.

Bancorp currently has one stock-based compensation plan. At Bancorp's 2015 Annual Meeting of Shareholders, shareholders approved the 2015 Omnibus Equity Compensation Plan and authorized the shares available from the expiring 2005 plan for future awards under the 2015 plan. No additional shares were made available. As of June 30, 2016, there were 167,848 shares available for future awards. The 2005 Stock Incentive Plan expired in April 2015; however, options and SARs granted under this plan expire as late as 2025.

Options, which have not been granted since 2007, generally had a vesting schedule of 20% per year. Stock appreciation rights (“SARs”) granted have a vesting schedule of 20% per year. Options and SARs expire ten years after the grant date unless forfeited due to employment termination.

Restricted shares granted to officers vest over five years. All restricted shares have been granted at a price equal to the market value of common stock at the time of grant. For all grants prior to 2015, grantees are entitled to dividend payments during the vesting period. For grants in 2015 and 2016, forfeitable dividends are deferred until shares are vested.

Grants of performance stock units (“PSUs”) vest based upon service and a single three-year performance period which begins January 1 of the first year of the performance period. Because grantees are not entitled to dividend payments during the performance period, the fair value of these PSUs is estimated based upon the fair value of the underlying shares on the date of grant, adjusted for non-payment of dividends. Beginning in 2015, grants require a one year post-vesting holding periods. For 2015 and 2016, the fair value of such grants incorporates a liquidity discount of 4.80% and 4.50%, respectively, related to the holding period.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Grants of restricted stock units (“RSUs”) to directors are time-based and vest 12 months after grant date. Because grantees are entitled to deferred dividend payments at the end of the vesting period, fair value of the RSUs is estimated based on fair value of underlying shares on the date of grant.

Bancorp has recognized stock-based compensation expense, within salaries and employee benefits for employees, and within other non-interest expense for directors, in the consolidated statements of income as follows:

	For three months ended		For six months ended	
	June 30, 2016	2015	June 30, 2016	2015
(in thousands)				
Stock-based compensation expense before income taxes	\$560	\$494	\$1,073	\$995
Less: deferred tax benefit	(196)	(173)	(376)	(348)
Reduction of net income	\$364	\$321	\$697	\$647

Bancorp expects to record an additional \$1.1 million of stock-based compensation expense in 2016 for equity grants outstanding as of June 30, 2016. As of June 30, 2016, Bancorp has \$4.8 million of unrecognized stock-based compensation expense that is expected to be recorded as compensation expense over the next five years as awards vest. Bancorp received cash of \$1.0 million and \$1.6 million from the exercise of options during the first six months of 2016 and 2015, respectively.

Fair values of Bancorp’s stock options and SARs are estimated at the date of grant using the Black-Scholes option pricing model, a leading formula for calculating the value of stock options and SARs. This model requires the input of assumptions, changes to which can materially affect the fair value estimate. Fair value of restricted shares is determined by Bancorp’s closing stock price on the date of grant. The following assumptions were used in SAR valuations at the grant date in each year:

	2016	2015
Dividend yield	2.94 %	2.97 %
Expected volatility	19.31 %	22.81 %
Risk free interest rate	1.70 %	1.91 %
Expected life of SARs (in years)	7.3	7.5

Dividend yield and expected volatility are based on historical information for Bancorp corresponding to the expected life of options and SARs granted. Expected volatility is the volatility of the underlying shares for the expected term on a monthly basis. The risk free interest rate is the implied yield currently available on U.S. Treasury issues with a remaining term equal to the expected life of the options. The expected life of SARs is based on actual experience of past like-term SARs. Bancorp evaluates historical exercise and post-vesting termination behavior when determining the expected life.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

A summary of stock option and SARs activity and related information for the six months ended June 30, 2016 follows:

	Options and SARs (in thousands)	Exercise price		Weighted average exercise price	Aggregate intrinsic value (in thousands)	Weighted average fair value	Weighted average remaining contractual life (in years)
At December 31, 2015							
Vested and exercisable	656	\$14.02 -	19.44	\$ 15.75	\$ 6,191	\$ 3.39	3.7
Unvested	266	15.24 -	24.55	18.66	1,733	3.29	7.7
Total outstanding	922	14.02 -	24.55	16.59	7,924	3.36	4.8
Granted	87		25.76	25.76	216	3.56	
Exercised	(83)	14.02 -	17.89	17.08	785	3.96	
Forfeited	(1)	15.24 -	15.84	15.47	8	2.90	
At June 30, 2016							
Vested and exercisable	664	14.02 -	22.96	15.82	8,238	3.29	3.9
Unvested	260	15.24 -	25.76	21.48	1,756	3.43	8.3
Total outstanding	924	14.02 -	25.76	17.41	\$ 9,994	3.33	5.1
Vested year-to-date	92	15.24 -	22.96	17.44	\$ 990	3.14	

Intrinsic value for stock options and SARs is defined as the amount by which the current market price of the underlying stock exceeds the exercise or grant price.

A summary of restricted common stock activity for the periods ending December 31, 2015 and June 30, 2016, is outlined in the following table:

	Number	Grant date weighted- average cost
Unvested at December 31, 2014	171,139	\$ 16.63
Shares awarded	52,898	22.99
Restrictions lapsed and shares released to employees	(61,205)	15.89
Shares forfeited	(6,974)	18.97
Unvested at December 31, 2015	155,858	\$ 18.98
Shares awarded	51,122	25.78
Restrictions lapsed and shares released to employees	(48,290)	17.91
Shares forfeited	(8,596)	20.64
Unvested at June 30, 2016	150,094	\$ 21.55

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Bancorp awarded performance-based restricted stock units (“PSUs”) to executive officers of Bancorp, the single three-year performance period for which began January 1 of the award year. The following table outlines the PSU grants.

Grant year	Vesting period in years	Fair value	Expected shares to be awarded
2014	3	\$17.61	50,024
2015	3	20.02	31,887
2016	3	22.61	27,663

In the first quarter of 2016, Bancorp awarded 8,144 RSUs to directors of Bancorp with a grant date fair value of \$200 thousand. In the second quarter of 2016, 1,018 RSUs were cancelled, leaving 7,126 RSUs outstanding with a grant date fair value of \$175 thousand.

(14) Net Income Per Share

The following table reflects, for the three and six months ended June 30, 2016 and 2015, net income (numerator) and average shares outstanding (denominator) for basic and diluted net income per share computations:

(In thousands, except per share data)	Three months ended		Six months ended	
	June 30, 2016	2015	June 30, 2016	2015
Net income	\$10,109	\$9,002	\$19,944	\$18,257
Average shares outstanding	22,336	22,065	22,295	22,018
Dilutive securities	368	339	363	335
Average shares outstanding including dilutive securities including dilutive securities	22,704	22,404	22,658	22,353
Net income per share, basic	\$0.45	\$0.41	\$0.89	\$0.83
Net income per share, diluted	\$0.45	\$0.40	\$0.88	\$0.82

(15) Segments

Bancorp's principal activities include commercial banking and investment management and trust. Commercial banking provides a full range of loan and deposit products to individual consumers and businesses. Commercial banking also includes Bancorp's mortgage origination and securities brokerage activity. Investment management and trust provides wealth management services including investment management, trust and estate administration, and retirement plan services.

Financial information for each business segment reflects that which is specifically identifiable or allocated based on an internal allocation method. Income taxes are allocated based on the effective federal income tax rate adjusted for any tax exempt activity. All tax exempt activity and provision for loan losses have been allocated to the commercial banking segment. Measurement of performance of business segments is based on the management structure of Bancorp and is not necessarily comparable with similar information for any other financial institution. Information presented is also not necessarily indicative of the segments' operations if they were independent entities.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Selected financial information by business segment for the three and six month periods ended June 30, 2016 and 2015 follows:

(in thousands)	Commercial banking	Investment management and trust	Total
Three months ended June 30, 2016			
Net interest income	\$ 23,888	\$ 62	\$23,950
Provision for loan losses	750	-	750
Investment management and trust services	-	4,807	4,807
All other non-interest income	5,971	-	5,971
Non-interest expense	17,297	2,896	20,193
Income before income taxes	11,812	1,973	13,785
Tax expense	2,971	705	3,676
Net income	\$ 8,841	\$ 1,268	\$10,109
Three months ended June 30, 2015			
Net interest income	\$ 21,756	\$ 45	\$21,801
Provision (credit) for loan losses	-	-	-
Investment management and trust services	-	4,651	4,651
All other non-interest income	5,568	-	5,568
Non-interest expense	16,015	2,852	18,867
Income before income taxes	11,309	1,844	13,153
Tax expense	3,495	656	4,151
Net income	\$ 7,814	\$ 1,188	\$9,002

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

(in thousands)	Commercial banking	Investment management and trust	Total
Six months ended June 30, 2016			
Net interest income	\$ 47,295	\$ 124	\$47,419
Provision for loan losses	1,250	-	1,250
Investment management and trust services	-	9,419	9,419
All other non-interest income	11,441	-	11,441
Non-interest expense	34,192	5,541	39,733
Income before income taxes	23,294	4,002	27,296
Tax expense	5,922	1,430	7,352
Net income	\$ 17,372	\$ 2,572	\$19,944
Six months ended June 30, 2015			
Net interest income	\$ 43,316	\$ 99	\$43,415
Provision (credit) for loan losses	-	-	-
Investment management and trust services	-	9,203	9,203
All other non-interest income	10,689	-	10,689
Non-interest expense	31,206	5,440	36,646
Income before income taxes	22,799	3,862	26,661
Tax expense	7,029	1,375	8,404
Net income	\$ 15,770	\$ 2,487	\$18,257

(16) Income Taxes

Components of income tax expense from operations were as follows:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Current tax expense				
Federal	\$4,222	\$3,884	\$6,595	\$6,960
State	186	186	310	273
Total current tax expense	4,408	4,070	6,905	7,233
Deferred tax expense				
Federal	(711)	109	390	1,093
State	(21)	(28)	57	78
Total deferred tax expense (benefit)	(732)	81	447	1,171

Total income tax expense	\$3,676	\$4,151	\$7,352	\$8,404
--------------------------	---------	---------	---------	---------

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

An analysis of the difference between statutory and effective tax rates for the six months ended June 30, 2016 and 2015 follows:

	Six months ended June 30,	
	2016	2015
U.S. federal statutory tax rate	35.0%	35.0%
Tax exempt interest income	(1.3)	(1.4)
Tax credits	(9.5)	(2.5)
Cash surrender value of life insurance	(0.9)	(0.9)
State income taxes, net of federal benefit	0.9	0.9
Other, net	2.7	0.4
Effective tax rate	26.9%	31.5%

State income tax expense represents tax owed in Indiana. Kentucky and Ohio state bank taxes are based on capital levels, and are recorded as other non-interest expense.

US GAAP provides guidance on financial statement recognition and measurement of tax positions taken, or expected to be taken, in tax returns. As of June 30, 2016 and December 31, 2015, the gross amount of unrecognized tax benefits, including penalties and interest, was \$48 thousand and \$42 thousand, respectively. If recognized, tax benefits would reduce tax expense and accordingly, increase net income. The amount of unrecognized tax benefits may increase or decrease in the future for various reasons including adding amounts for current year tax positions, expiration of open income tax returns due to statutes of limitation, changes in management's judgment about the level of uncertainty, status of examination, litigation and legislative activity and addition or elimination of uncertain tax positions. Federal and state income tax returns are subject to examination for the years after 2011.

(17) Assets and Liabilities Measured and Reported at Fair Value

Bancorp follows the provisions of authoritative guidance for fair value measurements. This guidance is definitional and disclosure oriented and addresses how companies should approach measuring fair value when required by US GAAP. The guidance also prescribes various disclosures about financial statement categories and amounts which are measured at fair value, if such disclosures are not already specified elsewhere in US GAAP.

Authoritative guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between participants at the measurement date. The guidance also establishes a hierarchy to group assets and liabilities carried at fair value in three levels based upon the markets in which the assets and liabilities trade and the reliability of assumptions used to determine fair value. These levels are:

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

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

Level 3: Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions would reflect internal estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques could include pricing models, discounted cash flows and other similar techniques.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Authoritative guidance requires maximum use of observable inputs and minimum use of unobservable inputs in fair value measurements. Where there exists limited or no observable market data, Bancorp derives its own estimates by generally considering characteristics of the asset/liability, the current economic and competitive environment and other factors. For this reason, results cannot be determined with precision and may not be realized on an actual sale or immediate settlement of the asset or liability.

Bancorp's investment securities available-for-sale and interest rate swaps are recorded at fair value on a recurring basis. Other accounts including mortgage servicing rights, impaired loans and other real estate owned may be recorded at fair value on a non-recurring basis, generally in the application of lower of cost or market adjustments or write-downs of specific assets.

The portfolio of investment securities available-for-sale is comprised of U.S. Treasury and other U.S. government obligations, debt securities of U.S. government-sponsored corporations (including mortgage-backed securities), obligations of state and political subdivisions and corporate equity securities. U.S. Treasury and corporate equity securities are priced using quoted prices of identical securities in an active market. These measurements are classified as Level 1 in the hierarchy above. All other securities are priced using standard industry models or matrices with various assumptions such as yield curves, volatility, prepayment speeds, default rates, time value, credit rating and market prices for similar instruments. These assumptions are generally observable in the market place and can be derived from or supported by observable data. These measurements are classified as Level 2 in the hierarchy above.

Interest rate swaps are valued using primarily Level 2 inputs. Fair value measurements generally based on benchmark forward yield curves and other relevant observable market data. For purposes of potential valuation adjustments to derivative positions, Bancorp evaluates the credit risk of its counterparties as well as its own credit risk. To date, Bancorp has not realized any losses due to a counterparty's inability to perform and the change in value of derivative assets and liabilities attributable to credit risk was not significant during 2016.

Below are the carrying values of assets measured at fair value on a recurring basis.

(in thousands)	Fair value at June 30, 2016			
	Total	Level 1	Level 2	Level 3
Assets				
Investment securities available-for-sale				
Government sponsored enterprise obligations	\$333,826	\$-	\$333,826	\$-

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Mortgage-backed securities - government agencies	170,703	-	170,703	-
Obligations of states and political subdivisions	62,021	-	62,021	-
Corporate equity securities	757	757	-	-
Total investment securities available-for-sale	567,307	757	566,550	-
Interest rate swaps	1,282	-	1,282	-
Total assets	\$568,589	\$757	\$567,832	\$ -
Liabilities				
Interest rate swaps	\$2,048	\$-	\$2,048	\$ -

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

(in thousands)	Fair value at December 31, 2015			
Assets	Total	Level 1	Level 2	Level 3
Investment securities available-for-sale				
U.S. Treasury and other U.S. government obligations	\$80,000	\$80,000	\$-	\$ -
Government sponsored enterprise obligations	251,893	-	251,893	-
Mortgage-backed securities - government agencies	169,628	-	169,628	-
Obligations of states and political subdivisions	63,702	-	63,702	-
Corporate equity securities	653	653	-	-
Total investment securities available-for-sale	565,876	80,653	485,223	-
Interest rate swaps	461	-	461	-
Total assets	\$566,337	\$80,653	\$485,684	\$ -
Liabilities				
Interest rate swaps	\$554	\$-	\$554	\$ -

Bancorp had no financial instruments classified within Level 3 of the valuation hierarchy for assets and liabilities measured at fair value on a recurring basis at June 30, 2016 or December 31, 2015.

MSRs are recorded at fair value upon capitalization, are amortized to correspond with estimated servicing income, and are periodically assessed for impairment based on fair value at the reporting date. Fair value is based on a valuation model that calculates the present value of estimated net servicing income. The model incorporates assumptions that market participants would use in estimating future net servicing income. These measurements are classified as Level 3. At June 30, 2016 and December 31, 2015 there was no valuation allowance for the mortgage servicing rights, as the fair value exceeded the cost. Accordingly, the MSRs are not included in either table below for June 30, 2016 or December 31, 2015. See Note 8 for more information regarding MSRs.

For impaired loans in the table below, the fair value is calculated as the carrying value of only loans with a specific valuation allowance, less the specific allowance. Fair value of impaired loans was primarily measured based on the value of the collateral securing these loans. Impaired loans are classified within Level 3 of the fair value hierarchy. Collateral may be real estate and/or business assets including equipment, inventory, and/or accounts receivable. Bancorp determines the value of the collateral based on independent appraisals performed by qualified licensed appraisers. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Appraised values are discounted for costs to sell and may be discounted

further based on management's historical knowledge, changes in market conditions from the date of the most recent appraisal, and/or management's expertise and knowledge of the customer and the customer's business. Such discounts by management are subjective and are typically significant unobservable inputs for determining fair value. As of June 30, 2016, total impaired loans with a valuation allowance were \$1.5 million, and the specific allowance totaled \$356 thousand, resulting in a fair value of \$1.1 million, compared with total impaired loans with a valuation allowance of \$2.6 million, and the specific allowance allocation totaling \$544 thousand, resulting in a fair value of \$2.1 million at December 31, 2015. Losses represent the change in specific allowances for the period indicated.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Other real estate owned (“OREO”), which is carried at the lower of cost or fair value, is periodically assessed for impairment based on fair value at the reporting date. Fair value is based on appraisals performed by external parties which use judgments and assumptions that are property-specific and sensitive to changes in the overall economic environment. Appraisals may be further discounted based on management’s historical knowledge and/or changes in market conditions from the date of the most recent appraisal. Many of these inputs are not observable and, accordingly, these measurements are classified as Level 3. For OREO in the table below, fair value is the carrying value of only parcels of OREO which have a carrying value equal to appraised value. Losses represent write-downs which occurred during the period indicated. At June 30, 2016 and December 31, 2015, carrying value of all other real estate owned was \$5.1 million and \$4.5 million, respectively.

Below are the carrying values of assets measured at fair value on a non-recurring basis.

(in thousands)	Fair value at June 30, 2016				Losses for 6 month period ended June 30, 2016
	Total	Level 1	Level 2	Level 3	
Impaired loans	\$1,099	\$ -	\$ -	\$1,099	\$ (173)
Other real estate owned	4,353	-	-	4,353	-
Total	\$5,452	\$ -	\$ -	\$5,452	\$ (173)

(in thousands)	Fair value at December 31, 2015				Losses for 6 month period ended June 30, 2015
	Total	Level 1	Level 2	Level 3	
Impaired loans	\$2,058	\$ -	\$ -	\$2,058	\$ (2,524)
Other real estate owned	3,782	-	-	3,782	(175)
Total	\$5,840	\$ -	\$ -	\$5,840	\$ (2,699)

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

For the securities portfolio, Bancorp monitors the valuation technique utilized by pricing agencies to ascertain when transfers between levels have occurred. The nature of other assets and liabilities measured at fair value is such that transfers in and out of any level are expected to be rare. For the three months ended June 30, 2016, there were no transfers between Levels 1, 2, or 3. For Level 3 assets measured at fair value on a non-recurring basis as of June 30, 2016, the significant unobservable inputs used in the fair value measurements are presented below.

(Dollars in thousands)	Fair Value	Valuation technique	Significant unobservable input	Weighted average of input	
Impaired loans - collateral dependent	\$1,099	Appraisal	Appraisal discounts (%)	10.1	%
Other real estate owned	4,353	Appraisal	Appraisal discounts	19.3	

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****(18) Disclosure of Financial Instruments Not Reported at Fair Value**

US GAAP requires disclosure of the fair value of financial assets and liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or nonrecurring basis. Carrying amounts, estimated fair values, and placement in the fair value hierarchy of Bancorp's financial instruments are as follows:

(in thousands) June 30, 2016	Carrying amount	Fair value	Level 1	Level 2	Level 3
Financial assets					
Cash and short-term investments	\$50,234	\$50,234	\$50,234	\$-	\$-
Mortgage loans held for sale	6,405	7,054	-	7,054	-
Federal Home Loan Bank stock and other securities	6,347	6,347	-	6,347	-
Loans, net	2,152,410	2,189,877	-	-	2,189,877
Accrued interest receivable	6,799	6,799	6,799	-	-
Financial liabilities					
Deposits	2,349,948	2,350,358	-	-	2,350,358
Short-term borrowings	171,591	171,591	-	171,591	-
FHLB advances	43,002	44,700	-	44,700	-
Accrued interest payable	132	132	132	-	-
(in thousands) December 31, 2015	Carrying amount	Fair value	Level 1	Level 2	Level 3
Financial assets					
Cash and short-term investments	\$103,833	\$103,833	\$103,833	\$-	\$-
Mortgage loans held for sale	6,800	7,112	-	7,112	-
Federal Home Loan Bank stock and other securities	6,347	6,347	-	6,347	-
Loans, net	2,010,566	2,021,776	-	-	2,021,776
Accrued interest receivable	6,610	6,610	6,610	-	-
Financial liabilities					
Deposits	2,371,702	2,371,300	-	-	2,371,300
Short-term borrowings	87,003	87,003	-	87,003	-
FHLB advances	43,468	43,647	-	43,647	-
Accrued interest payable	127	127	127	-	-

Management used the following methods and assumptions to estimate the fair value of each class of financial instrument for which it is practicable to estimate the value.

Cash, short-term investments, accrued interest receivable/payable and short-term borrowings

For these short-term instruments, carrying amount is a reasonable estimate of fair value.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Mortgage loans held for sale

Mortgage loans held for sale are initially recorded at the lower of cost or market value. The portfolio is comprised of residential real estate loans and fair value is determined by market quotes for similar loans based on loan type, term, rate, size and the borrower's credit score.

Federal Home Loan Bank stock and other securities

For these securities without readily available market values, carrying amount is a reasonable estimate of fair value as it equals the amount due from FHLB or other issuer at upon redemption.

Loans, net

US GAAP prescribes the exit price concept for estimating fair value of loans. Because there is not an active market (exit price) for trading virtually all types of loans in Bancorp's portfolio, fair value of loans is estimated by discounting future cash flows using current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities (entrance price).

Deposits

Fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date. Fair value of fixed-rate certificates of deposits is estimated by discounting future cash flows using the rates currently offered for deposits of similar remaining maturities.

Federal Home Loan Bank advances

Fair value of FHLB advances is estimated by discounting future cash flows using estimates of current market rate for instruments with similar terms and remaining maturities.

Commitments to extend credit and standby letters of credit

Fair values of commitments to extend credit are estimated using fees currently charged to enter into similar agreements and creditworthiness of customers. Fair values of standby letters of credit are based on fees currently charged for similar agreements or estimated cost to terminate them or otherwise settle obligations with counterparties at the reporting date. Fair value of commitments to extend credit, letters of credit and lines of credit is not presented since management believes the fair value to be insignificant.

Limitations

Fair value estimates are made at a specific point in time based on relevant market information and information about financial instruments. Because no market exists for a significant portion of Bancorp's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Therefore, calculated fair value estimates in many instances cannot be substantiated by comparison to independent markets and, in many cases, may not be realizable in a current sale of the instrument. Changes in assumptions could significantly affect estimates.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****(19) Regulatory Matters**

Bancorp and the Bank are subject to various capital requirements prescribed by banking regulations and administered by state and federal banking agencies. Under these requirements, Bancorp and the Bank must meet minimum amounts and percentages of Tier 1, common equity Tier 1, and total capital, as defined, to risk weighted assets and Tier 1 capital to average assets. Risk weighted assets are determined by applying certain risk weightings prescribed by the regulations to various categories of assets and off-balance sheet commitments. Capital and risk weighted assets may be further subject to qualitative judgments by regulators as to components, risk weighting and other factors. Failure to meet the capital requirements can result in certain mandatory, and possibly discretionary, corrective actions prescribed by the regulations or determined to be necessary by the regulators, which could materially affect the unaudited consolidated financial statements.

In 2013, the Federal Reserve Board and the FDIC approved rules that substantially amended the regulatory risk-based capital rules applicable to Bancorp and Bank. The rules implemented the regulatory capital reforms of the Basel Committee on Banking Supervision reflected in "Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems" (Basel III) and changes required by the Dodd-Frank Act. The Basel III regulatory capital reforms became effective for Bancorp and Bank on January 1, 2015, and include new minimum risk-based capital and leverage ratios. Bancorp and the Bank met all capital requirements to which they were subject as of June 30, 2016.

The following table sets forth consolidated Bancorp's and the Bank's risk based capital amounts and ratios as of June 30, 2016 and December 31, 2015.

(Dollars in thousands)	Actual		Minimum for adequately capitalized		Minimum for well capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
June 30, 2016						
Total risk-based capital (1)						
Consolidated	\$321,916	13.01%	\$197,950	8.00%	NA	NA
Bank	311,600	12.62	197,528	8.00	\$246,910	10.00%
Common equity tier 1 risk-based capital						
Consolidated	298,341	12.06	111,321	4.50	NA	NA
Bank	288,025	11.66	111,159	4.50	148,212	6.00
Tier 1 risk-based capital (1)						

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Consolidated	298,341	12.06	148,428	6.00	NA	NA
Bank	288,025	11.66	148,212	6.00	148,212	6.00
Leverage (2)						
Consolidated	298,341	10.46	114,088	4.00	NA	NA
Bank	288,025	10.10	114,069	4.00	142,587	5.00

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

(Dollars in thousands)	Actual		Minimum for adequately capitalized		Minimum for well capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2015						
Total risk-based capital (1)						
Consolidated	\$307,666	13.31 %	\$184,923	8.00 %	NA	NA
Bank	298,129	12.91	184,743	8.00	\$230,929	10.00 %
Common equity tier 1 risk-based capital						
Consolidated	284,793	12.32	104,023	4.50	NA	NA
Bank	275,256	11.92	103,914	4.50	138,552	6.00
Tier 1 risk-based capital (1)						
Consolidated	284,793	12.32	138,698	6.00	NA	NA
Bank	275,256	11.92	138,552	6.00	138,552	6.00
Leverage (2)						
Consolidated	284,793	10.53	108,183	4.00	NA	NA
Bank	275,256	10.19	108,049	4.00	135,062	5.00

(1)Ratio is computed in relation to risk-weighted assets.

(2)Ratio is computed in relation to average assets.

NA Not applicable. Regulatory framework does not define well capitalized for holding companies.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

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

This item discusses the results of operations for Stock Yards Bancorp, Inc. ("Bancorp" or "Company"), and its subsidiary, Stock Yards Bank & Trust Company ("Bank") for the three and six months ended June 30, 2016 and compares these periods with the same periods of the previous year. Unless otherwise indicated, all references in this discussion to the Bank include Bancorp. In addition, the discussion describes the significant changes in the financial condition of Bancorp and the Bank that have occurred during the first six months of 2016 compared with same periods in the year ended December 31, 2015. This discussion should be read in conjunction with the consolidated financial statements and accompanying notes presented in Part 1, Item 1 of this report.

This report contains forward-looking statements under the Private Securities Litigation Reform Act that involve risks and uncertainties. Although Bancorp believes assumptions underlying forward-looking statements contained herein are reasonable, any of these assumptions could be inaccurate. Factors that could cause actual results to differ from results discussed in forward-looking statements include, but are not limited to the following: economic conditions both generally and more specifically in markets in which Bancorp and the Bank operate; competition for Bancorp's customers from other providers of financial services; government legislation and regulation which change from time to time and over which Bancorp has no control; changes in interest rates; material unforeseen changes in liquidity, results of operations, or financial condition of Bancorp's customers; and other risks detailed in Bancorp's filings with the Securities and Exchange Commission, all of which are difficult to predict and many of which are beyond the control of Bancorp.

Overview of 2016 through June 30

Bancorp completed the first six months of 2016 with net income of \$19.9 million or 9.2% more than the comparable period of 2015. The increase is due to higher net interest income and non-interest income. These increases were partially offset by higher non-interest expenses and higher provision for loan losses. Diluted earnings per share for the first six months of 2016 were \$0.88, compared with the first six months of 2015 at \$0.82. Bancorp's performance for the first half of 2016 reflected several positive factors, including:

Strong organic net loan growth, accelerating from the pace set over the past two years;

Continued high credit quality;

Diverse sources of fee income contributing to revenue growth; and

Solid returns on average assets and equity of 1.41% and 13.52%, respectively.

As is the case with most banks, Bancorp's primary revenue source is net interest income and fees from various financial services provided to customers. Net interest income is the difference between interest income earned on loans, investment securities and other interest earning assets less interest expense on deposit accounts and other interest bearing liabilities. Loan volume and interest rates earned on those loans are critical to overall profitability. Similarly, deposit volume is crucial to funding loans and rates paid on deposits directly impact profitability. Business volumes are influenced by competition, new business acquisition efforts and economic factors including market interest rates, business spending, consumer confidence and competitive conditions within the marketplace.

Net interest income increased \$4.0 million, or 9.2%, for the first six months of 2016, compared with the same period in 2015. The positive effects of increased volumes on earning assets and lower costs on time deposits were partially offset by the negative effect of declining interest rates earned. Net interest margin declined to 3.58% for the first six months of 2016, compared with 3.73% for the same period of 2015.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

In response to assessment of risk in the loan portfolio, including net loan growth, Bancorp recorded a \$1.25 million provision for loan losses in the first six months of 2016, compared with no provision in the first six months of 2015. The provision for loan losses represents a charge to earnings necessary to establish an allowance for loan losses that, in management's evaluation, is adequate to provide coverage for the inherent losses on outstanding loans.

Total non-interest income in the first six months of 2016 increased \$968 thousand, or 4.9%, compared with the same period in 2015, and comprised 31% of total revenues. Bancorp experienced increases in virtually all areas of non-interest income.

Total non-interest expense in the first six months of 2016 increased \$3.1 million, or 8.4%, compared with the same period in 2015, largely due to increases in salaries and benefits and higher amortization expense of investments in tax credit partnerships. These expenses were partially offset by gains on sales of foreclosed assets and lower other non-interest expenses. Bancorp's efficiency ratio in the first six months of 2016 was 57.8% compared to 57.5% in the same period in 2015. Excluding amortization of the investments in tax credit partnerships, the adjusted efficiency ratio, a non-GAAP measure, would have been 54.9% and 57.0% for the first half of 2016 and 2015, respectively. See the Non-GAAP Financial Measures section for details on reconciliation to US GAAP measures.

Bancorp's effective tax rate decreased to 26.9% in 2016 from 31.5% in 2015. The decrease in the effective tax rate from 2015 to 2016 is largely the result of higher tax credits in 2016.

Tangible common equity (TCE), a non-GAAP measure, is a measure of a company's capital which is useful in evaluating the quality and adequacy of capital. The ratio of tangible common equity to total tangible assets was 10.42% as of June 30, 2016, compared with 10.10% at December 31, 2015. See the Non-GAAP Financial Measures section for details on reconciliation to US GAAP measures.

On April 29, 2016 Bancorp declared a 3 for 2 stock split to be effected as a 50% stock dividend to shareholders of record on May 13, 2016, payable May 27, 2016. Share and per share information has been adjusted for this dividend.

The following sections provide more details on subjects presented in this overview.

a) Results Of Operations

Record net income of \$10.1 million for the three months ended June 30, 2016 increased \$1.1 million, or 12.3%, from \$9.0 million for the comparable 2015 period. Basic net income per share was \$0.45 for the second quarter of 2016, an increase of 9.8% from the \$0.41 for the second quarter of 2015. Net income per share on a diluted basis was \$0.45 for the second quarter of 2016, an increase of 12.5% from the \$0.40 for the same period in 2015. Bancorp recorded a \$750 thousand provision for loan losses in the second quarter of 2016, compared with no provision in the same period of 2015. See Note 14 for additional information related to net income per share.

Annualized return on average assets and annualized return on average stockholders' equity were 1.42% and 13.53%, respectively, for the second quarter of 2016, compared with 1.45% and 13.30%, respectively, for the same period in 2015.

Net income of \$19.9 million for the six months ended June 30, 2016 increased \$1.7 million, or 9.2%, from \$18.3 million for the comparable 2015 period. Basic net income per share was \$0.89 for the first six months of 2016, an increase of 7.2% from the \$0.83 for the first six months of 2015. Net income per share on a diluted basis was \$0.88 for the first six months of 2016, an increase of 7.3% from the \$0.82 for the first six months of 2015. Bancorp recorded a \$1.25 million provision for loan losses in the first six months of 2016, compared with no provision in the same period of 2015.

Annualized return on average assets and annualized return on average stockholders' equity were 1.41% and 13.52%, respectively, for the first six months of 2016, compared with 1.47% and 13.73%, respectively, for the same period in 2015.

Net Interest Income

The following tables present the average balance sheets for the three and six month periods ended June 30, 2016 and 2015 along with the related calculation of tax-equivalent net interest income, net interest margin and net interest spread for the related periods. See the notes following the tables for further explanation.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****Average Balances and Interest Rates – Taxable Equivalent Basis**

(Dollars in thousands)	Three months ended June 30							
	2016				2015			
	Average	Interest	Average		Average	Interest	Average	
	balances		rate		balances		rate	
Earning assets:								
Federal funds sold	\$85,914	\$111	0.52	%	\$56,671	\$51	0.36	%
Mortgage loans held for sale	5,432	59	4.37		7,701	74	3.85	
Securities:								
Taxable	413,536	2,060	2.00		347,249	1,907	2.20	
Tax-exempt	61,739	438	2.85		59,605	421	2.83	
FHLB stock and other securities	6,347	63	3.99		6,347	62	3.92	
Loans, net of unearned income	2,132,390	22,646	4.27		1,879,982	20,719	4.42	
Total earning assets	2,705,358	25,377	3.77		2,357,555	23,234	3.95	
Less allowance for loan losses	22,847				24,693			
	2,682,511				2,332,862			
Non-earning assets:								
Cash and due from banks	40,075				37,877			
Premises and equipment	42,110				40,148			
Accrued interest receivable and other assets	93,928				87,790			
Total assets	\$2,858,624				\$2,498,677			
Interest bearing liabilities:								
Deposits:								
Interest bearing demand deposits	\$705,878	\$245	0.14	%	\$516,765	\$134	0.10	%
Savings deposits	134,644	12	0.04		118,893	11	0.04	
Money market deposits	643,898	358	0.22		634,862	321	0.20	
Time deposits	252,058	364	0.58		287,402	472	0.66	
Securities sold under agreements to repurchase	53,514	29	0.22		58,060	32	0.22	
Federal funds purchased and other short term borrowings	28,152	23	0.33		14,420	5	0.14	
FHLB advances	43,081	181	1.69		41,017	224	2.19	
Total interest bearing liabilities	1,861,225	1,212	0.26		1,671,419	1,199	0.29	
Non-interest bearing liabilities:								
Non-interest bearing demand deposits	664,069				532,526			
Accrued interest payable and other liabilities	32,777				23,255			
Total liabilities	2,558,071				2,227,200			
Stockholders' equity	300,553				271,477			
Total liabilities and stockholders' equity	\$2,858,624				\$2,498,677			

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Net interest income	\$24,165		\$22,035	
Net interest spread	3.51	%	3.66	%
Net interest margin	3.59	%	3.75	%

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

(Dollars in thousands)	Six months ended June 30								
	2016			2015					
	Average	Interest	Average	Average	Interest	Average			
	balances		rate	balances		rate			
Earning assets:									
Federal funds sold	\$114,797	\$300	0.53	% \$71,679	\$119	0.33	%		
Mortgage loans held for sale	4,840	119	4.94	5,678	113	4.01			
Securities:									
Taxable	417,061	4,151	2.00	352,641	3,877	2.22			
Tax-exempt	62,142	872	2.82	59,684	837	2.83			
FHLB stock and other securities	6,347	127	4.02	6,347	126	4.00			
Loans, net of unearned income	2,084,413	44,727	4.32	1,874,791	41,244	4.44			
Total earning assets	2,689,600	50,296	3.76	2,370,820	46,316	3.94			
Less allowance for loan losses	22,766			24,950					
	2,666,834			2,345,870					
Non-earning assets:									
Cash and due from banks	39,296			37,359					
Premises and equipment	40,911			39,832					
Accrued interest receivable and other assets	91,304			89,079					
Total assets	\$2,838,345			\$2,512,140					
Interest bearing liabilities:									
Deposits:									
Interest bearing demand deposits	\$716,252	\$503	0.14	% \$508,902	\$263	0.10	%		
Savings deposits	132,848	24	0.04	116,650	21	0.04			
Money market deposits	650,635	714	0.22	654,782	655	0.20			
Time deposits	257,678	734	0.57	296,821	972	0.66			
Securities sold under agreements to repurchase	56,193	62	0.22	61,185	69	0.23			
Federal funds purchased and other short term borrowings	25,804	38	0.30	15,142	12	0.16			
FHLB advances	43,198	368	1.71	38,907	440	2.28			
Total interest bearing liabilities	1,882,608	2,443	0.26	1,692,389	2,432	0.29			
Non-interest bearing liabilities:									
Non-interest bearing demand deposits	628,269			526,423					
Accrued interest payable and other liabilities	30,921			25,224					
Total liabilities	2,541,798			2,244,036					
Stockholders' equity	296,547			268,104					
Total liabilities and stockholders' equity	\$2,838,345			\$2,512,140					
Net interest income		\$47,853			\$43,884				
Net interest spread			3.50	%			3.65	%	
Net interest margin			3.58	%			3.73	%	

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Notes to the average balance and interest rate tables:

Net interest income, the most significant component of the Bank's earnings is total interest income less total interest expense. The level of net interest income is determined by mix and volume of interest earning assets, interest bearing deposits and borrowed funds, and changes in interest rates.

Net interest spread is the difference between the taxable equivalent rate earned on interest earning assets less the rate expensed on interest bearing liabilities.

Net interest margin represents net interest income on a taxable equivalent basis as a percentage of average interest earning assets. Net interest margin is affected by both interest rate spread and the level of non-interest bearing sources of funds, primarily consisting of demand deposits and stockholders' equity.

Interest income on a fully tax equivalent basis includes the additional amount of interest income that would have been earned if investments in certain tax-exempt interest earning assets had been made in assets subject to federal taxes yielding the same after-tax income. Interest income on municipal securities and tax-exempt loans has been calculated on a fully tax equivalent basis using a federal income tax rate of 35%. Approximate tax equivalent adjustments to interest income were \$215 thousand and \$234 thousand, respectively, for the three month periods ended June 30, 2016 and 2015 and \$434 thousand and \$469 thousand, respectively, for the six month periods ended June 30, 2016 and 2015.

Average balances for loans include the principal balance of non-accrual loans and exclude participation loans accounted for as secured borrowings. These participation loans averaged \$10.1 million and \$7.9 million, respectively, for the three month periods ended June 30, 2016 and 2015 and \$8.6 million and \$8.0 million, respectively, for the six month periods ended June 30, 2016 and 2015.

Fully taxable equivalent net interest income of \$24.2 million for the three months ended June 30, 2016 increased \$2.1 thousand, or 9.7%, from \$22.0 million when compared with the same period last year. The positive effects of increased volumes on loans and lower costs on time deposits were partially offset by the negative effect of declining interest rates earned on loans. Net interest spread and net interest margin were 3.51% and 3.59%, respectively, for the second quarter of 2016 and 3.66% and 3.75%, respectively, for the second quarter of 2015.

Fully taxable equivalent net interest income of \$47.9 million for the six months ended June 30, 2016 increased \$4.0 million, or 9.0%, from \$43.9 million when compared with the same period last year. The positive effects of increased

volumes on earning assets and lower costs on time deposits were partially offset by the negative effect of declining interest rates earned. Net interest spread and net interest margin were 3.50% and 3.58%, respectively, for the first six months of 2016 and 3.65% and 3.73%, respectively, for the first six months of 2015.

Average earning assets increased \$318.8 million or 13.4%, to \$2.69 billion for the first six months of 2016 compared with 2015, reflecting growth in the loan portfolio and investment securities. Average interest bearing liabilities increased \$190.2 million, or 11.2%, to \$1.88 billion for the first six months of 2016 compared with 2015 primarily due to increases in interest bearing demand and savings deposits, federal funds purchased and FHLB advances, partially offset by decreases in time deposits, money market deposits and securities sold under agreements to repurchase.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Asset/Liability Management and Interest Rate Risk

Managing interest rate risk is fundamental for the financial services industry. The primary objective of interest rate risk management is to neutralize effects of interest rate changes on net income. By considering both on and off-balance sheet financial instruments, management evaluates interest rate sensitivity while attempting to optimize net interest income within the constraints of prudent capital adequacy, liquidity needs, market opportunities and customer requirements.

Interest Rate Simulation Sensitivity Analysis

Bancorp uses an earnings simulation model to estimate and evaluate the impact of an immediate change in interest rates on earnings in a one year forecast. The simulation model is designed to reflect the dynamics of interest earning assets, interest bearing liabilities and off-balance sheet financial instruments. By estimating the effects of interest rate increases and decreases, the model can reveal approximate interest rate risk exposure. The simulation model is used by management to gauge approximate results given a specific change in interest rates at a given point in time. The model is therefore a tool to indicate earnings trends in given interest rate scenarios and does not indicate actual expected results.

Bancorp assumes certain correlation rates, often referred to as a “beta” of interest-bearing deposits, wherein the rates paid to customers change at a different pace when compared with changes in benchmark interest rates. Generally, certificates of deposit are assumed to have a high correlation rate, while interest-bearing checking accounts are assumed to have a lower correlation rate. Actual results may differ due to factors including competitive pricing and money supply; however, Bancorp uses its historical experience as well as industry data to inform its assumptions.

The June 30, 2016 simulation analysis, which shows little interest rate sensitivity, indicates that an increase in interest rates of 100 to 200 basis points would have a negative effect on net interest income, and a decrease of 100 basis points in interest rates would also have a negative impact. These estimates are summarized below.

**Net
interest
income**

change

Increase 200bp	(2.75)%
Increase 100bp	(2.00)
Decrease 100bp	(3.28)
Decrease 200bp	N/A

Management expects that net interest margin will remain under pressure through 2016, and any near-term increases in prevailing interest rates would not immediately benefit Bancorp. Approximately 64% of its loan portfolio has fixed rates and 13% of its loan portfolio is priced at variable rates with floors of 4% or higher. Since the prime rate is currently 3.50%, a rise in rates would have a negative impact on net interest income until rates increase more than 50 bps and the rates on such loans would rise to compensate for higher interest costs. This effect is captured in the simulation analysis above. The extent of margin compression also will be affected by the need to respond to competitive pressures on funding sources.

The scenario of rates decreasing 200 bp is not reasonably possible given current low rates for short-term instruments and most deposits.

Undesignated derivative instruments described in Note 7 are recognized on the consolidated balance sheet at fair value, with changes in fair value, due to changes in prevailing interest rates, recorded in other non-interest income. Because of matching terms of offsetting contracts, in addition to collateral provisions which mitigate the impact of non-performance risk, changes in fair value subsequent to initial recognition have a minimal effect on earnings, and are therefore not included in the simulation analysis results above.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Derivatives designated as cash flow hedges described in Note 7 are recognized on the consolidated balance sheet at fair value, with changes in fair value, due to changes in prevailing interest rates, recorded net of tax in other comprehensive income.

Provision for Loan Losses

The provision for loan losses represents a charge to earnings necessary to establish an allowance for loan losses that, in management's evaluation, is adequate to provide coverage for inherent losses on outstanding loans. The allowance for loan losses is calculated after considering credit quality factors, and ultimately relies on an overall internal analysis of risk in the loan portfolio. Based on this analysis, the provision for loan losses is determined and recorded. The provision reflects an allowance methodology that is driven by risk ratings, historical losses, and qualitative factors. Bancorp recorded a \$1.25 million provision for loan losses in the first six months of 2016, compared with no provision for the same period of 2015.

Management utilizes loan grading procedures which result in specific allowance allocations for estimated inherent risk of loss. For all loans graded, but not individually reviewed for allowance purposes, a general allowance allocation is computed using historical data based on actual loss experience. Specific and general allocations plus consideration of qualitative factors represent management's best estimate of probable losses contained in the loan portfolio at the evaluation date. Although the allowance for loan losses is comprised of specific and general allocations, the entire allowance is available to absorb any credit losses. Based on this detailed analysis of credit risk, management considers the allowance for loan losses adequate to cover probable losses inherent in the loan portfolio at June 30, 2016.

An analysis of the changes in the allowance for loan losses and selected ratios for the three and six month periods ended June 30, 2016 and 2015 follows:

(Dollars in thousands)	Three months ended		Six months ended June	
	June 30,		30,	
	2016	2015	2016	2015
Balance at the beginning of the period	\$22,451	\$24,882	\$22,441	\$24,920
Provision for loan losses	750	-	1,250	-
Loan charge-offs, net of recoveries	(60)	(1,574)	(550)	(1,612)
Balance at the end of the period	\$23,141	\$23,308	\$23,141	\$23,308

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Average loans, net of unearned income	\$2,142,530		\$1,887,913		\$2,092,990		\$1,882,782	
Provision for loan losses to average loans (1)	0.04	%	0.00	%	0.06	%	0.00	%
Net loan charge-offs to average loans (1)	0.00	%	0.08	%	0.03	%	0.09	%
Allowance for loan losses to average loans	1.08	%	1.23	%	1.11	%	1.24	%
Allowance for loan losses to period-end loans	1.06	%	1.23	%	1.06	%	1.23	%

(1) Amounts not annualized

Loans are charged off when deemed uncollectible and a loss is identified or after underlying collateral has been liquidated; however, collection efforts may continue and future recoveries may occur. Periodically, loans are partially charged off to net realizable value based upon collateral analysis and collection status.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

An analysis of net charge-offs by loan category for the three and six month periods ended June 30, 2016 and 2015 follows:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Net loan charge-offs (recoveries)				
Commercial and industrial	\$41	\$1,311	\$357	\$1,316
Construction and development, excluding undeveloped land	-	-	(10)	-
Undeveloped land	-	-	-	-
Real estate mortgage - commercial investment	(157)	231	(158)	231
Real estate mortgage - owner occupied commercial	130	(12)	313	(11)
Real estate mortgage - 1-4 family residential	(2)	(2)	(1)	49
Home equity	-	12	-	8
Consumer	48	34	49	19
Total net loan charge-offs	\$60	\$1,574	\$550	\$1,612

Non-interest Income and Expenses

The following table sets forth major components of non-interest income and expenses for the three and six month periods ended June 30, 2016 and 2015.

(In thousands)	Three months ended June 30,			Six months ended June 30,			
	2016	2015	% Change	2016	2015	% Change	
Non-interest income:							
Investment management and trust services	\$4,807	\$4,651	3.4	% \$9,419	\$9,203	2.3	%
Service charges on deposit accounts	2,262	2,199	2.9	4,408	4,279	3.0	
Bankcard transaction revenue	1,433	1,246	15.0	2,743	2,368	15.8	
Mortgage banking revenue	1,030	913	12.8	1,824	1,741	4.8	
Brokerage commissions and fees	538	499	7.8	981	960	2.2	
Bank owned life insurance income	220	226	-2.7	441	448	-1.6	
Other	488	485	0.6	1,044	893	16.9	
Total non-interest income	\$10,778	\$10,219	5.5	% \$20,860	\$19,892	4.9	%

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Non-interest expenses:								
Salaries and employee benefits	\$11,971	\$11,383	5.2	%	\$24,166	\$22,483	7.5	%
Net occupancy expense	1,546	1,450	6.6		3,070	2,919	5.2	
Data processing expense	1,881	1,756	7.1		3,425	3,210	6.7	
Furniture and equipment expense	291	260	11.9		576	507	13.6	
FDIC insurance expense	351	317	10.7		679	614	10.6	
Amortization of investment in tax credit partnerships	1,016	159	539.0		2,031	317	540.7	
Other	3,137	3,542	-11.4		5,786	6,596	-12.3	
Total non-interest expenses	\$20,193	\$18,867	7.0	%	\$39,733	\$36,646	8.4	%

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

The largest component of non-interest income is investment management and trust (“IM&T”) revenue. The magnitude of IM&T revenue distinguishes Bancorp from other community banks of similar asset size. Assets under management, stated at market value, totaled \$2.34 billion at June 30, 2016, compared with \$2.29 billion at June 30, 2015. IM&T services revenue, which constitutes an average of 45% of non-interest income, increased \$156 thousand, or 3.4%, in the second quarter of 2016, and \$216 thousand, or 2.3% for the first six months, as compared with the same periods in 2015. Recurring fees, which generally comprise over 95% of the investment management and trust revenue, increased \$57 thousand, or 1%, for the first six months of 2016, compared with the same period of 2015. Most recurring fees earned for managing accounts are based on a percentage of market value on a monthly basis. Some revenues of the IM&T department, most notably executor, insurance, and some employee benefit plan-related fees, are non-recurring in nature and the timing of these revenues corresponds with the related administrative activities. Total non-recurring fees increased \$159 thousand for the first six months of 2016, compared with the same period in 2015. Management believes the IM&T department will continue to factor significantly in Bancorp’s financial results and provide strategic diversity to revenue streams.

Service charges on deposit accounts increased \$63 thousand, or 2.9%, in the second quarter of 2016, and \$129 thousand, or 3.0%, for the first six months of 2016, as compared with the same periods in 2015. Service charge income is driven by transaction volume, which can fluctuate throughout the year. A significant component of service charges is related to fees earned on overdrawn checking accounts. Management expects this source of revenue to slowly decline due to anticipated changes in customer behavior and ongoing regulatory restrictions.

Bankcard transaction revenue increased \$187 thousand, or 15.0%, in the second quarter of 2016, and \$375 thousand, or 15.8% for the first six months of 2016, compared with the same periods in 2015, and primarily represents income the Bank derives from customers’ use of debit and credit cards. Interchange income on debit cards increased \$17 thousand, or 1.4%, and \$62 thousand, or 2.6%, for the first six months of 2016, compared with 2015, as a result of increased volume. However, Bancorp expects a slight decrease in interchange rates on debit cards as service providers gravitate to lower cost options in a competitive market. Late in 2015, Bancorp began offering credit cards to business customers. Income on credit cards totaled \$172,000 in the second quarter and \$314,000 for the first six months of 2016. Bancorp expects volume of credit card transactions to increase slowly as customers are added.

Mortgage banking revenue primarily includes gains on sales of mortgage loans. Bancorp’s mortgage banking department originates residential mortgage loans to be sold in the secondary market. Interest rates on the loans sold are locked with the borrower and investor prior to closing the loans, thus Bancorp bears no interest rate risk related to these loans. The department offers conventional, VA and FHA financing, for purchases and refinances, as well as programs for first-time home buyers. Interest rates on mortgage loans directly impact the volume of business transacted by the mortgage banking department. Mortgage banking revenue increased \$117 thousand, or 12.8%, in the second quarter of 2016, and \$83 thousand or 4.8%, for the first six months of 2016, as compared with the same periods in 2015, attributable mainly to slightly higher sales prices on loans. Rates declined in 2016 compared with the

same period in 2015, but lower rates were not enough to stimulate refinance activity at a level previously experienced. Bancorp experienced a slight increase in purchase transactions, but it was virtually offset by a decrease in refinance activity.

Brokerage commissions and fees increased \$39 thousand, or 7.8%, in the second quarter of 2016, and \$21 thousand or 2.2% for the first six months of 2016, as compared with the same periods in 2015, corresponding to overall brokerage volume. Brokerage commissions and fees earned consist primarily of stock, bond and mutual fund sales as well as wrap fees on accounts. Wrap fees are charges for investment programs that bundle together a suite of services, such as brokerage, advisory, research and management, and are based on a percentage of assets. Bancorp deploys its brokers primarily through its branch network via an arrangement with a third party broker-dealer, while larger managed accounts are serviced in the Bank's IM&T department.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Bank Owned Life Insurance (BOLI) income totaled \$220 thousand and \$226 thousand for the second quarter of 2016 and 2015, respectively, and totaled \$441 thousand and \$448 thousand for the first six months of 2016 and 2015, respectively. BOLI represents the cash surrender value for life insurance policies on certain key employees who have provided consent for Bancorp to be the beneficiary of a portion of such policies. The related change in cash surrender value and any death benefits received under the policies are recorded as non-interest income. This income helps offset the cost of various employee benefits.

Other non-interest income was virtually flat for the second quarter of 2016, and increased \$151 thousand, or 16.9%, in the first six months of 2016, as compared with the same periods in 2015. Included in this category is swap fee income, which totaled \$231 thousand for the first six months of 2016. Bancorp earned no swap fee income in the first six months of 2015. Opportunities to earn swap fee income are infrequent due to the specialized nature of the transactions. This category includes a variety of other factors, none of which resulted in individually significant variances.

Salaries and employee benefits increased \$588 thousand, or 5.2%, for the second quarter of 2016, and \$1.7 million, or 7.5% for the first six months of 2016, as compared with the same periods of 2015. For the second quarter and the first six months, the increase is largely due to higher compensation expenses, reflecting both increased incentive compensation related to accelerated loan and earnings growth as well as the addition of personnel associated with continued expansion in the Cincinnati and Indianapolis markets. To a lesser extent, Bancorp had some additional compensation expense due to new hires in anticipation of expected retirement of certain officers. These increases were partially offset by lower health insurance costs. At June 30, 2016, Bancorp had 549 full-time equivalent employees compared with 538 at June 30, 2015.

Net occupancy expense increased \$96 thousand, or 6.6%, in the second quarter of 2016, and \$151 thousand, or 5.2%, for the first six months of 2016, as compared with the same periods of 2015. The increase was largely due to higher rent and depreciation for locations added during 2015 and increased maintenance expense company-wide.

Data processing expense increased \$125 thousand, or 7.1% in the second quarter of 2016, and \$215 thousand, or 6.7% for the first six months of 2016, compared with the same periods of 2015. The increase for the first six months of 2016 is largely due to increases in expenses for computer maintenance and bank card processing/reissuance. This category includes ongoing computer software amortization and maintenance related to investments in technology needed to maintain and improve the quality of delivery channels and internal resources.

Edgar Filing: Stock Yards Bancorp, Inc. - Form 10-Q

Furniture and equipment expense increased \$31 thousand, or 11.9% for the second quarter of 2016, and \$69 thousand, or 13.6% for the first six months of 2016, as compared with the same periods in 2015. These fluctuations relate to a variety of factors, none of which were individually significant. Costs of capital asset additions flow through the statement of income over the lives of the assets in the form of depreciation expense.

FDIC insurance expense increased \$34 thousand, or 10.7%, for the second quarter of 2016, and \$65 thousand or 10.6% for the first six months of 2016, as compared with the same periods in 2015. The assessment is calculated by the FDIC and adjusted quarterly. The increase in expense is due primarily to higher level of net assets driven by loan growth.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Amortization of investments in tax credit partnerships increased \$857 thousand for the second quarter of 2016, and \$1.7 million for the first six months of 2016, compared with the same periods of 2015. This expense reflects amortization of investments in partnerships which generate historic and New Market income tax credits and varies widely depending upon the timing of investments and related amortization. See the Income Taxes section below for details on amortization and income tax impact for these credits.

Other non-interest expenses decreased \$405 thousand or 11.4% in the second quarter of 2016, and \$810 thousand or 12.3% for the first six months of 2016, as compared with the same periods in 2015. The decreases for the six month period are largely due to \$189 thousand of net gains on sales of foreclosed assets in 2016 compared with \$163 thousand of net losses in 2015. Additionally, Bancorp reduced the reserve for estimated losses on unfunded commitments by \$45 thousand in the first six months of 2016, compared with a provision expense of \$202 thousand in 2015. This reserve is based on evaluation of credit risk related to available credit in the loan portfolio. MSR amortization declined \$250 thousand for the first six months of 2016 compared with 2015, as pools of MSRs added several years ago were fully amortized in 2015. This category also includes legal and professional fees, advertising, printing, mail and telecommunications, none of which had individually significant variances.

Income Taxes

For the first six months of 2016, Bancorp recorded income tax expense of \$7.4 million, compared with \$8.4 million for the same period in 2015. The effective rate for the six month period was 26.9% in 2016 and 31.5% in 2015. The decrease in the effective tax rate from 2015 to 2016 is largely the result of higher utilization of tax credits in 2016.

Bancorp invests in certain partnerships that yield low-income housing, historic and New Market income tax credits. The tax benefits and related investment amortization expenses for low-income housing credits are recognized in income tax expense using a proportional amortization method which amortizes the investment in proportion to the tax credits and other tax benefits received. The amortization method for investments in new markets and historic tax credit partnerships is the cost method which matches the amortization period with the time frame over which the credits are realized. For each of Bancorp's investments in tax credit partnerships, when taken as a whole, the tax benefit compared with the amortization results in a positive effect on net income.

Commitments

Bancorp uses a variety of financial instruments in the normal course of business to meet the financial needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. A discussion of Bancorp's commitments is included in Note 10.

Other commitments discussed in Bancorp's Annual Report on Form 10-K for the year ended December 31, 2015, have not materially changed since that report was filed, relative to qualitative and quantitative disclosures of fixed and determinable contractual obligations.

b) Financial Condition

Balance Sheet

Total assets increased \$92.7 million, or 3.3%, from \$2.82 billion on December 31, 2015 to \$2.91 billion on June 30, 2016. Loans grew \$142.5 million in the first six months of 2016 as a result of loan production which outpaced what had been record production in 2015. All of this growth has been organic and, importantly, each of Bancorp's three markets continues to participate in the accelerated lending activity. Securities available-for-sale increased \$1.4 million. Included in securities available-for-sale are short term obligations of U.S. Treasury or U.S. government sponsored entities. These securities, which totaled \$100 million at June 30, 2016 and December 31, 2015, normally have a maturity of less than one month, and are purchased at quarter-end as part of a tax minimization strategy.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

Total liabilities increased \$74.2 million, or 2.9%, from \$2.53 billion on December 31, 2015 to \$2.60 billion on June 30, 2016. Deposits decreased \$21.8 million or 0.9% due to seasonal fluctuations. Securities sold under agreement to repurchase decreased \$7.1 million or 11.0% due to normal cyclical activity. Federal funds purchased and other short-term borrowing increased \$91.7 million. Bancorp utilizes short-term lines of credit to manage its overall liquidity position. Other liabilities increased \$11.8 million or 42.2% largely due to an increase in secured borrowing related to participation loans. See the Elements of Loan Portfolio section below on details related to participations loans.

Elements of Loan Portfolio

The following table sets forth the major classifications of the loan portfolio.

(in thousands)

Loans by Type	June 30, 2016	December 31, 2015
Commercial and industrial	721,956	\$644,398
Construction and development, excluding undeveloped land	136,029	134,482
Undeveloped land (1)	20,342	21,185
Real estate mortgage:		
Commercial investment	572,438	528,290
Owner occupied commercial	333,862	329,365
1-4 family residential	240,770	226,575
Home equity - first lien	52,360	50,115
Home equity - junior lien	65,999	63,066
Subtotal: Real estate mortgage	1,265,429	1,197,411
Consumer	31,795	35,531
Total Loans	\$2,175,551	\$2,033,007

(1) Undeveloped land consists of land acquired for development by the borrower, but for which no development has yet taken place.

Bancorp occasionally enters into loan participation agreements with other banks to diversify credit risk. For certain sold participation loans, Bancorp has retained effective control of the loans, typically by restricting the participating institutions from pledging or selling their share of the loan without permission from Bancorp. US GAAP requires the participated portion of these loans to be recorded as secured borrowings. These participated loans are included in the

commercial and industrial and real estate mortgage loan totals above, and a corresponding liability is recorded in other liabilities. At June 30, 2016 and December 31, 2015, the total participated portions of loans of this nature were \$16.6 million and \$7.2 million, respectively.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****Non-performing Loans and Assets**

Information summarizing non-performing assets, including non-accrual loans follows:

(Dollars in thousands)	June 30, 2016	December 31, 2015		
Non-accrual loans	\$4,970	\$ 7,693		
Troubled debt restructuring	1,020	1,060		
Loans past due 90 days or more and still accruing	410	176		
Non-performing loans	6,400	8,929		
Foreclosed real estate	5,093	4,541		
Non-performing assets	\$11,493	\$ 13,470		
Non-performing loans as a percentage of total loans	0.29	%	0.44	%
Non-performing assets as a percentage of total assets	0.40	%	0.48	%

The following table sets forth the major classifications of non-accrual loans:

(in thousands)	June 30, 2016	December 31, 2015
Non-accrual loans by type		
Commercial and industrial	\$1,794	\$ 3,643
Construction and development, excluding undeveloped land	-	-
Undeveloped land	-	-
Real estate mortgage - commercial investment	280	278
Real estate mortgage - owner occupied commercial	1,635	2,761
Real estate mortgage - 1-4 family residential	977	906
Home equity and consumer loans	284	105
Total loans	\$4,970	\$ 7,693

c) Liquidity

The role of liquidity management is to ensure funds are available to meet depositors' withdrawal and borrowers' credit demands while at the same time maximizing profitability. This is accomplished by balancing changes in demand for funds with changes in the supply of those funds. Liquidity is provided by short-term liquid assets that can be converted to cash, investment securities available-for-sale, various lines of credit available to Bancorp, and the ability to attract funds from external sources, principally deposits. Management believes it has the ability to increase deposits at any time by offering rates slightly higher than market rate.

Bancorp's most liquid assets are comprised of cash and due from banks, available-for-sale marketable investment securities and federal funds sold. Federal funds sold totaled \$9.7 million at June 30, 2016. These investments normally have overnight maturities and are used for general daily liquidity purposes. The fair value of the available-for-sale investment portfolio was \$567.3 million at June 30, 2016. The portfolio includes maturities of approximately \$134.8 million over the next twelve months, including \$100 million of short-term securities which matured in July 2016. Combined with federal funds sold, these offer substantial resources to meet either new loan demand or reductions in Bancorp's deposit funding base. Bancorp pledges portions of its investment securities portfolio to secure public fund deposits, cash balances of certain investment management and trust accounts, and securities sold under agreements to repurchase. At June 30, 2016, total investment securities pledged for these purposes comprised 56% of the available-for-sale investment portfolio, leaving \$247.8 million of unpledged securities.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

Bancorp has a large base of non-maturity customer deposits, defined as demand, savings, and money market deposit accounts. At June 30, 2016, such deposits totaled \$2.10 billion and represented 89% of Bancorp's total deposits. Because these deposits are less volatile and are often tied to other products of Bancorp through long lasting relationships they do not put heavy pressure on liquidity. However, many of Bancorp's customers' deposit balances are historically high. When market conditions improve, these balances will likely decrease, putting some strain on Bancorp's liquidity position. As of June 30, 2016, Bancorp had \$498 thousand or 0.02% of total deposits, in brokered deposits.

Included in the total deposit balances at June 30, 2016 is \$133.4 million of public funds deposits, generally comprised of accounts from local government agencies and public school districts in our markets. As a result of property tax collections in the latter part of each year and some subsequent deployment, these accounts have an estimated remaining \$20 million of seasonal excess balances, which are expected to decline over the next three to six months. While this excess liquidity is maintained in low-yielding short-term investments and consequently results in lower net interest margin, it has a positive impact on net interest income.

Other sources of funds available to meet daily needs include FHLB advances. As a member of the FHLB of Cincinnati, Bancorp has access to credit products offered by the FHLB. Bancorp views these borrowings as a low cost alternative to other time deposits. At June 30, 2016, available credit from the FHLB totaled \$306.9 million. Additionally, Bancorp had available federal funds purchased lines with correspondent banks totaling \$39 million at June 30, 2016.

Bancorp's principal source of cash revenues is dividends paid to it as sole shareholder of the Bank. At June 30, 2016, the Bank may pay up to \$70.2 million in dividends to Bancorp without regulatory approval subject to the ongoing capital requirements of the Bank.

d) Capital Resources

At June 30, 2016, stockholders' equity totaled \$305.1 million, an increase of \$18.5 million since December 31, 2015. See the Consolidated Statement of Changes in Stockholders' Equity for further detail of the changes in equity since the end of 2015. One component of equity is accumulated other comprehensive income which, for Bancorp, consists of net unrealized gains or losses on securities available-for-sale and hedging instruments, as well as a minimum pension liability, each net of taxes. Accumulated other comprehensive income was \$5.5 million at June 30, 2016 compared with \$632 thousand on December 31, 2015. The \$4.8 million increase is primarily a reflection of the positive effect of the changing interest rate environment during the first six months of 2016 on the valuation of Bancorp's portfolio of

securities available-for-sale.

53

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

The following table sets forth Bancorp's and the Bank's risk based capital ratios as of June 30, 2016 and December 31, 2015.

	June 30, 2016	December 31, 2015	
Total risk-based capital (1)			
Consolidated	13.01 %	13.31	%
Bank	12.62	12.91	
Common equity tier 1 risk-based capital (1)			
Consolidated	12.06	12.32	
Bank	11.66	11.92	
Tier 1 risk-based capital (1)			
Consolidated	12.06	12.32	
Bank	11.66	11.92	
Leverage (2)			
Consolidated	10.46	10.53	
Bank	10.10	10.19	

Under the banking agencies risk-based capital guidelines, assets and credit-equivalent amounts of derivatives and off-balance sheet exposures are assigned to broad risk categories. The aggregate dollar amount in each risk (1) category is multiplied by the associated risk weight of the category. The resulting weighted values are added together, resulting in the Bancorp's total risk-weighted assets. These ratios are computed in relation to average assets.

(2) Ratio is computed in relation to average assets

In 2013, the Federal Reserve Board and the FDIC approved rules that substantially amended the regulatory risk-based capital rules applicable to Bancorp and Bank. The rules implemented the regulatory capital reforms of the Basel Committee on Banking Supervision reflected in "Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems" (Basel III) and changes required by the Dodd-Frank Act. The Basel III regulatory capital reforms became effective for Bancorp and Bank on January 1, 2015, and included new minimum risk-based capital and leverage ratios. The minimum capital level requirements applicable to bank holding companies and banks subject to the rules are:

- a common equity tier 1 capital ratio of 4.5%,
- a tier 1 risk-based capital ratio of 6% (increased from 4%),
- a total risk-based capital ratio of 8% (unchanged from current rules), and
- a tier 1 leverage ratio of 4% for all institutions.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

The rules also established a "capital conservation buffer" of 2.5%, to be phased in over three years through December 31, 2018, above the new regulatory minimum risk-based capital ratios, and will result in the following minimum ratios once the capital conservation buffer is fully phased in:

- a common equity tier 1 risk-based capital ratio of 7.0%,
- a tier 1 risk-based capital ratio of 8.5%, and
- a total risk-based capital ratio of 10.5%.

The rules allowed banks and their holding companies with less than \$250 billion in assets a one-time opportunity to opt-out of a requirement to include unrealized gains and losses in accumulated other comprehensive income in their capital calculation. Bancorp opted out of this requirement.

As of June 30, 2016, Bancorp meets the requirements to be considered well capitalized under the rules, and is not subject to limitations due to the capital conservation buffer.

e) Non-GAAP Financial Measures

In addition to capital ratios defined by banking regulators, Bancorp considers various ratios when evaluating capital adequacy and overhead, including tangible common equity to tangible assets, tangible common equity per share, and adjusted efficiency ratio, all of which are non-GAAP measures. Bancorp believes the tangible common equity ratios are important because of their widespread use by investors as means to evaluate capital adequacy, as they reflect the level of capital available to withstand unexpected market conditions. Because US GAAP does not include capital ratio measures, there are no US GAAP financial measures comparable to these ratios. In addition to the efficiency ratio normally presented, Bancorp considers an adjusted efficiency ratio. Bancorp believes excluding amortization of investments in tax credit partnerships from non-interest expense in this ratio is important because it provides a meaningful comparison to both prior periods and to other companies who do not invest in these partnerships.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

The following table reconciles Bancorp's calculation of tangible common equity to amounts reported under US GAAP.

(in thousands, except per share data)	June 30, 2016		December 31, 2015	
Total equity	\$305,051		\$286,519	
Less core deposit intangible	(1,500))	(1,601))
Less goodwill	(682))	(682))
Tangible common equity	\$302,869		\$284,236	
Total assets	\$2,909,519		\$2,816,801	
Less core deposit intangible	(1,500))	(1,601))
Less goodwill	(682))	(682))
Total tangible assets	\$2,907,337		\$2,814,518	
Total shareholders' equity to total assets	10.48	%	10.17	%
Tangible common equity ratio	10.42		10.10	
Number of outstanding shares	22,510		22,379	
Book value per share	\$13.55		\$12.80	
Tangible common equity per share	13.45		12.70	

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY**

The following table reconciles Bancorp's calculation of adjusted efficiency ratios to the ratio reported under US GAAP.

(amounts in thousands)	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Non-interest expense	\$20,193	\$18,867	\$39,733	\$36,646
Net interest income (tax-equivalent)	24,165	22,035	47,853	43,884
Non-interest income	10,778	10,219	20,860	19,892
Total revenue	\$34,943	\$32,254	\$68,713	\$63,776
Efficiency ratio	57.8 %	58.5 %	57.8 %	57.5 %

(amounts in thousands)	2016	2015	2016	2015
Non-interest expense	\$20,193	\$18,867	\$39,733	\$36,646
Less: amortization of investments in tax credit partnerships	(1,016)	(159)	(2,031)	(317)
Adjusted non-interest expense	19,177	18,708	37,702	36,329
Net interest income (tax-equivalent)	24,165	22,035	47,853	43,884
Non-interest income	10,778	10,219	20,860	19,892
Total revenue	\$34,943	\$32,254	\$68,713	\$63,776
Adjusted efficiency ratio	54.9 %	58.0 %	54.9 %	57.0 %

f) Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers*, which outlines a single comprehensive model for use in accounting for revenue arising from contracts with customers, and supersedes most current revenue recognition guidance. The ASU was originally effective for fiscal years and interim periods beginning after December 15, 2016. In August 2015, FASB issued ASU 2015-14 which delays the effective date. The effective date will be annual reporting periods beginning after December 15, 2017, and the interim periods within that year. Bancorp is evaluating the potential impact of adoption of ASU 2014-09.

In February 2016, FASB issued ASU No. 2016-02, *Leases*, which requires lessees to recognize the assets and liabilities that arise from leases on the balance sheet. A lessee should recognize on the balance sheet a liability to make

lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for lease term. The new guidance is effective for annual and interim reporting periods beginning after December 15, 2018. The amendment should be applied at the beginning of the earliest period presented using a modified retrospective approach with earlier application permitted as of the beginning of an interim or annual reporting period. Bancorp is evaluating the potential impact of adoption of ASU 2016-02.

Table Of Contents

STOCK YARDS BANCORP, INC. AND SUBSIDIARY

In March 2016, FASB issued ASU No. 2016-09, *Compensation – Stock Compensation*. The new guidance simplifies certain aspects related to income taxes, statement of cash flows, and forfeitures when accounting for share-based payment transactions. The new guidance is effective for annual and interim reporting periods beginning after December 15, 2016. Certain of the amendments related to timing of the recognition of tax benefits and tax withholding requirements should be applied using a modified retrospective transition method. Amendments related to the presentation of the statement of cash flows should be applied retrospectively. All other provisions may be applied on a prospective or modified retrospective basis. After adoption of the ASU, Bancorp would record the excess tax benefits related to stock compensation as a component of income tax expense rather than additional paid-in capital. For the year ended December 31, 2015, the excess tax benefit recorded to additional paid-in capital was \$673 thousand. Bancorp is considering the potential impact of early adoption of ASU 2016-09.

In June 2016, FASB issued ASU 2016-13, *Measurement of Credit Losses on Financial Instruments*, which significantly changes the way entities recognize impairment of many financial assets by requiring immediate recognition of estimated credit losses expected to occur over their remaining life. The new guidance is effective for annual and interim reporting periods beginning after December 15, 2019. Bancorp is evaluating the potential impact of adoption of ASU 2016-13.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Information required by this item is included in Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

Item 4. Controls and Procedures

Bancorp maintains disclosure controls and procedures designed to ensure that it is able to collect the information it is required to disclose in reports it files with the Securities and Exchange Commission (“SEC”), and to record, process, summarize and report this information within the time periods specified in the rules and forms of the SEC. Based on their evaluation of Bancorp’s disclosure controls and procedures as of the end of the quarterly period covered by this report, the Chief Executive and Chief Financial Officers believe that these controls and procedures are effective to ensure that Bancorp is able to collect, process and disclose the information it is required to disclose in reports it files with the SEC within the required time periods.

Based on the evaluation of Bancorp's disclosure controls and procedures by the Chief Executive and Chief Financial Officers, there were no significant changes during the quarter ended June 30, 2016 in Bancorp's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, Bancorp's internal control over financial reporting.

Table Of Contents**STOCK YARDS BANCORP, INC. AND SUBSIDIARY****PART II – OTHER INFORMATION****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table shows information relating to the repurchase of shares of common stock by Bancorp during the three months ended June 30, 2016.

	Total number of shares purchased (1)	Average price paid per share	Total number of shares purchased as part of publicly announced plan	Maximum number of shares that may yet be purchased under the plan
April 1 - April 30	296	\$ 25.87	—	—
May 1 - May 31	1,848	28.17	—	—
June 1 - June 30	—	—	—	—
Total	2,144	\$ 27.85	—	—

Activity represents shares of stock withheld to pay taxes due upon exercise of stock appreciation rights and vesting (1) of restricted stock. This activity has no impact on the number of shares that may be purchased under a Board-approved plan.

Item 6. Exhibits

The following exhibits are filed or furnished as a part of this report:

Exhibit Description of exhibit

Number

31.1 Certifications pursuant to Section 302 of the Sarbanes-Oxley Act by David P. Heintzman

31.2 Certifications pursuant to Section 302 of the Sarbanes-Oxley Act by Nancy B. Davis

32 Certifications pursuant to 18 U.S.C. Section 1350

101 The following financial statements from the Stock Yards Bancorp, Inc. June 30, 2016 Quarterly Report on Form 10-Q, filed on August 5, 2016, formatted in eXtensible Business Reporting Language (XBRL):

(1) Consolidated Balance Sheets

(2) Consolidated Statements of Income

(3) Consolidated Statements of Comprehensive Income

(4) Consolidated Statements of Changes in Stockholders' Equity

(5) Consolidated Statements of Cash Flows

(6) Notes to Consolidated Financial Statements

Table Of Contents

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.

STOCK YARDS BANCORP, INC.

By: /s/ David P. Heintzman

Date: August 5, 2016

David P. Heintzman, Chairman and Chief Executive Officer

By: /s/ Nancy B. Davis

Date: August 5, 2016

Nancy B. Davis, Executive Vice President, Treasurer and Chief Financial Officer