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FIRST MERCHANTS CORP
Form 10-Q
May 09, 2008

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

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

For the quarterly period ended March 31, 2008

OR

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

For the Transition Period from _____ to _____

Commission File Number 0-17071

First Merchants Corporation

(Exact name of registrant as specified in its charter)

Indiana

35-1544218

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

200 East Jackson Street
Muncie, IN

47305-2814

(Address of principal executive offices)

(Zip code)

(765) 747-1500

(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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer [] Accelerated filer [X] Non-accelerated filer []
Smaller reporting company []

(Do not check if smaller reporting company)

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

As of April 30, 2008, there were 18,204,227 outstanding common shares, without par value, of the registrant.

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PART I. FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

CONSOLIDATED CONDENSED BALANCE SHEETS

(Dollars in thousands, except per share amounts)

	March 31, 2008	December 31, 2007
	----- (Unaudited)	-----
ASSETS:		
Cash and due from banks	\$ 89,961	\$ 134,683
Interest-bearing deposits.....	21,280	24,931
Investment securities available for sale	415,638	440,836
Investment securities held to maturity	10,417	10,331
Mortgage loans held for sale.....	3,494	3,735
Loans, net of allowance for loan losses of \$29,094 and \$28,228.	2,908,616	2,848,615
Premises and equipment	44,526	44,445
Federal Reserve and Federal Home Loan Bank stock.....	25,345	25,250
Interest receivable	21,212	23,402
Core deposit intangibles	11,621	12,412
Goodwill	123,435	123,444
Cash surrender value of life insurance.....	71,663	70,970
Other assets	19,950	19,033
	-----	-----
Total assets	\$ 3,767,158	\$ 3,782,087
	=====	=====
LIABILITIES:		
Deposits:		
Noninterest-bearing	\$ 380,364	\$ 370,397
Interest-bearing	2,432,763	2,473,724
	-----	-----
Total deposits	2,813,127	2,844,121
Borrowings:		
Federal funds purchased	111,144	52,350
Securities sold under repurchase agreements	103,024	106,497
Federal Home Loan Bank Advances	244,468	294,101
Subordinated debentures, revolving credit lines and term loans	115,826	115,826
	-----	-----
Total borrowings	574,462	568,774
Interest payable	7,621	8,325

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Other liabilities.....	23,107	20,931
	-----	-----
Total liabilities	3,418,317	3,442,151
COMMITMENTS AND CONTINGENT LIABILITIES		
STOCKHOLDERS' EQUITY:		
Cumulative Preferred Stock, \$1,000 par value:		
Authorized -- 600 shares		
Issued and outstanding - 125 shares.....	125	
Preferred stock, no-par value:		
Authorized and unissued - 500,000 shares		
Common Stock, \$.125 stated value:		
Authorized -- 50,000,000 shares		
Issued and outstanding - 17,978,263 and 18,002,787 shares....	2,247	2,250
Additional paid-in capital	137,633	137,801
Retained earnings	206,710	202,750
Accumulated other comprehensive income/(loss).....	2,126	(2,865)
	-----	-----
Total stockholders' equity	348,841	339,936
	-----	-----
Total liabilities and stockholders' equity	\$ 3,767,158	\$ 3,782,087
	=====	=====

See notes to consolidated condensed financial statements.

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CONSOLIDATED CONDENSED STATEMENTS OF INCOME
(Dollars in thousands, except per share amounts)
(Unaudited)

	Three Months Ended March 31,	
	2008	2007
Interest Income:		
Loans receivable		
Taxable	\$51,101	\$49,645
Tax exempt	165	201
Investment securities		
Taxable	3,249	3,282
Tax exempt	1,513	1,661
Federal funds sold	8	1
Deposits with financial institutions	282	123
Federal Reserve and Federal Home Loan Bank stock	335	328
	-----	-----
Total interest income	56,653	55,241
	-----	-----
Interest Expense:		
Deposits	19,433	21,806

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Borrowings	6,411	6,360
	-----	-----
Total interest expense	25,844	28,166
	-----	-----
Net Interest Income	30,809	27,075
Provision for loan losses	3,823	1,599
	-----	-----
Net Interest Income After Provision for Loan Losses	26,986	25,476
	-----	-----
Other Income:		
Service charges on deposit accounts	2,931	2,883
Fiduciary activities	2,142	2,036
Other customer fees	1,679	1,491
Commission income	1,669	1,638
Earnings on cash surrender value of life insurance	738	685
Net gains and fees on sales of loans	643	532
Net realized gains/(losses) on sales of available-for-sale securities	73	(1)
Other income	652	540
	-----	-----
Total other income	10,527	9,804
	-----	-----
Other expenses:		
Salaries and benefits	16,098	14,726
Net occupancy	1,805	1,598
Equipment	1,654	1,722
Marketing	484	487
Outside data processing fees.....	882	951
Printing and office supplies.....	281	299
Core deposit amortization.....	790	791
Other expenses	4,279	3,620
	-----	-----
Total other expenses	26,273	24,194
	-----	-----
Income Before Income Tax	11,240	11,086
Income tax expense	3,114	3,315
	-----	-----
Net Income	\$ 8,126	\$ 7,771
	=====	=====
Per share:		
Basic	\$.45	\$.42
Diluted45	.42
Dividends23	.23

See notes to consolidated condensed financial statements.

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CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)

(Unaudited)

Three Months E
March 31

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	----- 2008 -----	-----
Net Income.....	\$ 8,126	\$
Other comprehensive income net of tax:		
Unrealized gains on securities available for sale:		
Unrealized holding gains arising during the period, net of income tax benefit of \$(1,824) and \$(298).....	3,388	
Unrealized gains on cash flow hedges:		
Unrealized gains arising during the period, net of income tax of \$(1,183) and \$(41)	1,774	
Amortization of items previously recorded in accumulated other comprehensive income, net of income tax expense of \$85 and \$0	(127)	
Reclassification adjustment for gains/(losses) included in net income, net of income tax expense of \$29 and \$0	(44)	
	----- 4,991 -----	
Comprehensive income	\$ 13,117	\$ =====

See notes to consolidated condensed financial statements.

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CONSOLIDATED CONDENSED STATEMENTS OF STOCKHOLDERS' EQUITY
(Dollars in thousands)
(Unaudited)

	2008 -----	2007 -----
Balances, January 1	\$ 339,936	\$ 327,325
Net income	8,126	7,771
Cash dividends on common stock	(4,166)	(4,260)
Other comprehensive income net of tax.....	4,991	616
Stock issued under dividend reinvestment and stock purchase plan	272	291
Stock options exercised, net	1,160	140
Tax benefit from stock options exercised	96	17

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Stock redeemed	(2,137)	(3,503)
Cumulative preferred stock issued	125	
Share-based compensation	438	251
	-----	-----
Balances, March 31	\$ 348,841	\$ 328,648
	=====	=====

See notes to consolidated condensed financial statements.

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CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(Dollars in thousands)
(Unaudited)

		Thru
		----- 2008 -----
Cash Flows From Operating Activities:		
Net income.....	\$	8,
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan losses.....		3,
Depreciation and amortization.....		1,
Share-based compensation.....		
Tax benefits from stock options exercised.....		
Mortgage loans originated for sale.....		(28,
Proceeds from sales of mortgage loans.....		29,
Change in interest receivable.....		2,
Change in interest payable.....		(
Other adjustments.....		1,

Net cash provided by operating activities.....	\$	16,

Cash Flows From Investing Activities:		
Net change in interest-bearing deposits.....	\$	3,
Purchases of		
Securities available for sale.....		(
Securities held to maturity.....		(
Proceeds from maturities of		
Securities available for sale.....		30,
Securities held to maturity.....		
Purchase of Federal Reserve and		
Federal Home Loan Bank Stock.....		
Purchase of bank owned life insurance		
Net change in loans.....		(63,
Other adjustments.....		(1,

Net cash used by investing activities.....	\$	(31,

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Cash Flows From Financing Activities:

Net change in		
Demand and savings deposits.....	\$	(11,
Certificates of deposit and other time deposits.....		(19,
Borrowings.....		62,
Repayment of borrowings.....		(57,
Cash dividends on common stock.....		(4,
Stock issued under dividend reinvestment and stock purchase plans.....		1,
Stock options exercised.....		1,
Cumulative preferred stock issued.....		
Tax benefit from stock options exercised.....		
Stock redeemed.....		(2,

Net cash used by financing activities.....		(29,

Net Change in Cash and Cash Equivalents.....		(44,
Cash and Cash Equivalents, January 1.....		134,

Cash and Cash Equivalents, March 31.....	\$	89,
		=====
 Additional cash flows information:		
Interest paid	\$	26
Income tax paid		1

See notes to consolidated condensed financial statements.

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Table dollars in thousands)

(Unaudited)

NOTE 1. General

Financial Statement Preparation

The significant accounting policies followed by First Merchants Corporation ("Corporation") and its wholly owned subsidiaries for interim financial reporting are consistent with the accounting policies followed for annual financial reporting. All adjustments, which are of a normal recurring nature and are in the opinion of management necessary for a fair statement of the results for the periods reported, have been included in the accompanying consolidated condensed financial statements.

The consolidated condensed balance sheet of the Corporation as of December 31, 2007 has been derived from the audited consolidated balance sheet of the Corporation as of that date. Certain information and note disclosures normally included in the Corporation's annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These consolidated condensed financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Corporation's Form 10-K annual report filed with the Securities and Exchange Commission. The results of operations for the three months ended March 31, 2008 are not necessarily indicative of the results to be expected for the year.

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NOTE 2. Share-Based Compensation

Stock options and restricted stock awards ("RSAs") have been issued to directors, officers and other management employees under the Corporation's 1994 Stock Option Plan and The 1999 Long-term Equity Incentive Plan. The stock options, which have a ten year life, become 100 percent vested ranging from three months to two years and are fully exercisable when vested. Option exercise prices equal the Corporation's common stock closing price on NASDAQ on the date of grant. RSAs provide for the issuance of shares of the Corporation's common stock at no cost to the holder and generally vest after three years. The RSAs vest only if the employee is actively employed by the Corporation on the vesting date and, therefore, any unvested shares are forfeited.

The Corporation's 2004 Employee Stock Purchase Plan ("ESPP") provides eligible employees of the Corporation and its subsidiaries an opportunity to purchase shares of common stock of the Corporation through annual offerings financed by payroll deductions. The price of the stock to be paid by the employees may not be less than 85 percent of the lesser of the fair market value of the Corporation's common stock at the beginning or at the end of the offering period. Common stock purchases are made annually and are paid through advance payroll deductions of up to 20 percent of eligible compensation.

SFAS 123(R) required the Corporation to begin recording compensation expense in 2006 related to unvested share-based awards outstanding as of December 31, 2005, by recognizing the unamortized grant date fair value of these awards over the remaining service periods of those awards, with no change in historical reported fair values and earnings. Awards granted after December 31, 2005 are valued at fair value in accordance with provisions of SFAS 123(R) and are recognized on a straight-line basis over the service periods of each award. To complete the exercise of vested stock options, RSA's and ESPP options, the Corporation generally issues new shares from its authorized but unissued share pool. Share-based compensation for the three months ended March 31, 2008 and 2007 totaled \$438,000 and \$251,000, respectively. Share based compensation has been recognized as a component of salaries and benefits expense in the accompanying Consolidated Condensed Statements of Income.

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Table dollars in thousands)

(Unaudited)

NOTE 2. Share-Based Compensation continued

The estimated fair value of the stock options granted during 2008 and in prior years was calculated using a Black Scholes option pricing model. The following summarizes the assumptions used in the 2008 Black Scholes model:

Risk-free interest rate	2.69%
Expected price volatility	32.13%
Dividend yield	3.68%
Forfeiture rate	5.00%
Weighted-average expected life, until exercise	6.53 years

The Black Scholes model incorporates assumptions to value share-based awards. The risk-free rate of interest, for periods equal to the expected life of the option, is based on a zero-coupon U.S. government instrument over a similar contractual term of the equity instrument. Expected price volatility is based on

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historical volatility of the Corporation's common stock. In addition, the Corporation generally uses historical information to determine the dividend yield and weighted-average expected life of the options, until exercise. Separate groups of employees that have similar historical exercise behavior with regard to option exercise timing and forfeiture rates are considered separately for valuation and attribution purposes.

Share-based compensation expense recognized in the Consolidated Condensed Statements of Income is based on awards ultimately expected to vest and is reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods, if actual forfeitures differ from those estimates. Pre-vesting forfeitures were estimated to be approximately 5 percent for the three months ended March 31, 2008, based on historical experience.

The following table summarizes the components of the Corporation's share-based compensation awards recorded as expense:

	Three Months March 31 2008	
	-----	-----
Stock and ESPP Options:		
Pre-tax compensation expense	\$ 181	\$
Income tax benefit	(15)	
	-----	-----
Stock and ESPP option expense, net of income taxes	\$ 166	\$
	=====	=====
Restricted Stock Awards:		
Pre-tax compensation expense	\$ 257	\$
Income tax benefit	(90)	
	-----	-----
Restricted stock awards expense, net of income taxes	\$ 167	\$
	=====	=====
Total Share-Based Compensation:		
Pre-tax compensation expense	\$ 438	\$
Income tax benefit	(105)	
	-----	-----
Total share-based compensation expense, net of income taxes	\$ 333	\$
	=====	=====

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As of March 31, 2008, unrecognized compensation expense related to stock options, RSAs and ESPP options totaling \$551,000, \$2,531,000 and \$46,000, respectively, is expected to be recognized over weighted-average periods of 1.42, 2.00 and 0.25 years, respectively.

Stock option activity under the Corporation's stock option plans as of March 31, 2008 and changes during the three months ended March 31, 2008 were as follows:

	Number of Shares	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (in Years)
	-----	-----	-----
Outstanding at January 1, 2008	1,054,430	\$ 24.30	
Granted	72,300	27.93	
Exercised	(100,722)	22.59	
Cancelled	(13,390)	22.32	

Outstanding at March 31, 2008	1,012,618	\$ 24.76	5.68
	=====		
Vested and Expected to Vest at March 31, 2008 ...	999,957	\$ 24.72	5.64
Exercisable at March 31, 2008	882,768	\$ 24.39	5.13

The weighted-average grant date fair value was \$6.54 for stock options granted during the three months ended March 31, 2008.

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Corporation's closing stock price on the last trading day of the first three months of 2008 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their stock options on March 31, 2008. The amount of aggregate intrinsic value will change based on the fair market value of the Corporation's common stock.

The aggregate intrinsic value of stock options exercised during the first three months of 2008 was \$502,000. Exercise of options during this same period resulted in cash receipts of \$1,160,000. The Corporation recognized a tax benefit of approximately \$96,000 in the first three months of 2008, related to the exercise of employee stock options and has been recorded as an increase to additional paid-in capital.

The following table summarizes information on unvested restricted stock awards outstanding as of March 31, 2008:

	Number of Shares	Weighted-Average Grant-Date Fair Value
	-----	-----
Unvested RSAs at January 1, 2008	98,027	\$ 27.12
Granted	61,525	27.81
Forfeited	(1,227)	25.67

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Vested	(488)		25.97

Unvested RSAs at March 31, 2008	157,837	\$	27.85
	=====		

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Table dollars in thousands)

(Unaudited)

NOTE 2. Share-Based Compensation continued

The grant date fair value of ESPP options was estimated at the beginning of the July 1, 2007 offering period and approximates \$184,000. The ESPP options vests during the twelve month period ending June 30, 2008. At March 31, 2008, total unrecognized compensation expense related to unvested ESPP options was \$46,000, which is expected to be recognized over a period of three months.

Note 3. Disclosures About Fair Value of Assets and Liabilities

Effective January 1, 2008, the Corporation adopted Statement of Financial Accounting Standards No. 157, Fair Value Measurements (FAS 157). FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 has been applied prospectively as of the beginning of the year.

FAS 157 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 market participants at the measurement date. FAS 157 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

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

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

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

Available-for-sale securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. There are no securities classified within Level 1 of the hierarchy. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Level 2 securities include treasury securities, agencies, mortgage backs, state and

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municipal, corporate obligations, and marketable equity securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy and include mortgage backed securities and corporate obligations.

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying balance sheet measured at fair value on a recurring basis and the level within the FAS 157 fair value hierarchy in which the fair value measurements fall at March 31, 2008.

	Fair Value	Fair Value Measurement	
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Available-for-sale securities	\$415,638		\$404,477

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Table dollars in thousands)

(Unaudited)

The following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying balance sheet using significant unobservable Level 3 inputs:

	Available-for-Sale Securities
Beginning balance	\$ 12,023
Total realized and unrealized gains and losses Included in other comprehensive income	(862)
Ending balance	\$ 11,161

There were no gains or losses included in the first quarter earnings attributable to the change in unrealized gains or losses related to assets and liabilities still held at March 31, 2008.

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

Impaired Loans

Loan impairment is reported when scheduled payments under contractual terms are

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deemed uncollectible. Impaired loans are carried at the present value of estimated future cash flows using the loan's existing rate, or the fair value of collateral if the loan is collateral dependent. A portion of the allowance for loan losses is allocated to impaired loans if the value of such loans is deemed to be less than the unpaid balance. If these allocations cause the allowance for loan losses to increase, such increase is reported as a component of the provision for loan losses. Loan losses are charged against the allowance when management believes the uncollectability of the loan is confirmed. During the first quarter of 2008, certain impaired loans were partially charged-off or re-evaluated, resulting in a remaining balance for these loans, net of specific reserve, of \$13,679,000 as of March 31, 2008. The valuation would be considered Level 3, consisting of appraisals of underlying collateral and discounted cash flow analysis.

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Table dollars in thousands)

(Unaudited)

NOTE 4. Investment Securities

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale at March 31, 2008				
U.S. Treasury	\$ 1,501	\$ 32		\$ 1,533
U.S. Government-sponsored agency securities.....	51,880	776		52,656
State and municipal	146,266	3,805	\$ 5	150,066
Mortgage-backed securities	190,303	4,199	187	194,315
Corporate obligations	13,700		2,146	11,554
Marketable equity securities.....	6,215		701	5,514
	-----	-----	-----	-----
Total available for sale	409,865	8,812	3,039	415,638
	-----	-----	-----	-----
Held to maturity at March 31, 2008				
State and municipal.....	10,405	453	113	10,745
Mortgage-backed securities.....	12			12
	-----	-----	-----	-----
Total held to maturity	10,417	453	113	10,757
	-----	-----	-----	-----
Total investment securities	\$420,282	\$ 9,265	\$ 3,152	\$426,395
	=====	=====	=====	=====

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale at December 31, 2007				
U.S. Treasury	\$ 1,501	\$ 18		\$ 1,519
U.S. Government-sponsored agency securities	67,793	240	\$ 98	67,935
State and municipal	150,744	2,324	156	152,912
Mortgage-backed securities	199,591	1,654	1,444	199,801
Corporate obligations	13,740		1,294	12,446

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Marketable equity securities	6,835		612	6,223
	-----	-----	-----	-----
Total available for sale	440,204	4,236	3,604	440,836
	-----	-----	-----	-----
Held to maturity at December 31, 2007				
State and municipal	10,317	237	298	10,256
Mortgage-backed securities	14			14
	-----	-----	-----	-----
Total held to maturity	10,331	237	298	10,270
	-----	-----	-----	-----
Total investment securities	\$450,535	\$ 4,473	\$ 3,902	\$451,106
	=====	=====	=====	=====

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Table dollars in thousands)

(Unaudited)

NOTE 5. Loans and Allowance

	March 31, 2008

Loans:	
Commercial and industrial loans	\$ 724,643
Agricultural production financing and other loans to farmers	123,314
Real estate loans:	
Construction	178,171
Commercial and farmland	961,431
Residential	728,956
Individuals' loans for household and other personal expenditures	174,857
Tax-exempt loans	11,646
Lease financing receivables, net of unearned income.....	8,438
Other loans	26,254

Allowance for loan losses.....	2,937,710 (29,094)

Total Loans.....	\$ 2,908,616
	=====

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Allowance for loan losses:	
Balances, January 1	\$ 28,228
Provision for losses	3,823
Recoveries on loans	913

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Loans charged off	(3,870)
Balances, March 31	\$ 29,094

Non Performing Assets:	March 31, 2008	December 31, 2007
Non-accrual loans.....	\$ 27,465	\$ 29,031
Renegotiated loans.....	142	145
Non performing loans (NPL).....	27,607	29,176
Real estate owned and repossessed assets.....	7,372	2,573
Non performing assets (NPA).....	34,979	31,749
90+ days delinquent.....	4,996	3,578
NPAS & 90+ days delinquent.....	\$ 39,975	\$ 35,327

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(Table dollars in thousands)

(Unaudited)

NOTE 6. Net Income Per Share

Basic net income per share is computed by dividing net income by the weighted-average shares outstanding during the reporting period. Diluted net income per share is computed by dividing net income by the combination of all dilutive common share equivalents, comprised of shares issuable under the Corporation's share-based compensation plans, and the weighted-average shares outstanding during the reporting period.

Dilutive common share equivalents include the dilutive effect of in-the-money share-based awards, which are calculated based on the average share price for each period using the treasury stock method. Under the treasury stock method, the exercise price of share-based awards, the amount of compensation expense, if any, for future service that the Corporation has not yet recognized, and the amount of estimated tax benefits that would be recorded in additional paid-in-capital when share-based awards are exercised, are assumed to be used to repurchase common stock in the current period.

	Three Months Ended March 2008		
Net Income	Weighted- Average Shares	Per Share Amount	Net Income

Basic net income per share:
Net income available to

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common stockholders.....	\$ 8,126	17,938,442	\$.45	\$ 7,
			=====	
Effect of dilutive stock options.....		116,525		
	-----	-----		-----
Diluted net income per share:				
Net income available to				
common stockholders				
and assumed conversions.....	\$ 8,126	18,054,967	\$.45	\$ 7,
	=====	=====	=====	=====

Stock options to purchase 571,407 and 610,971 shares for the three months ended March 31, 2008 and 2007 were not included in the earnings per share calculation because the exercise price exceeded the average market price.

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(Table dollars in thousands)
(Unaudited)

Note 7. Impact of Accounting Changes

EFFECT OF NEWLY ISSUED ACCOUNTING STANDARDS

Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (FAS 159) became effective for the Corporation on January 1, 2008. FAS 159 allows companies an option to report selected financial assets and liabilities at fair value. Because we did not elect the fair value measurement provision for any of our financial assets or liabilities, the adoption of SFAS 159 did not have any impact on our 2008 consolidated financial statements. Presently, we have not determined whether we will elect the fair value measurement provisions for future transactions.

Effective January 1, 2008, the Corporation adopted EITF 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements and EITF 06-10, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements. The adoption of EITF 06-4 and EITF 06-10 did not have any impact on our 2008 consolidated financial statements.

Future Accounting Matters

Financial Accounting Standards Board Statement No. 141 (SFAS 141R), "Business Combinations (Revised 2007)," was issued in December 2007 and replaces SFAS 141 which applies to all transactions and other events in which one entity obtains control over one or more other businesses. SFAS 141R requires an acquirer, upon initially obtaining control of another entity, to recognize the assets, liabilities and any non-controlling interest in the acquiree at fair value as of the acquisition date. Contingent consideration is required to be recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of that consideration may be determinable beyond a reasonable doubt. This fair value approach replaces the cost allocation process required under SFAS 141 whereby the cost of an acquisition was allocated to the individual asset acquired and liabilities assumed based on their estimated fair

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value. SFAS 141R requires acquirers to expense acquisition-related costs as incurred rather than allocating such costs to the assets acquired and liabilities assumed. Under SFAS 141R, the requirements of SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities," would have to be met in order to accrue for a restructuring plan in purchase accounting. Pre-acquisition contingencies are to be recognized at fair value, unless it is a non-contractual contingency that is not likely to materialize, in which case, nothing should be recognized in purchase accounting. Instead, that contingency would be subject to the probable and estimable recognition criteria under SFAS 5, "Accounting for Contingencies." The Corporation is evaluating the requirements of SFAS 141R to determine if it will have a significant impact on the Corporation's financial condition or results of operations.

Financial Accounting Standards Board Statement No. 160 (SFAS 160), "Noncontrolling Interest in Consolidated Financial Statements, an amendment of ARB Statement No. 51," was issued in December 2007 and establishes accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 clarifies that a non-controlling interest in a subsidiary, which is sometimes referred to as a minority interest, is an ownership interest in the consolidated entity that should be reported as a component of equity in the consolidated financial statements. Among other requirements, SFAS 160 requires consolidated net income to be reported at amounts that are attributable to both the parent and the non-controlling interest. It also requires disclosure, on the face of the consolidated income statement, of the amounts of consolidated net income attributable to the parent and to the non-controlling interest. SFAS 160 is effective for the Corporation on January 1, 2009 and is not expected to have a significant impact on the Corporation's financial statements.

Financial Accounting Standards Board Statement No. 161 (SFAS 161), "Disclosures About Derivative Instruments and Hedging Activities, an Amendment of FASB Statement No. 133," was issued in March 2008 and amends and expands the disclosure requirements of SFAS 133 to provide greater transparency about (i) how and why an entity uses derivative instruments, (ii) how derivative instruments and related hedge items are accounted for under SFAS 133 and its related interpretations, and (iii) how derivative instruments and related hedged items affect an entity's financial position, results of operations and cash flows. To meet those objectives, SFAS 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments and disclosures about credit-risk-related contingent features in derivative agreements. SFAS 161 is effective for the Corporation on January 1, 2009 and is not expected to have a significant impact on the Corporation's financial statements.

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

of Operations

FORWARD-LOOKING STATEMENTS

We from time to time include forward-looking statements in our oral and written communication. We may include forward-looking statements in filings with the Securities and Exchange Commission, such as this Form 10-Q, in other written materials and in oral statements made by senior management to analysts,

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investors, representatives of the media and others. We intend these forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and we are including this statement for purposes of these safe harbor provisions. Forward-looking statements can often be identified by the use of words like "believe", "continue", "pattern", "estimate", "project", "intend", "anticipate", "expect" and similar expressions or future or conditional verbs such as "will", "would", "should", "could", "might", "can", "may", or similar expressions. These forward-looking statements include:

- * statements of our goals, intentions and expectations;
- * statements regarding our business plan and growth strategies;
- * statements regarding the asset quality of our loan and investment portfolios; and
- * estimates of our risks and future costs and benefits.

These forward-looking statements are subject to significant risks, assumptions and uncertainties, including, among other things, the following important factors which could affect the actual outcome of future events:

- * fluctuations in market rates of interest and loan and deposit pricing, which could negatively affect our net interest margin, asset valuations and expense expectations;
- * adverse changes in the economy, which might affect our business prospects and could cause credit-related losses and expenses;
- * adverse developments in our loan and investment portfolios;
- * competitive factors in the banking industry, such as the trend towards consolidation in our market;
- * changes in the banking legislation or the regulatory requirements of federal and state agencies applicable to bank holding companies and banks like our affiliate banks;
- * acquisitions of other businesses by us and integration of such acquired businesses;
- * changes in market, economic, operational, liquidity, credit and interest rate risks associated with our business; and
- * the continued availability of earnings and excess capital sufficient for the lawful and prudent declaration and payment of cash dividends.

Because of these and other uncertainties, our actual future results may be materially different from the results indicated by these forward-looking statements. In addition, our past results of operations do not necessarily indicate our anticipated future results.

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of Operations continued

CRITICAL ACCOUNTING POLICIES

Generally accepted accounting principles are complex and require us to apply significant judgments to various accounting, reporting and disclosure matters. We must use assumptions and estimates to apply these principles where actual measurement is not possible or practical. For a complete discussion of our significant accounting policies, see "Notes to the Consolidated Financial Statements" in our Annual Report on Form 10-K for the year ended December 31, 2007. Certain policies are considered critical because they are highly dependent upon subjective or complex judgments, assumptions and estimates. Changes in such estimates may have a significant impact on the financial statements. We have reviewed the application of these policies with the Audit Committee of our Board of Directors.

We believe there have been no significant changes during the quarter ended March 31, 2008 to the items that we disclosed as our critical accounting policies and estimates in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2007.

BUSINESS SUMMARY

We are a diversified financial holding company headquartered in Muncie, Indiana. Since its organization in 1982, the Corporation has grown to include 65 banking center locations in 18 Indiana and 3 Ohio counties. In addition to its branch network, the Corporation's delivery channels include ATMs, check cards, interactive voice response systems and internet technology.

The Corporation's business activities are currently limited to one significant business segment, which is community banking. As of March 31, 2008, the Corporation's financial service affiliates included four nationally chartered banks: First Merchants Bank, National Association, First Merchants Bank of Central Indiana, National Association, Lafayette Bank and Trust Company, National Association and Commerce National Bank. The banks provide commercial and retail banking services. In addition, our trust company, multi-line insurance company and a title company provide trust asset management services, retail and commercial insurance agency services and title services, respectively.

Management believes that its vision, mission, culture statement and core values produce profitable growth for stockholders. Management also believes it is important to maintain a strong control environment as we continue to grow our businesses. Interest rate and market risks inherent in our asset and liability balances are managed within prudent ranges, while ensuring adequate liquidity and funding. Sound credit policies are maintained and interest rate and market risks inherent in our asset and liability balances are managed within prudent ranges, while ensuring adequate liquidity and funding.

RESULTS OF OPERATIONS

Net income for the three months ended March 31, 2008, equaled \$8,126,000, compared to \$7,771,000 in the same period of 2007. Diluted earnings per share were \$.45, an increase of 7.1 percent from the \$.42 reported for the first quarter 2007.

Annualized returns on average assets and average stockholders' equity for the three months ended March 31, 2008, were .86 percent and 9.43 percent, respectively, compared with .88 percent and 9.47 percent for the same period of

2007.

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CAPITAL

Our regulatory capital continues to exceed regulatory "well capitalized" standards. Tier I regulatory capital consists primarily of total stockholders' equity and subordinated debentures issued to business trusts categorized as qualifying borrowings, less non-qualifying intangible assets and unrealized net securities gains. Our Tier I capital to average assets ratio was 7.3 percent at March 31, 2008 and 7.2 percent at year end 2007. In addition, at March 31, 2008, we had a Tier I risk-based capital ratio of 8.6 percent and total risk-based capital ratio of 11.2 percent. Regulatory capital guidelines require a Tier I risk-based capital ratio of at least 4.0 percent and a total risk-based capital ratio of at least 8.0 percent.

Our GAAP capital ratio, defined as total stockholders' equity to total assets, equaled 9.3 percent at March 31, 2008 and 9.0 percent at December 31, 2007. When we acquire other companies for stock, GAAP capital increases by the entire amount of the purchase price.

Our tangible capital ratio, defined as total stockholders' equity less intangibles net of tax to total assets less intangibles net of tax, equaled 6.0 percent as of March 31, 2008, and 5.7 percent at December 31, 2007.

We believe that all of the above capital ratios are meaningful measurements for evaluating our safety and soundness. Additionally, we believe the following table is also meaningful when considering our performance measures. The table details and reconciles tangible earnings per share, return on tangible capital and tangible assets to traditional GAAP measures.

(Dollars in thousands)	March 31, 2008 =====	December 31, 2007 =====
Average goodwill	\$ 123,435	\$ 123,191
Average core deposit intangible (CDI)	11,978	13,868
Average deferred tax on CDI	(3,178)	(3,659)
	-----	-----
Intangible adjustment	\$ 132,235	\$ 133,400
	=====	=====
Average stockholders' equity (GAAP capital)	\$ 344,780	\$ 330,786
Intangible adjustment	(132,235)	(133,400)
	-----	-----
Average tangible capital	\$ 212,545	\$ 197,386
	=====	=====
Average assets	\$ 3,758,491	\$ 3,639,772
Intangible adjustment	(132,235)	(133,400)
	-----	-----
Average tangible assets	\$ 3,626,256	\$ 3,506,372
	=====	=====

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Net income	\$	8,126	\$	31,639
CDI amortization, net of tax		480		1,919
		-----		-----
Tangible net income	\$	8,606	\$	33,558
		=====		=====
Diluted earnings per share	\$.45	\$	1.73
Diluted tangible earnings per share	\$.48	\$	1.83
Return on average GAAP capital		9.43%		9.56%
Return on average tangible capital		16.42%		17.00%
Return on average assets86%		.87%
Return on average tangible assets95%		.96%

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ASSET QUALITY/PROVISION FOR LOAN LOSSES

Our primary business focus is middle market commercial and residential real estate, auto and small consumer lending, which results in portfolio diversification. We ensure that appropriate methods to understand and underwrite risk are utilized. Commercial loans are individually underwritten and judgmentally risk rated. They are periodically monitored and prompt corrective actions are taken on deteriorating loans. Retail loans are typically underwritten with statistical decision-making tools and are managed throughout their life cycle on a portfolio basis.

The allowance for loan losses is maintained through the provision for loan losses, which is a charge against earnings. The amount provided for loan losses and the determination of the adequacy of the allowance are based on a continuous review of the loan portfolio, including an internally administered loan "watch" list and an ongoing loan review. The evaluation takes into consideration identified credit problems, as well as the possibility of losses inherent in the loan portfolio that are not specifically identified.

At March 31, 2008, non-performing assets, which includes nonaccrual loans, restructured loans, and other real estate owned totaled \$34,979,000, an increase of \$3,203,000 from December 31, 2007 as noted in Note 5 Loans and Allowance, included within the Notes to Consolidated Condensed Financial Statements of this Form 10Q. Other real estate owned increased \$4,799,000 from December 31, 2007, primarily due to one borrower. Non-performing loans will increase or decrease going forward due to portfolio growth, routine problem loan recognition and resolution through collections, sales or charge-offs. The performance of any loan can be affected by external factors, such as economic conditions, or factors particular to a borrower, such as actions of a borrower's management.

At March 31, 2008, impaired loans totaled \$93,718,000, an increase of \$6,769,000 from December 31, 2007. At March 31, 2008, an allowance for losses was not deemed necessary for impaired loans totaling \$71,890,000, as there was no identified loss on these credits. An allowance of \$6,121,000 was recorded for the remaining balance of impaired loans of \$21,828,000 and is included in our allowance for loan losses. The increase of total impaired loans is primarily due to the increase of performing, substandard classified loans, which comprise a portion of our total impaired loans. A loan is deemed impaired when, based on current information or events, it is probable all amounts due of principle interest according to the contractual terms of the loan agreement will not be

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collected. All of our criticized loans, including substandard, doubtful and loss credits, are included in the impaired loan total.

At March 31, 2008, the allowance for loan losses was \$29,094,000, an increase of \$866,000 from year end 2007. As a percent of loans, the allowance was .99 percent at March 31, 2008 and .98 percent at December 31, 2007.

The provision for loan losses for the first three months of 2008 was \$3,823,000, an increase of \$2,224,000 from \$1,599,000 for the same period in 2007. The increase from the prior quarter was a result of increased net charge offs of \$1,637,000. The determination of the provision in any period is based on management's continuing review and evaluation of the loan portfolio, and its judgment as to the impact of current economic conditions on the portfolio. The evaluation by management includes consideration of past loan loss experience, changes in the composition of the loan portfolio, and the current condition and amount of loans outstanding.

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LIQUIDITY

Liquidity management is the process by which we ensure that adequate liquid funds are available for us and our subsidiaries. These funds are necessary in order to meet financial commitments on a timely basis. These commitments include withdrawals by depositors, funding credit obligations to borrowers, paying dividends to shareholders, paying operating expenses, funding capital expenditures, and maintaining deposit reserve requirements. Liquidity is monitored and closely managed by our asset/liability committee.

Our liquidity is dependent upon our receipt of dividends from our bank subsidiaries, which are subject to certain regulatory limitations and access to other funding sources. Liquidity of our bank subsidiaries is derived primarily from core deposit growth, principal payments received on loans, the sale and maturity of investment securities, net cash provided by operating activities, and access to other funding sources.

The most stable source of liability-funded liquidity for both the long-term and short-term is deposit growth and retention in the core deposit base. In addition, we utilize advances from the Federal Home Loan Bank ("FHLB") and a revolving line of credit with LaSalle Bank, N.A. as funding sources. At March 31, 2008, total borrowings from the FHLB were \$244,468,000. Our bank subsidiaries have pledged certain mortgage loans and investments to the FHLB. The total available remaining borrowing capacity from the FHLB at March 31, 2008, was \$35,029,000. At March 31, 2008, our revolving line of credit had no balance and a remaining borrowing capacity of \$25,000,000. On February 15, 2008, we paid down the outstanding \$25,000,000 balance on the revolving line of credit through an increase of the subordinated debenture with LaSalle.

The principal source of asset-funded liquidity is investment securities classified as available-for-sale, the market values of which totaled \$415,638,000 at March 31, 2008, a decrease of \$25,198,000 or 5.7 percent below December 31, 2007. Securities classified as held-to-maturity that are maturing within a short period of time can also be a source of liquidity. Securities classified as held-to-maturity and that are maturing in one year or less totaled \$1,033,000 at March 31, 2008. In addition, other types of assets such as cash and due from banks, federal funds sold and securities purchased under agreements to resell, and loans and interest-bearing deposits with other banks maturing within one year are sources of liquidity.

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In the normal course of business, we are a party to a number of other off-balance sheet activities that contain credit, market and operational risk that are not reflected in whole or in part in our consolidated financial statements. Such activities include: traditional off-balance sheet credit-related financial instruments, commitments under operating leases and long-term debt.

We provide customers with off-balance sheet credit support through loan commitments and standby letters of credit. Summarized credit-related financial instruments at March 31, 2008 are as follows:

(Dollars in thousands)	At March 31, 2008
=====	
Amounts of commitments:	
Loan commitments to extend credit	\$ 764,722
Standby letters of credit	25,009

	\$ 789,731
	=====

Since many of the commitments are expected to expire unused or be only partially used, the total amount of unused commitments in the preceding table does not necessarily represent future cash requirements.

In addition to owned banking facilities, we have entered into a number of long-term leasing arrangements to support our ongoing activities. The required payments under such commitments and borrowings at March 31, 2008 are as follows:

(Dollars in thousands)	2008 remaining	2009	2010	2011	2012	2013 and after	2014 and after
=====							
Operating leases	\$ 1,253	\$ 1,420	\$ 1,190	\$ 961	\$ 606	\$ 79	\$ 5
Borrowings	234,794	55,348	58,071	18,944	65,874	141,431	5
	-----	-----	-----	-----	-----	-----	-----
Total	\$236,047	\$ 56,768	\$ 59,261	\$ 19,905	\$ 66,480	\$141,510	\$5
	=====	=====	=====	=====	=====	=====	=====

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INTEREST SENSITIVITY AND DISCLOSURES ABOUT MARKET RISK

Asset/Liability Management has been an important factor in our ability to record consistent earnings growth through periods of interest rate volatility and product deregulation. Management and the Board of Directors monitor our liquidity and interest sensitivity positions at regular meetings to review how changes in interest rates may affect earnings. Decisions regarding investments and the pricing of loan and deposit products are made after analysis of reports designed to measure liquidity, rate sensitivity, our exposure to changes in net interest income given various rate scenarios and the economic and competitive environments.

It is our objective to monitor and manage risk exposure to net interest income caused by changes in interest rates. It is the goal of our Asset/Liability function to provide optimum and stable net interest income. To accomplish this,

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we use two asset liability tools. GAP/Interest Rate Sensitivity Reports and Net Interest Income Simulation Modeling are both constructed, presented, and monitored quarterly.

We believe that our liquidity and interest sensitivity position at March 31, 2008, remained adequate to meet our primary goal of achieving optimum interest margins while avoiding undue interest rate risk.

Net interest income simulation modeling, or earnings-at-risk, measures the sensitivity of net interest income to various interest rate movements. Our asset liability process monitors simulated net interest income under three separate interest rate scenarios; base, rising and falling. Estimated net interest income for each scenario is calculated over a 12-month horizon. The immediate and parallel changes to the base case scenario used in the model are presented on the following page. The interest rate scenarios are used for analytical purposes and do not necessarily represent our view of future market movements. Rather, these are intended to provide a measure of the degree of volatility interest rate movements may introduce into our earnings.

The base scenario is highly dependent on numerous assumptions embedded in the model, including assumptions related to future interest rates. While the base sensitivity analysis incorporates our best estimate of interest rate and balance sheet dynamics under various market rate movements, the actual behavior and resulting earnings impact will likely differ from that projected. For mortgage-related assets, the base simulation model captures the expected prepayment behavior under changing interest rate environments. Assumptions and methodologies regarding the interest rate or balance behavior of indeterminate maturity products, e.g., savings, money market, NOW and demand deposits, reflect our best estimate of expected future behavior.

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The comparative rising and falling scenarios below assume further interest rate changes in addition to the base simulation discussed above. These changes are immediate and parallel changes to the base case scenario. In addition, total rate movements (beginning point minus ending point) to each of the various driver rates utilized by us in the base simulation are as follows:

Driver Rates	RISING	FALLING
Prime	200 Basis Points	(200) Basis Points
Federal Funds	200	(200)
One-Year CMT	200	(156)
Three-Year CMT	200	(182)
Five-Year CMT	200	(200)
CD's	200	(158)
FHLB Advances	200	(200)

Results for the base, rising and falling interest rate scenarios are listed below, based upon our rate sensitive assets and liabilities at March 31, 2008. The net interest income shown represents cumulative net interest income over a 12-month time horizon. Balance sheet assumptions used for the base scenario are the same for the rising and falling simulations.

BASE RISING FALLING
(Dollars in thousands)

=====

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Net Interest Income	\$123,123	\$123,353	\$119,882
Variance from base		\$ 230	\$ (3,241)
Percent of change from base		(0.2)%	(2.6)%

The comparative rising and falling scenarios below assume further interest rate changes in addition to the base simulation discussed above. These changes are immediate and parallel changes to the base case scenario. In addition, total rate movements (beginning point minus ending point) to each of the various driver rates utilized by us in the base simulation are as follows:

Driver Rates	RISING	FALLING
Prime	200 Basis Points	(200) Basis Points
Federal Funds	200	(200)
One-Year CMT	200	(200)
Two-Year CMT	200	(200)
Three-Year CMT	200	(200)
Five-Year CMT	200	(200)
CD's	200	(193)
FHLB Advances	200	(200)

Results for the base, rising and falling interest rate scenarios are listed below, based upon our rate sensitive assets and liabilities at December 31, 2007. The net interest income shown represents cumulative net interest income over a 12-month time horizon. Balance sheet assumptions used for the base scenario are the same for the rising and falling simulations.

	BASE	RISING	FALLING
	(Dollars in thousands)		
Net Interest Income	\$117,693	\$120,089	\$116,063
Variance from base		\$ 2,396	\$ (1,630)
Percent of change from base		2.0 %	(1.4)%

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EARNING ASSETS

The following table presents the earning asset mix as of March 31, 2008, and December 31, 2007. Earning assets increased by \$31,958,000 in the three months ended March 31, 2008. Loans and loans held for sale increased by \$60,626,000. The three largest loan segments that increased were in commercial and industrial at \$61,492,000, commercial and farmland at \$14,197,000, and real estate construction at \$12,746,000. Loan segments that decreased were residential real estate of \$15,671,000 and loans to individuals of \$13,023,000. Investments decreased by \$25,000,000 as lower yielding investments matured and were reinvested in higher yielding loans.

EARNING ASSETS

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(Dollars in thousands)	March 31, 2008	December 2007
Interest-bearing time deposits	\$21,280	\$24,93
Investment securities available for sale	415,638	440,83
Investment securities held to maturity	10,417	10,33
Mortgage loans held for sale	3,494	3,73
Loans	2,937,710	2,876,84
Federal Reserve and Federal Home Loan Bank stock	25,345	25,25
	-----	-----
Total	\$3,413,884	\$3,381,92
	=====	=====

DEPOSITS AND BORROWINGS

The table below reflects the level of deposits and borrowed funds (federal funds purchased; repurchase agreements; Federal Home Loan Bank advances; and subordinated debentures, revolving credit lines and term loans) based on period ending amounts as of March 31, 2008 and December 31, 2007.

(Dollars in thousands)	March 31, 2008	December 31, 2007
Deposits	\$2,813,127	\$2,844,121
Federal funds purchased.....	111,144	52,350
Securities sold under repurchase agreements.....	103,024	106,497
Federal Home Loan Bank advances	244,468	294,101
Subordinated debentures, revolving credit lines, term loans and other	115,826	115,826
	-----	-----
	\$3,387,589	\$3,412,895
	=====	=====

We have continued to leverage our capital position with Federal Home Loan Bank advances, as well as repurchase agreements which are pledged against acquired investment securities as collateral for the borrowings. The interest rate risk is included as part of our interest simulation discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations under the headings "LIQUIDITY" and "INTEREST SENSITIVITY AND DISCLOSURES ABOUT MARKET RISK".

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NET INTEREST INCOME

Net Interest Income is the primary source of our earnings. It is a function of net interest margin and the level of average earning assets. The table below presents our asset yields, interest expense, and net interest income as a

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percent of average earning assets for the three months ended March 31, 2008 and 2007.

During the three months ended March 31, 2008, asset yields decreased 23 basis points on a fully taxable equivalent basis (FTE) and interest costs decreased 47 basis points (FTE), resulting in an 24 basis point (FTE) increase in net interest income as compared to the same period in 2007.

	Three Months Ended March 31,	
(Dollars in Thousands)	2008	2007
Annualized net interest income.....	\$ 123,237	\$ 108,302
Annualized FTE adjustment.....	\$ 3,615	\$ 4,010
Annualized net interest income On a fully taxable equivalent basis.....	\$ 126,852	\$ 112,312
Average earning assets.....	\$3,396,641	\$3,209,807
Interest income (FTE) as a percent of average earning assets.....	6.78%	7.01%
Interest expense as a percent of average earning assets.....	3.04%	3.51%
Net interest income (FTE) as a percent of average earning assets.....	3.74%	3.50%

Average earning assets include the average balance of securities classified as available for sale, computed based on the average of the historical amortized cost balances without the effects of the fair value adjustment. In addition, annualized amounts are computed utilizing a 30/360 day basis.

HEDGING ACTIVITIES

On August 1, 2006, the Corporation purchased three prime-based interest rate floor agreements with an aggregate notional amount of \$250 million and strike rates ranging from 6% to 7%. The combined purchase price of approximately \$550,000 was to be amortized on an allocated fair value basis over the three-year term of the agreements. On March 19, 2008, the Corporation received \$5,216,000 in connection with the termination of the three interest rate floor agreements. The contractual maturity of the floors was August 1, 2009. During the life of the floors, pre-tax gains of approximately \$4,662,500 were deferred in accumulated other comprehensive income (AOCI) in accordance with cash flow hedge accounting rules established by SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities (as amended). The amounts deferred in AOCI will be reclassified out of equity into earnings over the remaining sixteen months of the original contract. SFAS 133 requires that amounts deferred in AOCI be reclassified into earnings in the same periods during which the originally hedged cash flows (prime-based interest payments on loan assets) affects earnings, as long as the originally hedged cash flows remain probable of occurring (i.e. the principal amount of designated prime-based loans match or exceed the notional amount of the terminated floor through August 1, 2009). If the principal amount of the originally hedged loans falls below the notional

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amount of the terminate floors, then amounts in AOCI could be accelerated. The Corporation decided to terminate the interest rate floor agreements only after considering the impact of the transaction on its risk management objectives and after alternative strategies were in place to mitigate the adverse impact of falling interest rates on its net interest margin. At March 31, 2008, the remaining pre-tax gains are approximately \$4.2 million.

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OTHER INCOME

Total other income in the first three months of 2008 was \$723,000 or 7.4 percent higher than the same period of 2007.

Four items primarily account for the change:

1. Gains of \$277,000 related to the termination of three interest rate floor agreements occurred in the first quarter of 2008.
2. Other customer fees up \$188,000 due to increased fees to customers and increased interchange fees.
3. Net gains and fees on sales of mortgages loans increased \$111,000 due to additional loans sold in the secondary market.
4. Trust fees increased \$106,000 as a result of increased trust business.

OTHER EXPENSES

Other expenses in the first three months of 2008 were \$2,079,000 or 8.6 percent higher than the same period in 2007.

Two items primarily account for the change:

1. Salary and employee benefit expenses were \$1,372,000 higher in the first quarter of 2008, as compared to the same period in 2007 primarily due to staff additions and normal annual increases. Approximately \$187,000 of the increase is due to increases in share-based compensation expense.
2. Expenses related to other real estate owned and repossessed assets were \$193,000 higher in 2008 than in the same period in 2007.

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INCOME TAXES

Income tax expense, for the three months ended March 31, 2008, decreased by \$201,000 from the same period in 2007. The effective tax rate was 27.7 and 29.9 percent for the 2008 and 2007 periods.

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OTHER

The Securities and Exchange Commission maintains a Web site that contains reports, proxy and information statements and other information regarding registrants that file electronically with the Commission, including us, and that address is (<http://www.sec.gov>).

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The information required under this item is included as part of Management's Discussion and Analysis of Financial Condition and Results of Operations, under the headings "LIQUIDITY" and "INTEREST SENSITIVITY AND DISCLOSURES ABOUT MARKET RISK".

Item 4. Controls and Procedures

At the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective. Disclosure controls and procedures are controls and procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934 are recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

There have been no changes in our internal controls over financial reporting identified in connection with the evaluation referenced above that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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FIRST MERCHANTS CORPORATION
FORM 10-Q
PART II. OTHER INFORMATION

Item 1. Legal Proceedings

None

Item 1.A. Risk Factors

There have been no material changes from the risk factors previously disclosed in the Corporation's December 31, 2007 Annual Report on Form 10-K.

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

- a. None
- b. None

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c. Issuer Purchases of Equity Securities

The following table presents information relating to our purchases of equity securities during the quarter ended March 31, 2008, as follows(1):

PERIOD	TOTAL NUMBER OF SHARES PURCHASED	AVERAGE PRICE PAID PER SHARE	TOTAL NUMBER OF SHARES PURCHASED AS PART OF PUBLICLY ANNOUNCED PLANS OR PROGRAMS	MA APPROX OF SH BE THE
01/01/08 - 01/31/08	103,443(1)	\$22.64	95,000	3
02/01/08 - 02/29/08	30,308(2)	26.87	0	3
03/01/08 - 03/31/08	1,983(2)	29.44	0	3

(1) On December 4, 2007, the Corporation's Board authorized management to repurchase up to 500,000 shares of the Corporation's Common Stock. This authorization was publicly announced and expires December 31, 2008. Of the 103,443 shares referenced above, 95,000 shares were purchased in open market transactions pursuant to this authorization. There were 390,000 remaining shares that may yet be purchased pursuant to such authorizations as of March 31, 2008. The remaining 8,443 shares were purchased in connection with the exercise of certain outstanding stock options.

(2) These shares were purchased in connection with the exercise of certain outstanding stock options.

Item 3. Defaults Upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

None

Item 5. Other Information

a. None

b. None

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PART II. OTHER INFORMATION

Item 6. Exhibits

Exhibit No.: Description of Exhibit: Form 10-Q Page No.:

31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes - Oxley Act of 2002	32
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes - Oxley Act of 2002	33
32	Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	34

FIRST MERCHANTS CORPORATION

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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.

First Merchants Corporation

(Registrant)

Date: May 9, 2008

by /s/ Michael C. Rechin

Michael C. Rechin
President and
Chief Executive Officer
(Principal Executive Officer)

Date: May 9, 2008

by /s/ Mark K. Hardwick

Mark K. Hardwick
Executive Vice President and
Chief Financial Officer
(Principal Financial Officer)

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INDEX TO EXHIBITS

INDEX TO EXHIBITS

(a)3. Exhibits:

Exhibit No.:	Description of Exhibit:	Form 10-Q Page No.:
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31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes - Oxley Act of 2002	32
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EXHIBIT-31.1

FIRST MERCHANTS CORPORATION

FORM 10-Q
CERTIFICATIONS PURSUANT TO
SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002

CERTIFICATION

I, Michael C. Rechin, President and Chief Executive Officer of First Merchants Corporation, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of First Merchants Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

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3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in the Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2008

by /s/ Michael C. Rechin

Michael C. Rechin
President and
Chief Executive Officer
(Principal Executive Officer)

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EXHIBIT-31.2

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FIRST MERCHANTS CORPORATION
FORM 10-Q
CERTIFICATIONS PURSUANT TO
SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002

CERTIFICATION

I, Mark K. Hardwick, Executive Vice President and Chief Financial Officer of First Merchants Corporation, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of First Merchants Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in the Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report, based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on

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our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

- (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
- (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2008

by: /s/Mark K. Hardwick

Mark K. Hardwick
Executive Vice President and
Chief Financial Officer
(Principal Financial Officer)

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EXHIBIT-32

CERTIFICATIONS PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the quarterly report of First Merchants Corporation (the "Corporation") on Form 10-Q for the period ending March 31, 2008 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael C. Rechin, President and Chief Executive Officer of the Corporation, do hereby certify, in accordance with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o (d)); and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation.

Date: May 9, 2008

by /s/ Michael C. Rechin

Michael C. Rechin
President and
Chief Executive Officer
(Principal Executive Officer)

A signed copy of this written statement required by Section 906 has been provided to First Merchants Corporation and will be retained by First Merchants Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

In connection with the quarterly report of First Merchants Corporation (the "Corporation") on Form 10-Q for the period ending March 31, 2008 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark K. Hardwick, Executive Vice President and Chief Financial Officer of the

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Corporation, do hereby certify, in accordance with 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o (d)); and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation.

Date: May 9, 2008

by /s/ Mark K. Hardwick

Mark K. Hardwick
Executive Vice President and
Chief Financial Officer
(Principal Financial Officer)

A signed copy of this written statement required by Section 906 has been provided to First Merchants Corporation and will be retained by First Merchants Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

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