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1ST SOURCE CORP
Form 10-Q/A
August 01, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A
AMENDMENT NO. 1

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

For the quarterly period ended June 30, 2003

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 0-6233

1st SOURCE CORPORATION
(Exact name of registrant as specified in its charter)

INDIANA

(State or other jurisdiction of
incorporation or organization)

35-1068133

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

100 North Michigan Street, South Bend, Indiana 46601
(Address of principal executive offices) (Zip Code)
(574) 235-2702

(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 X No _____

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes X No _____

Number of shares of common stock outstanding as of July 25, 2003 - 21,077,534 shares.

EXPLANATORY NOTE

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This amendment to Form 10-Q for the quarterly period ended June 30, 2003, is being filed to correct two typographical errors included under the table heading of Supplemental Loan Information as of June 30, 2003, on page 18 of the originally filed report, which was filed under Part I, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations. The typographical errors are as follows:

- Correctly state the Aircraft financing non-accrual loans as \$18,925
- Correctly state the Total non-accrual loans as \$41,930

This 10-Q/A is filed solely to correct these two typographical errors in Part I, Item 2.

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CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
1ST SOURCE CORPORATION AND SUBSIDIARIES
(UNAUDITED - DOLLARS IN THOUSANDS)

	June 30, 2003	December 31, 2002

ASSETS		
Cash and due from banks	\$ 122,422	\$ 120,894

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Federal funds sold and interest bearing deposits with other banks	61,351	81,881
Investment securities available-for-sale (amortized cost of \$676,431 and \$640,224 at June 30, 2003 and December 31, 2002, respectively)	684,926	647,617
Trading account securities	13,303	13,347
Mortgages held for sale	125,724	146,640
Loans - net of unearned discount		
Commercial and agricultural	427,760	428,367
Truck and automobile financing	486,712	445,195
Aircraft financing	288,110	323,802
Construction equipment financing	270,582	303,126
Loans secured by real estate	527,047	567,950
Consumer loans	98,577	111,012
	-----	-----
Total loans	2,098,788	2,179,452
Reserve for loan losses	(63,194)	(59,218)
	-----	-----
Net loans	2,035,594	2,120,234
Equipment owned under operating leases, net of accumulated depreciation	80,135	93,893
Net premises and equipment	39,376	40,899
Other assets	131,642	142,063
	-----	-----
Total assets	\$ 3,294,473	\$ 3,407,468
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Noninterest bearing	444,705	419,289
Interest bearing	2,199,039	2,293,616
	-----	-----
Total deposits	2,643,744	2,712,905
Federal funds purchased and securities sold under agreements to repurchase	172,586	212,040
Other short-term borrowings	35,707	48,638
Long-term debt	17,253	16,878
Guaranteed preferred beneficial interests in 1st Source's subordinated debentures	54,750	54,750
Other liabilities	53,261	52,828
	-----	-----
Total liabilities	2,977,301	3,098,039
Shareholders' equity:		
Preferred stock-no par value	--	--
Common stock-no par value	7,578	7,579
Capital surplus	214,001	214,001
Retained earnings	95,855	90,897
Cost of common stock in treasury	(5,535)	(7,637)
Accumulated other comprehensive income	5,273	4,589
	-----	-----
Total shareholders' equity	317,172	309,429
	-----	-----
Total liabilities and shareholders' equity	\$ 3,294,473	\$ 3,407,468
	=====	=====

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The accompanying notes are a part of the consolidated financial statements.

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CONSOLIDATED STATEMENTS OF INCOME
 1ST SOURCE CORPORATION AND SUBSIDIARIES
 (UNAUDITED - DOLLARS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

	Three Months Ended June 30,		Six
	2003	2002	2003
Interest and Fee Income:			
Loans	\$ 36,103	\$ 43,134	\$ 72,71
Investment securities:			
Taxable	4,710	5,586	9,24
Tax-exempt	1,445	1,550	2,88
Other	295	127	44
TOTAL INTEREST INCOME	42,553	50,397	85,28
Interest Expense:			
Deposits	13,187	18,227	26,95
Short-term borrowings	1,498	1,211	2,76
Guaranteed preferred beneficial interests in 1st Source's subordinated debentures	941	794	1,88
Long-term debt	187	213	38
TOTAL INTEREST EXPENSE	15,813	20,445	31,98
NET INTEREST INCOME	26,740	29,952	53,29
Provision for loan losses	4,901	10,750	10,45
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	21,839	19,202	42,84
Noninterest Income:			
Trust fees	2,736	2,661	5,37
Service charges on deposit accounts	3,922	3,684	7,64
Loan servicing and sale income	4,445	1,124	7,65
Equipment rental income	6,455	7,464	13,22
Other income	4,635	3,009	8,61
Investment securities and other investment losses	(275)	0	(55)
TOTAL NONINTEREST INCOME	21,918	17,942	41,95
Noninterest Expense:			
Salaries and employee benefits	18,290	16,417	35,53
Net occupancy expense	1,785	1,678	3,64
Furniture and equipment expense	2,677	2,626	5,31
Depreciation - leased equipment	5,050	5,966	10,40
Supplies and communication	1,558	1,594	3,06
Loan collection and repossession expense	3,972	1,438	5,57

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Other expense	3,943	3,944	8,52
TOTAL NONINTEREST EXPENSE	37,275	33,663	72,07
INCOME BEFORE INCOME TAXES	6,482	3,481	12,72
Income taxes	1,792	714	3,57
NET INCOME	\$ 4,690	\$ 2,767	\$ 9,15
Other Comprehensive Income, Net of Tax:			
Change in unrealized appreciation of available-for-sale securities	881	2,372	68
Total Comprehensive Income	\$ 5,571	\$ 5,139	\$ 9,83
Per Common Share:			
Basic Net Income Per Common Share	\$ 0.22	\$ 0.13	\$ 0.4
Diluted Net Income Per Common Share	\$ 0.22	\$ 0.13	\$ 0.4
Dividends	\$ 0.090	\$ 0.090	\$ 0.18
Basic Weighted Average Common Shares Outstanding	21,071,946	20,950,747	21,036,32
Diluted Weighted Average Common Shares Outstanding	21,407,824	21,368,441	21,368,94

The accompanying notes are a part of the consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS
1ST SOURCE CORPORATION AND SUBSIDIARIES
(UNAUDITED - DOLLARS IN THOUSANDS)

	Six Months Ended June	
	2003	2002
Operating activities:		
Net income	\$ 9,150	\$ 6,975
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	10,451	22,559
Depreciation of premises and equipment	13,053	14,685
Amortization of investment security premiums and accretion of discounts, net	2,696	2,127
Amortization of mortgage servicing rights	3,846	2,903
Mortgage servicing asset impairment charges	5,415	1,177
Deferred income taxes	(1,677)	8,937
Realized investment securities losses	555	488
Change in mortgages held for sale	20,916	88,599
Realized losses (gains) on securitized loans	311	(4,499)

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Change in trading account securities	43	--
Decrease in interest receivable	1,333	1,482
Decrease in interest payable	(376)	(3,571)
Increase in other assets	(173)	(4,088)
Other	4,002	(4,309)
	-----	-----
Net cash from operating activities	69,545	133,465
Investing activities:		
Proceeds from sales and maturities of investment securities	70,119	128,299
Purchases of investment securities	(109,886)	(119,725)
Net change in short-term investments	20,530	(6,373)
Loans sold or participated to others	49,403	168,660
Net change in loans	24,785	(205,616)
Net change in equipment owned under operating leases	3,350	(5,826)
Purchases of premises and equipment	(994)	(3,097)
	-----	-----
Net cash from investing activities	57,307	(43,678)
Financing activities:		
Net change in demand deposits, NOW accounts and savings accounts	(33,292)	65,067
Net decrease in certificates of deposit	(35,869)	(156,538)
Net decrease in short-term borrowings	(52,385)	(30,252)
Proceeds from issuance of long-term debt	694	37
Payments on long-term debt	(319)	(158)
Acquisition of treasury stock	(370)	(2,158)
Cash dividends	(3,783)	(3,763)
	-----	-----
Net cash from financing activities	(125,324)	(127,765)
Net change in cash and cash equivalents	1,528	(37,978)
Cash and cash equivalents, beginning of year	120,894	129,431
	-----	-----
Cash and cash equivalents, end of period	\$ 122,422	\$ 91,453
	=====	=====

The accompanying notes are a part of the consolidated financial statements

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1ST SOURCE CORPORATION
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements reflect all adjustments (all of which are normal and recurring in nature) which are, in the opinion of management, necessary for a fair presentation of the consolidated financial position, the results of operations, and cash flows for the periods presented. These unaudited consolidated financial statements have been prepared according to the rules and regulations of the Securities and Exchange Commission (SEC) and, therefore, certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been omitted. The Notes to the Consolidated Financial Statements appearing in 1st Source Corporation's

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(1st Source) Annual Report on Form 10-K (2002 Annual Report), which include descriptions of significant accounting policies, should be read in conjunction with these interim financial statements. The balance sheet at December 31, 2002 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. Certain amounts in the prior period consolidated financial statements have been reclassified to conform with the current year presentation. These reclassifications had no effect on total assets, shareholders' equity or net income as previously reported.

1st Source accounts for its stock-based compensation plans under the recognition and measurement principles provided in Accounting Principles Board Opinion (APB) No. 25, "Accounting for Stock Issued to Employees", and related Interpretations. Stock-based employee compensation expense for the Executive Incentive Plan and the Restricted Stock Award Plan is recognized in net income. For the stock option plans, the stock option agreement, and the Employee Stock Purchase Plan, no compensation expense is recognized in net income as all options granted under these plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation," as amended by SFAS 148, requires pro forma disclosures of net income and earnings per share for companies not adopting its fair value accounting method for stock-based employee compensation. The pro forma disclosures below use the fair value method of SFAS 123 to measure compensation expense for stock-based employee compensation plans.

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(Dollars in thousands, except per share data)

	THREE MONTHS ENDED JUNE 30		
	2003	2002	
Net income, as reported	\$ 4,690	\$ 2,767	\$
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	310	--	
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(442)	(21)	
Pro forma net income	\$ 4,558	\$ 2,746	\$
Earnings per share:			
Basic--as reported	\$ 0.22	\$ 0.13	\$
Basic--pro forma	\$ 0.22	\$ 0.13	\$
Diluted--as reported	\$ 0.22	\$ 0.13	\$
Diluted--pro forma	\$ 0.21	\$ 0.13	\$

Note 2. Recent Accounting Pronouncements

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CONSOLIDATION OF VARIABLE INTEREST ENTITIES: In January 2003, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. (FIN) 46, "Consolidation of Variable Interest Entities." The objective of this interpretation is to provide guidance on how to identify a variable interest entity (VIE) and determine when the assets, liabilities, noncontrolling interests, and results of operations of a VIE need to be included in a company's consolidated financial statements. A company that holds variable interests in an entity will need to consolidate the entity if the company's interest in the VIE is such that the company will absorb a majority of the VIE's expected losses and/or receive a majority of the entity's expected residual returns, if they occur. FIN 46 also requires additional disclosures by primary beneficiaries and other significant variable interest holders. The provisions of this interpretation became effective upon issuance. As of June 30, 2003 and December 31, 2002, 1st Source had a variable interest in a securitization trust. This securitization trust is a qualifying special purpose entity, which is exempt from the consolidation requirements of FIN 46.

1st Source adopted FIN 46 on July 1, 2003. In its current form, FIN 46 may require 1st Source to de-consolidate its investment in 1st Source Capital Trust I, II, and III (the Trusts) in future financial statements. The potential de-consolidation of subsidiary trusts of bank holding companies formed in connection with the issuance of trust preferred securities, like the Trusts, appears to be an unintended consequence of FIN 46. It is currently unknown if, or when, the FASB will address this issue. In July 2003, the Board of Governors of the Federal Reserve System issued a supervisory letter instructing bank holding companies to continue to include the trust preferred securities in their Tier I capital for regulatory capital purposes until notice is given to the contrary. The Federal Reserve intends to review the regulatory implications of any accounting treatment changes and, if necessary or warranted, provide further appropriate guidance. There can be no assurance that the Federal Reserve will continue to allow institutions to include trust preferred securities in Tier I capital for regulatory capital purposes. As of June 30, 2003, assuming 1st Source was not allowed to include the \$54.75 million in trust preferred securities issued by the Trusts in Tier 1 capital, 1st Source would still be well capitalized per regulatory guidelines.

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GUARANTEES: In November 2002, the FASB issued FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others." This interpretation expands the disclosures to be made by a guarantor in its financial statements about its obligations under certain guarantees and requires the guarantor to recognize a liability for the fair value of an obligation assumed under a guarantee. The initial recognition and measurement provisions of FIN 45 are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The disclosure requirements of FIN 45 are effective for financial statements of interim or annual periods ending after December 15, 2002, and were adopted in 1st Source's 2002 Annual Report. Implementation of the remaining provisions of FIN 45 during the first quarter of 2003 did not have a significant impact on the financial statements.

AMENDMENT OF STATEMENT 133 ON DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES: In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." This statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts. The provisions in this Statement require that contracts with comparable characteristics be accounted for similarly. The provisions of SFAS No. 149 are effective for contracts entered into or modified after June 30, 2003, and for hedging relationships designated after June 30, 2003. 1st Source does not expect

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the requirements of SFAS No. 149 to have a material impact on the results of operations or financial position.

ACCOUNTING FOR CERTAIN FINANCIAL INSTRUMENTS WITH CHARACTERISTICS OF BOTH LIABILITIES AND EQUITY: In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This Statement establishes standards on the classification and measurement of certain financial instruments with characteristics of both liability and equity. SFAS No. 150 is effective for all financial instruments entered into or modified after May 31, 2003, and to all other instruments that exist as of the beginning of the first interim period beginning after June 15, 2003. 1st Source does not expect the requirements of SFAS No. 150 to have an impact on the results of operations or financial position.

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Note 3. Reserve for Loan Losses

The reserve for loan losses is maintained at a level believed to be adequate by management to absorb probable losses inherent in the loan portfolio. The determination of the reserve requires significant judgment reflecting management's best estimate of probable loan losses related to specifically identified loans as well as probable losses in the remainder of the various loan portfolios. The methodology for assessing the appropriateness of the reserve consists of several key elements, which include: specific reserves for identified special attention loans (classified loans and leases and internal watch list credits), percentage allocations for special attention loans without specific reserves, formula reserves for each business lending division portfolio including a higher percentage reserve allocation for special attention loans without a specific reserve and reserves for pooled homogeneous loans. Management's evaluation is based upon a continuing review of these portfolios, estimates of future customer performance, collateral values and disposition and forecasts of future economic and geopolitical events, all of which are subject to judgment and will change.

Note 4. Financial Instruments with Off-Balance-Sheet Risk

To meet the financing needs of its customers, 1st Source and its subsidiaries are parties to financial instruments with off-balance-sheet risk in the normal course of business. These off-balance-sheet financial instruments include commitments to originate, purchase and sell loans and standby letters of credit. The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated statements of financial condition. 1st Source's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for loan commitments and standby letters of credit is represented by the dollar amount of those instruments. 1st Source uses the same credit policies and collateral requirements in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Trustcorp Mortgage Company and 1st Source Bank (Bank), subsidiaries of 1st Source, grant mortgage loan commitments to borrowers, subject to normal loan underwriting standards. The interest rate risk associated with these loan commitments is managed by entering into contracts for future deliveries of loans. Loan commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Letters of credit are conditional commitments issued by 1st Source to guarantee the performance of a customer to a third party. The credit risk

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involved and collateral obtained in issuing letters of credit is essentially the same as that involved in extending loan commitments to customers.

As of June 30, 2003 and December 31, 2002, 1st Source had commitments outstanding to originate and purchase mortgage loans aggregating \$533.00 million and \$364.00 million, respectively. Outstanding commitments to sell loans aggregated \$286.00 million at June 30, 2003 and \$240.00 million at December 31, 2002. Standby letters of credit totaled \$112.85 million and \$117.21 million at June 30, 2003 and December 31, 2002, respectively. Standby letters of credit have terms ranging from six months to one year.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Except for historical information contained herein, the matters discussed in this document express "forward-looking statements." Generally, the words "believe," "expect," "intend," "estimate," "anticipate," "project," "will" and similar expressions indicate forward-looking statements. Those statements, including statements, projections, estimates or assumptions concerning future events or performance, and other statements that are other than statements of historical fact, are subject to material risks and uncertainties. 1st Source cautions readers not to place undue reliance on any forward-looking statements, which speak only as of the date made. 1st Source may make other written or oral forward-looking statements from time to time. Readers are advised that various important factors could cause 1st Source's actual results or circumstances for future periods to differ materially from those anticipated or projected in such forward-looking statements. Such factors include, but are not limited to, changes in law; regulations or accounting principles generally accepted in the United States; 1st Source's competitive position within its markets served; increasing consolidation within the banking industry; unforeseen changes in interest rates; unforeseen changes in loan prepayment assumptions; unforeseen downturns in or major events affecting the local, regional or national economies or the industries in which 1st Source has credit concentrations; and other matters discussed in 1st Source's filings with the SEC, including its Annual Report on Form 10-K for 2002, which filings are available from the SEC. 1st Source undertakes no obligation to publicly update or revise any forward-looking statements.

The following management's discussion and analysis is presented to provide information concerning the financial condition of 1st Source as of June 30, 2003, as compared to December 31, 2002, and the results of operations for the six months ended June 30, 2003 and 2002. This discussion and analysis should be read in conjunction with 1st Source's consolidated financial statements and the financial and statistical data appearing elsewhere in this report and 1st Source's 2002 Annual Report.

FINANCIAL CONDITION

1st Source's assets at June 30, 2003 were \$3.29 billion, down 3.32% from December 31, 2002. Total loans were down 3.70% and total deposits decreased 2.55% over the comparable figures at the end of 2002.

Nonperforming assets at June 30, 2003, were \$58.18 million compared to \$64.12 million at December 31, 2002 and \$69.83 million at March 31, 2003, a decrease of 9.26% and 16.68%, respectively. Nonperforming assets decreased due to the liquidation of repossessions and a decrease in truck non-accrual loans. This decrease was offset by an increase in aircraft non-accrual loans. At June 30, 2003, nonperforming assets were 2.67% of net loans and leases compared

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to 2.65% at December 31, 2002.

At June 30, 2003, other assets consisted of \$27.03 million in intangible assets, \$26.79 million in cash surrender value of corporate owned life insurance, \$19.14 million in originated and purchased mortgage servicing rights, \$13.45 million in accrued interest receivable, \$12.58 million in repossessions, \$4.80 million in other real estate and \$27.84 million in all other assets.

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CAPITAL

As of June 30, 2003, total shareholders' equity was \$317.17 million, up 2.50% from the \$309.43 million at December 31, 2002. The 1st Source equity-to-assets ratio was 9.63% as of June 30, 2003, compared to 9.08% at December 31, 2002. Book value per common share rose to \$15.05 at June 30, 2003, up from \$14.77 at December 31, 2002.

1st Source declared and paid dividends per common share of \$0.09 during the second quarter of 2003. The dividend payout ratio, representing dividends per share divided by earnings per share, was 40.91% for the second quarter of 2003. The dividend payout is continually reviewed by management and the Board of Directors.

The banking regulators have established guidelines for leverage capital requirements, expressed in terms of Tier 1 or core capital as a percentage of average assets, to measure the soundness of a financial institution. These guidelines require all banks to maintain a minimum leverage capital ratio of 4.00% for adequately capitalized banks and 5.00% for well-capitalized banks. 1st Source's leverage capital ratio was 10.38% at June 30, 2003.

The Federal Reserve Board has established risk-based capital guidelines for U.S. banking organizations. The guidelines establish a conceptual framework calling for risk weights to be assigned to on and off-balance sheet items in arriving at risk-adjusted total assets, with the resulting ratio compared to a minimum standard to determine whether a bank has adequate capital. The minimum standard risk-based capital ratios effective in 2003 are 4.00% for adequately capitalized banks and 6.00% for well-capitalized banks for Tier 1 risk-based capital and 8.00% and 10.00%, respectively, for total risk-based capital. 1st Source's Tier 1 risk-based capital ratio on June 30, 2003 was 12.46% and the total risk-based capital ratio was 13.80%.

LIQUIDITY AND INTEREST RATE SENSITIVITY

The Bank's liquidity is monitored and closely managed by the Asset/Liability Committee (ALCO), whose members are comprised of the Bank's senior management. Asset and liability management includes the management of interest rate sensitivity and the maintenance of an adequate liquidity position. The purpose of interest rate sensitivity management is to stabilize net interest income during periods of changing interest rates.

Liquidity management is the process by which the Bank ensures that adequate liquid funds are available to meet financial commitments on a timely basis. Financial institutions must maintain liquidity to meet day-to-day requirements of depositors and borrowers, take advantage of market opportunities and provide a cushion against unforeseen needs.

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Liquidity of the Bank is derived primarily from core deposit growth,

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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 is deposit growth and retention of the core deposit base. The principal source of asset funded liquidity is available for sale investment securities, cash and due from banks, federal funds sold, securities purchased under agreements to resell and loans and interest bearing deposits with other banks maturing within one year. Additionally, liquidity is provided by bank lines of credit, repurchase agreements and the ability to borrow from the Federal Reserve Bank and Federal Home Loan Bank.

Close attention is given to various interest rate sensitivity gaps and interest rate spreads. Maturities of rate sensitive assets are relative to the maturities of rate sensitive liabilities and interest rate forecasts. At June 30, 2003, the consolidated statement of financial condition was rate sensitive by \$139.55 million more assets than liabilities scheduled to reprice within one year or approximately 1.08%.

RESULTS OF OPERATIONS

Net income for the three and six month periods ended June 30, 2003, was \$4.69 million and \$9.15 million respectively, compared to \$2.77 million and \$6.98 million for the same periods in 2002. Diluted net income per common share was \$0.22 and \$0.43, respectively, for the three and six month periods ended June 30, 2003, compared to \$0.13 and \$0.33 for the same periods in 2002. Return on average common shareholders' equity was 5.88% for the six months ended June 30, 2003, compared to 4.53% in 2002. The return on total average assets was 0.56% for the six months ended June 30, 2003 compared to 0.40% in 2002.

The increase in net income for the six months ended June 30, 2003 over the first six months of 2002, was primarily the result of a \$12.11 million decrease in the provision for loan losses and a \$5.65 million increase in mortgage banking income, offset by a \$7.20 million decrease in net interest income, a \$2.54 million increase in salaries and employee benefit expense and a \$3.70 million increase in loan collection and repossession expense. Details of the changes in the various components of net income are further discussed below.

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NET INTEREST INCOME

The taxable equivalent net interest income for the three months ended June 30, 2003, was \$27.50 million, a decrease of 10.56% over the same period in 2002. The net interest margin on a fully taxable equivalent basis' was 3.66% for the three months ended June 30, 2003 compared to 3.90% for the three months ended June 30, 2002. The taxable equivalent net interest income for the six-month period ended June 30, 2003, was \$54.82 million, a decrease of 11.72% over 2002, resulting in a net yield of 3.69%, compared to 3.95% for the same period in 2002.

Total average earning assets decreased 4.73% and 5.48%, respectively, for the three and six-month periods ended June 30, 2003, over the comparative periods in 2002. Average loan outstandings decreased by 11.70% and 10.95% for the three and six-month periods, compared to the same periods in 2002, due primarily to decreased loan volume in commercial loans secured by transportation and construction equipment. Total average investment securities increased 4.20% and 2.65% for the three and six-month periods over one year ago due to an increase in municipal and other securities which more than offset a decrease in United States treasury securities. Average mortgages held for sale increased 41.38%, as demand for mortgage loans was greater in the second quarter of 2003 due to the interest rate environment. The taxable equivalent yields on total

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average earning assets were 5.77% and 6.49% for the three-month periods ended June 30, 2003 and 2002, respectively, and 5.84% and 6.65% for the six-month periods ended June 30, 2003 and 2002, respectively.

Average interest bearing deposits decreased 10.28% and 10.08% for the three and six month periods, respectively, over the same periods in 2002. The rate on average interest-bearing deposits was 2.41% and 2.99% for the three-month periods ended June 30, 2003 and 2002 and 2.48% and 3.13% for the six-month periods ended June 30, 2003 and 2002 due to a decrease in public funds and brokered deposits. These higher cost deposits were not pursued due to lower funding needs. The rate on average interest-bearing funds was 2.54% and 2.95% for the three months ended June 30, 2003 and 2002, respectively. For the six months ended June 30, 2003 and 2002, the rate on average interest bearing funds was 2.57% and 3.08%, respectively.

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The following table sets forth consolidated information regarding average balances and rates.

DISTRIBUTION OF ASSETS, LIABILITIES AND SHAREHOLDERS' EQUITY
INTEREST RATES AND INTEREST DIFFERENTIAL
(Dollars in thousands)

	Three months ended 2003		
	Average Balance	Interest Income/ Expense	Yield/ Rate
ASSETS:			
Investment securities:			
Taxable	\$ 504,210	\$ 4,710	3.75%
Tax exempt (1)	165,963	2,136	5.16%
Mtg - Held for Sale	137,651	2,141	6.24%
Net loans (2 & 3)	2,112,248	34,034	6.46%
Other investments	93,378	296	1.27%
Total Earning Assets	3,013,449	43,317	5.77%
Cash and due from banks	91,161		
Reserve for loan losses	(62,976)		
Other assets	257,936		
Total	\$ 3,299,570		
LIABILITIES AND SHAREHOLDERS' EQUITY:			
Interest bearing deposits	\$ 2,196,935	\$ 13,187	2.41%
Short-term borrowings	231,971	1,498	2.59%
Guaranteed preferred beneficial interest in 1st Source's subordinated debentures	54,750	942	6.90%
Long-term debt	17,305	187	4.33%

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Total Interest Bearing Liabilities	2,500,961	15,813	2.54%
Noninterest bearing deposits	428,384		
Other liabilities	54,290		
Shareholders' equity	315,934		

Total	\$ 3,299,570		
	=====		
Net Interest Income		\$ 27,504	
		=====	
Net Yield on Earning Assets on a Taxable			-----
Equivalent Basis			3.66%
			=====

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	Six months e 2003		
	Average Balance	Interest Income/ Expense	Yield Rate
	-----	-----	-----
ASSETS:			
Investment securities:			
Taxable	\$ 498,345	\$ 9,244	3.74%
Tax exempt (1)	164,870	4,251	5.20%
Mtg - Held for Sale	131,480	3,844	5.90%
Net loans (2 & 3)	2,131,930	69,019	6.53%
Other investments	68,599	445	1.31%
	-----	-----	-----
Total Earning Assets	2,995,225	86,802	5.84%
Cash and due from banks	88,583		
Reserve for loan losses	(62,038)		
Other assets	265,026		

Total	\$ 3,286,796		
	=====		
LIABILITIES AND SHAREHOLDERS' EQUITY:			
Interest bearing deposits	\$ 2,194,050	\$ 26,958	2.48%
Short-term borrowings	242,411	2,763	2.30%
Guaranteed preferred beneficial interest in 1st Source's subordinated debentures	54,750	1,881	6.93%
Long-term debt	17,400	385	4.46%
	-----	-----	-----
Total Interest Bearing Liabilities	2,508,611	31,986	2.57%
Noninterest bearing deposits	410,223		

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Other liabilities	54,075	
Shareholders' equity	313,887	

Total	\$ 3,286,796	=====

Net Interest Income		\$ 54,816
		=====
Net Yield on Earning Assets on a Taxable		
Equivalent Basis		3.69%
		=====

- (1) Interest income includes the effects of taxable equivalent adjustments, using a 35% rate. Tax equivalent adjustments were \$1,370 in 2003 and \$1,447 in 2002.
- (2) Loan income includes fees on loans of \$2,574 in 2003 and \$2,557 in 2002. Loan income also includes the effects of taxable equivalent adjustments, using a 35% rate for 2003 and 2002. The tax equivalent adjustments were \$150 in 2003 and \$153 in 2002.
- (3) For purposes of this computation, nonaccruing loans are included in the daily average loan amounts outstanding.

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PROVISION AND RESERVE FOR LOAN LOSSES

The provision for loan losses for the three-month periods ended June 30, 2003, and 2002 was \$4.90 million and \$10.75 million, respectively, and \$10.45 million and \$22.56 million for the six-month periods ended June 30, 2003 and 2002, respectively. Net Charge-offs of \$3.55 million were recorded for the second quarter 2003, compared to \$11.22 million for the same quarter a year ago. Year-to-date net charge-offs of \$6.48 million have been recorded in 2003, compared to net charge-offs of \$22.76 million through June 2002.

In the second quarter 2003, 1st Source experienced moderate improvement in credit quality. Overall delinquencies have decreased, even though there has been a slight increase in construction equipment delinquencies due to bad weather and to 1st Source slow payments from state and municipal governments. Loan delinquencies were down to 1.51% on June 30, 2003, as compared to 2.51% on June 30, 2002, and 1.80% at the end of 2002. Second quarter 2003 net charge-offs increased slightly as compared to first quarter 2003. The reserve for loan losses as a percentage of loans outstanding at the end of the period continued to increase. A summary of loan loss experience during the three-month and six-month periods ended June 30, 2003 and 2002 is provided below.

Summary of Reserve for Loan Losses

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	(Dollars in Thousands)		
	Three Months Ended June 30,		Six Months June
	2003	2002	2003
Reserve for loan losses - beginning balance	\$ 61,843	\$ 57,892	\$ 59,218
Charge-offs	(4,453)	(11,696)	(8,123)
Recoveries	903	474	1,648
Net charge-offs	(3,550)	(11,222)	(6,475)
Provision for loan losses	4,901	10,750	10,451
Reserve for loan losses - ending balance	\$ 63,194	\$ 57,420	\$ 63,194
Loans outstanding at end of period	\$ 2,098,788	\$ 2,373,043	\$ 2,098,788
Average loans outstanding during period	2,112,248	2,393,107	2,131,930
Reserve for loan losses as a percentage of loans outstanding at end of period	3.01%	2.42%	3.01%
Ratio of net charge-offs during period to average loans outstanding	0.67%	1.88%	0.61%

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NONPERFORMING ASSETS

Nonperforming assets were as follows:

(Dollars in thousands)

	June 30, 2003	Dec 31, 2002	June 30, 2002
Loans past due 90 days or more	\$ 289	\$ 154	\$ 411
Non-accrual loans	41,930	35,664	51,483
Other real estate	3,213	4,362	3,362
Repossessions	12,583	21,343	4,591
Equipment owned under operating leases	168	2,594	1,149
Total nonperforming assets	\$58,183	\$64,117	\$60,996

Nonperforming assets totaled \$58.18 million at June 30, 2003, decreasing 9.26% from \$64.12 million at December 31, 2002 and decreasing 4.62% from \$61.00 million at June 30, 2002. The decrease during the second quarter was primarily related to the liquidation of repossessions and a decrease in truck non-accrual loans offset by an increase in aircraft non-accrual loans. Nonperforming assets as a percentage of total loans and leases increased to 2.67% at June 30, 2003

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from 2.65% at December 31, 2002 and 2.45% at June 30, 2002.

Repossessions consist primarily of aircraft, \$10.39 million of the \$12.58 million as of June 30, 2003. These aircraft primarily have come from defaulted loans to air cargo operators and aircraft dealers. There are also automobiles, light trucks, construction equipment and environmental equipment in repossessed assets at June 30, 2003. At the time of repossession, the recorded amount of the loan is written down, if necessary, to the estimated value of the equipment or vehicle by a charge to the reserve for loan losses, unless the equipment is in the process of immediate sale. Subsequent write-downs are included in non-interest expense.

Repossessed assets have a valuation determined by the sales and credit officers or a third party. The estimated value is determined on an orderly liquidation basis. Sources typically include vehicle and equipment dealers, valuation guides and other third parties, including appraisers. A number of variables can lead to a decrease in value after the asset is repossessed. These include deterioration in the market, discovery of new or additional information about the asset, and validity or invalidity of prior liens. Valuation adjustments and net losses upon disposition of repossessions for the three-month periods ended June 30, 2003 and 2002 totaled \$2.48 million and \$0.78 million, respectively, and \$2.72 million and \$0.69 million for the six month periods ended June 30, 2003 and 2002, respectively.

The number of repossessed aircraft continues to decrease. Since the credit problems of early 2002 continued throughout the year, 1st Source finished 2002 having repossessed 35 aircraft. In addition, 1st Source has repossessed another 4 aircraft in 2003. 1st Source has arranged for disposal of 23 planes leaving 16 repossessed aircraft included in repossessed assets as of June 30, 2003.

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SUPPLEMENTAL LOAN INFORMATION AS OF JUNE 30, 2003

(Dollars in thousands)

	Loan outstandings	Non-accrual loans	Other real estate and repossessions	Ye net c
	-----	-----	-----	-----
Commercial and agricultural loans	\$ 427,760	\$ 3,797	\$ 1,877	\$
Truck and automobile financings	486,712	6,764	272	
Aircraft financing	288,110	18,925	10,392	
Construction equipment financing	270,582	8,499	1,871	
Loans secured by real estate	527,047	3,192	344	
Consumer loans	98,577	753	1,040	
	-----	-----	-----	-----
Total	\$ 2,098,788	\$ 41,930	\$ 15,796	\$
	=====	=====	=====	=====

For financial statements purposes, non-accrual loans are included in loan outstandings, whereas repossessions and other real estate are included in other assets. Net credit losses include net charge-offs on loans and valuation adjustments and gains and losses on disposition of repossessions and defaulted operating leases.

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NON-INTEREST INCOME

Non-interest income for the three-month periods ended June 30, 2003 and 2002 was \$21.92 million and \$17.94 million, respectively, and \$41.96 million and \$36.62 million for the six-month periods ended June 30, 2003 and 2002, respectively. The predominant factor behind the growth in 2003 was mortgage loan servicing and sale income, which reached record levels in both the second quarter and first half of the year.

(Dollars in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Non-interest Income:				
Trust fees	\$ 2,736	\$ 2,661	\$ 5,376	\$ 5,321
Service charges on deposit accounts	3,922	3,684	7,646	7,155
Mortgage banking	4,094	(46)	7,187	1,538
Securitization income	922	1,418	1,599	2,539
Insurance commissions	616	531	1,428	1,057
Equipment rental income	6,455	7,464	13,226	14,744
Other income	3,448	2,230	6,050	4,758
Investment securities and other investment losses	(275)	--	(555)	(488)
	-----	-----	-----	-----
Total Non-interest Income	\$21,918	\$ 17,942	\$ 41,957	\$36,624
	=====	=====	=====	=====

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The increase in mortgage banking revenue on both a year-over-year and a quarter-over-quarter basis was driven primarily by heavy origination volumes and higher gains on sales of loans into the secondary market which more than offset mortgage servicing rights impairment. Origination volumes were high as interest rates for new loans were at historically low levels. Mortgage servicing rights impairment was \$3.64 million and \$1.18 million, respectively, for the three months ended June 30, 2003 and 2002. For the six months ended June 30, 2003 and 2002, mortgage servicing rights impairment was \$5.42 million and \$1.18 million, respectively. The carrying value of mortgage servicing rights was impacted by high prepayment speeds on mortgage loans. The high prepayment speeds were the result of mortgage loan refinancings due to historically low interest rates.

The second quarter and first half of 2003 saw increases in trust fees, service charges on deposit accounts and insurance commission income. Equipment rental income decreased due to the decrease in the operating lease portfolio. Other income increased due to increased trading security account income. Trading account security income may be adversely affected by an increase in interest rates.

Securitization income decreased in the second quarter and first half of 2003 as sales into the securitization decreased, thereby reducing the gain on sale. During the second quarter, 1st Source began liquidating its aircraft and auto rental loan securitization due to a reduced demand for loans and a continued strong deposit base. The 1998 1st Source Master Trust Securitization (Master Trust) was issued in July 1998 with a seven year revolving period followed by scheduled amortization beginning July 2005. It is anticipated the liquidation process will take several years. As a result of an increase in the

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Master Trust's commercial paper costs and liquidity fees, together with the decision to voluntarily liquidate the Master Trust, 1st Source's second quarter earnings were adversely impacted by a pre-tax impairment charge of \$275,000. This charge was recorded as an other investment loss. As of June 30, 2003, there were \$309.06 million outstanding auto and aircraft loans in the Master Trust as compared to \$387.79 million at December 31, 2002.

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NON-INTEREST EXPENSE

Non-interest expense for the three-month periods ended June 30, 2003 and 2002 was \$37.28 million and \$33.66 million, respectively, and \$72.08 million and \$65.91 million for the six-month periods ended June 30, 2003 and 2002, respectively. The increase in non-interest expense in 2003 was primarily due to increased salaries and employee benefits and increased loan collection and repossession expense.

(Dollars in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
Non-interest Expense:				
Salaries and employee benefits	\$18,290	\$16,417	\$35,537	\$32,995
Net occupancy expense	1,785	1,678	3,649	3,380
Furniture and equipment expense	2,677	2,626	5,318	5,355
Depreciation - leased equipment	5,050	5,966	10,408	12,113
Supplies and communications	1,558	1,594	3,069	3,261
Business development and marketing expense	854	1,010	1,563	1,610
Intangible asset amortization	647	625	1,441	838
Repossession valuation adjustment, loan collection and repossession expenses	3,972	1,438	5,570	1,875
Other expense	2,442	2,310	5,522	4,481
	-----	-----	-----	-----
Total Non-interest Expense	\$37,275	\$33,663	\$72,077	\$65,908
	=====	=====	=====	=====

The increase in salaries and employee benefits on a year-over-year basis reflect increased mortgage commissions of \$1.12 million, incentives of \$0.60 million and group insurance expenses of \$0.31 million. Loan collection and repossession expense is up substantially as 1st Source continues to work through problem loans and liquidate repossessions. Net occupancy expense, furniture and equipment expense, supplies and communication, business development and marketing expense all remained comparable to 2002 levels. Leased equipment depreciation decreased due to the decrease in the operating lease portfolio. Intangible asset amortization increased for the six months ended June 30, 2003, due to the June 2002 reclassification of certain goodwill to unidentifiable intangible assets in accordance with SFAS No. 147, Acquisitions of Certain Financial Institutions. Other expenses increased primarily due to higher insurance costs and losses on the disposition of leasehold improvements at three branches that were closed as of March 31, 2003.

INCOME TAXES

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The provision for income taxes for the six months ended June 30, 2003, was \$3.58 million, compared to \$1.68 million for the comparable period in 2002. The provision for income taxes for the six months ended June 30, 2003, and 2002, is at a rate which management believes approximates the effective rate for the year.

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ITEM 3.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in market risks faced by 1st Source since December 31, 2002. For information regarding 1st Source's market risk, refer to 1st Source's Annual Report on Form 10-K for the year ended December 31, 2002.

ITEM 4.

CONTROLS AND PROCEDURES

1st Source carried out an evaluation, under the supervision and with the participation of 1st Source's management, including 1st Source's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of 1st Source's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, at June 30, 2003, 1st Source's disclosure controls and procedures are effective in accumulating and communicating to management (including such officers) the information relating to 1st Source (including its consolidated subsidiaries) required to be included in 1st Source's periodic SEC filings.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings.

1st Source and its subsidiaries are defendants in various legal proceedings arising in the normal course of business. In the opinion of management, based upon present information including the advice of legal counsel, the ultimate resolution of these proceedings will not have a material effect on 1st Source's financial condition or results of operations.

ITEM 2. Changes in Securities and Use of Proceeds.

None

ITEM 3. Defaults Upon Senior Securities.

None

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

The following actions were taken by the shareholders of 1st Source at the annual shareholders' meeting held April 22, 2003:

1. Election of Directors

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The directors named below were re-elected to the board of directors for terms expiring in April 2006, as follows:

Nominee	Votes For	Votes Withheld
William P. Johnson	19,471,748	39,626
Claire P. Skinner	19,471,680	34,833

In addition, the following directors continued in office after the 2003 annual meeting:

TERMS EXPIRING IN APRIL 2004:

Daniel B. Fitzpatrick
Wellington D. Jones III
Dane A. Miller, Ph.D.
Toby S. Wilt

TERMS EXPIRING IN APRIL 2005:

Lawrence E. Hiler
Rex Martin
Christopher J. Murphy III
Timothy K. Ozark

Finally, in July 2003, the Board elected David Bowers as a director to fill a vacancy. Mr. Bowers will stand for re-election at the next annual shareholders meeting in April 2004.

2. Amendment to 1982 Executive Incentive Plan

An amendment to the 1982 Executive Incentive Plan and the 1982 Restricted Stock Award Plan which would allow the Executive Compensation Committee of the Board of Directors to extend the forfeiture period on issued shares on a discretionary basis was approved, as follows:

Votes in Favor	Votes Against	Abstentions
18,513,836	722,764	280,135

ITEM 5. Other Information.

None

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ITEM 6. Exhibits and Reports on Form 8-K.

(a) The following exhibits are filed with this report:

1. Exhibit 99.1 Certification of Chief Executive Officer required by Rule 13a-14(a).
2. Exhibit 99.2 Certification of Chief Financial Officer required by Rule 13a-14(a).
3. Exhibit 99.3 Certification pursuant to 18 U.S.C. Section 1350 of Chief Executive Officer.
4. Exhibit 99.4 Certification pursuant to 18 U.S.C. Section 1350 of Chief Financial Officer.

(b) Reports on Form 8-K.

A report on Form 8-K, dated April 30, 2003, was filed under report item numbers 5 and 7, concerning 1st Source's results of operations for the quarter ended March 31, 2003.

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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.

1st Source Corporation

DATE: 08/01/03

/s/Christopher J. Murphy III

Christopher J. Murphy III
Chairman of the Board, President and CEO

DATE: 08/01/03

/s/Larry E. Lentych

Larry E. Lentych
Treasurer and Chief Financial Officer
Principal Accounting Officer