

BANCORPSOUTH INC  
Form 10-Q  
May 05, 2006

**Table of Contents**

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

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended March 31, 2006**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number: 1-12991**

**BANCORPSOUTH, INC.**

(Exact name of registrant as specified in its charter)

**Mississippi**

(State or other jurisdiction of incorporation or  
organization)

**64-0659571**

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

**One Mississippi Plaza, 201 South Spring Street,  
Tupelo,  
Mississippi**

(Address of principal executive offices)

**38804**

(Zip Code)

Registrant's telephone number, including area code: (662) 680-2000

**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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check One):  
Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer

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

Yes  No

As of May 3, 2006, the registrant had outstanding 79,305,448 shares of common stock, par value \$2.50 per share.

**BANCORPSOUTH, INC.**  
**CONTENTS**

	Page
<u>PART I. Financial Information</u>	
<u>ITEM 1. Financial Statements</u>	
<u>Consolidated Condensed Balance Sheets (Unaudited) March 31, 2006 and December 31, 2005</u>	3
<u>Consolidated Condensed Statements of Income (Unaudited) Three Months Ended March 31, 2006 and 2005</u>	4
<u>Consolidated Condensed Statements of Cash Flows (Unaudited) Three Months Ended March 31, 2006 and 2005</u>	5
<u>Notes to Consolidated Condensed Financial Statements (Unaudited)</u>	6
<u>ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	13
<u>ITEM 3. Quantitative and Qualitative Disclosures About Market Risk</u>	25
<u>ITEM 4. Controls and Procedures</u>	25
 <u>PART II. Other Information</u>	
<u>ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	25
<u>ITEM 6. Exhibits</u>	25
<u>Ex-31.1 Section 302 Certification of the CEO</u>	
<u>Ex-31.2 Section 302 Certification of the CFO</u>	
<u>Ex-32.1 Section 906 Certification of the CEO</u>	
<u>Ex-32.2 Section 906 Certification of the CFO</u>	

**FORWARD-LOOKING STATEMENTS**

Certain statements contained in this Report may not be based on historical facts and are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements may be identified by reference to a future period(s) or by the use of forward-looking terminology, such as anticipate, believe, estimate, expect, foresee, might, will, intend, could, would or plan, or future or conditional verb tenses, and variations or negatives of such terms. These forward-looking statements include, without limitation, those relating to BancorpSouth's net interest margin, deposits, interest earning assets and interest bearing liabilities, net interest revenue, loan demand, valuation of mortgage servicing rights, revenue, key indicators of BancorpSouth's financial performance (such as return on average assets and return on average shareholders' equity), capital resources, BancorpSouth's financial products and services, liquidity and liquidity strategies, provision for credit losses, allowance for credit losses, future acquisitions, the effect of certain legal claims, the impact of federal and state regulatory requirements for capital, the impact and applicability of certain tax assessments and administrative appeals, the adoption of SFAS No. 123R, the adoption of SFAS No. 156, additional share repurchases under BancorpSouth's stock repurchase program and BancorpSouth's future growth and profitability. We caution you not to place undue reliance on the forward-looking statements contained in this report, in that actual results could differ materially from those indicated in such forward-looking statements as a result of a variety of factors. These factors include, but are not limited to, the rate of economic recovery in the areas affected by Hurricane Katrina, the ability of BancorpSouth to increase noninterest revenue and expand noninterest revenue business, the ability of BancorpSouth to fund growth with lower cost liabilities, the ability of BancorpSouth to maintain credit quality, the ability of BancorpSouth to provide and market competitive services and products, the ability of BancorpSouth to diversify revenue, the ability of BancorpSouth to attract, train and retain qualified personnel, the ability of BancorpSouth to operate and integrate new technology, changes in consumer preferences, changes in BancorpSouth's operating or expansion strategy, changes in economic conditions and government fiscal and monetary policies, legislation and court decisions related to the amount of damages recoverable in legal proceedings, fluctuations in prevailing interest rates and the effectiveness of BancorpSouth's interest rate hedging strategies, the ability of BancorpSouth to balance interest rate, credit, liquidity and capital risks, the ability of BancorpSouth to collect amounts due under loan agreements and attract deposits, laws and regulations affecting

financial institutions in general, the ability of BancorpSouth to identify and effectively integrate potential acquisitions, the ability of BancorpSouth to manage its growth and effectively serve an expanding customer and market base, geographic concentrations of BancorpSouth's assets and susceptibility to economic downturns in that area, availability of and costs associated with maintaining and/or obtaining adequate and timely sources of liquidity, the ability of BancorpSouth to compete with other financial services companies, the ability of BancorpSouth to repurchase its common stock on favorable terms, possible adverse rulings, judgments, settlements and other outcomes of pending or threatened litigation or tax assessments, other factors generally understood to affect the financial condition or results of financial services companies and other factors detailed from time to time in BancorpSouth's press releases and filings with the Securities and Exchange Commission. We undertake no obligation to update these forward-looking statements to reflect events or circumstances that occur after the date of this report.

**Table of Contents**

**PART I.**  
**FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS.**

BANCORPSOUTH, INC. AND SUBSIDIARIES  
Consolidated Condensed Balance Sheets

	March 31, 2006 (Unaudited)	December 31, 2005 (1)
	(In thousands)	
<b>ASSETS</b>		
Cash and due from banks	\$ 386,543	\$ 461,659
Interest bearing deposits with other banks	6,809	6,809
Held-to-maturity securities, at amortized cost	1,777,923	1,412,529
Available-for-sale securities, at fair value	1,336,745	1,353,882
Federal funds sold and securities purchased under agreement to resell	224,298	409,531
Loans and leases	7,433,156	7,401,212
Less: Unearned income	37,869	35,657
Allowance for credit losses	96,017	101,500
Net loans	7,299,270	7,264,055
Loans held for sale	38,521	74,271
Premises and equipment, net	270,605	261,172
Accrued interest receivable	85,616	78,730
Goodwill	139,335	138,754
Other assets	324,251	307,282
<b>TOTAL ASSETS</b>	<b>\$ 11,889,916</b>	<b>\$ 11,768,674</b>
<b>LIABILITIES</b>		
Deposits:		
Demand: Noninterest bearing	\$ 1,790,418	\$ 1,798,892
Interest bearing	3,071,176	2,965,057
Savings	771,933	729,279
Other time	4,159,676	4,114,030
Total deposits	9,793,203	9,607,258
Federal funds purchased and securities sold under agreement to repurchase	643,401	748,139
Other short-term borrowings		2,000
Accrued interest payable	28,492	24,435
Junior subordinated debt securities	144,847	144,847
Long-term debt	136,857	137,228
Other liabilities	145,551	127,601
<b>TOTAL LIABILITIES</b>	<b>10,892,351</b>	<b>10,791,508</b>
<b>SHAREHOLDERS EQUITY</b>		

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Common stock, \$2.50 par value Authorized - 500,000,000 shares, Issued - 79,207,075 and 79,237,345 shares, respectively	198,018	198,093
Capital surplus	110,000	108,961
Accumulated other comprehensive loss	(16,904)	(16,233)
Retained earnings	706,451	686,345
<b>TOTAL SHAREHOLDERS EQUITY</b>	<b>997,565</b>	<b>977,166</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS EQUITY</b>	<b>\$ 11,889,916</b>	<b>\$ 11,768,674</b>

(1) Derived from  
audited financial  
statements.

See accompanying notes to consolidated condensed financial statements.

**Table of Contents**

BANCORPSOUTH, INC. AND SUBSIDIARIES  
Consolidated Condensed Statements of Income  
(Unaudited)

	Three months ended March 31,	
	2006	2005
	(In thousands, except for per share amounts)	
<b>INTEREST REVENUE:</b>		
Loans and leases	\$ 127,200	\$ 103,805
Deposits with other banks	141	111
Federal funds sold and securities purchased under agreement to resell	2,846	391
Held-to-maturity securities:		
Taxable	14,323	9,766
Tax-exempt	1,887	1,598
Available-for-sale securities:		
Taxable	10,904	13,745
Tax-exempt	1,363	1,677
Loans held for sale	1,238	1,018
 Total interest revenue	 159,902	 132,111
 <b>INTEREST EXPENSE:</b>		
Deposits	53,133	37,905
Federal funds purchased and securities sold under agreement to repurchase	5,902	2,161
Other	4,938	4,916
 Total interest expense	 63,973	 44,982
 Net interest revenue	 95,929	 87,129
Provision for credit losses	(3,860)	4,787
 Net interest revenue, after provision for credit losses	 99,789	 82,342
 <b>NONINTEREST REVENUE:</b>		
Mortgage lending	3,176	5,628
Service charges	15,450	14,726
Trust income	2,016	1,889
Security gains, net	10	70
Insurance commissions	17,445	15,932
Other	14,673	15,674
 Total noninterest revenue	 52,770	 53,919

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NONINTEREST EXPENSE:			
Salaries and employee benefits		57,573	53,240
Occupancy, net of rental income		7,442	6,412
Equipment		5,763	5,449
Other		25,230	24,587
Total noninterest expense		96,008	89,688
Income before income taxes		56,551	46,573
Income tax expense		18,806	14,829
Net income	\$	37,745	\$ 31,744
Earnings per share: Basic	\$	0.48	\$ 0.41
Diluted	\$	0.47	\$ 0.40
Dividends declared per common share	\$	0.19	\$ 0.19

See accompanying notes to consolidated condensed financial statements.



**Table of Contents**

BANCORPSOUTH, INC. AND SUBSIDIARIES  
Consolidated Condensed Statements of Cash Flows  
(Unaudited)

	Three months ended March 31,	
	2006	2005
	(In thousands)	
Net cash provided by operating activities	\$ 69,946	\$ 76,877
Investing activities:		
Proceeds from calls and maturities of held-to-maturity securities	86,126	118,880
Proceeds from calls and maturities of available-for-sale securities	108,169	67,816
Proceeds from sales of available-for-sale and trading securities		33,295
Purchases of held-to-maturity securities	(451,766)	(48,440)
Purchases of available-for-sale securities	(94,897)	(28,112)
Net (increase) decrease in short-term investments	185,233	(57,661)
Net increase in loans and leases	(29,627)	(72,686)
Purchases of premises and equipment	(15,627)	(13,400)
Proceeds from sale of premises and equipment	2,409	149
Net cash paid for acquisitions	(475)	(248)
Other, net	3,220	(1,269)
Net cash used in investing activities	(207,235)	(1,676)
Financing activities:		
Net increase in deposits	185,945	20,316
Net decrease in short-term debt and other liabilities	(106,753)	(35,736)
Repayment of long-term debt	(371)	(2,786)
Issuance of common stock	1,276	2,656
Purchase of common stock	(2,968)	(4,126)
Payment of cash dividends	(14,956)	(18,802)
Net cash provided by financing activities	62,173	(38,478)
Increase (decrease) in cash and cash equivalents	(75,116)	36,723
Cash and cash equivalents at beginning of period	468,468	322,536
Cash and cash equivalents at end of period	\$ 393,352	\$ 359,259

See accompanying notes to consolidated condensed financial statements.

Table of Contents

**BANCORPSOUTH, INC. AND SUBSIDIARIES**  
**Notes to Consolidated Condensed Financial Statements**  
**(Unaudited)**

**NOTE 1 BASIS OF FINANCIAL STATEMENT PRESENTATION AND PRINCIPLES OF CONSOLIDATION**

The accompanying unaudited interim consolidated condensed financial statements of BancorpSouth, Inc. (the Company ) have been prepared in conformity with accounting principles generally accepted in the United States of America and follow general practices within the industries in which the Company operates. For further information, refer to the audited consolidated financial statements and footnotes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005. In the opinion of management, all adjustments necessary for a fair presentation of the consolidated condensed financial statements have been included and all such adjustments were of a normal recurring nature. The results of operations for the three-month period ended March 31, 2006 are not necessarily indicative of the results to be expected for the full year.

The consolidated condensed financial statements include the accounts of the Company, its wholly-owned subsidiaries, BancorpSouth Bank (the Bank ) and Risk Advantage, Inc., and the Bank s wholly-owned subsidiaries, Century Credit Life Insurance Company, Personal Finance Corporation, BancorpSouth Insurance Services, Inc., BancorpSouth Investment Services, Inc. and BancorpSouth Municipal Development Corporation.

Key employees and directors of the Company and its subsidiaries have been granted stock options under the Company s stock incentive plans. Prior to January 1, 2006, the Company accounted for those plans under the recognition and measurement principles of Accounting Principles Board ( APB ) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. No stock-based employee compensation cost was reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The fair value of each option granted was estimated on the date of grant using the Black-Scholes option-pricing model. The Company adopted Statement of Financial Accounting Standards ( SFAS ) No. 123R, Share-Based Payment, on January 1, 2006. As a result of the adoption of SFAS No. 123R, the Company recognized compensation cost for previously granted unvested awards of approximately \$21,000 during the first quarter of 2006. These awards were granted in 2005 with a fair value determined using the Black-Scholes option-pricing model with the following assumptions: 10 year expected option life, 3.40% dividend yield, 21.00% volatility and 3.50% risk-free interest rate. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, Accounting for Stock-Based Compensation, for the three months ended March 31, 2005:

		Three months ended March 31, 2005 (In thousands, except per share amounts)
Net income, as reported	\$	31,744
Deduct: Stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects		(174)
Pro forma net income	\$	31,570
Basic earnings per share: As reported	\$	0.41
Pro forma		0.40
Diluted earnings per share: As reported	\$	0.40
Pro forma		0.40

**Table of Contents****NOTE 2 LOANS AND LEASES**

The composition of the loan and lease portfolio by collateral type as of the dates indicated was as follows:

	March 31,		December
	2006	2005	31,
	(In thousands)		2005
Commercial and agricultural	\$ 922,152	\$ 833,095	\$ 930,259
Consumer and installment	377,204	391,331	388,610
Real estate mortgage:			
1-4 Family	2,557,335	2,338,940	2,518,224
Other	3,244,839	3,072,031	3,228,445
Lease financing	298,336	264,339	302,311
Other	33,290	36,383	33,363
Total	\$ 7,433,156	\$ 6,936,119	\$ 7,401,212

The following table presents information concerning non-performing loans as of the dates indicated:

	March 31,		December
	2006	2005	31,
	(In thousands)		2005
Non-accrual loans	\$ 10,157	\$ 13,184	\$ 8,816
Loans 90 days or more past due	13,661	16,622	17,744
Restructured loans	2,197	2,182	2,239
Total non-performing loans	\$ 26,015	\$ 31,988	\$ 28,799

**NOTE 3 ALLOWANCE FOR CREDIT LOSSES**

The following table summarizes the changes in the allowance for credit losses for the periods indicated:

	Three months ended		Year ended
	March 31,		December
	2006	2005	31,
	(In thousands)		2005
Balance at beginning of period	\$ 101,500	\$ 91,673	\$ 91,673
Provision charged (credited) to expense	(3,860)	4,787	24,467
Recoveries	915	1,531	4,557
Loans and leases charged off	(2,538)	(5,285)	(20,433)
Other, net			1,236
Balance at end of period	\$ 96,017	\$ 92,706	\$ 101,500

**Table of Contents****NOTE 4 PER SHARE DATA**

The computation of basic earnings per share is based on the weighted average number of common shares outstanding. The computation of diluted earnings per share is based on the weighted average number of common shares outstanding plus the shares resulting from the assumed exercise of all outstanding share-based awards using the treasury stock method.

The following table provides a reconciliation of the numerators and denominators of the basic and diluted earnings per share computations for the periods shown:

	Three months ended March 31,					
	2006			2005		
	Income (Numerator)	Shares (Denominator)	Per Share Amount	Income (Numerator)	Shares (Denominator)	Per Share Amount
	(In thousands, except per share amounts)					
<b>Basic EPS</b>						
Income available to common shareholders	\$ 37,745	79,212	\$ 0.48	\$ 31,744	78,204	\$ 0.41
Effect of dilutive share-based awards		330			314	
<b>Diluted EPS</b>						
Income available to common shareholders plus assumed exercise of all outstanding share-based awards	\$ 37,745	79,542	\$ 0.47	\$ 31,744	78,518	\$ 0.40

**NOTE 5 COMPREHENSIVE INCOME**

The following table presents the components of other comprehensive income and the related tax effects allocated to each component for the periods indicated:

	Three months ended March 31,					
	Before tax amount	2006 Tax (expense) benefit	Net of tax amount	Before tax amount	2005 Tax (expense) benefit	Net of tax amount
	(In thousands)					
Unrealized gains on available-for-sale securities:						
Unrealized losses arising during holding period	\$ (1,079)	\$ 414	\$ (665)	\$ (16,674)	\$ 6,383	\$ (10,291)
Less: Reclassification adjustment for net (gains) losses realized in net income	(8)	3	(5)	(15)	6	(9)
Other comprehensive loss	\$ (1,087)	\$ 417	\$ (670)	\$ (16,689)	\$ 6,389	\$ (10,300)

Net income	37,745	31,744
Comprehensive income	\$ 37,075	\$ 21,444

**NOTE 6 JUNIOR SUBORDINATED DEBT SECURITIES**

In 2002, the Company issued \$128,866,000 in 8.15% Junior Subordinated Debt Securities to BancorpSouth Capital Trust I (the Trust ), a business trust. The Trust used the proceeds from the issuance of five million shares of 8.15% trust preferred securities, \$25 face value per share, to acquire the 8.15% Junior Subordinated Debt Securities.

8

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**Table of Contents**

Both the Junior Subordinated Debt Securities and the trust preferred securities mature on January 28, 2032 and are callable at the option of the Company after January 28, 2007.

Pursuant to the merger with Business Holding Corporation ( BHC ) on December 31, 2004, the Company assumed the liability for \$6,186,000 in Junior Subordinated Debt Securities issued to Business Holding Company Trust I, a statutory trust. Business Holding Company Trust I used the proceeds from the issuance of 6,000 shares of trust preferred securities to acquire the Junior Subordinated Debt Securities. Both the Junior Subordinated Debt Securities and the trust preferred securities mature on April 7, 2034, and are callable at the option of the Company, in whole or in part, on any January 7, April 7, July 7, or October 7 on or after April 7, 2009. The Junior Subordinated Debt Securities and the trust preferred securities pay a per annum rate of interest, reset quarterly, equal to the three-month London Interbank Offered Rate ( LIBOR ) plus 2.80% from January 30, 2004 to April 7, 2009 and thereafter at LIBOR plus 2.85%.

Pursuant to the merger with Premier Bancorp, Inc. ( Premier ) on December 31, 2004, the Company assumed the liability for \$3,093,000 in Junior Subordinated Debt Securities issued to Premier Bancorp Capital Trust I, a statutory trust. Premier Bancorp Capital Trust I used the proceeds from the issuance of 3,000 shares of trust preferred securities to acquire the Junior Subordinated Debt Securities. Both the Junior Subordinated Debt Securities and the trust preferred securities mature on November 7, 2032, and are callable at the option of the Company, in whole or in part, on any February 7, May 7, August 7 or November 7 on or after November 7, 2007. The Junior Subordinated Debt Securities and the trust preferred securities pay a per annum rate of interest, reset quarterly, equal to the three-month LIBOR plus 3.45%.

Pursuant to the merger with American State Bank Corporation ( ASB ) on December 1, 2005, the Company assumed the liability for \$6,702,000 in Junior Subordinated Debt Securities issued to American State Capital Trust I, a statutory trust. American State Capital Trust I used the proceeds from the issuance of 6,500 shares of trust preferred securities to acquire the Junior Subordinated Debt Securities. Both the Junior Subordinated Debt securities and the trust preferred securities mature on April 7, 2034, and are callable at the option of the Company, in whole or in part, on July 7, October 7, January 7 or April 7 on or after April 7, 2009. The Junior Subordinated Debt Securities and the trust preferred securities pay a per annum rate of interest, reset quarterly, equal to the three-month LIBOR plus 2.80%.

**NOTE 7 GOODWILL AND OTHER INTANGIBLE ASSETS**

The changes in the carrying amount of goodwill for the three months ended March 31, 2006 were as follows:

	Community Banking	General Corporate and Other (In thousands)	Total
Balance as of December 31, 2005	\$ 103,462	\$ 35,292	\$ 138,754
Purchase accounting adjustments	431	150	581
Balance as of March 31, 2006	\$ 103,893	\$ 35,442	\$ 139,335

**Table of Contents**

The following tables present information regarding the components of the Company's identifiable intangible assets for the dates indicated:

	As of March 31, 2006		As of December 31, 2005	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Amortized intangible assets				
Core deposit intangibles	\$ 20,699	\$ 10,038	\$ 20,699	\$ 9,455
Customer relationship intangibles	23,164	8,676	22,890	8,051
Non-solicitation intangibles	65	43	52	35
Total	\$ 43,928	\$ 18,757	\$ 43,641	\$ 17,541
Unamortized intangible assets:				
Trade names	\$ 688	\$	\$ 688	\$
Pension plan intangibles	1,057		1,057	
Total	\$ 1,745	\$	\$ 1,745	\$

	Three months ended March 31, 2006		2005	
	(In thousands)			
Aggregate amortization expense for:				
Core deposit intangibles			\$ 583	\$ 615
Customer relationship intangibles			625	697
Non-solicitation intangibles			8	6
Total			\$ 1,216	\$ 1,318

The following table presents information regarding estimated amortization expense on the Company's amortizable identifiable intangible assets for the year ended December 31, 2006, and the succeeding four years:

	Core	Customer	Non-	Total
	Deposit Intangibles	Relationship Intangibles	Solicitation Intangibles	
	(In thousands)			
Estimated Amortization Expense:				
For year ended December 31, 2006	\$2,240	\$2,361	\$ 22	\$4,623
For year ended December 31, 2007	2,015	2,047	7	4,069
For year ended December 31, 2008	1,735	1,811		3,546
For year ended December 31, 2009	1,546	1,554		3,100
For year ended December 31, 2010	1,207	1,360		2,567

**NOTE 8 PENSION AND OTHER POSTRETIREMENT BENEFITS**

The following table presents the components of net periodic benefit costs for the periods indicated:

10

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**Table of Contents**

	Pension Benefits		Other Benefits	
	Three months ended		Three months ended	
	March 31,		March 31,	
	2006	2005	2006	2005
	(In thousands)			
Service cost	\$ 1,743	\$ 1,394	\$	\$ 1
Interest cost	1,328	1,160	8	37
Expected return on assets	(1,500)	(1,413)		
Amortization of unrecognized transition amount	5	5		
Recognized prior service cost	60	62	166	198
Recognized net (gain) loss	412	215	(7)	
Net periodic benefit costs	\$ 2,048	\$ 1,423	\$ 167	\$ 236

**NOTE 9 RECENT PRONOUNCEMENTS**

In March 2006, SFAS No. 156, Accounting for Servicing of Financial Assets, was issued. SFAS No. 156 amends SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, as it relates to the accounting for separately recognized servicing assets and servicing liabilities by requiring that all separately recognized servicing assets and servicing liabilities be initially measured by fair value, if practicable. SFAS No. 156 also permits the subsequent measurement of separately recognized servicing assets and servicing liabilities at fair value. SFAS No. 156 was adopted by the Company effective January 1, 2006 with the Company electing to measure its servicing rights at fair value at each reporting date. The adoption of SFAS No. 156 has had no material impact on the financial position or results of operations of the Company during the first quarter of 2006.

**NOTE 10 BUSINESS COMBINATIONS**

On December 1, 2005, ASB, a financial holding company with approximately \$358 million in assets headquartered in Jonesboro, Arkansas, merged with and into the Company. Pursuant to the merger, ASB's subsidiary, American State Bank, merged with and into the Bank. Consideration paid to complete this transaction consisted of 1,127,544 shares of the Company's common stock in addition to cash paid to the ASB shareholders in the aggregate amount of \$25,001,242. This transaction was accounted for as a purchase. This acquisition was not material to the financial position or results of operations of the Company.

**NOTE 11 SEGMENT REPORTING**

The Company's principal activity is community banking, which includes providing a full range of deposit products, commercial loans and consumer loans. The general corporate and other operating segment includes leasing, mortgage lending, trust services, credit card activities, insurance services, investment services and other activities not allocated to community banking.

Results of operations and selected financial information by operating segment for the three-month period ended March 31, 2006 and 2005 were as follows:

**Table of Contents**

	Community Banking	General Corporate and Other (In thousands)	Total
Three months ended March 31, 2006:			
<b>Results of Operations</b>			
Net interest revenue	\$ 86,941	\$ 8,988	\$ 95,929
Provision for credit losses	(3,859)	(1)	(3,860)
Net interest revenue after provision for credit losses	90,800	8,989	99,789
Noninterest revenue	24,639	28,131	52,770
Noninterest expense	61,098	34,910	96,008
Income before income taxes	54,341	2,210	56,551
Income taxes	18,071	735	18,806
Net income	\$ 36,270	\$ 1,475	\$ 37,745
<b>Selected Financial Information</b>			
Total assets (at end of period)	\$ 9,906,646	\$ 1,983,270	\$ 11,889,916
Depreciation and amortization	6,092	1,298	7,390
Three months ended March 31, 2005:			
<b>Results of Operations</b>			
Net interest revenue	\$ 79,577	\$ 7,552	\$ 87,129
Provision for credit losses	4,805	(18)	4,787
Net interest revenue after provision for credit losses	74,772	7,570	82,342
Noninterest revenue	24,864	29,055	53,919
Noninterest expense	57,205	32,483	89,688
Income before income taxes	42,431	4,142	46,573
Income taxes	13,510	1,319	14,829
Net income	\$ 28,921	\$ 2,823	\$ 31,744
<b>Selected Financial Information</b>			
Total assets (at end of period)	\$ 9,063,991	\$ 1,765,113	\$ 10,829,104
Depreciation and amortization	6,028	3,545	9,573

**NOTE 12 MORTGAGE SERVICING RIGHTS**

Mortgage Servicing Rights (MSRs) are capitalized based on the fair value of the servicing right on the date the corresponding mortgage loan is sold. In determining the fair value of capitalized mortgage servicing rights, the Company utilizes the expertise of an independent third party. Utilizing assumptions about factors such as mortgage interest rates, discount rates, mortgage loan prepayment speeds, market trends and industry demand, an estimate of the fair value of the Company's capitalized MSRs is performed by the independent third party and reviewed by management. Since valuation is determined using discounted cash flow models, the primary risk inherent in MSRs is the impact of fluctuating interest rates on the estimated life of the servicing revenue stream. The use of different estimates or assumptions could also produce different fair values. The Company does not hedge the value of

capitalized MSRs and, therefore, the Company is susceptible to significant fluctuations in the fair value of its MSRs in changing interest rate environments.

**Table of Contents**

The Company has one class of servicing asset comprised of closed end loans for 1-4 family residences, secured by first liens. The following table presents the activity in the Company's one class of mortgage servicing asset for the period indicated:

	2006 (In thousands)
Fair value as of January 1	\$ 36,456
Additions:	
Origination of servicing assets	1,277
Changes in fair value:	
Due to change in valuation inputs or assumptions used in the valuation model	63
Other changes in fair value	(9)
Fair value as of March 31	\$ 37,787

All of the changes to the values of the MSRs are recorded as part of Mortgage Lending noninterest revenue on the income statement. As part of Mortgage Lending noninterest revenue, the Company recorded contractual servicing fees of \$2.02 million and \$2.06 million and servicing fees and ancillary fees of \$240 thousand and \$310 thousand for the quarters ended March 31, 2006 and 2005, respectively.

**NOTE 13 COMMITMENTS AND CONTINGENT LIABILITIES**

The State Tax Commission of the State of Mississippi completed its audit of the Bank's state income tax return for the tax years 1998 through 2001 in the second quarter of 2004. As a result of this audit, the State Tax Commission assessed the Bank additional taxes of approximately \$5.4 million along with interest and penalties totaling approximately \$3.8 million. Based on the advice of legal counsel, management believes that there is no substantial basis for the position taken by the Mississippi State Tax Commission and that the Company has meritorious defenses to dispute this assessment of additional taxes. The Company is in the midst of the administrative process and a final decision has not been rendered by the State Tax Commission. There can be no assurance that the Company will be successful in having the assessment reduced at this stage or on further appeal, if any. The Company's potential exposure with regard to this assessment will be the additional tax, interest and penalties assessed in May 2004 plus interest that will continue to accrue from May 2004 through the administrative and/or appeals process and legal costs associated with this process. Management does not believe that the outcome of this matter will have a material effect on the Company's consolidated financial position, although any significant additional assessment could have a materially adverse effect on earnings in the period in which it is recorded.

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

BancorpSouth, Inc. (the Company) is a regional financial holding company with approximately \$11.9 billion in assets headquartered in Tupelo, Mississippi. BancorpSouth Bank (the Bank), the Company's wholly-owned banking subsidiary, has commercial banking operations in Mississippi, Tennessee, Alabama, Arkansas, Texas and Louisiana. The Bank and its consumer finance, credit insurance, insurance agency and brokerage subsidiaries provide commercial banking, leasing, mortgage origination and servicing, insurance, brokerage and trust services to corporate customers, local governments, individuals and other financial institutions through an extensive network of branches and offices.

Management's discussion and analysis provides a narrative discussion of the Company's financial condition and results of operations of the Company. For a complete understanding of the following discussion, you should refer to the unaudited consolidated condensed financial statements for the three-month periods ended March 31, 2006 and 2005 and the notes to such financial statements found in Item 1. Financial Statements of this report. This discussion and analysis is based on reported financial information. The information that follows is provided to



**Table of Contents**

enhance comparability of financial information between periods and to provide a better understanding of the Company's operations.

As a financial holding company, the financial condition and operating results of the Company are heavily influenced by economic trends nationally and in the specific markets in which the Company's subsidiaries provide financial services. Most of the revenue of the Company is derived from the operation of its principal operating subsidiary, the Bank. The financial condition and operating results of the Bank are affected by the level and volatility of interest rates on loans, investment securities, deposits and other borrowed funds, and the impact of economic cycles on loan demand and creditworthiness of existing borrowers. The financial services industry is highly competitive and heavily regulated. The Company's success depends on its ability to compete aggressively within its markets while maintaining sufficient asset quality and cost controls to generate net income.

The table below summarizes the Company's net income, net income per share, return on average assets and return on average shareholders' equity for the three months ended March 31, 2006 and 2005. Management believes these amounts and ratios are key indicators of the Company's financial performance.

(Dollars in thousands, except per share amounts)	Three months ended		% Change
	2006	2005	
Net income	\$37,745	\$31,744	18.90%
Net income per share: Basic	\$ 0.48	\$ 0.41	17.07
Diluted	\$ 0.47	\$ 0.40	17.50
Return on average assets (annualized)	1.30%	1.18%	10.17
Return on average shareholders' equity (annualized)	15.72%	14.02%	12.13

The increase in net income for the first quarter of 2006 when compared to the first quarter of 2005 is attributable to several factors. The Company's primary source of revenue, net interest revenue earned by the Bank, reflected continued positive trends for the three months ended March 31, 2006 compared to the same period of 2005. Net interest revenue is the difference between interest earned on loans and investments and interest paid on deposits and other obligations. The Company's net interest revenue was positively impacted by increases in interest rates as well as the increased loan demand resulting from favorable economic activity throughout most of the Bank's markets and the Company's continued focus on funding this growth with maturing investment securities and lower-cost liabilities. These factors combined to increase the Company's net interest revenue to \$95.93 million for the first quarter of 2006, an \$8.80 million, or 10.10%, increase from \$87.13 million for the first quarter of 2005. The Company also reduced its allowance for credit losses by \$4.77 million, which had been increased in the third quarter of 2005 related to Hurricane Katrina, as the impact of the hurricane on the Company's customers has been less than originally estimated. In recent years, the Company has taken steps to diversify its revenue stream by increasing its noninterest revenue from mortgage lending activities, insurance agency activities, brokerage activities, and other bank-related fees. Management believes this diversification is important to reduce the impact of fluctuations in net interest revenue on the overall operating results of the Company. These diversification efforts resulted in an increase in insurance commissions and other bank-related fees for the three months ended March 31, 2006 as compared to the same period of 2005. However, total noninterest income decreased 2.13% for the first quarter of 2006 compared to the same period of 2005 as mortgage lending revenue decreased 43.57%. The decrease in mortgage lending revenue for the first quarter of 2006 primarily resulted from the impact of a \$1.96 million net increase in the fair value of the Company's mortgage servicing asset for the first quarter of 2005 compared to a \$52,000 net increase in the fair value of the Company's mortgage servicing asset for the first quarter of 2006. Other noninterest revenue decreased 6.39% for the first quarter of 2006 compared to the first quarter of 2005 when the Company recorded a \$1.7 million gain on the sale of the Company's membership in the PULSE Network, an electronic banking network to which the Company retains access.

Improved asset quality allowed annualized net charge-offs to fall to 0.09% of average loans for the first three months of 2006 from 0.22% of average loans for the first three months of 2005. Noninterest expense totaled \$96.0 million for the first quarter of 2006 compared to \$89.69 million for the first quarter of 2005, an increase of \$6.32



**Table of Contents**

million, or 7.05%. The increase in noninterest expense for the first quarter of 2006 resulted primarily from the impact of costs related to the integration and operation of American State Bank Corporation that was acquired and merged into the Company on December 1, 2005 and increased costs related to additional locations and facilities added since March 31, 2005. The major components of net income are discussed in more detail in the various sections that follow.

**CRITICAL ACCOUNTING POLICIES**

During the three months ended March 31, 2006, there was no significant change in the Company's critical accounting policies and no significant change in the application of critical accounting policies as presented in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, with the exception of the following change regarding mortgage servicing rights.

**Mortgage Servicing Rights**

The Company recognizes as assets the rights to service mortgage loans for others, known as MSR's. Prior to the Company's adoption of SFAS No. 156, MSR's were capitalized based on the relative fair value of the servicing right and the mortgage loan on the date the mortgage loan is sold. As a result of the Company's adoption of SFAS No. 156 on January 1, 2006, the Company carries MSR's at fair value. In determining the fair value of capitalized mortgage servicing rights, the Company utilizes the expertise of an independent third party. Utilizing assumptions about factors such as mortgage interest rates, discount rates, mortgage loan prepayment speeds, market trends and industry demand, an estimate of the fair value of the Company's capitalized MSR's is performed by the independent third party and reviewed by management. Since valuation is determined using discounted cash flow models, the primary risk inherent in MSR's is the impact of fluctuating interest rates on the estimated life of the servicing revenue stream. The use of different estimates or assumptions could also produce different fair values. The Company does not hedge the value of capitalized MSR's and, therefore, the Company is susceptible to significant fluctuations in the fair value of its MSR's in changing interest rate environments. At March 31, 2006, the Company's mortgage servicing asset was \$37.79 million.

**RESULTS OF OPERATIONS****Net Interest Revenue**

Net interest revenue is the difference between interest revenue earned on assets, such as loans, leases and securities, and interest expense paid on liabilities, such as deposits and borrowings, and continues to provide the Company with its principal source of revenue. Net interest revenue is affected by the general level of interest rates, changes in interest rates and by changes in the amount and composition of interest earning assets and interest bearing liabilities. The Company's long-term objective is to manage those assets and liabilities to maximize net interest revenue, while balancing interest rate, credit, liquidity and capital risks. For purposes of the following discussion, revenue from tax-exempt loans and investment securities has been adjusted to a fully taxable equivalent basis, using an effective tax rate of 35%.

Net interest revenue was \$98.34 million for the three months ended March 31, 2006, compared to \$89.44 million for the same period in 2005, representing an increase of \$8.90 million, or 9.95%. The increase in net interest revenue for the first quarter of 2006 is related to the combination of growth in loans during a rising interest rate environment and the Company's continued focus on funding this growth with maturing investment securities and lower-cost liabilities. Interest revenue increased \$27.89 million, or 20.75%, to \$162.31 million for the three months ended March 31, 2006 from \$134.42 million for the three months ended March 31, 2005. The increase in interest revenue for the three months ended March 31, 2006 is attributable to a \$730.13 million, or 7.33%, increase in average interest earning assets to \$10.68 billion for the first quarter of 2006 from \$9.95 billion for the first quarter of 2005 and an increase in the yield of those assets of 68 basis points to 6.16% for the first quarter of 2006 from 5.48% for the first quarter of 2005.



**Table of Contents**

Interest expense increased \$18.99 million, or 42.22%, to \$63.97 million for the three months ended March 31, 2006 from \$44.98 million for the three months ended March 31, 2005. Average interest bearing liabilities increased \$500.68 million, or 5.95%, to \$8.91 billion for the first quarter of 2006 from \$8.41 billion for the first quarter of 2005. The average rate paid on those liabilities also increased 74 basis points to 2.91% for the first quarter of 2006 from 2.17% for the first quarter of 2005.

The relative performance of the Company's lending and deposit-raising functions is frequently measured by two calculations—net interest margin and net interest rate spread. Net interest margin is determined by dividing fully taxable equivalent net interest revenue by average earning assets. Net interest rate spread is the difference between the average fully taxable equivalent yield earned on interest earning assets (earning asset yield) and the average rate paid on interest bearing liabilities. Net interest margin is generally greater than the net interest rate spread because of the additional income earned on those assets funded by noninterest bearing liabilities, or free funding, such as noninterest bearing demand deposits and shareholders' equity.

Net interest margin for the first quarter of 2006 and 2005 was 3.73% and 3.64%, respectively, representing an increase of 9 basis points. Net interest rate spread for the first quarter of 2006 was 3.25%, a decrease of 6 basis points from 3.31% for the same period of 2005. The decrease in the net interest rate spread was primarily a result of the larger increase in the average rate paid on interest bearing liabilities, from 2.17% for the first quarter of 2005 to 2.91% for the first quarter of 2006, than the increase in the average rate earned on interest earning assets from 5.48% for the first quarter of 2005 to 6.16% for the first quarter of 2006. However, an increase in the net interest margin resulted from a larger percentage increase in the earning asset yield relative to the percentage increase in the average earning assets. The earning asset yield increase for the first quarter of 2006 was a result of favorable economic activity throughout most of the Bank's markets resulting in stronger loan demand. The Company has also invested funds from maturing securities in higher rate loans or new higher rate short- and intermediate-term investments.

**Interest Rate Sensitivity**

The interest rate sensitivity gap is the difference between the maturity or repricing opportunities of interest sensitive assets and interest sensitive liabilities for a given period of time. A prime objective of asset/liability management is to maximize net interest margin while maintaining a reasonable mix of interest sensitive assets and liabilities. The following table presents the Company's interest rate sensitivity at March 31, 2006:

**Table of Contents**

	Interest Rate Sensitivity - Maturing or Repricing Opportunities			
	0 to 90 Days	91 Days to 1 Year	Over 1 Year to 5 Years	Over 5 Years
	(In thousands)			
<b>Interest earning assets:</b>				
Interest bearing deposits with banks	\$ 6,809	\$	\$	\$
Federal funds sold and securities purchased under agreement to resell	224,298			
Held-to-maturity securities	150,238	140,962	1,108,583	378,140
Available-for-sale and trading securities	28,174	274,076	586,749	447,746
Loans and leases, net of unearned interest	3,937,735	1,322,217	2,006,867	128,468
Loans held for sale	38,521			
<b>Total interest earning assets</b>	<b>4,385,775</b>	<b>1,737,255</b>	<b>3,702,199</b>	<b>954,354</b>
<b>Interest bearing liabilities:</b>				
Interest bearing demand deposits and savings	3,530,521	312,588		
Other time deposits	844,937	1,975,130	1,335,681	3,928
Federal funds purchased and securities sold under agreement to repurchase and other short-term borrowings	643,401			
Long-term debt and junior subordinated debt securities	479	1,483	58,297	221,445
Other	23	82	246	77
<b>Total interest bearing liabilities</b>	<b>5,019,361</b>	<b>2,289,283</b>	<b>1,394,224</b>	<b>225,450</b>
Interest rate sensitivity gap	\$ (633,586)	\$ (552,028)	\$ 2,307,975	\$ 728,904
Cumulative interest sensitivity gap	\$ (633,586)	\$ (1,185,614)	\$ 1,122,361	\$ 1,851,265

**Provision for Credit Losses and Allowance for Credit Losses**

The provision for credit losses is the periodic cost of providing an allowance or reserve for estimated probable losses on loans and leases. The Bank employs a systematic methodology for determining its allowance for credit losses that considers both qualitative and quantitative factors and requires that management make material estimates and assumptions that are particularly susceptible to significant change. Some of the quantitative factors considered by the Bank include loan and lease growth, changes in nonperforming and past due loans and leases, historical loan and lease loss experience, delinquencies, management's assessment of loan and lease portfolio quality, the value of collateral and concentrations of loans and leases to specific borrowers or industries. Some of the qualitative factors that the Bank considers include existing general economic conditions and the inherent risks of individual loans and leases. The allowance for credit losses is based principally upon the Bank's loan and lease classification system, delinquencies and historic loss rates. The Bank has a disciplined approach for assigning credit ratings and classifications to individual credits. Each credit is assigned a grade by the appropriate loan officer, which serves as a basis for the credit analysis of the entire portfolio. The assigned grade reflects the borrower's creditworthiness, collateral values, cash flows and other factors. An independent loan review department of the Bank is responsible for reviewing the credit rating and classification of individual credits and assessing trends in the portfolio, adherence to internal credit policies and procedures and other factors that may affect the overall adequacy of the allowance. The work of the loan review

department is supplemented by governmental regulatory agencies in connection with their periodic examinations of the Bank, which provides an additional independent level of review. The loss factors assigned to each classification are based upon the attributes of the loans and leases typically assigned to each grade (such as loan to collateral values and borrower creditworthiness). Management periodically

**Table of Contents**

reviews the loss factors assigned in light of the general economic environment and overall condition of the loan and lease portfolio and modifies the loss factors assigned to each classification as it deems appropriate. The overall allowance generally includes a component representing the results of other analyses intended to ensure that the allowance is adequate to cover other probable losses inherent in the portfolio. This component considers analyses of changes in credit risk resulting from the differing underwriting criteria in acquired loan and lease portfolios, industry concentrations, changes in the mix of loans and leases originated, overall credit criteria and other economic indicators. The provision for credit losses, the allowance for credit losses as a percentage of loans and leases outstanding at March 31, 2006 and 2005 and net charge-offs and net charge-offs as a percentage of average loans and leases for the three months ended March 31, 2006 and 2005 are shown in the following table:

	Three months ended March 31,		% Change
	2006	2005	
	(Dollars in thousands)		
Provision for credit losses	\$(3,860)	\$4,787	(180.64)%
Allowance for credit losses as a percentage of loans and leases outstanding at period-end	1.30%	1.34%	(2.99)
Net charge-offs	\$ 1,623	\$3,754	(56.77)
Net charge-offs as a percentage of average loans and leases (annualized)	0.09%	0.22%	(59.09)

The provision for credit losses decreased for the three-month period ended March 31, 2006 compared to the three-month period ended March 31, 2005, reflecting the \$4.77 million pre-tax reduction in the allowance for credit losses related to Hurricane Katrina's impact on the Mississippi Gulf Coast region, originally recorded in the third quarter of 2005. As a result, the Company reported a credit balance in its provision for credit losses for the first quarter of 2006. As contacts with many customers have been re-established, losses related to loans in the impacted area are not expected to be as great as originally anticipated immediately following the hurricane. The Company will continue its assessment of credit losses for those loans to customers in the affected region. At March 31, 2006, \$2.64 million of the allowance for credit losses was specifically related to loans to customers in the impacted area. In addition to the reduction in the allowance for credit losses, the Company experienced an improvement in net charge-offs during the first quarter of 2006 compared to the first quarter of 2005 as net charge-offs decreased 56.77% to \$1.62 million for the three-month period ended March 31, 2006 compared to \$3.75 million for the three-month period ended March 31, 2005. The Company's credit quality remains strong as evidenced by the decrease in non-performing loans, down 18.67% compared to non-performing loans at March 31, 2005.

The breakdown of the allowance by loan and lease category is based, in part, on evaluations of specific loan and lease histories and on economic conditions within specific industries or geographical areas. Accordingly, because all of these conditions are subject to change, the allocation is not necessarily indicative of the breakdown of any future allowance or losses. The following table presents (a) the breakdown of the allowance for credit losses by loan and lease category and (b) the percentage of each category in the loan and lease portfolio to total loans and leases at the dates indicated:

**Table of Contents**

	2006		March 31, 2005		December 31, 2005	
	Allowance for Credit Losses	% of Total Loans and Leases	Allowance for Credit Losses	% of Total Loans and Leases	Allowance for Credit Losses	% of Total Loans and Leases
	(Dollars in thousands)					
Commercial and agricultural	\$ 11,252	12.41%	\$ 10,275	12.01%	\$ 12,171	12.57%
Consumer and installment	8,330	5.07%	7,427	5.65%	10,458	5.25%
Real estate mortgage	73,146	78.06%	70,805	78.01%	75,570	77.64%
Lease financing	2,983	4.01%	3,051	3.81%	3,014	4.08%
Other	306	0.45%	1,148	0.52%	287	0.46%
<b>Total</b>	<b>\$ 96,017</b>	<b>100.00%</b>	<b>\$ 92,706</b>	<b>100.00%</b>	<b>\$ 101,500</b>	<b>100.00%</b>

The following table provides an analysis of the allowance for credit losses for the periods indicated:

	Three months ended		Year ended December 31, 2005
	2006	March 31, 2005	
	(Dollars in thousands)		
Balance, beginning of period	\$ 101,500	\$ 91,673	\$ 91,673
Loans and leases charged off:			
Commercial and agricultural	(112)	(1,319)	(2,172)
Consumer and installment	(1,062)	(2,359)	(7,651)
Real estate mortgage	(1,357)	(1,352)	(10,187)
Lease financing	(7)	(255)	(423)
<b>Total loans charged off</b>	<b>(2,538)</b>	<b>(5,285)</b>	<b>(20,433)</b>
Recoveries:			
Commercial and agricultural	96	557	1,063
Consumer and installment	720	568	2,384
Real estate mortgage	95	396	1,089
Lease financing	4	10	21
<b>Total recoveries</b>	<b>915</b>	<b>1,531</b>	<b>4,557</b>
<b>Net charge-offs</b>	<b>(1,623)</b>	<b>(3,754)</b>	<b>(15,876)</b>
<b>Provision charged (credited) to operating expense</b>	<b>(3,860)</b>	<b>4,787</b>	<b>24,467</b>

Other, net			1,236
Balance, end of period	\$ 96,017	\$ 92,706	\$ 101,500
Average loans for period	\$ 7,371,764	\$ 6,874,571	\$ 7,026,009
Ratios:			
Net charge-offs to average loans (annualized)	0.09%	0.22%	0.23%

**Noninterest Revenue**

The components of noninterest revenue for the three months ended March 31, 2006 and 2005 and the corresponding percentage changes are shown in the following tables:

**Table of Contents**

	Three months ended March 31,		
	2006	2005	% Change
	(Dollars in thousands)		
Mortgage lending	\$ 3,176	\$ 5,628	(43.57)%
Service charges	15,450	14,726	4.92
Trust income	2,016	1,889	6.72
Securities gains, net	10	70	(85.71)
Insurance commissions	17,445	15,932	9.50
Other	14,673	15,674	(6.39)
Total noninterest revenue	\$ 52,770	\$ 53,919	(2.13)%

The Company's revenue from mortgage lending typically fluctuates as mortgage interest rates change and is primarily attributable to two activities, origination of new mortgage loans and servicing mortgage loans. The Company's normal practice is to generate mortgage loans to sell them in the secondary market with MSR to the loans either retained or released with the loan sold. The Company adopted SFAS No. 156 on January 1, 2006. As a result, the Company carries MSRs at fair value.

Origination revenue is comprised of loan origination fees, net gains or losses from the sale of the mortgage loans originated and the capitalized value of the MSR. Origination volume of \$122.31 million and \$121.60 million produced origination revenue of \$860 thousand and \$1.33 million for the quarters ended March 31, 2006 and 2005, respectively. Revenue from the servicing process includes fees from the actual servicing of loans and the recognition of changes in the valuation of the Company's MSRs. Revenue from the servicing of loans was \$2.26 million and \$2.34 million for the quarters ended March 31, 2006 and 2005, respectively. Revenues from changes in the valuation of the Company's MSRs are generally a result of changes in mortgage rates from the previous reporting date. An increase in mortgage rates typically result in an increase in the value of the MSRs while a decrease in mortgage rates will typically result in a decrease in the value of MSRs. The Company does not hedge the value of its MSRs and is susceptible to significant fluctuations in its value in changing interest rate environments. The revenue from the change in MSRs was \$52 thousand compared to \$1.96 million for the quarters ended March 31, 2006 and 2005, respectively.

Service charges on deposit accounts increased for the first quarter of 2006 when compared to the first quarter of 2005 because of higher volumes of items processed and growth in the number of deposit accounts. Trust income increased 6.72% for the first quarter of 2006 compared to the first quarter of 2005 as a result of increases in the value of assets under care (either managed or in custody).

Insurance commissions grew 9.50% to \$17.45 million for the first quarter of 2006 compared to the same period in 2005, after two consecutive quarters in which growth was significantly affected by the impact of Hurricane Katrina. The increase in insurance commissions is primarily a result of the increase in policies written since March 31, 2005 coupled with higher policy premiums. The Company plans to continue to expand the products and services offered by its insurance agencies.

Other noninterest revenue for the first three months of 2006 included a gain of \$2.41 million from the sale of student loans originated by the Company compared to a \$2.49 million gain for sales of student loans in the first three months of 2005. Other noninterest revenue for the first three months of 2005 included a \$1.7 million gain on the sale of the Company's membership in the PULSE network, an electronic banking network to which the Company retains access.

**Table of Contents****Noninterest Expense**

The components of noninterest expense for the three months ended March 31, 2006 and 2005 and the corresponding percentage changes are shown in the following tables:

	Three months ended March 31,		% Change
	2006	2005	
	(Dollars in thousands)		
Salaries and employee benefits	\$ 57,573	\$ 53,240	8.14%
Occupancy, net of rental income	7,442	6,412	16.06
Equipment	5,763	5,449	5.76
Other	25,230	24,587	2.62
Total noninterest expense	\$ 96,008	\$ 89,688	7.05%

Salaries and employee benefits expense for the three months ended March 31, 2006 increased compared to the same periods in 2005, primarily as a result of the salaries and employee benefits of employees of American State Bank Corporation acquired on December 1, 2005 and the hiring of employees to staff the banking locations added during 2005 and 2006. Occupancy expense also increased on a comparable three-month period basis primarily because of additional locations and facilities opened since March 31, 2005, including the acquisition in December of 2005. Equipment expense increased for the comparable three-month periods because of increased depreciation related to the equipment replacement purchases made as a result of Hurricane Katrina during the last 4 months of 2005 coupled with increases in various maintenance contracts. The increase in other noninterest expense reflected normal increases and general inflation in the cost of services and supplies purchased by the Company during the first quarter of 2006 compared to the first quarter of 2005.

**Income Tax**

Income tax expense was \$18.8 million for the first quarter of 2006, a 26.82% increase from \$14.8 million for the first quarter of 2005. The increase in income tax expense in the first quarter of 2006 compared to the first quarter of 2005 was primarily the result of the increase in net income before tax, as net income before tax increased 21.42% for the first quarter of 2006 compared to the first quarter of 2005. The effective tax rates for the first quarter of 2006 and 2005 were 33.26% and 31.84%, respectively. The increase in effective tax rates for 2006 compared to 2005 was the result of the increase in income before tax, combined with the slight decrease in overall tax exempt revenue.

**FINANCIAL CONDITION****Earning Assets**

The percentage of earning assets to total assets measures the effectiveness of management's efforts to invest available funds into the most efficient and profitable uses. Earning assets at March 31, 2006 were \$10.78 billion, or 90.66% of total assets, compared with \$10.62 billion, or 90.26% of total assets, at December 31, 2005.

The securities portfolio is used to make various term investments, to provide a source of liquidity and to serve as collateral to secure certain types of deposits. Held-to-maturity securities at March 31, 2006 were \$1.78 billion, compared with \$1.41 billion at December 31, 2005, a 25.87% increase. Available-for-sale securities were \$1.34 billion at March 31, 2006, compared to \$1.35 billion at December 31, 2005, a 1.27% decrease.

The Bank's loan and lease portfolio makes up the single largest component of the Company's earning assets. The Bank's lending activities include both commercial and consumer loans and leases. Loan and lease originations are derived from a number of sources, including direct solicitation by the Bank's loan officers, real estate broker referrals, mortgage loan companies, current savers and borrowers, builders, attorneys, walk-in customers and, in



**Table of Contents**

some instances, other lenders. The Bank has established disciplined and systematic procedures for approving and monitoring loans and leases that vary depending on the size and nature of the loan or lease. Loans and leases, net of unearned income, totaled \$7.40 billion at March 31, 2006, which represented a 0.40% increase from \$7.37 billion at December 31, 2005.

At March 31, 2006, the Company did not have any concentrations of loans in excess of 10% of total loans outstanding. Loan concentrations are considered to exist if there are amounts loaned to a multiple number of borrowers engaged in similar activities, which would cause them to be similarly impacted by economic or other conditions. However, the Company does conduct business in a geographically concentrated area, and the ability of the Company's borrowers to repay loans is to some extent dependent upon the economic conditions prevailing in the Company's market areas.

In the normal course of business, management becomes aware of possible credit problems in which borrowers exhibit potential for the inability to comply with the contractual terms of their loans, but which do not currently meet the criteria for disclosure as non-performing loans. Historically, some of these loans are ultimately restructured or placed in non-accrual status. At March 31, 2006, no particular loans of material significance were known to be potential non-performing loans.

Collateral for some of the Company's loans is subject to fair value evaluations that fluctuate with market conditions and other external factors. In addition, while the Company has certain underwriting obligations related to such evaluations from a review standpoint, evaluations of some real property and other collateral are dependent upon third party independent appraisers employed either by the Company's customers or as independent contractors of the Company.

The Company's policy provides that loans, other than installment loans, are generally placed in non-accrual status if, in management's opinion, payment in full of principal or interest is not expected or payment of principal or interest is more than 90 days past due, unless the loan is both well secured and in the process of collection. Non-performing loans were 0.35% of loans and leases, net of unearned income, at March 31, 2006 and 0.39% of loans and leases, net of unearned interest, at December 31, 2005.

**Deposits and Other Interest Bearing Liabilities**

Deposits originating within the communities served by the Bank continue to be the Company's primary source of funding its earning assets. The Company has been able to effectively compete for deposits in its primary market areas, while continuing to manage the exposure to rising interest rates. Deposits totaled \$9.79 billion at March 31, 2006 as compared to \$9.61 billion at December 31, 2005, representing a 1.94% increase. Noninterest bearing demand deposits decreased by \$8.47 million, or 0.47%, to \$1.79 billion at March 31, 2006 from \$1.80 billion at December 31, 2005, while interest bearing demand, savings and time deposits increased \$194.42 million, or 2.49%, to \$8.00 billion at March 31, 2006 from \$7.81 billion at December 31, 2005. By using maturing investment securities and lower cost demand deposits to fund recent loan growth, the Bank has restricted its growth in higher priced deposits. The most significant deposit growth in the Bank has occurred in the Mississippi Gulf Coast communities served by the Bank. The Bank's deposits there have increased \$90.91 million, or 17.37% between September 30, 2005 and March 31, 2006. This increase is primarily attributable to the receipt of insurance proceeds and other forms of financial assistance by customers affected by Hurricane Katrina. As the rebuilding process takes place along the Mississippi Gulf Coast, these deposits may be withdrawn to fund the reconstruction.

**Liquidity and Capital Resources**

One of the Company's goals is to provide adequate funds to meet increases in loan demand or any potential increase in the normal level of deposit withdrawals. This goal is accomplished primarily by generating cash from the Bank's operating activities and maintaining sufficient short-term liquid assets. These sources, coupled with a stable deposit base and a strong reputation in the capital markets, allow the Company to fund earning assets and maintain the availability of funds. Management believes that the Bank's traditional sources of maturing loans and investment securities, sales of loans held for sale, cash from operating activities and a strong base of core deposits are adequate to meet the Company's liquidity needs for normal operations over both the short-term and the long-term.

**Table of Contents**

To provide additional liquidity, the Company utilizes short-term financing through the purchase of federal funds and securities lending arrangements. Further, the Company maintains a borrowing relationship with the Federal Home Loan Bank which provides liquidity to fund term loans with borrowings of matched or longer maturities.

If the Company's traditional sources of liquidity were constrained, the Company would be forced to pursue avenues of funding not typically used and the Company's net interest margin could be impacted negatively. The Company utilizes, among other tools, maturity gap tables, interest rate shock scenarios and an active asset and liability management committee to analyze, manage and plan asset growth and to assist in managing the Company's net interest margin and overall level of liquidity. The Company's approach to providing adequate liquidity has been successful in the past and management does not anticipate any near- or long-term changes to its liquidity strategies.

**Off-Balance Sheet Arrangements**

In the ordinary course of business, the Company enters into various off-balance sheet commitments and other arrangements to extend credit that are not reflected in the consolidated condensed balance sheets of the Company. The business purpose of these off-balance sheet commitments is the routine extension of credit. While most of the commitments to extend credit are made at variable rates, included in these commitments are forward commitments to fund individual fixed-rate mortgage loans. Fixed-rate lending commitments expose the Company to risks associated with increases in interest rates. As a method to manage these risks, the Company enters into forward commitments to sell individual fixed-rate mortgage loans. The Company also faces the risk of deteriorating credit quality of borrowers to whom a commitment to extend credit has been made; however, no significant credit losses are expected from these commitments and arrangements.

**Regulatory Requirements for Capital**

The Company is required to comply with the risk-based capital guidelines established by the Board of Governors of the Federal Reserve System. These guidelines apply a variety of weighting factors that vary according to the level of risk associated with the assets. Capital is measured in two Tiers: Tier I consists of common shareholders' equity and qualifying noncumulative perpetual preferred stock, less goodwill and certain other intangible assets; and Tier II consists of general allowance for losses on loans and leases, hybrid debt capital instruments and all or a portion of other subordinated capital debt, depending upon remaining term to maturity. Total capital is the sum of Tier I and Tier II capital. The Company's Tier I capital and total capital, as a percentage of total risk-adjusted assets, was 12.48% and 13.72%, respectively, at March 31, 2006. Both ratios exceeded the required minimum levels for these ratios of 4% and 8%, respectively, at March 31, 2006. In addition, the Company's Tier I leverage capital ratio (Tier I capital divided by total assets, less goodwill) was 8.49% at March 31, 2006, compared to the required minimum leverage capital ratio of 4%.

The Federal Deposit Insurance Corporation's capital-based supervisory system for insured financial institutions categorizes the capital position for banks into five categories, ranging from well capitalized to critically undercapitalized. For a bank to classify as well capitalized, the Tier I capital, total capital and leverage capital ratios must be at least 6%, 10% and 5%, respectively. The Bank met the criteria for the well capitalized category at March 31, 2006 as its Tier I capital, total capital and leverage capital ratios were 12.07%, 13.30%, and 8.18%, respectively.

There are various legal and regulatory limits on the extent to which the Bank may pay dividends or otherwise supply funds to the Company. In addition, federal and state regulatory agencies have the authority to prevent a bank or bank holding company from paying a dividend or engaging in any other activity that, in the opinion of the agency, would constitute an unsafe or unsound practice. The Company does not expect these limitations to cause a material adverse effect with regard to its ability to meet its cash obligations.

**Table of Contents****Uses of Capital**

The Company may pursue acquisition transactions of depository institutions and businesses closely related to banking which further the Company's business strategies. The Company anticipates that consideration for any such transactions would be shares of the Company's common stock, cash or a combination thereof. For example, the merger of American State Bank Corporation was completed on December 1, 2005, and the consideration in that transaction was a combination of shares of the Company's common stock and cash.

On April 27, 2005, the Company announced a new stock repurchase program pursuant to which the Company may acquire up to 3.0 million shares of its common stock in the open market at prevailing market prices or in privately negotiated transactions during the period from May 1, 2005 through April 30, 2007. The extent and timing of any repurchases will depend on market conditions and other corporate considerations. Repurchased shares will be held as authorized but unissued shares. These authorized but unissued shares will be available for use in connection with the Company's stock option plans, other compensation programs, other transactions or for other corporate purposes as determined by the Company's Board of Directors. As of March 31, 2006, 465,500 shares had been repurchased under this program. The Company will continue to evaluate additional share repurchases under this repurchase program and will evaluate whether to adopt a new stock repurchase program before the current program expires. The Company conducts its stock repurchase program by using funds received in the ordinary course of business. The Company has not experienced, and does not expect to experience, a material adverse effect on its capital resources or liquidity in connection with its stock repurchase program during the terms of the program. See Part II, Item 2. Unregistered Sales of Equity Securities and Use of Proceeds. of this report for information about the Company's repurchases during the three months ended March 31, 2006.

From January 1, 2001 through March 31, 2006, the Company had repurchased approximately 11.0 million shares of its common stock under various approved repurchase plans.

In 2002, the Company issued \$128,866,000 in 8.15% Junior Subordinated Debt Securities to BancorpSouth Capital Trust I (the "Trust"), a business trust. The Trust used the proceeds from the issuance of 5.0 million shares of 8.15% trust preferred securities, \$25 face value per share, to acquire the 8.15% Junior Subordinated Debt Securities. Both the Junior Subordinated Debt Securities and the trust preferred securities mature on January 28, 2032, and are callable at the option of the Company after January 28, 2007. The \$125 million in trust preferred securities issued by the Trust qualifies as Tier I capital under Federal Reserve Board guidelines. The Company may prepay the Junior Subordinated Debt Securities, and in turn the trust preferred securities, at a prepayment price of 100% of the principal amount of these securities within 90 days of a determination by the Federal Reserve Board that trust preferred securities will no longer qualify as Tier I capital.

The Company assumed \$9.3 million in Junior Subordinated Debt Securities and the related \$9.0 million in trust preferred securities pursuant to the mergers on December 31, 2004 with Premier Bancorp, Inc. and Business Holding Corporation and assumed \$6.7 million in Junior Subordinated Debt Securities and the related \$6.5 million in trust preferred securities pursuant to the merger on December 1, 2005 with American State Bank Corporation (see Note 6 to the consolidated condensed financial statements included in this report). The aggregate \$15.5 million in trust preferred securities qualifies as Tier I capital under Federal Reserve Board guidelines.

**Certain Litigation Contingencies**

The Company and its subsidiaries are engaged in lines of business that are heavily regulated and involve a large volume of financial transactions with numerous customers through offices in six states. Although the Company and its subsidiaries have developed policies and procedures to minimize the impact of legal noncompliance and other disputes, litigation presents an ongoing risk.

As such, the Company and its subsidiaries are defendants in various lawsuits arising out of the normal course of business, including claims against entities to which the Company is a successor as a result of business combinations. In the opinion of management, the ultimate resolution of such matters should not have a material adverse effect on the Company's consolidated financial position or results of operations. Litigation is, however, inherently uncertain,

**Table of Contents**

and the Company cannot make assurances that it will prevail in any of these actions, nor can it estimate with reasonable certainty the amount of damages that it might incur.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

During the three months ended March 31, 2006, there were no significant changes to the quantitative and qualitative disclosures about market risks presented in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

**ITEM 4. CONTROLS AND PROCEDURES.**

The Company, with the participation of its management, including its Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rules 13a-15 and 15d-15 under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation and as of the end of the period covered by this report, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to information required to be disclosed in its reports that the Company files or submits to the Securities and Exchange Commission under the Securities Exchange Act of 1934. There have been no changes in the Company's internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II  
OTHER INFORMATION**

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.**

The Company made the following purchases of its common stock during the quarter ended March 31, 2006:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
January 1 - January 31	60,000	\$ 23.41	60,000	2,599,500
February 1 - February 28				2,599,500
March 1 - March 31	65,000	24.05	65,000	2,534,500
Total	125,000			

(1) On April 27, 2005 the Company announced a stock repurchase program pursuant to which the Company may purchase up to 3.0 million shares of its common stock prior to April 30, 2007. During the three months ended March 31, 2006, the Company terminated no repurchase plans or programs expired.

**ITEM 6. EXHIBITS.**

(3.1) Restated Articles of Incorporation of the Company (filed as Exhibit 3.1 to the Company's Registration Statement on Form S-4 (Registration No. 33-88274) filed on January 6, 1995, and incorporated herein by reference).



**Table of Contents**

- (3.2) Amendment to Restated Articles of Incorporation of the Company (filed as Exhibit 3.2 to the Company's Registration Statement on Form S-4 (Registration No. 33-88274) filed on January 6, 1995, and incorporated herein by reference).
- (3.3) Amended and Restated Bylaws of the Company (filed as Exhibit 3(b) to the Company's Annual Report on Form 10-K for the year ended December 31, 1998 (file No. 1-12991) and incorporated herein by reference).
- (3.4) Amendment to Amended and Restated Bylaws (filed as Exhibit 3(c) to the Company's Annual Report on Form 10-K for the year ended December 31, 2000 (file No. 1-12991) and incorporated herein by reference).
- (4.1) Specimen Common Stock Certificate (filed as Exhibit 4 to the Company's Annual Report on Form 10-K for the year ended December 31, 1994 (file number 0-10826) and incorporated herein by reference).
- (4.2) Rights Agreement, dated as of April 24, 1991, including as Exhibit A the forms of Rights Certificate and of Election to Purchase and as Exhibit B the summary of Rights to Purchase Common Shares (filed as Exhibit 1 to the Company's registration statement on Form 8-A filed April 24, 1991 (file number 0-10826) and incorporated herein by reference).
- (4.3) First Amendment to Rights Agreement, dated as of March 28, 2001 (filed as Exhibit 2 to the Company's amended registration statement on Form 8-A/A filed March 28, 2001 (file number 1-12991) and incorporated herein by reference).
- (4.4) Amended and Restated Certificate of Trust of BancorpSouth Capital Trust I, dated as of October 31, 2001 (filed as Exhibit 4.12 to the Company's Registration Statement on Form S-3 filed on November 2, 2001 (Registration No. 33-72712) and incorporated herein by reference).
- (4.5) Second Amended and Restated Trust Agreement of BancorpSouth Capital Trust I, dated as of January 28, 2002 (filed as Exhibit 4.13 to the Company's Current Report on Form 8-K filed on January 28, 2002 and incorporated herein by reference).
- (4.6) Junior Subordinated Indenture, dated as of January 28, 2002 (filed as Exhibit 4.8 to the Company's Current Report on Form 8-K filed on January 28, 2002 (file number 1-12991) and incorporated herein by reference).
- (4.7) Guarantee Agreement (filed as Exhibit 4.25 to the Company's Current Report on Form 8-K filed on January 28, 2002 (file number 1-12991) and incorporated herein by reference).
- (4.8) Junior Subordinated Debt Security Specimen (filed as an exhibit to the Company's Current Report on Form 8-K filed on January 28, 2002 (file number 1-12991) and incorporated herein by reference).
- (4.9) Trust Preferred Security Certificate for BancorpSouth Capital Trust I (filed as an exhibit to the Company's Current Report on Form 8-K filed on January 28, 2002 (file number 1-12991) and incorporated herein by reference).
- (4.10) Certain instruments defining the rights of certain holders of long-term debt securities of the Registrant are omitted pursuant to Item 601(b)(4)(iii)(A) of Regulation S-K. The Registrant hereby agrees to furnish copies of these instruments to the SEC upon request.
- (31.1)

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Certification of the Chief Executive Officer of BancorpSouth, Inc. pursuant to Rule 13a-14 or 15d-14 of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*

- (31.2) Certification of the Chief Financial Officer of BancorpSouth, Inc. pursuant to Rule 13a-14 or 15d-14 of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.\*
- (32.1) Certification of the Chief Executive Officer of BancorpSouth, Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*
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\* Filed herewith.

**Table of Contents**

**SIGNATURES**

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

BancorpSouth, Inc.

(Registrant)

DATE: May 4, 2006

/s/ L. Nash Allen, Jr.

L. Nash Allen, Jr.  
Treasurer and  
Chief Financial Officer



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