

**BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM**

Washington, D.C. 20551

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 September 30, 2008

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

For the Transition Period from _____ to _____

FDIC Certificate No. 57659

MIDSOUTH BANK

(Exact name of registrant as specified in its charter)

Tennessee

(State or Other Jurisdiction of
Incorporation or Organization)

75-3143086

(IRS Employer Identification Number)

One East College Street, Murfreesboro, TN 37133-7100

(Address of principal executive offices)

(615) 278-7100

(Registrant's telephone number)

N/A

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

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

Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: Common stock, \$1.00 par value, outstanding: 3,748,367 shares at November 6, 2008.

MIDSOUTH BANK

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

The unaudited consolidated financial statements of the Registrant, MidSouth Bank (the “Bank”), which are included in this Report are as follows:

Consolidated Balance Sheets - September 30, 2008 and December 31, 2007.

Consolidated Statements of Operations - For the three months and nine months ended September 30, 2008 and 2007.

Consolidated Statements of Comprehensive Earnings (Losses) - For the three months and nine months ended September 30, 2008 and 2007.

Consolidated Statements of Cash Flows - For the nine months ended September 30, 2008 and 2007.

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Item 4T. Controls and Procedures

Certain information for this part of the Report is incorporated by reference to Item 2 of Part I of this Report, entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

Item 1A. Risk Factors

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

Item 3. Defaults Upon Senior Securities

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PART I – FINANCIAL INFORMATION
Item 1 – Financial Statements

MIDSOUTH BANK

Consolidated Balance Sheets

September 30, 2008 and December 31, 2007

	September 30, 2008 <i>(Unaudited)</i>	December 31, 2007 <i>(Audited)</i>
	<i>(In thousands)</i>	
<u>Assets</u>		
Loans, less allowance for loan losses of \$2,269,000 and \$2,032,000, respectively	\$ 207,479	191,074
Securities available-for-sale, at market (amortized cost of \$29,386,000 and \$30,848,000, respectively)	29,682	31,248
Loans held for sale	170	987
Federal funds sold	223	-
Restricted equity securities	1,611	1,439
Interest-bearing accounts at other financial institutions	13	20
Total earning assets	<u>239,178</u>	<u>224,768</u>
Cash and due from banks	8,663	8,838
Bank premises and equipment, net	10,249	10,752
Accrued interest receivable	914	1,054
Foreclosed assets	1,525	1,309
Other assets	<u>291</u>	<u>261</u>
Total assets	<u>\$ 260,820</u>	<u>246,982</u>
<u>Liabilities and Stockholders' Equity</u>		
Deposits	\$ 220,632	207,448
Advances from Federal Home Loan Bank	7,465	7,346
Federal funds purchased and securities sold under agreement to repurchase	1,632	226
Accrued interest payable	276	631
Accounts payable and other liabilities	<u>518</u>	<u>353</u>
Total liabilities	<u>230,523</u>	<u>216,004</u>
Stockholders' equity:		
Preferred stock, no par, authorized 20,000,000 shares, no shares issued	-	-
Common stock, par value \$1 per share, authorized 20,000,000 shares, 3,747,867 and 3,741,629 shares issued and outstanding, respectively	3,748	3,742
Additional paid-in capital	33,852	33,774
Deficit	(7,599)	(6,938)
Net unrealized gains on available-for-sale securities	<u>296</u>	<u>400</u>
Total stockholders' equity	<u>30,297</u>	<u>30,978</u>
COMMITMENTS AND CONTINGENCIES		
Total liabilities and stockholders' equity	<u>\$ 260,820</u>	<u>246,982</u>

See accompanying notes to consolidated financial statements (unaudited).

MIDSOUTH BANK

Consolidated Statements of Operations

Three Months and Nine Months Ended September 30, 2008 and 2007

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
	(In Thousands, Except Per Share Amounts)			
Interest income:				
Interest and fees on loans	\$ 3,184	\$ 3,373	\$ 9,521	\$ 9,451
Interest and dividends on taxable securities	408	486	1,252	1,444
Interest on Federal funds sold	-	8	7	184
Interest and dividends on restricted equity securities	23	20	65	52
Total interest income	3,615	3,887	10,845	11,131
Interest expense:				
Interest on negotiable order of withdrawal accounts	30	84	113	262
Interest on money market and other savings accounts	197	252	650	710
Interest on certificates of deposit	1,011	1,445	3,525	4,399
Interest on advances from Federal Home Loan Bank	90	14	198	14
Interest on Federal funds purchased and securities sold under agreement to repurchase	24	14	34	20
Total interest expense	1,352	1,809	4,520	5,405
Net interest income before provision for loan losses	2,263	2,078	6,325	5,726
Provision for loan losses	365	122	994	240
Net interest income after provision for loan losses	1,898	1,956	5,331	5,486
Non-interest income:				
Service charges on deposit accounts	127	80	334	214
Other fees and commissions	107	85	282	234
Fees from mortgage originations	131	102	366	320
Fees from brokerage operations	138	139	407	342
Gain on sale of restricted equity securities	-	14	-	14
Gain (loss) on sales of foreclosed assets, net	(37)	-	4	-
Total non-interest income	466	420	1,393	1,124
Non-interest expenses:				
Salaries and employee benefits	1,284	1,163	3,853	3,381
Occupancy expenses	223	205	659	571
Furniture and equipment expense	120	108	381	328
FDIC insurance	42	44	126	90
Advertising expense	100	95	317	265
Professional fees	106	81	350	208
Data processing expense	148	129	460	405
Director fees	31	28	93	84
Other operating expense	403	354	1,146	1,038
Total non-interest expenses	2,457	2,207	7,385	6,370
Earnings (loss) before income taxes	(93)	169	(661)	240
Income taxes	-	-	-	-
Earnings (loss)	\$ (93)	\$ 169	\$ (661)	\$ 240
Basic earnings (loss) per common share	\$ (0.02)	\$ 0.05	\$ (0.18)	\$ 0.07
Diluted earnings (loss) per common share	\$ (0.02)	\$ 0.04	\$ (0.18)	\$ 0.06

See accompanying notes to consolidated financial statements (unaudited).

MIDSOUTH BANK

Consolidated Statements of Comprehensive Earnings (Losses)

***Three Months and Nine Months Ended September 30, 2008 and 2007
(Unaudited)***

	Three Months Ended September 30,		Nine Months Ended September 30,	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
Net earnings (loss)	\$ (93)	\$ 169	\$ (661)	\$ 240
Other comprehensive losses:				
Unrealized gains (losses) on available-for-sale securities arising during period	<u>472</u>	<u>527</u>	<u>(104)</u>	<u>(48)</u>
Comprehensive earnings (losses)	<u>\$ 379</u>	<u>\$ 696</u>	<u>\$ (765)</u>	<u>\$ 192</u>

See accompanying notes to consolidated financial statements (unaudited).

MIDSOUTH BANK

Consolidated Statements of Cash Flows

Nine Months Ended September 30, 2008 and 2007

Increase (Decrease) in Cash and Cash Equivalents

(Unaudited)

	Nine Months Ended September 30, <u>2008</u> <u>2007</u> (In Thousands)	
Cash flows from operating activities:		
Interest received	\$ 10,936	\$ 10,970
Fees received	1,023	1,124
Proceeds from sale of loans	29,886	23,159
Origination of loans held for sale	(28,703)	(21,763)
Interest paid	(4,875)	(5,507)
Cash paid to suppliers and employees	<u>(6,651)</u>	<u>(5,881)</u>
Net cash provided by operating activities	<u>1,616</u>	<u>2,102</u>
Cash flows from investing activities:		
Repayments of mortgage-backed securities	3,092	2,617
Purchase of available-for-sale securities	(7,490)	(5,997)
Purchase of restricted equity securities	(172)	(428)
Sale of restricted equity securities	-	145
Maturities of available-for-sale securities	5,909	5,210
Loans made to customers, net of repayments	(18,571)	(32,126)
Capitalized cost of foreclosed assets	(64)	-
Proceeds from sales of foreclosed assets	1,024	-
Purchase of premises and equipment	<u>(74)</u>	<u>(260)</u>
Net cash used in investing activities	<u>(16,346)</u>	<u>(30,839)</u>
Cash flows from financing activities:		
Net increase in non-interest bearing, savings and NOW deposit accounts	5,279	576
Net increase in time deposits	7,871	3,036
Net increase in mortgage escrow deposits	34	38
Proceeds from advances from the Federal Home Loan Bank	71,584	10,750
Repayments of advances from the Federal Home Loan Bank	(71,465)	(3,200)
Increase in securities sold under agreement to repurchase	1,632	-
Repayments of Federal funds purchased	(226)	-
Proceeds from sale of common stock	<u>62</u>	<u>4,167</u>
Net cash provided by financing activities	<u>14,771</u>	<u>15,367</u>
Net increase (decrease) in cash and cash equivalents	41	(13,370)
Cash and cash equivalents at beginning of period	<u>8,858</u>	<u>19,599</u>
Cash and cash equivalents at end of period	<u>\$ 8,899</u>	<u>\$ 6,229</u>

See accompanying notes to consolidated financial statements (unaudited).

MIDSOUTH BANK

Consolidated Statements of Cash Flows, Continued

Nine Months Ended September 30, 2008 and 2007

Increase (Decrease) in Cash and Cash Equivalents

(Unaudited)

	<u>2008</u>	<u>2007</u>
	<i>(In Thousands)</i>	
Reconciliation of earnings (loss) to net cash provided by operating activities:		
Earnings (loss)	\$ (661)	\$ 240
Adjustments to reconcile earnings (loss) to net cash provided by operating activities:		
Depreciation	559	453
Provision for loan losses	994	240
Stock option compensation expense	22	46
Amortization and accretion, net	(49)	(67)
Decrease in loans held for sale	817	1,396
Gain on sale of restricted equity securities	-	(14)
Decrease (increase) in accrued interest receivable	140	(66)
Decrease in accrued interest payable	(355)	(102)
Increase in other assets	(12)	(48)
Gain on sale of foreclosed assets	(4)	-
Increase in other liabilities	<u>165</u>	<u>24</u>
Total adjustments	<u>2,277</u>	<u>1,862</u>
Net cash provided by operating activities	<u>\$ 1,616</u>	<u>\$ 2,102</u>

Supplemental Schedule of Non-Cash Activities:

Unrealized loss in value of securities available-for-sale	<u>\$ (104)</u>	<u>\$ (48)</u>
Transfer of loans to other real estate	<u>\$ 1,172</u>	<u>\$ 851</u>

See accompanying notes to consolidated financial statements (unaudited).

MIDSOUTH BANK

Notes to Consolidated Financial Statements

(Unaudited)

Basis of Presentation

The accompanying consolidated financial statements have been prepared, without audit, pursuant to the rules and regulations of the Board of Governors of the Federal Reserve System. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. The consolidated financial statements include the financial results of MidSouth Bank and its wholly-owned subsidiary, MSB Services, Inc. (collectively the "Bank"). All intercompany accounts have been eliminated in consolidation.

In the opinion of management, the consolidated financial statements contain all adjustments and disclosures necessary to summarize fairly the financial position of the Bank as of September 30, 2008 and December 31, 2007 and the results of operations for the three and nine months ended September 30, 2008 and 2007, comprehensive earnings (losses) for the three and nine months ended September 30, 2008 and 2007 and changes in cash flows for the nine months ended September 30, 2008 and 2007. All adjustments were of a normal recurring nature. The interim financial statements should be read in conjunction with the notes to the consolidated financial statements presented in the Bank's Annual Report on Form 10-KSB as filed with the Board of Governors of the Federal Reserve System. The results for interim periods are not necessarily indicative of results to be expected for the complete fiscal year.

Certain reclassifications have been made to 2007 financial information to conform to the 2008 presentation.

Critical Accounting Policies

Our accounting and reporting policies are in accordance with accounting principles generally accepted in the United States of America as defined by the Public Company Accounting Oversight Board and conform to general practices accepted within the banking industry. Our most significant accounting policies are presented in the Bank's December 31, 2007 Form 10-KSB and the notes to the audited consolidated financial statements contained therein. Certain accounting policies require management to make significant estimates and assumptions that have a material effect on the carrying value of certain assets and liabilities, and we consider these to be critical accounting policies. The estimates and assumptions used are based on historical experience and other factors that management believes to be reasonable under the circumstances. Actual results could differ significantly from these estimates and assumptions, which could have a material impact on the carrying value of assets and liabilities at the balance sheet dates and on our results of operations for the reporting periods.

MIDSOUTH BANK

Notes to Consolidated Financial Statements, Continued

(Unaudited)

Allowance for Loan Losses

Transactions in the allowance for loan losses were as follows:

	Nine Months Ended September 30,	
	<u>2008</u>	<u>2007</u>
	<i>(In Thousands)</i>	
Balance, January 1, 2008 and 2007, respectively	\$ 2,032	1,922
Add (deduct):		
Losses charged to allowance	(761)	(274)
Recoveries credited to allowance	4	69
Provision for loan losses	994	240
Adjustment to reclassify allowance for off-balance sheet items	-	(10)
Balance, September 30, 2008 and 2007, respectively	<u>\$ 2,269</u>	<u>1,947</u>

The provision for loan losses was \$994,000 and \$240,000 for the first nine months of 2008 and 2007, respectively. The increase in the provision from 2007 to 2008 is due to growth in the loan portfolio over the last year, to reserve for some loan losses that the Bank has taken in 2008 and to provide for experientially anticipated losses in the Bank's loan portfolio in the areas of real estate, construction and commercial lending. This is discussed in more detail under "Results of Operations." The provision for loan losses represents a charge to earnings necessary, after loan charge-offs and recoveries, to maintain the allowance for loan losses at an appropriate level which is adequate to absorb estimated losses inherent in the loan portfolio. Such estimated losses arise primarily from the loan portfolio but may also result from other sources, including commitments to extend credit and letters of credit. The level of the allowance is determined on a monthly basis using procedures which include: (1) categorizing commercial and commercial real estate loans into risk categories to estimate loss probabilities based primarily on the historical loss experience of those risk categories and current economic conditions; (2) analyzing significant commercial and commercial real estate credits and calculating specific reserves as necessary; (3) assessing various homogeneous consumer loan categories to estimate loss probabilities based primarily on historical loss experience; and (4) considering various other factors, such as changes in credit concentrations, loan mix, and economic conditions which may not be specifically quantified in the loan analysis process.

The allowance for loan losses consists of an allocated portion and an unallocated or general portion. The allocated portion is maintained to cover estimated losses applicable to specific segments of the loan portfolio. The unallocated portion is maintained to absorb losses which probably exist as of the evaluation date but are not identified by the more objective processes used for the allocated portion of the allowance due to risk of errors or imprecision. While the total allowance consists of an allocated portion and an unallocated portion, these terms are primarily used to describe a process. Both portions of the allowance are available to provide for inherent loss in the entire portfolio.

The allowance for loan losses is increased by provisions for loan losses charged to expense and is reduced by loans charged off net of recoveries on loans previously charged off. The provision is based on management's determination of the amount of the allowance necessary to provide for estimated loan losses based on its evaluation of the loan portfolio. Determining the appropriate level of the allowance and the amount of the provision involves uncertainties and matters of judgment and therefore cannot be determined with precision.

MIDSOUTH BANK

Notes to Consolidated Financial Statements, Continued

(Unaudited)

Stock Option Arrangement

In October, 2004, the Shareholders of the Bank approved the MidSouth Bank 2004 Stock Option Arrangement (the "Arrangement"). The Arrangement provides for the granting of stock options, and authorizes the issuance of common stock upon the exercise of such options, for up to 380,000 shares of common stock to employees and organizers of the Bank and up to 143,080 shares of common stock for future use as decided by the Directors of the Bank. As of September 30, 2008, 470,000 options had been granted of which 41,500 have been exercised and 6,500 have been forfeited. Options that are forfeited revert to the Arrangement and can be granted again in the future. As of September 30, 2008, 335,978 options were exercisable. The weighted average exercise price of outstanding stock options and exercisable stock options for the nine months ended September 30, 2008 was \$10.03 per share and \$10.00 per share, respectively. The weighted average remaining contractual term of outstanding and exercisable stock options for the nine months ended September 30, 2008 was 6.0 years and 5.9 years, respectively. The aggregate intrinsic value of outstanding and exercisable stock options for the nine months ended September 30, 2008 was \$831,000 and \$672,000, respectively. As of September 30, 2008, there were total unrecognized compensation costs of \$53,000 related to non-vested share-based compensation arrangements granted under the Arrangement. Those costs are expected to be recognized over a remaining weighted average period of 1.7 years. Compensation expense related to stock options totaled \$22,000 and \$46,000 for the nine months ended September 30, 2008 and 2007, respectively, and \$4,000 and \$21,000 for the three months ended September 30, 2008 and 2007, respectively.

Under the Arrangement, stock option awards may be granted in the form of incentive stock options or non-statutory stock options, with a ten-year option to purchase. Exercise prices of incentive stock options must be equal to or greater than 100% of the fair market value of the common stock on the grant date and otherwise in compliance with the requirements of the Internal Revenue Code applicable to incentive stock options and the terms of the Plan.

Stock Warrants

As part of the original offering, any shares purchased received non-detachable common stock purchase warrants which provide the stockholder the ability to purchase one additional whole share of common stock for every two shares of common stock purchased. The purchase price for the additional shares is equal to the greater of \$10 or 110% of the book value of the stock at the date of exercise. For each recipient, one half of the warrants received were required to be exercised within three years from January 20, 2004 (the date of issuance) and the other half within five years of the date of issuance. Any unexercised "three-year" warrants have expired. All remaining "five-year" warrants that are not exercised by January 20, 2009 will be forfeited. As of September 30, 2008, 606,071 of these warrants have been exercised, 128,690 have been forfeited or cancelled and 524,225 are exercisable.

Fair Value

During the first quarter of 2008, the Bank adopted Statement of Financial Accounting Standards ("SFAS") No. 157 "Fair Value Measurements," which establishes a fair value hierarchy and requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) or identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

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

Level 3: Unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

MIDSOUTH BANK

Notes to Consolidated Financial Statements, Continued

(Unaudited)

Assets and Liabilities Measured on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis are summarized below:

<i>(in 000's)</i>	Fair Value Measurements at September 30, 2008 Using			
	Carrying Value at September 30, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>Assets:</u>				
Available-for-sale securities	\$ 29,682	-	29,682	-
Impaired loans	5,717	-	5,717	-

Available-for-sale securities are measured on a recurring basis and are obtained from an independent pricing service. The fair values are based on quoted market prices of comparable securities, broker quotes or comprehensive interest rate tables and pricing matrices.

Impaired loan balances in the table above represent those collateral-dependent loans where management has estimated the credit loss by comparing the loans' carrying values against the expected realized fair values of the collateral securing those loans. As of September 30, 2008, impaired loans had a carrying amount of \$6,174,000, with a valuation allowance of \$457,000.

Recently Issued Pronouncements

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

In October 2008, the FASB issued FASB Staff Position ("FSP") No. 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active." This FSP clarifies the application of SFAS No. 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. This FSP was effective for the Bank upon issuance, including prior periods for which financial statements have not been issued; and, therefore was effective for the Bank's financial statements as of and for the three and nine month periods ended September 30, 2008. Adoption of FSP No. FAS 157-3 did not have a significant impact on the Bank's financial position, results of operations or cash flows.

MIDSOUTH BANK

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

General

MidSouth Bank is a state chartered bank which began operations on January 20, 2004. The reader should keep in mind that many of the items discussed in this Report are affected by the fact that the Bank is a relatively new financial institution with limited operating history and results. Such things as "percentage increases" or "percentage decreases" can be deceptively large based on the fact that the Bank is growing rapidly and has been conducting banking operations for a relatively short period of time.

MidSouth Bank operates as a full-service community bank chartered under the laws of the State of Tennessee with deposits insured through the Deposit Insurance Fund administered by the Federal Deposit Insurance Corporation ("FDIC"). It is a member of the Federal Reserve System and its primary federal regulator is the Board of Governors of the Federal Reserve System ("Federal Reserve"). The Bank offers a wide range of banking services including checking, savings, money market accounts, certificates of deposit and loans for consumers and businesses. The Bank has trust powers and has an active trust department that provides both trust services and (as agent) alternative investment products for its customers. The Bank is subject to regulation, supervision, and examination by the Tennessee Department of Financial Institutions and the Federal Reserve. However, such regulation, supervision and examination are for the protection of consumers, the Deposit Insurance Fund administered by the FDIC, and the banking system and not for the protection of investors or other stakeholders. The area served by MidSouth Bank is Rutherford County in Tennessee, and adjacent geographic areas in Middle Tennessee. Services are provided at the main office, three full-service banking offices in Murfreesboro, Tennessee and two full-service banking offices located in Smyrna, Tennessee.

The Bank has targeted commercial business lending, commercial residential real estate lending and consumer lending as potential growth areas in its highly competitive markets. The Bank seeks to build a loan portfolio which is capable of adjusting to swings in the interest rate market, and it is the Bank's policy to maintain a diverse loan portfolio not dependent on any particular market or industrial segment.

The purpose of this discussion is to provide insight into the financial condition and results of operations of the Bank. This discussion should be read in conjunction with the annual consolidated financial statements filed in conjunction with the Bank's Annual Report on Form 10-KSB for the year ended December 31, 2007 as filed with the Federal Reserve in March of 2008. The Annual Report on Form 10-KSB also contains important information concerning the Bank, its operations, applicable laws and regulations, and other matters.

As noted above, percentage increases in the financial statements of relatively new banks, like MidSouth Bank, can be misleading. They tend to be larger and more volatile than would be the case for most banks that have been established for extended periods of time.

Recent Developments

The U. S. and global economies have experienced and are experiencing significant stress and disruptions in the financial sector. Dramatic slowdowns in the housing industry with falling home prices and increasing foreclosures and unemployment have resulted in major issues for financial institutions, including government-sponsored entities and investment banks. As the impact of financial declines ripples through the economy, it can be expected that many or most economic sectors will be adversely affected, thus impacting many or most components of the Bank's customer base. These issues have caused many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail.

In response to the financial crisis affecting the banking and financial markets, in October 2008, the Emergency Economic Stabilization Act of 2008 (the "EESA") was signed into law. Pursuant to the EESA, the U. S. Treasury (the "Treasury") will have the authority to, among other things, purchase up to \$700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U. S. financial markets.

MIDSOUTH BANK

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

Recent Developments (continued)

In addition, the Treasury announced that it has been authorized to purchase equity positions in U. S. financial institutions. Under this program, known as the Troubled Assets Relief Program Capital Purchase Program (the "TARP Capital Purchase Program"), from the \$700 billion authorized by the EESA, the Treasury will be allowed to purchase up to \$250 billion of senior preferred stock in U. S. financial institutions. In conjunction with the purchase of senior preferred stock, the Treasury will receive warrants to purchase common stock with an aggregate market price equal to 15% of the total amount of the senior preferred investment. Participating financial institutions will be required to adopt the Treasury's standards for executive compensation and corporate governance for the period during which the Treasury holds equity issued under the TARP Capital Purchase Program, and they will be restricted from increasing dividends to common shareholders or repurchasing common stock for three years without the consent of the Treasury.

Further, after receiving a recommendation from the boards of the Federal Deposit Insurance Corporation ("the FDIC") and the Federal Reserve System (the Federal Reserve"), the Treasury signed the systemic risk exception to the FDIC Act, enabling the FDIC to temporarily provide a 100% guarantee of the senior debt of all FDIC-insured institutions and their holding companies, as well as deposits in non-interest bearing transaction deposit accounts under a Temporary Liquidity Guarantee Program. Coverage under the Temporary Liquidity Guarantee Program is available for 30 days without charge and thereafter at a cost of 75 basis points per annum for senior unsecured debt and 10 basis points per annum for non-interest bearing transaction deposits.

The Bank has not made a definitive decision as to whether it will participate in either the Temporary Liquidity Guarantee Program or the TARP Capital Purchase Program.

It is not clear at this time what impact the EESA, the TARP Capital Purchase Program, the Temporary Liquidity Guarantee Program, other liquidity and funding initiatives of the Federal Reserve and other agencies that have been previously announced, and any additional programs that may be initiated in the future will have on the Bank and the U. S. and global financial markets.

Forward-Looking Statements

Management's discussion of the Bank and management's analysis of the Bank's operations and prospects, and other matters, may include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 and other provisions of federal and state securities laws. Although the Bank believes that the assumptions underlying such forward-looking statements contained in this Report are reasonable, any of the assumptions could be inaccurate and, accordingly, there can be no assurance that the forward-looking statements included herein will prove to be accurate. The use of such words as expect, anticipate, forecast, project and comparable terms should be understood by the reader to indicate that the statement is "forward-looking" and thus subject to change in a manner that can be unpredictable. Factors that could cause actual results to differ from the results anticipated, but not guaranteed, in this Report, include (without limitation) economic and social conditions, relative declines in residential real estate construction in the United States, issues related to "subprime" mortgages, competition for loans, mortgages, and other financial services and products, changes in interest rates, unforeseen changes in liquidity, results of operations, and financial conditions affecting the Bank's customers, as well as other risks that cannot be accurately quantified or completely identified. Many factors affecting the Bank's financial condition and profitability, including changes in economic conditions, the volatility of interest rates, political events and competition from other providers of financial services simply cannot be predicted. Because these factors are unpredictable and beyond the Bank's control, earnings may fluctuate from period to period. The purpose of this type of information is to provide readers with information relevant to understanding and assessing the financial condition and results of operations of the Bank, and not to predict the future or to guarantee results. The Bank is unable to predict the types of circumstances, conditions, and factors that can cause anticipated results to change. The Bank undertakes no obligation to publish revised forward-looking statements to reflect the occurrence of changes or unanticipated events, circumstances, or results.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Results of Operations

The Bank had a loss of \$661,000 for the first nine months of 2008, compared to earnings of \$240,000 for the first nine months of 2007. On a per share basis, the loss was \$0.18 per common share of stock for the first nine months of 2008 compared to earnings of \$0.07 per basic common share of stock for the first nine months of 2007.

These figures include provisions for loan losses of \$994,000 and \$240,000 for the first nine months of 2008 and 2007, respectively. The increase in the provision for loan losses and an increase in salaries and employee benefits were the primary factors for the decrease in earnings from September 30, 2007 to September 30, 2008.

The provision for loan losses increased due to increased loan volumes in comparison with the previous year, coupled with recent economic trends that are affecting the construction lending and commercial lending segments of the Bank's loan portfolio. As 2008 began, the national economy, was either entering, or had already entered, a recession. Also, the Bank had already foreclosed on several properties that were collateral for construction loans, and there were other loans in the portfolio that Bank management had identified as impaired loans. The Bank has since properly charged off some loans in its portfolio that were deemed uncollectible. In addition, management has taken a very critical approach in analyzing the loan portfolio, and therefore, recommended large additional provisions to the Bank's loan loss reserve during the first nine months of 2008. Such increases can be expected to continue for at least the next 12 months taking into consideration recent economic declines.

The increase in salaries and employee benefits is attributable to several factors, such as hiring several individuals to appropriately fill key positions, including the addition of a full-time chief financial officer during the fourth quarter of 2007. Also, salaries and employee benefits were affected by incentive plans that are driven by volume and fee factors in areas like mortgage loans and brokerage services. As the Bank benefits from the income generated by these areas, incentive payments increase for the individuals helping to generate the related income.

Computation of Earnings (Loss) Per Share

The following is a summary of the components comprising basic and diluted earnings (loss) per common share of stock (EPS):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
	<i>(In Thousands, Except Per Share Amounts)</i>			
Basic EPS Computation:				
Numerator – Net (loss) earnings for the period	\$ (93)	\$ 169	\$ (661)	\$ 240
Denominator – Weighted average number of common shares outstanding	<u>3,746,441</u>	<u>3,739,459</u>	<u>3,743,655</u>	<u>3,690,372</u>
Basic (loss) earnings per common share	<u>\$ (0.02)</u>	<u>\$ 0.05</u>	<u>\$ (0.18)</u>	<u>\$ 0.07</u>
Diluted EPS Computation:				
Numerator – Net (loss) earnings for the period	\$ (93)	\$ 169	\$ (661)	\$ 240
Denominator:				
Weighted average number of common shares				
Outstanding	3,746,441	3,739,459	3,743,655	3,690,372
Effect of stock options	-	80,916	-	102,894
Effect of stock warrants	-	107,686	-	200,687
	<u>3,746,441</u>	<u>3,928,061</u>	<u>3,743,655</u>	<u>3,993,953</u>
Diluted earnings (loss) per common share	<u>\$ (0.02)</u>	<u>\$ 0.04</u>	<u>\$ (0.18)</u>	<u>\$ 0.06</u>

The effect of stock options and stock purchase warrants was excluded for the three and nine months ended September 30, 2008 since the Bank had a loss from continuing operations, and the exercise of options and warrants would have been anti-dilutive.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Net Interest Income

Net interest income represents the amount by which interest earned on various earning assets exceeds interest paid on deposits and other interest-bearing liabilities and is the most significant component of the Bank's earnings. Total interest income for the nine months ended September 30, 2008 was \$10,845,000 and total interest expense was \$4,520,000. Net interest income for the first nine months of 2008 totaled \$6,325,000. For the same period in 2007 total interest income was \$11,131,000 and total interest expense was \$5,405,000. This represents a 2.6% decrease in total interest income and a 16.4% decrease in interest expense from 2007 to 2008. Net interest income for the first nine months of 2007 was \$5,726,000. This represents an increase of 10.5% in net interest income from 2007 to 2008. The increase in net interest income for the quarter ended September 30, 2008 was \$185,000 or 8.9% as compared to the same period in 2007.

Over the past six months, management has seen an increase in the Bank's net interest margin. In effecting that change in our net interest margin, management has sought opportunities to lock in interest spreads on larger transactions by match funding loans and has maintained shorter maturities on time deposits to allow for the expected rate decreases. The Bank has not matched a number of the special certificate of deposit rates that have been offered in recent months by some of the regional banks in the Middle Tennessee market, because those rates appear to be above normal market prices. Instead, management has elected to leverage the Bank's balance sheet somewhat using short-term advances that were priced lower than the certificates of deposit that moved to other financial institutions. As a result, the Bank's cost of interest-bearing liabilities has decreased each of the last nine months, also enhancing the Bank's interest margin. Management believes that the Bank's net interest margin may level out or slightly decrease during the fourth quarter of 2008 since two of the Bank's primary indices, Federal Reserve Prime and LIBOR, have fallen.

Provision for Loan Losses

The provision for loan losses represents a charge to earnings necessary to establish an allowance for loan losses that, in management's evaluation, is adequate to provide coverage for estimated losses on outstanding loans and to provide for uncertainties in the economy. The provision for loan losses and the amount added to the allowance for loan losses was \$994,000 for the first nine months of 2008 and \$240,000 for the same period in 2007, and was \$365,000 and \$122,000 for the three months ended September 30, 2008 and 2007, respectively. The level of the allowance and the amount of the provision involve evaluation of uncertainties and matters of judgment. Management believes the allowance for loan losses at September 30, 2008 and December 31, 2007 to be adequate. The total allowance for loan losses was \$2,269,000 or 1.08% of loans, at September 30, 2008 and \$2,032,000, or 1.05% of loans, at December 31, 2007.

As noted under "Results of Operations," the provision for loan losses increased during the first nine months of 2008 due to increased loan volumes in comparison with the previous year, coupled with consideration of the impact on the loan portfolio of a general economic downturn in the construction and commercial lending segments. Significant additional allocations to the loan loss reserve are expected for at least the next 12 months.

Non-Interest Income

The Bank's non-interest income consists primarily of service charges on deposits, fees on mortgage originations, fees from brokerage operations and other fees and commissions. Total non-interest income for the nine months ended September 30, 2008 was \$1,393,000 and \$1,124,000 for the same period in 2007. Total non-interest income increased 23.9% from 2007 to 2008. The increase for the three months ended September 30, 2008 was \$46,000 or 11.0% as compared to the same period in 2007. Management projects that other fees and commissions and service charges on deposit accounts will increase throughout the remainder of 2008 due to growth of the Bank and will continue to enhance earnings, although net interest income will continue to provide the core earnings for the Bank. The increase in fees is primarily related to growth in volumes in investment brokerage activities and fees on deposit accounts.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Non-Interest Expense

Non-interest expenses consist primarily of employee costs, occupancy expenses, furniture and equipment expenses, data processing expenses and other operating expenses. Total non-interest expense for the nine months ended September 30, 2008 was \$7,385,000 and \$6,370,000 for the same period in 2007. The change in non-interest expense from 2007 to 2008 was an increase of 15.9%. The increase for the three months ended September 30, 2008 was \$250,000 or 11.3% as compared to the same period in 2007. The increase in non-interest expense is due to the growth of the Bank, including the addition of personnel, combined with an increase in professional fees.

The expense related to employee salaries and benefits increased by 14.0% from \$3,381,000 for the nine months ended September 30, 2007 to \$3,853,000 for the comparable period ended September 30, 2008. In addition to the key personnel that have been added in the past year, the Bank has also seen group insurance costs rise, and incentive expenses have increased due to increased fee volumes related to investment brokerage. Additionally, the Bank's professional fee expenses increased by 68.3%, from \$208,000 in the first nine months of 2007 to \$350,000 for the same period in 2008, due to the Bank's increased fees related to the Bank's audit and compliance initiatives and increased legal fees related to the Bank's enhanced collection efforts during 2008.

To offset the increase in non-interest expenses, management has renegotiated, or is in the process of renegotiating, more favorable financial terms on several key contracts, i.e., group insurance, data processing, item processing, supply procurement, etc. The benefits of the negotiations of these relationships will be realized beginning in the fourth quarter of 2008 and over the course of the next 12 to 15 months.

Income Taxes

The Bank had a loss during the first nine months of 2008, and therefore, no income tax expense has been recorded. The Bank will record no income tax expense for 2008 due to the Bank's cumulative losses from the previous years of operation.

Financial Condition

Balance Sheet Summary

The Bank's total assets were \$260,820,000 at September 30, 2008 and \$246,982,000 at December 31, 2007. Loans, net of allowance for loan losses, totaled \$207,479,000 at September 30, 2008 and \$191,074,000 at December 31, 2007. Securities available-for-sale totaled \$29,682,000 at September 30, 2008 and \$31,248,000 at December 31, 2007. Restricted equity securities totaled \$1,611,000 and \$1,439,000 at September 30, 2008 and December 31, 2007, respectively. The percentage changes for these assets are a 5.6% increase in total assets, an 8.6% increase in loans net of allowance for loan losses, a 5.0% decrease in securities available-for-sale and a 12.0% increase in restricted equity securities.

Total liabilities increased by 6.7% to \$230,523,000 at September 30, 2008 from \$216,004,000 at December 31, 2007. Stockholders' equity decreased 2.2% to \$30,297,000 at September 30, 2008 from \$30,978,000 at December 31, 2007. A more detailed discussion of assets, liabilities and capital follows.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations, Continued

Financial Condition, Continued

Loans

Loans categories are as follows:

	<u>September 30, 2008</u>		<u>December 31, 2007</u>	
	<u>Amount</u> <i>(In Thousands)</i>	<u>Percentage</u>	<u>Amount</u> <i>(In Thousands)</i>	<u>Percentage</u>
Commercial, financial and agricultural	\$ 102,240	48.8%	\$ 106,564	55.2%
Consumer	4,070	1.9	3,480	1.8
Real estate – mortgage	40,317	19.2	27,611	14.3
Real estate – construction	<u>63,121</u>	<u>30.1</u>	<u>55,451</u>	<u>28.7</u>
Total	<u>\$ 209,748</u>	<u>100.0%</u>	<u>\$ 193,106</u>	<u>100.0%</u>

Loans are a large component of the Bank’s assets and are a primary source of income. The loan portfolio is composed of four primary loan categories: commercial, financial and agricultural; consumer; real estate - mortgage; and real estate - construction. The table above sets forth the loan categories and the percentage of such loans in the portfolio at September 30, 2008 and December 31, 2007.

As represented in the table, primary loan growth was in real estate mortgage and real estate construction loans. At September 30, 2008, real estate loans are nearly 50% of total loans. Accordingly, the Bank has a significant concentration of credit that is dependent on the continuing progress of the local real estate market. Though this market has slowed considerably over the past 12 to 18 months, real estate sales continue at a reasonable pace and are definitely better than on a national level. Accordingly, management is making loans even more conservatively than in the past.

The Bank follows the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 114, “Accounting by Creditors for Impairment of a Loan” and SFAS No. 118, “Accounting by Creditors for Impairment of a Loan - Income Recognition and Disclosures”. These pronouncements apply to impaired loans except for large groups of smaller-balance homogeneous loans that are collectively evaluated for impairment including residential mortgage and consumer installment loans.

The federal regulatory agencies have also issued two “guidances” that could have a significant impact on real-estate related lending, and thus, on the operation of the Bank. One part of the guidance could require lenders to restrict lending secured primarily by certain categories of commercial real estate to a level of 300% of their capital or to raise additional capital. This could have the effect of causing the Bank to reorient its loan strategy away from, or to limit its expansion of, commercial real estate lending, which has been a material part of the Bank’s lending strategy. This could also have a negative impact on the Bank’s lending and profitability. The other guidance relates to the structuring of certain types of mortgages that allows negative amortization of consumer mortgage loans. Although the Bank does not engage at present in a significant amount of lending using these types of instruments, the guidance could have the effect of making the Bank less competitive in consumer mortgage lending.

A loan is impaired when it is probable that the Bank will be unable to collect the scheduled payments of principal and interest due under the contractual terms of the loan agreement. Impaired loans are measured at the present value of expected future cash flows discounted at the loan’s effective interest rate, at the loan’s observable market price, or the fair value of the collateral if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, the Bank recognizes an impairment by creating a valuation allowance with a corresponding charge to the provision for loan losses or by adjusting an existing valuation allowance for the impaired loan with a corresponding charge or credit to the provision for loan losses.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Financial Condition, Continued

Loans, Continued

The Bank's one-to-four family residential mortgage and consumer loans, which total approximately \$38,580,000 and \$4,070,000, respectively at September 30, 2008, are divided into various groups of smaller-balance homogeneous loans that are collectively evaluated for impairment and thus are not subject to the provisions of SFAS Nos. 114 and 118. Substantially all other loans of the Bank are evaluated for impairment under the provisions of SFAS Nos. 114 and 118.

The Bank considers all loans subject to the provisions of SFAS Nos. 114 and 118 that are on nonaccrual status to be impaired. Loans are placed on nonaccrual status when doubt as to timely collection of principal or interest exists, or when principal or interest is past due 90 days or more unless such loans are well-secured and in the process of collection. Delays or shortfalls in loan payments are evaluated with various other factors to determine if a loan is impaired. Generally, delinquencies under 90 days are considered insignificant unless certain other factors are present which indicate impairment is probable. The decision to place a loan on nonaccrual status is also based on an evaluation of the borrower's financial condition, collateral, liquidation value, and other factors that affect the borrower's ability to pay.

Generally, at the time a loan is placed on nonaccrual status, all interest accrued on the loan in the current fiscal year is reversed from income, and all interest accrued and uncollected from the prior year is charged off against the allowance for loan losses. Thereafter, interest on nonaccrual loans is recognized as interest income only to the extent that cash is received and future collection of principal is not in doubt. If the collectibility of outstanding principal is doubtful, such interest received is applied as a reduction of principal. A nonaccrual loan may be restored to accruing status when principal and interest are no longer past due and unpaid and future collection of principal and interest on a timely basis is not in doubt. At September 30, 2008 there were two non-accrual loans totaling \$235,000, and there were no non-accrual loans at December 31, 2007.

Other loans may be classified as impaired when the current net worth and financial capacity of the borrower or the collateral pledged, if any, is viewed as inadequate. In those cases, such loans have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt, and if such deficiencies are not corrected, there is a probability that the Bank will sustain some loss. In such cases, interest income continues to accrue as long as the loan does not meet the Bank's criteria for nonaccrual status.

Generally the Bank also classifies as impaired any loans the terms of which have been modified in a troubled debt restructuring. Interest is accrued on such loans that continue to meet the modified terms of their loan agreements. At September 30, 2008 and December 31, 2007, the Bank had no loans that have had the terms modified in a troubled debt restructuring.

The Bank's charge-off policy for impaired loans is similar to its charge-off policy for all loans in that loans are charged-off in the month when they are considered uncollectible.

Impaired loans and related allowance for loan loss allocation amounts at September 30, 2008 and December 31, 2007 were as follows:

	September 30, <u>2008</u>	December 31, <u>2007</u>
	<i>(In Thousands)</i>	
Recorded investment	\$ 6,174	4,970
Loan loss reserve	\$ 457	465

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Financial Condition, Continued

Loans, Continued

The average recorded investment in impaired loans for September 30, 2008 and December 31, 2007 was \$5,621,000 and \$2,670,000, respectively. The related total amount of interest income recognized on the accrual basis for the period that such loans were impaired was \$242,000 for the first nine months of 2008 and \$195,000 for year end 2007. The Bank's level of impaired loans increased over the past nine months as a result of a "softness" in the construction segment of the real estate market and due to a couple of commercial loan relationships. There has been an over supply of houses and residential lots, and the increase in impaired loans is a reflection of this. Bank management believes that existing loan loss reserves are adequate to absorb potential losses that may occur resulting from the "softness" of these portfolio components.

At September 30, 2008 and December 31, 2007, there were \$17,419,000 and \$16,088,000, respectively, in loans included in the Bank's internal classified loan list. Loans are listed as classified when information obtained about possible credit problems of the borrower has prompted management to question the ability of the borrower to comply with the agreed repayment terms of the loan agreement. The loan classifications do not represent or result from trends or uncertainties which management expects will materially impact future operating results, liquidity or capital resources.

The allowance for loan losses is discussed under "Provision for Loan Losses". The Bank maintains its allowance for loan losses at an amount considered by management to be adequate to provide for the possibility of loan losses in the loan portfolio.

Essentially all of the Bank's loans originate from Rutherford and adjacent counties in Tennessee. The Bank seeks to exercise prudent risk management in lending, including diversification by loan category and industry segment, as well as by identification of credit risks.

The Bank's management believes there is a significant opportunity to continue to increase the loan portfolio in the Bank's primary market area. The Bank has targeted commercial business lending, commercial and residential real estate lending and consumer lending. The Bank seeks to build a loan portfolio which is capable of adjusting to swings in the interest rate market, and it is the Bank's policy to maintain a diverse loan portfolio not dependent on any particular market or industrial segment. Management has set a goal for loans to approximate 100% of deposits.

Securities

Securities are a significant component of the Bank's earning assets. Securities available-for-sale totaled \$29,682,000 at September 30, 2008. This represents a 5.0% decrease from the December 31, 2007 total of \$31,248,000. Restricted equity securities totaled \$1,611,000 and \$1,439,000 at September 30, 2008 and December 31, 2007, respectively.

The Bank has adopted the provisions of SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Under the provisions of the Statement, securities are classified in three categories and accounted for as follows:

- Debt securities that the enterprise has the positive intent and ability to hold to maturity are classified as held-to-maturity securities and reported at amortized costs.
- Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Financial Condition, Continued

Securities, Continued

- Debt and equity securities not classified as either held-to-maturity securities or trading securities are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses excluded from earnings and reported in a separate component of stockholders' equity.

The Bank has classified all its securities as available-for-sale. The investment securities portfolio is the second largest component of the Bank's earning assets and represented 11.4% of total assets at September 30, 2008. The Bank uses the investment securities portfolio to meet pledging requirements for deposits of public funds, securities sold under agreement to repurchase and secured Fed Funds lines of credit. The average yield on the investment securities portfolio during the first nine months of 2008 was 4.42%.

Deposits

Deposits are the principal source of funds for the Bank. The Bank has targeted local consumers, professionals, governments and commercial businesses as its central customer base; therefore, deposit instruments in the form of demand deposits, savings accounts, money market deposit accounts, certificates of deposit and individual retirement accounts are offered to customers.

Total deposits were \$220,632,000 and \$207,448,000 at September 30, 2008 and December 31, 2007, respectively, an increase of 6.4%. The increase in deposits is primarily due to the Bank's participating in Promontory Interfinancial Network's program entitled Certificate of Deposit Account Registry Service[®], or "CDARS[®]," which began in the third quarter of 2008. This program allows the Bank to provide FDIC insurance for customers up to \$50 million on deposited funds that normally would only be eligible for coverage up to \$250,000 through December 31, 2009, and up to \$100,000 thereafter. As of September 30, 2008 the deposits in that program had grown to a total of \$23.4 million in certificates of deposit. Additional funds are expected to come into that program due to the general public's concern over recent bank failures.

Management believes Rutherford County and the surrounding area is a reasonably strong economic market offering growth opportunities for the Bank; however, the Bank competes with several of the larger bank holding companies that have bank offices in this area, as well as other community banks. No assurances of market growth can be given due to the competitive factors. Even though the Bank is in a very competitive market, management currently believes that its market share will be expanded. Management firmly believes that its position as a locally-owned financial institution that offers personalized service will contribute significantly to quality loans and deposit growth and profitability.

Non-interest bearing deposits increased 15.2% from \$25,987,000 on December 31, 2007 to \$29,949,000 on September 30, 2008. Total interest-bearing deposits increased by 5.1% from \$181,461,000 on December 31, 2007 to \$190,683,000 on September 30, 2008.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Financial Condition, Continued

Deposits, Continued

The table below sets forth the total balances of our deposits by type as of September 30, 2008 and December 31, 2007, and the percent change in balances over the intervening period:

	September 30, <u>2008</u>	December 31, <u>2007</u>	<u>% Change</u>
	<i>(In Thousands)</i>		
Non-interest bearing accounts	\$ 29,949	\$ 25,987	15.2%
NOW accounts	22,443	30,599	(26.7)
Money market accounts	45,127	36,095	25.0
Savings accounts	1,637	1,162	40.9
Certificates of deposit	116,542	108,283	7.6
Individual retirement accounts	<u>4,934</u>	<u>5,322</u>	<u>(7.3)</u>
Total deposits	<u>\$ 220,632</u>	<u>\$ 207,448</u>	<u>6.4%</u>

Liquidity and Asset Management

The Bank's management seeks to maximize net interest income by managing the Bank's assets and liabilities within appropriate constraints on capital, liquidity and interest rate risk. Liquidity is the ability to maintain sufficient cash levels necessary to fund operations, meet the requirements of depositors and borrowers and fund attractive investment opportunities. The Bank's primary source of liquidity is expected to be a stable core deposit base. In addition, short-term investments, loan payments and investment security maturities provide a secondary source. Higher levels of liquidity bear corresponding costs, measured in terms of lower yields on short-term more liquid earning assets and higher interest expense involved in extending liability maturities.

The Bank maintains a formal asset and liability management process to quantify, monitor and control interest rate risk and to assist management in maintaining stability in the net interest margin under varying interest rate environments. The Bank accomplishes this process through the development and implementation of lending, funding and pricing strategies designed to maximize net interest income under varying interest rate environments subject to specific liquidity and interest rate risk guidelines.

Analysis of rate sensitivity and rate gap analysis are the primary tools used to assess the direction and magnitude of changes in net interest income resulting from changes in interest rates. Included in the analysis are cash flows and maturities of financial instruments held for purposes other than trading, changes in market conditions, loan volumes and pricing and deposit volume and mix. These assumptions are inherently uncertain, and, as a result, net interest income cannot be precisely estimated nor can the impact of higher or lower interest rates on net interest income be precisely predicted. Actual results will differ due to timing, magnitude and frequency of interest rate changes and changes in market conditions and management's strategies, among other factors.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Liquidity and Asset Management, Continued

The Bank's securities portfolio consists of earning assets that provide interest income. Securities classified as available-for-sale include securities intended to be used as part of the Bank's asset/liability strategy and/or securities that may be sold in response to changes in interest rate, prepayment risk, the need or desire to increase capital and similar economic factors. Securities totaling \$1.2 million mature or will be subject to rate adjustments within the next 12 months.

A secondary source of liquidity is the Bank's loan portfolio. At September 30, 2008, loans of approximately \$114.4 million either will become due or will be subject to rate adjustments within 12 months from the respective date.

As for liabilities, certificates of deposit of \$100,000 or greater of approximately \$40 million will become due during the next 12 months. Management does not anticipate any significant reductions from withdrawable accounts such as negotiable order of withdrawal accounts, money market demand accounts, demand deposits and regular savings accounts in the future.

In previous filings, management had stated that the Bank anticipates that it will renovate and expand its main office facilities beginning sometime during 2008. Considering the Bank's current lack of earnings and the economic conditions in which the Bank is currently operating, management believes that it is prudent to delay construction until the Bank has sustained positive earnings for a reasonable period of time.

Capital Position and Dividends

At September 30, 2008 and December 31, 2007, total stockholders' equity was \$30,297,000 and \$30,978,000 or 11.6% and 12.5%, respectively, of total assets.

The Bank's principal regulators have established minimum risk-based capital requirements and leverage capital requirements for the Bank. These guidelines classify capital into two categories of Tier 1 and Total risk-based capital. Total risk-based capital consists of Tier 1 (or core) capital (essentially common equity less intangible assets) and Tier 2 capital (essentially qualifying long-term debt, of which the Bank has none, and a part of the allowance for possible loan losses). In determining risk-based capital requirements, assets are assigned risk-weights of 0% to 100%, depending on regulatory assigned levels of credit risk associated with such assets.

There are statutory, regulatory and prudential limitations on the payment of dividends by the Bank. Tennessee law restricts the amount of dividends that may be paid by the Bank. In no event is a Tennessee-chartered bank permitted to pay dividends, in any calendar year, that exceed the total of its net income of that year combined with its retained net income of the preceding two years without the prior approval of the Commissioner of the Tennessee Department of Financial Institutions. Prior regulatory approval must be obtained before declaring any dividends if the amount of the Bank's capital and surplus is below certain statutory limits. Dividends can also be restricted under federal law, and under state safety and soundness considerations, as a result of a declining or inadequate capital level. Future dividends may be paid at the discretion of the board of directors consistent with the regulatory, legal and prudential considerations discussed elsewhere in this document.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

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

Capital Position and Dividends, Continued

The table below sets forth the Bank's capital ratios as of the periods indicated.

	<u>September 30,</u> <u>2008</u>	<u>December 31,</u> <u>2007</u>
Tier 1 Risk-Based Capital	12.20%	13.40%
Regulatory Minimum	4.00%	4.00%
Well-capitalized Minimum	6.00%	6.00%
Total Risk-Based Capital	13.13%	14.30%
Regulatory Minimum	8.00%	8.00%
Well-capitalized Minimum	10.00%	10.00%
Tier 1 Leverage	11.68%	12.96%
Regulatory Minimum	4.00%	4.00%
Well-capitalized Minimum	5.00%	5.00%

The ratios are high when compared to industry averages and result from the fact that the Bank raised a very large amount of capital at its inception. In addition, the Bank received approximately \$62,000 additional capital in the first nine months of 2008 related to the exercise of warrants and options, and additional capital is expected to be raised from the exercise of the existing warrants until they expire in January 2009. The currently planned emphasis is on asset quality and growth in core deposits, both of which are expected to be aided by the large stockholder base.

Off Balance Sheet Arrangements

At September 30, 2008, the Bank had unfunded loan commitments outstanding of approximately \$65.8 million and outstanding standby letters of credit of approximately \$2.1 million. Because these commitments generally have fixed expiration dates and many will expire without being drawn upon, the total commitment level does not necessarily represent future cash requirements. If needed to fund these outstanding commitments, the Bank has the ability to liquidate Federal funds sold or securities available-for-sale or on a short-term basis to borrow and purchase Federal funds from other financial institutions. Additionally, the Bank could sell participations in these or other loans to correspondent banks. As mentioned above, the Bank has been able to fund its ongoing liquidity needs through its stable core deposit base, loan payments, its investment security maturities and short-term borrowings.

Impact of Inflation

Although interest rates are significantly affected by inflation, the inflation rate is immaterial when reviewing the Bank's results of operations.

MIDSOUTH BANK

FORM 10-Q, CONTINUED

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Pursuant to Item 305(e) of Regulation S-K, the Registrant is not required to provide this information.

Item 4T. Controls and Procedures

Within the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and the Chief Financial Officer, of the design and operation of our disclosure controls and procedures. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective for gathering, analyzing and disclosing the information that we are required to disclose in the reports we file under the Securities Exchange Act of 1934, as amended ("Exchange Act") within the time periods specified in the Federal Reserve's rules and forms. Our Chief Executive Officer and Chief Financial Officer also concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to our Bank required to be included in our periodic Federal Reserve filings. We are continually reviewing and documenting our disclosure controls and procedures, including our internal controls and procedures for financial reporting, and may from time to time make changes designed to enhance their effectiveness and to ensure that our systems evolve with our business.

The Bank's common stock is registered under Section 12(g) of the Exchange Act, and is therefore subject to the requirements of Section 404, and other provisions, of the Sarbanes-Oxley Act of 2002 ("SOX"). Under SOX, the Public Company Accounting Oversight Board has imposed significant internal procedures, internal controls, and other requirements on public companies such as the Bank, and compliance with these requirements may prove expensive to the Bank.

Please refer also to Item 2 of Part I of this Report for additional information concerning controls and procedures.

Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) during the quarter ended September 30, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

MIDSOUTH BANK

PART II. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

None.

Item 1A. RISK FACTORS

Not applicable.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

- (a) Shares of the Bank's common stock were issued during the third quarter of 2008 pursuant to the exercise of stock options and stock purchase warrants issued by the Bank in its initial offering of securities during its formation as a commercial bank, as follows:

<u>Date of Sale</u>	<u>Number of Shares of Common Stock Sold</u>	<u>Price Per Share</u>
7/23/08	3,500	\$ 10.00
7/29/08	450	\$ 10.00
8/28/08	255	\$ 10.00
9/11/08	250	\$ 10.00
9/12/08	120	\$ 10.00

The shares were sold for cash in the amount of \$45,750.

There were no underwriters and no underwriting discounts or commissions. All sales were for cash.

The Bank's common stock is exempt from registration under applicable Tennessee and federal securities laws.

The shares of common stock issued pursuant to the exercise of the Bank's stock purchase warrants are not convertible or exchangeable into other equity securities.

The proceeds of the sales are being used by the Bank for general corporate purposes.

- (b) Not Applicable.
- (c) Not Applicable.
- (d) No repurchases for our securities were made during the quarter ended September 30, 2008. The only restrictions on working capital and/or dividends are those reported in Part I of this Report on Form 10-Q, as well as those discussed with respect to dividends in the Bank's Annual Report on Form 10-KSB, particularly in the section "Supervision and Regulation" and in the discussion of the Bank's common stock.

MIDSOUTH BANK

PART II. OTHER INFORMATION, CONTINUED

Item 3. DEFAULTS UPON SENIOR SECURITIES

- (a) None.
- (b) Not Applicable.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

Item 5. OTHER INFORMATION

None.

Item 6. EXHIBITS

- (a)(1) Exhibit 31.1 and 31.2 consist of Rule 13a-14(a)/15d-14(a) certifications.
 - (2) Exhibit 32 consists of Section 1350 certifications. As set forth in Item 601 of Regulation S-K, any certification furnished pursuant to this Item will not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934 (15 U.S.C. 78r), or otherwise subject to the liability of that section. Further, any certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that the registrant specifically incorporates it by reference.
- (b) None.

MIDSOUTH BANK

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.

MIDSOUTH BANK

(Registrant)

DATE: November 12, 2008 /s/ Lee M. Moss
Lee M. Moss
Chairman and Chief Executive Officer

DATE: November 12, 2008 /s/ Kevin D. Busbey
Kevin D. Busbey
Senior Vice President and Chief Financial Officer

CERTIFICATIONS

I, Lee M. Moss, certify that:

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

November 12, 2008

/s/ Lee M. Moss

Lee M. Moss

Chairman and Chief Executive Officer

CERTIFICATIONS

I, Kevin D. Busbey, certify that:

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

November 12, 2008

/s/ Kevin D. Busbey
Kevin D. Busbey
Senior Vice President and Chief Financial Officer

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

In connection with the Quarterly Report of MidSouth Bank (the “Bank”) on Form 10-Q for the period ending September 30, 2008 as filed with the Federal Reserve on the date hereof (the “Report”), the undersigned, Lee M. Moss and Kevin D. Busbey, to the best of our knowledge certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Bank.

/s/ Lee M. Moss
Lee M. Moss
Chairman and Chief Executive Officer
November 12, 2008

/s/ Kevin D. Busbey
Kevin D. Busbey
Senior Vice President and Chief Financial Officer
November 12, 2008

* As set forth in Item 601 of Regulation S-K, any certification furnished pursuant to this Item will not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934 (15 U.S.C. 78r), or otherwise subject to the liability of that section. Further, any certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that the registrant specifically incorporates it by reference.