FIFTH THIRD BANCORP
Form 10-Q
August 03, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended June 30, 2006

Commission File Number 0-8076

FIFTH THIRD BANCORP

(Exact name of Registrant as specified in its charter)

Ohio	**31-0854434**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

Fifth Third Center

Cincinnati, Ohio 45263

(Address of principal executive offices)

Registrant s telephone number, including area code: (513) 534-5300

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the Registrant is 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 x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

There were 557,894,188 shares of the Registrant s Common Stock, without par value, outstanding as of June 30, 2006.

FIFTH THIRD BANCORP

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This report may contain forward-looking statements about the Registrant and/or the company as combined with acquired entities within the meaning of Sections 27A of the Securities Act of 1933, as amended, and Rule 175 promulgated thereunder, and 21E of the Securities Exchange Act of 1934, as amended, and Rule 3b-6 promulgated thereunder, that involve inherent risks and uncertainties. This report may contain certain forward-looking statements with respect to the financial condition, results of operations, plans, objectives, future performance and business of the Registrant and/or the combined company including statements preceded by, followed by or that include the words or phrases such as believes, expects, anticipates, plans, trend, objective, continue, remain or similar expressions or future or conditional verbs such as should, could, might, can, may or similar expressions. There are a number of important factors that could cause future results to differ mater from historical performance and these forward-looking statements. Factors that might cause such a difference include, but are not limited to: (1) competitive pressures among depository institutions increase significantly; (2) changes in the interest rate environment reduce interest margins; (3) prepayment speeds, loan origination and sale volumes, charge-offs and loan loss provisions; (4) general economic conditions, either national or in the states in which the Registrant, one or more acquired entities and/or the combined company do business, are less favorable than expected; (5) political developments, wars or other hostilities may disrupt or increase volatility in securities markets or other economic conditions; (6) changes and trends in the securities markets; (7) legislative or regulatory changes or actions, or significant litigation, adversely affect the Registrant, one or more acquired entities and/or the combined company or the businesses in which the Registrant, one or more acquired entities and/or the combined company are engaged; (8) difficulties in combining the operations of acquired entities and (9) the impact of reputational risk created by the developments discussed above on such matters as business generation and retention, funding and liquidity. Additional information concerning factors that could cause actual results to differ materially from those expressed or implied in the forward-looking statements is available in the Registrant s Annual Report on Form 10-K for the year ended December 31, 2005, filed with the United States Securities and Exchange Commission (SEC). Copies of this filing are available at no cost on the SEC s Web site at www.sec.gov or on the Registrant s Web site at www.53.com. The Registrant undertakes no obligation to release revisions to these forward-looking statements or reflect events or circumstances after the date of this report.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (Item 2)

The following is management s discussion and analysis of certain significant factors that have affected Fifth Third Bancorp s (the Registrant or Fifth Third) financial condition and results of operations during the periods included in the Condensed Consolidated Financial Statements, which are a part of this filing. Reference to the Registrant incorporates the parent holding company and all consolidated subsidiaries.

TABLE 1: Selected Financial Data

($ in millions, except per share data)	For the three months ended June 30, 2006	2005	Percent Change	For the six months ended June 30, 2006	2005	Percent Change
Income Statement Data						
Net interest income *(a)*	$ **716**	758	(5)%	$ **1,434**	1,517	(5)%
Noninterest income	**655**	635	3	**1,272**	1,242	2
Total revenue *(a)*	**1,371**	1,393	(2)	**2,706**	2,759	(2)
Provision for loan and lease losses	**71**	60	18	**149**	127	17
Noninterest expense	**759**	728	4	**1,490**	1,432	4
Net income	**382**	417	(8)	**746**	822	(9)
Common Share Data						
Earnings per share, basic	$ **.69**	.75	(8)%	$ **1.34**	1.48	(9)%
Earnings per share, diluted	**.69**	.75	(8)	**1.34**	1.47	(9)
Cash dividends per common share	**.40**	.35	14	**.78**	.70	11
Book value per share	**17.13**	16.82	2			
Dividend payout ratio	**58.0%**	46.7	24	**58.2%**	47.6	22
Financial Ratios						
Return on average assets	**1.45%**	1.63	(11)%	**1.43%**	1.63	(12)%
Return on average equity	**16.0**	18.1	(12)	**15.7**	18.1	(13)
Average equity as a percent of average assets	**9.09**	8.98	1	**9.13**	9.00	4
Tangible equity	**6.92**	6.89				
Net interest margin *(a)*	**3.01**	3.29	(9)	**3.04**	3.33	(9)
Efficiency *(a)*	**55.3**	52.2	6	**55.0**	51.9	6
Credit Quality						
Net losses charged off	$ **67**	55	22%	$ **140**	118	18%
Net losses charged off as a percent of average loans and leases	**.37%**	.34	9	**.40%**	.37	8
Allowance for loan and lease losses as a percent of loans and leases	**1.04**	1.09	(5)			
Allowance for credit losses as a percent of loans and leases *(b)*	**1.14**	1.20	(5)			
Nonperforming assets as a percent of loans, leases and other assets, including other real estate owned	**.49**	.51	(4)			
Average Balances						
Loans and leases, including held for sale	$ **73,093**	66,762	9%	$ **72,367**	$ 65,924	10%
Total securities and other short-term investments	**22,439**	25,716	(13)	**22,677**	25,916	(12)
Total assets	**105,741**	102,765	3	**105,241**	101,891	3
Transaction deposits	**49,282**	47,624	3	**49,116**	47,603	3
Core deposits	**59,731**	55,910	7	**59,217**	55,641	6
Wholesale funding	**32,903**	34,274	(4)	**33,013**	33,820	(2)
Shareholders equity	**9,607**	9,224	4	**9,604**	9,166	5

Regulatory Capital Ratios			
Tier I capital	**8.52%**	8.48	%
Total risk-based capital	**10.45**	10.80	(3)
Tier I leverage	**8.38**	7.76	8

(a) Amounts presented on a fully taxable equivalent basis.

(b) The allowance for credit losses is the sum of the allowance for loan and lease losses and the reserve for unfunded commitments.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

OVERVIEW

This overview of management s discussion and analysis highlights selected information in the financial results of the Registrant and may not contain all of the information that is important to you. For a more complete understanding of trends, events, commitments, uncertainties, liquidity, capital resources and critical accounting policies and estimates, you should carefully read this entire document. Each of these items could have an impact on the Registrant s financial condition and results of operations.

The Registrant is a diversified financial services company headquartered in Cincinnati, Ohio. At June 30, 2006, the Registrant had $106.1 billion in assets, operated 19 affiliates with 1,138 full-service Banking Centers including 116 Bank Mart® locations open seven days a week inside select grocery stores and 2,034 Jeanie® ATMs in Ohio, Kentucky, Indiana, Michigan, Illinois, Florida, Tennessee, West Virginia, Pennsylvania and Missouri. The Registrant reports on five business segments: Commercial Banking, Branch Banking, Consumer Lending, Investment Advisors and Fifth Third Processing Solutions (FTPS). During the first quarter of 2006, the Registrant began separating its Retail line of business into the Branch Banking and Consumer Lending business segments. All prior year information has been updated to reflect this presentation.

The Registrant believes that banking is first and foremost a relationship business where the strength of the competition and challenges for growth can vary in every market. Its affiliate operating model provides a competitive advantage by keeping the decisions close to the customer and by emphasizing individual relationships. Through its affiliate operating model, individual managers, from the banking center to the executive level, are given the opportunity to tailor financial solutions for their customers.

The Registrant s revenues are fairly evenly dependent on net interest income and noninterest income. For the three months ended June 30, 2006, net interest income, on a fully taxable equivalent (FTE) basis, and noninterest income provided 52% and 48% of total revenue, respectively. Therefore, changes in interest rates, credit quality, economic trends and the capital markets are primary factors that drive the performance of the Registrant. As discussed later in the Risk Management section, risk identification, measurement, monitoring, control and reporting are important to the management of risk and to the financial performance and capital strength of the Registrant.

The Registrant continues to focus on funding growth in loans and leases with growth in core deposits, which includes demand deposits, interest checking, savings, money market and other time deposits. When core deposit growth does not meet the growth in loans and leases, the Registrant has utilized cash flows from the securities portfolio as well as wholesale funding, which includes certificates $100,000 and over, foreign office deposits, federal funds purchased, short-term bank notes, other short-term borrowings and long-term debt.

Net interest income, which continues to be the Registrant s largest revenue source, is the difference between interest income earned on assets, such as loans, leases and securities, and interest expense paid on liabilities, such as deposits and borrowings. Net interest income is affected by the general level of interest rates, the relative level of short- and long-term interest rates, changes in interest rates and changes in the amount and composition of interest-earning assets and interest-bearing liabilities. Generally, the rates of interest the Registrant earns on its assets and owes on its liabilities are established for a period of time. The change in market interest rates over time exposes the Registrant to interest rate risk through potential adverse changes to net interest income and financial position. The Registrant manages this risk by continually analyzing and adjusting the composition of its assets and liabilities based on their payment streams and interest rates, the timing of their maturities and their sensitivity to changes in market interest rates. Additionally, in the ordinary course of business, the Registrant enters into certain derivative transactions as part of its overall strategy to manage its interest rate and prepayment risks.

The Registrant is also exposed to the risk of losses on its loan and lease portfolio as a result of changing expected cash flows caused by loan defaults and inadequate collateral, among other factors.

Noninterest income is derived primarily from electronic funds transfer (EFT) and merchant transaction processing fees, card interchange, fiduciary and investment management fees, banking fees and service charges and mortgage banking revenue.

Net interest income, net interest margin, net interest rate spread and the efficiency ratio are presented in Management s Discussion and Analysis of Financial Condition and Results of Operations on an FTE basis. The FTE basis adjusts for the tax-favored status of income from certain loans and securities held by the Registrant that are not taxable for federal income tax purposes. The Registrant believes this presentation to be the preferred industry measurement of net interest income as it provides a relevant comparison between taxable and non-taxable amounts.

The Registrant s net income was $382 million in the second quarter of 2006, an eight percent decrease compared to $417 million for the same period last year. Earnings per diluted share were $.69 for the second quarter, an eight percent decrease from $.75 for the same period last year. The Registrant s quarterly dividend increased to $.40 per common share from $.35 in the second quarter of 2005, an increase of 14%.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Net interest income (FTE) decreased five percent compared to the same period last year. Net interest margin decreased to 3.01% in the second quarter of 2006 from 3.29% in the same period last year and from 3.08% in the first quarter of 2006 largely due to the rise in short-term interest rates and the corresponding impact on the cost of certain wholesale funding categories, the impact of the primarily fixed-rate securities portfolio and mix shifts within the core deposit base. Noninterest income increased three percent over the same period last year with strong growth in electronic payment processing revenue and corporate banking revenue offset by an $8 million decline in operating lease revenue as a result of the year-over-year runoff from the consumer automobile lease portfolio and a $5 million, or 10%, decline in mortgage banking revenue due to lower gains on loan sales. Despite a 25% increase in volume-related bankcard expenditures and a nine percent increase in occupancy expense related to the addition of de-novo banking centers, noninterest expense increased only four percent over the same quarter last year as the Registrant continues to realize cost savings from expense control initiatives.

Credit quality metrics remained stable during the second quarter of 2006. Net charge-offs as a percent of average loans and leases were .37% in the second quarter of 2006 compared to .42% in the first quarter of 2006 and .34% in the second quarter of 2005. At June 30, 2006, nonperforming assets as a percent of loans and leases were down to .49% from .51% at March 31, 2006 and June 30, 2005.

The Registrant s capital ratios exceed the well-capitalized guidelines as defined by the Board of Governors of the Federal Reserve System (FRB). As of June 30, 2006, the Tier I capital ratio was 8.52% and the total risk-based capital ratio was 10.45%.

The Registrant continues to invest in the geographic areas that offer the best growth prospects, as it believes this investment is the most cost efficient method of expansion within its largest affiliate markets. During the first six months of 2006, the Registrant opened 25 new banking centers that did not involve the relocation or consolidation of existing facilities, with plans to add a total of 50 net banking centers (excluding relocations and consolidations) in key markets for the full-year 2006.

RECENT ACCOUNTING STANDARDS

Note 2 of the Notes to Condensed Consolidated Financial Statements provides a complete discussion of the new accounting standards adopted by the Registrant during 2006 and 2005 and the expected impact of accounting standards issued but not yet required to be adopted.

CRITICAL ACCOUNTING POLICIES

Allowance for Loan and Lease Losses

The Registrant maintains an allowance to absorb probable loan and lease losses inherent in the portfolio. The allowance is maintained at a level the Registrant considers to be adequate and is based on ongoing quarterly assessments and evaluations of the collectibility and historical loss experience of loans and leases. Credit losses are charged and recoveries are credited to the allowance. Provisions for loan and lease losses are based on the Registrant s review of the historical credit loss experience and such factors that, in management s judgment, deserve consideration under existing economic conditions in estimating probable credit losses. In determining the appropriate level of the allowance, the Registrant estimates losses using a range derived from base and conservative estimates. The Registrant s strategy for credit risk management includes a combination of conservative exposure limits significantly below legal lending limits and conservative underwriting, documentation and collections standards. The strategy also emphasizes diversification on a geographic, industry and customer level, regular credit examinations and quarterly management reviews of large credit exposures and loans experiencing deterioration of credit quality.

Larger commercial loans that exhibit probable or observed credit weakness are subject to individual review. Where appropriate, allowances are allocated to individual loans based on management s estimate of the borrower s ability to repay the loan given the availability of collateral, other sources of cash flow and legal options available to the Registrant. The review of individual loans includes those loans that are impaired as provided in SFAS No. 114, Accounting by Creditors for Impairment of a Loan. Any allowances for impaired loans are measured based on the present value of expected future cash flows discounted at the loan s effective interest rate or the fair value of the underlying collateral. The Registrant evaluates the collectibility of both principal and interest when assessing the need for loss accrual. Historical loss rates are applied to other commercial loans not subject to specific allowance allocations. The loss rates are derived from a migration analysis, which tracks the net charge-off experience sustained on loans according to their internal risk grade. The risk grading system currently utilized for allowance analysis purposes encompasses 10 categories. The Registrant also maintains a dual risk rating system that provides for 13 probability of default grade categories and an additional six grade categories for estimating actual losses given an event of default. The probability of default and estimated loss given default evaluations are not separated in the 10-grade risk rating system. The Registrant is in the process of completing significant validation and testing of the dual risk rating system prior to implementation for allowance analysis purposes. The dual risk rating system is expected to be consistent with Basel II requirements and will allow for more precision in the analysis of commercial credit risk.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Homogenous loans and leases, such as consumer installment, residential mortgage and automobile leases are not individually risk graded. Rather, standard credit scoring systems and delinquency monitoring are used to assess credit risks. Allowances are established for each pool of loans based on the expected net charge-offs for one year. Loss rates are based on the average net charge-off history by loan category.

Historical loss rates for commercial and consumer loans may be adjusted for significant factors that, in management s judgment, reflect the impact of any current conditions on loss recognition. Factors that management considers in the analysis include the effects of the national and local economies, trends in the nature and volume of loans (delinquencies, charge-offs and nonaccrual loans), changes in mix, credit score migration comparisons, asset quality trends, risk management and loan administration, changes in the internal lending policies and credit standards, collection practices and examination results from bank regulatory agencies and the Registrant s internal credit examiners.

Regardless of the extent of the evaluation of the previously discussed factors, certain inherent but undetected losses are probable within the loan and lease portfolios. An unallocated component to the allowance is maintained to recognize the imprecision in estimating and measuring loss when evaluating allowances for individual loans or pools of loans. Allowances on individual loans and historical loss rates are reviewed quarterly and adjusted as necessary based on changing borrower and/or collateral conditions and actual collection and charge-off experience.

Loans acquired by the Registrant through a purchase business combination are evaluated for possible credit impairment. Reduction to the carrying value of the acquired loans as a result of credit impairment is recorded as an adjustment to goodwill. The Registrant does not carry over the acquired company s allowance for loan and lease losses nor does the Registrant add to its existing allowance for the acquired loans as part of purchase accounting.

The Registrant s determination of the allowance for commercial loans is sensitive to the risk grade it assigns to these loans. In the event that 10% of commercial loans in each risk category would experience a downgrade of one risk category, the allowance for commercial loans would increase by approximately $71 million at June 30, 2006. The Registrant s determination of the allowance for residential and retail loans is sensitive to changes in estimated loss rates. In the event that estimated loss rates would increase by 10%, the allowance for residential and retail loans would increase by approximately $23 million at June 30, 2006. As several quantitative and qualitative factors are considered in determining the allowance for loan and lease losses, these sensitivity analyses do not necessarily reflect the nature and extent of future changes in the allowance for loan and lease losses. They are intended to provide insights into the impact of adverse changes in risk grades and inherent losses and do not imply any expectation of future deterioration in the risk rating or loss rates. Given current processes employed by the Registrant, management believes the risk grades and inherent loss rates currently assigned are appropriate.

The Registrant s primary market areas for lending are Ohio, Kentucky, Indiana, Michigan, Illinois, Florida, Tennessee, West Virginia, Pennsylvania and Missouri. When evaluating the adequacy of allowances, consideration is given to this regional geographic concentration and the closely associated effect changing economic conditions have on the Registrant s customers.

In the current year, the Registrant has not substantively changed any material aspect of its overall approach to determine its allowance for loan and lease losses. There have been no material changes in assumptions or estimation techniques as compared to prior periods that impacted the determination of the current period allowance for loan and lease losses. Based on the procedures discussed above, the Registrant is of the opinion that the allowance of $753 million was adequate, but not excessive, to absorb estimated credit losses associated with the loan and lease portfolio at June 30, 2006.

Reserve for Unfunded Commitments

The reserve for unfunded commitments is maintained at a level believed by management to be sufficient to absorb estimated probable losses related to unfunded credit facilities. The determination of the adequacy of the reserve is based upon an evaluation of the unfunded credit facilities, including an assessment of historical commitment utilization experience, credit risk grading and credit grade migration. Net adjustments to the reserve for unfunded commitments are included in other noninterest expense.

Taxes

The Registrant estimates income tax expense based on amounts expected to be owed to the various tax jurisdictions in which the Registrant conducts business. On a quarterly basis, management assesses the reasonableness of its effective tax rate based upon its current estimate of the amount and components of net income, tax credits and the applicable statutory tax rates expected for the full year. The estimated income tax expense is recorded in the Condensed Consolidated Statements of Income.

Deferred income tax assets and liabilities are determined using the balance sheet method and are reported in accrued taxes, interest and expenses in the Condensed Consolidated Balance Sheets. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax basis of assets and liabilities and recognizes enacted changes in tax rates and laws. Deferred tax assets are recognized subject to management judgment that realization is more likely than not.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Accrued taxes represent the net estimated amount due or to be received from taxing jurisdictions and are reported in accrued taxes, interest and expenses in the Condensed Consolidated Balance Sheets. The Registrant evaluates and assesses the relative risks and appropriate tax treatment of transactions and filing positions after considering statutes, regulations, judicial precedent and other information and maintains tax accruals consistent with its evaluation of these relative risks and merits. Changes to the estimate of accrued taxes occur periodically due to changes in tax rates, interpretations of tax laws, the status of examinations being conducted by taxing authorities and changes to statutory, judicial and regulatory guidance that impact the relative risks of tax positions. These changes, when they occur, can affect deferred taxes and accrued taxes as well as the current period s income tax expense and can be significant to the operating results of the Registrant. See Note 2 of the Notes to the Condensed Consolidated Financial Statements for discussion of the recently issued accounting statement, which clarifies the accounting for uncertainty in income taxes. As described in greater detail in Note 9 of the Notes to the Condensed Consolidated Financial Statements, the Internal Revenue Service is currently challenging the Registrant s tax treatment of certain leasing transactions.

Valuation of Servicing Rights

When the Registrant sells loans through either securitizations or individual loan sales in accordance with its investment policies, it often retains servicing rights. Servicing rights resulting from loan sales are amortized in proportion to and over the period of estimated net servicing revenues. Servicing rights are assessed for impairment monthly, based on fair value, with temporary impairment recognized through a valuation allowance and permanent impairment recognized through a write-off of the servicing asset and related valuation allowance. Key economic assumptions used in measuring any potential impairment of the servicing rights include the prepayment speeds of the underlying loans, the weighted-average life, the discount rate, the weighted-average coupon and the weighted-average default rate, as applicable. The primary risk of material changes to the value of the servicing rights resides in the potential volatility in the economic assumptions used, particularly the prepayment speeds.

The Registrant monitors risk and adjusts its valuation allowance as necessary to adequately reserve for any probable impairment in the portfolio. For purposes of measuring impairment, the servicing rights are stratified based on the financial asset type and interest rates. In addition, the Registrant obtains an independent third-party valuation of mortgage servicing rights (MSR) on a quarterly basis. Fees received for servicing loans owned by investors are based on a percentage of the outstanding monthly principal balance of such loans and are included in noninterest income as loan payments are received. Costs of servicing loans are charged to expense as incurred.

The change in the fair value of MSRs at June 30, 2006, due to immediate 10% and 20% adverse changes in the current prepayment assumption would be approximately $22 million and $42 million, respectively, and due to immediate 10% and 20% favorable changes in the current prepayment assumption would be approximately $24 million and $49 million, respectively. The change in the fair value of the MSR portfolio at June 30, 2006, due to immediate 10% and 20% adverse changes in the discount rate assumption would be approximately $20 million and $39 million, respectively, and due to immediate 10% and 20% favorable changes in the discount rate assumption would be approximately $22 million and $45 million, respectively. Sensitivity analysis related to other consumer and commercial servicing rights is not material to the Registrant s Condensed Consolidated Financial Statements. These sensitivities are hypothetical and should be used with caution. As the figures indicate, change in fair value based on a 10% and 20% variation in assumptions typically cannot be extrapolated because the relationship of the change in assumptions to change in fair value may not be linear. Also, the effect of variation in a particular assumption on the fair value of the retained interests is calculated without changing any other assumption; in reality, changes in one factor may result in changes in another, which might magnify or counteract the sensitivities. Additionally, the effect of the Registrant s non-qualifying hedging strategy, which is maintained to lessen the impact of changes in value of the MSR portfolio, is excluded from the above analysis.

STATEMENTS OF INCOME ANALYSIS

Net Interest Income

The Registrant continues to face a challenging net interest income environment as a result of rising short-term interest rates. Net interest income (FTE) was $716 million for the second quarter of 2006, a decline of $2 million compared to the sequential quarter and a decline of $42 million compared to the prior year quarter. In terms of mix between volume and yield, the impact of changes in interest rates on net interest income (FTE) was a year-over-year decrease of 11%. The decline also resulted in continued compression of net interest margin to 3.01% from 3.08% in the first quarter and 3.29% in the second quarter of 2005. The Registrant currently expects modest margin compression in the third quarter with future trends dependent on the timing of further short-term interest rate increases and the overall direction of the forward curve as well as overall deposit and loan growth trends.

Contraction in the net interest margin occurred in the second quarter despite growth in average earning assets. Total average earning assets increased four percent on an annualized sequential basis and three percent over the second quarter of 2005. Margin compression was the result of a 13 basis points (bp) sequential and a 53 bp year-over-year decrease in net interest rate spread. The decrease in net interest spread was the result of higher funding costs and the yield curve continuing to be flat, the impact of the primarily fixed-rate security portfolio and a change in mix within core deposits. The average interest rate spread between the 3-month Treasury bill and the 10-year Treasury note compressed from 123 bp in the second quarter of 2005 to 24 bp in the second quarter of 2006, illustrating the relative pressure between shorter-term and longer-term funding costs and general security portfolio

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

re-investment opportunities. The decrease in net interest rate spread was partially offset by an increased benefit from free funding of 68 bp in the second quarter of 2006, up 6 bp from the first quarter of 2006 and 25 bp over the second quarter of 2005. The large increase in the benefit of free funding over the second quarter of 2005 was the result of higher funding costs and an improvement in the net free funding position of the Registrant, calculated as the total of noninterest-bearing liabilities and equity less noninterest-earning assets, which increased three percent to $16.7 billion.

The growth in average loans and leases over the second quarter of 2005 outpaced core deposit growth for the same period by $2.5 billion. The funding shortfall was more than offset by a $3.5 billion reduction in the average available-for-sale securities portfolio, as the Registrant continues to use cash flows from its securities portfolio to reduce its reliance on wholesale funding. For the second quarter of 2006, wholesale funding represented 42% of interest-bearing liabilities, down from 45% for the same period in the prior year. In the current interest rate environment, the Registrant expects to continue to use cash flows from its securities portfolio during the remainder of 2006 to fund its loan and lease growth that is in excess of its core deposit growth.

The Registrant continues to emphasize its highly competitive daily rate deposit pricing strategy. As part of this strategy, the Registrant maintains competitive deposit rates in all of its affiliate markets and across all of its deposit products. Additionally, a migration of interest checking balances into money market, savings and time deposit accounts has continued. During the second quarter of 2006, interest checking balances were 37% of average interest-bearing core deposits and savings and money market combined to represent 40%, compared to 46% and 34%, respectively, in the second quarter of 2005.

The cost of interest-bearing core deposits was 3.12% in the second quarter of 2006, up from 2.88% in the first quarter of 2006 and 1.86% in the second quarter of 2005. Despite the increasing deposit rates, the relative cost advantage of interest-bearing core deposits compared to wholesale funding increased from 130 bp in the second quarter of 2005 and 162 bp in the first quarter of 2006 to 188 bp in the second quarter of 2006.

Interest income (FTE) from loans and leases increased $291 million, or 31%, compared to the second quarter of 2005. The increase resulted from the growth in average loans and leases of nine percent for the second quarter of 2006 over the comparable period in 2005 as well as a 111 bp increase in average rates. The increase in average loans and leases included growth in commercial loans and leases of 11% and growth in average consumer loans and leases of seven percent compared to the second quarter of 2005.

Interest income (FTE) from investment securities and short-term investments decreased $31 million to $253 million for the second quarter of 2006 compared to the same period in 2005 due to the previously mentioned reduction of the investment securities portfolio. The average yield on taxable securities increased by only 10 bp as a result of 84% of the debt securities within the available-for-sale portfolio being fixed-rate securities and the relative stability in longer-term interest rates.

The interest expense on core deposits increased $163 million, or 83%, in the second quarter of 2006 over the comparable period in 2005 due to increases in short-term interest rates and increasing average balances. Average interest-bearing core deposits increased $4 billion, or nine percent, compared to the second quarter of 2005. The Registrant continues to focus on growing its core deposit balances in order to fund loan growth, improve the funding mix and improve net interest margin trends.

The interest expense on wholesale funding increased by $139 million, or 52%, in the second quarter over the comparable period in 2005 due to increasing interest rates partially offset by a $1.4 billion decrease in average balances. The cost of wholesale funding increased from 3.16% in the second quarter of 2005 to 5.00% in the second quarter of 2006 due to the increases in the short-end of the interest rate curve. Included within other short-term borrowings are the Registrant s customer repo sweep balances, which were $2.7 billion and $2.8 billion on an average basis for the three months ended June 30, 2006 and 2005, respectively.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

TABLE 2: Consolidated Average Balance Sheets and Analysis of Net Interest Income (FTE)

For the three months ended	June 30, 2006			June 30, 2005			Attribution of Change in Net Interest Income (a)		
			Average Yield/			Average Yield/		Yield/	
($ in millions)	Average Balance	Revenue/ Cost	Rate	Average Balance	Revenue/ Cost	Rate	Volume	Rate	Total
Assets									
Interest-earning assets:									
Loans and leases *(b)*:									
Commercial loans	**$ 20,239**	**$ 363**	**7.19%**	$ 17,768	$ 248	5.60%	$ 38	77	115
Commercial mortgage	**9,980**	**176**	**7.08**	9,042	136	6.01	15	25	40
Commercial construction	**5,840**	**111**	**7.67**	5,467	80	5.90	6	25	31
Commercial leases	**3,729**	**47**	**5.03**	3,436	44	5.15	4	(1)	3
Subtotal commercial	**39,788**	**697**	**7.03**	35,713	508	5.71	63	126	189
Residential mortgage	**8,756**	**129**	**5.90**	8,453	115	5.45	4	10	14
Residential construction	**735**	**11**	**6.02**	576	8	5.36	2	1	3
Other consumer loans	**22,430**	**377**	**6.75**	20,169	287	5.71	34	56	90
Consumer leases	**1,384**	**16**	**4.70**	1,851	21	4.52	(5)		(5)
Subtotal consumer	**33,305**	**533**	**6.42**	31,049	431	5.56	35	67	102
Total loans and leases	**73,093**	**1,230**	**6.75**	66,762	939	5.64	98	193	291
Securities:									
Taxable	**21,642**	**239**	**4.43**	24,771	268	4.33	(35)	6	(29)
Exempt from income taxes *(b)*	**616**	**11**	**7.33**	815	15	7.29	(4)		(4)
Other short-term investments	**181**	**3**	**5.60**	130	1	3.28	1	1	2
Total interest-earning assets	**95,532**	**1,483**	**6.23**	92,478	1,223	5.30	60	200	260
Cash and due from banks	**2,564**			2,822					
Other assets	**8,393**			8,182					
Allowance for loan and lease losses	**(748)**			(717)					
Total assets	**$ 105,741**			$ 102,765					
Liabilities									
Interest-bearing liabilities:									
Interest checking	**$ 17,025**	**$ 102**	**2.39%**	$ 19,267	$ 71	1.49%	$ (9)	40	31
Savings	**12,064**	**87**	**2.90**	9,697	35	1.44	10	42	52
Money market	**6,429**	**64**	**4.01**	4,755	28	2.37	12	24	36
Other time deposits	**10,449**	**105**	**4.00**	8,286	61	2.93	18	26	44
Certificates - $100,000 and over	**5,316**	**61**	**4.64**	3,946	29	2.92	12	20	32
Foreign office deposits	**4,382**	**52**	**4.77**	3,907	29	2.98	4	19	23
Federal funds purchased	**3,886**	**48**	**4.97**	3,952	29	2.97		19	19
Short-term bank notes				230	2	2.84	(1)	(1)	(2)
Other short-term borrowings	**4,854**	**52**	**4.31**	5,190	34	2.63	(2)	20	18
Long-term debt	**14,465**	**196**	**5.45**	17,049	147	3.46	(25)	74	49

Total interest-bearing liabilities	**78,870**	**767**	**3.90**	76,279	465	2.44	19	283	302
Demand deposits	**13,764**			13,905					
Other liabilities	**3,500**			3,357					
Total liabilities	**96,134**			93,541					
Shareholders equity	**9,607**			9,224					
Total liabilities and shareholders equity	**$ 105,741**			$ 102,765					
Net interest income margin		**$ 716**	**3.01%**		$ 758	3.29%	$ 41	(83)	(42)
Net interest rate spread			**2.33**			2.86			
Interest-bearing liabilities to interest-earning assets			**82.56**			82.48			

(a) *Changes in interest not solely due to volume or yield/rate are allocated in proportion to the absolute dollar amount of change in volume and yield/rate.*

(b) *The net taxable equivalent adjustment amounts included in the above table are $6 million and $8 million for the three months ended June 30, 2006 and 2005, respectively.*

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TABLE 3: Consolidated Average Balance Sheets and Analysis of Net Interest Income (FTE)

For the six months ended	June 30, 2006			June 30, 2005			Attribution of Change in Net Interest Income (a)		
($ in millions)	Average Balance	Revenue/ Cost	Average Yield/ Rate	Average Balance	Revenue/ Cost	Average Yield/ Rate	Volume	Yield/ Rate	Total
Assets									
Interest-earning assets:									
Loans and leases *(b)*:									
Commercial loans	**$ 19,852**	**$ 691**	**7.01%**	$ 17,921	$ 481	5.42%	$ 57	153	210
Commercial mortgage	**9,712**	**336**	**6.96**	8,715	254	5.87	31	51	82
Commercial construction	**6,024**	**222**	**7.43**	5,170	146	5.69	27	49	76
Commercial leases	**3,708**	**93**	**5.08**	3,414	88	5.18	7	(2)	5
Subtotal commercial	**39,296**	**1,342**	**6.88**	35,220	969	5.55	122	251	373
Residential mortgage	**8,555**	**249**	**5.87**	8,435	230	5.49	3	16	19
Residential construction	**720**	**21**	**5.94**	522	14	5.30	5	2	7
Other consumer loans	**22,334**	**734**	**6.63**	19,832	552	5.62	75	107	182
Consumer leases	**1,462**	**35**	**4.87**	1,915	44	4.66	(11)	2	(9)
Subtotal consumer	**33,071**	**1,039**	**6.34**	30,704	840	5.52	72	127	199
Total loans and leases	**72,367**	**2,381**	**6.63**	65,924	1,809	5.53	194	378	572
Securities:									
Taxable	**21,878**	**481**	**4.44**	24,852	534	4.33	(66)	13	(53)
Exempt from income taxes *(b)*	**630**	**23**	**7.47**	835	31	7.32	(8)		(8)
Other short-term investments	**169**	**4**	**5.31**	229	2	2.06	(1)	3	2
Total interest-earning assets	**95,044**	**2,889**	**6.13**	91,840	2,376	5.22	119	394	513
Cash and due from banks	**2,616**			2,721					
Other assets	**8,327**			8,046					
Allowance for loan and lease losses	**(746)**			(716)					
Total assets	**$ 105,241**			$ 101,891					
Liabilities									
Interest-bearing liabilities:									
Interest checking	**$ 17,312**	**$ 201**	**2.34%**	$ 19,618	$ 134	1.38%	$ (17)	84	67
Savings	**11,827**	**163**	**2.79**	9,519	61	1.30	18	84	102
Money market	**6,258**	**119**	**3.83**	4,770	53	2.26	20	46	66
Other time deposits	**10,101**	**194**	**3.87**	8,038	113	2.83	33	48	81
Certificates - $100,000 and over	**4,995**	**109**	**4.41**	3,744	54	2.92	22	33	55
Foreign office deposits	**4,217**	**96**	**4.59**	4,122	56	2.72	1	39	40
Federal funds purchased	**4,217**	**99**	**4.72**	4,060	54	2.68	2	43	45
Short-term bank notes				501	6	2.60	(3)	(3)	(6)
Other short-term borrowings	**4,786**	**97**	**4.07**	5,062	61	2.41	(3)	39	36
Long-term debt	**14,798**	**377**	**5.14**	16,331	267	3.29	(27)	137	110

Total interest-bearing liabilities	**78,511**	**1,455**	**3.74**	75,765	859	2.29	46	550	596
Demand deposits	**13,719**			13,696					
Other liabilities	**3,407**			3,264					
Total liabilities	**95,637**			92,725					
Shareholders equity	**9,604**			9,166					
Total liabilities and shareholders equity	**$ 105,241**			$ 101,891					
Net interest income margin		**$ 1,434**	**3.04%**		$ 1,517	3.33%	$ 73	(156)	(83)
Net interest rate spread			**2.39**			2.93			
Interest-bearing liabilities to interest-earning assets			**82.60**			82.50			

(a) *Changes in interest not solely due to volume or yield/rate are allocated in proportion to the absolute dollar amount of change in volume and yield/rate.*

(b) *The net taxable equivalent adjustment amounts included in the above table are $13 million and $17 million for the six months ended June 30, 2006 and 2005, respectively.*

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Provision for Loan and Lease Losses

The Registrant provides as an expense an amount for probable loan and lease losses within the loan portfolio that is based on the factors discussed in the Critical Accounting Policies section. The provision is recorded to bring the allowance for loan and lease losses to a level deemed appropriate by the Registrant. Actual credit losses on loans and leases are charged against the allowance for loan and lease losses. The amount of loans actually removed from the Condensed Consolidated Balance Sheets is referred to as charge-offs. Net charge-offs include current period charge-offs less recoveries in the current period on previously charged off assets.

The provision for loan and lease losses increased to $71 million in the second quarter of 2006 compared to $60 million in the same period last year. The increase is due to both the increase in net charge-offs from $55 million in the second quarter of 2005 to $67 million and increased loan growth in the second quarter of 2006. The allowance for loan and lease losses as a percent of loans and leases declined to 1.04% from 1.09% at June 30, 2005. Refer to the Credit Risk Management section for further information on the provision for loan and lease losses, net charge-offs and other factors considered by the Registrant in assessing the credit quality of the loan portfolio and the allowance for loan and lease losses.

Noninterest Income

For the three and six months ended June 30, 2006, noninterest income increased by three percent and two percent, respectively. The components of noninterest income for these periods are as follows:

TABLE 4: Noninterest Income

	For the three months ended June 30,		Percent	For the six months ended June 30,		Percent
($ in millions)	**2006**	**2005**	**Change**	**2006**	**2005**	**Change**
Electronic payment processing revenue	**$ 211**	183	15%	**$ 407**	354	15%
Service charges on deposits	**135**	132	2	**261**	253	3
Mortgage banking net revenue	**41**	46	(10)	**88**	87	1
Investment advisory revenue	**96**	92	5	**187**	182	3
Corporate banking revenue	**82**	74	10	**157**	136	16
Other noninterest income	**76**	93	(19)	**157**	200	(23)
Securities gains, net	**14**	15	(6)	**15**	30	(48)
Total noninterest income	**$ 655**	635	3%	**$ 1,272**	1,242	2%

During the first quarter of 2006, the Registrant refined its presentation of noninterest income in order to provide more granularity around its revenue streams. The primary result of this refinement was the consolidation of the Registrant s interest rate derivative sales, international service fees, institutional sales and loan and lease syndication fees into a new income statement line item named corporate banking revenue. Corporate banking revenue increased to $82 million in the second quarter of 2006, up 10% over the comparable period in 2005. The growth in corporate banking revenue was largely attributable to continued strong sales in international services and loan and lease related fees.

Electronic payment processing revenue increased $28 million in the second quarter of 2006 compared to the same period last year. EFT revenue increased $14 million, or 14%, to $116 million, as a result of continued success in attracting financial institution customers as well as an $8 million increase in issuer interchange. Merchant processing revenue increased 17%, to $95 million, compared to the same period in 2005. Trends in the second quarter of 2006 are representative of continuing momentum in attracting new customer relationships moderated by slower growth in the level of retail sales transaction volumes. The Registrant continues to see significant opportunities to attract new retailers and financial institution customers. The Registrant handles electronic processing for over 117,000 merchant locations and 1,500 financial institutions worldwide, including The Kroger Co., Nordstrom, Inc., the Armed Forces Financial Network and, most recently, Linens n Things, Inc., Talbots, Uno Restaurant Holdings Corporation and Rollins, Inc. (wholly-owned subsidiaries include: Orkin, Inc., Western Pest Services and the Industrial Fumigant Company).

Service charges on deposits increased two percent in the second quarter of 2006 compared to the same period last year. Commercial deposit revenue increased two percent while consumer deposit revenue increased three percent. Despite growth in the number of relationships and overall activity, commercial service charges were negatively impacted compared to the second quarter last year by a 43% increase in earnings credits on commercial customer demand deposit accounts due to the higher interest rate environment. Net new consumer deposit account production increased by over 50% through the first half of 2006 compared to the same period last year. Growth in the number of customer deposit account relationships has improved consumer deposit revenue and deposit generation continues to be a primary focus of the Registrant.

Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Mortgage banking net revenue decreased to $41 million in the second quarter of 2006 from $46 million in the same period last year. Mortgage originations were $2.6 billion in the second quarter of 2006 and 2005. The components of mortgage banking net revenue for the three and six months ended June 30, 2006 and 2005 are as follows:

TABLE 5: Components of Mortgage Banking Net Revenue

	For the three months ended June 30,		For the six months ended June 30,	
($ in millions)	**2006**	**2005**	**2006**	**2005**
Origination fees and gains (losses) on loan sales	**$ 27**	38	**48**	61
Servicing revenue:				
Servicing fees	**30**	27	**59**	52
Servicing rights amortization	**(17)**	(16)	**(31)**	(33)
Net valuation adjustments on servicing rights and free-standing derivatives entered into to economically hedge MSR	**1**	(3)	**12**	7
Net servicing revenue	**14**	8	**40**	26
Mortgage banking net revenue	**$ 41**	46	**88**	87

Mortgage net servicing revenue increased by $6 million as compared to the same period last year. Net servicing revenue is comprised of gross servicing fees and amortization as well as valuation adjustments on mortgage servicing rights and mark-to-market adjustments on both settled and outstanding free-standing derivative financial instruments. The Registrant s total residential mortgage loans serviced at June 30, 2006 and 2005 were $35.8 billion and $32.3 billion, respectively, with $27.1 billion and $24.5 billion, respectively, of residential mortgage loans serviced for others.

Net valuation adjustments on servicing rights and free-standing derivatives were affected by the general rise in longer-term interest rates in the second quarter of 2006 and the corresponding general decrease in prepayment speeds, which led to the reversal of $6 million in temporary impairment on the MSR portfolio in the second quarter as compared to a recognition of $21 million in temporary impairment during the second quarter of 2005. Servicing rights are deemed impaired when a borrower s loan rate is distinctly higher than prevailing rates. Impairment on servicing rights is reversed when the prevailing rates return to a level commensurate with the borrower s loan rate. The Registrant recognized a net loss of $5 million and net gain of $18 million in the second quarter of 2006 and 2005, respectively, related to changes in fair value and settlement of free-standing derivatives purchased to economically hedge the MSR portfolio.

The Registrant maintains a non-qualifying hedging strategy to manage a portion of the risk associated with changes in impairment on the MSR portfolio. In the second quarter of 2006, the Registrant primarily used principal only swaps, interest rate swaps and swaptions to hedge the economic risk of the MSR portfolio as they were deemed to be the best available instruments for several reasons. Principal only swaps hedge the mortgage-LIBOR spread because they appreciate in value as a result of tightening spreads. They also provide prepayment protection by increasing in value when prepayment speeds increase, as opposed to MSRs that lose value in a faster prepayment environment. Receive fixed/pay floating interest rate swaps and swaptions increase in value when interest rates do not increase as quickly as expected. As of June 30, 2006 and 2005, the Registrant held a combination of free-standing derivatives, including principal only swaps, swaptions and interest rate swaps with a net negative fair value of $3 million and a net positive fair value of $11 million, respectively, on outstanding notional amounts of $.9 billion and $3.7 billion, respectively. In addition to the derivative positions used to economically hedge the MSR portfolio, the Registrant began to acquire various securities (primarily principal only strips) during 2005 and 2006 as a component of its non-qualifying hedging strategy. Principal only strips increase in value as prepayment speeds increase, thus providing an economic hedge for the MSR portfolio. As of June 30, 2006, the Registrant s available-for-sale securities portfolio included $240 million of securities related to the non-qualifying hedging strategy.

Investment advisory revenues increased by $4 million, or five percent, in the second quarter of 2006 compared to the same period last year. The increase in revenue was primarily related to improved securities and brokerage income and private client revenues. The Registrant continues to focus its sales efforts on integrating services across business lines and working closely with retail and commercial team members to take advantage of a diverse and expanding customer base. The Registrant is one of the largest money managers in the Midwest and as of June 30, 2006 had over $203 billion in assets under care and $31 billion in assets under management.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

The major components of other noninterest income are as follows:

TABLE 6: Components of Other Noninterest Income

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Cardholder fees	$ **11**	11	**23**	22
Consumer loan and lease fees	**13**	15	**24**	28
Operating lease income	**7**	15	**15**	35
Bank owned life insurance income	**22**	22	**43**	45
Insurance income	**7**	7	**14**	12
Other	**16**	23	**38**	58
Total other noninterest income	$ **76**	93	**157**	200

Other noninterest income decreased by 19% in the second quarter of 2006 compared to the same period last year. The decrease was primarily attributable to the continued runoff in the operating lease portfolio. Consumer operating lease revenues result from the consolidation of a special purpose entity in 2003 that was formed for the purpose of the sale and subsequent leaseback of leased automobiles. The consolidation was the result of the Registrant s adoption of FASB Interpretation No. 46. Declines in operating lease revenues will continue throughout 2006, however to a lesser extent, as automobile leases continue to mature and are partially offset by originations of commercial operating leases.

Noninterest Expense

During the second quarter, the Registrant continued to invest in the expansion of the retail distribution network and in the information technology infrastructure. Operating expense levels are often measured using the efficiency ratio (noninterest expense divided by the sum of net interest income (FTE) and noninterest income), which was 55.3% and 52.2% for the second quarter of 2006 and 2005, respectively. The Registrant continues to focus on efficiency initiatives as part of its core emphasis on operating leverage and views its recent investments as its platform for future growth and increasing expense efficiency.

With the continued focus on expense control, the Registrant expects growth in noninterest expenses to be consistent with recent trends. Cost savings initiatives will continue to be somewhat mitigated by investments in certain high opportunity markets, as evidenced by the 25 net new banking centers added in the first half and the 25 net new banking centers expected to be added in the second half of 2006.

The major components of noninterest expense are as follows:

TABLE 7: Noninterest Expense

($ in millions)	For the three months ended June 30, 2006	2005	Percent Change	For the six months ended June 30, 2006	2005	Percent Change
Salaries, wages and incentives	$ **303**	295	3%	$ **586**	561	5%
Employee benefits	**69**	67	4	**156**	148	5
Equipment expense	**29**	25	16	**56**	50	12
Net occupancy expense	**59**	54	9	**118**	108	9
Other noninterest expense	**299**	287	4	**574**	565	1

Total noninterest expense	**$**	**759**	728	4%	**$**	**1,490**	1,432	4%

Total noninterest expense increased four percent in the second quarter of 2006 compared to the same period last year. The increase in expenses is primarily due to the recognition of approximately $9 million of incremental expense related to the adoption of SFAS No. 123 (R) and the April 2006 issuance of stock-based awards to retirement-eligible employees, increases in bankcard volume-related costs and the increase in occupancy expenses offset by a decrease in operating lease expense. Net occupancy expenses increased nine percent in the second quarter of 2006 over the same period last year primarily due to the addition of 61 net new banking centers since June 30, 2005.

Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

The major components of other noninterest expense are as follows:

TABLE 8: Components of Other Noninterest Expense

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Marketing and communications	$ **32**	31	**65**	61
Postal and courier	**12**	12	**25**	24
Bankcard	**79**	63	**148**	126
Loan and lease	**20**	23	**41**	39
Travel	**14**	14	**25**	27
Information technology and operations	**27**	25	**51**	52
Operating lease	**4**	10	**10**	26
Other	**111**	109	**209**	210
Total other noninterest expense	$ **299**	287	**574**	565

Total other noninterest expense increased by $12 million from the second quarter of 2005 primarily due to increases in bankcard expenses. Bankcard expense increased 25% compared to last year due to an increase in the number of merchant and retail customers as well as continued organic growth in debit and credit card usage. The decrease in operating lease expense is attributable to the continued runoff in the operating lease portfolio. The remaining expense captions continue to be well-controlled.

Applicable Income Taxes

The Registrant s income before income taxes, applicable income tax expense and effective tax rate for each of the periods are as follows:

TABLE 9: Applicable Income Taxes

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Income before income taxes and cumulative effect	$ **535**	597	**1,054**	1,183
Applicable income taxes	**153**	180	**312**	361
Effective tax rate	**28.5%**	30.1	**29.6**	30.5

Applicable income tax expense for all periods include the benefit from tax-exempt income, tax-advantaged investments and general business tax credits, partially offset by the effect of nondeductible expenses. Income tax expense for the second quarter of 2006 includes the favorable resolution of certain tax examinations and statute expirations.

Cumulative Effect of Change in Accounting Principle

In the first quarter of 2006, the Registrant recognized a benefit of approximately $4 million, net of $2 million of tax, related to the adoption of SFAS No. 123 (Revised 2004). The benefit recognized relates to the Registrant s estimate of forfeiture experience to be realized for all unvested stock-based awards outstanding.

BUSINESS SEGMENT REVIEW

The Registrant reports on five business segments: Commercial Banking, Branch Banking, Consumer Lending, Investment Advisors and Processing Solutions. During the first quarter of 2006, the Registrant began reporting its Retail line of business as two business segments, Branch Banking and Consumer Lending. All prior year information has been updated to reflect this presentation. Further detailed financial information on each business segment is included in Note 14 of the Notes to the Condensed Consolidated Financial Statements.

Results of the Registrant s business segments are presented based on its management structure and management accounting practices. The structure and practices are specific to the Registrant; therefore, the financial results of the Registrant s business segments are not necessarily comparable with similar information for other financial institutions. The Registrant refines its methodologies from time to time as management accounting practices are improved and businesses change. Revisions to the Registrant s methodologies are applied on a retroactive basis.

The Registrant manages interest rate risk centrally at the corporate level by employing a funds transfer pricing (FTP) methodology. This methodology insulates the business segments from interest rate risk, enabling them to focus on servicing customers through loan originations and deposit taking. The FTP system assigns charge and credit rates to classes of assets and liabilities, respectively, based on expected duration. The Registrant has not changed the conceptual application of FTP during 2005 or 2006. The net impact of the FTP methodology is included in Other/Eliminations.

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The financial results of the business segments include allocations for shared services and headquarters expenses. Even with these allocations, the financial results are not necessarily indicative of the business segments financial condition and results of operations as if they were to exist as independent entities. Additionally, the business segments form synergies by taking advantage of cross-sell opportunities and when funding operations by accessing the capital markets as a collective unit. Net income by business segment is summarized as follows:

TABLE 10: Business Segment Results

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Commercial Banking	$ **202**	193	**396**	372
Branch Banking	**240**	205	**464**	394
Consumer Lending	**37**	54	**80**	102
Investment Advisors	**40**	31	**74**	56
Processing Solutions	**50**	32	**80**	67
Other/Eliminations	**(187)**	(98)	**(348)**	(169)
Net income	$ **382**	417	**746**	822

Commercial Banking

Commercial Banking provides a comprehensive range of financial services and products to large and middle-market businesses, governments and professional customers. In addition to the traditional lending and depository offerings, Commercial Banking products and services include, among others, cash management, foreign exchange and international trade finance, derivatives and capital markets services, asset-based lending, real estate finance, public finance, commercial leasing and syndicated finance. The table below contains selected financial data for the Commercial Banking segment.

TABLE 11: Commercial Banking Selected Financial Data

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Income Statement Data				
Net interest income (FTE)	$ **380**	352	**755**	695
Provision for loan and lease losses	**31**	23	**67**	52
Noninterest income:				
Corporate banking revenue	**78**	73	**150**	132
Service charges on deposits	**38**	38	**77**	76
Other noninterest income	**12**	15	**24**	30
Noninterest expense:				
Salaries, incentives and benefits	**60**	59	**121**	114
Other noninterest expenses	**129**	117	**253**	227
Income before taxes	**288**	279	**565**	540
Applicable income taxes *(a)*	**86**	86	**169**	168
Net income	$ **202**	193	**396**	372

Average Balance Sheet Data				
Commercial loans	**$ 33,377**	30,026	**32,924**	29,677
Demand deposits	**5,994**	6,160	**6,087**	6,187
Interest checking	**3,762**	2,913	**3,844**	2,826
Savings and money market	**5,238**	4,686	**5,335**	4,589
Certificates over $100,000 and other time	**1,537**	1,074	**1,473**	1,004

(a) Includes taxable-equivalent adjustments of $3 million for the three months ended June 30, 2006 and 2005 and $7 million and $6 million for the six months ended June 30, 2006 and 2005, respectively.

Net income increased $9 million, or four percent, compared to the second quarter of 2005 largely as a result of loan and deposit growth. Average commercial loans and leases increased 11% to $33.4 billion over the second quarter of 2005, with growth occurring in all loan categories. Despite average demand deposits declining modestly from the prior year second quarter, average core deposits increased nine percent to $15.0 billion in the second quarter of 2006 from $13.8 billion in 2005. The increase in average core deposits and loans and the related net FTP impact led to a $28 million increase in net interest income compared to the same period last year.

Noninterest income increased modestly compared to the same quarter last year as fee captions displayed mixed results. Overall, corporate banking revenue increased $5 million, or seven percent, largely due to growth in nearly all sub-captions. Noninterest expense increased $13 million, or eight percent, compared to the second quarter of 2005 as continued strong production volumes contributed to increases in loan and bankcard related expense and other noninterest expense.

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Branch Banking

Branch Banking provides a full range of deposit and loan and lease products to individuals and small businesses through 1,138 banking centers. Branch Banking offers depository and loan products, such as checking and savings accounts, home equity lines of credit, credit cards and loans for automobile and other personal financing needs, as well as products designed to meet the specific needs of small businesses, including cash management services. The table below contains selected financial data for the Branch Banking segment.

TABLE 12: Branch Banking Selected Financial Data

($ in millions)		For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Income Statement Data					
Net interest income	$	**476**	416	**928**	809
Provision for loan and lease losses		**26**	23	**48**	43
Noninterest income:					
Electronic payment processing		**49**	41	**93**	77
Service charges on deposits		**93**	91	**178**	171
Investment advisory income		**23**	22	**46**	43
Other noninterest income		**29**	31	**56**	56
Noninterest expense:					
Salaries, incentives and benefits		**117**	115	**232**	227
Net occupancy and equipment expenses		**38**	34	**74**	65
Other noninterest expenses		**118**	112	**230**	214
Income before taxes		**371**	317	**717**	607
Applicable income taxes		**131**	112	**253**	213
Net income	$	**240**	205	**464**	394
Average Balance Sheet Data					
Consumer loans	$	**11,274**	10,529	**11,257**	10,389
Commercial loans		**4,308**	3,947	**4,300**	3,838
Demand deposits		**5,677**	5,718	**5,642**	5,595
Interest checking		**10,915**	14,052	**11,180**	14,406
Savings and money market		**11,612**	8,618	**11,270**	8,538
Time deposits		**12,751**	9,908	**12,203**	9,668

Net income increased $35 million, or 17%, compared to the second quarter of 2005 as growth in average loans and leases and deposits led to a 15% increase in net interest income. Average loans and leases increased eight percent compared to the second quarter of 2005 and total deposits increased seven percent over the second quarter of 2005 with double-digit increases in savings, money market and consumer time deposits mitigated by a 22% decrease in interest checking. As a result of the growth in average loans, core deposits and the related net FTP impact, net interest income increased $60 million compared to the same period last year.

Noninterest income increased $9 million, or five percent, from the second quarter of 2005 as Branch Banking continues to realize results from its cross-sell initiatives. Increases in nearly every caption were led by electronic payment processing revenue, which increased $8 million, or 20%.

Noninterest expense increased by four percent compared to the second quarter of 2005 as costs were contained despite the effect from the Registrant s continued de-novo banking center growth strategy. Net occupancy and equipment expenses increased 13% as a result of the continued opening of new banking centers. Since the second quarter of 2005, 61 net new banking centers were opened. The Registrant continues to position itself for sustained long-term growth through new banking center additions in key markets.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Consumer Lending

Consumer Lending includes the Registrant s mortgage and home equity lending activities and other indirect lending activities. Mortgage and home equity lending activities include the origination, retention and servicing of mortgage and home equity loans or lines of credit, sales and securitizations of those loans or pools of loans or lines of credit and all associated hedging activities. Other indirect lending activities include loans to consumers through auto dealers and federal and private student education loans. The table below contains selected financial data for the Consumer Lending segment.

TABLE 13: Consumer Lending Selected Financial Data

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Income Statement Data				
Net interest income	$ **99**	107	**198**	211
Provision for loan and lease losses	**23**	14	**51**	41
Noninterest income:				
Mortgage banking net revenue	**39**	43	**85**	82
Other noninterest income	**21**	33	**47**	72
Noninterest expense:				
Salaries, incentives and benefits	**28**	24	**56**	47
Other noninterest expenses	**51**	62	**101**	119
Income before taxes	**57**	83	**122**	158
Applicable income taxes	**20**	29	**42**	56
Net income	$ **37**	54	**80**	102
Average Balance Sheet Data				
Consumer loans	$ **20,321**	18,825	**20,108**	18,599

Net income decreased $17 million, or 31%, compared to the second quarter of 2005 largely due to the effects of the flattening yield curve. Compared to the second quarter of 2005, net interest income decreased $8 million, or seven percent, despite average loans and leases increasing eight percent, due to a 31 bp decline in the spread between loans yields and the related FTP charge as a result of the increasing competitive nature in this segment.

The Registrant had mortgage originations of $2.6 billion for the three months ended June 30, 2006 and 2005. Despite the stable origination volume, mortgage banking net revenue declined $4 million due to lower gains on sales. Decreases in other noninterest income and expense were largely a result of the runoff of the consumer automobile lease portfolio as operating lease income and expense decreased from the second quarter of 2005 by $11 million and $8 million, respectively.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Investment Advisors

Investment Advisors provides a full range of investment alternatives for individuals, companies and not-for-profit organizations. The Registrant s primary services include trust, asset management, retirement plans and custody. Fifth Third Securities, Inc., an indirect wholly-owned subsidiary of the Registrant, offers full-service retail brokerage services to individual clients and broker dealer services to the institutional marketplace. Fifth Third Asset Management, Inc., an indirect wholly-owned subsidiary of the Registrant, provides asset management services and also advises the Registrant s proprietary family of mutual funds, Fifth Third Funds.* The table below contains selected financial data for the Investment Advisors segment.

TABLE 14: Investment Advisors Selected Financial Data

($ in millions)	For the three months ended June 30, 2006	For the three months ended June 30, 2005	For the six months ended June 30, 2006	For the six months ended June 30, 2005
Income Statement Data				
Net interest income	$ **59**	47	**113**	92
Provision for loan and lease losses	**1**	1	**3**	3
Noninterest income:				
Investment advisory income	**97**	92	**188**	183
Other noninterest income	**4**	4	**9**	7
Noninterest expense:				
Salaries, incentives and benefits	**42**	41	**85**	84
Other noninterest expenses	**55**	53	**107**	108
Income before taxes	**62**	48	**115**	87
Applicable income taxes	**22**	17	**41**	31
Net income	$ **40**	31	**74**	56
Average Balance Sheet Data				
Loans and leases	$ **3,072**	2,592	**3,058**	2,541
Core deposits	**4,658**	3,978	**4,398**	4,062

Net income increased $9 million, or 30%, in the second quarter of 2006 compared to the same period last year. This increase was the result of a 27% improvement in net interest income due to loan and deposit growth and the related FTP impact. Average loans and leases increased to $3.1 billion, a 19% increase from the second quarter last year while core deposits increased 17% to $4.7 billion. Noninterest income increased $5 million, or five percent, with retail brokerage and private client services both posting increases of $2 million. Noninterest expense increased four percent compared to the same period last year primarily related to an increase in incentive compensation from improved performance in retail brokerage.

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Fifth Third Funds investments are: NOT INSURED BY THE FDIC or any other government agency, are not deposits or obligations of, or guaranteed by, any bank, the distributor or of the Funds any of their respective affiliates, and involve investment risks, including the possible loss of the principal amount invested. *An investor should consider the fund s investment objectives, risks and charges and expenses carefully before investing or sending money. The Funds prospectus contains this and other important information about the Funds. To obtain a prospectus or any other information about Fifth Third Funds, please call 1-800-282-5706 or visit www.53.com. Please read the prospectus carefully before investing. Fifth Third Funds are distributed by Fifth Third Funds Distributor, Inc., 3435 Stelzer Road, Columbus, Ohio 43219.*

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Processing Solutions

Fifth Third Processing Solutions provides electronic funds transfer, debit, credit and merchant transaction processing, operates the Jeanie® ATM network and provides other data processing services to affiliated and unaffiliated customers. The table below contains selected financial data for the Processing Solutions segment.

TABLE 15: Processing Solutions Selected Financial Data

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Income Statement Data				
Net interest income	$ **9**	9	**18**	17
Provision for loan and lease losses	**2**	3	**4**	5
Noninterest income:				
Merchant processing	**97**	82	**184**	161
EFT processing	**73**	67	**143**	127
Other noninterest income	**28**	3	**33**	19
Noninterest expense:				
Salaries, incentives and benefits	**18**	13	**36**	27
Processing costs	**89**	74	**172**	147
Other noninterest expenses	**21**	22	**41**	41
Income before taxes	**77**	49	**125**	104
Applicable income taxes	**27**	17	**45**	37
Net income	$ **50**	32	**80**	67

Net income increased $18 million, or 58%, compared to the second quarter of 2005. Merchant and EFT revenues increased by 18% and 10%, respectively, primarily due to new customer additions and related increased volume. Other noninterest income increased $25 million primarily due to a $24 million gain from the MasterCard Incorporated redemption of a portion of the common shares held by the Registrant. The strong increase in noninterest income was mitigated by a 17% increase in noninterest expense, which increased due to headcount additions, investment in information technology and processing costs. The 20% increase in processing costs resulted primarily from volume-related costs as merchant transactions processed increased 19% over the second quarter of 2005. The Registrant continues to see significant opportunities to attract new financial institution customers and retailers within this business segment.

Other/Eliminations

Other/Eliminations includes the unallocated portion of the investment portfolio, certain wholesale funding, unassigned equity and certain support activities and other items not attributed to the business segments.

The results of Other/Eliminations were primarily impacted by the decrease in interest income from investment securities and the increased cost of wholesale funding. Interest income from the securities portfolio decreased $33 million from the second quarter of 2005 due to the continued runoff of the securities portfolio in 2005 and 2006. Interest expense on wholesale funding increased $139 million from the second quarter of 2005. This increase in interest expense resulted from the increase in the average interest rate on wholesale funding, which rose from 3.16% in the second quarter of 2005 to 5.00% in the second quarter of 2006.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

BALANCE SHEET ANALYSIS

Loans

The table below summarizes the end of period total loans and leases, which includes loans held for sale, by major category:

TABLE 16: Components of Total Loans and Leases (including held for sale)

	June 30, 2006		December 31, 2005		June 30, 2005	
($ in millions)	Balance	Percent of Total	Balance	Percent of Total	Balance	Percent of Total
Commercial:						
Commercial loans	**$ 20,618**	**29%**	$ 19,299	27%	$ 18,017	27%
Commercial mortgage	**9,792**	**13**	9,188	13	9,091	14
Commercial construction	**5,950**	**8**	6,342	9	5,590	8
Commercial leases	**3,740**	**5**	3,698	5	3,537	5
Total commercial loans and leases	**40,100**	**55**	38,527	54	36,235	54
Consumer:						
Residential mortgage	**8,780**	**12**	8,296	12	7,808	12
Residential construction	**748**	**1**	695	1	611	1
Credit card	**945**	**1**	866	1	749	1
Home equity	**12,277**	**16**	12,000	17	11,521	17
Other consumer loans	**9,360**	**13**	9,250	13	8,343	12
Consumer leases	**1,298**	**2**	1,595	2	1,812	3
Total consumer loans and leases	**33,408**	**45**	32,702	46	30,844	46
Total loans and leases	**$ 73,508**	**100%**	$ 71,229	100%	$ 67,079	100%

Total loans and leases increased 10% over the second quarter of 2005. Total commercial loans and leases increased $3.9 billion, or 11%, compared to June 30, 2005. The increase in commercial loans and leases was primarily driven by strong growth in commercial and industrial loans which increased 14% over the second quarter 2005. The mix of commercial loans was essentially unchanged from prior periods.

Total consumer loans and leases increased $2.6 billion, or eight percent, compared to June 30, 2005, as a result of double-digit growth in residential construction, residential mortgage, credit card and other consumer loans. The Registrant is continuing to devote significant focus on producing retail loan originations given the attractive yields available in these products. Consumer lease balances decreased 19% from December 31, 2005 and 28% compared to June 30, 2005 largely resulting from continued competition from captive finance companies offering promotional lease rates. Excluding consumer leases, consumer loans increased 11% over June 30, 2005.

The table below summarizes the average total loans and leases by major category:

TABLE 17: Components of Average Total Loans and Leases (including held for sale)

	June 30, 2006	December 31, 2005	June 30, 2005
($ in millions)	Balance	Balance	Balance

		Percent of Total		Percent of Total		Percent of Total
Commercial:						
Commercial loans	**$ 20,239**	**27%**	$ 18,909	27%	$ 17,768	26%
Commercial mortgage	**9,980**	**14**	9,159	13	9,042	14
Commercial construction	**5,840**	**8**	6,051	9	5,467	8
Commercial leases	**3,729**	**5**	3,611	5	3,436	5
Total commercial loans and leases	**39,788**	**54**	37,730	54	35,713	53
Consumer:						
Residential mortgage	**8,756**	**12**	8,444	12	8,453	13
Residential construction	**735**	**1**	673	1	576	1
Credit card	**897**	**1**	825	1	755	1
Home equity	**12,193**	**17**	11,884	17	11,325	17
Other consumer loans	**9,340**	**13**	9,251	13	8,089	12
Consumer leases	**1,384**	**2**	1,682	2	1,851	3
Total consumer loans and leases	**33,305**	**46**	32,759	46	31,049	47
Total loans and leases	**$ 73,093**	**100%**	$ 70,489	100%	$ 66,762	100%
Total portfolio loans and leases (excluding held for sale)	**$ 72,209**		$ 69,218		$ 65,649	

Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

With strong growth in each category, average commercial loans and leases increased $4.1 billion, or 11%, compared to the second quarter of 2005. The Registrant experienced double-digit growth in more than half of its affiliates, including 18% growth in the Florida markets and 21% growth in the Chicago market.

On an average basis, consumer loans and leases increased $2.3 billion, or seven percent, compared to the second quarter of 2005, highlighted by 39% growth in the Florida markets and strong growth in the Tennessee and Chicago affiliates. The growth in average consumer loans and leases was a result of strong growth in each category mitigated by decreases in consumer leases.

Investment Securities

Total investment securities were $20.9 billion, $22.4 billion and $25.0 billion at June 30, 2006, December 31, 2005 and June 30, 2005, respectively. During the second quarter of 2006, increasing interest rates across the yield curve resulted in an increase in the net unrealized loss on the available-for-sale securities portfolio from $851 million at March 31, 2006 to $1.0 billion at June 30, 2006. Securities are classified as available-for-sale when, in management s judgment, they may be sold in response to or in anticipation of changes in market conditions. The Registrant maintains its intent and ability to hold these securities to the earlier of the recovery of the losses or maturity. At June 30, 2006, 93% of the unrealized losses in the available-for-sale security portfolio were comprised of securities issued by U.S. Treasury and Government agencies, U.S. Government sponsored agencies and states and political subdivisions as well as agency mortgage-backed securities. The Registrant believes the price movements in these securities were the result of the movement in market interest rates, particularly given the negligible inherent credit risk for these securities.

In the second quarter of 2006, the Registrant continued its efforts to reduce the level of available-for-sale securities on the balance sheet. On an amortized cost basis, period end available-for-sale securities decreased $1.2 billion since December 31, 2005 and $3.4 billion since June 30, 2005. At June 30, 2006, available-for-sale securities have decreased to 22% of interest-earning assets, compared to 24% and 27% at December 31, 2005 and June 30, 2005, respectively. At June 30, 2006, 16% of the debt securities in the available-for-sale portfolio were adjustable-rate instruments, compared to 17% at December 31, 2005 and 19% at June 30, 2005. The estimated weighted-average life of the debt securities in the available-for-sale portfolio was 4.8 years at June 30, 2006 compared to 4.3 years at December 31, 2005 and 3.7 years at June 30, 2005. The increase in the weighted-average life results from lower prepayment expectations due to rising interest rates.

Information presented in the following table is on a weighted-average life basis anticipating future prepayments. Yield information is presented on an FTE basis and is computed utilizing historical cost balances. Maturity and yield calculations for the total available-for-sale portfolio exclude equity securities that have no stated yield or maturity.

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

TABLE 18: Characteristics of Available-for-Sale and Other Securities

As of June 30, 2006 ($ in millions)	Amortized Cost	Fair Value	Weighted-Average Life (in years)	Weighted-Average Yield
U.S. Treasury and Government agencies:				
Average life of one year or less	$ 2	$ 2	0.3	2.93%
Average life 1 5 years				
Average life 5 10 years	499	459	6.9	3.71
Average life greater than 10 years	4	4	12.7	6.05
Total	505	465	6.9	3.72
U.S. Government sponsored agencies:				
Average life of one year or less	116	115	0.1	4.43
Average life 1 5 years	1,348	1,288	2.9	3.81
Average life 5 10 years	352	321	6.4	4.07
Average life greater than 10 years				
Total	1,816	1,724	3.4	3.90
Obligations of states and political subdivisions *(a)*:				
Average life of one year or less	51	51	0.5	7.78
Average life 1 5 years	319	325	3.3	7.47
Average life 5 10 years	240	245	6.4	7.15*(b)*
Average life greater than 10 years	40	40	11.9	6.90*(b)*
Total	650	661	4.7	7.37
Agency mortgage-backed securities:				
Average life of one year or less	40	40	0.6	6.31
Average life 1 5 years	9,752	9,256	3.7	4.33
Average life 5 10 years	5,373	5,043	6.9	4.88
Average life greater than 10 years	81	74	10.7	4.79
Total	15,246	14,413	4.9	4.53
Other bonds, notes and debentures *(c)*:				
Average life of one year or less	23	23	0.5	4.41
Average life 1 5 years	1,031	1,001	3.2	4.87
Average life 5 10 years	1,070	1,031	7.7	5.13
Average life greater than 10 years	16	15	22.2	3.71
Total	2,140	2,070	5.6	4.98
Other securities *(d)*	1,019	1,012		
Total available-for-sale and other securities	$ 21,376	$ 20,345	4.8	4.58%

(a) *Taxable-equivalent yield adjustments included in above table are 2.58%, 2.48%, 2.39%, 2.30% and 2.45% for securities with an average life of one year or less, 1-5 years, 5-10 years, greater than 10 years and in total, respectively.*

(b) *Weighted-average yield excludes $17 million and $35 million of securities with an average life of 5-10 years and greater than 10 years, respectively, related to qualified zone academy bonds whose yields are realized through income tax credits. The weighted-average effective yield of these instruments is 6.77%.*

(c) Other bonds, notes and debentures consist of non-agency mortgage backed securities, certain other asset backed securities (primarily automobile and commercial loan backed securities) and corporate bond securities.

(d) Other securities consist of FHLB and Federal Reserve Bank restricted stock holdings that are carried at cost, Federal Home Loan Mortgage Corporation (FHLMC) preferred stock holdings, certain mutual fund holdings and equity security holdings.

TABLE 19: Components of Investment Securities (amortized cost basis)

($ in millions)	June 30, 2006	December 31, 2005	June 30, 2005
Available-for-sale and other:			
U.S. Treasury and Government agencies	**$ 505**	506	504
U.S. Government sponsored agencies	**1,816**	2,034	2,406
Obligations of states and political subdivisions	**650**	657	787
Agency mortgage-backed securities	**15,246**	16,127	17,280
Other bonds, notes and debentures	**2,140**	2,119	2,838
Other securities	**1,019**	1,090	999
Total available-for-sale and other securities	**$ 21,376**	22,533	24,814
Held-to-maturity:			
Obligations of states and political subdivisions	**$ 347**	378	295
Other bonds, notes and debentures	**11**	11	12
Total held-to-maturity	**$ 358**	389	307

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Management s Discussion and Analysis of Financial Condition and Results of Operations (continued)

Deposits

The table below summarizes the end of period total deposits by major category:

TABLE 20: Deposits

($ in millions)	June 30, 2006 Balance	June 30, 2006 Percent of Total	December 31, 2005 Balance	December 31, 2005 Percent of Total	June 30, 2005 Balance	June 30, 2005 Percent of Total
Demand	**$ 14,078**	**20%**	$ 14,609	22%	$ 14,393	23%
Interest checking	**16,788**	**24**	18,282	27	18,811	30
Savings	**12,061**	**17**	11,276	17	9,653	15
Money market	**6,505**	**9**	6,129	9	4,732	7
Other time	**10,627**	**15**	9,313	14	8,513	14
Certificates - $100,000 and over	**5,691**	**8**	4,343	6	3,986	6
Foreign office	**4,773**	**7**	3,482	5	3,089	5
Total deposits	**$ 70,523**	**100%**	$ 67,434	100%	$ 63,177	100%

Deposit balances represent an important source of funding and revenue growth opportunity. The Registrant is continuing to focus on transaction account deposit growth in its retail and commercial franchises by enhancing its product offering and providing competitive rates. The Registrant s goal is to continue to grow the core deposit component of its funding profile. At June 30, 2006, core deposits represented 57% of the Registrant s asset funding base, compared to 54% at June 30, 2005.

Total deposits increased 12% compared to June 30, 2005 primarily attributable to 25% or greater growth in savings, money market and other time deposits, mitigated by an 11% decrease in interest checking. The Registrant continues to realize a mix shift as customers move from lower-yield transaction accounts to higher-yield time deposits. Overall, transaction deposits increased four percent compared to the second quarter of 2005. The Registrant experienced double-digit transaction account deposit growth in the Detroit, Evansville, Indianapolis, Lexington, Louisville, Orlando and Tampa affiliates.

Foreign office deposits represent U.S. dollar denominated deposits of the Registrant s foreign branch located in the Cayman Islands. The Registrant utilizes these deposit balances as a method to fund earning asset growth.

The table below summarizes the average total deposits by major category:

TABLE 21: Average Deposits

($ in millions)	June 30, 2006 Balance	June 30, 2006 Percent of Total	December 31, 2005 Balance	December 31, 2005 Percent of Total	June 30, 2005 Balance	June 30, 2005 Percent of Total
Demand	**$ 13,764**	**20%**	$ 14,099	21%	$ 13,905	22%
Interest checking	**17,025**	**25**	17,828	26	19,267	31
Savings	**12,064**	**17**	11,036	17	9,697	15
Money market	**6,429**	**9**	5,974	9	4,755	7
Other time	**10,449**	**15**	9,143	14	8,286	13
Certificates - $100,000 and over	**5,316**	**8**	4,354	7	3,946	6
Foreign office	**4,382**	**6**	3,703	6	3,907	6

Total deposits	**$ 69,429**	**100%**	$ 66,137	100%	$ 63,763	100%

Borrowings

Total short-term borrowings were $7.8 billion at June 30, 2006 compared to $9.6 billion at December 31, 2005 and $9.5 billion at June 30, 2005. Long-term debt decreased five percent and 17% compared to December 31, 2005 and June 30, 2005, respectively. The Registrant continues to explore additional alternatives regarding the level and cost of various other sources of funding. Refer to the Liquidity Risk Management section for discussion on the Registrant s liquidity management.

TABLE 22: Borrowings

($ in millions)	**June 30, 2006**	**December 31, 2005**	**June 30, 2005**
Federal funds purchased	**$ 2,493**	5,323	4,523
Other short-term borrowings	**5,275**	4,246	4,972
Long-term debt	**14,502**	15,227	17,494
Total borrowings	**$ 22,270**	24,796	26,989

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Quantitative and Qualitative Disclosure about Market Risk (Item 3)

RISK MANAGEMENT OVERVIEW

Managing risk is an essential component of successfully operating a financial services company. The Registrant s risk management function is responsible for the identification, measurement, monitoring, control and reporting of risk and avoidance of those risks that are inconsistent with the Registrant s risk profile. The Enterprise Risk Management division, led by the Registrant s Chief Risk Officer, ensures consistency in the Registrant s approach to managing and monitoring risk within the structure of the Registrant s affiliate operating model. The risks faced by the Registrant include, but are not limited to, credit, market, operational and regulatory compliance. In addition, the Internal Audit division provides an independent assessment of the Registrant s internal control structure and related systems and processes. The Enterprise Risk Management division includes the following key functions:

- Risk Policy - ensures consistency in the approach to risk management as the Registrant s clearinghouse for credit, market and operational risk policies, procedures and guidelines;

- Operational Risk Management - responsible for the risk self-assessment process, the change control evaluation process, fraud prevention and detection, and root cause analysis and corrective action plans relating to identified operational losses;

- Insurance Risk Management - responsible for all property, casualty and liability insurance policies including the claims administration process for the Registrant;

- Capital Markets Risk Management - responsible for establishing and monitoring proprietary trading limits, monitoring liquidity and interest rate risk and utilizing value at risk and earnings at risk models;

- Credit Risk Review - responsible for evaluating the sufficiency of underwriting, documentation and approval processes for consumer and commercial credits;

- Compliance Risk Management - responsible for oversight of compliance with all banking regulations;

- Risk Strategies and Reporting - responsible for quantitative analytics and Board of Directors and senior management reporting on credit, market and operational risk metrics.

Designated risk managers have been assigned to the business lines reporting jointly to the senior executives within the division or affiliate and to the Enterprise Risk Management division. Affiliate risk management is handled by regional risk managers who are responsible for multiple affiliates and who report jointly to affiliate presidents and the Enterprise Risk Management division.

Risk management oversight and governance is provided by the Risk and Compliance Committee of the Board of Directors and through multiple management committees whose membership includes a broad cross-section of line of business, affiliate and support representatives. The Risk and Compliance Committee of the Board of Directors consists of three outside directors and has the responsibility for the oversight of credit, market, operational, regulatory compliance and strategic risk management activities for the Registrant, as well as for the Registrant s overall aggregate risk profile. The Risk and Compliance Committee has approved the formation of key management governance committees that are responsible for evaluating risks and controls. These committees include the Market Risk Committee, the Credit Risk Committee and the Operational Risk Committee. There are also new products and initiatives processes applicable to every line of business to ensure an appropriate standard readiness assessment is performed before launching a new product or initiative. Significant risk policies approved by the management governance committees are also reviewed and approved by the Board of Directors Risk and Compliance Committee.

CREDIT RISK MANAGEMENT

The objective of the Registrant s credit risk management strategy is to quantify and manage credit risk exposure on an aggregate portfolio basis, as well as to limit the risk of loss resulting from an individual customer default. The Registrant s credit risk management strategy is based on three core principles: conservatism, diversification and monitoring. The Registrant believes that effective credit risk management begins with conservative lending practices. These practices include conservative exposure and counterparty limits and conservative underwriting, documentation and collection standards. The Registrant s credit risk management strategy also emphasizes diversification on a geographic, industry and customer level, regular credit examinations and monthly management reviews of large credit exposures and credits experiencing deterioration of credit quality. Lending officers with the authority to extend credit are delegated specific authority amounts, the utilization of which is closely monitored. Lending activities are largely decentralized, while the Enterprise Risk Management division manages the policy process centrally. The Credit Risk Review function, within the Enterprise Risk Management division, provides objective assessments of the quality of underwriting and documentation, the accuracy of risk grades and the charge-off and reserve analysis process.

The Registrant s credit review process and overall assessment of required allowances is based on quarterly assessments of the probable estimated losses inherent in the loan and lease portfolio. The Registrant uses these assessments to promptly identify potential problem loans or leases within the portfolio, maintain an adequate allowance and take any necessary charge-offs. In addition to the individual review of larger commercial loans that exhibit probable or observed credit weakness, the commercial credit review process includes the use of two risk grading systems. The risk grading system currently utilized for allowance analysis purposes encompasses 10 categories. The Registrant also maintains a dual risk grading system that provides for 13 probability of default grade categories and an additional six grade categories for estimating actual losses given an event of default. The probability of default and estimated loss given default evaluations are not separated in the 10-grade risk rating system. The Registrant is in the process of completing significant validation and testing of the dual risk rating system prior to implementation for

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Quantitative and Qualitative Disclosure about Market Risk (continued)

allowance analysis purposes. The dual risk rating system is consistent with Basel II expectations and allows for more precision in the analysis of commercial credit risk. Scoring systems and delinquency monitoring are used to assess the credit risk in the Registrant s homogenous consumer loan portfolios.

Portfolio Diversity

The Registrant s credit risk management strategy includes minimizing concentrations of risk through diversification. The following table provides breakouts of the commercial loan and lease portfolio, including held for sale, by major industry classification, by loan size and by state, illustrating the diversity and granularity of the Registrant s portfolio.

TABLE 23: Commercial Loan and Lease Portfolio *(a)*

		2006			**2005**	
As of June 30 ($ in millions)	**Outstanding**	**Exposure**	**Nonaccrual**	**Outstanding**	**Exposure**	**Nonaccrual**
By industry:						
Real estate	**$ 10,029**	**12,433**	**31**	8,957	10,826	29
Construction	**5,403**	**8,961**	**42**	4,538	7,232	49
Manufacturing	**4,805**	**10,507**	**33**	4,311	9,366	38
Retail trade	**3,701**	**6,244**	**11**	3,298	5,466	18
Transportation and warehousing	**1,945**	**2,280**	**6**	1,512	1,797	7
Business services	**1,927**	**3,536**	**10**	1,892	3,413	23
Wholesale trade	**1,906**	**3,574**	**15**	1,787	3,272	8
Healthcare	**1,702**	**2,967**	**8**	1,545	2,682	6
Individuals	**1,629**	**2,157**	**12**	1,871	2,393	10
Financial services and insurance	**1,173**	**3,853**	**4**	961	2,810	1
Other services	**968**	**1,323**	**15**	899	1,214	7
Other	**958**	**1,425**	**4**	745	1,114	
Accommodation and food	**896**	**1,318**	**10**	1,015	1,438	8
Public administration	**815**	**992**		812	951	
Communication and information	**617**	**1,234**	**3**	530	1,146	1
Agribusiness	**576**	**803**	**1**	537	825	4
Entertainment and recreation	**539**	**761**	**1**	502	696	3
Utilities	**296**	**1,082**		275	812	
Mining	**215**	**408**	**3**	248	417	
Total	**$ 40,100**	**65,858**	**209**	36,235	57,870	212
By loan size:						
Less than $200,000	**5%**	**4**	**16**	6	4	19
$200,000 to $1 million	**18**	**13**	**30**	20	15	39
$1 million to $5 million	**32**	**27**	**40**	35	30	32
$5 million to $10 million	**18**	**16**	**14**	17	16	10
$10 million to $25 million	**20**	**24**		17	23	
Greater than $25 million	**7**	**16**		5	12	
Total	**100%**	**100**	**100**	100	100	100
By state:						
Ohio	**24%**	**28**	**36**	28	31	35
Michigan	**22**	**20**	**20**	23	21	26

Indiana	**10**	**9**	**18**	10	10	10
Illinois	**10**	**10**	**11**	10	10	11
Florida	**10**	**9**	**6**	9	8	3
Kentucky	**6**	**6**	**6**	6	6	7
Tennessee	**3**	**3**	**2**	2	2	3
Pennsylvania	**1**	**2**		1	1	
West Virginia	**1**					1
Out-of-footprint	**13**	**13**	**1**	11	11	4
Total	**100%**	**100**	**100**	100	100	100

(a) *Outstanding reflects total commercial customer loan and lease balances, including held for sale and net of unearned income, and exposure reflects total commercial customer lending commitments.*

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Quantitative and Qualitative Disclosure about Market Risk (continued)

The commercial portfolio is further characterized by 87% of outstanding balances and exposures concentrated within the Registrant s primary market areas of Ohio, Kentucky, Indiana, Michigan, Illinois, Florida, Tennessee, West Virginia and Pennsylvania. Exclusive of a national large-ticket leasing business, the commercial portfolio is characterized by 91% of exposures and 94% of outstanding balances concentrated within these nine states. The mortgage and construction segments of the commercial portfolio are characterized by 97% of exposures and outstanding balances concentrated within these nine states.

Analysis of Nonperforming Assets

Nonperforming assets include: (i) nonaccrual loans and leases on which ultimate collectibility of the full amount of the principal and/or interest is uncertain; (ii) loans and leases that have been renegotiated to provide for a reduction or deferral of interest or principal because of deterioration in the financial position of the borrower and (iii) other assets, including other real estate owned and repossessed equipment. Loans are placed on nonaccrual status when the principal or interest is past due 90 days or more (unless the loan is both well secured and in process of collection) and payment of the full principal and/or interest under the contractual terms of the loan are not expected. Additionally, loans are placed on nonaccrual status upon deterioration of the financial condition of the borrower. When a loan is placed on nonaccrual status, the accrual of interest, amortization of loan premium, accretion of loan discount and amortization or accretion of deferred net loan fees or costs are discontinued. Commercial loans on nonaccrual status are reviewed for impairment at least quarterly. If the principal or a portion of principal is deemed a loss, the loss amount is charged off to the allowance for loan and lease losses.

Total nonperforming assets were $358 million at June 30, 2006, compared to $361 million at December 31, 2005 and $340 million at June 30, 2005. Nonperforming assets as a percent of total loans, leases and other assets, including other real estate owned was .49% as of June 30, 2006 compared to .52% as of December 31, 2005 and .51% as of June 30, 2005. Commercial nonaccrual credits as a percent of loans decreased since the second quarter of 2005, from .59% to .52%. Consumer nonaccrual credits as a percent of loans increased slightly since the second quarter of 2005, from .20% to .22%. Overall, nonaccrual credits continue to represent a small portion of the portfolio at just .38% as of June 30, 2006, compared to .41% as of June 30, 2005. Total loans and leases 90 days past due have increased from $129 million as of June 30, 2005 to $191 million as of June 30, 2006, with the increase driven primarily from the commercial component.

TABLE 24: Summary of Nonperforming Assets and Delinquent Loans

($ in millions)	**June 30, 2006**	**December 31, 2005**	**June 30, 2005**
Commercial loans and leases	**$ 129**	145	132
Commercial mortgages	**62**	51	56
Commercial construction	**18**	31	24
Residential mortgage and construction	**34**	30	25
Consumer loans and leases	**38**	37	36
Total nonaccrual loans and leases	**281**	294	273
Renegotiated loans and leases			1
Other assets, including other real estate owned	**77**	67	66
Total nonperforming assets	**$ 358**	361	340
Commercial loans and leases	**$ 50**	21	24
Commercial mortgages	**16**	8	7
Commercial construction	**6**	6	3
Credit card receivables	**13**	10	10
Residential mortgage and construction *(a)*	**58**	53	44
Consumer loans and leases	**48**	57	41
Total 90 days past due loans and leases	**$ 191**	155	129

Nonperforming assets as a percent of total loans, leases and other assets, including other real estate owned	**.49%**	.52	.51
Allowance for loan and lease losses as a percent of total nonperforming assets	**210**	206	212

(a) *Information for all periods presented excludes advances made pursuant to servicing agreements to Government National Mortgage Association (GNMA) mortgage pools whose repayments are insured by the Federal Housing Administration or guaranteed by the Department of Veterans Affairs. These advances were $10 million as of June 30, 2006 and $13 million as of December 31, 2005 and June 30, 2005.*

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Quantitative and Qualitative Disclosure about Market Risk (continued)

Analysis of Net Loan Charge-offs

The table below provides a summary of credit loss experience and net charge-offs as a percentage of average loans and leases outstanding by loan category:

TABLE 25: Summary of Credit Loss Experience

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Losses charged off:				
Commercial loans	**$ (31)**	(24)	**(66)**	(41)
Commercial mortgage loans	**(5)**	(3)	**(8)**	(5)
Construction loans	**(3)**		**(3)**	(1)
Commercial lease financing	**(2)**		**(2)**	(9)
Residential mortgage loans	**(6)**	(5)	**(10)**	(9)
Consumer loans	**(46)**	(40)	**(96)**	(82)
Consumer lease financing	**(3)**	(4)	**(8)**	(9)
Total losses	**(96)**	(76)	**(193)**	(156)
Recoveries of losses previously charged off:				
Commercial loans	**9**	6	**12**	9
Commercial mortgage loans	**1**	1	**1**	3
Construction loans				1
Commercial lease financing	**1**	1	**3**	1
Residential mortgage loans				
Consumer loans	**16**	12	**31**	22
Consumer lease financing	**2**	1	**6**	2
Total recoveries	**29**	21	**53**	38
Net losses charged off:				
Commercial loans	**(22)**	(18)	**(54)**	(32)
Commercial mortgage loans	**(4)**	(2)	**(7)**	(2)
Construction loans	**(3)**		**(3)**	
Commercial lease financing	**(1)**	1	**1**	(8)
Residential mortgage loans	**(6)**	(5)	**(10)**	(9)
Consumer loans	**(30)**	(28)	**(65)**	(60)
Consumer lease financing	**(1)**	(3)	**(2)**	(7)
Total net losses charged off	**$ (67)**	(55)	**(140)**	(118)
Net charge-offs as a percent of average loans and leases (excluding held for sale):				
Commercial loans	**.44%**	.41	**.54**	.36
Commercial mortgage loans	**.18**	.07	**.14**	.05
Construction loans	**.16**	.02	**.08**	
Commercial lease financing	**.03**	(.03)	**(.04)**	.48
Residential mortgage loans	**.24**	.24	**.26**	.24
Consumer loans	**.57**	.56	**.60**	.61
Consumer lease financing	**.30**	.55	**.27**	.79

Total net losses charged off	**.37**	.34	**.40**	.37

Net charge-offs as a percent of average loans and leases outstanding increased by 3 bp over the second quarter of 2005, to .37% for the second quarter of 2006, and decreased by 5 bp from last quarter. The increase in net charge-offs during the second quarter is partially a result of $6 million in losses realized from the sale of approximately $38 million in nonaccrual loans and leases during the quarter. The Registrant has experienced continued improvement in consumer lease financing net charge-off activity, with a decrease in the ratio of consumer lease financing net charge-offs to average consumer leases outstanding compared to the second quarter of 2005. The ratio of residential mortgage loan net charge-offs to average residential mortgage loans outstanding was stable compared to the second quarter of 2005.

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Quantitative and Qualitative Disclosure about Market Risk (continued)

Allowance for Credit Losses

The allowance for credit losses is comprised of the allowance for loan and lease losses and the reserve for unfunded commitments. The allowance for loan and lease losses provides coverage for probable losses in the loan and lease portfolio. The Registrant evaluates the allowance each quarter to determine its adequacy to cover inherent losses. In the current year, the Registrant has not substantively changed any material aspect to its overall approach in the determination of the allowance for loan and lease losses and there have been no material changes in assumptions or estimation techniques as compared to prior periods that impacted the determination of the current period allowance. The Registrant maintains a reserve for unfunded commitments to provide coverage for probable losses on credit facilities that have not been funded. The methodology used to determine the adequacy of the reserve for unfunded commitments is similar to the Registrant s methodology for determining the allowance for loan and lease losses. The provision for unfunded commitments is included in other noninterest expense on the Condensed Consolidated Statements of Income.

TABLE 26: Changes in Allowance for Credit Losses

($ in millions)	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
Allowance for loan and lease losses:				
Beginning balance	**$ 749**	717	**744**	713
Net losses charged off	**(67)**	(55)	**(140)**	(118)
Provision for loan and lease losses	**71**	60	**149**	127
Ending balance	**$ 753**	722	**753**	722
Reserve for unfunded commitments:				
Beginning balance	**$ 69**	67	**70**	72
Provision for unfunded commitments	**5**	4	**4**	(2)
Acquisitions				1
Ending balance	**$ 74**	71	**74**	71

The allowance for loan and lease losses at June 30, 2006 decreased to 1.04% of the total loan and lease portfolio compared to 1.09% at June 30, 2005 due to an overall improved assessment of inherent losses in the portfolio from the consideration of historical and anticipated loss rates.

Residential Mortgage Portfolio

Certain mortgage products have contractual features that may increase credit exposure to the Registrant in the event of a decline in housing prices. These types of mortgage products offered by the Registrant include high loan-to-value (LTV) ratios, multiple loans on the same collateral that when combined result in a high LTV (80/20) and interest-only loans. Table 27 provides the amount of these loans as a percent of the residential mortgage loans in the Registrant s portfolio and the delinquency rates of these loan products as of June 30, 2006 and 2005. Table 28 shows the Registrant s originations of these products for the three and six months ended June 30, 2006 and 2005. The Registrant does not currently originate mortgage loans that permit principal payment deferral or payments that are less than the accruing interest.

The Registrant also sells certain of these mortgage products in the secondary market with recourse. The outstanding balances and delinquency rates for these loans sold with recourse as of June 30, 2006 and 2005 were $1.1 billion and 1.53% and $614 million and 0.51%, respectively.

The Registrant manages credit risk in the mortgage portfolio through conservative underwriting and documentation standards and geographic and product diversification. The Registrant may also package and sell loans in the portfolio without recourse or may purchase mortgage insurance for the loans sold in order to mitigate credit risk.

TABLE 27: Residential Mortgage Outstandings

	2006			2005		
As of June 30 ($ in millions)	Balance	Percent of total	Delinquency Ratio	Balance	Percent of total	Delinquency Ratio
Greater than 80% LTV with no mortgage insurance	**$ 1,871**	**22%**	**3.23%**	$ 2,267	29%	2.01%
Interest-only	**1,218**	**14**	**.07**	636	8	
Greater than 80% LTV and interest-only	**554**	**6**	**.39**	184	2	1.07
80/20 loans	**33**		**.25**	123	2	

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Quantitative and Qualitative Disclosure about Market Risk (continued)

TABLE 28: Residential Mortgage Originations

	2006		2005	
($ in millions)	Balance	Percent of total	Balance	Percent of total
For the three months ended June 30:				
Greater than 80% LTV with no mortgage insurance	**$ 208**	**8%**	$ 335	14%
Interest-only	**334**	**13**	346	14
Greater than 80% LTV and interest-only	**52**	**2**	118	5
80/20 loans	**132**	**5**	132	5
For the six months ended June 30:				
Greater than 80% LTV with no mortgage insurance	**392**	**8**	609	14
Interest-only	**614**	**13**	591	13
Greater than 80% LTV and interest-only	**153**	**3**	168	4
80/20 loans	**232**	**5**	211	5

MARKET RISK MANAGEMENT

Market risk arises from the potential for fluctuations in interest rates, foreign exchange rates and equity prices that may result in potential reduction in net income. Interest rate risk, a component of market risk, is the exposure to adverse changes in net interest income or financial position due to changes in interest rates. Management considers interest rate risk a prominent market risk in terms of its potential impact on earnings. Interest rate risk can occur for any one or more of the following reasons: (i) assets and liabilities may mature or reprice at different times; (ii) short-term and long-term market interest rates may change by different amounts or (iii) the remaining maturity of various assets or liabilities may shorten or lengthen as interest rates change. In addition to the direct impact of interest rate changes on net interest income, interest rates can indirectly impact earnings through their effect on loan demand, credit losses, mortgage origination fees, the value of servicing rights and other sources of the Registrant s earnings. Consistency of the Registrant s net interest income is largely dependent upon the effective management of interest rate risk.

Net Interest Income Simulation Model

The Registrant employs a variety of measurement techniques to identify and manage its interest rate risk, including the use of an earnings simulation model to analyze net interest income sensitivity to changing interest rates. The model is based on actual cash flows and repricing characteristics for all of the Registrant s financial instruments and incorporates market-based assumptions regarding the effect of changing interest rates on the prepayment rates of certain assets and liabilities. The model also includes senior management projections of the future volume and pricing of each of the product lines offered by the Registrant as well as other pertinent assumptions about the balance sheet. Actual results will differ from these simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and management strategies.

The Registrant s Asset Liability Risk Management Committee (ALCO), which includes senior management representatives and is accountable to the Risk and Compliance Committee of the Board of Directors, monitors and manages interest rate risk within Board approved policy limits. In addition to the risk management activities of ALCO, the Registrant has a Market Risk Management function as part of the Enterprise Risk Management Division that provides independent oversight of market risk activities. The Registrant s current interest rate risk policy limits are determined by measuring the anticipated change in net interest income over a 12-month and 24-month horizon assuming a 200 bp parallel increase or decrease in market interest rates. In accordance with the current policy, the rate movements occur over one year and are sustained thereafter.

The following table shows the Registrant s estimated earnings sensitivity profile on the asset and liability positions as of June 30, 2006:

TABLE 29: Estimated Earnings Sensitivity Profile

	Change in Net Interest Income (FTE)	
Change in interest rates (bp)	**12 Months**	**24 Months**
+ 200	(2.56)%	(5.57)
+ 100	(1.32)	(2.79)
- 100	1.65	3.82
- 200	3.41	5.51

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Quantitative and Qualitative Disclosure about Market Risk (continued)

Market Value of Equity

The Registrant also utilizes the market value of equity (MVE) as a measurement tool in managing interest rate sensitivity. Whereas net interest income simulation highlights exposures over a relatively short time horizon, the MVE analysis incorporates all cash flows over the estimated remaining life of all balance sheet and derivative positions. The MVE of the balance sheet, at a point in time, is defined as the discounted value of asset and derivative cash flows less the discounted value of liability cash flows. The sensitivity of MVE to changes in the level of interest rates is a measure of the longer-term repricing risk. In contrast to the net interest income simulation, which assumes interest rates will change over a period of time, MVE uses instantaneous changes in rates. MVE values only the current balance sheet and does not incorporate the growth assumptions that are used in the net interest income simulation model. As with the net interest income simulation model, assumptions about the timing and variability of balance sheet cash flows are critical in the MVE analysis. Particularly important are the assumptions driving prepayments and the expected changes in balances and pricing of the transaction deposit portfolios. The following table shows the Registrant s MVE sensitivity profile as of June 30, 2006:

TABLE 30: Estimated MVE Sensitivity Profile

Change in Interest Rates (bp)	Change in MVE