CITY HOLDING CO
Form 10-Q
August 09, 2006

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

FORM 10-Q

(Mark One)

x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For The Quarterly Period Ended June 30, 2006
OR
o TRANSITION REPORT PURSANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For The Transition Period From ____________To_____________.

Commission File number **0-11733**

CITY HOLDING COMPANY
(Exact name of registrant as specified in its charter)

West Virginia	**55-0619957**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
25 Gatewater Road Charleston, West Virginia	**25313**
(Address of principal executive offices)	(Zip Code)

(304) 769-1100
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant has (1) 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 o

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 o	Accelerated filer x	Non-accelerated filer o

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

Yes oNo x

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date.

Common stock, $2.50 Par Value - 17,565,971 shares as of August 7, 2006.

FORWARD-LOOKING STATEMENTS

All statements other than statements of historical fact included in this Quarterly Report on Form 10-Q, including statements in Management’s Discussion and Analysis of Financial Condition and Result of Operations are, or may be deemed to be, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Such information involves risks and uncertainties that could result in the Company’s actual results differing from those projected in the forward-looking statements. Important factors that could cause actual results to differ materially from those discussed in such forward-looking statements include, but are not limited to: (1) the Company may incur additional provision for loan losses due to negative credit quality trends in the future that may lead to a deterioration of asset quality; (2) the Company may incur increased charge-offs in the future; (3) the Company may experience increases in the default rates on previously securitized loans that would result in impairment losses or lower the yield on such loans; (4) the Company may continue to benefit from strong recovery efforts on previously securitized loans resulting in improved yields on this asset; (5) the Company could have adverse legal actions of a material nature; (6) the Company may face competitive loss of customers; (7) the Company may be unable to manage its expense levels; (8) the Company may have difficulty retaining key employees; (9) changes in the interest rate environment may have results on the Company’s operations materially different from those anticipated by the Company’s market risk management functions; (10) changes in general economic conditions and increased competition could adversely affect the Company’s operating results; (11) changes in other regulations and government policies affecting bank holding companies and their subsidiaries, including changes in monetary policies, could negatively impact the Company’s operating results; and (12) the Company may experience difficulties growing loan and deposit balances. Forward-looking statements made herein reflect management’s expectations as of the date such statements are made. Such information is provided to assist stockholders and potential investors in understanding current and anticipated financial operations of the Company and is included pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances that arise after the date such statements are made.

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City Holding Company and Subsidiaries

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PART I, ITEM 1 - FINANCIAL STATEMENTS
Consolidated Balance Sheets
City Holding Company and Subsidiaries
(in thousands, except share and per share data)

		June 30 2006 (Unaudited)		December 31 2005 (Note A)
Assets				
Cash and due from banks	$	**59,282**	$	81,822
Interest-bearing deposits in depository institutions		**35,388**		4,451
Cash and Cash Equivalents		**94,670**		86,273
Loans held for sale		**10,012**		-
Securities available for sale, at fair value		**512,474**		549,966
Securities held-to-maturity, at amortized cost (approximate fair value at June 30, 2006 and December 31, 2005 - $57,092 and $58,892)		**54,372**		55,397
Total Securities		**566,846**		605,363
Gross loans		**1,647,539**		1,612,827
Allowance for loan losses		**(15,268)**		(16,790)
Net Loans		**1,632,271**		1,596,037
Bank owned life insurance		**54,058**		52,969
Premises and equipment		**43,094**		42,542
Accrued interest receivable		**11,271**		13,134
Net deferred tax asset		**30,095**		27,929
Intangible assets		**59,219**		59,559
Other assets		**20,485**		18,791
Total Assets	$	**2,522,021**	$	2,502,597
Liabilities				
Deposits:				
Noninterest-bearing	$	**345,207**	$	376,076
Interest-bearing:				
Demand deposits		**427,813**		437,639
Savings deposits		**319,189**		302,571
Time deposits		**880,261**		812,134
Total Deposits		**1,972,470**		1,928,420
Short-term borrowings		**142,156**		152,255
Long-term debt		**90,854**		98,425
Other liabilities		**32,421**		31,356
Total Liabilities		**2,237,901**		2,210,456
Shareholders' Equity				
Preferred stock, par value $25 per share: 500,000 shares authorized; none issued		**-**		-
Common stock, par value $2.50 per share: 50,000,000 shares authorized; 18,499,282 shares issued and outstanding at June 30, 2006 and December		**46,249**		46,249

31, 2005, less 928,811 and 395,465 shares in treasury, respectively

Capital surplus		**103,825**		104,435
Retained earnings		**177,467**		160,747
Cost of common stock in treasury		**(30,486)**		(11,278)
Accumulated other comprehensive income:				
Unrealized loss on securities available-for-sale		**(8,750)**		(4,839)
Unrealized loss on derivative instruments		**(1,012)**		-
Underfunded pension liability		**(3,173)**		(3,173)
Total Accumulated Other Comprehensive Loss		**(12,935)**		(8,012)
Total Shareholders' Equity		**284,120**		292,141
Total Liabilities and Shareholders' Equity	**$**	**2,522,021**	$	2,502,597

See notes to consolidated financial statements.

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Consolidated Statements of Income *(Unaudited)*
City Holding Company and Subsidiaries
(in thousands , except earnings per share data)

	Three Months Ended June 30		Six Months Ended June 30	
	2006	2005	**2006**	2005
Interest Income				
Interest and fees on loans	**$ 30,451**	$ 24,523	**$ 60,014**	$ 46,713
Interest on investment securities:				
Taxable	**7,489**	7,682	**14,748**	15,328
Tax-exempt	**455**	447	**922**	882
Interest on loans held for sale	**200**	-	**200**	-
Interest on deposits in depository institutions	**415**	24	**566**	42
Interest on federal funds sold	**-**	-	**-**	4
Total Interest Income	**39,010**	32,676	**76,450**	62,969
Interest Expense				
Interest on deposits	**10,520**	6,605	**19,721**	12,473
Interest on short-term borrowings	**1,326**	787	**2,452**	1,364
Interest on long-term debt	**1,239**	1,662	**2,499**	3,247
Total Interest Expense	**13,085**	9,054	**24,672**	17,084
Net Interest Income	**25,925**	23,622	**51,778**	45,885
Provision for loan losses	**675**	-	**1,675**	-
Net Interest Income After Provision for Loan Losses	**25,250**	23,622	**50,103**	45,885
Non-Interest Income				
Investment securities gains	**-**	18	**-**	21
Service charges	**10,903**	9,685	**20,764**	18,128
Insurance commissions	**521**	545	**1,135**	1,137
Trust and investment management fee income	**504**	462	**1,070**	1,053
Bank owned life insurance	**678**	545	**1,215**	1,536
Other income	**857**	843	**1,667**	1,667
Total Non-Interest Income	**13,463**	12,098	**25,851**	23,542
Non-Interest Expense				
Salaries and employee benefits	**8,764**	8,404	**17,396**	16,324
Occupancy and equipment	**1,624**	1,564	**3,223**	3,039
Depreciation	**1,071**	994	**2,121**	1,938
Professional fees and litigation expense	**571**	514	**966**	1,079
Postage, delivery, and statement mailings	**689**	615	**1,333**	1,268
Advertising	**755**	762	**1,529**	1,467
Telecommunications	**525**	513	**1,001**	986
Bankcard expenses	**458**	560	**1,001**	1,085
Insurance and regulatory	**381**	365	**769**	731
Office supplies	**372**	275	**754**	478

Repossessed asset gains, net of expenses		**(129)**		(16)		**(125)**		(15)
Loss on early estinguishment of debt		**-**		-		**282**		-
Other expenses		**2,474**		2,289		**4,802**		4,472
Total Non-Interest Expense		**17,555**		16,839		**35,052**		32,852
Income Before Income Taxes		**21,158**		18,881		**40,902**		36,575
Income tax expense		**7,397**		6,532		**14,275**		12,548
Net Income	**$**	**13,761**	$	12,349	**$**	**26,627**	$	24,027
Basic earnings per common share	**$**	**0.78**	$	0.72	**$**	**1.49**	$	1.42
Diluted earnings per common share	**$**	**0.77**	$	0.71	**$**	**1.49**	$	1.40
Dividends declared per common share	**$**	**0.28**	$	0.25	**$**	**0.56**	$	0.50
Average common shares outstanding:								
Basic		**17,719**		17,268		**17,860**		16,938
Diluted		**17,772**		17,477		**17,917**		17,146

See notes to consolidated financial statements.

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Consolidated Statements of Changes in Shareholders' Equity *(Unaudited)*
City Holding Company and Subsidiaries
Six Months Ended June 30, 2006 and 2005
(in thousands)

	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balances at December 31, 2004	$ 42,298	$ 55,512	$ 128,175	$ (8,761)	$ (1,144)	$ 216,080
Comprehensive income:						
Net income			24,027			24,027
Other comprehensive income, net of deferred income taxes of $1,460:						
Net unrealized losses on available-for-sale securities of $3,497, net of reclassification adjustment for gains included in net income of $20					(2,086)	(2,086)
Net unrealized loss on interest rate floors of $173					(104)	(104)
Total comprehensive income						21,837
Cash dividends declared ($0.50 per share)			(8,651)			(8,651)
Issuance of 1,580,034 shares for acquisition of Classic Bancshares, net 108,173 shares owned and transferred to treasury	3,951	53,739		(3,351)		54,339
Issuance of stock awards net		(307)		454		147
Exercise of 38,368 stock options		(675)		1,172		497
Purchase of 137,476 shares for treasury				(4,625)		(4,625)
Balances at June 30, 2005	$ 46,249	$ 108,269	$ 143,551	$ (15,111)	$ (3,334)	$ 279,624

	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balances at December 31, 2005	**$ 46,249**	**$ 104,435**	**$ 160,747**	**$ (11,278)**	**$ (8,012)**	**$ 292,141**
Comprehensive income:						
Net income			**26,627**			**26,627**

Other comprehensive loss, net of deferred income taxes of $3,282:						
Unrealized losses on available-for-sale securities of $6,518, net of taxes					**(3,911)**	**(3,911)**
Net unrealized loss on interest rate floors of $1,687					**(1,012)**	**(1,012)**
Total comprehensive income						**21,704**
Cash dividends declared ($0.56 per share)			**(9,907)**			**(9,907)**
Issuance of stock awards net		**(58)**		**245**		**187**
Exercise of 32,007 stock options		**(747)**		**1,172**		**425**
Excess tax benefit on stock -based compensation		**195**				**195**
Purchase of 572,053 treasury shares				**(20,625)**		**(20,625)**
Balances at June 30, 2006	**$ 46,249**	**$ 103,825**	**$ 177,467**	**$ (30,486)**	**$ (12,935)**	**$ 284,120**

See notes to consolidated financial statements.

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Consolidated Statements of Cash Flows *(Unaudited)*
City Holding Company and Subsidiaries
(in thousands)

	Six Months Ended June 30	
	2006	2005
Operating Activities		
Net income	**$ 26,627**	$ 24,027
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization and accretion	**(1,453)**	1,048
Provision for loan losses	**1,675**	-
Depreciation of premises and equipment	**2,121**	1,938
Deferred income tax expense	**1,010**	1,874
Net periodic employee benefit cost	**123**	24
Loss on early extinguishment of debt	**282**	-
Realized investment securities gains	**-**	(21)
Loss (gain) on sale of premises and equipment	**15**	(67)
Proceeds from bank-owned life insurance	**125**	910
Increase in value of bank-owned life insurance	**(1,214)**	(1,536)
Decrease (increase) in accrued interest receivable	**1,863**	(727)
Increase in other assets	**(3,523)**	(3,923)
Increase (decrease) in other liabilities	**820**	(3,789)
Net Cash Provided by Operating Activities	**28,471**	19,758
Investing Activities		
Proceeds from maturities and calls of securities held-to-maturity	**909**	2,822
Proceeds from sale of money market and mutual fund securities available-for-sale	**500,250**	668,100
Purchases of money market and mutual fund securities available-for-sale	**(509,516)**	(666,650)
Proceeds from sales of securities available-for-sale	**3,223**	1,604
Proceeds from maturities and calls of securities available-for-sale	**39,320**	71,617
Purchases of securities available-for-sale	**(3,018)**	(11,737)
Net (increase) in loans	**(45,337)**	(15,132)
Sales of premises and equipment	**-**	101
Purchases of premises and equipment	**(2,688)**	(1,352)
Acquisition, net cash received	**-**	(7,121)
Net Cash (Used in) Provided by Investing Activities	**(16,857)**	42,252
Financing Activities		
Net (decrease) in noninterest-bearing deposits	**(30,869)**	(16,310)
Net increase (decrease) in interest-bearing deposits	**75,016**	(13,249)
Net (decrease) in short-term borrowings	**(12,410)**	(13,323)
Repayment of long-term debt	**(2,731)**	(329)
Redemption of trust preferred securities	**(2,705)**	-
Purchases of treasury stock	**(20,625)**	(4,625)
Exercise of stock options	**425**	497
Excess tax benefits from stock-based compensation arrangements	**195**	-
Dividends paid	**(9,513)**	(7,806)
Net Cash Used in Financing Activities	**(3,217)**	(55,145)

Increase in Cash and Cash Equivalents		**8,397**		6,865
Cash and cash equivalents at beginning of period		**86,273**		56,084
Cash and Cash Equivalents at End of Period	**$**	**94,670**	$	62,949

See notes to consolidated financial statements.

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Notes to Consolidated Financial Statements (Unaudited)
June 30, 2006
Note A - Basis of Presentation

The accompanying consolidated financial statements, which are unaudited, include all of the accounts of City Holding Company ("the Parent Company") and its wholly-owned subsidiaries (collectively, "the Company"). All material intercompany transactions have been eliminated. The consolidated financial statements include all adjustments that, in the opinion of management, are necessary for a fair presentation of the results of operations and financial condition for each of the periods presented. Such adjustments are of a normal recurring nature. The results of operations for the six months ended June 30, 2006 are not necessarily indicative of the results of operations that can be expected for the year ending December 31, 2006. The Company's accounting and reporting policies conform with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Such policies require management to make estimates and develop assumptions that affect the amounts reported in the consolidated financial statements and related footnotes. Actual results could differ from management's estimates.

The consolidated balance sheet as of December 31, 2005 has been extracted from audited financial statements included in the Company's 2005 Annual Report to Stockholders. Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with U.S. generally accepted accounting principles have been omitted. These financial statements should be read in conjunction with the financial statements and notes thereto included in the 2005 Annual Report of the Company.

Certain amounts in the 2005 financial statements have been reclassified to conform to the 2006 presentation. Such reclassifications had no impact on net income or shareholders' equity.

Note B -Previously Securitized Loans

Between 1997 and 1999, the Company completed six securitization transactions involving approximately $760 million in 125% of fixed rate, junior-lien underlying mortgages. The Company retained a financial interest in each of the securitizations. Principal amounts owed to investors were evidenced by securities ("Notes"). The Notes were subject to redemption, in whole but not in part, at the option of the Company, as owner of the retained interests in the securitization transactions, or at the option of the Note insurer, on or after the date on which the related Note balance declined to 5% or less of the original Note balance. Once the Notes were redeemed, the Company became the beneficial owner of the mortgage loans and recorded the loans as assets of the Company within the loan portfolio. During 2003 and 2004, the outstanding Note balances of the six securitizations declined below this 5% threshold and the Company exercised its redemption options on each of those securitizations. The table below summarizes information regarding delinquencies, net credit recoveries, and outstanding collateral balances of previously securitized loans for the dates presented:

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(in thousands)		As of and for the Six Months Ended June 30, **2006**		2005 *(in thousands)*		As of and for the Year Ended December 31, 2005
Previously Securitized Loans:						
Total principal amount of loans outstanding	**$**	**39,976**	$	59,403	$	48,061
Discount		**(17,723)**		(17,733)		(17,805)
Net book value	**$**	**22,253**	$	41,670	$	30,256
Principal amount of loans between 30 and 89 days past due	**$**	**866**	$	2,536	$	1,848
Principal amount of loans 90 days and above past due		**277**		376		268
Net credit recoveries during the period		**2,552**		1,306		3,225

In accordance with Statement of Position 03-3, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*, issued by the Accounting Standards Executive Committee, the Company is accounting for the difference between the carrying value and the expected total cash flows from these loans as an adjustment of the yield earned on the loans over their remaining lives. The discount is accreted to income over the period during which payments are probable of collection and are reasonably estimable. Additionally, the collectibility of previously securitized loans is evaluated over the remaining lives of the loans. An impairment charge on previously securitized loans would be provided through the Company's provision for loan losses if the discounted present value of estimated future cash flows declines below the recorded value of previously securitized loans. No such impairment charges were recorded for the six months ended June 30, 2006, or for the year ending December 31, 2005.

As the Company redeemed the outstanding Notes from its securitizations, no gain or loss was recognized in the Company's financial statements and the remaining mortgage loans were recorded in the Company's loan portfolio at carrying value. Because the book value of the mortgage loans incorporates assumptions for expected prepayment and default rates, the book value of the loans is generally less than the contractual outstanding balance of the mortgage loans. As of June 30, 2006, the Company reported a book value of previously securitized loans of $22.3 million whereas the actual contractual outstanding balance of previously securitized loans at June 30, 2006, was $40.0 million. The difference ("the discount") between the book value and the expected total cash flows from previously securitized loans is accreted into interest income over the life of the loans.

During the first six months of 2006 and 2005, the Company recognized $5.2 million and $5.9 million, respectively, of interest income from its previously securitized loans.

Note C -Derivative Instruments

The Company utilizes interest rate floors to mitigate exposure to interest rate risk. As of June 30, 2006, the Company has entered into seven interest rate floor contracts with a total notional amount of $500 million at a cost of $5.8 million that are designated as cash flow hedges. The objective of these interest rate floors is to protect the overall cash flows from the Company's monthly interest receipts on a rolling portfolio of $500 million of variable-rate loans outstanding from the risk of a decrease in those cash flows to a level such that the yield on the underlying loans would be less than a range of 6.00% to 8.00%.

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The notional amounts and estimated fair values of interest rate floor derivative positions outstanding at period end are presented in the following table. The estimated fair values of the interest rate floors on variable-rate loans are based on quoted market prices.

(*in thousands*)	**June 30, 2006**		December 31, 2005	
	Notional Value	**Estimated Fair Value**	Notional Value	Estimated Fair Value
Interest rate floors on variable-rate loans	**$ 500,000**	**$ 2,935**	$ 400,000	$ 1,270

The weighted-average strike rates for interest rate floors outstanding at June 30, 2006 are 6.00% to 8.00%.

Interest rate contracts involve the risk of dealing with counterparties and their ability to meet contractual terms. These counterparties must have an investment grade credit rating and be approved by the Company's Asset and Liability Committee.

For cash flow hedges, the effective portion of the gain or loss on the derivative hedging instrument is reported in other comprehensive income, while the ineffective portion (indicated by the excess of the cumulative change in the fair value of the derivative over that which is necessary to offset the cumulative change in expected future cash flows on the hedge transaction) is recorded in current earnings as other income or other expense. The Company recognized a charge for the decrease in fair value of $1.0 million, net of taxes, in Other Comprehensive Income for the six months ending June 30, 2006 on these derivative instruments.

During the second quarter of 2006, the Company redesignated an interest rate floor contract with a total notional amount of $100 million that had previously been accounted for as a cash flow hedge as a freestanding derivative. As a result of this redesignation, the Company recorded a $0.1 million charge to expense to reflect changes in fair value of this instrument. This interest rate floor has no fair value reflected in the Company's Consolidated Balance Sheet at June 30, 2006, matures in 23 months and has strike rate of 6.00%.

Note D - Short-term borrowings

The components of short-term borrowings are summarized below:

(in thousands)	**June 30, 2006**	December 31, 2005
Security repurchase agreements	**$ 95,296**	$ 76,443
Short-term FHLB advances	**46,860**	75,812
Total short-term borrowings	**$ 142,156**	$ 152,255

Securities sold under agreements to repurchase were sold to corporate and government customers as an alternative to available deposit products. The underlying securities included in repurchase agreements remain under the Company's control during the effective period of the agreements.

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Note E - Long-Term Debt

The components of long-term debt are summarized below:

(dollars in thousands)	Maturity	June 30, 2006	Weighted Average Interest Rate
FHLB Advances	2008	$ **46,941**	3.55%
FHLB Advances	2009	**10,021**	4.86%
FHLB Advances	2010	**3,000**	6.05%
FHLB Advances	2011	**1,000**	5.98%
FHLB Advances	Thereafter	**3,556**	4.90%
Junior subordinated debentures owed to City Holding Capital Trust	2028 (a)	**26,336**	9.15%
Total long-term debt		**$ 90,854**	

(a) Junior Subordinated Debentures owed to City Holding Capital Trust are redeemable prior to maturity at the option of the Company (i) on or after April 1, 2008, in whole at any time or in part from time-to-time, at declining redemption prices ranging from 104.58% to 100.00% on April 1, 2018, and thereafter, or (ii) in whole, but not in part, at any time within 90 days following the occurrence and during the continuation of certain pre-defined events.

The Company formed a statutory business trust, City Holding Capital Trust (“the Capital Trust”), under the laws of Delaware. The Capital Trust was created for the exclusive purpose of (i) issuing trust-preferred capital securities (“Capital Securities”), which represent preferred undivided beneficial interests in the assets of the trust, (ii) using the proceeds from the sale of the Capital Securities to acquire junior subordinated debentures (“Debentures”) issued by the Company, and (iii) engaging in only those activities necessary or incidental thereto. The trust is considered a variable interest entity for which the Company is not the primary beneficiary. Accordingly, the accounts of the trusts are not included in the Company’s consolidated financial statements.

The Capital Securities issued by the statutory business trust qualify as Tier 1 capital for the Company under the Federal Reserve Board guidelines. In March 2005, the Federal Reserve Board issued a final rule that allows the inclusion of trust preferred securities issued by unconsolidated subsidiary trusts in Tier 1 capital, but with stricter limits. Under this ruling, after a five-year transition period, the aggregate amount of trust preferred securities and certain other capital elements would be limited to 25% of Tier 1 capital elements, net of goodwill. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Tier 2 capital, subject to restrictions. The Company expects to include all of its $25.5 million in trust preferred securities in Tier 1 capital. The trust preferred securities could be redeemed without penalty if they were no longer permitted to be included in Tier 1 capital.

Note F - Employee Benefit Plans

On January 1, 2006, the Company adopted SFAS No. 123R, “Share-Based Payment,” which is a revision of SFAS No. 123, “Accounting for Stock Issued for Employees.” SFAS No. 123R establishes accounting requirements for share-based compensation to employees and carries forward prior guidance on accounting for awards to non-employees. Prior to the adoption of SFAS No. 123R, the Company reported employee compensation expense under stock option plans only if options were granted below market prices at grant date in accordance with the intrinsic value method of Accounting Principles Board Opinion (“APB”) No. 25, “Accounting for Stock Issued to Employees,” and related interpretations. In accordance with APB No. 25, the Company reported no compensation expense on options granted as the exercise price of the options granted always equaled the market price of the underlying stock on the date of grant. SFAS No. 123R eliminated the ability to account for stock-based compensation using APB No. 25 and requires that such transactions be recognized as compensation cost in the income statement based on their fair values on the measurement date, which is generally the date of the grant.

The Company transitioned to SFAS No. 123R using the modified prospective application method ("modified prospective application"). As permitted under modified prospective application, as it is applicable to the Company, SFAS No. 123R applies to new awards and to awards modified, repurchased, or cancelled after January 1, 2006. Additionally, compensation cost for non-vested awards that were outstanding as of January 1, 2006 will be recognized as the remaining requisite service is rendered during the period of and/or the periods after the adoption of SFAS No. 123R, adjusted for estimated forfeitures. The recognition of compensation cost for those earlier awards is based on the same method and on the same grant-date fair values previously determined for the pro forma disclosures reported by the Company for periods prior to January 1, 2006.

The fair value of the Company's employee stock options granted is estimated at the date of grant using the Black-Scholes option-pricing model. This model requires the input of highly subjective assumptions, changes to which can materially affect the fair value estimate. Additionally, there may be other factors that would otherwise have a significant effect on the value of employee stock options granted, but are not considered by the model. Because the Company’s employee stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the fair value estimate, in management’s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options at the time of grant. The assumptions used in the Black-Scholes option-pricing model are as follows:

	For the Six Months Ended June 30,	
	2006	2005
Risk-free interest rate	**3.93%**	3.71%
Expected dividend yield	**2.98%**	3.12%
Volatility factor	**0.384**	0.388
Expected life of option	**5 years**	5 years

As the Company has not issued any options during the six months ended June 30, 2006, the factors for June 30, 2006 are consistent with amounts reported in the Company’s 2005 Annual Report.

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There was no material impact on the Company's income before income taxes and net income from the adoption of SFAS No. 123R. Prior to the adoption of SFAS No. 123R, the Company presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the Consolidated Statements of Cash Flows. SFAS No. 123R requires the cash flows from the tax benefits resulting from tax deductions in excess of the compensation expense recognized for those options to be classified as financing cash flows. An excess tax benefit totaling $0.2 million is classified as a financing cash inflow for the six months ended June 30, 2006.

Stock-based compensation expense is recognized ratably over the requisite service period for all awards. Unrecognized stock-based compensation expense related to stock options totaled $0.4 million at June 30, 2006. At June 30, 2006, this unrecognized expense is expected to be recognized over 1.5 years based on the weighted average-life of the option.

The following pro forma information presents net income, earnings per share, and diluted earnings per share for the three and six months ended June 30, 2005 as if the fair value method of SFAS No. 123R had been used to measure compensation cost for stock-based compensation plans. For purposes of these pro forma disclosures, the estimated fair value of options is amortized to expense over the options' vesting periods.

(in thousands, except earnings per share data)	For the Three Months Ended June 30, 2005	For the Six Months Ended June 30, 2005
Net income, as reported	$ 12,349	$ 24,027
Pro forma stock-based employee compensation expense, net of tax	(172)	(204)
Net income, pro forma	$ 12,177	$ 23,823
Basic earnings per share, as reported	$ 0.72	$ 1.42
Basic earnings per share, pro forma	$ 0.71	$ 1.41
Diluted earnings per share, as reported	$ 0.71	$ 1.40
Diluted earnings per share, pro forma	$ 0.70	$ 1.39

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A summary of the Company's stock option activity and related information is presented below for the six months ended June 30:

	2006			2005		
	Options		**Weighted-Average Exercise Price**	Options		Weighted-Average Exercise Price
Outstanding at January 1	**318,132**	**$**	**28.56**	602,307	$	16.51
Granted	**-**		**-**	99,000		32.15
Exercised	**(32,007)**		**13.30**	(38,368)		12.95
Forfeited	**-**		**-**	(60,000)		33.90
Outstanding at June 30	**286,125**	**$**	**30.27**	602,939	$	17.57

Additional information regarding stock options outstanding and exercisable at June 30, 2006, is provided in the following table:

Ranges of Exercise Prices	No. of Options Outstanding	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (Months)	Aggregate Intrinsic Value (in thousands)	No. of Options Currently Exercisable	Weighted-Average Exercise Price of Options Currently Exercisable	Aggregate Intrinsic Value of Options Currently Exercisable (in thousands)
$13.30	24,100	$ 13.30	67	$ 550	24,100	$ 13.30	$ 550
$28.00 - $36.90	262,025	31.83	97	1,161	189,400	31.66	881
	286,125			$ 1,711	213,500		$ 1,431

In addition to stock options, the Company also grants restricted stock awards to certain officers and employees. The Company records compensation expense with respect to such awards in an amount equal to the fair market value of the common stock covered by each award on the date of grant. The restricted shares awarded become fully vested after various periods of continued employment from the respective dates of grant. The Company becomes entitled to an income tax deduction in an amount equal to the taxable income reported by the holders of the restricted shares when the restrictions are released and the shares are issued. The deferred compensation cost reflected in shareholders' equity is being amortized as compensation expense over the respective vesting periods using the straight-line method. Restricted shares are forfeited if officers and employees terminate prior to the lapsing of restrictions. The Company records forfeitures of restricted stock as treasury share repurchases and any compensation cost previously recognized is reversed in the period of forfeiture. Stock-based compensation expense associated with stock awards, included in salaries and employee benefits, was $0.1 million for the six month period ended June 30, 2006. There was no expense associated with stock awards for the 2005 reporting period. Unrecognized stock-based compensation expense related to non-vested stock awards was $0.3 million at June 30, 2006. At June 30, 2006, this unrecognized expense is expected to be recognized over 4 years based on the weighted average-life of the options.

The Company provides retirement benefits to its employees through the City Holding Company 401(k) Plan and Trust ("the 401(k) Plan"), which is intended to be compliant with Employee Retirement Income Security Act (ERISA) section 404(c). Any employee who has attained age 21 is eligible to participate beginning the first day of the month following employment. Unless specifically chosen otherwise, every employee is automatically enrolled in the 401(k) Plan and may make before-tax contributions of between 1% and 15% of eligible pay up to the dollar limit imposed by Internal Revenue Service regulations. The first 6% of an employee's contribution is matched 50% by the Company. The employer matching contribution is invested according to the investment elections chosen by the employee. Employees are 100% vested in both employee and employer contributions and the earnings they generate. The Company's total expense associated with the retirement benefit plan approximated $0.3 million for both of the six month periods ended June 30, 2006 and June 30, 2005 and approximated $0.1 million for both of the three month periods ended June 30, 2006 and June 30, 2005.

The Company also maintains a defined benefit pension plan ("the Defined Benefit Plan") that covers approximately 300 current and former employees. The Defined Benefit Plan was frozen in 1999 subsequent to the Company's acquisition of the plan sponsor. The Defined Benefit Plan maintains an October 31 year-end for purposes of computing its benefit obligations. The Company made contributions to the Defined Benefit Plan approximating $0.1 million for both of the six month periods ended June 30, 2006 and 2005.

The following table presents the components of the net periodic pension cost of the Defined Benefit Plan:

	Three months ended June 30,		Six months ended June 30,	
(in thousands)	**2006**	2005	**2006**	2005
Components of net periodic cost:				
Interest cost	**$ 213**	$ 165	**$ 341**	$ 331
Expected return on plan assets	**(238)**	(191)	**(382)**	(381)
Net amortization and deferral	**102**	50	**164**	74
Net Periodic Pension Cost	**$ 77**	$ 24	**$ 123**	$ 24

Note G - Commitments and Contingencies

The Company is a party to certain financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. The Company has entered into agreements with its customers to extend credit or provide a conditional commitment to provide payment on drafts presented in accordance with the terms of the underlying credit documents. The Company also provides overdraft protection to certain demand deposit customers that represent an unfunded commitment. Overdraft protection commitments, which are included with other commitments below, are uncollateralized and are paid at the Company's discretion. Conditional commitments generally include standby and commercial letters of credit. Standby letters of credit represent an obligation of the Company to a designated third party contingent upon the failure of a customer of the Company to perform under the terms of the underlying contract between the customer and the third party. Commercial letters of credit are issued specifically to facilitate trade or commerce. Under the terms of a commercial letter of credit, drafts will be drawn when the underlying transaction is consummated, as intended, between the customer and a third party. The funded portion of these financial instruments is reflected in the Company's balance sheet, while the unfunded portion of these commitments is not reflected in the balance sheet. The table below presents a summary of the contractual obligations of the Company resulting from significant commitments:

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(in thousands)	**June 30, 2006**	December 31, 2005
Commitments to extend credit:		
Home equity lines	**$ 144,671**	$ 148,259
Credit card lines	**37,259**	39,646
Commercial real estate	**60,063**	65,966
Other commitments	**137,006**	145,535
Standby letters of credit	**8,769**	7,250
Commercial letters of credit	**525**	312

Loan commitments and standby and commercial letters of credit have credit risks essentially the same as that involved in extending loans to customers and are subject to the Company's standard credit policies. Collateral is obtained based on management's credit assessment of the customer. Management does not anticipate any material losses as a result of these commitments.

Note H - Total Comprehensive Income

The following table sets forth the computation of total comprehensive income:

	Six months ended June 30,	
(in thousands)	**2006**	2005
Net income	**$ 26,627**	$ 24,027
Unrealized security losses arising during the period	**(6,518)**	(3,497)
Reclassification adjustment for gains included in income	**-**	20
	(6,518)	(3,477)
Unrealized loss on interest rate floors	**(1,687)**	(173)
Other comprehensive income before income taxes	**(8,205)**	(3,650)
Tax effect	**3,282**	1,460
Total comprehensive income	**$ 21,704**	$ 21,837

Note I - Earnings per Share

The following table sets forth the computation of basic and diluted earnings per share:

	Three months ended June 30,		Six months ended June 30,	
(in thousands, except per share data)	**2006**	2005	**2006**	2005
Net income	**$ 13,761**	**$** 12,349	**$ 26,627**	**$** 24,027
Average shares outstanding	**17,719**	17,268	**17,860**	16,938
Effect of dilutive securities:				
Employee stock options	**53**	209	**57**	208

Shares for diluted earnings per share		**17,772**		17,477		**17,917**		17,146
Basic earnings per share	**$**	**0.78**	**$**	0.72	**$**	**1.49**	$	1.42
Diluted earnings per share	**$**	**0.77**	**$**	0.71	**$**	**1.49**	$	1.40

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Options to purchase 43,750 shares of common stock at exercise prices between $36.25 and $36.90 and 90,000 shares of common stock at exercise prices between $32.89 and $33.90 per share were outstanding during the second quarter of 2006 and 2005, respectively, but were not included in the computation of diluted earnings per share because the options' exercise price was greater than the average market price of the common shares and therefore, the effect would have been anti-dilutive.

Note J - Acquisitions

On May 20, 2005, City completed the acquisition of Classic Bancshares ("Classic") and the merger of Classic's subsidiary, Classic Bank, into City National Bank. City and Classic had entered into a definitive agreement and plan of merger on December 29, 2004. Classic operated 10 full-service branches located in Eastern Kentucky and Southeastern Ohio. The primary reason for the merger with Classic was for City to expand its presence in the Huntington/Ashland WV-KY-OH Metropolitan Statistical Area ("MSA"). With the acquisition of Classic, City is now the largest commercial banking franchise in the Huntington/Ashland WV-KY-OH MSA. On May 20, 2005, Classic had total assets of $338 million, net loans of $254 million, deposits of $252 million, and $38 million of shareholders' equity. The acquisition was accounted for using the purchase accounting method and the results of operations of Classic are included in City's consolidated statement of income from the date of acquisition forward.

Pro forma information regarding the acquisition has not been presented as the acquisition is not deemed to be significant, and pro forma results assuming that the acquisition had occurred at the beginning of 2005 would not be materially different than the results reported herein.

Note K - Recent Accounting Pronouncements

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes--an interpretation of FASB Statement No. 109 (FIN 48), which clarifies the accounting and disclosure for uncertain in tax positions, as defined. FIN 48 requires that a tax position meet a "probable recognition threshold" for the benefit of the uncertain tax position to be recognized in the financial statements. A tax position that fails to meet the probable recognition threshold will result in either reduction of a current or deferred tax asset or receivable, or recording a current or deferred tax liability. FIN 48 also provides guidance on measurement, derecognition of tax benefits, classification, interim period accounting disclosure, and transition requirements in accounting for uncertain tax positions. This interpretation is effective for fiscal years beginning after December 15, 2006. The Company is assessing the impact of adopting the new pronouncement and is currently unable to estimate its impact, if any, on the Company's consolidated financial statements.

Note L - Subsequent Event

On August 3, 2006, the Company entered into a definitive agreement to sell its credit card portfolio of approximately $11.5 million to Elan Financial Services (Elan), a wholly owned subsidiary of U.S. Bancorp. As part of this agreement, the Company and Elan have entered into an agent marketing agreement that will enable the Company's customers to continue to receive credit card products, while allowing Elan the exclusive marketing rights to the Company's current and prospective customer base. This transaction is expected to be completed by December 31, 2006, subject to closing conditions, and is expected to result in an estimated pre-tax gain in excess of $3.4 million for the Company.

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

Critical Accounting Policies

The accounting policies of the Company conform with U.S. generally accepted accounting principles and require management to make estimates and develop assumptions that affect the amounts reported in the financial statements and related footnotes. These estimates and assumptions are based on information available to management as of the date of the financial statements. Actual results could differ from management's estimates. As this information changes, management's estimates and assumptions used to prepare the Company's financial statements and related disclosures may also change. The most significant accounting policies followed by the Company are presented in Note One to the audited financial statements included in the Company's 2005 Annual Report to Stockholders. The information included in this Quarterly Report on Form 10-Q, including the Consolidated Financial Statements, Notes to Consolidated Financial Statements, and Management's Discussion and Analysis of Financial Condition and Results of Operations, should be read in conjunction with the financial statements and notes thereto included in the 2005 Annual Report of the Company. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, management has identified the determination of the allowance for loan losses, income taxes, and previously securitized loans to be the accounting areas that require the most subjective or complex judgments and, as such, could be most subject to revision as new information becomes available.

Pages 24-28 of this Quarterly Report on Form 10-Q provide management's analysis of the Company's allowance for loan losses and related provision. The allowance for loan losses is maintained at a level that represents management's best estimate of probable losses in the loan portfolio. Management's determination of the adequacy of the allowance for loan losses is based upon an evaluation of individual credits in the loan portfolio, historical loan loss experience, current economic conditions, and other relevant factors. This determination is inherently subjective as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change. The allowance for loan losses related to loans considered to be impaired is generally evaluated based on the discounted cash flows using the impaired loan's initial effective interest rate or the fair value of the collateral for certain collateral dependent loans.

The Company is subject to federal and state income taxes in the jurisdictions in which it conducts business. In computing the provision for income taxes, management must make judgments regarding interpretation of laws in those jurisdictions. Because the application of tax laws and regulations for many types of transactions is susceptible to varying interpretations, amounts reported in the financial statements could be changed at a later date upon final determinations by taxing authorities. On a quarterly basis, the Company estimates its annual effective tax rate for the year and uses that rate to provide for income taxes on a year-to-date basis.

Note B, beginning on page 9 of this Quarterly Report on Form 10-Q, and pages 28 and 29 provide management's analysis of the Company's previously securitized loans. Amounts reported in the Consolidated Balance Sheets as "previously securitized loans" represent the carrying value of loans beneficially owned by the Company as a result of having fully redeemed the obligations owed to investors ("Notes") in certain of the Company's securitization transactions. The carrying value of previously securitized loans is determined using assumptions with regard to loan prepayment and default rates. Using cash flow modeling techniques that incorporate these assumptions, the Company estimated total future cash collections expected to be received from these loans and determined the yield at which the resulting discount would be accreted into income. If, upon periodic evaluation, the estimate of the total probable collections is increased or decreased but is still greater than the sum of the original carrying amount less subsequent collections plus the discount accreted to date, and it is probable that collection will occur, the amount of the discount to be accreted is adjusted accordingly and the amount of periodic accretion is adjusted over the remaining lives of the loans. If, upon periodic evaluation, the discounted present value of estimated future cash flows declines below the recorded value of previously securitized loans, an impairment charge would be provided through the Company's provision for loan losses. Please refer to Note B of Notes to Consolidated Financial Statements, on pages 9 - 10 for further discussion of SOP 03-3.

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Financial Summary

Six Months Ended June 30, 2006 vs. 2005

The Company reported consolidated net income of $26.6 million, or $1.49 per diluted common share, for the six months ended June 30, 2006, compared to $24.0 million, or $1.40 per diluted common share for the six months ended June 30, 2005. Return on average assets ("ROA") was 2.12% and return on average equity ("ROE") was 18.1% for the first six months of 2006, compared to 2.10% and 20.3%, respectively, for the first six months of 2005.

Net interest income increased $5.9 million from $45.9 million for the six months ended June 30, 2005, to $51.8 million for the six months ended June 30, 2006 (see *Net Interest Income*). For the first six months of 2006, the Company has recorded a provision for loan losses of $1.7 million, while no provision for loan losses was recorded for the first six months of 2005 (see *Allowance and Provision for Loan Losses*). Primarily on the strength of increased service charge revenues, ($2.6 million or 14.5%), non-interest income increased $2.3 million from the six months ended June 30, 2005 to the six months ended June 30, 2006. Non-interest expenses increased $2.2 million primarily due to the acquisition of Classic, which was completed during the second quarter of 2005.

Three Months Ended June 30, 2006 vs. 2005

The Company reported consolidated net income of $13.8 million, or $0.77 per diluted common share, for the three months ended June 30, 2006, compared to $12.3 million, or $0.71 per diluted common share, for the second quarter of 2005. Return on average assets ("ROA") was 2.17% and return on average equity ("ROE") was 18.8% for the second quarter of 2006, compared to 2.09% and 19.8%, respectively, for the second quarter of 2005.

The Company's net interest income for the second quarter of 2006 increased $2.3 million compared to the second quarter of 2005 (see *Net Interest Income*). The Company recorded a provision for loan losses of $0.7 million for the second quarter of 2006 while no provision for loan losses was recorded for the second quarter of 2005 (see *Allowance and Provision for Loan Losses*). As further discussed under the caption Non-Interest Income and Expense, non-interest income increased $1.4 million from the quarter ended June 30, 2005, to the quarter ended June 30, 2006. This increase was primarily due to an increase of $1.2 million, or 12.6%, in service charge revenues. Non-interest expenses increased $0.8 million principally due to the acquisition of Classic, which was completed during the second quarter of 2005.

Net Interest Income

Six Months Ended June 30, 2006 vs. 2005

On a tax equivalent basis, net interest income increased $5.9 million, or 12.8%, from $46.4 million in the first six months of 2005 to $52.3 million in the first six months of 2006. This increase was primarily due to a widening of the Company's net interest margin that increased net interest income by $4.4 million from the first six months of 2005. Interest income from the Company's loan portfolio excluding Previously Securitized Loans increased $7.1 million from the second quarter of 2005 as the yield on these loans increased 88 basis points. In addition to benefiting from increased yields on loans, the Company has also been able to increase the average balances of its traditional loan portfolio (residential real estate, home equity, commercial and consumer loans) due to both internal growth and the acquisition of Classic during the second quarter of 2005. The increase in average balances of $236 million, or 17.3%, from the first six months of 2005 increased interest income associated with these loans by $6.9 million.

These increases were partially offset by increased interest expenses associated with higher rates paid on interest-bearing deposit accounts and increased balances of interest-bearing deposits. As a result of an increase of 67 basis points in the rate paid on interest-bearing deposits, interest expense increased $4.7 million from the first six months ended June 30, 2005. In addition, as a result of an increase in the average balances of interest-bearing deposits of $211 million, or 15.2%, interest expense increased $2.6 million from the first six months of 2005. The increase in the average balance of interest-bearing deposits from the six months ended June 30, 2005 is attributable to the Classic acquisition and internal growth.

In addition to increased deposit interest expense, the Company's increase in interest income was also partially offset by a decrease in interest income from Previously Securitized Loans of $0.7 million from the six months ended June 30, 2005. This decrease is due to a decrease in the average balances of these loans of $24.2 million, or 48.2%, from $50.2 million for the six months ended June 30, 2005 to $26.0 million for the six months ended June 30, 2006. As a result of this decrease, interest income from Previously Securitized Loans decreased $2.9 million from the six months ended

June 30, 2005. This reduction was partially mitigated by an increase in the yield on these assets from 23.75% for the first six months of 2005 to 40.41% for the first six months of 2006 (see *Previously Securitized Loans*).

The net interest margin for the first six months of 2006 of 4.64% represented a 20 basis point increase from the first six months of 2005's net interest margin of 4.44%. In order to offset the decreasing balances of high yielding previously securitized loans and resultant lower levels of interest income from these assets, the Company positioned its balance sheet to benefit from rising interest rates by emphasizing variable rate loan products. Excluding the impact of previously securitized loans and the Classic acquisition, the Company's net interest margin increased 33 basis points, or $3.2 million, for the six months ended June 30, 2005 when compared to the six months ended June 30, 2006.

Three Months Ended June 30, 2006 vs. 2005

The Company's tax equivalent net interest income increased $2.3 million, or 9.7%, from $23.9 million during the second quarter of 2005 to $26.2 million during the second quarter of 2006. This increase was primarily attributable to a widening of the Company's net interest margin, which increased net interest income by $2.1 million from the second quarter of 2005. The increase was due primarily to an increase of 89 basis points in the Company's traditional loan portfolio (residential real estate, home equity, commercial, and installment loans). As a result, interest income from the Company's traditional loan portfolio increased $3.7 million from the second quarter of 2005. Also contributing to increased interest income was growth in the Company's traditional loan portfolio due to internal growth and the acquisition of Classic Bancshares, Inc. during the second quarter of 2005. As a result of this growth of $178 million, or 12.5%, in the average balances of traditional loan products, interest income from these loans increased $2.5 million.

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These increases were partially offset by increased interest expense associated with higher rates paid on interest-bearing deposits and increased balances of interest-bearing deposits. Interest expense increased $2.7 million due to a 75 basis point increase in the rate paid on interest-bearing deposits from the second quarter of 2005. Meanwhile, increased average balances of deposits of $190 million, or 13.2%, from the second quarter of 2005 were due to internal growth and the acquisition of Classic during the second quarter of 2005. Growth in average balances of deposits increased interest expense by $1.2 million.

Interest income from previously securitized loans decreased $0.3 million from the second quarter of 2005. This decrease was related to a decrease in the average balance of the loans from $45.6 million for the quarter ended June 30, 2005, to $24.0 million for the quarter ended June 30, 2006. However, this reduction was partially mitigated as the yield on these loans rose from 24.95% from the second quarter of 2005 to 41.92% for the second quarter of 2006 (see *Previously Securitized Loans*).

The net interest margin for the second quarter of 2006 of 4.58% represented a 16 basis point increase from the second quarter of 2005's net interest margin of 4.42%. In order to offset the decreasing balances of high yielding previously securitized loans and resultant lower levels of interest income from these assets, the Company positioned its balance sheet to benefit from rising interest rates by emphasizing variable rate loan products. Excluding the impact of previously securitized loans, the Company's net interest margin increased 27 basis points, or $1.6 million, when comparing the quarter ended June 30, 2006 to the quarter ended June 30, 2005.

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Table One
Average Balance Sheets and Net Interest Income
(in thousands)

	Six months ended June 30,					
	2006			2005		
	Average Balance	**Interest**	**Yield/ Rate**	Average Balance	Interest	Yield/ Rate
Assets						
Loan portfolio (1):						
Residential real estate	**$ 594,954**	**$ 16,864**	**5.72%**	$ 494,968	$ 13,809	5.63%
Home equity	**305,787**	**11,556**	**7.62**	305,410	8,876	5.86
Commercial financial and agriculture	**643,420**	**23,385**	**7.33**	511,674	15,241	6.01
Installment loans to individuals	**52,691**	**2,993**	**11.52**	49,249	2,870	11.75
Previously securitized loans	**26,037**	**5,217**	**40.41**	50,230	5,917	23.75
Total loans	**1,622,889**	**60,015**	**7.46**	1,411,531	46,713	6.67
Securities:						
Taxable	**576,640**	**14,748**	**5.16**	651,275	15,328	4.75
Tax-exempt (2)	**43,843**	**1,418**	**6.52**	39,269	1,357	6.97
Total securities	**620,483**	**16,166**	**5.25**	690,544	16,685	4.87
Loans held for sale	**3,218**	**200**	**12.53**	-	-	-
Deposits in depository institutions	**24,490**	**566**	**4.66**	4,391	42	1.93
Federal funds sold	**-**	**-**	**-**	290	4	2.78
Total interest-earning assets	**2,271,080**	**76,947**	**6.83**	2,106,756	63,444	6.07
Cash and due from banks	**51,726**			41,063		
Bank premises and equipment	**42,575**			36,229		
Other assets	**169,162**			123,538		
Less: allowance for loan losses	**(16,881)**			(17,485)		
Total assets	**$ 2,517,662**			$ 2,290,101		
Liabilities						
Interest-bearing demand deposits	**$ 441,474**	**$ 2,588**	**1.18%**	$ 421,005	$ 1,561	0.75%
Savings deposits	**312,542**	**1,658**	**1.07**	284,281	823	0.58
Time deposits	**848,306**	**15,474**	**3.68**	685,619	10,089	2.97
Short-term borrowings	**156,431**	**2,452**	**3.16**	151,158	1,364	1.82
Long-term debt	**93,773**	**2,499**	**5.37**	151,796	3,247	4.31
Total interest-bearing liabilities	**1,852,526**	**24,671**	**2.69**	1,693,859	17,084	2.03
Noninterest-bearing demand deposits	**342,298**			331,046		
Other liabilities	**28,544**			28,522		

Stockholders' equity	**294,294**			236,674		
Total liabilities and stockholders' equity	**$ 2,517,662**			$ 2,290,101		
Net interest income		**$ 52,276**			$ 46,360	
Net yield on earning assets			**4.64%**			4.44%

(1) For purposes of this table, non-accruing loans have been included in average balances and loan fees, which are immaterial, have been included in interest income.

(2) Computed on a fully federal tax-equivalent basis assuming a tax rate of approximately 35%.

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Table Two
Rate Volume Analysis of Changes in Interest Income and Interest Expense
(in thousands)

	Six months ended June 30, 2006 vs. 2005 Increase (Decrease) Due to Change In:		
	Volume	Rate	Net
Interest-earning assets:			
Loan portfolio			
Residential real estate	$ 2,789	$ 266	$ 3,055
Home equity	11	2,669	2,680
Commercial, financial, and agriculture	3,924	4,220	8,144
Installment loans to individuals	201	(78)	123
Previously securitized loans	(2,850)	2,150	(700)
Total loans	4,075	9,227	13,302
Securities:			
Taxable	(1,757)	1,177	(580)
Tax-exempt (1)	158	(97)	61
Total securities	(1,599)	1,080	(519)
Loans held for sale	200	-	200
Deposits in depository institutions	192	332	524
Federal funds sold	(4)	-	(4)
Total interest-earning assets	$ 2,864	$ 10,639	$ 13,503
Interest-bearing liabilities:			
Demand deposits	$ 76	$ 951	$ 1,027
Savings deposits	82	753	835
Time deposits	2,394	2,991	5,385
Short-term borrowings	48	1,040	1,088
Long-term debt	(1,241)	493	(748)
Total interest-bearing liabilities	$ 1,359	$ 6,228	$ 7,587
Net Interest Income	$ 1,505	$ 4,411	$ 5,916

(1) Fully federal taxable equivalent using a tax rate of 35%.

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Table Three
Average Balance Sheets and Net Interest Income
(in thousands)

	Three months ended June 30,					
	2006			2005		
	Average Balance	**Interest**	**Yield/ Rate**	Average Balance	Interest	Yield/ Rate
Assets						
Loan portfolio (3):						
Residential real estate	**$ 596,758**	**$ 8,484**	**5.70%**	$ 523,607	$ 7,290	5.58%
Home equity	**309,270**	**5,962**	**7.73**	304,475	4,602	6.06
Commercial financial and agriculture	**651,501**	**12,092**	**7.44**	545,511	8,258	6.07
Installment loans to individuals	**48,880**	**1,400**	**11.49**	54,704	1,537	11.27
Previously securitized loans	**24,045**	**2,513**	**41.92**	45,583	2,836	24.95
Total loans	**1,630,454**	**30,451**	**7.49**	1,473,880	24,523	6.67
Securities:						
Taxable	**579,058**	**7,489**	**5.19**	645,375	7,682	4.77
Tax-exempt (4)	**43,388**	**700**	**6.47**	41,209	688	6.70
Total securities	**622,446**	**8,189**	**5.28**	686,584	8,370	4.89
Loans held for sale	**6,400**	**200**	**12.53**	-	-	-
Deposits in depository institutions	**33,986**	**416**	**4.91**	5,061	24	1.90
Total interest-earning assets	**2,293,286**	**39,256**	**6.87**	2,165,525	32,917	6.10
Cash and due from banks	**50,217**			38,292		
Bank premises and equipment	**42,621**			38,104		
Other assets	**170,273**			140,301		
Less: allowance for loan losses	**(16,911)**			(17,489)		
Total assets	**$ 2,539,486**			$ 2,364,733		
Liabilities						
Interest-bearing demand deposits	**$ 438,851**	**$ 1,329**	**1.21%**	$ 428,700	$ 845	0.79%
Savings deposits	**318,702**	**926**	**1.17**	291,368	468	0.64
Time deposits	**865,554**	**8,265**	**3.83**	713,383	5,292	2.98
Short-term borrowings	**161,082**	**1,326**	**3.30**	158,170	787	2.00
Long-term debt	**92,267**	**1,239**	**5.39**	154,723	1,662	4.31
Total interest-bearing liabilities	**1,876,456**	**13,085**	**2.80**	1,746,344	9,054	2.08
Noninterest-bearing demand deposits	**342,115**			340,340		
Other liabilities	**28,526**			28,098		
Stockholders' equity	**292,389**			249,951		

Total liabilities and stockholders' equity	**$ 2,539,486**			$ 2,364,733		
Net interest income		**$ 26,171**			$ 23,863	
Net yield on earning assets			**4.58%**			4.42%

(3) For purposes of this table, non-accruing loans have been included in average balances and loan fees, which are immaterial, have been included in interest income.

(4) Computed on a fully federal tax-equivalent basis assuming a tax rate of approximately 35%.

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Table Four
Rate Volume Analysis of Changes in Interest Income and Interest Expense
(in thousands)

	Three months ended June 30, 2006 vs. 2005 Increase (Decrease) Due to Change In:		
	Volume	Rate	Net
Interest-earning assets:			
Loan portfolio			
Residential real estate	$ 1,018	$ 176	$ 1,194
Home equity	72	1,288	1,360
Commercial, financial, and agriculture	1,604	2,230	3,834
Installment loans to individuals	(164)	27	(137)
Previously securitized loans	(1,340)	1,017	(323)
Total loans	1,190	4,738	5,928
Securities:			
Taxable	(789)	596	(193)
Tax-exempt (1)	36	(24)	12
Total securities	(753)	572	(181)
Loans held for sale	200	-	200
Deposits in depository institutions	137	255	392
Total interest-earning assets	$ 774	$ 5,565	$ 6,339
Interest-bearing liabilities:			
Demand deposits	$ 20	$ 464	$ 484
Savings deposits	44	414	458
Time deposits	1,129	1,844	2,973
Short-term borrowings	14	525	539
Long-term debt	(671)	248	(423)
Total interest-bearing liabilities	$ 536	$ 3,495	$ 4,031
Net Interest Income	$ 238	$ 2,070	$ 2,308

(1) Fully federal taxable equivalent using a tax rate of 35%.

Allowance and Provision for Loan Losses

Management systematically monitors the loan portfolio and the adequacy of the allowance for loan losses (“ALLL”) on a quarterly basis to provide for probable losses inherent in the portfolio. Management assesses the risk in each loan type based on historical trends, the general economic environment of its local markets, individual loan performance, and other relevant factors. Individual credits are selected throughout the year for detailed loan reviews, which are utilized by management to assess the risk in the portfolio and the adequacy of the allowance. Due to the nature of commercial lending, evaluation of the adequacy of the allowance as it relates to these loan types is often based more upon specific credit review, with consideration given to the potential impairment of certain credits and historical loss percentages, adjusted for general economic conditions and other inherent risk factors. Conversely, due to the homogeneous nature of the real estate and installment portfolios, the portions of the allowance allocated to those portfolios are primarily based on prior loss history of each portfolio, adjusted for general economic conditions and other inherent risk factors.

In evaluating the adequacy of the allowance for loan losses, management considers both quantitative and qualitative factors. Quantitative factors include actual repayment characteristics and loan performance, cash flow analyses, and estimated fair values of underlying collateral. Qualitative factors generally include overall trends within the portfolio, composition of the portfolio, changes in pricing or underwriting, seasoning of the portfolio, and general economic conditions.

The allowance not specifically allocated to individual credits is generally determined by analyzing potential exposure and other qualitative factors that could negatively impact the adequacy of the allowance. Loans not individually evaluated for impairment are grouped by pools with similar risk characteristics and the related historical loss percentages are adjusted to reflect current inherent risk factors, such as unemployment, overall economic conditions, concentrations of credit, loan growth, classified and impaired loan trends, staffing, adherence to lending policies, and loss trends.

Determination of the allowance for loan losses is subjective in nature and requires management to periodically reassess the validity of its assumptions. Differences between actual losses and estimated losses are assessed such that management can timely modify its evaluation model to ensure that adequate provision has been made for risk in the total loan portfolio.

As a result of the Company's quarterly analysis of the adequacy of the ALLL, the Company recorded a provision for loan losses of $0.7 million in the second quarter of 2006. The decrease in the provision for loan losses from $1.0 million in the first quarter of 2006 was due to recent improvements within the Company's consumer and home equity portfolios. Changes in the amount of the provision and related allowance are based upon City's detailed methodology and are directionally consistent with changes in quality of the Company's loan portfolio.

The Company had net charge-offs of $0.9 million for the second quarter of 2006, with overdraft depository accounts representing $0.6 million of this total. While charge-offs on overdrafts of depository accounts are appropriately taken against the ALLL, the revenue associated with overdraft of depository accounts is reflected in service charges and has been steadily growing as the core base of checking accounts has grown. Net charge-offs on real estate loans and installment loans were $0.2 million and $0.1 million, respectively, while commercial loans experienced no net charge-offs for the quarter ended June 30, 2006.

Due to a number of strategic initiatives to strengthen the loan portfolio implemented by management in recent years, including tightening credit standards, changing the overall mix of the portfolio to include a higher proportion of real estate secured loans, and identifying and charging off or resolving problem loans, the quality of the Company's loan portfolio remains solid. At June 30, 2006, non-performing assets as a percentage of loans and other real estate owned were 0.25%. Average non-performing assets as a percentage of loans and other real estate owned for the Company's peer group (bank holding companies with total assets between $1 billion and $5 billion) for the most recently reported quarter ended March 31, 2006, was 0.71%. Another contributing factor that has enabled the Company to maintain its allowance at lower levels than peers is the composition of the Company's loan portfolio, which is weighted more toward residential mortgage loans and less toward non-real estate secured commercial loans than its' peers. As a result, the Company's ALLL as a percentage of loans outstanding is 0.93% (1.00% including loans held for sale) at June 30, 2006, compared to the average of the Company's peer group of 1.20% for the most recently reported quarter. The Company believes its methodology for determining the adequacy of its ALLL adequately provides for probable losses inherent in the loan portfolio and produces a provision for loan losses that is directionally consistent with changes in asset quality and loss experience.

The allowance allocated to the commercial loan portfolio (see Table Seven) decreased $0.1 million, or 1.1%, from $7.6 million at December 31, 2005 to $7.5 million at June 30, 2006. This decline was primarily related to two commercial loans that repaid/reduced during the six months ended June 30, 2006, which was partially offset by increases in commercial balances. From the quarter ended December 31, 2005 to the quarter ended June 30, 2006, average balances of commercial loans have increased $25.2 million, or 4.0%.

The allowance allocated to the residential real estate portfolio (see Table Seven) increased $0.1 million, or 2.7%, from $4.0 million at December 31, 2005 to $4.1 million at June 30, 2006. Increases in the average balances of the residential real estate portfolio (0.7% from the quarter ended December 31, 2005) have been essentially offset by improvements in the asset quality of this portfolio.

The allowance allocated to the consumer loan portfolio (see Table Seven) decreased $1.6 million, or 58.1%, from $2.8 million at December 31, 2005 to $1.2 million at June 30, 2006. The decrease was primarily attributable to the allowance related to loans reclassified to loans held for sale during the second quarter of 2006. Excluding this reduction, the allowance allocated to the consumer loan portfolio decreased $0.2 million from December 31, 2005. This reduction was primarily due to a continued trend of decreasing consumer loan balances. Excluding the reclassification of the credit card portfolio loans to loans held for sale, consumer loans have declined $5.0 million, or 8.2%, from December 31, 2005 to June 30, 2006. Increased net charge-offs and increases in other inherent risk factors in this portfolio have partially offset this decrease.

The allowance allocated to overdraft deposit accounts (see Table Seven) increased $0.1 million, or 3.7%, from $2.4 million at December 31, 2005 to $2.5 million at June 30, 2006. This increase was attributable to a slight increase in the balances of overdraft deposit accounts from December 31, 2005.

As previously discussed, the carrying value of the previously securitized loans incorporates an assumption for expected cash flows to be received over the life of these loans. To the extent that the present value of expected cash flows is less than the carrying value of these loans, the Company would provide for such losses through the provision for loan losses.

Based on the Company’s analysis of the adequacy of the allowance for loan losses and in consideration of the known factors utilized in computing the allowance, management believes that the allowance for loan losses as of June 30, 2006, is adequate to provide for probable losses inherent in the Company’s loan portfolio. Future provisions for loan losses will be dependent upon trends in loan balances including the composition of the loan portfolio, changes in loan quality and loss experience trends, and potential recoveries of previously charged-off loans, among other factors. The Company believes that its methodology for determining its allowance for loan losses adequately provides for probable losses inherent in the loan portfolio at June 30, 2006.

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Table Five
Analysis of the Allowance for Loan Losses

(in thousands)	Six months ended June 30, **2006**	2005	Year ended December 31, 2005
Balance at beginning of period	**$ 16,790**	$ 17,815	$ 17,815
Allowance from acquisition	**-**	3,265	3,265
Reduction of allowance for loans held for sale	**(1,368)**	-	-
Charge-offs:			
Commercial, financial, and agricultural	**(228)**	(1,092)	(1,673)
Real estate-mortgage	**(528)**	(981)	(1,491)
Installment loans to individuals	**(607)**	(571)	(1,711)
Overdraft deposit accounts	**(1,913)**	(1,576)	(3,584)
Total charge-offs	**(3,276)**	(4,220)	(8,459)
Recoveries:			
Commercial, financial, and agricultural	**65**	440	605
Real estate-mortgage	**161**	62	303
Installment loans to individuals	**349**	380	679
Overdraft deposit accounts	**872**	556	1,182
Total recoveries	**1,447**	1,438	2,769
Net charge-offs	**(1,829)**	(2,782)	(5,690)
Provision for loan losses	**1,675**	-	1,400
Balance at end of period	**$ 15,268**	$ 18,298	$ 16,790
As a Percent of Average Total Loans:			
Net charge-offs (annualized)	**(0.22)%**	(0.39)%	(0.38)%
Provision for loan losses (annualized)	**0.21%**	-	0.09%
As a Percent of Non-Performing Loans:			
Allowance for loan losses	**408.02%**	463.95%	401.96%

Table Six
Non-Performing Assets

(in thousands)	As of June 30, **2006**	2005	As of December 31, 2005

Non-accrual loans	**$**	**3,046**	$	2,709	$	2,785
Accruing loans past due 90 days or more		**573**		936		1,124
Previously securitized loans past due 90 days or more		**123**		299		268
Total non-performing loans		**3,742**		3,944		4,177
Other real estate, excluding property associated with previously securitized loans		**294**		471		135
Other real estate, associated with previously securitized loans		**92**		-		-
Total other real estate owned		**386**		471		135
Total non-performing assets	**$**	**4,128**	$	4,415	$	4,312

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Table Seven
Allocation of the Allowance For Loan Losses

(in thousands)	As of June 30, **2006**	2005	As of December 31, 2005
Commercial, financial and agricultural	**$ 7,533**	$ 8,845	$ 7,613
Real estate - mortgage	**4,084**	4,724	3,977
Installment loans to individuals	**1,182**	2,859	2,819
Overdraft deposit accounts	**2,469**	1,870	2,381
Allowance for Loan Losses	**$ 15,268**	$ 18,298	$ 16,790

Previously Securitized Loans
Between 1997 and 1999, the Company originated and securitized $760 million in 125% loan to junior-lien underlying mortgages in six separate pools. The Company had a retained interest in the securitizations. Principal amounts owed to investors in the securitizations were evidenced by securities ("Notes"). The Notes were subject to redemption, in whole but not in part, at the option of the Company, as owner of the retained interests, or at the option of the Note insurer, on or after the date on which the related Note balance had declined to 5% or less of the original Note balance. Once the Notes were redeemed, the Company became the beneficial owner of the mortgage loans and recorded the loans as assets of the Company within the loan portfolio. During 2004 and 2003, the Notes outstanding on each of the Company's six securitizations declined below the 5% threshold and the Company exercised its redemption option on each of those securitizations.

As the Company redeemed the outstanding Notes, no gain or loss was recognized in the Company's financial statements and the remaining mortgage loans were recorded in the Company's loan portfolio, as "previously securitized loans," at the lower of carrying value or fair value. Because the carrying value of the mortgage loans incorporated assumptions for expected prepayment and default rates, the carrying value of the loans was generally less than the actual outstanding contractual balance of the loans. As of June 30, 2006, the Company reported a carrying value of previously securitized loans of $22.3 million, while the actual outstanding contractual balance of these loans was $40.0 million. The Company accounts for the difference between the carrying value and the total expected cash flows of previously securitized loans as an adjustment of the yield earned on these loans over their remaining lives. The discount is accreted to income over the period during which payments are probable of collection and are reasonably estimable. The Company evaluates the collectibility of previously securitized loans in accordance with Statement of Position 03-3 (see Note B). If upon evaluation of estimated collections and collections to date, the estimated total amount of collections is reduced below the original value of the loans, the loans will be considered impaired and subject to further evaluation.

During the six months ended June 30, 2006 and for the year ending December 31, 2005, the Company has experienced net recoveries on these loans primarily due to increased collection efforts and the elimination of external servicing fees after the Company assumed servicing underlying loans. Subsequent to our assumption of the servicing of these loans, the Company has averaged net increased cash flows of approximately $0.5 million per month. While the Company does not expect to maintain recoveries at these levels, it does expect that credit losses will be more favorable than those incurred while the external servicing agent was servicing these loans due to the increased collection efforts from its internal staff. Because the previously securitized loans have been experiencing higher recoveries than previously assumed, the accretable yield has increased which has caused the yield on the previously securitized loans to increase. As a result, the yield is now estimated to be in the range of 41% and 43%, depending on defaults and prepayment rates experienced on these loans in the future.

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During the first six months of 2006 and 2005, the Company recognized $5.2 million and $5.9 million, respectively, of interest income on its previously securitized loans. Cash receipts for the three and six months ended June 30, 2006 and 2005 are summarized in the following table:

(in thousands)	Three months ended June 30, **2006**	Three months ended June 30, 2005	Six months ended June 30, **2006**	Six months ended June 30, 2005
Principal receipts	**$ 3,474**	$ 8,834	**$ 7,804**	$ 16,941
Interest income receipts	**1,440**	2,729	**3,003**	5,442
Total cash receipts	**$ 4,914**	$ 11,563	**$ 10,807**	$ 22,383

Based on current cash flow projections, the Company believes that the carrying value of previously securitized loans will approximate:

As of:	Forecasted Balance:
December 31, 2006	$18 million
December 31, 2007	14 million
December 31, 2008	10 million
December 31, 2009	8 million

Non-Interest Income and Non-Interest Expense

Six Months Ended June 30, 2006 vs. 2005

Non-Interest Income: Net of investment securities gains, non-interest income increased $2.3 million, or 9.8%, from $23.5 million for the first six months of 2005 to $25.8 million in 2006. The Company's primary source of non-interest income is derived from service charges from depository accounts. Service charges from depository accounts increased $2.6 million, or 14.5%, from $18.1 million during the six months ended June 30, 2005 to $20.7 million during the six months ended June 30, 2006. This increase is due to an increase in the utilization of services by the Company's customer base and the acquisition of Classic Bancshares, Inc. during the second quarter of 2005. The effect of this increase was partially mitigated by a $0.3 million decrease in bank-owned life insurance revenues from the settlement of an insured claim during the first six months of 2005.

Non-Interest Expense: Total non-interest expense increased $2.2 million, or 6.7%, from $32.9 million in the first six months of 2005 to $35.1 million in the first six months of 2006. This increase was primarily attributable to increased compensation expenses and other miscellaneous non-interest expenses related to the Company's acquisition of Classic Bancshares, Inc. during the second quarter of 2005 and to a $0.3 million charge related to the early redemption of some of its trust preferred securities during the six months ended June 30, 2006.

Three Months Ended June 30, 2006 vs. 2005

Non-Interest Income: Net of investment securities gains, non-interest income increased $1.4 million, or 11.4%, to $13.5 million in the second quarter of 2006 as compared to $12.1 million in the second quarter of 2005. The largest source of non-interest income is service charges from depository accounts, which increased $1.2 million, or 12.6%, from $9.7 million during the second quarter of 2005 to $10.9 million during the second quarter of 2006. This increase was due to an increase in the utilization of services by the Company's customer base.

Non-Interest Expense: Non-interest expenses increased $0.8 million from $16.8 million in the second quarter of 2005 to $17.6 million in the second quarter of 2006. The increase was primarily attributable to increased compensation expenses and other miscellaneous non-interest expenses related to the Company's acquisition of Classic Bancshares, Inc. during the second quarter of 2005.

Risk Management

Market risk is the risk of loss due to adverse changes in current and future cash flows, fair values, earnings or capital due to adverse movements in interest rates and other factors, including foreign exchange rates and commodity prices. Because the Company has no significant foreign exchange activities and holds no commodities, interest rate risk represents the primary risk factor affecting the Company's balance sheet and net interest margin. Significant changes in interest rates by the Federal Reserve could result in similar changes in LIBOR interest rates, prime rates, and other benchmark interest rates that could affect the estimated fair value of the Company's investment securities portfolio, interest paid on the Company's short-term and long-term borrowings, interest earned on the Company's loan portfolio and interest paid on its deposit accounts.

The Company's Asset and Liability Committee ("ALCO") has been delegated the responsibility of managing the Company's interest-sensitive balance sheet accounts to maximize earnings while managing interest rate risk. ALCO, comprised of various members of executive and senior management, is also responsible for establishing policies to monitor and limit the Company's exposure to interest rate risk and to manage the Company's liquidity position. ALCO satisfies its responsibilities through monthly meetings during which product pricing issues, liquidity measures and interest sensitivity positions are monitored.

In order to measure and manage its interest rate risk, the Company uses an asset/liability management and simulation software model to periodically update the interest sensitivity position of the Company's balance sheet. The model is also used to perform analyses that measure the impact on net interest income and capital as a result of various changes in the interest rate environment. Such analyses quantify the effects of various interest rate scenarios on projected net interest income.

The Company's policy objective is to avoid negative fluctuations in net income or the economic value of equity of more than 15% within a 12-month period, assuming an immediate parallel increase or decrease of 300 basis points. The Company measures the long-term risk associated with sustained increases and decreases in rates through analysis of the impact to changes in rates on the economic value of equity.

However, it is important to understand that a parallel downward shift of 300 basis points in interest rates from the current rate would result in both a 2.25% Fed Funds rate and long-term interest rates of approximately 3.00%. While it is true that short-term interest rates such as the Fed Funds rate have been at these low levels in the recent past, long-term interest rates have not reached levels as low as would be associated with this "worst-case" interest rate environment in well over 30 years. Based upon the Company's belief that the likelihood of an immediate 300 basis point decline in both long-term and short-term interest rates from current levels is remote, the Company has chosen to reflect only its risk to a decrease of 200 basis points from current rates.

The Company has entered into interest rate floors with a total notional value of $600 million at June 30, 2006, with terms of 3, 4, and 5 years to facilitate the management of its short-term interest rate risk. These derivative instruments provide the Company protection against the impact declining interest rates on future income streams from certain variable rate loans. Please refer to Note C on pages 10 - 11 for further discussion of the use and accounting for such derivative instruments.

The following table summarizes the sensitivity of the Company's net income to various interest rate scenarios. The results of the sensitivity analyses presented below differ from the results used internally by ALCO in that, in the analyses below, interest rates are assumed to have an immediate and sustained parallel shock. The Company recognizes that rates are volatile, but rarely move with immediate and parallel effects. Internally, the Company considers a variety of interest rate scenarios that are deemed to be possible while considering the level of risk it is willing to assume in "worst-case" scenarios such as shown by the following:

Immediate Basis Point Change in Interest Rates	Implied Federal Funds Rate Associated with	Estimated Increase (Decrease) in	Estimated Increase (Decrease) in

	Change in Interest Rates	Net Income Over 12 Months	Economic Value of Equity
June 30, 2006:			
+300	**8.25%**	**+5.8%**	**+0.7%**
+200	**7.25**	**+4.1**	**+1.1**
+100	**6.25**	**+1.7**	**+0.7**
-100	**4.25**	**(3.2)**	**(0.9)**
-200	**3.25**	**(6.7)**	**(1.9)**
December 31, 2005:			
+300	7.25%	+10.1%	+2.2%
+200	6.25	+8.1	+2.1
+100	5.25	+4.4	+1.4
-100	3.25	(6.7)	(3.4)
-200	2.25	(10.0)	(4.9)

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These results are highly dependent upon assumptions made by management, including, but not limited to, assumptions regarding the manner in which interest-bearing demand deposit and saving deposit accounts reprice in different interest rate scenarios, pricing behavior of competitors, prepayments of loans and deposits under alternative rate environments, and new business volumes and pricing. As a result, there can be no assurance that the results above will be achieved in the event that interest rates increase or decrease during 2006 and beyond.

Liquidity

The Company evaluates the adequacy of liquidity at both the Parent Company level and at City National. At the Parent Company level, the principal source of cash is dividends from City National. Dividends paid by City National to the Parent Company are subject to certain legal and regulatory limitations. Generally, any dividends in amounts that exceed the earnings retained by City National in the current year plus retained net profits for the preceding two years must be approved by regulatory authorities. Approval is also required if dividends declared would cause City National's regulatory capital to fall below specified minimum levels. At June 30, 2006, City National could pay dividends up to $14.5 million plus an amount equal to its net profits for the remainder of 2006, as defined by statute, up to the dividend declaration date without prior regulatory approval.

The Parent Company used cash obtained from the dividends received primarily to: (1) pay common dividends to shareholders, (2) remit interest payments on the Company's trust-preferred securities, and (3) fund repurchase of the Company's common shares.

Over the next 12 months, the Parent Company has an obligation to remit interest payments approximating $2.3 million on the junior subordinated debentures held by City Holding Capital Trust. Additionally, the Parent Company anticipates continuing the payment of dividends, which are expected to approximate $19.7 million on an annualized basis over the next 12 months based on common shareholders of record at June 30, 2006. However, interest payments on the debentures can be deferred for up to five years under certain circumstances and dividends to shareholders can, if necessary, be suspended. In addition to these anticipated cash needs, the Parent Company has operating expenses and other contractual obligations, which are estimated to require $0.5 million of additional cash over the next 12 months. As of June 30, 2006, the Parent Company reported a cash balance of $34.6 million and management believes that the Parent Company's available cash balance, together with cash dividends from City National will be adequate to satisfy its funding and cash needs over the next twelve months.

Excluding the interest and dividend payments discussed above, the Parent Company has no significant commitments or obligations in years after 2006 other than the repayment of its $25.5 million obligation under the debentures held by City Holding Capital Trust. However, this obligation does not mature until April 2028, or earlier at the option of the Parent Company. It is expected that the Parent Company will be able to obtain the necessary cash, either through dividends obtained from City National or the issuance of other debt, to fully repay the debentures at their maturity.

City National manages its liquidity position in an effort to effectively and economically satisfy the funding needs of its customers and to accommodate the scheduled repayment of borrowings. Funds are available to City National from a number of sources, including depository relationships, sales and maturities within the investment securities portfolio, and borrowings from the FHLB and other financial institutions. As of June 30, 2006, City National's assets are significantly funded by deposits and capital. However, City National maintains borrowing facilities with the FHLB and other financial institutions that are accessed as necessary to fund operations and to provide contingency funding mechanisms. As of June 30, 2006, City National has the capacity to borrow an additional $284.6 million from the FHLB and other financial institutions under existing borrowing facilities. City National maintains a contingency funding plan, incorporating these borrowing facilities, to address liquidity needs in the event of an institution-specific or systematic financial industry crisis. Additionally, City National maintains a significant percentage (90.4% or $512.5 million at June 30, 2006) of its investment securities portfolio in the highly liquid available-for-sale classification. Although it has no current intention to do so, these securities could be liquidated, if necessary, to provide an additional funding source. City National also segregates certain mortgage loans, mortgage-backed securities, and other investment securities in a separate subsidiary so that it can separately monitor the asset quality of these primarily mortgage-related assets, which could be used to raise cash through securitization transactions or obtain additional equity or debt financing if necessary.

The Company manages its asset and liability mix to balance its desire to maximize net interest income against its desire to minimize risks associated with capitalization, interest rate volatility, and liquidity. With respect to liquidity, the Company has chosen a conservative posture and believes that its liquidity position is strong. The Company's net loan to asset ratio is 64.7% as of June 30, 2006 and deposit balances fund 78.2% of total assets. The Company has obligations to extend credit, but these obligations are primarily associated with existing home equity loans that have predictable borrowing patterns across the portfolio. The Company has significant investment security balances that totaled $566.8 million at June 30, 2006, and that greatly exceeded the Company's non-deposit sources of borrowing which totaled $265.4 million. Further, the Company's deposit mix has a very high proportion of transaction and savings accounts that fund 43.3% of the Company's total assets.

As illustrated in the Consolidated Statements of Cash Flows, the Company generated $28.5 million of cash from operating activities during the first six months of 2006, primarily from interest income received on loans and investments, net of interest expense paid on deposits and borrowings. The Company used $16.9 million of cash in investing activities during the first six months of 2006 primarily for the purchase of money market and mutual fund securities, net of proceeds from these securities and from maturities and calls of securities available-for-sale. The Company used $3.2 million of cash in financing activities during the first six months of 2006, principally as a result of a decrease in noninterest bearing deposits of $30.9 million, treasury stock purchases of $20.6 million, cash dividends paid to the Company's common stockholders of $9.5 million and a decrease in short and long term debt of $15.1 million. These decreases were partially offset by an increase in interest-bearing deposits of $75.0 million.

Capital Resources

During the first six months of 2006, Shareholders' Equity decreased $8.0 million, or 2.7%, from $292.1 million at December 31, 2005 to $284.1 million at June 30, 2006. This decrease was primarily due to common stock purchases of $20.6 million, dividends declared during the first six months of 2006 of $9.9 million and a $4.9 million reduction in accumulated other comprehensive income, which was partially offset by reported net income of $26.6 million. The reduction in accumulated other comprehensive income during the six months ended June 30, 2006 was due to unrealized losses, net of taxes, on the Company's available for sale investment securities of $3.9 million and unrealized losses, net of taxes, on the Company's derivative instruments of $1.0 million.

The Company has authorization to purchase up to 1,000,000 shares of the Company's common stock in open market transactions, block transactions, private transactions, or otherwise at such times and prices as determined appropriate by management as authorized by the Company's Board of Directors in June 2005. Since the repurchase plan was adopted, the Company has purchased 777,153 shares of its common stock. There were 572,053 shares repurchased during the first six months of 2006 and there can be no assurance that the Company will continue to reacquire its common shares or to what extent the repurchase program will be successful. As of June 30, 2006, the Company may repurchase an additional 222,847 shares from time to time depending on market conditions under the authorization.

Regulatory guidelines require the Company to maintain a minimum total capital to risk-adjusted assets ratio of 8.0%, with at least one-half of capital consisting of tangible common stockholders' equity and a minimum Tier I leverage ratio of 4.0%. Similarly, City National is also required to maintain minimum capital levels as set forth by various regulatory agencies. Under capital adequacy guidelines, City National is required to maintain minimum total capital, Tier I capital, and leverage ratios of 8.0%, 4.0%, and 4.0%, respectively. To be classified as "well capitalized," City National must maintain total capital, Tier I capital, and leverage ratios of 10.0%, 6.0%, and 5.0%, respectively.

The Company's regulatory capital ratios remained strong for both City Holding and City National as illustrated in the following table:

			Actual	
	Minimum	Well-Capitalized	**June 30, 2006**	December 31, 2005
City Holding:				
Total	8.0%	10.0%	**15.5%**	16.4%
Tier I Risk-based	4.0	6.0	**14.6**	15.4
Tier I Leverage	4.0	5.0	**10.3**	11.0
City National:				
Total	8.0%	10.0%	**13.5%**	14.0%
Tier I Risk-based	4.0	6.0	**12.6**	13.0
Tier I Leverage	4.0	5.0	**8.9**	9.2

Item 3 - Quantitative and Qualitative Disclosure of Market Risk

The information called for by this item is provided under the caption "Risk Management" under Item 2—Management's Discussion and Analysis of Financial Condition and Results of Operations.

Item 4 - Controls and Procedures

Pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934, the Company carried out an evaluation, with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures (as defined under Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company required to be included in the Company's periodic SEC filings. There has been no change in the Company's internal control over financial reporting during the quarter ended June 30, 2006 that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

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PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Company is engaged in various legal actions that it deems to be in the ordinary course of business. The Company believes that it has adequately provided for probable costs of current litigation. As these legal actions are resolved, however, the Company could realize positive and/or negative impact to its financial performance in the period in which these legal actions are ultimately decided. There can be no assurance that current actions will have immaterial results, either positive or negative, or that no material actions may be presented in the future.

Item 1A. Risk Factors

There have been no material changes to the factors disclosed in Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2005.

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

The following table sets forth information regarding the Company's common stock repurchases transacted during the quarter:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs **(a)**	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
April 1 - April 30, 2006	66,156	$ 35.97	66,156	428,172
May 1 - May 31, 2006	100,625	$ 36.02	100,625	327,547
June 1 - June 30, 2006	104,700	$ 35.40	104,700	222,847

(a) In June 2005, the Company announced that the Board of Directors had authorized the Company to buy back up to 1,000,000 shares of its common stock, in open market transactions at prices that are accretive to continuing shareholders. No timetable was placed on the duration of this share repurchase program.

Item 3. Defaults Upon Senior Securities None.

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

The Company held its Annual Meeting of Shareholders on May 10, 2006 at which time shareholders were asked to consider the following five proposals, which were more fully described in the Company's definitive proxy statement on Schedule 14A filed with the Securities and Exchange Commission on March 24, 2006:

1. To elect four Class I directors to serve for a term of three years.
2. To approve an amendment to the Company's Articles of Incorporation to provide a waiver of liability of directors under certain circumstances, as permitted under the West Virginia Business Corporation Act enacted in 2002.
3. To approve an amendment to the Company's Articles of Incorporation to change the percentage of votes required to remove a director from office from 51% to two-thirds of the shares issued and outstanding.
4. To approve an amendment to the Company's Articles of Incorporation to provide that in the event that a vote brought before the Company's Board of Directors results in a tie vote, the vote of the Chairman of the Board of the Company or his duly appointed delegate (who shall also be a Director) shall be counted twice.
5. To ratify the Board of Directors' appointment of Ernst & Young LLP as independent registered public accounting firm for City Holding Company for 2006.

The vote tabulation was as follows:

1. Election of four Class I directors to the Board of Directors:

Director/Nominee	Votes For	Votes Withheld
David Hambrick	10,044,557	4,853,236
James L. Rossi	10,790,999	3,836,794
James E. Songer	10,682,411	3,945,382
Mary H. Williams	10,796,763	3,831,030

There were 4,702 broker non-votes in the election of directors.

2. Approval of an amendments to the Company's Articles of Incorporation to provide a waiver of liability of directors under certain circumstances, as permitted under the West Virginia Business Corporation Act enacted in 2002:

Votes For	Against	Abstain
13,767,519	599,789	265,186

There was one broker non-vote for this amendment.

3. Approval of an amendment to the Company's Articles of Incorporation to change the percentage of votes required to remove a director from office from 51% to two-thirds of the shares issued and outstanding:

Votes For	Against	Abstain
4,538,241	7,201,502	107,441

There were 2,785,311 broker non-votes for this amendment.

4. Approval of an amendment to the Company's Articles of Incorporation to provide that in the event of a vote brought before the Company's Board of Directors results in a tie vote, the vote of the Chairman of the Board of the Company or his duly appointed delegate (who shall also be a Director) shall be counted twice:

Votes For	Against	Abstain
9,509,967	4,832,639	289,886

There were three broker non-votes for this amendment.

5. Ratification of the Board of Directors' appointment of Ernst & Young LLP as independent registered public accounting firm for

City Holding Company for 2006.

Votes For	Against	Abstain
14,404,541	173,977	53,977

There were no broker non-votes in the ratification of independent registered public accounting firm.

Item 5. Other Information None.

Item 6. Exhibits

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(a) Exhibits

3.1	Amendment to City Holding Company Articles of Incorporation as of May 10, 2006 and filed with the West Virginia Secretary of State
31(a)	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Charles R. Hageboeck
31(b)	Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for David L. Bumgarner
32(a)	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for Charles R. Hageboeck
32(b)	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for David L. Bumgarner

SIGNATURES

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

City Holding Company
(Registrant)

/s/ Charles R. Hageboeck
Charles R. Hageboeck
President and Chief Executive Officer
(Principal Executive Officer)

/s/ David L. Bumgarner
David L. Bumgarner
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)

Date: August 7, 2006