UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2020

OR

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

For the transition period from ______ to ______

Commission File Number: 001-38895

South Plains Financial, Inc.

(Exact name of registrant as specified in its charter)

Texas	**75-2453320**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5219 City Bank Parkway **Lubbock, Texas**	**79407**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (806) 792-7101

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, $1.00 par value per share	SPFI	The Nasdaq Stock Market, LLC

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

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

Large accelerated filer	☐	Accelerated filer	☐
Non-accelerated filer	☒	Smaller reporting company	☒
		Emerging growth company	☒

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

As of May 13, 2020, the registrant had 18,059,174 shares of common stock, par value $1.00 per share, outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

SOUTH PLAINS FINANCIAL, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except per share data)

	March 31, 2020 (Unaudited)	December 31, 2019
ASSETS		
Cash and due from banks	$ 46,883	$ 56,246
Interest-bearing deposits in banks	89,179	101,853
Cash and cash equivalents	136,062	158,099
Securities available for sale	734,791	707,650
Loans held for sale	62,636	49,035
Loans held for investment	2,108,805	2,143,623
Allowance for loan losses	(29,074)	(24,197)
Accrued interest receivable	11,015	13,924
Premises and equipment, net	61,829	61,873
Bank-owned life insurance	69,756	69,397
Goodwill	19,968	18,757
Intangible assets	8,213	8,632
Other assets	32,562	30,374
Total assets	$ 3,216,563	$ 3,237,167
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest-bearing	$ 740,946	$ 790,921
Interest-bearing	1,924,902	1,905,936
Total deposits	2,665,848	2,696,857
Short-term borrowings	17,400	37,165
Accrued expenses and other liabilities	38,560	29,098
Notes payable & other borrowings	95,000	95,000
Subordinated debt securities	26,472	26,472
Junior subordinated deferrable interest debentures	46,393	46,393
Total liabilities	2,889,673	2,930,985
Stockholders' equity:		
Common stock, $1.00 par value per share, 30,000,000 shares authorized; 18,056,014 and 18,036,115 issued and outstanding at March 31, 2020 and December 31, 2019, respectively	18,056	18,036
Additional paid-in capital	140,699	140,492
Retained earnings	153,238	146,696
Accumulated other comprehensive income	14,897	958
Total stockholders' equity	326,890	306,182
Total liabilities and stockholders' equity	$ 3,216,563	$ 3,237,167

The accompanying notes are an integral part of these consolidated financial statements.

SOUTH PLAINS FINANCIAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)
(Dollars in thousands, except per share data)

	Three Months Ended March 31,	
	2020	**2019**
Interest income:		
Loans, including fees	$ 31,015	$ 28,098
Securities:		
Taxable	3,780	2,176
Non taxable	396	225
Federal funds sold and interest-bearing deposits in banks	546	1,505
Total interest income	35,737	32,004
Interest expense:		
Deposits	4,283	5,889
Notes payable & other borrowings	450	650
Subordinated debt securities	404	406
Junior subordinated deferrable interest debentures	401	513
Total interest expense	5,538	7,458
Net interest income	30,199	24,546
Provision for loan losses	6,234	608
Net interest income, after provision for loan losses	23,965	23,938
Noninterest income:		
Service charges on deposit accounts	1,983	1,905
Income from insurance activities	1,159	1,750
Net gain on sales of loans	8,540	4,660
Bank card services and interchange fees	2,238	2,010
Realized gain on sale of securities	2,318	—
Investment commissions	455	333
Fiduciary fees	829	375
Other	1,353	1,042
Total noninterest income	18,875	12,075
Noninterest expense:		
Salaries and employee benefits	20,810	19,125
Occupancy and equipment, net	3,600	3,407
Professional services	1,572	1,706
Marketing and development	768	717
IT and data services	847	693
Bank card expenses	1,052	724
Appraisal expenses	455	323
Other	4,907	3,341
Total noninterest expense	34,011	30,036
Income before income taxes	8,829	5,977
Income tax expense	1,746	1,204
Net income	$ 7,083	$ 4,773

The accompanying notes are an integral part of these consolidated financial statements.

SOUTH PLAINS FINANCIAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (CONTINUED)
(Unaudited)
(Dollars in thousands, except per share data)

	Three Months Ended March 31, 2020	Three Months Ended March 31, 2019
Earnings per share:		
Basic	$ 0.39	$ 0.32
Diluted	$ 0.38	$ 0.32
Net income	$ 7,083	$ 4,773
Other comprehensive income:		
Change in net unrealized loss on securities available for sale	21,189	2,907
Change in net losses on cash flow hedges	(1,227)	—
Reclassification adjustment for (gain) included in net income	(2,318)	—
Tax effect	(3,705)	(611)
Other comprehensive income	13,939	2,296
Comprehensive income	$ 21,022	$ 7,069

The accompanying notes are an integral part of these consolidated financial statements.

SOUTH PLAINS FINANCIAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(Unaudited)
(Dollars in thousands, except per share data)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Less: ESOP Owned Shares	Total
	Shares	Amount						
Three Months Ended March 31,								
Balance at January 1, 2019	14,771,520	$ 14,772	$ 80,412	$ 119,834	$ (2,243)	$ —	$ (58,195)	$ 154,580
Net income	—	—	—	4,773	—	—	—	4,773
Cumulative change in accounting principle	—	—	—	(1,279)	—	—	—	(1,279)
Other comprehensive (loss), (net of tax)	—	—	—	—	2,296	—	—	2,296
Balance at March 31, 2019	14,771,520	$ 14,772	$ 80,412	$ 123,328	$ 53	$ —	$ (58,195)	$ 160,370
Balance at January 1, 2020	18,036,115	$ 18,036	$ 140,492	$ 146,696	$ 958	$ —	$ —	$ 306,182
Net income	—	—	—	7,083	—	—	—	7,083
Cash dividends:								
Common - $0.03 per share	—	—	—	(541)	—	—	—	(541)
Other comprehensive income, (net of tax)	—	—	—	—	13,939	—	—	13,939
Exercise of employee stock options and vesting of restricted stock units, net of 660 shares for cashless exercise and net of 4,986 shares for taxes	19,899	20	(103)	—	—	—	—	(83)
Stock based compensation	—	—	310	—	—	—	—	310
Balance at March 31, 2020	18,056,014	$ 18,056	$ 140,699	$ 153,238	$ 14,897	$ —	$ —	$ 326,890

The accompanying notes are an integral part of these consolidated financial statements.

SOUTH PLAINS FINANCIAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in thousands)

	For the Three Months Ended March 31, 2020	2019
Cash flows from operating activities:		
Net income	$ 7,083	$ 4,773
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	6,234	608
Depreciation and amortization	1,606	1,252
Accretion and amortization	379	(308)
Other gains, net	(2,383)	(3)
Net gain on sales of loans	(8,540)	(4,660)
Proceeds from sales of loans held for sale	210,963	142,435
Loans originated for sale	(216,024)	(120,840)
Earnings on bank-owned life insurance	(359)	(327)
Stock based compensation	310	—
Net change in:		
Accrued interest receivable and other assets	(2,986)	1,371
Accrued expenses and other liabilities	8,032	5,028
Net cash from operating activities	4,315	29,329
Cash flows from investing activities:		
Activity in securities available for sale:		
Purchases	(112,358)	(5,192)
Sales	94,514	—
Maturities, prepayments, and calls	11,513	7,552
Loan originations and principal collections, net	31,937	41,201
Purchases of premises and equipment, net	(1,156)	(1,032)
Proceeds from sales of premises and equipment	83	3
Proceeds from sales of foreclosed assets	513	405
Net cash from investing activities	25,046	42,937
Cash flows from financing activities:		
Net change in deposits	(31,008)	27,475
Net change in short-term borrowings	(19,765)	1,210
Payments to tax authorities for stock-based compensation	(84)	—
Payments made on notes payable and other borrowings	—	(7,530)
Cash dividends on common stock	(541)	—
Net cash from financing activities	(51,398)	21,155
Net change in cash and cash equivalents	$ (22,037)	$ 93,421
Beginning cash and cash equivalents	158,099	245,989
Ending cash and cash equivalents	$ 136,062	$ 339,410
Supplemental disclosures of cash flow information:		
Interest paid on deposits and borrowed funds	$ 5,771	$ 7,140
Income taxes paid	—	—
Supplemental schedule of noncash investing and financing activities:		
Loans transferred to foreclosed assets	$ 574	$ 460
Business combination measurement period adjustment	1,211	—

The accompanying notes are an integral part of these consolidated financial statements.

SOUTH PLAINS FINANCIAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands except per share data)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations – South Plains Financial, Inc. (“SPFI”) is a Texas corporation and registered bank holding company that conducts its principal activities through its subsidiaries from offices located throughout Texas and Eastern New Mexico. Principal activities include commercial and retail banking, along with insurance, investment, trust, and mortgage services. The following are subsidiaries of SPFI:

Wholly Owned, Consolidated Subsidiaries:	
City Bank	Bank subsidiary
Windmark Insurance Agency, Inc. (“Windmark”)	Non-bank subsidiary
Ruidoso Retail, Inc.	Non-bank subsidiary
CB Provence, LLC	Non-bank subsidiary
CBT Brushy Creek, LLC	Non-bank subsidiary
CBT Properties, LLC	Non-bank subsidiary
Wholly Owned, Equity Method Subsidiaries:	
South Plains Financial Capital Trusts (SPFCT) III-V	Non-bank subsidiaries

Basis of Presentation and Consolidation – The consolidated financial statements in this Quarterly Report on Form 10-Q (this “Form 10-Q”) include the accounts of SPFI and its wholly owned consolidated subsidiaries (collectively referred to as the “Company”) identified above. All significant intercompany balances and transactions have been eliminated in consolidation.

The interim consolidated financial statements in this Form 10-Q have not been audited by an independent registered public accounting firm, but in the opinion of management, reflect all adjustments necessary for a fair presentation of the Company’s financial position and results of operations. All such adjustments were of a normal and recurring nature. The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q adopted by the Securities and Exchange Commission (“SEC”). Accordingly, the financial statements do not include all of the information and footnotes required by GAAP for complete financial statements and should be read in conjunction with the Company’s audited consolidated financial statements, and notes thereto in the Company’s Annual Report on Form 10-K, for the year ended December 31, 2019. Operating results for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year or any future period.

Use of Estimates – The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Determination of the adequacy of the allowance for loan losses is a material estimate that is particularly susceptible to significant change in the near term; the assumptions used in stock-based compensation, the valuation of foreclosed assets, and fair values of financial instruments can also involve significant management estimates.

Change in Capital Structure
On March 11, 2019, the Company amended and restated its Certificate of Formation. The Amended and Restated Certificate of Formation increased the number of authorized shares of common stock, par value $1.00 per share, from 1,000,000 to 30,000,000.

The Company completed a 29-to-1 stock split of the Company’s outstanding shares of common stock for shareholders of record as of March 11, 2019. The stock split was payable in the form of a dividend on or about March 11, 2019. Shareholders received 29 additional shares for each share held as of the record date. All share and per share amounts in the consolidated financial statements have been retroactively adjusted to reflect this stock split for all periods presented.

Loans – Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding principal balances net of any unearned income, charge-offs, unamortized deferred fees and costs on originated loans, and premiums or discounts on purchased loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the straight-line method, which is not materially different from the effective interest method required by GAAP.

Loans are placed on nonaccrual status when, in management’s opinion, collection of interest is unlikely, which typically occurs when principal or interest payments are more than ninety days past due. When interest accrual is discontinued, all unpaid accrued interest is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses – The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The Company's allowance for loan losses consists of specific valuation allowances established for probable losses on specific loans and general valuation allowances calculated based on historical loan loss experience for similar loans with similar characteristics and trends, judgmentally adjusted for general economic conditions and other qualitative risk factors internal and external to the Company.

The allowance for loan losses is evaluated on a quarterly basis by management and is based upon management's review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral. The bank subsidiary's loans are generally secured by specific items of collateral including real property, crops, livestock, consumer assets, and other business assets.

While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on various factors. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require the bank subsidiary to recognize additional losses based on their judgments about information available to them at the time of their examination. Because of these factors, it is reasonably possible that the estimated losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. All loans rated substandard or worse and greater than $250,000 are specifically reviewed to determine if they are impaired. Factors considered by management in determining whether a loan is impaired include payment status and the sources, amounts, and probabilities of estimated cash flow available to service debt in relation to amounts due according to contractual terms. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Loans that are determined to be impaired are then evaluated to determine estimated impairment, if any. GAAP allows impairment to be measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Loans that are not individually determined to be impaired or are not subject to the specific review of impaired status are subject to the general valuation allowance portion of the allowance for loan loss.

The Company may modify its loan agreement with a borrower. The modification will be considered a troubled debt restructuring if the following criteria are met: (1) the borrower is experiencing a financial difficulty and (2) the Company makes a concession that it would not otherwise make. Concessions may include debt forgiveness, interest rate change, or maturity extension. Each of these loans is impaired and is evaluated for impairment, with a specific reserve recorded as necessary based on probable losses related to collateral and cash flow. A loan will no longer be required to be reported as restructured in calendar years following the restructure if the interest rate at the time of restructure is greater than or equal to the rate the Company was willing to accept for a new extension of credit with similar risk and the loan is in compliance with its modified terms.

Acquired Loans – Loans that the Company acquires in connection with business combinations are recorded at fair value with no carryover of the acquired entity's related allowance for loan losses. The fair value of the acquired loans involves estimating the amount and timing of principal and interest cash flows expected to be collected on the loans and discounting those cash flows at a market rate of interest.

The excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable discount and is recognized into interest income over the remaining life of the loan. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the nonaccretable discount. These loans are accounted for under ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality.* The nonaccretable discount includes estimated future credit losses expected to be incurred over the life of the loan. Subsequent decreases to the expected cash flows will require the Company to evaluate the need for an additional allowance. Subsequent improvement in expected cash flows will result in the reversal of a corresponding amount of the nonaccretable discount which the Company will then reclassify as accretable discount that will be recognized into interest income over the remaining life of the loan.

Loans acquired through business combinations that meet the specific criteria of ASC 310-30 are individually evaluated each period to analyze expected cash flows. To the extent that the expected cash flows of a loan have decreased due to credit deterioration, the Company then establishes an allowance.

Loans acquired through business combinations that do not meet the specific criteria of ASC 310-30 are accounted for under ASC 310-20. These loans are initially recorded at fair value, and include credit and interest rate marks associated with acquisition accounting adjustments. Purchase premiums or discounts are subsequently amortized as an adjustment to yield over the estimated contractual lives of the loans. There is no allowance for loan losses established at the acquisition date for acquired performing loans. An allowance for loan losses is recorded for any credit deterioration in these loans subsequent to acquisition.

Acquired loans that met the criteria for impaired or nonaccrual of interest prior to the acquisition may be considered performing upon acquisition, regardless of whether the customer is contractually delinquent, if the Company expects to fully collect the new carrying value (i.e. fair value) of the loans. As such, the Company may no longer consider the loan to be nonaccrual or nonperforming at the date of acquisition and may accrue interest on these loans, including the impact of any accretable discount. In addition, charge-offs on such loans would be first applied to the nonaccretable difference portion of the fair value adjustment.

Goodwill and Other Intangible Assets – Goodwill resulting from business combinations is generally determined as the excess of the fair value of the consideration transferred over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill is not amortized, but is tested for impairment at least annually or more frequently if events and circumstances exist that indicate that an impairment test should be performed. Intangible assets with definite lives are amortized over their estimated useful lives.

Core deposit intangible ("CDI") is a measure of the value of checking and savings deposit relationships acquired in a business combination. The fair value of the CDI stemming from any given business combination is based on the present value of the expected cost savings attributable to the core deposit funding relative to an alternative source of funding. CDI is amortized over the estimated useful lives of the existing deposit relationships acquired, but does not exceed 10 years. Significantly all CDI is amortized using the sum of the years digits method.

The remaining other intangible assets consist of customer relationship and employment agreement intangible assets and are amortized over their estimated useful lives of 5 years.

Stock-based Compensation – The Company sponsors an equity incentive plan under which options to acquire shares of the Company's common stock may be granted periodically to all full-time employees and directors of the Company or its affiliates at a specific exercise price to acquire shares of the Company's common stock. Shares are issued out of authorized and unissued common shares that have been reserved for issuance under such plan. Compensation cost is measured based on the estimated fair value of the award at the grant date and is recognized in earnings on a straight-line basis over the requisite service period. The fair value of stock options is estimated at the date of grant using the Black-Scholes option pricing model. This model requires assumptions as to the expected stock volatility, dividends, terms and risk-free rates. The expected volatility is based on the combination of the Company's historical volatility and the volatility of comparable peer banks. The expected term represents the period of time that options are expected to be outstanding from the grant date. The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for the appropriate life of each stock option.

Recent Accounting Pronouncements – *Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC")* constitutes GAAP for nongovernmental entities. Updates to ASC are prescribed in Accounting Standards Updates ("ASU"), which are not authoritative until incorporated into ASC.

ASU 2016-02 Leases (Topic 842). The FASB amended existing guidance that requires that lessees recognize lease assets and lease liabilities on the balance sheet and disclose key information about leasing arrangements. The Company is in the process of determining the effect of the standard on its consolidated operating results and financial condition. These amendments are effective for the Company for annual periods beginning after December 15, 2021 and interim periods beginning after December 15, 2022.

ASU 2016-13 Financial Instruments - Credit Losses (Topic 326). The FASB issued guidance to replace the incurred loss model with an expected loss model, which is referred to as the current expected credit loss ("CECL") model. The CECL model is applicable to the measurement of credit losses on financial assets measured at amortized cost, including loan receivables, held to maturity securities, and debt securities. ASU 2016-13 is effective for the Company for annual periods beginning after December 15, 2022, including interim periods within those fiscal years. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company is currently evaluating the impact adoption of ASU 2016-13 will have on its consolidated operating results and financial condition.

ASU 2017-04, Intangibles - Goodwill and Other (Topic 350). This ASU simplifies the accounting for goodwill impairment for all entities by eliminating Step 2 from the current provisions. Under the new guidance, an entity should perform the goodwill impairment test by comparing the fair value of a reporting unit with its carrying value and recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value. The Company elected to early adopt ASU 2017-04 on January 1, 2020, and it did not have a significant impact on its financial statements. The Company's policy is to test goodwill for impairment annually or on an interim basis if an event triggering impairment may have occurred. During the period ended March 31, 2020, the economic disruption and uncertainty surrounding the ongoing COVID-19 pandemic and the recent volatility in the market price of crude oil resulted in a decrease in the Company's stock price. The Company believed this resulted in a triggering event requiring an interim goodwill impairment quantitative analysis. Under the new simplified guidance, the Company's estimated fair value as of March 31, 2020, exceeded its carrying amount resulting in no impairment charge for the period. Management will continue to evaluate the economic conditions at future reporting periods for applicable changes.

Subsequent Events – The Company has evaluated subsequent events and transactions from March 31, 2020 through the date of this Form 10-Q was filed with the SEC for potential recognition or disclosure as required by GAAP and determined that outside of the items noted below there were no material subsequent events requiring recognition or disclosure.

The Paycheck Protection Program (the "PPP") was created by the CARES Act and administered by the U.S. Small Business Administration (the "SBA"). The Company had closed and funded $210 million in PPP loans as of May 5, 2020. These PPP loans are fully guaranteed by the SBA and have no impact on our risk-based capital ratios. The Company also has access to the PPP Liquidity Facility (the "PPPLF") established by the Board of Governors of the Federal Reserve System (the "Federal Reserve") at a borrowing rate of 0.35%. The Company has not utilized the PPPLF.

2. SECURITIES

The amortized cost and fair value of securities, with gross unrealized gains and losses, at period-end follow:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2020				
Available for sale:				
U.S. government and agencies	$ 4,750	$ 85	$ —	$ 4,835
State and municipal	206,206	3,537	(89)	209,654
Mortgage-backed securities	361,847	14,234	—	376,081
Collateralized mortgage obligations	107,380	237	(207)	107,410
Asset-backed and other amortizing securities	34,524	2,287	—	36,811
	$ 714,707	$ 20,380	$ (296)	$ 734,791

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2019				
Available for sale:				
U.S. government and agencies	$ 4,750	$ 57	$ —	$ 4,807
State and municipal	94,512	1,091	(911)	94,692
Mortgage-backed securities	463,899	3,727	(3,110)	464,516
Collateralized mortgage obligations	107,443	15	(169)	107,289
Asset-backed and other amortizing securities	35,833	522	(9)	36,346
	$ 706,437	$ 5,412	$ (4,199)	$ 707,650

The amortized cost and fair value of securities at March 31, 2020 are presented below by contractual maturity. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Other securities are shown separately since they are not due at a single maturity date.

	Available for Sale	
	Amortized Cost	Fair Value
Within 1 year	$ 5,772	$ 5,862
After 1 year through 5 years	—	—
After 5 years through 10 years	15,730	16,150
After 10 years	189,454	192,477
Other	503,751	520,302
	$ 714,707	$ 734,791

At both March 31, 2020 and December 31, 2019, there were no holdings of securities of any one issuer, other than the U.S. government and its agencies, in an amount greater than 10% of stockholders' equity.

Securities with a carrying value of approximately $260.5 million and $211.0 million at March 31, 2020 and December 31, 2019, respectively, were pledged to collateralize public deposits and for other purposes as required or permitted by law.

The following table segregates securities with unrealized losses at the periods indicated, by the duration they have been in a loss position:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
March 31, 2020						
U.S. government and agencies	$ —	$ —	$ —	$ —	$ —	$ —
State and municipal	21,741	88	384	1	22,125	89
Mortgage-backed securities	—	—	—	—	—	—
Collateralized mortgage obligations	10,071	207	—	—	10,071	207
Asset-backed and other amortizing securities	—	—	—	—	—	—
	$ 31,812	$ 295	$ 384	$ 1	$ 32,196	$ 296
December 31, 2019						
U.S. government and agencies	$ —	$ —	$ —	$ —	$ —	$ —
State and municipal	58,389	910	387	1	58,776	911
Mortgage-backed securities	284,120	3,070	4,661	40	288,781	3,110
Collateralized mortgage obligations	60,039	169	—	—	60,039	169
Asset-backed and other amortizing securities	2,661	9	—	—	2,661	9
	$ 405,209	$ 4,158	$ 5,048	$ 41	$ 410,257	$ 4,199

There were 12 securities with an unrealized loss at March 31, 2020. Management does not believe that these losses are other than temporary as there is no intent to sell any of these securities before recovery and it is not probable that we will be required to sell any of these securities before recovery, and credit loss, if any, is not material. Any unrealized losses are largely due to increases in market interest rates over the yields available at the time the underlying securities were purchased. The fair value is expected to recover as the securities approach their maturity date or if market yields for such investments decline. Management does not believe any of the securities are impaired due to reasons of credit quality. Accordingly, as of March 31, 2020, management believes the impairments detailed in the table above are temporary and no impairment loss has been realized in the Company's consolidated financial statements.

3. LOANS

Loans are summarized by category as of the periods presented below:

	March 31, 2020	December 31, 2019
Commercial real estate	$ 641,739	$ 658,195
Commercial - specialized	303,116	309,505
Commercial - general	424,750	441,398
Consumer:		
1-4 family residential	356,540	362,796
Auto loans	212,912	215,209
Other consumer	72,162	74,000
Construction	97,586	82,520
	2,108,805	2,143,623
Allowance for loan losses	(29,074)	(24,197)
Loans, net	$ 2,079,731	$ 2,119,426

The Company has certain lending policies, underwriting standards, and procedures in place that are designed to maximize loan income with an acceptable level of risk. Management reviews and approves these policies, underwriting standards, and procedures on a regular basis and makes changes as appropriate. Management receives frequent reports related to loan originations, quality, concentrations, delinquencies, non-performing, and potential problem loans. Diversification in the loan portfolio is a means of managing risk associated with fluctuations in economic conditions, both by type of loan and geography.

Commercial – General and Specialized – Commercial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably. Underwriting standards have been designed to determine whether the borrower possesses sound business ethics and practices, evaluate current and projected cash flows to determine the ability of the borrower to repay their obligations, as agreed and ensure appropriate collateral is obtained to secure the loan. Commercial loans are primarily made based on the identified cash flows of the borrower and, secondarily, on the underlying collateral provided by the borrower. Most commercial loans are secured by the assets being financed or other business assets, such as real estate, accounts receivable, or inventory, and include personal guarantees. Owner-occupied real estate is included in commercial loans, as the repayment of these loans is generally dependent on the operations of the commercial borrower's business rather than on income-producing properties or the sale of the properties. Commercial loans are grouped into two distinct sub-categories: specialized and general. Commercial related segments that are considered "specialized" include agricultural production and real estate loans, energy loans, and finance, investment, and insurance loans. Commercial related segments that contain a broader diversity of borrowers, sub-industries, or serviced industries are grouped into the "general category." These include goods, services, restaurant & retail, construction, and other industries.

Commercial Real Estate – Commercial real estate loans are also subject to underwriting standards and processes similar to commercial loans. These loans are underwritten primarily based on projected cash flows for income-producing properties and collateral values for non-income-producing properties. The repayment of these loans is generally dependent on the successful operation of the property securing the loans or the sale or refinancing of the property. Real estate loans may be adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Company's real estate portfolio are diversified by type and geographic location. This diversity helps reduce the exposure to adverse economic events that affect any single market or industry.

Construction – Loans for residential construction are for single-family properties to developers, builders, or end-users. These loans are underwritten based on estimates of costs and completed value of the project. Funds are advanced based on estimated percentage of completion for the project. Performance of these loans is affected by economic conditions as well as the ability to control costs of the projects.

Consumer – Loans to consumers include 1-4 family residential loans, auto loans, and other loans for recreational vehicles or other purposes. The Company utilizes a computer-based credit scoring analysis to supplement its policies and procedures in underwriting consumer loans. The Company's loan policy addresses types of consumer loans that may be originated and the collateral, if secured, which must be perfected. The relatively smaller individual dollar amounts of consumer loans that are spread over numerous individual borrowers also minimizes the Company's risk. The Company generally requires mortgage title insurance and hazard insurance on 1-4 family residential loans.

The allowance for loan losses was $29.1 million at March 31, 2020, compared to $24.2 million at December 31, 2019. The allowance for loan losses to loans held for investment was 1.38% at March 31, 2020 and 1.13% at December 31, 2019. The increase in the allowance for loan losses from December 31, 2019 to March 31, 2020 is a result of economic effects from the COVID-19 pandemic as well as the decline in oil and gas prices. The full extent of the impact on the economy and the Company's customers is unknown at this time. Accordingly, additional provisions for loan losses may be necessary in future periods.

The following table details the activity in the allowance for loan losses. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

	Beginning Balance	Provision for Loan Losses	Charge-offs	Recoveries	Ending Balance
For the three months ended March 31, 2020					
Commercial real estate	$ 5,049	$ 2,035	$ —	$ 108	$ 7,192
Commercial - specialized	2,287	2,218	(14)	64	4,555
Commercial - general	9,609	(798)	(848)	17	7,980
Consumer:					
1-4 family residential	2,093	651	—	—	2,744
Auto loans	3,385	1,316	(441)	52	4,312
Other consumer	1,341	593	(367)	72	1,639
Construction	433	219	—	—	652
Total	$ 24,197	$ 6,234	$ (1,670)	$ 313	$ 29,074
For the three months ended March 31, 2019					
Commercial real estate	$ 5,579	$ (352)	$ —	$ 108	$ 5,335
Commercial - specialized	2,516	(179)	(33)	23	2,327
Commercial - general	8,173	262	(4)	73	8,504
Consumer:					

1-4 family residential	2,249	156	(19)	30	2,416
Auto loans	2,994	299	(259)	33	3,067
Other consumer	1,192	212	(279)	49	1,174
Construction	423	210	(75)	—	558
Total	$ 23,126	$ 608	$ (669)	$ 316	$ 23,381

The following table shows the Company’s investment in loans disaggregated based on the method of evaluating impairment:

	Recorded Investment		Allowance for Loan Losses	
	Individually Evaluated	Collectively Evaluated	Individually Evaluated	Collectively Evaluated
March 31, 2020				
Commercial real estate	$ 1,279	$ 640,460	$ —	$ 7,192
Commercial - specialized	2,189	300,927	676	3,879
Commercial - general	1,091	423,659	126	7,854
Consumer:				
1-4 family residential	1,868	354,672	—	2,744
Auto loans	—	212,912	—	4,312
Other consumer	—	72,162	—	1,639
Construction	—	97,586	—	652
Total	$ 6,427	$ 2,102,378	$ 802	$ 28,272
December 31, 2019				
Commercial real estate	$ 299	$ 657,896	$ —	$ 5,049
Commercial - specialized	573	308,932	—	2,287
Commercial - general	1,396	440,002	525	9,084
Consumer:				
1-4 family residential	1,899	360,897	—	2,093
Auto loans	—	215,209	—	3,385
Other consumer	—	74,000	—	1,341
Construction	—	82,520	—	433
Total	$ 4,167	$ 2,139,456	$ 525	$ 23,672

Impaired loan information follows:

	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
March 31, 2020						
Commercial real estate	$ 1,279	$ 1,279	$ —	$ 1,279	$ —	$ 1,169
Commercial - specialized	2,189	573	1,616	2,189	676	1,767
Commercial - general	1,534	589	502	1,091	126	1,632
Consumer:				—		
1-4 family	2,287	1,868	—	1,868	—	2,028
Auto loans	—	—	—	—	—	—
Other consumer	—	—	—	—	—	—
Construction	—	—	—	—	—	—
Total	$ 7,289	$ 4,309	$ 2,118	$ 6,427	$ 802	$ 6,596
December 31, 2019						
Commercial real estate	$ 754	$ 299	$ —	$ 299	$ —	$ 1,059
Commercial - specialized	573	573	—	573	—	1,345
Commercial - general	1,839	—	1,396	1,396	525	2,173
Consumer:				—		
1-4 family	2,318	1,899	—	1,899	—	2,187
Auto loans	—	—	—	—	—	—
Other consumer	—	—	—	—	—	—
Construction	—	—	—	—	—	—
Total	$ 5,484	$ 2,771	$ 1,396	$ 4,167	$ 525	$ 6,764

All impaired loans $250,000 and greater were specifically evaluated for impairment. Interest income recognized using a cash-basis method on impaired loans for the three-month period ended March 31, 2020 and the year ended December 31, 2019 was not significant. Additional funds committed to be advanced on impaired loans are not significant.

The table below provides an age analysis on accruing past-due loans and nonaccrual loans:

	30-89 Days Past Due	90 Days or More Past Due	Nonaccrual
March 31, 2020			
Commercial real estate	$ 2,243	$ —	$ 1,327
Commercial - specialized	449	—	1,610
Commercial - general	1,692	—	2,163
Consumer:			
1-4 Family residential	2,176	946	800
Auto loans	720	146	—
Other consumer	634	120	—
Construction	958	—	—
Total	$ 8,872	$ 1,212	$ 5,900
December 31, 2019			
Commercial real estate	$ 37	$ 116	$ 162
Commercial - specialized	708	—	1,172
Commercial - general	1,747	—	2,254
Consumer:			
1-4 Family residential	1,212	932	1,105
Auto loans	1,468	183	—
Other consumer	848	121	—
Construction	1,159	—	—
Total	$ 7,179	$ 1,352	$ 4,693

The Company grades its loans on a thirteen-point grading scale. These grades fit in one of the following categories: (i) pass, (ii) special mention, (iii) substandard, (iv) doubtful, or (v) loss. Loans categorized as loss are charged-off immediately. The grading of loans reflect a judgment about the risks of default associated with the loan. The Company reviews the grades on loans as part of our on-going monitoring of the credit quality of our loan portfolio.

Pass loans have financial factors or nature of collateral that are considered reasonable credit risks in the normal course of lending and encompass several grades that are assigned based on varying levels of risk, ranging from credits that are secured by cash or marketable securities, to watch credits which have all the characteristics of an acceptable credit risk but warrant more than the normal level of monitoring.

Special mention loans have potential weaknesses that deserve management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of repayment prospects for the loans at some future date.

Substandard loans are inadequately protected by the current net worth and paying capacity of the borrower or by the collateral pledged, if any. These loans have a well-defined weakness or weaknesses that jeopardize collection and present the distinct possibility that some loss will be sustained if the deficiencies are not corrected. A protracted workout on these credits is a distinct possibility. Prompt corrective action is therefore required to strengthen the Company’s position, and/or to reduce exposure and to assure that adequate remedial measures are taken by the borrower. Credit exposure becomes more likely in such credits and a serious evaluation of the secondary support to the credit is performed. Substandard loans can be accruing or can be nonaccrual depending on the circumstances of the individual loans.

Doubtful loans have all the weaknesses inherent in substandard loans with the added characteristics that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions, and values highly questionable and improbable. All doubtful loans are on nonaccrual.

The following table summarizes the internal classifications of loans:

	Pass	Special Mention	Substandard	Doubtful	Total
March 31, 2020					
Commercial real estate	$ 614,829	$ 20,926	$ 5,984	$ —	$ 641,739
Commercial - specialized	283,187	—	19,929	—	303,116
Commercial - general	418,316	—	6,434	—	424,750
Consumer:					
1-4 family residential	350,874	—	5,666	—	356,540
Auto loans	212,094	—	818	—	212,912
Other consumer	71,878	—	284	—	72,162
Construction	97,586	—	—	—	97,586
Total	$ 2,048,764	$ 20,926	$ 39,115	$ —	$ 2,108,805
December 31, 2019					
Commercial real estate	$ 632,641	$ 22,313	$ 3,241	$ —	$ 658,195
Commercial - specialized	307,239	—	2,266	—	309,505
Commercial - general	428,155	—	13,243	—	441,398
Consumer:					
1-4 family residential	356,422	—	6,374	—	362,796
Auto loans	214,363	—	846	—	215,209
Other consumer	73,716	—	284	—	74,000
Construction	82,520	—	—	—	82,520
Total	$ 2,095,056	$ 22,313	$ 26,254	$ —	$ 2,143,623

Under section 4013 of the CARES Act, banks may elect to deem that loan modifications do not result in a TDR if they are (1) related to the COVID-19 pandemic; (2) executed on a loan that was not more than 30 days past due as of December 31, 2019; and (3) executed between March 1, 2020, and the earlier of (A) 60 days after the date of termination of the national emergency or (B) December 31, 2020. The Company had not made an election as of March, 31, 2020.

Additionally, other short-term modifications made on a good faith basis in response to the COVID-19 pandemic to borrowers who were current prior to any relief are not TDRs under ASC Subtopic 310-40 and the Joint Interagency Regulatory Guidance. This includes short-term (e.g., up to six months) modifications such as payment deferrals, fee waivers, extensions of repayment terms, or delays in payment that are insignificant. Borrowers considered current are those that are less than 30 days past due on their contractual payments at the time a modification program is implemented.

In response to the COVID-19 pandemic, the Company has implemented a short-term deferral modification program that complies with ASC Subtopic 310-40 and the Joint Interagency Regulatory Guidance. As such, there were no loans modified as troubled debt restructurings during the three-month period ended March 31, 2020 and the year ended December 31, 2019.

4. GOODWILL AND INTANGIBLES

Goodwill and other intangible assets are summarized below:

	March 31, 2020	December 31, 2019
Beginning goodwill	$ 18,757	$ —
Arising from business combinations	-	18,757
Measurement period acquisition adjustment	1,211	—
Ending goodwill	$ 19,968	$ 18,757
Amortized intangible assets		
Customer relationship intangibles	$ 6,679	$ 6,679
Less: Accumulated amortization	(506)	(202)
	6,173	6,477
Other intangibles	2,309	2,309
Less: Accumulated amortization	(269)	(154)
	2,040	2,155
Other intangible assets, net	$ 8,213	$ 8,632

5. BORROWING ARRANGEMENTS

Subordinated debt securities

In December 2018, the Company issued $26.5 million in subordinated debt securities. $12.4 million of the securities have a maturity date of December 2028 and an average fixed rate of 5.74% for the first five years. The remaining $14.1 million of securities have a maturity date of December 2030 and an average fixed rate of 6.41% for the first seven years. After the expiration of the fixed rate periods, all securities will float at the *Wall Street Journal* prime rate, with a floor of 4.5% and a ceiling of 7.5%. These securities pay interest quarterly, are unsecured, and may be called by the Company at any time after the remaining maturity is five years or less. Additionally, these securities qualify for Tier 2 capital treatment, subject to regulatory limitations.

6. STOCK-BASED COMPENSATION

Equity Incentive Plan

The 2019 Equity Incentive Plan ("Plan") was approved by the Company's Board of Directors on January 16, 2019 and by its shareholders on March 6, 2019. The purpose of the Plan is to: (i) attract and retain the best available personnel for positions of substantial responsibility, (ii) provide additional incentive to employees, directors and consultants, and (iii) promote the success of the Company's business. This Plan permits the grant of incentive stock options, nonstatutory stock options, stock appreciation rights, restricted stock, restricted stock units, performance units, performance shares, and other stock-based awards. The maximum aggregate number of shares of common stock that may be issued pursuant to all awards under the Plan is 2,300,000. The maximum aggregate number of shares that may be issued under the Plan may be increased annually by up to 3% of the total issued and outstanding common shares of the Company at the beginning of each fiscal year.

The fair value of each option award is estimated on the date of grant using a closed form option valuation ("Black-Scholes") model that uses the assumptions noted in the table below. Expected volatilities are based on historical volatilities of the Company's common stock and similar peer company averages. The Company uses historical data to estimate option exercise and post-vesting termination behavior. The expected term of options granted represents the period of time that options granted are expected to be outstanding, which takes in to account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on U.S. Treasury yield curve in effect at the time of the grant.

Options

A summary of activity in the Plan during the three months ended March 31, 2020 is presented in the table below:

Three Months Ended March 31, 2020	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life in Years	Aggregate Intrinsic Value
Outstanding at beginning of year:	1,462,997	$ 13.42		$
Granted	248,966	20.93		
Exercised	(851)	16.00		
Forfeited	—	—		
Expired	—	—		
Balance, March 31, 2020	1,711,112	$ 14.51	6.35	$ 4,097
Exercisable at end of period	1,094,992	$ 12.04	5.50	$ 4,097
Vested at end of period	1,091,586	$ 12.04	5.50	$ 4,097

A summary of assumptions used to calculate the fair values of the awards granted during the periods noted is presented below:

	Three Months Ended March 31, 2020	Three Months Ended March 31, 2019
Expected volatility	27.46%	27.46%
Expected dividend yield	0.70%	0.70%
Expected term (years)	6.2 years	6.0 years
Risk-free interest rate	1.44%	2.39%
Weighted average grant date fair value	$ 5.68	$ 6.15

The total intrinsic value of options exercised during the three months ended March 31, 2020 was $4,000. There were no options exercised during the three months ended March 31, 2019.

On January 16, 2019, the Company approved the conversion of its previously issued stock appreciation rights ("SARs") to stock options. There were 1,401,000 outstanding SARs that were converted effective as of May 6, 2019. The fair value of the SARs was $11.5 million at the conversion date. During the modification of these awards from liabilities to equity, the Company accelerated the expiration date, between two and four years, on 750,000 of the stock options. As a result, the fair value of the stock options after modification was $11.2 million. However, since the fair value of the new equity awards was less than the fair value of the liability awards, no adjustment was made to the Company's income statement. The $11.5 million was reclassified from liabilities to equity upon conversion on May 6, 2019.

Restricted Stock Units

A summary of activity in the Plan during the three months ended March 31, 2020 is presented in the table below:

Three Months Ended March 31, 2020	Number of Shares	Weighted-Average Grant Date Fair Value
Outstanding at beginning of year:	81,200	$ 19.46
Granted	5,970	20.93
Exercised	(24,694)	19.79
Forfeited	—	—
Balance, March 31, 2020	62,476	$ 19.47

Restricted stock units granted under the Plan typically vest over five years, but vesting periods may vary. Compensation expense for these grants will be recognized over the vesting period of the awards based on the fair value of the stock at the issue date.

The total unrecognized compensation cost for the awards outstanding under the Plan at March 31, 2020 was $3.9 million and will be recognized over a weighted average remaining period of 2.05 years. The total fair value of restricted stock units vested during the three months ended March 31, 2019 was $489,000. There was no vesting of restricted stock units during the three months ended March 31, 2019.

7. COMMITMENTS AND CONTINGENCIES

Financial instruments with off-balance-sheet risk - The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the Company's consolidated financial statements. The Company's exposure to credit loss is represented by the contractual amount of these commitments. The Company follows the same credit policies in making commitments as it does for recorded instruments.

Financial instruments whose contract amounts represent credit risk outstanding follow:

	March 31, 2020	December 31, 2019
Commitments to grant loans and unfunded commitments under lines of credit	$ 471,650	$ 409,969
Standby letters of credit	12,036	10,748

Commitments to grant loans and extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The commitments for lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Company, is based on management's credit evaluation of the customer.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those letters of credit are primarily issued to support public and private borrowing arrangements. Essentially all letters of credit issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company requires collateral supporting those commitments if deemed necessary.

Litigation - The Company is a defendant in legal actions arising from time to time in the ordinary course of business. Management believes that the aggregate ultimate liability, if any, arising from these matters will not materially affect the Company's consolidated financial statements.

Federal Home Loan Bank ("FHLB") Letters of Credit - The Company uses FHLB letters of credit to pledge to certain public deposits. The balance of these FHLB letters of credit was $199.0 million at March 31, 2020 and December 31, 2019, respectively.

8. CAPITAL AND REGULATORY MATTERS

The Company and its bank subsidiary are subject to various regulatory capital requirements administered by its banking regulators. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and its bank subsidiary's financial statements. Under capital guidelines and the regulatory framework for prompt corrective action, the Company and its bank subsidiary must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

In July 2013, the Board of Governors of the Federal Reserve System published final rules for the adoption of the Basel III regulatory capital framework ("Basel III"). Basel III, among other things, (i) introduced a new capital measure called Common Equity Tier 1 ("CET1"), (ii) specified that Tier 1 capital consists of CET1 and Additional Tier 1 Capital instruments meeting specified requirements, (iii) defined Common Equity Tier 1 narrowly by requiring that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital and (iv) expanded the scope of the deductions/adjustments as compared to existing regulations. Basel III became effective for the Company and its bank subsidiary on January 1, 2016 with certain transition provisions fully phased-in on January 1, 2019.

Quantitative measures established by regulation to ensure capital adequacy require the Company and its bank subsidiary to maintain minimum amounts and ratios (set forth in the following table) of total, Tier 1 and CET1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of March 31, 2020 and December 31, 2019, that the Company and its bank subsidiary met all capital adequacy requirements to which they are subject.

As of March 31, 2020, the bank subsidiary was well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based, CET1 and Tier 1 leverage ratios as set forth in the following tables. There are no conditions or events since March 31, 2020 that management believes have changed the bank subsidiary's category.

The Company and its bank subsidiary's actual capital amounts and ratios follow:

	Actual		Minimum Required Under BASEL III Fully Phased-In		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
March 31, 2020						
Total Capital to Risk Weighted Assets:						
Consolidated	$ 384,538	15.23%	$ 265,086	10.50%	N/A	N/A
City Bank	375,390	14.87%	265,042	10.50%	$ 252,421	10.00%
Tier I Capital to Risk Weighted Assets:						
Consolidated	328,812	13.02%	214,594	8.50%	N/A	N/A
City Bank	346,136	13.71%	214,558	8.50%	201,937	8.00%
Common Equity Tier 1 to Risk Weighted Assets:						
Consolidated	283,812	11.24%	176,724	7.00%	N/A	N/A
City Bank	346,136	13.71%	176,695	7.00%	164,074	6.50%
Tier I Capital to Average Assets:						
Consolidated	328,812	10.34%	127,209	4.00%	N/A	N/A
City Bank	346,136	10.89%	128,260	4.00%	158,916	5.00%
December 31, 2019						
Total Capital to Risk Weighted Assets:						

Consolidated	$	373,684	14.88%	$	263,769	10.50%		N/A	N/A
City Bank		368,322	14.67%		263,702	10.50%	$	251,145	10.00%
Tier I Capital to Risk Weighted Assets:									
Consolidated		322,835	12.85%		213,527	8.50%		N/A	N/A
City Bank		343,945	13.70%		213,473	8.50%		200,916	8.00%
Common Equity Tier 1 to Risk Weighted Assets:									
Consolidated		277,835	11.06%		175,846	7.00%		N/A	N/A
City Bank		343,945	13.70%		175,801	7.00%		163,244	6.50%
Tier I Capital to Average Assets:									
Consolidated		322,835	10.74%		120,219	4.00%		N/A	N/A
City Bank		343,945	11.45%		121,235	4.00%		150,175	5.00%

State banking regulations place certain restrictions on dividends paid by banks to their shareholders. Dividends paid by the Company's bank subsidiary would be prohibited if the effect thereof would cause the bank subsidiary's capital to be reduced below applicable minimum capital requirements.

9. DERIVATIVES

The Company utilizes interest rate and cash flow swap agreements as part of its asset-liability management strategy to help manage its interest rate and cash flow risk position. The notional amount of the interest rate and cash flow swaps do not represent amounts exchanged by the parties. The amount exchanged is determined by reference to the notional amounts and the other terms of the individual interest rate and cash flow swap agreements.

The following table reflects the fair value hedges included in the consolidated balance sheets:

	March 31, 2020		December 31, 2019	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Included in other liabilities:				
Interest rate swaps related to fixed rate loans	$ 10,464	$ 1,012	$ 10,557	$ 351
Included in other assets:				
Interest rate swaps related to fixed rate loans	$ —	$ —	$ —	$ —

The following table reflects the cash flow hedges included in the consolidated balance sheets:

	March 31, 2020		December 31, 2019	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Included in other liabilities:				
Cash flow swaps related to state and municipal securities	$ 123,760	$ 1,233	$ —	$ —
Included in other assets:				
Cash flow swaps related to state and municipal securities	$ —	$ —	$ —	$ —

Mortgage banking derivatives

The following table reflects the amount and fair value of mortgage banking derivatives in the consolidated balance sheets:

	March 31, 2020		December 31, 2019	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Included in other assets:				
Forward contracts related to mortgage loans held for sale	$ —	$ —	$ —	$ —
Interest rate lock commitments	223,919	4,470	52,875	814
Total included in other assets	$ 223,919	$ 4,470	$ 52,875	$ 814
Included in other liabilities:				
Forward contracts related to mortgage loans held for sale	$ 171,034	$ 3,272	$ 58,948	$ 141
Interest rate lock commitments	—	—	—	—
Total included in other liabilities	$ 171,034	$ 3,272	$ 58,948	$ 141

10. EARNINGS PER SHARE

The factors used in the earnings per share computation follow:

	Three Months Ended March 31,	
	2020	2019
Net income	$ 7,083	$ 4,773
Weighted average common shares outstanding - basic	18,043,105	14,771,520
Effect of dilutive securities:		
Stock-based compensation awards	418,817	38
Weighted average common shares outstanding - diluted	18,461,922	14,771,558
Basic earnings per share	$ 0.39	$ 0.32
Diluted earnings per share	$ 0.38	$ 0.32

11. SEGMENT INFORMATION

Financial results by reportable segment are detailed below:

Three Months Ended March 31, 2020	Banking	Insurance	Consolidated
Net interest income	$ 30,199	$ —	$ 30,199
Provision for loan loss	(6,234)	—	(6,234)
Noninterest income	17,761	1,114	18,875
Noninterest expense	(32,831)	(1,180)	(34,011)
Income before income taxes	8,895	(66)	8,829
Income tax (expense) benefit	(1,758)	12	(1,746)
Net income	$ 7,137	$ (54)	$ 7,083

Three Months Ended March 31, 2019	Banking	Insurance	Consolidated
Net interest income	$ 24,546	$ —	$ 24,546
Provision for loan loss	(608)	—	(608)
Noninterest income	10,371	1,704	12,075
Noninterest expense	(29,073)	(963)	(30,036)
Income before income taxes	5,236	741	5,977
Income tax (expense) benefit	(1,140)	(64)	(1,204)
Net income	$ 4,096	$ 677	$ 4,773

12. FAIR VALUE DISCLOSURES

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability is not adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

Valuation techniques that are consistent with the market approach, the income approach and/or the cost approach are required by GAAP. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset. Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The fair value hierarchy for valuation inputs gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- *Level 1 Inputs* - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- *Level 2 Inputs* - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.
- *Level 3 Inputs* - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

The following table summarizes fair value measurements:

	Level 1	Level 2	Level 3	Total
March 31, 2020				
Assets (liabilities) measured at fair value on a recurring basis:				
Securities available for sale:				
U.S. government and agencies	$ —	$ 4,835	$ —	$ 4,835
State and municipal	—	209,654	—	209,654
Mortgage-backed securities	—	376,081	—	376,081
Collateralized mortgage obligations	—	107,410	—	107,410
Asset-backed and other amortizing securities	—	36,811	—	36,811
Loans held for sale (mandatory)	—	46,409	—	46,409
Mortgage servicing rights	—	2,110	—	2,110
Asset derivatives	—	4,470	—	4,470
Liability derivatives	—	(5,517)	—	(5,517)
Assets measured at fair value on a non-recurring basis:				
Impaired loans	—	—	5,625	5,625
Other real estate owned	—	—	1,944	1,944
Loans held for sale (best efforts)	—	16,554	—	16,554
December 31, 2019				
Assets (liabilities) measured at fair value on a recurring basis:				
Securities available for sale:				
U.S. government and agencies	$ —	$ 4,807	$ —	$ 4,807
State and municipal	—	94,692	—	94,692
Mortgage-backed securities	—	464,516	—	464,516
Collateralized mortgage obligations	—	107,289	—	107,289
Asset-backed and other amortizing securities	—	36,346	—	36,346
Loans held for sale (mandatory)	—	32,809	—	32,809
Mortgage servicing rights	—	2,054	—	2,054
Asset derivatives	—	814	—	814
Liability derivatives	—	(492)	—	(492)
Assets measured at fair value on a non-recurring basis:				
Impaired loans	—	—	3,642	3,642
Other real estate owned	—	—	1,883	1,883
Loans held for sale (best efforts)	—	16,226	—	16,226

Securities – Fair value is calculated based on market prices of similar securities using matrix pricing. Matrix pricing is a mathematical technique commonly used to price debt securities that are not actively traded.

Loans held for sale (mandatory) – Loans held for sale originated for mandatory delivery are reported at fair value. Fair value is determined using quoted prices for similar assets, adjusted for specific attributes of that loan.

Mortgage servicing rights – Mortgage servicing rights are reported at fair value. Fair value is based on market prices for comparable mortgage servicing contracts.

Derivatives – Fair value of derivatives is based on valuation models using observable market data as of the measurement date.

Impaired loans – Impaired loans are reported at the fair value of the underlying collateral, less estimated disposal costs, if repayment is expected solely from the sale of the collateral. Collateral values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria.

Foreclosed assets – Foreclosed assets are transferred from loans at the lower of cost or fair value, less estimated costs to sell. Collateral values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria.

Loans held for sale (best efforts) – Loans held for sale originated for best efforts delivery are reported at fair value if, on an aggregate basis, the fair value for the loans is less than cost. In determining whether the fair value of loans held for sale is less than cost when quoted market prices are not available, the Company may consider outstanding investor commitments or discounted cash flow analyses with market assumptions. Such fair values are classified within either Level 2 or Level 3 of the fair value hierarchy.

The following table presents quantitative information about non-recurring Level 3 fair value measurements:

	Fair Value	Valuation Techniques	Unobservable Inputs	Range of Discounts
March 31, 2020				
Impaired loans	$ 5,625	Third party appraisals or inspections	Collateral discounts and selling costs	0%-100%
Other real estate owned	1,944	Third party appraisals or inspections	Collateral discounts and selling costs	15%-66%
December 31, 2019				
Impaired loans	$ 3,642	Third party appraisals or inspections	Collateral discounts and selling costs	0%-100%
Other real estate owned	1,883	Third party appraisals or inspections	Collateral discounts and selling costs	15%-66%

The estimated fair values, and related carrying amounts, of the Company’s financial instruments are as follows:

	Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
March 31, 2020					
Financial assets:					
Cash and cash equivalents	$ 136,062	$ 136,062	$ —	$ —	$ 136,062
Loans, net	2,079,731	—	—	2,083,267	2,083,267
Accrued interest receivable	11,015	—	11,015	—	11,015
Bank-owned life insurance	69,756	—	69,756	—	69,756
Financial liabilities:					
Deposits	$ 2,665,848	$ 2,481,434	$ 184,414	$ —	$ 2,665,848
Accrued interest payable	2,051	—	2,051	—	2,051
Notes payable & other borrowings	95,000	—	95,000	—	95,000
Junior subordinated deferrable interest debentures	46,393	—	46,393	—	46,393
Subordinated debt securities	26,472	—	26,472	—	26,472

	Carrying Amount	Level 1	Level 2	Level 3	Total Fair Value
December 31, 2019					
Financial assets:					
Cash and cash equivalents	$ 158,099	$ 158,099	$ —	$ —	$ 158,099
Loans, net	2,119,426	—	—	2,123,289	2,123,289
Accrued interest receivable	13,924	—	13,924	—	13,924
Bank-owned life insurance	69,397	—	69,397	—	69,397
Financial liabilities:					
Deposits	$ 2,696,857	$ 2,354,999	$ 346,194	$ —	$ 2,701,193
Accrued interest payable	2,283	—	2,283	—	2,283
Notes payable & other borrowings	95,000	—	95,000	—	95,000
Junior subordinated deferrable interest debentures	46,393	—	46,393	—	46,393
Subordinated debt securities	26,472	—	26,472	—	26,472

13. BUSINESS COMBINATIONS

West Texas State Bank

In November 2019, the Company completed its acquisition of West Texas State Bank (“WTSB”). This transaction resulted in six additional branches. The Company paid the shareholders of WTSB $76.1 million in cash, for all outstanding stock of WTSB and resulted in 100% ownership interest.

The Company recognized total goodwill of $19.8 million which is calculated as the excess of both the consideration exchanged and liabilities assumed compared to the fair market value of identifiable assets acquired. None of the goodwill recognized is expected to be deductible for income tax purposes.

The Company incurred expenses related to the acquisition of approximately $955,000 for the year ended December 31, 2019, which are included in noninterest expense in the consolidated statements of comprehensive income.

Non-credit impaired loans had a fair value of $196.2 million at the acquisition date and contractual balance of $198.4 million. As of the acquisition date, the Company expects that an insignificant amount of the contractual balance of these loans will be uncollectible. The difference of $2.2 million will be recognized into interest income as an adjustment to yield over the life of the loans. Purchased credit impaired loans were insignificant.

Fair values of the assets acquired and liabilities assumed in this transaction as of the closing date are as follows:

Cash paid	$ 76,100
Assets acquired:	
Cash and cash equivalents	$ 77,903
Interest-bearing time deposits in banks	52,700
Federal funds purchased	26,468
Securities available for sale	68,398
Loans held for investment	195,228
Bank-owned life insurance	10,932
Premises and equipment, net	4,132
Accrued interest receivable	1,114
Core deposit intangible	6,679
Other assets	2,648
Total assets acquired	$ 446,202
Liabilities assumed	
Deposits	$ 386,176
Accrued interest payable	55
Deferred tax liability	762
Other liabilities	2,884
Total liabilities assumed	$ 389,877
Net assets acquired	$ 56,325
Goodwill recorded in acquisition	$ 19,775

In the first three months of 2020, the Company made measurement period adjustments to reflect facts and circumstances in existence as of the closing date of the acquisition. These adjustments primarily included a $1.2 million increase in goodwill, a $900,000 decrease in loans, and a $300,000 increase in other liabilities. The amount of income recorded in current period earnings that would have been recorded in the previous reporting period had the adjustment been recognized as of the acquisition date is not significant. The Company is still evaluating the fair values of other assets and other liabilities, additional adjustments may be recorded during the measurement period, but no later than one year from the closing date of the transaction. The Company will reflect measurement period adjustments, if any, in the period in which the adjustments are recognized, which may result in further adjustments to the values presented in the above table. The Company expects to finalize these values by the third quarter 2020.

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

The following discussion and analysis is intended to assist readers in understanding our financial condition as of and results of operations for the period covered by this Quarterly Report on Form 10-Q (this "Form 10-Q") and should be read in conjunction with our consolidated financial statements and the accompanying notes thereto included in this Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2019 (the "2019 Annual Report on Form 10-K") filed with the Securities and Exchange Commission (the "SEC") pursuant to Rule 424(b) of the Securities Act of 1933, as amended (the "Securities Act"), on March 25, 2020. Unless we state otherwise or the context otherwise requires, references in this Form 10-Q to "we," "our," "us" and "the Company" refer to South Plains Financial, Inc., a Texas corporation, our wholly-owned banking subsidiary, City Bank, a Texas banking association and our other consolidated subsidiaries. References in this Form 10-Q to the "Bank" refer to City Bank.

Cautionary Notice Regarding Forward-Looking Statements

This Form 10-Q contains statements that we believe are "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements reflect our current views with respect to, among other things, future events and our financial performance. These statements are often, but not always, made through the use of words or phrases such as "may," "might," "should," "could," "predict," "potential," "believe," "expect," "continue," "will," "anticipate," "seek," "estimate," "intend," "plan," "strive," "projection," "goal," "target," "outlook," "aim," "would," "annualized" and "outlook," or the negative version of those words or other comparable words or phrases of a future or forward-looking nature. These forward-looking statements are not historical facts, and are based on current expectations, estimates and projections about our industry, management's beliefs and certain assumptions made by management, many of which, by their nature, are inherently uncertain and beyond our control. Accordingly, we caution you that any such forward-looking statements are not guarantees of future performance and are subject to risks, assumptions, estimates and uncertainties that are difficult to predict. Although we believe that the expectations reflected in these forward-looking statements are reasonable as of the date made, actual results may prove to be materially different from the results expressed or implied by the forward-looking statements.

There are or will be important factors that could cause our actual results to differ materially from those indicated in these forward-looking statements, including, but not limited to, the following:

- the ongoing COVID-19 pandemic and its uncertain economic impact on the Company's customers and communities;
- our ability to effectively execute our expansion strategy and manage our growth, including identifying and consummating suitable acquisitions;
- business and economic conditions, particularly those affecting our market areas, as well as the concentration of our business in such market areas;
- high concentrations of loans secured by real estate located in our market areas;
- risks associated with our commercial loan portfolio, including the uncertain economic consequences of the ongoing COVID-19 pandemic or any deterioration in value of the general business assets that secure such loans;
- potential changes in the prices, values and sales volumes of commercial and residential real estate securing our real estate loans;
- risks associated with our agricultural loan portfolio, including the heightened sensitivity to weather conditions, commodity prices, and other factors generally outside the borrowers and our control;
- risks associated with the sale of crop insurance products, including termination of or substantial changes to the federal crop insurance program;
- risks related to the significant amount of credit that we have extended to a limited number of borrowers and in a limited geographic area;

- public funds deposits comprising a relatively high percentage of our deposits;
- potential impairment on the goodwill we have recorded or may record in connection with business acquisitions;
- our ability to maintain our reputation;
- our ability to successfully manage our credit risk and the sufficiency of our allowance for loan losses;
- our ability to attract, hire and retain qualified management personnel;
- our dependence on our management team, including our ability to retain executive officers and key employees and their customer and community relationships;
- interest rate fluctuations, which could have an adverse effect on our profitability;
- competition from banks, credit unions and other financial services providers;
- our ability to keep pace with technological change or difficulties we may experience when implementing new technologies;
- system failures, service denials, cyber-attacks and security breaches;
- our ability to maintain effective internal control over financial reporting;
- employee error, fraudulent activity by employees or customers and inaccurate or incomplete information about our customers and counterparties;
- increased capital requirements imposed by banking regulators, which may require us to raise capital at a time when capital is not available on favorable terms or at all;
- our ability to maintain adequate liquidity and to raise necessary capital to fund our acquisition strategy and operations or to meet increased minimum regulatory capital levels;
- costs and effects of litigation, investigations or similar matters to which we may be subject, including any effect on our reputation;
- natural disasters, severe weather, acts of god, acts of war or terrorism, outbreaks of hostilities, public health outbreaks (such as the ongoing COVID-19 pandemic), other international or domestic calamities, and other matters beyond our control;
- tariffs and trade barriers;
- compliance with governmental and regulatory requirements, including the Dodd-Frank Act Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), Economic Growth, Regulatory Relief, and Consumer Protection Act ("EGRRCPA"), and others relating to banking, consumer protection, securities and tax matters; and
- changes in the laws, rules, regulations, interpretations or policies relating to financial institutions, accounting, tax, trade, monetary and fiscal matters, including the policies of the Board of Governors of the Federal Reserve System ("Federal Reserve") and as a result of initiatives of the Trump administration.

The foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this Form 10-Q and the risk factors set forth in our 2019 Annual Report on Form 10-K. Because of these risks and other uncertainties, our actual future results, performance or achievements, or industry results, may be materially different from the results indicated by the forward-looking statements in this Form 10-Q. In addition, our past results of operations are not necessarily indicative of our future results. Accordingly, you should not rely on any forward-looking statements, which represent our beliefs, assumptions and estimates only as of the dates on which such forward-looking statements were made. Any forward-looking statement speaks only as of the date on which it is made, and we do not undertake any obligation to update or review any forward-looking statement, whether as a result of new information, future developments or otherwise, except as required by law.

Available Information

The Company maintains an Internet web site at www.spfi.bank. The Company makes available, free of charge, on its web site (under www.spfi.bank/financials-filings/sec-filings) the Company's annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or Section 15(d) of the Exchange Act as soon as reasonably practicable after the Company files such material with, or furnishes it to, the SEC. The Company also makes available, free of charge, through its web site (under www.spfi.bank/corporate-governance/documents-charters) links to the Company's Code of Conduct and the charters for its board committees. In addition, the SEC maintains an Internet site (at www.sec.gov) that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC.

The Company routinely posts important information for investors on its web site (under www.spfi.bank and, more specifically, under the News & Events tab at www.spfi.bank/news-events/press-releases). The Company intends to use its web site as a means of disclosing material non-public information and for complying with its disclosure obligations under SEC Regulation FD (Fair Disclosure). Accordingly, investors should monitor the Company's web site, in addition to following the Company's press releases, SEC filings, public conference calls, presentations and webcasts.

The information contained on, or that may be accessed through, the Company's web site is not incorporated by reference into, and is not a part of, this Form 10-Q.

Overview

We are a bank holding company headquartered in Lubbock, Texas, and our wholly-owned subsidiary, City Bank, is one of the largest independent banks in West Texas. We have additional banking operations in the Dallas, El Paso, Greater Houston, the Permian Basin, and College Station Texas markets, and the Ruidoso and Eastern New Mexico markets. Through City Bank, we provide a wide range of commercial and consumer financial services to small and medium-sized businesses and individuals in our market areas. Our principal business activities include commercial and retail banking, along with insurance, investment, trust and mortgage services.

Recent Developments

COVID-19 Update

The spread of the novel coronavirus ("COVID-19") has caused significant disruptions in the U.S. economy since it was declared a pandemic in March 2020 by the World Health Organization. The changes have impacted our clients, their industries, as well as the financial services industry. At this time, we cannot predict the impact or how long the economy or our impacted clients will be disrupted.

The Company's Business Continuity Oversight Committee has monitored the spread of the COVID-19 pandemic since late January 2020 and has continuously escalated the Company's response as well as employee and customer communications. As the COVID-19 pandemic continued to spread across the globe, the Company created a Pandemic Task Force to implement South Plains' Business Continuity Plan to ensure the safety of the Company's employees and customers while maintaining the operational and financial integrity of the Bank. Non-essential employees were transitioned to a work-from-home environment, strict protocols for employees deemed essential were adopted to ensure adequate social distancing and all Bank facilities are receiving incremental cleaning and sanitization. The Company has restricted access to its bank lobbies and are allowing customers in by appointment only while providing essential banking services through the Bank's drive-through windows and digital platforms. The Company's operations center provides essential employees the necessary room to social distance while seamlessly supporting the Bank's customers and performing the critical tasks necessary to keep the Bank's operations running efficiently. The facility also provides support for the Bank's employees who are working remotely.

While the duration of the COVID-19 pandemic and the scope of its impact on the economy is uncertain, the Bank is proactively working with its borrowers in those sectors most affected by the pandemic and offering loan modifications to borrowers who are or may be unable to meet their contractual payment obligations because of the effects of the COVID-19 pandemic. The Bank has also assigned its Chairman, Chief Executive Officer, Chief Credit Officer and Chief Lending Officer to partner with the Bank's lenders on those borrowers most impacted by the pandemic to ensure the Company is proactively addressing those credits with the appropriate oversight and modifications when warranted, helping those borrowers bridge the gap until the economy begins to normalize. As part of the Bank's efforts to support its customers and protect the Bank, and in accordance with the Joint Interagency Regulatory Guidance, the Bank has offered varying forms of loan modifications ranging from 90-day payment deferrals to 6- to 12-month interest only terms to provide borrowers relief. As of March 31, 2020, total loan modifications attributed to the COVID-19 pandemic were approximately $155 million, or 7%, of the Company's loan portfolio. As of May 1st, 2020, total loan modifications attributed to COVID-19 had increased to approximately $390 million, or 18%, of the Company's loan portfolio.

The Bank has also been active in assisting its customers in accessing the Paycheck Protection Program (the "PPP") administered by the Small Business Administration (the "SBA") and created under the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"). As of May 5th, 2020, the Bank had originated over $210 million in PPP loans for over 1,800 customers whose PPP loan applications were approved and funded. The Bank intends to continue accepting and processing new PPP loan applications for as long as funding for the program remains available. The Bank will utilize its lines of credit with the Federal Home Loan Bank of Dallas (the "FHLB") and/or the Federal Reserve Bank of Dallas (the "FRB") to supplement funding for these loans as needed. Helping City Bank's customers access PPP loans is just one way that the Bank has been helping its customers and communities during this challenging time. City Bank has also been a supporter of the South Plains and Permian Basin food banks and recently increased its financial support given the challenging economic environment for so many.

The Company and City Bank remain well capitalized. We also have excess liquidity on hand as well as over $450 million in unpledged securities and access to lines of credit with the FHLB, the FRB and other banks.

Stock Repurchase Program

The Company temporarily suspended its stock repurchase program in response to the ongoing COVID-19 pandemic. Suspending the stock repurchase program will allow the Company to preserve capital and provide liquidity to meet the credit needs of the customers, small businesses and local communities served by the Company and City Bank. The Company believes that it remains strong and well-capitalized, and the Company may reinstate the stock repurchase program in the future.

Highlights

We had net income of $7.1 million for the three months ended March 31, 2020, compared to net income of $4.8 million for the three months ended March 31, 2019. Return on average equity was 9.00% and return on average assets was 0.89% for the three months ended March 31, 2020, compared to 8.98% and 0.71%, respectively, for the three months ended March 31, 2019.

Our total assets decreased $20.6 million, or 0.6%, to $3.22 billion at March 31, 2020, compared to $3.24 billion at December 31, 2019. Our gross loans held for investment decreased $34.8 million, or 1.6%, to $2.11 billion at March 31, 2020, compared to $2.14 billion at December 31, 2019. Our securities portfolio increased $27.1 million, or 3.8%, to $734.8 million at March 31, 2020, compared to $707.7 million at December 31, 2019. Total deposits decreased $31.0 million, or 1.1%, to $2.67 billion at March 31, 2020, compared to $2.70 billion at December 31, 2019.

Results of Operations

Net Income

Net income increased by $2.3 million to $7.1 million for the three months ended March 31, 2020, compared to $4.8 million for the three months ended March 31, 2019. This increase was primarily the result of an increase of $5.7 million in net interest income and an increase of $6.8 million in noninterest income, partially offset by an increase of $5.6 million in the provision for loan losses and an increase of $4.0 million in noninterest expense.

Net Interest Income

Net interest income is the principal source of the Company's net income and represents the difference between interest income (interest and fees earned on assets, primarily loans and investment securities) and interest expense (interest paid on deposits and borrowed funds). We generate interest income from interest-earning assets that we own, including loans and investment securities. We incur interest expense from interest-bearing liabilities, including interest-bearing deposits and other borrowings, notably FHLB advances and subordinated notes. To evaluate net interest income, we measure and monitor (i) yields on our loans and other interest-earning assets, (ii) the costs of our deposits and other funding sources, (iii) our net interest spread and (iv) our net interest margin. Net interest spread is the difference between rates earned on interest-earning assets and rates paid on interest-bearing liabilities. Net interest margin is calculated as the annualized net interest income on a fully tax-equivalent basis divided by average interest-earning assets.

Changes in the market interest rates and interest rates we earn on interest-earning assets or pay on interest-bearing liabilities, as well as the volume and types of interest-earning assets, interest-bearing and noninterest-bearing liabilities, are usually the largest drivers of periodic changes in net interest spread, net interest margin and net interest income.

The following tables present, for the periods indicated, information about: (i) weighted average balances, the total dollar amount of interest income from interest-earning assets and the resultant average yields; (ii) average balances, the total dollar amount of interest expense on interest-bearing liabilities and the resultant average rates; (iii) net interest income; (iv) the interest rate spread; and (v) the net interest margin. For purposes of this table, interest income, net interest margin and net interest spread are shown on a fully tax-equivalent basis.

	Three Months Ended March 31,					
	2020			2019		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
	(Dollars in thousands)					
Assets:						
Interest-earning assets:						
Total loans[1]	$ 2,167,015	$ 31,055	5.76%	$ 1,955,783	$ 28,141	5.84%
Investment securities – taxable	560,677	3,592	2.58	309,670	2,109	2.76
Investment securities – non-taxable	78,933	501	2.55	32,172	286	3.61
Other interest-earning assets [2]	151,133	734	1.95	243,610	1,571	2.62
Total interest-earning assets	2,957,758	35,882	4.88	2,541,235	32,107	5.12
Noninterest-earning assets	250,659			176,437		
Total assets	$ 3,208,417			$ 2,717,672		
Liabilities and Shareholders' Equity:						
Interest-bearing liabilities:						
NOW, savings and money market deposits	$ 1,545,937	$ 2,656	0.69%	$ 1,470,199	$ 4,534	1.25%
Time deposits	353,471	1,627	1.85	309,687	1,355	1.77
Short-term borrowings	30,744	93	1.22	22,722	111	1.98
Notes payable & other longer-term borrowings	96,209	357	1.49	95,000	539	2.30
Subordinated debt securities	26,472	404	6.14	27,727	406	5.94
Junior subordinated deferrable interest debentures	46,393	401	3.48	46,393	513	4.48
Total interest-bearing liabilities	$ 2,099,226	$ 5,538	1.06%	$ 1,971,728	$ 7,458	1.53%
Noninterest-bearing liabilities:						
Noninterest-bearing deposits	$ 765,637			$ 501,120		
Other liabilities	27,152			29,153		
Total noninterest-bearing liabilities	792,789			530,273		
Shareholders' equity	316,402			215,671		
Total liabilities and shareholders' equity	$ 3,208,417			$ 2,717,672		
Net interest income		$ 30,344			$ 24,649	
Net interest spread			3.82%			3.59%
Net interest margin[3]			4.13%			3.93%

(1) Average loan balances include nonaccrual loans and loans held for sale.
(2) Includes income and average balances for interest-earning deposits at other banks, nonmarketable securities, federal funds sold and other miscellaneous interest-earning assets.
(3) Net interest margin is calculated as the annualized net interest income, on a fully tax-equivalent basis, divided by average interest-earning assets.

Increases and decreases in interest income and interest expense result from changes in average balances (volume) of interest-earning assets and interest-bearing liabilities, as well as changes in average interest rates. The following tables sets forth the effects of changing rates and volumes on our net interest income during the period shown. Information is provided with respect to (i) effects on interest income attributable to changes in volume (change in volume multiplied by prior rate) and (ii) effects on interest income attributable to changes in rate (changes in rate multiplied by prior volume). Change applicable to both volume and rate have been allocated to volume.

	Three Months Ended March 31, 2020 over 2019		
	Change due to:		Total Variance
	Volume	Rate	
	(Dollars in thousands)		
Interest-earning assets:			
Loans	$ 3,039	$ (125)	$ 2,914
Investment securities – taxable	1,709	(226)	1,483
Investment securities – non-taxable	416	(201)	215
Other interest-earning assets	(596)	(241)	(837)
Total increase (decrease) in interest income	4,568	(793)	3,775
Interest-bearing liabilities:			
NOW, Savings, MMDAs	234	(2,112)	(1,878)
Time deposits	192	80	272
Short-term borrowings	39	(57)	(18)
Notes payable & other borrowings	7	(189)	(182)
Subordinated debt securities	(18)	16	(2)

Junior subordinated deferrable interest debentures	—	(112)	(112)
Total increase (decrease) interest expense:	454	(2,374)	(1,920)
Increase (decrease) in net interest income	$ 4,114	$ 1,581	$ 5,695

Net interest income for the three months ended March 31, 2020 was $30.2 million, compared to $24.5 million for the three months ended March 31, 2019, an increase of $5.7 million, or 23.0%. The increase in net interest income was comprised of a $3.7 million, or 11.7%, increase in interest income and by a $2.0 million, or 25.7%, decrease in interest expense. The growth in interest income was primarily attributable to a $211.2 million, or 10.8%, increase in average loans outstanding for the three-month period ended March 31, 2020, compared to the three-month period ended March 31, 2019. The increase in average loans outstanding was primarily due to our acquisition of West Texas State Bank ("WTSB") in November 2019. The average of all other interest-earning assets during this period grew $205.3 million. The interest income on the $416.5 million growth in average interest-earning assets was partially offset by a decrease of 24 basis points in yield on earning assets.

The $2.0 million decrease in interest expense for the three months ended March 31, 2020 was primarily related to a 47 basis point decrease in the rate paid on interest-bearing liabilities, partially offset by an increase of $119.5 million, or 6.7%, in average interest-bearing deposits over the same period in 2019. Additionally, average noninterest-bearing demand deposits increased to $792.8 million at March 31, 2020 from $530.3 million at March 31, 2019. The increase in average deposits from March 31, 2019 to March 31, 2020 was due primarily to the WTSB acquisition.

For the three months ended March 31, 2020, net interest margin and net interest spread were 4.13% and 3.82%, respectively, compared to 3.93% and 3.59% for the same period in 2019, which reflects the increase in interest income and the decrease in interest expense discussed above.

Provision for Loan Losses

Credit risk is inherent in the business of making loans. We establish an allowance for loan losses through charges to earnings, which are shown in the statements of income as the provision for loan losses. Specifically identifiable and quantifiable known losses are promptly charged off against the allowance. The provision for loan losses is determined by conducting a quarterly evaluation of the adequacy of our allowance for loan losses and charging the shortfall or excess, if any, to the current quarter's expense. This has the effect of creating variability in the amount and frequency of charges to our earnings. The provision for loan losses and the amount of allowance for each period are dependent upon many factors, including loan growth, net charge offs, changes in the composition of the loan portfolio, delinquencies, management's assessment of the quality of the loan portfolio, the valuation of problem loans and the general economic conditions in our market areas.

The provision for loan losses for the three months ended March 31, 2020 was $6.2 million, compared to $608,000 for the three months ended March 31, 2019. The increase in the provision for loan losses in the first quarter of 2020 compared to the same quarter in 2019 is primarily a result of the uncertain economic effects from the ongoing COVID-19 pandemic as well as the decline in oil and gas prices. The allowance for loan losses as a percentage of loans held for investment was 1.38% at March 31, 2020 and 1.13% at December 31, 2019. Further discussion of the allowance for loan losses is noted below.

Noninterest Income

While interest income remains the largest single component of total revenues, noninterest income is an important contributing component. The largest portion of our noninterest income is associated with our mortgage banking activities. Other sources of noninterest income include service charges on deposit accounts, bank card services and interchange fees, and income from insurance activities.

The following table sets forth the major components of our noninterest income for the periods indicated:

	Three Months Ended March 31,		
	2020	2019	Increase (Decrease)
	(Dollars in thousands)		
Noninterest income:			
Service charges on deposit accounts	$ 1,983	$ 1,905	$ 78
Income from insurance activities	1,159	1,750	(591)
Bank card services and interchange fees	2,238	2,010	228
Mortgage banking activities	8,753	4,866	3,887
Investment commissions	455	333	122
Fiduciary income	829	376	453
Gain on sale of securities	2,318	—	2,318
Other income and fees[1]	1,140	835	305
Total noninterest income	$ 18,875	$ 12,075	$ 6,800

(1) Other income and fees includes the increase in the cash surrender value of life insurance, safe deposit box rental, check printing, collections, wire transfer and other miscellaneous services.

Noninterest income for the three months ended March 31, 2020 was $18.9 million, compared to $12.1 million for the three months ended March 31, 2019, an increase of $6.8 million, or 56.3%. Income from mortgage banking activities increased $3.9 million, or 79.9%, to $8.8 million for the three months ended March 31, 2020 from $4.9 million for the three months ended March 31, 2019. The increase was primarily the result of an increase of $3.9 million in mortgage banking activities revenue, due to an increase of $95.2 million in mortgage loan originations during this period, and a $2.3 million gain on sale of securities in the first quarter of 2020. Fiduciary income increased $453,000, or 120.5%, to $829,000 for the three months ended March 31, 2020 from $376,000 for the three months ended March 31, 2019. The increase in fiduciary income was primarily due to new customer acquisition with estate executorship and trust management as the primary services in late third quarter 2019. Income from insurance activities decreased to $1.2 million for the three months ended March 31, 2020 from $1.8 million for the three months ended March 31, 2019 due to ASC 606 Revenue from Contracts with Customers becoming effective for the Company's interim reporting periods in March 2020. The result of adoption is that there is a delay in the annual cycle of revenue recognition for insurance activities as compared to previous years.

Noninterest Expense

The following table sets forth the major components of our noninterest expense for the periods indicated:

	Three Months Ended March 31, 2020	Three Months Ended March 31, 2019	Increase (Decrease)
	(Dollars in thousands)		
Noninterest expense:			
Salaries and employee benefits	$ 20,810	$ 19,125	$ 1,685
Occupancy expense, net	3,600	3,407	193
Professional services	1,572	1,706	(134)
Marketing and development	768	717	51
IT and data services	847	693	154
Bankcard expenses	1,052	724	328
Appraisal expenses	455	323	132
Other expenses(1)	4,907	3,341	1,566
Total noninterest expense	$ 34,011	$ 30,036	$ 3,975

(1) Other expenses include items such as telephone expenses, postage, courier fees, directors' fees, and insurance.

Noninterest expense for the three months ended March 31, 2020 was $34.0 million compared to $30.0 million for the three months ended March 31, 2019, an increase of $4.0 million, or 13.2%. Salaries and employee benefits increased $1.7 million, or 8.8%, from $19.1 million for the three months ended March 31, 2019 to $20.8 million for the three months ended March 31, 2020. This increase in salaries and employee benefits expense for the first quarter of 2020 compared to the first quarter of 2019 was primarily driven by the WTSB acquisition and increased commissions paid on the higher volume of mortgage loan originations. Other noninterest expenses increased $1.6 million for the three months ended March 31, 2020, compared to the same period in 2019. This increase was primarily due to core expenses for the acquired WTSB branches, higher commissions and other variable mortgage expenses as a result of increased production, $331,000 in data conversion expenses and $300,000 in computer equipment purchased in connection with upgrading the equipment at the acquired branches as well as at existing branches. The computer equipment purchases were expensed due to the individual items falling below the Company's capitalization threshold.

Financial Condition

Our total assets decreased $20.6 million, or 0.6%, to $3.22 billion at March 31, 2020, compared to $3.24 billion at December 31, 2019. Our gross loans held for investment decreased $34.8 million, or 1.6%, to $2.11 billion at March 31, 2020, compared to $2.14 billion at December 31, 2019. Our securities portfolio increased $27.1 million, or 3.8%, to $734.8 million at March 31, 2020, compared to $707.7 million at December 31, 2019. Total deposits decreased $31.0 million, or 1.1%, to $2.67 billion at March 31, 2020, compared to $2.70 billion at December 31, 2019.

Loan Portfolio

Our loans represent the largest portion of earning assets, greater than our securities portfolio or any other asset category, and the quality and diversification of the loan portfolio is an important consideration when reviewing the Company's financial condition. We originate substantially all of the loans in our portfolio, except certain loan participations that are independently underwritten by the Company prior to purchase.

The following table presents the balance and associated percentage of each major category in our gross loan portfolio at the dates indicated:

	March 31, 2020		December 31, 2019	
	Amount	% of Total	Amount	% of Total
	(Dollars in thousands)			
Commercial real estate	$ 641,739	30.4%	$ 658,195	30.7%
Commercial – specialized	303,116	14.4	309,505	14.4
Commercial – general	424,750	20.2	441,398	20.7
Consumer:				
1-4 family residential	356,540	16.9	362,796	16.9
Auto loans	212,912	10.1	215,209	10.0
Other consumer	72,162	3.4	74,000	3.5
Construction	97,586	4.6	82,520	3.8
Gross loans	2,108,805	100.0%	2,143,623	100.0%
Allowance for loan losses	(29,074)		(24,197)	
Net loans	$ 2,079,731		$ 2,119,426	

Loans held for investment decreased $34.8 million, or 1.6%, to $2.11 billion at March 31, 2020, compared to $2.14 billion at December 31, 2019. This decrease in our loans was primarily due to $34.5 million in seasonal agricultural production loan net paydowns in the first quarter of 2020.

The Bank is primarily involved in real estate, commercial, agricultural and consumer lending activities with customers throughout Texas and Eastern New Mexico. We have a collateral concentration, as 67.1% of our loans held for investment were secured by real property as of March 31, 2020, compared to 65.5% as of December 31, 2019. We believe that these loans are not concentrated in any one single property type and that they are geographically dispersed throughout the areas we serve. Although the Bank has diversified portfolios, its debtors' ability to honor their contracts is substantially dependent upon the general economic conditions of the markets in which it operates, which consist primarily of agribusiness, wholesale/retail, oil and gas and related businesses, healthcare industries and institutions of higher education.

We have established concentration limits in the loan portfolio for commercial real estate loans and unsecured lending, among other loan types. All loan types are within established limits. We use underwriting guidelines to assess the borrowers' historical cash flow to determine debt service, and we further stress test the debt service under higher interest rate scenarios. Financial and performance covenants are used in commercial lending to allow us to react to a borrower's deteriorating financial condition, should that occur.

Commercial Real Estate. Our commercial real estate portfolio includes loans for commercial property that is owned by real estate investors, construction loans to build owner-occupied properties, and loans to developers of commercial real estate investment properties and residential developments. Commercial real estate loans are subject to underwriting standards and processes similar to our commercial loans. These loans are underwritten primarily based on projected cash flows for income-producing properties and collateral values for non-income-producing properties. The repayment of these loans is generally dependent on the successful operation of the property securing the loans or the sale or refinancing of the property. Real estate loans may be adversely affected by conditions in the real estate markets or in the general economy. The properties securing our real estate portfolio are diversified by type and geographic location. This diversity helps reduce the exposure to adverse economic events that affect any single market or industry.

Commercial real estate loans decreased $16.5 million, or 2.5%, to $641.7 million as of March 31, 2020 from $658.2 million as of December 31, 2019. The decrease in commercial real estate loans during this period was mostly driven by the early payoff of several loans, as well as normal scheduled principal reductions outpacing our organic loan growth.

Commercial – General and Specialized. Commercial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably. Underwriting standards have been designed to determine whether the borrower possesses sound business ethics and practices, to evaluate current and projected cash flows to determine the ability of the borrower to repay their obligations, and to ensure appropriate collateral is obtained to secure the loan. Commercial loans are primarily made based on the identified cash flows of the borrower and, secondarily, on the underlying collateral provided by the borrower. Most commercial loans are secured by the assets being financed or other business assets, such as real estate, accounts receivable, or inventory, and typically include personal guarantees. Owner-occupied real estate is included in commercial loans, as the repayment of these loans is generally dependent on the operations of the commercial borrower's business rather than on income-producing properties or the sale of the properties. Commercial loans are grouped into two distinct sub-categories: specialized and general. Commercial related loans that are considered "specialized" include agricultural production and real estate loans, energy loans, and finance, investment, and insurance loans. Commercial related loans that contain a broader diversity of borrowers, sub-industries, or serviced industries are grouped into the "general category." These include goods, services, restaurant and retail, construction, and other industries.

Commercial specialized loans decreased $6.4 million, or 2.1%, to $303.1 million as of March 31, 2020 from $309.5 million as of December 31, 2019. This decrease was primarily due to $34.5 million in seasonal agricultural production loan net paydowns, partially offset by an increase of $28.7 million in energy loans.

Commercial general loans decreased $16.6 million, or 3.8%, to $424.8 million as of March 31, 2020 from $441.4 million as of December 31, 2019. The decrease in commercial general loans was primarily due to the early payoff of two relationships totaling $22.2 million during the first quarter of 2020, partially offset by organic loan growth.

Consumer. We utilize a computer-based credit scoring analysis to supplement our policies and procedures in underwriting consumer loans. Our loan policy addresses types of consumer loans that may be originated and the collateral, if secured, which must be perfected. The relatively smaller individual dollar amounts of consumer loans that are spread over numerous individual borrowers also minimize our risk. Residential real estate loans are included in consumer loans. We generally require mortgage title insurance and hazard insurance on these residential real estate loans.

Consumer and other loans decreased $10.4 million, or 1.6%, to $641.6 million as of March 31, 2020, from $652.0 million as of December 31, 2019. The decreases in these loans were primarily a result of a net decrease of $6.3 million in 1-4 family residential loans as refinancing activities caused paydowns to exceed new growth. Additionally, indirect auto loan originations slowed in March as the economy began to worsen. As of March 31, 2020, our consumer loan portfolio was comprised of $356.5 million in 1-4 family residential loans, $212.9 million in auto loans, and $72.2 million in other consumer loans.

Construction. Loans for residential construction are for single-family properties to developers, builders, or end-users. These loans are underwritten based on estimates of costs and completed value of the project. Funds are advanced based on estimated percentage of completion for the project. Performance of these loans is affected by economic conditions as well as the ability to control costs of the projects.

Construction loans increased $15.1 million, or 18.3%, to $97.6 million as of March 31, 2020 from $82.5 million as of December 31, 2019. The increase resulted from continued organic growth as well advances on lines of credit to fund construction progress.

Allowance for Loan Losses

The allowance for loan losses provides a reserve against which loan losses are charged as those losses become evident. Management evaluates the appropriate level of the allowance for loan losses on a quarterly basis. The analysis takes into consideration the results of an ongoing loan review process, the purpose of which is to determine the level of credit risk within the portfolio and to ensure proper adherence to underwriting and documentation standards. Additional allowances are provided to those loans which appear to represent a greater than normal exposure to risk. The quality of the loan portfolio and the adequacy of the allowance for loan losses is reviewed by regulatory examinations and the Company’s internal and external loan reviews. The allowance for loan losses consists of two elements: (1) specific valuation allowances established for probable losses on specific loans and (2) historical valuation allowances calculated based on historical loan loss experience for similar loans with similar characteristics and trends, judgmentally adjusted for general economic conditions and other qualitative risk factors internal and external to the Company.

To determine the adequacy of the allowance for loan losses, the loan portfolio is broken into categories based on loan type. Historical loss experience factors by category, adjusted for changes in trends and conditions, are used to determine an indicated allowance for each portfolio category. These factors are evaluated and updated based on the composition of the specific loan portfolio. Other considerations include volumes and trends of delinquencies, nonaccrual loans, levels of bankruptcies, criticized and classified loan trends, expected losses on real estate secured loans, new credit products and policies, economic conditions, concentrations of credit risk, and the experience and abilities of the Company’s lending personnel. In addition to the portfolio evaluations, impaired loans with a balance of $250,000 or more are individually evaluated based on facts and circumstances of the loan to determine if a specific allowance amount may be necessary. Specific allowances may also be established for loans whose outstanding balances are below the above threshold when it is determined that the risk associated with the loan differs significantly from the risk factor amounts established for its loan category.

The allowance for loan losses was $29.1 million at March 31, 2020, compared to $24.2 million at December 31, 2019, an increase of $4.9 million, or 20.2%. The increase is primarily a result of management’s estimate of economic effects of the COVID-19 pandemic as well as the decline in oil and gas prices. These effects caused us to downgrade the risk ratings on some of the more at-risk sectors in our portfolio, primarily energy and hospitality during the first quarter of 2020.

The following table provides an analysis of the allowance for loan losses at the dates indicated.

	Beginning Balance	Charge-offs	Recoveries	Provision	Ending Balance
	(Dollars in thousands)				
Three Months Ended March 31, 2020					
Commercial real estate	$ 5,049	$ —	$ 108	$ 2,035	$ 7,192
Commercial – specialized	2,287	(14)	64	2,218	4,555
Commercial – general	9,609	(848)	17	(798)	7,980
Consumer:					
1-4 family residential	2,093	—	—	651	2,744
Auto loans	3,385	(441)	52	1,316	4,312
Other consumer	1,341	(367)	72	593	1,639
Construction	433	—	—	219	652
Total	$ 24,197	$ (1,670)	$ 313	$ 6,234	$ 29,074

	Beginning Balance	Charge-offs	Recoveries	Provision	Ending Balance
	(Dollars in thousands)				
Three Months Ended March 31, 2019					
Commercial real estate	$ 5,579	$ —	$ 108	$ (352)	$ 5,335
Commercial – specialized	2,516	(33)	23	(179)	2,327
Commercial – general	8,173	(4)	73	262	8,504
Consumer:					
1-4 family residential	2,249	(19)	30	156	2,416
Auto loans	2,994	(259)	33	299	3,067
Other consumer	1,192	(279)	49	212	1,174
Construction	423	(75)	—	210	558
Total	$ 23,126	$ (669)	$ 316	$ 608	$ 23,381

Net charge-offs totaled $1.4 million and were 0.25% (annualized) of average loans outstanding for the three months ended March 31, 2020, compared to $353,000 and 0.07% for the three months ended March 31, 2019. The increase in net charge-offs in the first quarter of 2020 was primarily the result of a $518,000 charge-off on a retail commercial relationship as well as two smaller commercial – general charge-offs during the first quarter of 2020. The allowance for loan losses as a percentage of loans held for investment was 1.38% at March 31, 2020 and 1.13% at December 31, 2019.

While the entire allowance for loan losses is available to absorb losses from any part of our loan portfolio, the following table sets forth the allocation of the allowance for loan losses for the periods presented and the percentage of allowance in each classification to total allowance:

	March 31, 2020		December 31, 2019	
	Amount	% of Total	Amount	% of Total
	(Dollars in thousands)			
Commercial real estate	$ 7,192	24.7%	$ 5,049	20.9%
Commercial – specialized	4,555	15.7	2,287	9.5
Commercial – general	7,980	27.5	9,609	39.7
Consumer:				
1-4 family residential	2,744	9.4	2,093	8.6
Auto loans	4,312	14.8	3,385	14.0
Other consumer	1,639	5.6	1,341	5.5
Construction	652	2.3	433	1.8
Total allowance for loan losses	$ 29,074	100.0%	$ 24,197	100.0%

Asset Quality

Loans are considered delinquent when principal or interest payments are past due 30 days or more. Delinquent loans may remain on accrual status between 30 days and 90 days past due. Loans on which the accrual of interest has been discontinued are designated as nonaccrual loans. Typically, the accrual of interest on loans is discontinued when principal or interest payments are past due 90 days or when, in the opinion of management, there is a reasonable doubt as to collectability in the normal course of business. When loans are placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Income on nonaccrual loans is subsequently recognized only to the extent that cash is received and the loan's principal balance is deemed collectible. Loans are restored to accrual status when loans become well-secured and management believes full collectability of principal and interest is probable.

A loan is considered impaired when it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. Impaired loans include loans on nonaccrual status and performing restructured loans. Income from loans on nonaccrual status is recognized to the extent cash is received and when the loan's principal balance is deemed collectible. Depending on a particular loan's circumstances, we measure impairment of a loan based upon either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the collateral less estimated costs to sell if the loan is collateral dependent. A loan is considered collateral dependent when repayment of the loan is based solely on the liquidation of the collateral. Fair value, where possible, is determined by independent appraisals, typically on an annual basis. Between appraisal periods, the fair value may be adjusted based on specific events, such as if deterioration of quality of the collateral comes to our attention as part of our problem loan monitoring process, or if discussions with the borrower lead us to believe the last appraised value no longer reflects the actual market for the collateral. The impairment amount on a collateral-dependent loan is charged-off to the allowance if deemed not collectible and the impairment amount on a loan that is not collateral-dependent is set up as a specific reserve.

Real estate we acquire as a result of foreclosure or by deed-in-lieu of foreclosure is classified as other real estate owned ("OREO") until sold and is initially recorded at fair value less costs to sell when acquired, establishing a new cost basis.

The following table sets forth the allocation of our nonperforming assets among our different asset categories as of the dates indicated. Nonperforming loans include nonaccrual loans and loans past due 90 days or more.

	March 31, 2020	December 31, 2019
	(Dollars in thousands)	
Nonaccrual loans:		
Commercial real estate	$ 1,327	$ 162
Commercial – specialized	1,610	1,172
Commercial – general	2,163	2,254
Consumer:		
1-4 family residential	800	1,105
Auto loans	—	—
Other consumer	—	—
Construction	—	—
Total nonaccrual loans	5,900	4,693
Past due loans 90 days or more and still accruing	1,212	1,352
Total nonperforming loans	7,112	6,045
Other real estate owned	1,944	1,883
Total nonperforming assets	$ 9,056	$ 7,928
Restructured loans - nonaccrual[1]	$ 102	$ 436
Restructured loans - accruing	$ 1,775	$ 1,804

(1) Restructured loans, nonaccrual, are included in nonaccrual loans which are a component of nonperforming loans.

In cases where a borrower experiences financial difficulties and we make certain concessionary modifications to contractual terms, the loan is classified as a troubled debt restructuring ("TDR"). Included in certain loan categories of impaired loans are TDRs on which we have granted certain material concessions to the borrower as a result of the borrower experiencing financial difficulties. The concessions granted by us may include, but are not limited to: (1) a modification in which the maturity date, timing of payments or frequency of payments is modified, (2) an interest rate lower than the current market rate for new loans with similar risk, or (3) a combination of the first two factors.

If a borrower on a restructured accruing loan has demonstrated performance under the previous terms, is not experiencing financial difficulty and shows the capacity to continue to perform under the restructured terms, the loan will remain on accrual status. Otherwise, the loan will be placed on nonaccrual status until the borrower demonstrates a sustained period of performance, which generally requires six consecutive months of payments. Loans identified as TDRs are evaluated for impairment using the present value of the expected cash flows or the estimated fair value of the collateral, if the loan is collateral dependent. The fair value is determined, when possible, by an appraisal of the property less estimated costs related to liquidation of the collateral. The appraisal amount may also be adjusted for current market conditions. Adjustments to reflect the present value of the expected cash flows or the estimated fair value of collateral dependent loans are a component in determining an appropriate allowance for loan losses, and as such, may result in increases or decreases to the provision for loan losses in current and future earnings.

We had no loans restructured as TDRs during the first three months of 2020 or 2019. TDRs are excluded from our nonperforming loans unless they otherwise meet the definition of nonaccrual loans or are past due 90 days or more.

COVID-19 Industry Exposures. The Company's COVID-19 industry exposures at March 31, 2020 were:

- Restaurant and retail owner-occupied loans totaled $83.0 million (3.9% of total loans). The average loan size is $285,000. There was $913,000 in classified loans and $778,000 in loans past due greater than 30 days. The related allowance for loan losses to total restaurant and retail owner-occupied loans is 1.98%.

- Hospitality and assisted living center loans totaled $113.5 million (5.4% of total loans). The average loan size is $2.7 million. There was $2.8 million in classified loans and no loans past due more than 30 days. The related allowance for loan losses to total hospitality and assisted living center loans is 3.36%.

Oil and Gas Exposures. The Company's direct energy sector loans totaled $90.0 million (4.3% of total loans) at March 31, 2020. There was $857,000 in nonaccrual loans. Management has expanded the monitoring of the loans in this category. The related allowance for loan losses to direct engery loans is 3.97%.

Securities Portfolio

The securities portfolio is the second largest component of the Company's interest-earning assets, and the structure and composition of this portfolio is important to an analysis of the financial condition of the Company. The portfolio serves the following purposes: (i) it provides a source of pledged assets for securing certain deposits and borrowed funds, as may be required by law or by specific agreement with a depositor or lender; (ii) it provides liquidity to even out cash flows from the loan and deposit activities of customers; (iii) it can be used as an interest rate risk management tool, since it provides a large base of assets, the maturity and interest rate characteristics of which can be changed more readily than the loan portfolio to better match changes in the deposit base and other funding sources of the Company; and (iv) it is an alternative interest-earning asset when loan demand is weak or when deposits grow more rapidly than loans.

The securities portfolio consists of securities classified as either held-to-maturity or available-for-sale. All held-to-maturity securities are reported at amortized cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period to maturity. All available-for-sale securities are reported at fair value. Securities available-for-sale consist primarily of state and municipal securities, mortgage-backed securities and U.S. government sponsored agency securities. We determine the appropriate classification at the time of purchase.

Our securities portfolio increased $27.1 million, or 3.8%, to $734.8 million at March 31, 2020, compared to $707.7 million at December 31, 2019. The increase was due to the purchase of $112.4 million in Texas municipal securities, partially offset by the sale of $92.2 million in mortgage-backed. The sale of the mortgage-backed securities occurred in January 2020 and generated a gain of $2.3 million.

The following table summarizes the fair value of the securities portfolio as of the dates presented.

	March 31, 2020			December 31, 2019		
	Amortized Cost	Fair Value	Unrealized Gain/(Loss)	Amortized Cost	Fair Value	Unrealized Gain/(Loss)
	(Dollars in thousands)					
Available-for-sale						
U.S. government and agencies	$ 4,750	$ 4,835	$ 85	$ 4,750	$ 4,807	$ 57
State and municipal	206,206	209,654	3,448	94,512	94,692	180
Mortgage-backed securities	361,847	376,081	14,234	463,899	464,516	617
Collateralized mortgage obligations	107,380	107,410	30	107,443	107,289	(154)
Asset-backed and other amortizing securities	34,524	36,811	2,287	35,833	36,346	513
Total available-for-sale	$ 714,707	$ 734,791	$ 20,084	$ 706,437	$ 707,650	$ 1,213

Certain securities have fair values less than amortized cost and, therefore, contain unrealized losses. At March 31, 2020, we evaluated the securities which had an unrealized loss for other-than-temporary impairment and determined all declines in value to be temporary. We anticipate full recovery of amortized cost with respect to these securities by maturity, or sooner in the event of a more favorable market interest rate environment. We do not intend to sell these securities and it is not probable that we will be required to sell them before recovery of the amortized cost basis, which may be at maturity.

The following table sets forth certain information regarding contractual maturities and the weighted average yields of our investment securities as of the date presented. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligation with or without call or prepayment penalties.

	As of March 31, 2020							
	Due in One Year or Less		Due after One Year Through Five Years		Due after Five Years Through Ten Years		Due after Ten Years	
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield
	(Dollars in thousands)							
Available-for-sale								
U.S. government and agencies	$ 4,750	2.75%	$ —	0.00%	$ —	—%	$ —	—%
State and municipal	1,022	1.71	—	0.00	15,730	2.16	189,454	2.52
Mortgage-backed securities	—	—	901	1.62	16,242	2.01	344,704	2.45
Collateralized mortgage obligations	—	0.00	—	0.00	—	0.00	107,380	1.41
Asset-backed and other amortizing securities	—	—	—	—	—	—	34,524	2.82
Total available-for-sale	$ 5,772	2.75%	$ 901	1.62%	$ 31,972	2.08%	$ 676,062	2.32%

	As of December 31, 2019							
	Due in One Year or Less		Due after One Year Through Five Years		Due after Five Years Through Ten Years		Due after Ten Years	
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield
	(Dollars in thousands)							
Available-for-sale								
U.S. government and agencies	$ —	0.00%	$ 4,750	2.75%	$ —	—%	$ —	—%
State and municipal	470	4.00	1,028	1.71	14,206	2.08	78,808	2.90
Mortgage-backed securities	—	—	1,009	1.60	23,513	2.18	439,377	2.56
Collateralized mortgage obligations	——	0.00	—	0.00	—	0.00	107,443	2.26
Asset-backed and other amortizing securities	—	—	—	—	—	—	35,833	2.82
Total available-for-sale	$ 470	4.00%	$ 6,787	2.42%	$ 37,719	2.15%	$ 661,461	2.56%

Deposits

Deposits represent the Company's primary and most vital source of funds. We offer a variety of deposit products including demand deposits accounts, interest-bearing products, savings accounts and certificate of deposits. We put continued effort into gathering noninterest-bearing demand deposit accounts through loan production, customer referrals, marketing staffs, mobile and online banking and various involvements with community networks.

Total deposits at March 31, 2020 were $2.67 billion, representing a decrease of $31.0 million, or 1.1%, compared to $2.70 billion at December 31, 2019. As of March 31, 2020, 27.8% of total deposits were comprised of noninterest-bearing demand accounts, 59.5% of interest-bearing non-maturity accounts and 12.7% of time deposits.

The following table shows the deposit mix as of the dates presented:

	March 31, 2020		December 31, 2019	
	Amount	% of Total	Amount	% of Total
	(Dollars in thousands)			
Noninterest-bearing deposits	$ 740,946	27.8%	$ 790,921	29.3%
NOW and other transaction accounts	311,999	11.7	318,379	11.8
Money market and other savings	1,274,141	47.8	1,231,534	45.7
Time deposits	338,762	12.7	356,023	13.2
Total deposits	$ 2,665,848	100.0%	$ 2,696,857	100.0%

The following tables set forth the remaining maturity of time deposits of $100,000 and greater as of the date indicated:

(Dollars in thousands)	March 31, 2020
Time deposits $100,000 or greater with remaining maturity of:	
Three months or less	$ 43,562
After three months through six months	25,046
After six months through twelve months	55,197
After twelve months	129,269
Total	$ 253,074

Borrowed Funds

In addition to deposits, we utilize advances from the FHLB and other borrowings as a supplementary funding source to finance our operations.

FHLB Advances. The FHLB allows us to borrow, both short and long-term, on a blanket floating lien status collateralized by first mortgage loans and commercial real estate loans as well as FHLB stock. At March 31, 2020 and December 31, 2019, we had total remaining borrowing capacity from the FHLB of $504.8 million and $394.3 million, respectively.

The following table sets forth our FHLB borrowings as of and for the periods indicated:

	As of/For the Three Months Ended March 31,	
	2020	**2019**
	(Dollars in thousands)	
Amount outstanding at end of the period	$ 95,000	$ 95,000
Weighted average interest rate at end of the period	0.76%	2.32%
Maximum month-end balance during the period	$ 95,000	$ 95,000
Average balance outstanding during the period	$ 95,000	$ 95,000
Weighted average interest rate during the period	1.51%	2.30%

Federal Reserve Bank of Dallas. The Bank has a line of credit with the FRB. The amount of the line is determined on a monthly basis by the FRB. The line is collateralized by a blanket floating lien on all agriculture, commercial and consumer loans. The amount of the line was $540.6 million and $547.0 million at March 31, 2020 and December 31, 2019, respectively.

The following table sets forth our FRB borrowings as of and for the periods indicated:

	As of/For the Three Months Ended March 31,	
	2020	**2019**
	(Dollars in thousands)	
Amount outstanding at end of the period	$ —	$ —
Weighted average interest rate at end of the period	0.00%	0.00%
Maximum month-end balance during the period	$ —	$ —
Average balance outstanding during the period	$ 1,209	$ —
Weighted average interest rate during the period	0.25%	0.00%

Lines of Credit. The Bank has uncollateralized lines of credit with multiple banks as a source of funding for liquidity management. The total amount of the lines was $135.0 million as of March 31, 2020 and December 31, 2019. The lines were not used during the three or three month periods ended March 31, 2020 or the three or three month periods ending March 31, 2019.

Subordinated Debt Securities. In December 2018, the Company issued $26.5 million in subordinated debt securities. Securities totaling $12.4 million have a maturity date of December 2028 and an average fixed rate of 5.74% for the first five years. The remaining $14.1 million of securities have a maturity date of December 2030 and an average fixed rate of 6.41% for the first seven years. After the fixed rate periods, all securities will float at the *Wall Street Journal* prime rate, with a floor of 4.5% and a ceiling of 7.5%. These securities pay interest quarterly, are unsecured, and may be called by the Company at any time after the remaining maturity is five years or less. Additionally, these securities qualify for tier 2 capital treatment, subject to regulatory limitations. The balance of subordinated debt securities as of March 31, 2020 and December 31, 2019 was $26.5 million.

Junior Subordinated Deferrable Interest Debentures and Trust Preferred Securities. Between March 2004 and June 2007, the Company formed three wholly-owned statutory business trusts solely for the purpose of issuing trust preferred securities, the proceeds of which were invested in junior subordinated deferrable interest debentures. The trusts are not consolidated and the debentures issued by the Company to the trusts are reflected in the Company's consolidated balance sheets. The Company records interest expense on the debentures in its consolidated financial statements. The amount of debentures outstanding was $46.4 million at March 31, 2020 and December 31, 2019. The Company has the right, as has been exercised in the past, to defer payments of interest on the securities for up to twenty consecutive quarters. During such time, corporate dividends may not be paid. The Company is current in its interest payments on the debentures.

The chart below indicates certain information about each of the statutory trusts and the junior subordinated deferrable interest debentures, including the date the junior subordinated deferrable interest debentures were issued, outstanding amounts of trust preferred securities and junior subordinated deferrable interest debentures, the maturity date of the junior subordinated deferrable interest debentures, the interest rates on the junior subordinated deferrable interest debentures and the investment banker.

Name of Trust	Issue Date	Amount of Trust Preferred Securities	Amount of Debentures	Stated Maturity Date of Trust Preferred Securities and Debentures(1)	Interest Rate of Trust Preferred Securities and Debentures(2)(3)
		(Dollars in thousands)			
South Plains Financial Capital Trust III	2004	$ 10,000	$ 10,310	2034	3-mo. LIBOR + 265 bps; 4.46%
South Plains Financial Capital Trust IV	2005	20,000	20,619	2035	3-mo. LIBOR + 139 bps; 2.13%
South Plains Financial Capital Trust V	2007	15,000	15,464	2037	3-mo. LIBOR + 150 bps; 2.24%
Total		$ 45,000	$ 46,393		

(1) May be redeemed at the Company's option.
(2) Interest payable quarterly with principal due at maturity.
(3) Rate as of last reset date, prior to March 31, 2020.

Liquidity and Capital Resources

Liquidity

Liquidity refers to the measure of our ability to meet the cash flow requirements of depositors and borrowers, while at the same time meeting our operating, capital and strategic cash flow needs, all at a reasonable cost. We continuously monitor our liquidity position to ensure that assets and liabilities are managed in a manner that will meet all short-term and long-term cash requirements. We manage our liquidity position to meet the daily cash flow needs of customers, while maintaining an appropriate balance between assets and liabilities to meet the return on investment objectives of our shareholders.

Interest rate sensitivity involves the relationships between rate-sensitive assets and liabilities and is an indication of the probable effects of interest rate fluctuations on the Company's net interest income. Interest rate-sensitive assets and liabilities are those with yields or rates that are subject to change within a future time period due to maturity or changes in market rates. The model is used to project future net interest income under a set of possible interest rate movements. The Company's Investment/Asset Liability Committee (the "ALCO Committee"), reviews this information to determine if the projected future net interest income levels would be acceptable. The Company attempts to stay within acceptable net interest income levels.

Our liquidity position is supported by management of liquid assets and access to alternative sources of funds. Our liquid assets include cash, interest-bearing deposits in correspondent banks, federal funds sold, and fair value of unpledged investment securities. Other available sources of liquidity include wholesale deposits, and additional borrowings from correspondent banks, FHLB advances, and the Federal Reserve discount window. At March 31, 2020, the Bank had the capacity to borrow additional funds from the FHLB of up to approximately $504.8 million and the capacity to borrow from the Federal Reserve discount window of approximately $540.6 million. The Federal Reserve has also lowered the primary credit rate to 0.25% and extended the term to 90 days to enhance liquidity and encourage use of the Federal Reserve discount window. In addition, the Company maintains overnight fed fund purchase arrangements with correspondent banks.

Our short-term and long-term liquidity requirements are primarily met through cash flow from operations, redeployment of prepaying and maturing balances in our loan and investment portfolios, and increases in customer deposits. Other alternative sources of funds will supplement these primary sources to the extent necessary to meet additional liquidity requirements on either a short-term or long-term basis. Management believes that these sources of liquidity will provide adequate funding and liquidity to address the economic uncertainties caused by the ongoing COVID-19 pandemic. However, during this period management is closely monitoring the Company's potential liquidity needs, and if general economic conditions, the COVID-19 pandemic, or other events cause these sources of liquidity to become restricted or are eliminated, the Company may not be able to raise adequate funds or may incur substantially higher funding costs or operating restrictions in order to raise the necessary funds to support the Company's operations and growth.

Capital Requirements

Total shareholders' equity increased to $326.9 million as of March 31, 2020, compared to $306.2 million as of December 31, 2019, an increase of $20.7 million, or 6.8%. The increase from December 31, 2019 was primarily the result of $7.1 million in net earnings for the three months ended March 31, 2020, and a change in accumulated other comprehensive income of $13.9 million, net of tax.

We are subject to various regulatory capital requirements administered by the federal and state banking regulators. Failure to meet regulatory capital requirements may result in certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on our financial statements. Under capital adequacy guidelines and the regulatory framework for "prompt corrective action," we must meet specific capital guidelines that involve quantitative measures of our assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting policies. The capital amounts and classifications are subject to qualitative judgments by the federal banking regulators about components, risk weightings and other factors. Qualitative measures established by regulation to ensure capital adequacy required us to maintain minimum amounts and ratio of common equity tier 1 ("CET1") capital, tier 1 capital and total capital to risk-weighted assets and of tier 1 capital to average consolidated assets, referred to as the "leverage ratio."

The risk-based capital ratios measure the adequacy of a bank's capital against the riskiness of its assets and off-balance sheet activities. Failure to maintain adequate capital is a basis for "prompt corrective action" or other regulatory enforcement action. In assessing a bank's capital adequacy, regulators also consider other factors such as interest rate risk exposure; liquidity, funding and market risks; quality and level of earnings; concentrations of credit, quality of loans and investments; risks of any nontraditional activities; effectiveness of bank policies; and management's overall ability to monitor and control risks.

At March 31, 2020, both the Company and the Bank met all the capital adequacy requirements to which the Company and the Bank were subject. At March 31, 2020, the Bank was "well capitalized" under the regulatory framework for prompt corrective action. Management believes that no conditions or events have occurred since March 31, 2020 that would materially adversely change such capital classifications. From time to time, we may need to raise additional capital to support the Company's and the Bank's further growth and to maintain our "well capitalized" status.

The following table presents the Company's and the Bank's regulatory capital ratios as of the dates indicated.

	March 31, 2020		December 31, 2019	
	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)			
South Plains Financial, Inc.:				
Total capital (to risk-weighted assets)	$ 384,538	15.23%	$ 373,684	14.88%
Tier 1 capital (to risk-weighted assets)	328,812	13.02	322,835	12.85
CET 1 capital (to risk-weighted assets)	283,812	11.24	277,835	11.06
Tier 1 capital (to average assets)	328,812	10.34	322,835	10.74
City Bank:				
Total capital (to risk-weighted assets)	$ 375,390	14.87%	$ 368,322	14.67%
Tier 1 capital (to risk-weighted assets)	346,136	13.71	343,945	13.70
CET 1 capital (to risk-weighted assets)	346,136	13.71	343,945	13.70
Tier 1 capital (to average assets)	346,136	10.89	343,945	11.45

Off-Balance Sheet Arrangements

We are a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of our customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit to our customers is represented by the contractual or notional amount of those instruments. Commitments to extend credit and standby letters of credit are not recorded as an asset or liability by the Company until the instrument is exercised. The contractual or notional amounts of those instruments reflect the extent of involvement we have in particular classes of financial instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Because many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company uses the same credit policies in making commitments and conditional obligations as they do for on-balance sheet instruments. The amount and nature of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the potential borrower.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private short-term borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company holds collateral supporting those commitments for which collateral is deemed necessary.

The following table summarizes commitments we have made as of the dates presented.

	March 31, 2020	December 31, 2019
	(Dollars in thousands)	
Commitments to grant loans and unfunded commitments under lines of credit	$ 471,650	$ 409,969
Standby letters of credit	12,036	10,748
Total	$ 483,686	$ 420,717

We use our line of credit with the FHLB to take out letters of credit. These letters of credit pledged as collateral for certain public fund deposits. These letters of credit are off-balance sheet liabilities and would only be funded in the event of a default by the Company. See “Borrowed Funds - FHLB Advances” herein for a discussion for amounts of letters of credit.

We believe that we will be able to meet our contractual obligations as they come due through the maintenance of adequate cash levels. We expect to maintain adequate cash levels through profitability, loan and securities repayment and maturity activity and continued deposit gathering activities. We have in place various borrowing mechanisms for both short-term and long-term liquidity needs.

Interest Rate Sensitivity and Market Risk

As a financial institution, our primary component of market risk is interest rate volatility. Our interest rate risk policy provides management with the guidelines for effective funds management, and we have established a measurement system for monitoring our net interest rate sensitivity position. We have historically managed our sensitivity position within our established guidelines.

Fluctuations in interest rates will ultimately impact both the level of income and expense recorded on most of our assets and liabilities, and the market value of all interest-earning assets and interest-bearing liabilities, other than those which have a short term to maturity. Interest rate risk is the potential of economic losses due to future interest rate changes. These economic losses can be reflected as a loss of future net interest income and/or a loss of current fair market values. The objective is to measure the effect on net interest income and to adjust the balance sheet to minimize the inherent risk while at the same time maximizing income.

We manage our exposure to interest rates by structuring our balance sheet in the ordinary course of business. Based upon the nature of our operations, we are not subject to foreign exchange or commodity price risk. We do not own any trading assets.

Our exposure to interest rate risk is managed by the ALCO Committee, in accordance with policies approved by the Bank’s board of directors. The ALCO Committee formulates strategies based on appropriate levels of interest rate risk. In determining the appropriate level of interest rate risk, the ALCO Committee considers the impact on earnings and capital on the current outlook on interest rates, potential changes in interest rates, regional economies, liquidity, business strategies and other factors. The ALCO Committee meets regularly to review, among other things, the sensitivity of assets and liabilities to interest rate changes, the book and market values of assets and liabilities, commitments to originate loans and the maturities of investments and borrowings. Additionally, the ALCO Committee reviews liquidity, cash flow flexibility, maturities of deposits and consumer and commercial deposit activity. Management employs methodologies to manage interest rate risk, which include an analysis of relationships between interest-earning assets and interest-bearing liabilities and an interest rate shock simulation model.

We use interest rate risk simulation models and shock analyses to test the interest rate sensitivity of net interest income and fair value of equity, and the impact of changes in interest rates on other financial metrics. Contractual maturities and re-pricing opportunities of loans are incorporated in the model. The average lives of non-maturity deposit accounts are based on decay assumptions and are incorporated into the model. All of the assumptions used in our analyses are inherently uncertain and, as a result, the model cannot precisely measure future net interest income or precisely predict the impact of fluctuations in market interest rates on net interest income. Actual results will differ from the model’s simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and the application and timing of various management strategies.

On a quarterly basis, we run a simulation model for a static balance sheet and other scenarios. These models test the impact on net interest income from changes in market interest rates under various scenarios. Under the static model, rates are shocked instantaneously and ramped rates change over a 12-month and 24-month horizon based upon parallel and non-parallel yield curve shifts. Parallel shock scenarios assume instantaneous parallel movements in the yield curve compared to a flat yield curve scenario. Non-parallel simulation involves analysis of interest income and expense under various changes in the shape of the yield curve. Our internal policy regarding internal rate risk simulations currently specifies that for gradual parallel shifts of the yield curve, estimated net interest income at risk for the subsequent one-year period should not decline by more than 7.5% for a 100 basis point shift, 15% for a 200 basis point shift, and 22.5% for a 300 basis point shift.

The following tables summarize the simulated change in net interest income over a 12-month horizon as of the dates indicated:

	March 31, 2020	December 31, 2019
Change in Interest Rates (Basis Points)	**Percent Change in Net Interest Income**	**Percent Change in Net Interest Income**
+300	0.04	(2.44)
+200	(0.63)	(1.40)
+100	(0.76)	(0.71)
-100	(2.82)	(0.23)

Impact of Inflation

Our consolidated financial statements and related notes included elsewhere in this Form 10-Q have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). GAAP requires the measurement of financial position and operating results in terms of historical dollars, without considering changes in the relative value of money over time due to inflation or recession.

Unlike many industrial companies, substantially all of our assets and liabilities are monetary in nature. As a result, interest rates have a more significant impact on our performance than the effects of general levels of inflation. Interest rates may not necessarily move in the same direction or in the same magnitude as the prices of goods and services. However, other operating expenses do reflect general levels of inflation.

Critical Accounting Policies and Estimates

Our accounting and reporting policies conform to GAAP and conform to general practices within the industry in which we operate. To prepare financial statements in conformity with GAAP, management makes estimates, assumptions and judgments based on available information. These estimates, assumptions and judgments affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the financial statements and, as this information changes, actual results could differ from the estimates, assumptions and judgments reflected in the financial statements. In particular, management has identified several accounting policies that, due to the estimates, assumptions and judgments inherent in those policies, are critical in understanding our financial statements.

The Jumpstart Our Business Startups Act (the "JOBS Act") permits us an extended transition period for complying with new or revised accounting standards affecting public companies. We have elected to take advantage of this extended transition period, which means that the financial statements included in this Form 10-Q, as well as any financial statements that we file in the future, will not be subject to all new or revised accounting standards generally applicable to public companies for the transition period for so long as we remain an emerging growth company or until we affirmatively and irrevocably opt out of the extended transition period under the JOBS Act.

The following is a discussion of the critical accounting policies and significant estimates that we believe require us to make the most complex or subjective decisions or assessments. Additional information about these policies can be found in Note 1 of the Company's consolidated financial statements as of March 31, 2020.

Basis of Presentation and Consolidation. The consolidated financial statements include the accounts of the Company and its wholly owned consolidated subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Cash and Cash Equivalents. The Company includes all cash on hand, balances due from other banks, and Federal funds sold, all of which have original maturities within three months, as cash and cash equivalents.

Securities. Investment securities may be classified into trading, held-to-maturity, or available-for-sale portfolios. Securities that are held principally for resale in the near term are classified as trading. Securities that management has the ability and positive intent to hold to maturity are classified as held-to-maturity and recorded at amortized cost. Securities not classified as trading or held-to-maturity are available-for-sale and are reported at fair value with unrealized gains and losses excluded from earnings, but included in the determination of other comprehensive income. Management uses these assets as part of its asset/liability management strategy; they may be sold in response to changes in liquidity needs, interest rates, resultant prepayment risk changes, and other factors. Management determines the appropriate classification of securities at the time of purchase. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Realized gains and losses and declines in value judged to be other-than-temporary are included in gain or loss on sale of securities. The cost of securities sold is based on the specific identification method.

Loans. Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding principal balances net of any unearned income, charge-offs, unamortized deferred fees and costs on originated loans, and premiums or discounts on purchased loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the straight-line method, which is not materially different from the effective interest method required by GAAP.

Loans are placed on non-accrual status when, in management's opinion, collection of interest is unlikely, which typically occurs when principal or interest payments are more than ninety days past due. When interest accrual is discontinued, all unpaid accrued interest is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses. The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The Company's allowance for loan losses consists of specific valuation allowances established for probable losses on specific loans and general valuation allowances calculated based on historical loan loss experience for similar loans with similar characteristics and trends, judgmentally adjusted for general economic conditions and other qualitative risk factors internal and external to the Company.

The allowance for loan losses is evaluated on a quarterly basis by management and is based upon management's review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral. The Bank's loans are generally secured by specific items of collateral including real property, crops, livestock, consumer assets, and other business assets.

While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on various factors. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require the Bank to recognize additional losses based on their judgments about information available to them at the time of their examination. Because of these factors, it is reasonably possible that the estimated losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. All loans rated substandard or worse and greater than $250,000 are specifically reviewed to determine if they are impaired. Factors considered by management in determining whether a loan is impaired include payment status and the sources, amounts, and probabilities of estimated cash flow available to service debt in relation to amounts due according to contractual terms. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Loans that are determined to be impaired are then evaluated to determine estimated impairment, if any. GAAP allows impairment to be measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Loans that are not individually determined to be impaired or are not subject to the specific review of impaired status are subject to the general valuation allowance portion of the allowance for loan loss.

Loans Held for Sale. Loans held for sale are comprised of residential mortgage loans. Loans that are originated for best efforts delivery are carried at the lower of aggregate cost or fair value as determined by aggregate outstanding commitments from investors or current investor yield requirements. All other loans held for sale are carried at fair value. Loans sold are typically subject to certain indemnification provisions with the investor; management does not believe these provisions will have any significant consequences.

Recently Issued Accounting Pronouncements

See Note 1, Summary of Significant Accounting Policies, in the notes to the consolidated financial statements included elsewhere in this Form 10-Q regarding the impact of new accounting pronouncements which we have adopted.

Item 3. Quantitative and Qualitative Disclosure about Market Risk

The Company manages market risk, which, as a financial institution is primarily interest rate volatility, through the ALCO Committee of the Bank, in accordance with policies approved by its board of directors. The Company uses an interest rate risk simulation model and shock analysis to test the interest rate sensitivity of net interest income and fair value of equity, and the impact of changes in interest rates on other financial metrics. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Interest Rate Sensitivity and Market Risk” herein for a discussion of how we manage market risk.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Form 10-Q, the Company carried out an evaluation, under the supervision and with the participation of its management, including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of its disclosure controls and procedures. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management was required to apply judgment in evaluating its controls and procedures. Based on this evaluation, the Company’s Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act) were effective as of the end of the period covered by this Form 10-Q.

Internal Control over Financial Reporting

There were no changes in the Company’s internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the three months ended March 31, 2020 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company and its subsidiaries are subject to various legal actions, as described in our Annual Report on Form 10-K for the year ended December 31, 2019 (the "2019 Annual Report on Form 10-K") filed with the Securities and Exchange Commission (the "SEC") pursuant to Rule 424(b) of the Securities Act of 1933, as amended (the "Securities Act"), on March 25, 2020. There are no material developments in the legal actions described in our 2019 Annual Report on Form 10-K.

In connection with the recent acquisition of West Texas State Bank ("WTSB"), the Company and the Bank filed a lawsuit in the 72nd Judicial District Court of Lubbock County, Texas: *South Plains Financial, Inc. and City Bank v. R. Jay Phillips and West Texas State Bank*, Case No. 202053938, on April 8, 2020 (as amended). The petition names as defendants Mr. R. Jay Phillips ("Phillips") and WTSB.

The petition alleges that Phillips, the former Chairman of the Board and Chief Executive Officer of WTSB, made false representations and misstatements to the Company and the Bank regarding the amount of expenses that were to be incurred as a result of WTSB's termination of its core data processing contract, as required under the terms of the transaction. In particular, the petition alleges that Phillips' material misrepresentations, which were certified in writing, resulted in an incorrect quantification of WTSB's transaction-related expenses and, in turn, inflated the consideration paid by the Company. The petition seeks actual damages, punitive damages, exemplary damages, and attorney's fees, and, alternatively, rescission of the Company's acquisition of WTSB.

Phillips filed a counterclaim on May 6, 2020 seeking indemnification from City Bank, as successor to WTSB through merger, including reimbursement and payment of expenses incurred in connection with the lawsuit. The Company intends to vigorously pursue its claim; however, it is not possible at this time to determine with any degree of certainty the ultimate outcome of the litigation. If the case is not resolved, the lawsuit could result in costs associated with indemnification of Phillips and advancement of expenses not covered by insurance.

Except as described above or in our 2019 Annual Report on Form 10-K, we are not presently involved in any other litigation, nor to our knowledge is any litigation threatened against us, that in management's opinion would result in any material adverse effect on our financial position or results of operations or that is not expected to be covered by insurance.

Item 1A. Risk Factors

In evaluating an investment in any of our securities, investors should consider carefully, among other things, information under the heading "Cautionary Notice Regarding Forward-Looking Statements" in Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations," of this Quarterly Report on Form 10-Q for the three months ended March 31, 2020 (this "Form 10-Q") and the risk factors previously disclosed under the heading "Risk Factors" in Part I, Item 1A of our 2019 Annual Report on Form 10-K. The following risk factors represent material changes in the risk factors disclosed by the Company in the 2019 Annual Report on Form 10-K.

The COVID-19 pandemic is adversely affecting us and our customers, employees, and third-party service providers, and the adverse impacts on our business, financial position, results of operations, and prospects could be significant.

The COVID-19 pandemic has negatively impacted the global economy, disrupted global supply chains, lowered equity market valuations, created significant volatility and disruption in financial markets, increased unemployment levels and decreased consumer confidence generally. In addition, the pandemic has resulted in temporary closures of many businesses and the institution of social distancing and sheltering in place requirements in many states and communities. The pandemic could influence the recognition of credit losses in our loan portfolios and increase our allowance for credit losses, particularly as businesses remain closed and as more customers are expected to draw on their lines of credit or seek additional loans to help finance their businesses. Furthermore, the pandemic could affect the stability of our deposit base as well as our capital and liquidity position, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, result in lost revenue and cause us to incur additional expenses. Similarly, because of changing economic and market conditions affecting issuers, we may be required to recognize other-than-temporary impairments in future periods on the securities we hold as well as reductions in other comprehensive income.

The extent of the impact of the COVID-19 pandemic on our capital, liquidity, and other financial positions and on our business, results of operations, and prospects will depend on a number of evolving factors, including: (i) the duration, extent, and severity of the pandemic, (ii) the response of governmental and nongovernmental authorities, (iii) the effect on our customers, counterparties, employees, and third-party service providers, (iv) the effect on economies and markets, and (v) the success of hardship relief efforts to bridge the gap to reopening the economy.

The duration of the pandemic and the resulting business interruptions and related impacts on our business and operations, which will depend on future developments, are highly uncertain and cannot be reasonably estimated at this time. The pandemic could cause us to experience higher credit losses in our lending portfolio, impairment of our goodwill and other financial assets, reduced demand for our products and services, and other negative impacts on our financial position, results of operations, and prospects.

The U.S. government has implemented programs to directly compensate individuals and grant or loan money to businesses in an effort to provide funding while the economy is shut down. Many banks, including City Bank, have implemented hardship relief programs that include payment deferral and short-term funding options. The success of these programs could mute the effect on the Company's credit losses, which may be difficult to determine.

A significant number of our borrowers have requested and received short-term loan payment deferrals. These deferrals may negatively impact our revenue and other results of operations in the near term and, if not effective in mitigating the effect of COVID-19 on our customers, may adversely affect our business and results of operations more substantially over a longer period of time. Moreover, the cumulative effects of COVID-19 and the measures implemented by governments to combat the pandemic on the mortgaged properties may cause borrowers to be unable to meet their payment obligations under mortgage loans that we hold and may result in significant losses.

The extent to which COVID-19 impacts our business, results of operations and financial condition will depend on future developments, which are highly uncertain and are difficult to predict, including, but not limited to, the duration and spread of the pandemic, its severity, the actions to contain the virus or treat its impact, and how quickly and to what extent normal economic and operating conditions can resume. Even after COVID-19 has subsided, we may continue to experience materially adverse impacts to our business as a result of the virus's global economic impact, including the availability of credit, adverse impacts on our liquidity and any recession that has occurred or may occur in the future.

There are no comparable recent events that provide guidance as to the effect the spread of COVID-19 as a global pandemic may have, and, as a result, the ultimate impact of the outbreak is highly uncertain and subject to change. We do not yet know the full extent of the impacts on our business, our operations or the global economy as a whole. However, the effects could have a material impact on our results of operations and heighten many of our known risks described in the "Risk Factors" section of our Annual Report on Form 10-K for the fiscal year ended December 31, 2019.

Current and future restrictions on our workforce's access to our facilities and our reliance on third parties could limit our ability to meet customer servicing expectations and have a material adverse effect on our operations.

We rely on business processes and profit center activity that largely depend on people, technology, and the use of complex systems and models to manage our business, including access to information technology systems and models as well as information, applications, payment systems and other services provided by third parties. In response to COVID-19, we have modified our business practices with a majority of our employees working remotely from their homes to have our operations uninterrupted as much as possible. Further, technology in employees' homes may not be as robust as in our offices and could cause the networks, information systems, applications, and other tools available to employees to be more limited or less reliable than in our offices, the continuation of these work-from-home measures introduces additional operational risk, especially including increased cybersecurity risk. These cyber risks include greater phishing, malware, and other cybersecurity attacks, vulnerability to disruptions of our information technology infrastructure and telecommunications systems for remote operations, increased risk of unauthorized dissemination of confidential information, limited ability to restore the systems in the event of a systems failure or interruption, great risk of a security breach resulting in destruction or misuse of valuable information, and potential impairment of our ability to perform critical functions, including wiring funds, all of which could expose us to risks of data or financial loss, litigation and liability and could seriously disrupt our operations and the operations of any impacted customers.

Moreover, we rely on many third parties in our business operations, including appraisers of real property collateral, vendors that supply essential services such as loan servicers, providers of financial information, systems and analytical tools and providers of electronic payment and settlement systems, and local and federal government agencies, offices, and courthouses. In light of the developing measures responding to the pandemic, many of these entities have limited the availability and access of their services. For example, loan origination could be delayed due to the limited availability of real estate appraisers for the collateral. Loan closings could be delayed related to reductions in available staff in recording offices or the closing of courthouses in certain counties, which slows the process for title work, mortgage and UCC filings in those counties. If the third party service providers continue to have limited capacities for a prolonged period or if additional limitations or potential disruptions in these services materialize, it may negatively affect our operations.

Changes in market interest rates or capital markets, including volatility resulting from the COVID-19 pandemic, could affect our revenues and expenses, the value of assets and obligations, and the availability and cost of capital or liquidity.

The COVID-19 pandemic has significantly affected the financial markets and has resulted in a number of Federal Reserve actions. Market interest rates have declined significantly. On March 3, 2020, the 10-year Treasury yield fell below 1.00% for the first time, and the Federal Reserve reduced the target federal funds rate by 50 basis points to 1.00% to 1.25%. On March 15, 2020, the Federal Reserve further reduced the target federal funds rate by 100 basis points to 0.00% to 0.25% and announced a

$700 billion quantitative easing program in response to the expected economic downturn caused by the COVID-19 pandemic. The Federal Reserve reduced the interest that it pays on excess reserves from 1.60% to 1.10% on March 3, 2020, and then to 0.10% on March 15, 2020. We expect that these reductions in interest rates, especially if prolonged, could adversely affect our net interest income and margins and our profitability.

Given our business mix, and the fact that most of our assets and liabilities are financial in nature, we tend to be sensitive to market interest rate movements and the performance of the financial markets. Our primary source of income is net interest income, which is the difference between the interest income generated by our interest-earning assets (consisting primarily of loans and, to a lesser extent, securities) and the interest expense generated by our interest-bearing liabilities. Prevailing economic conditions, fiscal and monetary policies and the policies of various regulatory agencies all affect market rates of interest and the availability and cost of credit, which, in turn, significantly affect financial institutions' net interest income. If the interest we pay on deposits and other borrowings increases at a faster rate than increases in the interest we receive on loans and investments, net interest income, and, therefore, our earnings, could be affected. Earnings could also be affected if the interest we receive on loans and other investments falls more quickly than the interest we pay on deposits and other borrowings.

In addition, the continued spread of COVID-19 has also led to disruption and volatility in financial markets, which could increase our cost of capital and adversely affect our ability to access financial markets, which may in turn affect the value of the subordinated notes. This market volatility has resulted in a significant decline, and we may continue to experience further declines, in our stock price and market capitalization, which could result in goodwill impairment charges.

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

None

Item 3. Defaults upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit Number	Description
3.1	Amended and Restated Certificate of Formation of South Plains Financial, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Form S-1 filed with the Commission on April 12, 2019) (File No. 333-230851)
3.2	Amended and Restated Bylaws of South Plains Financial, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Form S-1 filed with the Commission on April 12, 2019) (File No. 333-230851)
31.1*	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2**	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101*	The following material from South Plains Financial, Inc.'s Form 10-Q for the quarter ended March 31, 2020, formatted in XBRL (eXtensible Business Reporting Language), filed herewith: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Statements of Changes in Stockholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Unaudited Consolidated Financial Statements.

* Filed with this Form 10-Q

** Furnished with this Form 10-Q

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.

	South Plains Financial, Inc.
Date: May 13, 2020	By: /s/ Curtis C. Griffith Curtis C. Griffith Chairman and Chief Executive Officer
Date: May 13, 2020	By: /s/ Steven B. Crockett Steven B. Crockett Chief Financial Officer and Treasurer

Exhibit 31.1

CERTIFICATION PURSUANT TO
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Curtis C. Griffith, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of South Plains Financial, Inc. (the “registrant”) for the quarter ended March 31, 2020 (this “report”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting (as defined in the Exchange Act Rules 13a-15(f) and 15d-15(f)) that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 13, 2020

By: /s/ Curtis C. Griffith
Curtis C. Griffith
Chairman and Chief Executive Officer

Exhibit 31.2

CERTIFICATION PURSUANT TO RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Steven B. Crockett, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of South Plains Financial, Inc. (the “registrant”) for the quarter ended March 31, 2020 (this “report”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant’s internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 13, 2020

By: /s/ Steven B. Crockett

Steven B. Crockett
Chief Financial Officer

Exhibit 32.1

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

In connection with the Quarterly Report on Form 10-Q of South Plains Financial, Inc. (the “Company”) for the quarter ended March 31, 2020 (the “Report”), as filed with the Securities and Exchange Commission on the date hereof, I certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 13, 2020

By: /s/ Curtis C. Griffith
Curtis C. Griffith
Chairman and Chief Executive Officer

Exhibit 32.2

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

In connection with the Quarterly Report on Form 10-Q of South Plains Financial, Inc. (the “Company”) for the quarter ended March 31, 2020 (the “Report”), as filed with the Securities and Exchange Commission on the date hereof, I certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 13, 2020

By: /s/ Steven B. Crockett
Steven B. Crockett
Chief Financial Officer