MERCANTILE BANKSHARES CORP
Form 10-Q
November 09, 2001

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

FORM 10-Q

(MARK ONE)

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

For the Quarterly Period Ended September 30, 2001

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 0-5127

MERCANTILE BANKSHARES CORPORATION
(Exact name of registrant as specified in its charter)

Maryland	52-0898572
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2 Hopkins Plaza, Baltimore, Maryland	21201
(Address of principal executive offices)	(Zip code)

(410) 237-5900
(Registrant's telephone number, including area code)

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

As of October 31, 2001, registrant had outstanding 69,807,236 shares of Common Stock.

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements (Unaudited)

MERCANTILE BANKSHARES CORPORATION
CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share data)	September 2
ASSETS	
Cash and due from banks	$ 275,4
Interest-bearing deposits in other banks	3
Federal funds sold	122,2
Total cash and cash equivalents	398,0
Investment securities:	
Available-for-sale at fair value	
U.S. Treasury and government agencies -- amortized cost of $1,758,252 (2001) and $1,600,232 (2000)	1,815,2
States and political subdivisions -- amortized cost of $1,149 (2001) and $1,350 (2000)	1,1
Other investments -- amortized cost of $43,771 (2001) and $49,507 (2000)	56,2
Held-to-maturity at amortized cost	
States and political subdivisions -- fair value of $41,073 (2001) and $38,653 (2000)	39,1
Other investments -- fair value of $13,454 (2001) and $13,068 (2000)	13,4
Total investment securities	1,925,2
Loans held-for-sale	30,2
Loans	6,900,1
Less: allowance for loan losses	(141,0
Loans, net	6,759,1
Bank premises and equipment, less accumulated depreciation of $110,961 (2001) and $103,715 (2000)	101,7
Other real estate owned, net	1
Goodwill, net	104,8
Other intangible assets, net	7,2
Other assets	141,1
Total assets	$9,468,0
LIABILITIES	
Deposits:	
Noninterest-bearing deposits	$1,789,4
Interest-bearing deposits	5,458,2
Total deposits	7,247,7
Short-term borrowings	773,2
Accrued expenses and other liabilities	138,6

Long-term debt	84,2
Total liabilities	8,243,8
SHAREHOLDERS' EQUITY	
Preferred stock, no par value; authorized 2,000,000 shares; issued and outstanding -- None	
Common stock, $2 par value; authorized 130,000,000 shares; issued 69,816,937 shares in 2001 and 71,098,750 shares in 2000	139,6
Capital surplus	161,8
Retained earnings	879,8
Accumulated other comprehensive income (loss)	42,8
Total shareholders' equity	1,224,1
Total liabilities and shareholders' equity	$9,468,0

See notes to consolidated financial statements

MERCANTILE BANKSHARES CORPORATION
STATEMENT OF CONSOLIDATED INCOME

(Dollars in thousands, except per share data)	For the 9 Months Ended September 30, 2001	2000	For the 3 Months Ended September 30, 2001	2000
INTEREST INCOME				
Interest and fees on loans	$ 420,701	$ 399,361	$ 135,635	$ 142,454
Interest and dividends on investment securities:				
Taxable interest income	68,890	69,332	22,986	22,862
Tax-exempt interest income	1,506	780	504	431
Dividends	984	1,020	304	338
Other investment income	2,494	844	804	776
	73,874	71,976	24,598	24,407
Other interest income	3,384	1,319	811	712
Total interest income	497,959	472,656	161,044	167,573
INTEREST EXPENSE				
Interest on deposits	158,241	130,232	49,303	47,901
Interest on short-term borrowings	21,816	36,022	5,762	13,191
Interest on long-term debt	4,425	4,304	1,380	1,497
Total interest expense	184,482	170,558	56,445	62,589
NET INTEREST INCOME	313,477	302,098	104,599	104,984
Provision for loan losses	9,230	12,745	3,101	4,316
NET INTEREST INCOME AFTER				

PROVISION FOR LOAN LOSSES........	304,247	289,353	101,498	100,668
NONINTEREST INCOME				
Trust Division services...........	51,888	51,556	17,229	17,302
Service charges on deposit accounts.........................	20,457	17,890	7,157	6,194
Mortgage banking related fees.....	7,967	2,306	3,106	812
Investment securities gains and (losses).........................	3,135	69	1,596	--
Other income......................	23,763	21,402	8,649	7,757
Total noninterest income.......	107,210	93,223	37,737	32,065
NONINTEREST EXPENSES				
Salaries..........................	91,797	86,182	31,232	29,519
Employee benefits.................	22,293	19,575	7,157	6,092
Net occupancy expense of bank premises.........................	10,497	8,473	3,726	3,014
Furniture and equipment expenses..	17,500	16,797	5,752	5,578
Communications and supplies.......	9,852	9,171	3,279	3,098
Amortization of goodwill..........	6,939	3,444	2,134	1,528
Other expenses....................	35,779	36,020	13,307	12,556
Total noninterest expenses.....	194,657	179,662	66,587	61,385
Income before income taxes........	216,800	202,914	72,648	71,348
Applicable income taxes...........	79,739	73,412	26,569	25,968
NET INCOME........................	$ 137,061	$ 129,502	$ 46,079	$ 45,380
NET INCOME PER SHARE OF COMMON STOCK (Note 2):				
Basic............................	$ 1.93	$ 1.88	$ .66	$ .65
Diluted..........................	$ 1.92	$ 1.87	$ .65	$ .64

See notes to consolidated financial statements

MERCANTILE BANKSHARES CORPORATION
STATEMENT OF CONSOLIDATED CASH FLOWS

Increase (decrease) in cash and cash equivalents (Dollars in thousands)	For the 9 Months Ended September 30, 2001	2000
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income..	$ 137,061	$ 129,502
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses............................	9,230	12,745
Depreciation and amortization.........................	9,267	8,079
Amortization of goodwill..............................	6,939	3,444
Investment securities (gains) and losses..............	(3,135)	(69)

Write-downs of other real estate owned	36	20
Gains on sales of other real estate owned	(267)	(494)
Gains on sales of buildings	(510)	--
Net (increase) decrease in assets:		
Interest receivable	2,337	(5,716)
Other receivables	(69)	964
Other assets	(862)	(7,093)
Loans held-for-sale	(23,678)	1,068
Net increase (decrease) in liabilities:		
Interest payable	290	7,829
Accrued expenses	(472)	15,635
Taxes payable	45,522	4,788
Net cash provided by operating activities	181,689	170,702
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from maturities of investment securities held-to-maturity	3,181	7,367
Proceeds from maturities of investment securities available-for-sale	447,892	410,968
Proceeds from sales of investment securities available-for-sale	3,135	700
Purchases of investment securities held-to-maturity	(4,986)	(11,295)
Purchases of investment securities available-for-sale	(599,974)	(232,361)
Net increase in customer loans	(214,211)	(552,047)
Proceeds from sales of other real estate owned	1,568	1,903
Capital expenditures	(9,266)	(10,403)
Proceeds from sales of buildings	916	--
Acquisition of commercial mortgage company	(7,000)	--
Cash from acquired bank	--	13,104
Net cash used in investing activities	(378,745)	(372,064)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase (decrease) in noninterest-bearing deposits	195,986	118,598
Net increase (decrease) in checking plus interest and savings accounts	131,876	(141,211)
Net increase (decrease) in certificates of deposit	123,321	309,442
Net increase (decrease) in short-term borrowings	(8,208)	53,144
Repayment of long-term debt	(8,347)	(15,136)
Proceeds from issuance of shares	5,733	5,327
Repurchase of common shares	(61,953)	(36,086)
Dividends paid	(58,040)	(52,167)
Net cash provided by financing activities	320,368	241,911
Net increase (decrease) in cash and cash equivalents	123,312	40,549
Cash and cash equivalents at beginning of period	274,745	227,356
Cash and cash equivalents at end of period	$ 398,057	$ 267,905

See notes to consolidated financial statements

MERCANTILE BANKSHARES CORPORATION

STATEMENT OF CHANGES IN CONSOLIDATED SHAREHOLDERS' EQUITY

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001 AND 2000

(Dollars in thousands, except per share data)	Total	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)
BALANCE, DECEMBER 31, 1999	$ 974,040	$137,292	$ 47,798	$796,192	$(7,242)
Net income	129,502			129,502	
Unrealized gains (losses) on securities available-for-sale, net of reclassification adjustment, net of taxes	10,234				10,234
Comprehensive income	139,736				
Cash dividends paid:					
Common stock ($.76 per share)	(52,167)			(52,167)	
Issuance of 95,939 shares for dividend reinvestment and stock purchase plan	2,855	192	2,663		
Issuance of 23,662 shares for employee stock purchase dividend reinvestment plan	724	47	677		
Issuance of 117,214 shares for employee stock option plan	1,748	234	1,514		
Purchase of 1,193,000 shares under stock repurchase plan	(36,086)	(2,386)	(33,700)		
Issuance of 2,261,162 shares for bank acquisition	64,076	4,522	59,554		
Vested stock options	333		333		
Transfer to capital surplus	--		100,000	(100,000)	
BALANCE, SEPTEMBER 30, 2000	$1,095,259	$139,901	$178,839	$773,527	$ 2,992
BALANCE, DECEMBER 31, 2000	$1,173,301	$142,198	$214,454	$800,781	$15,868
Net income	137,061			137,061	
Unrealized gains (losses) on securities available-for-sale, net of reclassification adjustment, net of taxes (Note 5)	27,020				27,020
Comprehensive income	164,081				

Cash dividends paid:					
Common stock ($.82 per share)................	(58,040)			(58,040)	
Issuance of 84,817 shares for dividend reinvestment and stock purchase plan..........	3,128	169	2,959		
Issuance of 17,546 shares for employee stock purchase dividend reinvestment plan......	684	35	649		
Issuance of 115,824 shares for employee stock option plan......	1,921	232	1,689		
Purchase of 1,500,000 shares under stock repurchase plan........	(61,953)	(3,000)	(58,953)		
Vested stock options....	1,022		1,022		
BALANCE, SEPTEMBER 30, 2001..................	$1,224,144	$139,634	$161,820	$879,802	$42,888

See notes to consolidated financial statements

MERCANTILE BANKSHARES CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1) The consolidated financial statements, which include the accounts of the Corporation and all of its affiliates, are prepared in conformity with accounting principles generally accepted in the United States of America and follow general practice within the banking industry. In the opinion of management, the consolidated financial statements include all adjustments necessary for a fair presentation of the results for the interim period. These adjustments are of a normal recurring nature and include adjustments to eliminate all significant intercompany transactions. In view of the changing conditions in the national economy, the effect of actions taken by regulatory authorities and normal seasonal factors, the results for the interim period are not necessarily indicative of annual performance. For comparability, certain prior period amounts have been reclassified to conform with current period presentation.

   The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and contingent assets and liabilities at the date of the financial statements, and the disclosure of revenues and expenses during the reporting period. These estimates and assumptions are based on information available as of the date of the financial statements and could differ from actual results.

2) Basic and diluted earnings per share (EPS) amounts are computed in accordance with the provisions of Statement of Financial Accounting Standard No. 128, Earnings per Share. Basic EPS is computed by dividing income available to common shareholders by the weighted average number of common shares which were 70,844,309 and 68,791,551 for the first three quarters of 2001 and 2000, respectively, and 70,237,247 and 69,835,471 for the third

quarter of 2001 and 2000, respectively. Diluted EPS is computed using the same components as in basic EPS with the denominator adjusted for the dilutive effect of stock options. The adjusted weighted average shares were 71,476,039 and 69,308,001 for the nine months ended September 30, 2001 and 2000, respectively, and 70,863,482 and 70,409,909 for the third quarter of 2001 and 2000, respectively.

3) Under the provisions of Statements of Financial Accounting Standards No. 114 and 118, Accounting by Creditors for Impairment of a Loan, a loan is considered impaired, based upon current information and events, if it is probable that the Corporation will not collect all principal and interest payments according to the contractual terms of the loan agreement. Generally, a loan is considered impaired once either principal or interest payments become 90 days past due at the end of a calendar quarter. A loan may be considered impaired sooner if, in management's judgement, such action is warranted. The impairment of a loan is measured based upon the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if the repayment is expected to be provided predominantly by the underlying collateral. A majority of the Corporation's impaired loans are measured by reference to the fair value of the collateral. Interest income on impaired loans is recognized on the cash basis. Information with respect to impaired loans and the related valuation allowance (if the measure of the impaired loan is less than the recorded investment) as of September 30, 2001 and December 31, 2000 is shown below. A general allowance for impaired loans, for which no specific valuation allowance is necessary, is included.

(Dollars in thousands)	September 30, 2001	December 31, 2000
Impaired loans with a specific valuation allowance	$ 2,696	$ 3,828
Impaired loans with a general allowance	21,993	17,377
Impaired loans with no valuation allowance	7,027	5,788
Total impaired loans	$ 31,716	$ 26,993
Allowance for loan losses applicable to impaired loans with a specific valuation allowance	$ 1,251	$ 1,375
Allowance for loan losses applicable to impaired loans with a general allowance	3,964	4,889
Allowance for loan losses applicable to other than impaired loans	135,788	132,348
Total allowance for loan losses	$141,003	$138,612
Year-to-date interest income on impaired loans recorded on the cash basis	$ 257	$ 676
Year-to-date average recorded investment in impaired loans during the period	$ 31,517	$ 20,156
Quarter-to-date interest income on impaired loans recorded on the cash basis	$ 119	$ 482
Quarter-to-date average recorded investment in impaired loans during the period	$ 32,322	$ 22,013

Note: Impaired loans do not include large groups of smaller balance homogeneous loans that are evaluated collectively for impairment (e.g. residential mortgages and consumer installment loans). The allowance for loan losses related to these loans is included in the allowance for loan losses applicable to other than impaired loans.

4) Various commitments to extend credit (lines of credit) are made in the normal course of banking business. At September 30, 2001, total unused lines of credit approximated $2,803,080,000. In addition, letters of credit are issued for the benefit of customers by affiliated banks. Outstanding letters of credit were $194,510,000 at September 30, 2001.

5) The provisions of Statement of Financial Accounting Standards No. 130, Reporting Comprehensive Income, established standards for disclosing comprehensive income in financial statements. The following table summarizes the related tax effect of unrealized gains (losses) on securities available-for-sale for the nine months ended September 30, 2001 and 2000. The net amount is included in accumulated other comprehensive income (loss) in the Statement of Changes in Consolidated Shareholders' Equity on Page 5.

	For the 9 Months Ended September 30,					
	2001			2000		
(Dollars in thousands)	Pretax Amount	Tax (Expense) Benefit	Net Amount	Pretax Amount	Tax (Expense) Benefit	Net Amount
Unrealized gains (losses) on securities available-for-sale:						
Unrealized holding gains (losses) arising during the period............	$47,224	$(18,309)	$28,915	$16,488	$(6,212)	$10,276
Reclassification adjustment for (gains) losses included in net income................	(3,135)	1,240	(1,895)	(69)	27	(42)
Total..................	$44,089	$(17,069)	$27,020	$16,419	$(6,185)	$10,234

6) Under the provisions of Statement of Financial Accounting Standards No. 131, Disclosures about Segments of an Enterprise and Related Information, Mercantile Bankshares Corporation has two reportable segments -- its twenty Community Banks and Mercantile - Safe Deposit & Trust Company (MSD&T) which consists of the Banking Division and the Trust Division.

The following tables present selected segment information for the nine months ended September 30, 2001 and 2000. The components in the "Other" column consist of amounts for the nonbank affiliates and intercompany eliminations. Certain expense amounts such as operations overhead have been reclassified from internal financial reporting in order to provide for full cost absorption. These reclassifications are shown in the "Adjustments" line.

For the 9 Months Ended September 30, 2001

(Dollars in thousands)	MSD&T Banking	MSD&T Trust	Total MSD&T	Community Banks	Other	Total
Net interest income.....	$98,678	$ --	$ 98,678	$ 215,171	$ (372)	$ 313,477
Provision for loan losses.................	(4,743)	--	(4,743)	(4,487)	--	(9,230)
Noninterest income......	26,880	51,703	78,583	35,413	(6,786)	107,210
Noninterest expenses....	(59,475)	(29,983)	(89,458)	(109,349)	4,150	(194,657)
Adjustments.............	9,645	(1,381)	8,264	(14,914)	6,650	--
Income (loss) before income taxes...........	70,985	20,339	91,324	121,834	3,642	216,800
Income tax (expense) benefit................	(25,647)	(8,136)	(33,783)	(45,142)	(814)	(79,739)
Net income (loss).......	$45,338	$12,203	$ 57,541	$ 76,692	$ 2,828	$ 137,061
Average assets..........			$3,459,127	$5,834,626	$(167,130)	$9,126,623
Average equity..........			377,602	699,716	118,132	1,195,450

For the 9 Months Ended September 30, 2000

(Dollars in thousands)	MSD&T Banking	MSD&T Trust	Total MSD&T	Community Banks	Other	Total
Net interest income.....	$103,640	$ --	$ 103,640	$ 198,533	$ (75)	$ 302,098
Provision for loan losses.................	(6,208)	--	(6,208)	(6,537)	--	(12,745)
Noninterest income......	18,414	51,461	69,875	31,546	(8,198)	93,223
Noninterest expenses....	(53,207)	(29,023)	(82,230)	(101,185)	3,753	(179,662)
Adjustments.............	10,139	(1,811)	8,328	(9,812)	1,484	--
Income (loss) before income taxes...........	72,778	20,627	93,405	112,545	(3,036)	202,914
Income tax (expense) benefit................	(26,258)	(8,251)	(34,509)	(40,920)	2,017	(73,412)
Net income (loss).......	$ 46,520	$ 12,376	$ 58,896	$ 71,625	$ (1,019)	$ 129,502
Average assets..........			$3,102,932	$5,192,978	$(133,474)	$8,162,436
Average equity..........			355,830	630,758	42,942	1,029,530

7) The Corporation and its bank affiliates are subject to various regulatory capital requirements administered by the federal and state banking agencies. These requirements include maintaining certain capital ratios above minimum levels. These capital ratios include Tier 1 capital and Total risk-based capital as percents of net risk-weighted assets and Tier 1 capital as a percent of adjusted average total assets (leverage ratio). Management believes that, as of September 30, 2001, the Corporation and its bank affiliates exceeded all capital adequacy requirements to which they are subject.

Capital ratios and the amounts used to calculate them are presented in the following table for Mercantile Bankshares Corporation (MBC) and Mercantile - Safe Deposit & Trust Company (MSD&T), as of September 30, 2001 and 2000.

	September 30, 2001		September 30, 2000	
(Dollars in thousands)	MBC	MSD&T	MBC	MSD&T
Tier 1 capital..................	$1,069,428	$ 375,248	$1,001,190	$ 359,157
Total risk-based capital........	1,160,999	413,369	1,087,471	393,367
Net risk-weighted assets........	6,927,903	2,904,081	6,421,092	2,719,614
Adjusted average total assets...	9,166,460	3,477,351	8,389,912	3,147,639
Tier 1 capital ratio............	15.44%	12.92%	15.59%	13.21%
Total capital ratio.............	16.76%	14.23%	16.94%	14.46%
Leverage ratio..................	11.67%	10.79%	11.93%	11.41%

8) On November 8, 2001, Mercantile-Safe Deposit & Trust Company, our lead bank, settled a public offering of $200,000,000 of its 5.70% Senior Bank Notes, due 2011. Interest will be payable on May 15th and November 15th of each year, beginning May 15, 2002. The Bank Notes will mature on November 15, 2011, and will not be redeemable prior to maturity and no sinking fund will be provided.

Simultaneously, Mercantile-Safe Deposit & Trust Company entered into a swap agreement with a notional amount of $200,000,000 in which it will receive 5.70% and pay a floating rate based on the three month LIBOR rate.

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

MERCANTILE BANKSHARES CORPORATION

Consolidated Financial Results

Mercantile Bankshares Corporation reported that, for the quarter ended September 30, 2001, net income was $46,079,000, a 1.5% increase over net income of $45,380,000 for the same period in 2000. Diluted net income per share was $.65 for the third quarter 2001, an increase of 1.6% from the $.64 reported for the third quarter last year. Diluted cash net income per share, which excludes amortization of goodwill in the calculation, was $.68 for the third quarter 2001 as compared to $.67 for the same period in 2000.

For the first nine months of 2001, net income was $137,061,000, an increase of 5.8% over the $129,502,000 reported for the comparable period last year. Diluted net income per share for the first three quarters of 2001 was $1.92, a 2.7% increase over the $1.87 for the same period in 2000. Diluted cash net income per share was $2.01 for the first three quarters of 2001, an increase of 4.7% over the $1.92 reported for the same period last year.

Return on average assets for the third quarter was 1.97%, return on average tangible equity was 17.56% and average tangible equity to average assets was 11.88%. For the nine months ended September 30, 2001, the comparable ratios were 2.01%, 17.68% and 12.08%, respectively.

In regards to the terrorist attacks of September 11, 2001, the Corporation has no exposure that it is aware of, to customers who were victims of the attacks. Mercantile's exposure in specific industries expected to be impacted the most by the attacks is either nonexistent or not material. The Corporation may, however, be adversely effected by changes in general economic conditions resulting from the attacks.

Net Interest Income and Net Interest Margin

Net interest income for the quarter ended September 30, 2001, declined slightly to $104,599,000 from $104,984,000 the prior year. Although average loans grew a healthy 9.8%, this growth was offset by a decline in the net interest margin to 4.77% in the third quarter of 2001 from 5.25% in 2000. The increase in loans from second quarter 2001 was 1.2%, representing an annualized growth rate of 4.8%. The decline in net interest margin was attributable to the 350 basis point reduction in short-term interest rates by the Federal Reserve during the first three quarters of 2001, with a reduction of 75 basis points occurring in the third quarter. The Corporation is asset sensitive, with assets repricing more quickly than liabilities in response to changes in interest rates. As a result, Mercantile's net interest margin tends to compress and growth in net interest income tends to slow in a falling interest rate environment.

Net interest income for the first nine months of 2001 increased to $313,477,000 or 3.8% over the $302,098,000 for last year. The growth in net interest income was attributable to strong average loan growth of 13.4%, part of which was due to the two bank acquisitions completed in the second half of 2000. Partially offsetting the positive impact from loan growth was a decline in the net interest margin to 4.90%, from 5.27% for the first three quarters of last year. See the Analysis of Interest Rates and Interest Differentials on page 13 for further details.

Noninterest Income

For the third quarter 2001, noninterest income increased 17.7% from last year. Included in this increase was a gain from the sale of equity securities held in the available-for-sale portfolio. This $1,596,000 gain added one cent, after tax, to net income per share. Excluding the investment securities gain, noninterest income increased 12.7%. Trust Division revenues decreased slightly compared to third quarter last year. The decline in equity markets, as reflected in the 28% decline in the S&P 500 Index over the past year, had a negative impact on income from principal fees. New trust business substantially offset this impact. Mortgage banking revenues more than doubled from that reported for the third quarter last year, as revenues benefited from increased volume in residential and multifamily loan originations.

Noninterest income for the first three quarters of 2001 was $107,210,000, a 15.0% increase over the $93,223,000 for the comparable period in 2000. Included in this increase were gains of $3,135,000 from sales of equity securities held in the available-for-sale portfolio. Excluding the investment securities gains, the growth rate was 11.7% for the same period. The largest increase in noninterest income came from mortgage banking revenues which more than doubled to $7,967,000.

Noninterest Expenses

Noninterest expenses for the quarter ended September 30, 2001, increased 8.5% to $66,587,000 from $61,385,000 for the third quarter of 2000. The key measure of expense management is the efficiency ratio which was 45.3%, calculated excluding amortization of goodwill. The increase in salaries was partially a result of increased staff from acquisitions. Employee benefits increased from the prior year due to a general increase in costs for health and welfare benefit plans. The increase in net occupancy expense was also partially attributable to acquisitions. Amortization of goodwill increased by 39.7% over prior year.

For the first nine months of 2001, noninterest expenses increased 8.3% to $194,657,000 from $179,662,000 for the same period last year. Contributing to the increase in year-to-date noninterest expenses were increases in salaries, employee benefits and net occupancy expense. Amortization expense for the first three quarters of 2001 increased 101.5% due to prior year's bank acquisitions.

Analysis of Financial Condition

At September 30, 2001, total assets increased 5.9% to $9,468,004,000 compared to $8,938,030,000 at December 31, 2000. Loans at September 30, 2001 were $6,900,139,000, an increase of 3.1% from the $6,693,294,000 level at December 31, 2000.

Total deposits increased 6.6% to $7,247,724,000 as of September 30, 2001 from $6,796,541,000 at year-end 2000. Interest-bearing deposits were $5,458,235,000, an increase of 4.9% from December 31, 2000. Interest-bearing deposits at September 30, 2001 were 75.3% of total deposits and at December 31, 2000 they were 76.6%. Noninterest-bearing deposits increased 12.3% to $1,789,489,000 as of September 30, 2001, compared to $1,593,503,000 at the end of 2000.

Total shareholders' equity increased 4.3% to $1,224,144,000 at September 30, 2001, from $1,173,301,000 at December 31, 2000. The increase in shareholders' equity is net of 1,500,000 shares that were repurchased during the third quarter of 2001. For more details see the Statement of Changes in Consolidated Shareholders' Equity on page 5.

Asset Quality

Nonperforming Assets

Nonperforming assets consist of nonaccrual loans, renegotiated loans and other real estate owned (i.e., real estate acquired in foreclosure or in lieu of foreclosure). With respect to nonaccrual loans, the Corporation's policy is that, regardless of the value of the underlying collateral and/or guarantees, no interest is accrued on the entire balance once either principal or interest payments on any loan become 90 days past due at the end of a calendar quarter. All accrued and uncollected interest on such loans is eliminated from the income statement and is recognized only as collected. A loan may be put on nonaccrual status sooner than this standard if, in management's judgement, such action is warranted. During the nine months ended September 30, 2001, nonperforming assets increased $2,869,000 to $34,239,000. Nonperforming loans, one of the components of nonperforming assets, increased $3,679,000 while other real estate owned, the other component, decreased $810,000. Nonperforming assets as a percent of period-end loans and other real estate owned was .50% at September 30, 2001 and .47% at the end of last year. Nonperforming assets reported at September 30, 2001 compared favorably to the $38,404,000 or .55% of period-end loans reported at June 30, 2001.

The table below presents a comparison of nonperforming assets at September 30, 2001 and December 31, 2000.

Nonperforming Assets (Dollars in thousands)	September 30, 2001	December 31, 2000
Nonaccrual loans (1)	$34,044	$30,365
Renegotiated loans (1)	--	--
Loans contractually past due 90 days or more and still accruing interest	--	--
Total nonperforming loans	34,044	30,365
Other real estate owned	195	1,005
Total nonperforming assets	$34,239	$31,370
Nonperforming assets as a percent of period-end loans and other real estate owned	.50%	.47%

(1) Aggregate gross interest income of $2,531,000 and $3,276,000 for the first three quarters of 2001 and the year 2000, respectively, on nonaccrual and renegotiated loans, would have been recorded if these loans had been accruing on their original terms throughout the period or since origination if held for part of the period. The amount of interest income on the nonaccrual and renegotiated loans that was recorded totalled $491,000 and $1,126,000 for the first nine months of 2001 and the year 2000, respectively.

Note: The Corporation was monitoring loans estimated to aggregate $4,571,000 at September 30, 2001 and $3,778,000 at December 31, 2000, not classified as nonaccrual or renegotiated loans. These loans had characteristics which indicated they might result in such classification in the future.

Allowance and Provision for Loan Losses

Each Mercantile Bankshares Corporation (MBC) affiliate is required to maintain an allowance for loan losses adequate to absorb inherent losses in the loan portfolio. Management at each affiliate, along with MBC management, maintains a regular overview to assure that adequacy. On a periodic basis, significant credit exposures, nonperforming loans, impaired loans, historical losses by loan type and various statistical measurements of asset quality are examined to assure the adequacy of the allowance for loan losses.

The allowance for loan losses has been established through provisions for loan losses charged against income. The provision for loan losses for the first three quarters of 2001 was $9,230,000 and $12,745,000 for the same period last year. Loans deemed to be uncollectible are charged against the allowance for loan losses and any subsequent recoveries are credited to the allowance. Intensive collection efforts continue after charge-off in order to maximize recovery amounts. Net charge-offs were $6,839,000 for the first nine months of 2001 compared to $1,193,000 for the same period in 2000. A substantial portion of the loans charged off during 2001 related to one lease financing receivable. The allowance for loan losses to period-end loans was 2.04% at September 30, 2001 and 2.07% at the end of the third quarter of last year.

The following table presents a summary of the activity in the Allowance for Loan Losses:

Allowance for Loan Losses (Dollars in thousands)	For the 9 Months Ended September 30, 2001	For the 9 Months Ended September 30, 2000	For the 3 Months Ended September 30, 2001	For the 3 Months Ended September 30, 2000
Allowance balance -- beginning..................	$ 138,612	$ 117,997	$ 143,605	$ 126,508
Allowance of acquired bank...	--	3,660	--	3,660
Charge-offs:				
Commercial..................	(614)	(1,635)	(321)	(1,498)
Real estate -- construction.............	--	(11)	--	--
Real estate -- mortgage.....	(112)	(497)	(33)	(32)
Consumer....................	(2,432)	(2,012)	(907)	(739)
Lease financing............	(5,828)	--	(5,175)	--
Total......................	(8,986)	(4,155)	(6,436)	(2,269)
Recoveries:				
Commercial..................	535	1,344	100	660
Real estate -- construction.............	66	176	37	1
Real estate -- mortgage.....	205	319	33	13
Consumer....................	1,341	1,123	563	320
Lease financing............	--	--	--	--
Total......................	2,147	2,962	733	994
Net (charge-offs)/recoveries...........	(6,839)	(1,193)	(5,703)	(1,275)
Provision for loan losses....	9,230	12,745	3,101	4,316
Allowance balance -- ending..	$ 141,003	$ 133,209	$ 141,003	$ 133,209
Average loans................	$ 6,849,998	$ 6,042,438	$6,939,110	$6,320,282
Net (charge-offs)/recoveries -- annualized as a percent of average loans..............	.13%	.03%	.33%	.08%
Period-end loans............	$ 6,900,139	$ 6,436,612		
Allowance for loan losses as a percent of period-end loans......................	2.04%	2.07%		

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Recent FASB Pronouncements

On July 20, 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standard (SFAS) No. 141, Business Combinations and SFAS No. 142, Goodwill and Other Intangible Assets. SFAS No. 141 eliminates the pooling-of-interests method of accounting for business combinations, with limited exceptions for combinations initiated prior to July 1, 2001. Additionally, it further clarifies the criteria for recognition of intangible assets separately from goodwill. This Statement is effective for business combinations completed after June 30, 2001.

SFAS No. 142 discontinues the amortization of goodwill and intangible assets with indefinite lives. Instead these assets will be subject to at least an annual impairment review, and more frequently if certain impairment indicators are in evidence. Mercantile Bankshares will adopt SFAS No. 142 on January 1, 2002. Based on current amortization schedules, application of the nonamortization provisions of the Statement is expected to result in additional net income of $7.8 million for the year ended December 31, 2002. The first of the required impairment tests of goodwill will be performed during 2002. The impact, if any, of these impairment tests on the 2002 financial statements has not yet been assessed.

SFAS No. 143, Accounting for Asset Retirement Obligations, was issued in June 2001. This Statement addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and associated retirement costs. It requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred and the associated asset retirement costs be capitalized as part of the carrying amount of the long-lived asset. This Statement is effective for financial statements issued for fiscal years beginning after June 15, 2002. SFAS No. 143 is not expected to have a material effect on the Corporation's financial statements.

SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, was issued in August 2001. This Statement addresses financial accounting and reporting for the impairment or disposal of long-lived assets. It also establishes a single accounting model for long-lived assets to be disposed of by sale, which includes long-lived assets that are part of a discontinued operation. This Statement is effective for financial statements issued for fiscal years and interim periods beginning after December 15, 2001. SFAS No. 144 is not expected to have a material effect on the Corporation's financial statements.

Cautionary Statement

This report contains forward-looking statements within the meaning of and pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. A forward-looking statement encompasses any estimate, prediction, opinion or statement of belief contained in this report, and the underlying management assumptions. Such statements in this report include identification of trends, loan growth, comments on adequacy of the allowance for loan losses, effects of asset sensitivity and interest rate changes, and information concerning market risk referenced in Item 3. Forward-looking statements are based on current expectations and assessments of potential developments affecting market conditions, interest rates and other economic conditions, and results may ultimately vary from the statements made in this report.

MERCANTILE BANKSHARES CORPORATION

ANALYSIS OF INTEREST RATES AND INTEREST DIFFERENTIALS

The following table presents the distribution of the average consolidated balance sheets, interest income/expense and annualized yields earned and rates paid through the first nine months of 2001 and 2000.

	2001			2000		
(Dollars in thousands)	Average Balance	Income*/ Expense	Yield*/ Rate	Average Balance	Income*/ Expense	Yield*/ Rate
Earning assets						
Loans:						
Commercial...........	$2,366,886	$148,639	8.40%	$2,195,136	$152,490	9.28%
Real estate..........	3,682,316	225,005	8.17	3,111,515	202,398	8.69
Consumer.............	800,796	50,824	8.49	735,787	47,721	8.66
Total loans.........	6,849,998	424,468	8.28	6,042,438	402,609	8.90
Federal funds sold.....	105,641	3,295	4.17	27,965	1,313	6.27
Securities purchased under resale agreements...........	2,930	75	3.42	--	--	--
Securities:**						
Taxable securities						
U.S. Treasury securities..........	1,331,986	55,096	5.53	1,565,008	65,649	5.60
U.S. Agency securities..........	300,149	13,794	6.14	73,453	3,683	6.70
Other stocks and bonds...............	60,906	3,608	7.92	32,882	2,003	8.14
Tax-exempt securities						
States and political subdivisions........	40,603	2,492	8.21	20,892	1,290	8.25
Total securities....	1,733,644	74,990	5.78	1,692,235	72,625	5.73
Interest-bearing deposits in other banks.................	368	14	5.12	153	6	4.94
Total earning assets.............	8,692,581	502,842	7.73	7,762,791	476,553	8.20
Cash and due from banks..................	213,652			223,688		
Bank premises and equipment, net.........	103,304			97,539		
Other assets............	259,555			202,813		
Less: allowance for loan losses................	(142,469)			(124,395)		

Total assets........	$9,126,623			$8,162,436		
Interest-bearing liabilities						
Deposits:						
Savings deposits......	$2,422,166	32,425	1.79	$2,346,591	36,090	2.05
Time deposits $100,000 and over............	1,153,200	49,631	5.75	817,927	36,371	5.94
Other time deposits...	1,825,978	76,185	5.58	1,505,162	57,771	5.13
Total interest-bearing deposits...	5,401,344	158,241	3.92	4,669,680	130,232	3.73
Short-term borrowings..	739,080	21,816	3.95	859,715	36,022	5.60
Long-term debt.........	89,669	4,425	6.60	86,045	4,304	6.68
Total interest-bearing funds......	6,230,093	184,482	3.96	5,615,440	170,558	4.06
Noninterest-bearing deposits..............	1,585,413			1,419,046		
Other liabilities and accrued expenses.......	115,667			98,420		
Total liabilities...	7,931,173			7,132,906		
Shareholders' equity....	1,195,450			1,029,530		
Total liabilities and shareholders' equity............	$9,126,623			$8,162,436		
Net interest income.....		$318,360			$305,995	
Net interest rate spread................			3.77%			4.14%
Effect of noninterest-bearing funds.........			1.13			1.13
Net interest margin on earning assets.........			4.90%			5.27%
Taxable-equivalent adjustment included in:						
Loan income...........		$ 3,767			$ 3,248	
Investment securities income..............		1,116			649	
Total..............		$ 4,883			$ 3,897	

*Presented on a tax-equivalent basis using the statutory federal corporate income tax rate of 35%.
**Balances reported at amortized cost; excludes pretax unrealized gains (losses) on securities available-for-sale.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Information responsive to this Item as of December 31, 2000 appears under the captions "Asset/Liability and Liquidity Management", "Interest Rate Sensitivity Analysis" and "Earnings Simulation Model Projections" on pages 20-22 of the registrant's 2000 Annual Report to Shareholders, filed as Exhibit 13 to registrant's Annual Report on Form 10-K for the year ended December 31, 2000. The information in the Annual Report disclosed that the Corporation was asset sensitive, with net interest income decreasing in a declining rate environment. With the reduction in short-term interest rates by the Federal Reserve during 2001, the Corporation's banking affiliates, as well as the industry in general, are finding it increasingly difficult to reduce the interest rates paid on core deposits. As a result, the Corporation remains asset sensitive and subject to compression of the net interest margin in a declining rate environment.

PART II. OTHER INFORMATION
Item 5. Other Information

The 2002 Annual Meeting of Stockholders of the registrant is expected to be held on April 24, 2002.

Item 6. Exhibits and Reports on Form 8-K

(b) Form 8-K filed, dated July 19, 2001, Item 5.

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.

MERCANTILE BANKSHARES CORPORATION

November 8, 2001

Principal Executive Officer

/s/ Edward J. Kelly, III

By: Edward J. Kelly, III
President and
Chief Executive Officer

November 8, 2001

Principal Financial Officer

/s/ Terry L. Troupe

By: Terry L. Troupe
Chief Financial Officer

November 8, 2001

Chief Accounting Officer

/s/ Diana E. Nelson

By: Diana E. Nelson
Controller and Chief Accounting Officer