TF FINANCIAL CORP
Form 10-Q
November 13, 2006

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the period ended September 30, 2006

- or -

o 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: 0-24168

TF FINANCIAL CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**74-2705050**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
3 Penns Trail, Newtown, Pennsylvania	**18940**
(Address of Principal Executive Offices)	(Zip Code)

Registrant s telephone number, including area code: **(215) 579-4000**

Securities registered pursuant to Section 12(b) of the Act: **None**

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

Common Stock, par value $.10 per share

(Title of Class)

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 o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 Exchange Act). YES o NO x

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of the latest practicable date: October 30, 2006

Class	Outstanding
$.10 par value common stock	2,871,493 shares

CONTENTS

TF Financial Corporation and Subsidiaries

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

	Unaudited September 30, 2006 (in thousands)	**Audited December 31, 2005**
ASSETS		
Cash and cash equivalents	$ 6,492	$ 3,821
Certificates of deposit in other financial institutions	40	40
Investment securities available for sale at fair value	34,471	30,401
Investment securities held to maturity (fair value of $1,681 and $4,707 respectively)	1,676	4,690
Mortgage-backed securities available for sale at fair value	66,614	83,511
Mortgage-backed securities held to maturity (fair value of $8,124 and $10,385, respectively)	8,038	10,177
Loans receivable, net (including loans held for sale of $660 and $68, respectively)	500,029	490,959
Federal Home Loan Bank stock at cost	7,534	7,432
Accrued interest receivable	2,782	3,048
Premises and equipment, net	6,477	6,289
Core deposit intangible asset, net of accumulated amortization of $2,824 and $2,741, respectively		83
Goodwill	4,324	4,324
Other assets	16,300	16,064
TOTAL ASSETS	$ 654,777	$ 660,839
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities		
Deposits	$ 470,398	$ 470,521
Advances from the Federal Home Loan Bank	111,366	121,260
Advances from borrowers for taxes and insurance	1,284	1,915
Accrued interest payable	3,761	2,052
Other liabilities	2,581	2,443
Total liabilities	589,390	598,191
Stockholders equity		
Preferred stock, no par value; 2,000,000 shares authorized at September 30, 2006 and December 31, 2005, none issued		
Common stock, $0.10 par value; 10,000,000 shares authorized, 5,290,000 shares issued, 2,700,121 and 2,714,173 shares outstanding at September 30, 2006 and December 31, 2005, respectively, net of shares in treasury 2,418,630 and 2,390,943, respectively	529	529
Retained earnings	64,131	61,610
Additional paid-in capital	52,787	53,048
Unearned restricted stock		(1,080)
Unearned ESOP shares	(1,712)	(1,849)
Treasury stock at cost	(48,923)	(47,920)
Accumulated other comprehensive loss	(1,425)	(1,690)
Total stockholders equity	65,387	62,648
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 654,777	$ 660,839

The accompanying notes are an integral part of these statements

3

TF Financial Corporation and Subsidiaries

CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	For the three months ended September 30, 2006	2005	For the nine months ended September 30, 2006	2005
	(in thousands, except per share data)			
Interest income				
Loans, including fees	$ 8,243	$ 7,032	$ 24,081	$ 20,206
Mortgage-backed securities	872	1,135	2,841	3,730
Investment securities	453	383	1,354	1,060
Interest-bearing deposits and other	43	20	65	42
TOTAL INTEREST INCOME	9,611	8,570	28,341	25,038
Interest expense				
Deposits	2,949	2,052	7,757	5,419
Borrowings	1,144	935	3,880	2,832
TOTAL INTEREST EXPENSE	4,093	2,987	11,637	8,251
NET INTEREST INCOME	5,518	5,583	16,704	16,787
Provision for loan losses		150	150	450
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	5,518	5,433	16,554	16,337
Non-interest income				
Service fees, charges and other operating income	661	632	1,980	1,941
Gain on sale of loans	152	110	190	140
Loss on sale of mortgage-backed securities available for sale			(51)	
TOTAL NON-INTEREST INCOME	813	742	2,119	2,081
Non-interest expense				
Employee compensation and benefits	2,693	2,322	8,015	7,016
Occupancy and equipment	772	651	2,170	1,952
Federal deposit insurance premium	15	15	45	48
Professional fees	128	211	475	648
Marketing and advertising	176	191	528	553
Other operating	559	660	1,725	1,839
Amortization of core deposit intangible asset	27	34	83	102
TOTAL NON-INTEREST EXPENSE	4,370	4,084	13,041	12,158
INCOME BEFORE INCOME TAXES	1,961	2,091	5,632	6,260
Income taxes	549	546	1,573	1,634
NET INCOME	$ 1,412	$ 1,545	$ 4,059	$ 4,626
Earnings per share basic	$ 0.52	$ 0.57	$ 1.50	$ 1.69
Earnings per share diluted	$ 0.52	$ 0.55	$ 1.49	$ 1.64
Dividends paid	$ 0.19	$ 0.18	$ 0.57	$ 0.54

The accompanying notes are an integral part of these statements

4

TF Financial Corporation and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the nine months ended September 30, 2006 (in thousands)	2005
OPERATING ACTIVITIES		
Net income	$ 4,059	$ 4,626
Adjustments to reconcile net income to net cash provided by operating activities		
Amortization of		
Mortgage loan servicing rights	23	3
Deferred loan origination fees	(151)	(44)
Premiums and discounts on investment securities, net	49	59
Premiums and discounts on mortgage-backed securities, net	201	354
Premiums and discounts on loans, net	129	85
Discount on brokered deposits	12	
Core deposit intangibles	83	102
Provision for loan losses	150	450
Provision for decline in market value of MSR s	5	
Depreciation of premises and equipment	708	713
Increase in value of bank-owned life insurance	(373)	(377)
Stock grant expense	271	
Stock option expense	287	
Stock-based benefit programs: ESOP	402	376
Tax benefit arising from stock compensation	102	110
Proceeds from sale of loans originated for sale	8,380	7,388
Origination of loans held for sale	(8,911)	(7,160)
(Gain) loss on the sale of		
Mortgage loans available for sale	(60)	(57)
Mortgage-backed securities available for sale	51	
Real estate acquired through foreclosure	(29)	
Mortgage loans held to maturity	(130)	(83)
Income from mortgage loan derivatives	(1)	
Loss associated with forward loan sales	3	
(Increase) decrease in		
Accrued interest receivable	266	(2)
Other assets	(731)	(259)
Increase in		
Accrued interest payable	1,709	661
Other liabilities	138	834
NET CASH PROVIDED BY OPERATING ACTIVITIES	6,642	7,779
INVESTING ACTIVITIES		
Loan originations	(101,166)	(118,330)
Loan principal payments	71,412	86,718
Principal repayments on mortgage-backed securities held to maturity	2,133	3,506
Principal repayments on mortgage-backed securities available for sale	11,754	23,254
Proceeds from loan sales	16,251	1,108
Proceeds from sale of loan participations	5,027	
(Purchases) and maturities of certificates of deposit in other financial institutions, net		(2)
Purchase of investment securities available for sale	(3,795)	(10,821)
Purchase of mortgage-backed securities available for sale		(8,956)
Proceeds from maturities of investment securities held to maturity	3,018	1,280
Proceeds from the sale of mortgage-backed securities available for sale	4,971	

Purchase of Federal Home Loan Bank stock	(102)	(273)

5

	For the nine months ended September 30, 2006 (in thousands)	2005
Proceeds from the sale of real estate acquired through foreclosure	729	
Purchase of premises and equipment	(896)	(869)
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	9,336	(23,385)
FINANCING ACTIVITIES		
Net increase (decrease) in demand deposit/NOW accounts, passbook savings accounts and certificates of deposit	(135)	4,983
Net increase (decrease) in short-term Federal Home Loan Bank advances	(11,436)	6,499
Proceeds of long-term Federal Home Loan Bank advances	15,535	16,367
Repayment of long-term Federal Home Loan Bank advances	(13,993)	(11,303)
Net decrease in advances from borrowers for taxes and insurance	(631)	(548)
Treasury stock acquired	(1,421)	(1,773)
Exercise of stock options	312	602
Common stock dividends paid	(1,538)	(1,479)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	(13,307)	13,348
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	2,671	(2,258)
Cash and cash equivalents at beginning of period	3,821	7,900
Cash and cash equivalents at end of period	$ 6,492	$ 5,642
Supplemental disclosure of cash flow information		
Cash paid for		
Interest on deposits and advances from Federal Home Loan Bank	$ 9,928	$ 7,590
Income taxes	$ 1,415	$ 910

The accompanying notes are an integral part of these statements

TF FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - PRINCIPLES OF CONSOLIDATION

The consolidated financial statements as of September 30, 2006 (unaudited) and December 31, 2005 and for the nine-month periods ended September 30, 2006 and 2005 (unaudited) include the accounts of TF Financial Corporation (the Company) and its wholly owned subsidiaries Third Federal Bank (the Bank), TF Investments Corporation and Penns Trail Development Corporation. The Company s business is conducted principally through the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

NOTE 2 - BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and, therefore, do not include all of the disclosures or footnotes required by accounting principles generally accepted in the United States of America. In the opinion of management, all adjustments, consisting of normal recurring accruals, necessary for fair presentation of the consolidated financial statements have been included. The results of operations for the period ended September 30, 2006 are not necessarily indicative of the results which may be expected for the entire fiscal year or any other period. For further information, refer to consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2005.

NOTE 3 CONTINGENCIES

The Company, from time to time, is a party to routine litigation that arises in the normal course of business. In the opinion of management, the resolution of this litigation, if any, would not have a material adverse effect on the Company s consolidated financial position or results of operations.

NOTE 4 - OTHER COMPREHENSIVE INCOME

The Company s other comprehensive income consists of net unrealized losses on investment securities and mortgage-backed securities available for sale. Total comprehensive income for the three-month periods ended September 30, 2006 and 2005 was $2,603,000 and $506,000, net of applicable income tax expense of $1,163,000 and $11,000 respectively. Total comprehensive income for the nine-month periods ended September 30, 2006 and 2005 was $4,324,000 and $3,421,000, net of applicable income tax expense of $1,708,000 and $1,014,000, respectively.

NOTE 5 EARNINGS PER SHARE

The following tables illustrate the reconciliation of the numerators and denominators of the basic and diluted earnings per share computations (dollars in thousands, except per share data):

	Three months ended September 30, 2006		
	Income (numerator)	Weighted average shares (denominator)	Per share Amount
Basic earnings per share			
Income available to common stockholders	$ 1,412	2,698,490	$ 0.52
Effect of dilutive securities			
Stock options		21,858	
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	$ 1,412	2,720,348	$ 0.52

	Nine months ended September 30, 2006		
	Income (numerator)	Weighted average shares (denominator)	Per share Amount
Basic earnings per share			
Income available to common stockholders	$ 4,059	2,697,629	$ 1.50
Effect of dilutive securities			
Stock options		18,972	(0.01)
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	$ 4,059	2,716,601	$ 1.49

There were options to purchase 20,768 shares of common stock at a price of $34.14 per share which were outstanding during the nine months ended September 30, 2006 that were not included in the computation of diluted earnings per share because the options exercise prices were greater than the average market price of the common shares.

	Three months ended September 30, 2005		
	Income (numerator)	Weighted average shares (denominator)	Per share Amount
Basic earnings per share			
Income available to common stockholders	$ 1,545	2,732,451	$ 0.57
Effect of dilutive securities			
Stock options		63,247	(0.02)
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	$ 1,545	2,795,698	$ 0.55

	Nine months ended September 30, 2005		
	Income (numerator)	Weighted average shares (denominator)	Per share Amount
Basic earnings per share			
Income available to common stockholders	$ 4,626	2,741,848	$ 1.69
Effect of dilutive securities			
Stock options		70,671	(0.05)
Diluted earnings per share			
Income available to common stockholders plus effect of dilutive securities	$ 4,626	2,812,519	$ 1.64

There were options to purchase 41,284 shares of common stock at a weighted average price of $32.00 per share which were outstanding during the nine months ended September 30, 2005 that were not included in the computation of diluted earnings per share because the options exercise prices were greater than the average market price of the common shares.

NOTE 6- STOCK BASED COMPENSATION

The Company has stock benefit plans that allow the Company to grant options and stock to employees and directors. The options, which have a term of up to 10 years when issued, vest over a three to five year period. The exercise price of each option equals the market price of the Company s stock on the date of the grant.

On January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards (SFAS) 123R, Share-Based Payment, using the modified prospective transition method. Under this transition method, compensation cost to be recognized beginning in the first quarter of 2006 includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. Stock-based compensation expense included in net income related to stock options was $98,000, resulting in a tax benefit of $29,000, for the three months ended September 30, 2006. Stock-based compensation expense included in net income related to stock options was $287,000, resulting in a tax benefit of $86,000, for the nine months ended September 30, 2006. Results for prior periods have not been restated. As of September 30, 2006, there was $909,000 of total unrecognized compensation cost, net of estimated forfeitures, related to non-vested options under the Plan. That cost is expected to be recognized over a weighted average period of 27.5 months

Prior to 2006, the Company disclosed pro forma compensation expense quarterly and annually by calculating the stock option grant s fair value using the intrinsic value method under APB Opinion No. 25, Accounting for Stock Issued to Employees , as permitted by SFAS No. 123 Accounting for Stock-Based Compensation, which contains a fair value-based method for valuing stock-based compensation that entities may use, which measures compensation cost at the grant date based on the fair value of the award. Compensation is then recognized over the service period, which is usually the vesting period. No stock-based compensation expense related to stock options was reflected in net income in 2005, as all options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of the grant.

The tables below reflect the estimated impact the fair value method would have had on the Company s net income and net income per share if SFAS 123R had been in effect for the three and nine months ended September 30, 2005 (dollars in thousands except per share data):

Three months ended September 30, 2005	**Net income**	**Basic earnings per share**	**Diluted earnings per share**
As reported	$ 1,545	$ 0.57	$ 0.55
Deduct: stock-based compensation expense determined using the fair value method, net of related tax effects	17	0.01	
Pro forma	$ 1,528	$ 0.56	$ 0.55
Nine months ended September 30, 2005			
As reported	$ 4,626	$ 1.69	$ 1.64
Deduct: stock-based compensation expense determined using the fair value method, net of related tax effects	51	0.02	
Pro forma	$ 4,575	$ 1.67	$ 1.64

Option activity under the Company s stock option plan as of September 30, 2006 is as follows:

	2006			
	Number of shares	**Weighted average exercise price per share**	**Weighted average remaining contractual term (in years)**	**Aggregate intrinsic value ($000)**
Outstanding at January 1, 2006	384,848	$ 23.18		
Options granted	11,000	27.20		
Options exercised	20,717	15.07		
Options forfeited	8,509	29.69		
Outstanding at September 30, 2006	366,622	$ 23.61	3.56	$ 2,577
Options exercisable at September 30, 2006	179,391	$ 18.48	3.33	$ 2,181

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company s closing stock price on the last trading day of the third quarter of 2006 and the exercise price, multiplied by the number of in-the money options).

Stock options outstanding were 366,622 and 255,138 at September 30, 2006 and 2005, respectively. The aggregate intrinsic value of options exercised during the nine months ended September 30, 2006 and 2005 was $311,000 and $549,000, respectively. Exercise of stock options during the nine months ended September 30, 2006 and 2005 resulted in cash receipts of $312,000 and $602,000, respectively.

Stock-based compensation expense included in net income related to stock grants was $90,000 for the three months ended September 30, 2006. Stock-based compensation expense included in net income related to the Company s employee stock ownership plan totaled $88,000 and $91,000 for the three-month periods ended September 30, 2006 and 2005, respectively.

Stock-based compensation expense included in net income related to stock grants was $271,000 for the nine months ended September 30, 2006. Stock-based compensation expense included in net income related to the Company s employee stock ownership plan totaled $303,000 and $295,000 for the nine-month periods ended September 30, 2006 and 2005, respectively.

NOTE 7- EMPLOYEE BENEFIT PLANS

Net periodic defined benefit pension cost included the following (in thousands):

	Three months ended September 30 2006	2005
Components of net periodic benefit cost		
Service cost	$ 77	$ 78
Interest cost	53	53
Expected return on plan assets	(81)	(56)
Amortization of prior service cost	16	16
Recognized net actuarial (gain) loss	12	11
Net periodic benefit cost	$ 77	$ 102

	Nine months ended September 30 2006	2005
Components of net periodic benefit cost		
Service cost	$ 231	$ 234
Interest cost	158	159
Expected return on plan assets	(242)	(159)
Amortization of prior service cost	47	48
Amortization of transition obligation (asset)		
Recognized net actuarial (gain) loss	38	33
Net periodic benefit cost	$ 232	$ 315

The employer contributions made for the nine months ended September 30, 2006 and 2005 were $620,000 and $1,015,000, respectively. It is the policy of the Company to fund the maximum amount allowable under the individual aggregate cost method to the extent deductible under existing federal income tax regulations. The Company expects to make a contribution of $1.3 million prior to year-end.

NOTE 8- RECLASSIFICATIONS

Certain prior period amounts have been reclassified to conform to the current period presentation.

TF FINANCIAL CORPORATION AND SUBSIDIARIES

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

GENERAL

The Company may from time to time make written or oral forward-looking statements , including statements contained in the Company s filings with the Securities and Exchange Commission (including this Quarterly Report on Form 10-Q and the exhibits thereto), in its reports to stockholders and in other communications by the Company, which are made in good faith by the Company pursuant to the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements involve risks and uncertainties, such as statements of the Company s plans, objectives, expectations, estimates and intentions that are subject to change based on various important factors (some of which are beyond the Company s control). The following factors, among others, could cause the Company s financial performance to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System, inflation, interest rate, market and monetary fluctuations; the timely development of and acceptance of new products and services of the Company and the perceived overall value of these products and services by users, including the features, pricing and quality compared to competitors products and services; the willingness of users to substitute competitors products and services for the Company s products and services; the success of the Company in gaining regulatory approval of its products and services, when required; the impact of changes in financial services laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes, acquisitions; changes in consumer spending and saving habits; and the success of the Company at managing the risks involved in the foregoing.

The Company cautions that the foregoing list of important factors is not exclusive. The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company.

Financial Position

The Company s total assets at September 30, 2006 and December 31, 2005 were $654.8 million and $660.8 million, respectively, a decrease of $6.0 million, or 0.9%, during the nine-month period. Cash and cash equivalents increased by $2.7 million. Investment securities available for sale increased by $4.1 million due to purchases of $3.8 million of tax free municipal bonds and a $0.3 million increase in the market value of investment securities available for sale. Investment securities held to maturity decreased by $3.0 million as a result of security maturities. Mortgage-backed securities available for sale decreased by $16.9 million due to sales of $5.0 million, principal repayments of $11.8 million, and amortization of net premiums totaling $0.2 million offset by an increase in the market value of these securities of $0.1 million. Mortgage-backed securities held to maturity decreased by $2.1 million as a result of principal repayments.

Loans receivable increased by $9.1 million during the first nine months of 2006. Consumer and single-family residential mortgage loans of $49.9 million and commercial loans of $51.3 million were originated during the first nine months of 2006. Principal repayments of loans receivable were $71.4 million and proceeds from sales of loan participations totaled $5.0 million in the first nine months of 2006. Additionally, the Company sold $16.3 million of previously purchased loans. Loans originated for sale during this period totaled $8.9 million, and there were $8.4 million in proceeds from the sale of these loans in the secondary market during this period. In June 2006, the Company sold for $0.7 million the sole parcel of foreclosed real estate owned at December 31, 2005.

Total liabilities decreased by $8.8 million. Deposit balances decreased by $0.1 million during the first nine months of 2006. Savings, money market, interest-bearing, and non-interest bearing checking accounts decreased by a combined $43.4 million. Retail certificates of deposit increased by $31.6 million and broker originated deposits received during the second quarter of 2006 totaled $11.7 million. Advances from the Federal Home Loan Bank decreased by $9.9 million due to scheduled amortization payments of $14.0 million and repayments of $11.4 million of short term advances offset by a $15.5 million increase in long-term fixed rate advances,.

Total consolidated stockholders equity of the Company was $65.4 million or 10.0% of total assets at September 30, 2006. During the first nine months of 2006 the Company repurchased 48,404 shares of its common stock and issued 20,717 shares pursuant to the exercise of stock options. As of September 30, 2006, there were approximately 76,000 shares available for repurchase under the previously announced share repurchase plan.

Asset Quality

During the first nine months of 2006 and 2005, the Company s provision for loan losses was $150,000 and $450,000, respectively. Management of the Company believes that there has not been any significant deterioration in its asset quality during the first nine months of 2006.

The following table sets forth information regarding the Company s asset quality (dollars in thousands):

	September 30, 2006		**December 31, 2005**		**September 30, 2005**	
Non-performing loans	$ 1,131		$ 1.588		$ 570	
Ratio of non-performing loans to gross loans	0.22	%	0.32	%	0.12	%
Ratio of non-performing loans to total assets	0.17	%	0.24	%	0.09	%
Foreclosed property	$ 0		$ 700		$ 700	
Foreclosed property to total assets	N/A		0.11	%	0.11	%
Ratio of total non-performing assets to total assets	0.17	%	0.35	%	0.20	%
Ratio of allowance for loan losses to total loans	0.56	%	0.54	%	0.53	%
Ratio of allowance for loan losses to non-performing loans	248.45	%	166.31	%	176.12	%

Management maintains an allowance for loan losses at levels that are believed to be adequate; however, there can be no assurances that further additions will not be necessary or that losses inherent in the existing loan portfolio will not exceed the allowance. The following table sets forth the activity in the allowance for loan losses during the periods indicated (in thousands):

	2006		**2005**
Beginning balance, January 1,	$ 2,641		$ 2,307
Provision	150		450
Less: charge-off s (recoveries), net	(19	)	249
Ending balance, September 30,	2,810		2,508

13

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005

Net Income. The Company recorded net income of $1,412,000, or $0.52 per diluted share, for the three months ended September 30, 2006 as compared to net income of $1,545,000, or $0.55 per diluted share, for the three months ended September 30, 2005.

Average Balance Sheet

The following table sets forth information (dollars in thousands) relating to the Company s average balance sheet and reflects the average yield on assets and average cost of liabilities for the periods indicated. Yield and cost are computed by dividing income or expense by the average daily balance of interest-earning assets or interest-bearing liabilities, respectively, at-or for the three-month periods indicated.

	September 30, 2006 Average balance	Interest	Average yld/cost	2005 Average balance	Interest	Average yld/cost
ASSETS						
Interest-earning assets:						
Loans receivable(1)	$ 501,012	$ 8,243	6.53 %	$ 465,712	$ 7,032	5.99 %
Mortgage-backed securities	75,620	872	4.57 %	104,148	1,135	4.32 %
Investment securities(2)	41,957	555	5.25 %	39,553	466	4.67 %
Other interest-earning assets(3)	2,987	43	5.71 %	2,631	20	3.02 %
Total interest-earning assets	621,576	9,713	6.20 %	612,044	8,653	5.61 %
Non interest-earning assets	35,058			33,179		
Total assets	$ 656,634			$ 645,223		
LIABILITIES AND STOCKHOLDERS EQUITY						
Interest-bearing liabilities:						
Deposits	$ 471,556	2,949	2.48 %	$ 473,801	2,052	1.72 %
Advances from the FHLB	114,070	1,144	3.98 %	104,918	935	3.54 %
Total interest-bearing liabilities	585,626	4,093	2.77 %	578,719	2,987	