

CONSUMERS BANCORP INC /OH/  
Form 10-Q  
November 14, 2012

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

Quarterly Report Pursuant to Section 13 or 15 (d) or the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2012

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 No. 033-79130

**CONSUMERS BANCORP, INC.**

(Exact name of registrant as specified in its charter)

OHIO  
(State or other jurisdiction  
of incorporation or organization)

34-1771400  
(I.R.S. Employer Identification No.)

614 East Lincoln Way, P.O. Box 256, Minerva, Ohio  
(Address of principal executive offices)

44657  
(Zip Code)

(330) 868-7701

(Registrant's telephone number)

Not applicable

(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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.05 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if smaller reporting company) Smaller reporting company

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

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

Common Stock, no par value Outstanding at November 5, 2012  
2,060,743 Common Shares

**CONSUMERS BANCORP, INC.**

**FORM 10-Q**

**QUARTER ENDED September 30, 2012**

Table of Contents

	<b>Page Number (s)</b>
Part I – Financial Information	
Item 1 – Financial Statements (Unaudited)	
Consolidated Balance Sheets at September 30, 2012 and June 30, 2012	1
Consolidated Statements of Income for the three months ended September 30, 2012 and 2011	2
Consolidated Statements of Comprehensive Income for the three months ended September 30, 2012 and 2011	3
Consolidated Statements of Changes in Shareholders’ Equity for the three months ended September 30, 2012 and 2011	4
Condensed Consolidated Statements of Cash Flows for the three months ended September 30, 2012 and 2011	5
Notes to the Consolidated Financial Statements	6-26
Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations	27-37
Item 3 – Not Applicable for Smaller Reporting Companies	
Item 4 – Controls and Procedures	38
Part II – Other Information	
Item 1 – Legal Proceedings	39
Item 1A – Not Applicable for Smaller Reporting Companies	
Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds	39
Item 3 – Defaults Upon Senior Securities	39

Item 4 – Mine Safety Disclosure	39
Item 5 – Other Information	39
Item 6 – Exhibits	39
Signatures	40

## PART I – FINANCIAL INFORMATION

## Item 1 – Financial Statements

## CONSUMERS BANCORP, INC.

## CONSOLIDATED BALANCE SHEETS (Unaudited)

(Dollars in thousands, except per share data)	September 30, 2012	June 30, 2012
<b>ASSETS</b>		
Cash on hand and noninterest-bearing deposits in financial institutions	\$ 8,248	\$6,663
Federal funds sold and interest-bearing deposits in financial institutions	2,385	7,082
Total cash and cash equivalents	10,633	13,745
Certificates of deposit in other financial institutions	5,645	5,645
Securities, available-for-sale	105,662	105,335
Federal bank and other restricted stocks, at cost	1,186	1,186
Loans held for sale	408	377
Total loans	202,118	197,430
Less allowance for loan losses	(2,338	) (2,335 )
Net loans	199,780	195,095
Cash surrender value of life insurance	5,652	5,605
Premises and equipment, net	5,849	5,752
Accrued interest receivable and other assets	2,150	2,021
Total assets	\$ 336,965	\$334,761
<b>LIABILITIES</b>		
Deposits		
Non-interest bearing demand	\$ 66,131	\$65,915
Interest bearing demand	35,453	35,055
Savings	98,116	99,041
Time	84,757	84,470
Total deposits	284,457	284,481
Short-term borrowings		
Federal Home Loan Bank advances	15,005	13,722
Accrued interest and other liabilities	6,427	6,446
Total liabilities	2,316	2,222
Commitments and contingent liabilities	308,205	306,871
	—	—
<b>SHAREHOLDERS' EQUITY</b>		
Preferred stock (no par value, 350,000 shares authorized, none outstanding)	—	—
	5,258	5,205

Edgar Filing: CONSUMERS BANCORP INC /OH/ - Form 10-Q

Common stock (no par value, 3,500,000 shares authorized; 2,190,488 and 2,186,791 shares issued as of September 30, 2012 and June 30, 2012, respectively)		
Retained earnings	23,108	22,740
Treasury stock, at cost (129,745 and 130,442 common shares as of September 30, 2012 and June 30, 2012, respectively)	(1,650	) (1,659 )
Accumulated other comprehensive income	2,044	1,604
Total shareholders' equity	28,760	27,890
Total liabilities and shareholders' equity	\$ 336,965	\$ 334,761

See accompanying notes to consolidated financial statements

**CONSUMERS BANCORP, INC.****CONSOLIDATED STATEMENTS OF INCOME (Unaudited)**

(Dollars in thousands, except per share amounts)	Three Months ended	
	September 30, 2012	2011
Interest income		
Loans, including fees	\$2,605	\$2,535
Securities, taxable	383	480
Securities, tax-exempt	304	245
Federal funds sold and other interest bearing deposits	15	16
Total interest income	3,307	3,276
Interest expense		
Deposits	270	330
Short-term borrowings	6	11
Federal Home Loan Bank advances	50	60
Total interest expense	326	401
Net interest income	2,981	2,875
Provision for loan losses	25	92
Net interest income after provision for loan losses	2,956	2,783
Non-interest income		
Service charges on deposit accounts	342	356
Debit card interchange income	193	179
Bank owned life insurance income	47	51
Securities gains, net	21	49
Other	61	37
Total non-interest income	664	672
Non-interest expenses		
Salaries and employee benefits	1,565	1,326
Occupancy and equipment	314	258
Data processing expenses	85	139
Professional and director fees	92	94
FDIC Assessments	49	50
Franchise taxes	70	65
Marketing and advertising	117	76
Telephone and network communications	65	58
Debit card processing expenses	103	94
Amortization of intangible	-	41
Other	407	361
Total non-interest expenses	2,867	2,562
Income before income taxes	753	893
Income tax expense	138	206

Net Income	\$615	\$687
Basic and diluted earnings per share	\$0.30	\$0.34

See accompanying notes to consolidated financial statements



**CONSUMERS BANCORP, INC.**

Consolidated statements of comprehensive income

**(Unaudited)**

(Dollars in thousands)

	Three Months ended September 30, 2012    2011	
Net Income	\$615	\$687
Other comprehensive income, net of tax:		
Net change in unrealized gains:		
Available-for-sale securities:		
Unrealized gains arising during the period	689	446
Reclassification adjustment for gains included in income	(21 )	(49 )
Net unrealized gains	668	397
Income tax effect	228	135
Other comprehensive income	440	262
Total comprehensive income	\$1,055	\$949

See accompanying notes to consolidated financial statements.

**CONSUMERS BANCORP, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY****(Unaudited)**

(Dollars in thousands, except per share data)

	Three Months ended September 30,	
	2012	2011
Balance at beginning of period	\$27,890	\$25,324
Net Income	615	687
Other comprehensive income	440	262
Issuance of 697 shares for vested restricted stock awards	9	—
Common stock issued for dividend reinvestment and stock purchase plan (3,697 shares for three months in 2012)	53	—
Common cash dividends	(247 )	(226 )
Balance at the end of the period	\$28,760	\$26,047
Common cash dividends per share	\$0.12	\$0.11

See accompanying notes to consolidated financial statements.

**CONSUMERS BANCORP, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

(Dollars in thousands)	Three Months Ended September 30,	
	2012	2011
Cash flows from operating activities		
Net cash from operating activities	\$759	\$1,407
Cash flow from investing activities		
Securities available-for-sale		
Purchases	(5,478 )	(17,212 )
Maturities, calls and principal pay downs	4,973	5,660
Proceeds from sales of available-for-sale securities	530	4,951
Net decrease in certificates of deposits in other financial institutions	—	1,225
Net increase in loans	(4,710 )	(2,456 )
Acquisition of premises and equipment	(241 )	(26 )
Net cash from investing activities	(4,926 )	(7,858 )
Cash flow from financing activities		
Net increase (decrease) in deposit accounts	(24 )	14,108
Net change in short-term borrowings	1,283	624
Repayments of Federal Home Loan Bank advances	(19 )	(19 )
Issuance of treasury stock	9	—
Proceeds from dividend reinvestment and stock purchase plan	53	—
Dividends paid	(247 )	(226 )
Net cash from financing activities	1,055	14,487
Increase (decrease) in cash or cash equivalents	(3,112 )	8,036
Cash and cash equivalents, beginning of period	13,745	13,828
Cash and cash equivalents, end of period	\$10,633	\$21,864
Supplemental disclosure of cash flow information:		
Cash paid during the period:		
Interest	\$320	\$409
Federal income taxes	150	—

See accompanying notes to consolidated financial statements.



**CONSUMERS BANCORP, INC.**

**Notes to the Consolidated Financial Statements**

**(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

**Note 1 – Summary of Significant Accounting Policies:**

**Nature of Operations:** Consumers Bancorp, Inc. (the Corporation) is a bank holding company headquartered in Minerva, Ohio that provides, through its banking subsidiary, Consumers National Bank (the Bank), a broad array of products and services throughout its primary market area of Stark, Columbiana, Carroll and contiguous counties in Ohio. The Bank's business involves attracting deposits from businesses and individual customers and using such deposits to originate commercial, mortgage and consumer loans in its primary market area.

**Basis of Presentation:** The consolidated financial statements for interim periods are unaudited and reflect all adjustments (consisting of only normal recurring adjustments), which, in the opinion of management, are necessary to present fairly the financial position and results of operations and cash flows for the periods presented. The unaudited financial statements are presented in accordance with the requirements of Form 10-Q and do not include all disclosures normally required by accounting principles generally accepted in the United States of America. The financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Corporation's Form 10-K for the year ended June 30, 2012. The results of operations for the interim period disclosed herein are not necessarily indicative of the results that may be expected for a full year.

The consolidated financial statements include the accounts of the Corporation and the Bank. All significant inter-company transactions and accounts have been eliminated in consolidation.

**Segment Information:** Consumers Bancorp, Inc. is a bank holding company engaged in the business of commercial and retail banking, which accounts for substantially all of the revenues, operating income, and assets. Accordingly, all of its operations are recorded in one segment, banking.

**Reclassifications:** Certain items in prior financial statements have been reclassified to conform to the current presentation.



**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

**Note 2 – Securities**

Description of Securities	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2012				
Obligations of U.S. government-sponsored entities and agencies	\$ 7,426	\$ 68	\$ —	\$ 7,494
Obligations of state and political subdivisions	37,547	1,918	(51 )	39,414
Mortgage-backed securities – residential	46,107	1,189	(41 )	47,255
Collateralized mortgage obligations	11,283	146	(4 )	11,425
Trust preferred security	202	—	(128 )	74
Total securities	\$ 102,565	\$ 3,321	\$ (224 )	\$ 105,662

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2012				
Obligations of U.S. government-sponsored entities and agencies	\$ 8,487	\$ 80	\$ —	\$ 8,567
Obligations of state and political subdivisions	33,808	1,577	(109 )	35,276
Mortgage-backed securities - residential	48,255	1,108	(32 )	49,331
Collateralized mortgage obligations	12,154	25	(82 )	12,097
Trust preferred security	202	—	(138 )	64
Total securities	\$ 102,906	\$ 2,790	\$ (361 )	\$ 105,335

Proceeds from the sale of available-for-sale securities were as follows:

	Three Months Ended	
	September 30, 2012	2011
Proceeds from sales	\$ 530	\$ 4,951
Gross realized gains	21	49

The amortized cost and fair values of available-for-sale securities at September 30, 2012, by expected maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date, primarily mortgage-backed securities, collateralized mortgage obligations and the trust preferred security are shown separately.



**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

	Amortized Cost	Estimated Fair Value
Due in one year or less	\$2,502	\$ 2,512
Due after one year through five years	5,874	5,971
Due after five years through ten years	11,312	11,954
Due after ten years	25,285	26,471
Total	44,973	46,908
Mortgage-backed securities – residential	46,107	47,255
Collateralized mortgage obligations	11,283	11,425
Trust preferred security	202	74
Total	\$ 102,565	\$ 105,662

The following table summarizes the securities with unrealized losses at September 30, 2012 and June 30, 2012, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

Description of Securities	Less than 12 Months		12 Months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
September 30, 2012						
Obligations of states and political subdivisions	\$4,594	\$ (51 )	\$—	\$ —	\$4,594	\$ (51 )
Mortgage-backed securities - residential	7,494	(41 )	—	—	7,494	(41 )
Collateralized mortgage obligations	1,412	(4 )	—	—	1,412	(4 )
Trust preferred security	—	—	74	(128 )	74	(128 )
Total temporarily impaired	\$13,500	\$ (96 )	\$74	\$ (128 )	\$13,574	\$ (224 )

Description of Securities	Less than 12 Months	12 Months or more	Total
---------------------------	---------------------	-------------------	-------

Edgar Filing: CONSUMERS BANCORP INC /OH/ - Form 10-Q

	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
June 30, 2012						
Obligations of states and political subdivisions	\$6,002	\$ (109 )	\$—	\$ —	\$6,022	\$ (109 )
Mortgage-backed securities - residential	11,135	(32 )	—	—	11,135	(32 )
Collateralized mortgage obligations	6,411	(62 )	2,314	(20 )	8,725	(82 )
Trust preferred security	—	—	64	(138 )	64	(138 )
Total temporarily impaired	\$23,548	\$ (203 )	\$2,378	\$ (158 )	\$25,926	\$ (361 )

Management evaluates securities for other-than-temporary impairment (OTTI) on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. The securities portfolio is evaluated for OTTI by segregating the portfolio into two general segments and applying the appropriate OTTI model. Investment securities are generally evaluated for OTTI under FASB ASC Topic 320, *Accounting for Certain Investments in Debt and Equity Securities*. However, the trust preferred security is evaluated using the model outlined in FASB ASC Topic 325, *Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transfer in Securitized Financial Assets*.

**CONSUMERS BANCORP, INC.**

**Notes to the Consolidated Financial Statements**

**(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

In determining OTTI under the ASC Topic 320 model, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the entity has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

Unrealized losses on obligations of state and political subdivisions, residential mortgage-backed securities and collateralized mortgage obligations have not been recognized into income because the decline in fair value is not attributed to credit quality, management does not intend to sell and it is likely that management will not be required to sell the securities prior to their anticipated recovery. The decline in fair value of the residential mortgage-backed securities and collateralized mortgage obligations is attributable to higher than projected prepayment speeds increasing the premium amortization and the decline in fair value of obligations of state and political subdivisions is largely due to spreads for these securities being wider at September 30, 2012 than when the securities were purchased. The fair value is expected to recover as the securities approach maturity.

Under the ASC Topic 325 model, the present value of the remaining cash flows as estimated at the preceding evaluation date are compared to the current expected remaining cash flows. An OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows. The analysis of the trust preferred security falls within the scope of ASC Topic 325.

The Corporation owns a trust preferred security with an adjusted amortized cost of \$202 and a fair value of \$74, which represents collateralized debt obligations (CDOs) issued by other financial institutions, bank holding companies and a limited number of insurance companies. The security is part of a pool of issuers that support a more senior tranche of securities. Due to principal and/or interest deferrals by the issuers of the underlying securities, the cash interest payments for the trust preferred security are being deferred. On September 30, 2012, the lowest credit rating on this security was Fitch's rating of C, which is defined as highly speculative. The investment security is evaluated using a model to compare the present value of expected cash flows to prior periods expected cash flows to determine if there has been an adverse change in cash flows during the period. The discount rate used to calculate the cash flows is the coupon rate of the security, based on the forward LIBOR curve. The OTTI model considers the structure and term of

the CDO and the financial condition of the underlying issuers. In addition we use the model to “stress” the CDO, or make assumptions more severe than expected activity, to determine the degree to which assumptions could deteriorate before the CDO could no longer fully support repayment of the Corporation’s note class. According to the September 30, 2012 analysis, the expected cash flows were above the recorded amortized cost of the trust preferred security. The accumulated other-than-temporary impairment loss that has been recognized in earnings was \$780 at September 30, 2012 and June 30, 2012. If there is further deterioration in the underlying collateral of this security, other-than-temporary impairments may also occur in future periods. Due to the illiquidity in the market, it is unlikely the Corporation would be able to recover its investment in this security if the Corporation sold the security at this time.

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

**Note 3 – Loans**

Major classifications of loans were as follows:

	September 30, 2012	June 30, 2012
Commercial	\$ 23,506	\$ 23,041
Commercial real estate:		
Construction	2,607	1,546
Other	113,811	110,775
1 – 4 Family residential real estate:		
Owner occupied	33,417	34,000
Non-owner occupied	18,739	18,794
Construction	248	187
Consumer	10,121	9,407
Subtotal	202,449	197,750
Less: Net deferred loan fees	(331 )	(320 )
Allowance for loan losses	(2,338 )	(2,335 )
Net Loans	\$ 199,780	\$ 195,095

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table presents the activity in the allowance for loan losses by portfolio segment for the three months ending September 30, 2012:

	Commercial	Commercial Real Estate	1-4 Family Residential Real Estate	Consumer	Total
Allowance for loan losses:					
Beginning balance	\$ 143	\$ 1,283	\$ 712	\$ 197	\$2,335
Provision for loan losses	6	(8 )	(20 )	47	25
Loans charged-off	(4 )	—	(15 )	(19 )	(38 )
Recoveries	—	—	—	16	16
Total ending allowance balance	\$ 145	\$ 1,275	\$ 677	\$ 241	\$2,338

The following table presents the activity in the allowance for loan losses by portfolio segment for the three months ended September 30, 2011:

	Commercial	Commercial Real Estate	1-4 Family Residential Real Estate	Consumer	Total
Allowance for loan losses:					
Beginning balance	\$ 179	\$ 882	\$ 947	\$ 93	\$2,101
Provision for loan losses	(82 )	172	(33 )	35	92
Loans charged-off	—	—	(69 )	(50 )	(119 )
Recoveries	—	—	—	13	13
Total ending allowance balance	\$ 97	\$ 1,054	\$ 845	\$ 91	\$2,087



**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of September 30, 2012. Included in the recorded investment in loans is \$534 of accrued interest receivable net of deferred loan fees of \$331.

	Commercial	Commercial Real Estate	1-4 Family Residential Real Estate	Consumer	Total
Allowance for loan losses:					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	\$ 46	\$ 62	\$ 257	\$ —	\$ 365
Collectively evaluated for impairment	99	1,213	420	241	1,973
Total ending allowance balance	\$ 145	\$ 1,275	\$ 677	\$ 241	\$ 2,338
Recorded investment in loans:					
Loans individually evaluated for impairment	\$ 104	\$ 949	\$ 1,392	\$ —	\$ 2,445
Loans collectively evaluated for impairment	23,458	115,513	51,134	10,102	200,207
Total ending loans balance	\$ 23,562	\$ 116,462	\$ 52,526	\$ 10,102	\$ 202,652



**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of June 30, 2012. Included in the recorded investment in loans is \$494 of accrued interest receivable net of deferred loan fees of \$320.

	Commercial	Commercial Real Estate	1-4 Family Residential Real Estate	Consumer	Total
Allowance for loan losses:					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	\$ 50	\$ 82	\$ 258	\$ —	\$ 390
Collectively evaluated for impairment	93	1,201	454	197	1,945
Total ending allowance balance	\$ 143	\$ 1,283	\$ 712	\$ 197	\$ 2,335
Recorded investment in loans:					
Loans individually evaluated for impairment	\$ 148	\$ 996	\$ 1,417	\$ —	\$ 2,561
Loans collectively evaluated for impairment	22,940	111,352	51,683	9,388	195,363
Total ending loans balance	\$ 23,088	\$ 112,348	\$ 53,100	\$ 9,388	\$ 197,924

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table presents information related to loans individually evaluated for impairment by class of loans as of and for the three months ended September 30, 2012:

	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With no related allowance recorded:						
Commercial	\$ 11	\$ 11	\$ —	\$ 11	\$ —	\$ —
Commercial real estate:						
Other	94	94	—	103	—	—
1-4 Family residential real estate:						
Owner occupied	81	81	—	81	—	—
Non-owner occupied	57	58	—	57	1	1
With an allowance recorded:						
Commercial	93	93	46	122	—	—
Commercial real estate:						
Other	854	855	62	863	2	2
1-4 Family residential real estate:						
Owner occupied	310	310	42	314	—	—
Non-owner occupied	942	943	215	946	6	6
Total	\$ 2,442	\$ 2,445	\$ 365	\$ 2,497	\$ 9	\$ 9

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table presents information related to loans individually evaluated for impairment by class of loans as of June 30, 2012 and for the three months ended September 30, 2011:

	As of June 30, 2012			Three Months ended September 30, 2011		
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With no related allowance recorded:						
Commercial	\$12	\$ 12	\$ —	\$ 17	\$ —	\$ —
Commercial real estate:						
Other	144	144	—	635	3	3
1-4 Family residential real estate:						
Owner occupied	238	238	—	97	2	2
Non-owner occupied	64	65	—	43	—	—
With an allowance recorded:						
Commercial	136	136	50	63	—	—
Commercial real estate:						
Other	851	852	82	763	5	5
1-4 Family residential real estate:						
Owner occupied	160	160	13	218	2	2
Non-owner occupied	952	954	245	871	—	—
Total	\$2,557	\$ 2,561	\$ 390	\$ 2,707	\$ 12	\$ 12

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table presents the recorded investment in non-accrual and loans past due over 90 days still on accrual by class of loans as of September 30, 2012 and June 30, 2012:

	September 30, 2012		June 30, 2012	
	Non-accrual	Loans Past Due Over 90 Days Still Accruing	Non-accrual	Loans Past Due Over 90 Days Still Accruing
Commercial	\$ 93	\$ —	\$ 51	\$ —
Commercial real estate:				
Other	863	—	911	—
1 – 4 Family residential:				
Owner occupied	300	—	307	—
Non-owner occupied	716	—	663	—
Consumer	—	—	—	—
Total	\$ 1,972	\$ —	\$ 1,932	\$ —

Non-accrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table presents the aging of the recorded investment in past due loans as of September 30, 2012 by class of loans:

	Days Past Due			Total Past Due	Loans Not Past Due	Total
	30 - 59 Days	60 - 89 Days	90 Days or Greater & Non-accrual			
Commercial	\$9	\$ —	\$ 78	\$ 87	\$ 23,475	\$ 23,562
Commercial real estate:						
Construction	—	—	—	—	2,609	2,609
Other	26	—	280	306	113,547	113,853
1-4 Family residential:						
Owner occupied	159	—	254	413	33,126	33,539
Non-owner occupied	—	87	43	130	18,610	18,740
Construction	—	—	—	—	247	247
Consumer	7	—	—	7	10,095	10,102
Total	\$ 201	\$ 87	\$ 655	\$ 943	\$ 201,709	\$ 202,652

The above table of past due loans includes the recorded investment in non-accrual loans of \$63 in the 60-89 days past due category and \$1,254 in the loans not past due category.

The following table presents the aging of the recorded investment in past due loans as of June 30, 2012 by class of loans:

	Days Past Due			Total Past Due	Loans Not Past Due	Total
	30 - 59 Days	60 - 89 Days	90 Days or Greater & Non-accrual			
Commercial	\$85	\$ —	\$ 33	\$ 118	\$ 22,970	\$ 23,088

Commercial real estate:						
Construction	202	—	—	202	1,345	1,547
Other	82	—	268	350	110,451	110,801
1-4 Family residential:						
Owner occupied	174	—	178	352	33,766	34,118
Non-owner occupied	43	—	—	43	18,753	18,796
Construction	—	—	—	—	186	186
Consumer	—	8	—	8	9,380	9,388
Total	\$586	\$ 8	\$ 479	\$ 1,073	\$ 196,851	\$ 197,924

The above table of past due loans includes the recorded investment in non-accrual loans of \$43 in the 30 – 59 days past due category and \$1,410 in the loans not past due category.

### **Troubled Debt Restructurings:**

As of September 30, 2012, the recorded investment of loans classified as troubled debt restructurings was \$1,806 with \$193 of specific reserves allocated to these loans. As of June 30, 2012, the recorded investment of loans classified as troubled debt restructurings was \$1,973 with \$258 of specific reserves allocated to these loans. As of September 30, 2012 and June 30, 2012, the Corporation had not committed to lend any additional amounts to customers with outstanding loans that are classified as troubled debt restructurings.

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

During the three months ended September 30, 2012, there were no loan modifications completed that were classified as troubled debt restructurings. During the year ended June 30, 2012, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; a permanent reduction of the recorded investment in the loan; or a temporary reduction in the payment amount to interest only.

Modifications involving a reduction of the stated interest rate of the loan were for periods ranging from 12 months to 25 years. Modifications involving an extension of the maturity date were for a period of 6.5 years to 25 years.

The following table presents loans by class modified as troubled debt restructurings that occurred during the year ended June 30, 2012:

	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial 1	\$ 85	\$ 85	
Commercial real estate:			
Other	2	137	137
1 – 4 Family residential:			
Owner occupied	1	114	114
Non-owner occupied	7	534	466
Total	11	\$ 870	\$ 802

There were no troubled debt restructurings or impact on the provision for loan losses for the three months ended September 30, 2012. Troubled debt restructurings increased the allowance for loan losses by \$20 and resulted in charge offs of \$63 during the period ended September 30, 2011.

The following table presents loans by class modified as troubled debt restructurings for which there was a payment default within 12 months following the modification during the period ending September 30, 2012:

	Number of Loans	Recorded Investment
Commercial real estate:		
Other	1	\$ 428



**CONSUMERS BANCORP, INC.**

**Notes to the Consolidated Financial Statements**

**(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms. Subsequent to the payment default, the above referenced loan has been paid current under the modified terms of the loan. The troubled debt restructuring that subsequently defaulted did not increase the allowance for loan losses or have any charge-off during the periods ending September 30, 2012 or June 30, 2012.

**Credit Quality Indicators:**

The Corporation categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Corporation analyzes loans individually by classifying the loans as to credit risk. This analysis includes loans with a total outstanding loan relationship greater than \$100 and non-homogeneous loans, such as commercial and commercial real estate loans. Management monitors the loans on an ongoing basis for any changes in the borrower's ability to service their debt and affirm the risk ratings for the loans and leases in their respective portfolio on an annual basis. The Corporation uses the following definitions for risk ratings:

**Special Mention.** Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

**Substandard.** Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

**Doubtful.** Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Loans listed as not rated are either less than \$100 or are included in groups of homogeneous loans. Based on the most recent analysis performed, the recorded investment by risk category of loans by class of loans was as follows:

19

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

	As of September 30, 2012				
	Pass	Special Mention	Substandard	Doubtful	Not Rated
Commercial	\$22,292	\$ 38	\$ 74	\$ 104	\$1,054
Commercial real estate:					
Construction	2,421	158	—	—	30
Other	103,514	5,833	2,752	949	805
1-4 Family residential real estate:					
Owner occupied	3,953	—	99	391	29,096
Non-owner occupied	14,109	2,157	860	1,001	613
Construction	200	—	—	—	47
Consumer	—	—	—	—	10,102
Total	\$146,489	\$ 8,186	\$ 3,785	\$ 2,445	\$41,747

	As of June 30, 2012				
	Pass	Special Mention	Substandard	Doubtful	Not Rated
Commercial	\$21,642	\$ 240	\$ 14	\$ 148	\$1,044
Commercial real estate:					
Construction	1,353	163	—	—	31
Other	98,942	7,332	2,657	996	874
1-4 Family residential real estate:					
Owner occupied	4,256	—	99	398	29,365
Non-owner occupied	14,205	2,197	875	1,019	500
Construction	47	—	—	—	139
Consumer	—	—	—	—	9,388
Total	\$140,445	\$ 9,932	\$ 3,645	\$ 2,561	\$41,341

**Note 4 - Fair Value**

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants

on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

Financial assets and financial liabilities measured at fair value on a recurring basis include the following:

**Securities available-for-sale:** When available, the fair values of available-for-sale securities are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs). For securities where quoted market prices are not available, fair values are calculated based on market prices of similar securities (Level 2 inputs). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3 inputs). The fair value of the Level 3 security is obtained from a third-party pricing service. Discounted cash flows are calculated using spread to the swap and LIBOR curves. Rating agency and industry research reports as well as defaults and deferrals on the individual security is reviewed and incorporated into the calculation.

**Loans held for sale:** The fair value of loans held for sale is estimated based upon binding contracts and quotes from third party investors resulting in a Level 2 classification.

Assets and liabilities measured at fair value on a recurring basis are summarized below, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

	Balance at September 30, 2012	Fair Value Measurements at September 30, 2012 Using		
		Level 1	Level 2	Level 3
Assets:				
Obligations of U.S. government-sponsored entities and agencies	\$ 7,494	\$ —	\$ 7,494	\$ —
Obligations of states and political subdivisions	39,414	—	39,414	—
Mortgage-backed securities – residential	47,255	—	47,255	—
Collateralized mortgage obligations	11,425	—	11,425	—
Trust preferred security	74	—	—	74
Loans held for sale	408	—	415	—

	Balance at June 30, 2012	Fair Value Measurements at June 30, 2012 Using		
		Level 1	Level 2	Level 3
Assets:				
Obligations of U.S. government-sponsored entities and agencies	\$ 8,567	\$ —	\$ 8,567	\$ —
Obligations of states and political subdivisions	35,276	—	35,276	—
Mortgage-backed securities - residential	49,331	—	49,331	—
Collateralized mortgage obligations	12,097	—	12,097	—
Trust preferred security	64	—	—	64
Loans held for sale	377	—	387	—

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

There were no transfers between Level 1 and Level 2 during the first quarter of the 2013 fiscal year or the during the 2012 fiscal year.

The following table presents a reconciliation of the trust preferred security measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended September 30, 2012 and 2011:

	2012	2011
Beginning balance	\$ 64	\$ 67
Change in fair value included in other comprehensive income	10	(3 )
Ending balance, September 30	\$ 74	\$ 64

The significant unobservable inputs used in the fair value measurement of the Corporation's trust preferred security are probabilities of specific-issuer defaults and deferrals and specific-issuer recovery assumptions. Significant increases in specific-issuer default assumptions or decreases in specific-issuer recovery assumptions would result in a significantly lower fair value measurement. Conversely, decreases in specific-issuer default assumptions or increases in specific-issuer recovery assumptions would result in a higher fair value measurement.

Certain financial assets and financial liabilities are measured at fair value on a non-recurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances. Financial assets and financial liabilities measured at fair value on a non-recurring basis include the following:

**Impaired Loans:** At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales

and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.



**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

Financial assets and financial liabilities measured at fair value on a non-recurring basis are summarized below:

	Balance at September 30, 2012	Fair Value Measurements at September 30, 2012 Using		
		Level 1	Level 2	Level 3
Impaired loans:				
Commercial	\$ 47	\$ —	\$ —	\$ 47
Commercial real estate:				
Other	661	—	—	661
1-4 Family				
Owner occupied	161	—	—	161
Non-owner occupied	458	—	—	458

	Balance at June 30, 2012	Fair Value Measurements at June 30, 2012 Using		
		Level 1	Level 2	Level 3
Impaired loans:				
Commercial	\$ 11	\$ —	\$ —	\$ 11
Commercial real estate:				
Other	647	—	—	647
1-4 Family				
Owner occupied	40	—	—	40
Non-owner occupied	438	—	—	438

Impaired loans, which are generally measured for impairment using the fair value of the collateral for collateral dependent loans, had a principal balance of \$1,643, with a valuation allowance of \$317 at September 30, 2012. As of June 30, 2012, impaired loans with a principal balance of \$1,479 had a valuation allowance of \$343. The resulting impact to the provision for loan losses was a reduction of \$27 being recorded for the three month period ended September 30, 2012. For the three month period ended September 30, 2011, there was no additional provision for loan losses recorded.

The valuation technique used by an independent third party appraiser in the fair value measurement of collateral for collateral-dependent commercial real estate impaired loans primarily consisted of the sales comparison approach. The valuation technique used by an independent third party appraiser in the fair value measurement of collateral for collateral-dependent 1-4 family non-owner occupied impaired loans primarily consisted of the sales comparison and income approach. The significant unobservable inputs used in the fair value measurement relate to adjustments made to the value set forth in the appraisal by deducting estimated holding costs, costs to sell and a distressed sale adjustment. For the September 30, 2012 period, collateral discounts for commercial real estate impaired loans ranged from 30% to 39%, for 1-4 family owner occupied impaired loans ranged from 33% to 37% and for 1-4 family non-owner occupied impaired loans was 30%. For the June 30, 2012 period, collateral discounts for commercial real estate impaired loans ranged from 33% to 41% and for 1-4 family non-owner occupied impaired loans ranged from 15% to 39%.

**CONSUMERS BANCORP, INC.**

**Notes to the Consolidated Financial Statements**

**(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

Estimated fair value for cash and cash equivalents, certificates of deposits in other financial institutions, accrued interest receivable and payable, demand and savings deposits and short-term borrowings were considered to approximate carrying value. The methodologies for other financial assets and financial liabilities are discussed below:

**Loans:** Fair value for loans was estimated for portfolios of loans with similar financial characteristics. For adjustable rate loans that reprice at least annually and for fixed rate commercial loans with maturities of six months or less which possess normal risk characteristics, carrying value was determined to be fair value. Fair value of other types of loans (including adjustable rate loans which reprice less frequently than annually and fixed rate term loans or loans which possess higher risk characteristics) was estimated by discounting future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for similar anticipated maturities resulting in a Level 3 classification. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

**Time deposits:** Fair value of fixed-maturity certificates of deposit was estimated using the rates offered at September 30, 2012 and June 30, 2012, for deposits of similar remaining maturities. Estimated fair value does not include the benefit that result from low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market resulting in a Level 2 classification.

**Federal Home Loan Bank advances:** Fair value of Federal Home Loan Bank advances was estimated using current rates at September 30, 2012 and June 30, 2012 for similar financing resulting in a Level 2 classification.

Federal bank and other restricted stocks include stock acquired for regulatory purposes, such as Federal Home Loan Bank stock and Federal Reserve Bank stock that are accounted for at cost due to restrictions placed on their transferability; and therefore, are not subject to the fair value disclosure requirements. The Corporation's lending commitments have variable interest rates and "escape" clauses if the customer's credit quality deteriorates. Therefore, the fair values of these items are not significant and are not included in the following table.



**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

The following table shows the estimated fair values of financial instruments that are reported at amortized cost in the Corporation's consolidated balance sheets, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

	September 30, 2012		June 30, 2012	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
<b>Financial Assets:</b>				
<b>Level 1 inputs:</b>				
Cash and cash equivalents	\$ 10,633	\$ 10,633	\$ 13,745	\$ 13,745
<b>Level 2 inputs:</b>				
Certificates of deposits in other financial institutions	5,645	5,674	5,645	5,645
Accrued interest receivable	1,145	1,145	1,043	1,043
<b>Level 3 inputs:</b>				
Loans, net	199,780	200,813	195,095	196,592
<b>Financial Liabilities:</b>				
<b>Level 2 inputs:</b>				
Demand and savings deposits	199,700	199,700	200,011	200,011
Time deposits	84,757	85,520	84,470	85,262
Short-term borrowings	15,005	15,005	13,722	13,722
Federal Home Loan Bank advances	6,427	7,377	6,446	7,398
Accrued interest payable	62	62	56	56

**CONSUMERS BANCORP, INC.****Notes to the Consolidated Financial Statements****(Unaudited) (continued)**

(Dollars in thousands, except per share amounts)

**Note 5 – Earnings Per Share**

Basic earnings per share is the amount of earnings available to each share of common stock outstanding during the reporting period and is equal to net income divided by the weighted average number of shares outstanding during the period. Diluted earnings per share is the amount of earnings available to each share of common stock outstanding during the reporting period adjusted to include the effect of potentially dilutive common shares that may be issued upon the vesting of restricted stock awards. The following table details the calculation of basic and diluted earnings per share:

	For the Three Months Ended September 30,	
	2012	2011
Basic:		
Net income available to common shareholders	\$615	\$687
Weighted average common shares outstanding	2,057,751	2,049,974
Basic income per share	\$0.30	\$0.34
Diluted:		
Net income available to common shareholders	\$615	\$687
Weighted average common shares outstanding	2,057,751	2,049,974
Dilutive effect of restricted stock	416	256
Total common shares and dilutive potential common shares	2,058,167	2,050,230
Dilutive income per share	\$0.30	\$0.34

**CONSUMERS BANCORP, INC.**

**Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations**

**(Dollars in thousands, except per share data)**

**General**

The following is management’s analysis of the Corporation’s results of operations for the three month period ended September 30, 2012, compared to the same period in 2011, and the consolidated balance sheet at September 30, 2012 compared to June 30, 2012. This discussion is designed to provide a more comprehensive review of the operating results and financial condition than could be obtained from an examination of the financial statements alone. This analysis should be read in conjunction with the consolidated financial statements and related footnotes and the selected financial data included elsewhere in this report.

**Overview**

Consumers Bancorp, Inc., a bank holding company incorporated under the laws of the State of Ohio (the Corporation), owns all of the issued and outstanding common shares of Consumers National Bank, a bank chartered under the laws of the United States of America (the Bank). The Corporation’s activities have been limited primarily to holding the common shares of the Bank. The Bank’s business involves attracting deposits from businesses and individual customers and using such deposits to originate commercial, mortgage and consumer loans in its market area, consisting primarily of Stark, Columbiana, Carroll and contiguous counties in Ohio. The Bank also invests in securities consisting primarily of U.S. government sponsored entities, municipal obligations, mortgage-backed and collateralized mortgage obligations issued by Fannie Mae, Freddie Mac and Ginnie Mae.

**Results of Operations**

**Three Months Ended September 30, 2012 and September 30, 2011**

**Net Income**

In the first quarter of fiscal year 2013, net income was \$615, or \$0.30 per common share, compared with \$687, or \$0.34 per common share, in the prior year period. The following key factors summarize our results of operations for the three months ending September 30, 2012:

net interest income increased by \$106, or 3.7%, in 2012 from the same period in 2011;  
loan loss provision expense in 2012 totaled \$25 compared to \$92 from the same period in 2011;  
noninterest income declined by \$8, or 1.2%, in 2012 from the same prior year period mainly as a result of a decrease of \$28 in the net gains on the sale of securities; and  
noninterest expenses increased by \$305, or 11.9%, in 2012 principally as a result of higher salary and employee benefits due to staff hired in the lending area and new staff for the Jackson-Belden office that opened July 31, 2012.



## CONSUMERS BANCORP, INC.

### Management's Discussion and Analysis of Financial Condition

#### and Results of Operations (continued)

(Dollars in thousands, except per share data)

Return on average equity and return on average assets were 8.68% and 0.73%, respectively, for the first quarter of fiscal year 2013 compared to 10.55% and 0.90%, respectively, for the first quarter of fiscal year 2012.

#### Net Interest Income

Net interest income, the difference between interest income earned on interest-earning assets and interest expense incurred on interest-bearing liabilities, is the largest component of the Corporation's earnings. Net interest income is affected by changes in the volumes, rates and composition of interest-earning assets and interest-bearing liabilities. Net interest margin is calculated by dividing net interest income on a fully tax equivalent basis (FTE) by total average interest-earning assets. FTE income includes tax-exempt income, restated to a pre-tax equivalent, based on the statutory federal income tax rate. All average balances are daily average balances. Non-accruing loans are included in average loan balances.

The Corporation's net interest margin for the three months ended September 30, 2012 was 3.94%, compared to 4.10% for the same year ago period. Net interest income for the three months ended September 30, 2012 increased by \$106, or 3.7%, to \$2,981 from \$2,875 for the same year ago period. The increase in net interest income was primarily the result of a decline in the Corporation's cost of funds and an increase in average interest-earning assets.

Interest income for the three months ended September 30, 2012 increased by \$31, or 0.9%, from the same year ago period. An increase of \$26,323, or 9.0%, in average interest-earning assets more than offset the impact the low interest rate environment has had on the yield of average interest-earning assets. Interest expense for the three months ended September 30, 2012 decreased by \$75, or 18.7%, from the same year ago period. The Corporation's cost of funds decreased to 0.54% for the three month period ended September 30, 2012 from 0.75% for the same year ago period mainly due to lower market rates affecting the rates paid on most all interest-bearing deposit accounts and borrowings. The Corporation has introduced a NOW checking account product that pays a higher rate of interest to customers who meet certain qualifications, with one of the main qualifications being the frequent use of a debit card. As a result, debit card interchange income has increased (see discussion in "Non-Interest Income" section) and the cost of the NOW checking account increased from 0.15% to 0.20% from the same year ago period.



**CONSUMERS BANCORP, INC.**

## Management's Discussion and Analysis of Financial Condition

**and Results of Operations (continued)**

(Dollars in thousands, except per share data)

**Average Balance Sheets and Analysis of Net Interest Income for the Three Months Ended September 30,**

(In thousands, except percentages)

	2012			2011		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
Interest-earning assets:						
Taxable securities	\$68,921	\$383	2.24 %	\$69,400	\$480	2.79 %
Nontaxable securities (1)	37,500	452	5.00	25,594	362	5.76
Loans receivable (1)	199,169	2,613	5.21	178,357	2,541	5.65
Interest bearing deposits and federal funds sold	12,612	15	0.47	18,528	16	0.34
Total interest-earning assets	318,202	3,463	4.35 %	291,879	3,399	4.65 %
Noninterest-earning assets	17,751			13,466		
Total Assets	\$335,953			\$305,345		
Interest-bearing liabilities:						
NOW	\$35,344	\$18	0.20 %	\$15,720	\$6	0.15 %
Savings	100,055	27	0.11	82,725	36	0.17
Time deposits	84,330	225	1.06	88,511	288	1.29
Short-term borrowings	13,830	6	0.17	16,813	11	0.26
FHLB advances	6,434	50	3.08	7,523	60	3.16
Total interest-bearing liabilities	239,993	326	0.54 %	211,292	401	0.75 %
Noninterest-bearing liabilities:						
Noninterest-bearing checking accounts	65,384			66,214		
Other liabilities	2,462			1,923		
Total liabilities	307,839			279,429		
Shareholders' equity	28,114			25,916		
Total liabilities and shareholders' equity	\$335,953			\$305,345		

Edgar Filing: CONSUMERS BANCORP INC /OH/ - Form 10-Q

Net interest income, interest rate spread (1)	\$3,137	3.81 %	\$2,998	3.90 %
Net interest margin (net interest as a percent of average interest-earning assets) (1)		3.94 %		4.10 %
Federal tax exemption on non-taxable securities and loans included in interest income	\$ 156		\$ 123	
Average interest-earning assets to interest-bearing liabilities		132.59 %		138.14 %
(1) calculated on a fully taxable equivalent basis				

## **CONSUMERS BANCORP, INC.**

### Management's Discussion and Analysis of Financial Condition

#### **and Results of Operations (continued)**

(Dollars in thousands, except per share data)

#### **Provision for Loan Losses**

The provision for loan losses represents the charge to income necessary to adjust the allowance for loan losses to an amount that represents management's assessment of the estimated probable credit losses in the Bank's loan portfolio that have been incurred at each balance sheet date. For the three month period ended September 30, 2012, the provision for loan losses was \$25, a decrease of \$67 from the same prior year period. The allowance for loan losses as a percentage of loans was 1.18% at June 30, 2012 and 1.16% at September 30, 2012.

Net charge-offs for the three month period ending September 30, 2012 were \$22, or 0.04% of total average loans on an annualized basis, compared with \$106, or 0.24% of total average loans, for the same period last year. The provision for the 1-4 family residential real estate loan portfolio was a negative \$20 for the current period primarily as a result of improvement in the three year historical loss ratio for this portfolio. The provision for the commercial real estate loan portfolio was a negative \$8 for the current period primarily as a result of the upgrade of commercial real estate loans from special mention to pass.

Non-performing loans were \$1,972 as of September 30, 2012 and represented 0.98% of total loans. This compared with \$1,932, or 0.98%, at June 30, 2012 and \$2,019, or 1.12%, as of September 30, 2011. The allowance for loan losses to total non-performing loans at September 30, 2012 was 118.56% compared with 120.86% at June 30, 2012 and 103.37% at September 30, 2011.

The provision for loan losses for the period ending September 30, 2012 was considered sufficient by management for maintaining an appropriate allowance for loan losses for probable incurred credit losses.

#### **Non-Interest Income**

Non-interest income totaled \$664 for the first quarter of fiscal year 2013, compared to \$672 for the same period last year. Non-interest income for the first quarter of fiscal year 2013 included a net gain from the sale of securities of \$21 compared with a net gain of \$49 recognized during the same prior year period.

Service charges on deposits decreased by \$14, or 3.9%, during the first quarter of fiscal year 2013 mainly due to a decline in overdraft fee income from the same period last year. Debit card interchange income increased by \$14, or 7.8%, from the same period last year mainly due to an increase in debit card usage by our customers as a result of the new NOW checking account product previously discussed.

**Non-Interest Expenses**

Total non-interest expenses increased to \$2,867, or 11.9%, during the first quarter of fiscal year 2013, compared with \$2,562 during the same year ago period.

**CONSUMERS BANCORP, INC.**

Management's Discussion and Analysis of Financial Condition

**and Results of Operations (continued)**

(Dollars in thousands, except per share data)

Salaries and employee benefits increased by \$239, or 18.0%, during the first quarter of fiscal year 2013. The increase was primarily associated with staff additions in the lending area and new staff for the Jackson-Belden office that was opened July 31, 2012.

Occupancy and equipment increased by \$56, or 21.7%, during the first quarter of fiscal year 2013 mainly due to an increase in building depreciation expense associated with the Minerva, Ohio corporate headquarters and branch location. The book value of this location is being expensed over the remaining useful life since a new facility is planned to replace the current facility by spring of 2014.

Marketing and advertising expenses increased by \$41, or 53.9%, to \$117 compared to the same period last year mainly due to an increase in marketing efforts as a result of the opening of the Jackson, Ohio branch location.

Debit card processing expenses increased by \$9, or 9.6%, during the first quarter of fiscal year 2013 mainly as a result of increased debit card usage by our customers.

The amortization of intangible expense declined from the previous year since the core deposit purchase premium of the Lisbon, Ohio branch that was purchased in January 2000 is fully amortized.

Total other expenses increased by \$46, or 12.7%, during the first quarter of fiscal year 2013, mainly as a result of higher education and development expenses from the introduction of a management development program, higher office supplies expense as a result of opening the Jackson-Belden office and higher internet banking expenses as a result of an increased number of personal and business customers using the internet banking product.

**Income Taxes**

Income tax expense for the three month period ended September 30, 2012 decreased by \$68, to \$138 from \$206, compared to a year ago. The effective tax rate was 18.3% for the current quarter as compared to 23.1% for the same period last year. The decline in the effective tax rate was primarily the result of an increase in tax-exempt municipal income.

The effective tax rate differed from the federal statutory rate principally as a result of tax-exempt income from obligations of states and political subdivisions, loans and earnings on bank owned life insurance.

### **Financial Condition**

Total assets at September 30, 2012 were \$336,965 compared to \$334,761 at June 30, 2012, an increase of \$2,204, or an annualized 2.6%.



**CONSUMERS BANCORP, INC.**

Management's Discussion and Analysis of Financial Condition

**and Results of Operations (continued)**

(Dollars in thousands, except per share data)

Available-for-sale securities increased by \$327 from \$105,335 at June 30, 2012 to \$105,662 at September 30, 2012. Within the securities portfolio, the Corporation owns a trust preferred security with an adjusted amortized cost of \$202 and a fair value of \$74, which represents collateralized debt obligations (CDOs) issued by other financial institutions, bank holding companies and a limited number of insurance companies. The security is part of a pool of issuers that support a more senior tranche of securities. Due to principal and/or interest deferrals by the issuers of the underlying securities, the cash interest payments for the trust preferred security are being deferred. On September 30, 2012, the lowest credit rating on this security was Fitch's rating of C, which is defined as highly speculative. The investment security is evaluated using a model to compare the present value of expected cash flows to prior periods expected cash flows to determine if there has been an adverse change in cash flows during the period. The discount rate used to calculate the cash flows is the coupon rate of the security, based on the forward LIBOR curve. The OTTI model considers the structure and term of the CDO and the financial condition of the underlying issuers. In addition we use the model to "stress" the CDO, or make assumptions more severe than expected activity, to determine the degree to which assumptions could deteriorate before the CDO could no longer fully support repayment of the Corporation's note class. According to the September 30, 2012 analysis, the expected cash flows were above the recorded amortized cost of the trust preferred security. The accumulated other-than-temporary impairment loss that has been recognized in earnings was \$780 at September 30, 2012 and June 30, 2012. If there is further deterioration in the underlying collateral of this security, other-than-temporary impairments may also occur in future periods. Due to the illiquidity in the market, it is unlikely the Corporation would be able to recover its investment in this security if the Corporation sold the security at this time.

Loan receivables increased by \$4,688, or 2.4%, to \$202,118 at September 30, 2012 compared to \$197,430 at June 30, 2012 mainly as a result of expanded calling efforts.

**CONSUMERS BANCORP, INC.**

## Management's Discussion and Analysis of Financial Condition

**and Results of Operations (continued)**

(Dollars in thousands, except per share data)

**Non-Performing Assets**

The following table presents the aggregate amounts of non-performing assets and respective ratios as of the dates indicated.

	September 30, 2012	June 30, 2012	September 30, 2011		
Non-accrual loans	\$ 1,972	\$ 1,932	\$ 2,019		
Loans past due over 90 days and still accruing	—	—	—		
Total non-performing loans	1,972	1,932	2,019		
Other real estate owned	—	—	76		
Total non-performing assets	\$ 1,972	\$ 1,932	\$ 2,095		
Non-performing loans to total loans	0.98	% 0.98	% 1.12		%
Allowance for loan losses to total non-performing loans	118.56	% 120.86	% 103.37		%

As of September 30, 2012, impaired loans totaled \$2,445, of which \$1,843 are included in non-accrual loans. Commercial and commercial real estate loans are classified as impaired if management determines that full collection of principal and interest, in accordance with the terms of the loan documents, is not probable. Impaired loans and non-performing loans have been considered in management's analysis of the appropriateness of the allowance for loan losses. Management and the Board of Directors are closely monitoring these loans and believe that the prospects for recovery of principal and interest, less identified specific reserves, are favorable.

**Contractual Obligations, Commitments, Contingent Liabilities and Off-Balance Sheet Arrangements****Liquidity**

The objective of liquidity management is to ensure adequate cash flows to accommodate the demands of our customers and provide adequate flexibility for the Corporation to take advantage of market opportunities under both

normal operating conditions and under unpredictable circumstances of industry or market stress. Cash is used to fund loans, purchase investments, fund the maturity of liabilities, and at times to fund deposit outflows and operating activities. The Corporation's principal sources of funds are deposits; amortization and prepayments of loans; maturities, sales and principal receipts from securities; borrowings; and operations. Management considers the asset position of the Corporation to be sufficiently liquid to meet normal operating needs and conditions. The Corporation's earning assets are mainly comprised of loans and investment securities. Management continually strives to obtain the best mix of loans and investments to both maximize yield and insure the soundness of the portfolio, as well as to provide funding for loan demand as needed.

**CONSUMERS BANCORP, INC.**

Management's Discussion and Analysis of Financial Condition

**and Results of Operations (continued)**

(Dollars in thousands, except per share data)

Net cash inflow from operating activities for the three month period ended September 30, 2012 was \$759, net cash outflows from investing activities was \$4,926 and net cash inflows from financing activities was \$1,055. A major source of cash was \$5,503 from sales, maturities, calls or principal pay downs on available-for-sale securities and a \$1,283 increase in short-term borrowings. A major use of cash included the \$5,478 purchase of securities. Total cash and cash equivalents was \$10,633 as of September 30, 2012 compared to \$13,745 at June 30, 2012 and \$21,864 at September 30, 2011.

The Bank offers several types of deposit products to its customers. The rates offered by the Bank and the fees charged for them are competitive with others currently available in the market area. Deposits totaled \$284,457 at September 30, 2012 compared with \$284,481 at June 30, 2012. The overall cost for funds decreased by 21 basis points from the same year ago period.

To provide an additional source of liquidity, the Corporation has entered into an agreement with the Federal Home Loan Bank (FHLB) of Cincinnati. At September 30, 2012, FHLB advances totaled \$6,427 as compared with \$6,446 at June 30, 2012. As of September 30, 2012, the Bank had the ability to borrow an additional \$21,834 from the FHLB based on a blanket pledge of qualifying first mortgage loans. The Corporation considers the FHLB to be a reliable source of liquidity funding, secondary to its deposit base.

Short-term borrowings consisted of repurchase agreements which is a financing arrangement that matures daily. The Bank pledges securities as collateral for the repurchase agreements. Short-term borrowings increased to \$15,005 at September 30, 2012 from \$13,722 at June 30, 2012.

Jumbo time deposits (those with balances of \$100 thousand and over) totaled \$34,278 at September 30, 2012 and \$34,422 at June 30, 2012. These deposits are monitored closely by the Corporation and are mainly priced on an individual basis. When these deposits are from a municipality, certain bank-owned securities are pledged to guarantee the safety of these public fund deposits as required by Ohio law. The Corporation has the option to use a fee-paid broker to obtain deposits from outside its normal service area as an additional source of funding. The Corporation however, does not rely upon these deposits as a primary source of funding. Although management monitors interest

rates on an ongoing basis, a quarterly rate sensitivity report is used to determine the effect of interest rate changes on the financial statements. In the opinion of management, enough assets or liabilities could be repriced over the near term (up to three years) to compensate for such changes. The spread on interest rates, or the difference between the average earning assets and the average interest-bearing liabilities, is monitored quarterly.

## CONSUMERS BANCORP, INC.

### Management's Discussion and Analysis of Financial Condition

#### **and Results of Operations (continued)**

(Dollars in thousands, except per share data)

#### **Capital Resources**

Total shareholders' equity increased by \$870 from June 30, 2012 to \$28,760 as of September 30, 2012. The increase was mainly due to net income for the current three month period and an increase in the fair value of available-for-sale securities offset by cash dividends paid during the period.

The Bank is subject to various regulatory capital requirements administered by federal regulatory agencies. Capital adequacy guidelines and prompt corrective-action regulations involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Failure to meet various capital requirements can initiate regulatory action that could have a direct material effect on the Corporation's financial statements.

The Bank's leverage and risk-based capital ratios as of September 30, 2012 were 7.3% and 13.3%, respectively. This compares to leverage and risk-based capital ratios of 7.4% and 13.4%, respectively, as of June 30, 2012. The Bank exceeded minimum regulatory capital requirements to be considered well-capitalized for both periods. Management is not aware of any matters occurring subsequent to September 30, 2012 that would cause the Bank's capital category to change.

Regulatory reforms continue to be adopted which impose additional restrictions on current business practices and one such proposal is the Federal Reserve BASEL III capital plan rules. In June 2012, the Federal Reserve Board, Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively, the Agencies) each issued notices of proposed rulemaking that would revise and replace the Agencies' current capital rules to align with the BASEL III capital standards and meet certain requirements of the Dodd-Frank Act. Certain requirements of the notices of proposed rulemaking would establish more restrictive capital definitions, higher risk-weightings for certain asset classes, capital buffers and higher minimum capital ratios. The notices of proposed rulemaking were in a comment period through October 22, 2012, and are subject to further modification by the Agencies. We are currently evaluating the impact of the proposals on our regulatory capital ratios. There can be no guarantee that Basel III will be adopted in its current form, what changes may be made before adoption, or when ultimate adoption will occur.

### **Critical Accounting Policies**

The financial condition and results of operations for the Corporation presented in the Consolidated Financial Statements, accompanying notes to the Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations are, to a large degree, dependent upon the Corporation's accounting policies. The selection and application of these accounting policies involve judgments, estimates and uncertainties that are susceptible to change.

## CONSUMERS BANCORP, INC.

### Management's Discussion and Analysis of Financial Condition

#### and Results of Operations (continued)

(Dollars in thousands, except per share data)

The Corporation has identified the appropriateness of the allowance for loan losses and the valuation of securities as critical accounting policies and an understanding of these policies are necessary to understand the financial statements. Critical accounting policies are those policies that require management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Footnote one (Securities and Allowance for Loan Losses), footnote two (Securities), footnote three (Loans) and Management Discussion and Analysis of Financial Condition and Results from Operation (Critical Accounting Policies) of the 2012 Form 10-K provide detail with regard to the Corporation's accounting for the allowance for loan losses and valuation of securities and other-than-temporary impairment. There have been no significant changes in the application of accounting policies since June 30, 2012.

#### Forward-Looking Statements

When used in this report (including information incorporated by reference in this report), the words or phrases "will likely result," "are expected to," "will continue," "is anticipated," "estimate," "project," "believe" or similar expressions are intended to identify "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements may involve risks and uncertainties that are difficult to predict, may be beyond the Corporation's control, and could cause actual results to differ materially from those described in such statements. Any such forward-looking statements are made only as of the date of this report or the respective dates of the relevant incorporated documents, as the case may be, and, except as required by law, the Corporation undertakes no obligation to update these forward-looking statements to reflect subsequent events or circumstances. Factors that could cause actual results for future periods to differ materially from those anticipated or projected include, but are not limited to:

- regional and national economic conditions becoming less favorable than expected, resulting in, among other things, a deterioration in credit quality of assets and the underlying value of collateral could prove to be less valuable than otherwise assumed;
- the economic impact from the oil and gas activity in the region could be less than expected or the timeline for development could be longer than anticipated;
- the nature, extent, and timing of government and regulatory actions;
- material unforeseen changes in the financial condition or results of Consumers National Bank's customers;
- changes in levels of market interest rates which could reduce anticipated or actual margins;
- competitive pressures on product pricing and services; and
- a deterioration in market conditions causing debtors to be unable to meet their obligations.





**CONSUMERS BANCORP, INC.**

Management's Discussion and Analysis of Financial Condition

**and Results of Operations (continued)**

(Dollars in thousands, except per share data)

The risks and uncertainties identified above are not the only risks the Corporation faces. Additional risks and uncertainties not presently known to the Corporation or that the Corporation currently believes to be immaterial also may adversely affect the Corporation. Should any known or unknown risks and uncertainties develop into actual events, those developments could have material adverse effects on the Corporation's business, financial condition and results of operations.

**CONSUMERS BANCORP, INC.**

**Item 4 – Controls and Procedures**

**Evaluation of Disclosure Controls and Procedures**

As of the end of the period covered by the report, an evaluation was performed under the supervision and with the participation of the Corporation's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Corporation's disclosure controls and procedures pursuant to Exchange Act Rule 13a- 15e. Based on the evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective.

**Changes in Internal Controls Over Financial Reporting**

There have not been any changes in the Corporation's internal control over financial reporting that occurred during the Corporation's last quarter that has materially affected, or is reasonably likely to materially affect, internal control over financial reporting.

**CONSUMERS BANCORP, INC.**

**PART II – OTHER INFORMATION**

Item 1 – Legal Proceedings

None

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

None

Item 3 – Defaults Upon Senior Securities

None

Item 4 – Mine Safety Disclosures

Not Applicable

Item 5 – Other Information

None

Item 6 – Exhibits

Exhibit Number	Description
Exhibit 11	Statement regarding Computation of Per Share Earnings (included in Note 1 to the Consolidated Financial Statements).
Exhibit 31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
Exhibit 31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer

Exhibit 32.1 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes Oxley Act of 2002.

Exhibit 101 The following material from Consumers Bancorp, Inc.'s Form 10-Q Report for the quarterly period ended September 30, 2012, formatted in XBRL (Extensible Business Reporting Language) includes: (1) Unaudited Consolidated Balance Sheets, (2) Unaudited Consolidated Statements of Income, (3) Unaudited Consolidated Statements of Comprehensive Income, (4) Unaudited Consolidated Statement of Changes in Shareholders' Equity, (5) Unaudited Condensed Consolidated Statements of Cash Flows, and (6) the Notes to Unaudited Condensed Consolidated Financial Statements.

**CONSUMERS BANCORP, INC.**

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.

CONSUMERS BANCORP, INC.  
(Registrant)

Date: November 14, 2012 /s/ Ralph J. Lober  
Ralph J. Lober, II  
President & Chief Executive Officer  
(principal executive officer)

Date: November 14, 2012 /s/ Renee K. Wood  
Renee K. Wood  
Chief Financial Officer & Treasurer  
(principal financial officer)