MERIDIAN INTERSTATE BANCORP INC
Form 10-Q
August 09, 2012
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UNITED STATES

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 quarterly period ended June 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 number 001-33898

Meridian Interstate Bancorp, Inc.

(Exact name of registrant as specified in its charter)

Massachusetts	**20-4652200**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
10 Meridian Street, East Boston, Massachusetts	**02128**
(Address of Principal Executive Offices)	**Zip Code**

(617) 567-1500

(Registrant s telephone number, including area code)

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 and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x 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. (Check one):

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

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

At August 2, 2012, the registrant had 22,075,378 shares of no par value common stock outstanding.

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PART I FINANCIAL INFORMATION

ITEM 1. ***FINANCIAL STATEMENTS***

MERIDIAN INTERSTATE BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Unaudited)

	June 30, 2012	December 31, 2011
	(Dollars in thousands)	
ASSETS		
Cash and due from banks	$ 124,512	$ 156,622
Federal funds sold	63	63
Total cash and cash equivalents	124,575	156,685
Certificates of deposit - affiliate bank		2,500
Securities available for sale, at fair value	298,710	335,230
Federal Home Loan Bank stock, at cost	12,064	12,538
Loans held for sale	11,502	4,192
Loans	1,554,077	1,354,354
Less allowance for loan losses	(16,271)	(13,053)
Loans, net	1,537,806	1,341,301
Bank-owned life insurance	35,646	35,050
Foreclosed real estate, net	3,012	3,853
Investment in affiliate bank		12,607
Premises and equipment, net	38,447	36,991
Accrued interest receivable	6,828	7,282
Prepaid deposit insurance	445	1,257
Deferred tax asset, net	6,519	7,434
Goodwill	13,687	13,687
Other assets	10,753	3,773
Total assets	$ 2,099,994	$ 1,974,380
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits:		
Non interest-bearing	$ 172,661	$ 145,274
Interest-bearing Interest-bearing	1,527,976	1,459,214
Total deposits	1,700,637	1,604,488
Short-term borrowings - affiliate bank		6,471
Short-term borrowings - other	10,063	10,056
Long-term debt	144,551	114,923
Accrued expenses and other liabilities	15,976	18,498
Total liabilities	1,871,227	1,754,436

Stockholders equity:		
Common stock, no par value, 50,000,000 shares authorized; 23,000,000 shares issued		
Additional paid-in capital	98,000	97,669
Retained earnings	142,136	134,533
Accumulated other comprehensive income	5,485	3,985
Treasury stock, at cost, 668,084 and 584,881 shares at June 30, 2012 and December 31, 2011, respectively	(8,419)	(7,317)
Unearned compensation - ESOP, 641,700 and 662,400 shares at June 30, 2012 and December 31, 2011, respectively	(6,417)	(6,624)
Unearned compensation - restricted shares, 258,590 and 265,710 at June 30, 2012 and December 31, 2011, respectively	(2,018)	(2,302)
Total stockholders equity	228,767	219,944
Total liabilities and stockholders equity	$ 2,099,994	$ 1,974,380

See accompanying notes to unaudited consolidated financial statements.

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MERIDIAN INTERSTATE BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(Dollars in thousands, except per share amounts)			
Interest and dividend income:				
Interest and fees on loans	$ 18,565	$ 16,237	$ 36,553	$ 32,797
Interest on debt securities	2,006	2,896	4,204	6,001
Dividends on equity securities	292	255	653	499
Interest on certificates of deposit	9	9	18	17
Interest on other interest-earning assets	63	117	129	202
Other interest and dividend income	33	27	48	36
Total interest and dividend income	20,968	19,541	41,605	39,552
Interest expense:				
Interest on deposits	3,817	4,616	7,820	9,189
Interest on short-term borrowings	4	13	9	23
Interest on long-term debt	752	778	1,530	1,657
Total interest expense	4,573	5,407	9,359	10,869
Net interest income	16,395	14,134	32,246	28,683
Provision for loan losses	2,170	486	3,434	828
Net interest income, after provision for loan losses	14,225	13,648	28,812	27,855
Non-interest income:				
Customer service fees	1,505	1,497	3,084	2,795
Loan fees	177	161	239	277
Mortgage banking gains, net	537	169	1,162	605
Gain on sales of securities, net	1,259	2,922	2,342	3,789
Income from bank-owned life insurance	295	298	596	615
Equity income on investment in affiliate bank	67	333	310	818
Gain on sale of investment in affiliate bank	4,819		4,819	
Other income	1	4	1	15
Total non-interest income	8,660	5,384	12,553	8,914
Non-interest expenses:				
Salaries and employee benefits	8,642	7,058	17,943	14,159
Occupancy and equipment	2,058	1,869	4,095	4,085
Data processing	857	651	1,689	1,460
Marketing and advertising	650	540	1,209	1,081
Professional services	870	811	1,703	1,441
Foreclosed real estate	103	63	286	100
Deposit insurance	440	633	871	1,258
Other general and administrative	1,179	860	2,269	1,538

Total non-interest expenses	14,799	12,485	30,065	25,122
Income before income taxes	8,086	6,547	11,300	11,647
Provision for income taxes	2,639	2,382	3,697	4,271
Net income	$ 5,447	$ 4,165	$ 7,603	$ 7,376
Income per share:				
Basic	$ 0.25	$ 0.19	$ 0.35	$ 0.34
Diluted	$ 0.25	$ 0.19	$ 0.35	$ 0.33
Weighted average shares:				
Basic	21,630,660	21,852,665	21,647,237	21,917,330
Diluted	21,808,507	21,994,371	21,818,079	22,044,635

See accompanying notes to unaudited consolidated financial statements.

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MERIDIAN INTERSTATE BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(In thousands)			
Net income	$ 5,447	$ 4,165	$ 7,603	$ 7,376
Other comprehensive income (loss), net of taxes:				
Unrealized holding gain (loss) on securities available for sale	58	2,373	4,781	2,227
Reclassification adjustments for gain realized in income	(1,259)	(2,922)	(2,342)	(3,789)
Unrealized gain (loss)	(1,201)	(549)	2,439	(1,562)
Tax effect	487	175	(939)	592
Total other comprehensive income (loss)	(714)	(374)	1,500	(970)
Total comprehensive income	$ 4,733	$ 3,791	$ 9,103	$ 6,406

See accompanying notes to unaudited consolidated financial statements.

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MERIDIAN INTERSTATE BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

Six Months Ended June 30, 2012 and 2011

(Unaudited)

	Shares of Common Stock Outstanding	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Unearned Compensation - ESOP	Unearned Compensation - Restricted Shares	Total
				(Dollars in thousands)				
Six Months Ended June 30, 2011								
Balance at December 31, 2010	22,480,877	$ 97,005	$ 122,563	$ 8,038	$ (2,121)	$ (7,038)	$ (2,836)	$ 215,611
Net income			7,376					7,376
Other comprehensive loss				(970)				(970)
Purchase of treasury stock	(249,182)				(3,360)			(3,360)
ESOP shares earned (20,700 shares)		64				207		271
Share-based compensation expense	8,820	264					260	524
Balance at June 30, 2011	22,240,515	$ 97,333	$ 129,939	$ 7,068	$ (5,481)	$ (6,831)	$ (2,576)	$ 219,452
Six Months Ended June 30, 2012								
Balance at December 31, 2011	22,149,409	$ 97,669	$ 134,533	$ 3,985	$ (7,317)	$ (6,624)	$ (2,302)	$ 219,944
Net income			7,603					7,603
Other comprehensive income				1,500				1,500
Stock option exercise	3,101	(30)			39			9
Purchase of treasury stock	(86,304)				(1,141)			(1,141)
ESOP shares earned (20,700 shares)		66				207		273
Share-based compensation expense	7,120	295					284	579
Balance at June 30, 2012	22,073,326	$ 98,000	$ 142,136	$ 5,485	$ (8,419)	$ (6,417)	$ (2,018)	$ 228,767

See accompanying notes to unaudited consolidated financial statements.

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MERIDIAN INTERSTATE BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended June 30,	
	2012	2011
	(In thousands)	
Cash flows from operating activities:		
Net income	$ 7,603	$ 7,376
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Accretion of acquisition fair value adjustments	(306)	(1,019)
Earned ESOP shares	273	271
Provision for loan losses	3,434	828
Amortization (accretion) of net deferred loan origination fees/costs	(30)	250
Net amortization of securities available for sale	175	367
Depreciation and amortization expense	1,081	1,193
Gain on sales of securities, net	(2,342)	(3,789)
(Gain) loss and provision for foreclosed real estate, net	134	(109)
Deferred income tax provision (benefit)	(24)	119
Income from bank-owned life insurance	(596)	(615)
Equity income on investment in affiliate bank	(310)	(818)
Gain on sale of investment in affiliate bank	(4,819)	
Share-based compensation expense	579	524
Net changes in:		
Loans held for sale	(7,310)	9,677
Accrued interest receivable	454	369
Prepaid deposit insurance	812	1,183
Other assets	58	3,261
Accrued expenses and other liabilities	(2,522)	12,805
Net cash (used in) provided by operating activities	(3,656)	31,873
Cash flows from investing activities:		
Purchases of certificates of deposit		(2,500)
Maturities of certificates of deposit	2,500	
Activity in securities available for sale:		
Proceeds from maturities, calls and principal payments	91,952	73,896
Redemption (purchase) of mutual funds, net	(5,587)	2,230
Proceeds from sales	16,379	31,313
Purchases	(57,427)	(96,595)
Proceeds from sale of investment in affiliate bank	6,600	
Redemption of Federal Home Loan Bank stock	474	
Loans originated, net of principal payments received	(200,482)	(36,103)
Purchases of premises and equipment	(2,496)	(2,265)
Capitalized costs on foreclosed real estate		(37)
Proceeds from sales of foreclosed real estate	1,061	405
Net cash used in investing activities	(147,026)	(29,656)

(continued)

See accompanying notes to unaudited consolidated financial statements.

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MERIDIAN INTERSTATE BANCORP, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended June 30,	
	2012	**2011**
	(In thousands)	
Cash flows from financing activities:		
Net increase in deposits	96,167	81,900
Net change in borrowings with maturities less than three months	(6,463)	10,525
Proceeds from Federal Home Loan Bank advances with maturities of three months or more	62,500	
Repayment of Federal Home Loan Bank advances with maturities of three months or more	(32,500)	(20,000)
Stock option exercise	9	
Purchase of treasury stock	(1,141)	(3,360)
Net cash provided by financing activities	118,572	69,065
Net change in cash and cash equivalents	(32,110)	71,282
Cash and cash equivalents at beginning of period	156,685	155,493
Cash and cash equivalents at end of period	$ 124,575	$ 226,775
Supplemental cash flow information:		
Interest paid on deposits	$ 7,949	$ 9,524
Interest paid on borrowings	1,965	2,427
Income taxes paid, net of refunds	3,610	1,316
Non-cash investing and financing activities:		
Transfers from loans to foreclosed real estate	354	1,290
Receipt of common stock from sale of investment in affiliate bank	11,136	
Net amounts due from broker on security transactions	7,038	

See accompanying notes to unaudited consolidated financial statements.

MERIDIAN INTERSTATE BANCORP, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The consolidated financial statements include the accounts of Meridian Interstate Bancorp, Inc. and all other entities in which it has a controlling financial interest (collectively referred to as the Company), a 59.6%-owned subsidiary of Meridian Financial Services, Incorporated (Meridian), a mutual holding company. The Company was formed in a corporate reorganization in 2006 and owns East Boston Savings Bank and its subsidiaries (the Bank). The Company held a 43% share in Hampshire First Bank, a New Hampshire chartered bank, organized and headquartered in Manchester, New Hampshire, which was accounted for using the equity method. On November 16, 2011, Hampshire First Bank entered into an Agreement and Plan of Merger with NBT Bancorp, Inc. (NBT) and NBT Bank, N.A. The merger of Hampshire First Bank into NBT was completed on June 8, 2012, with the Company recognizing a pre-tax gain of $4.8 million and receiving $6.6 million of cash and 547,481 NBTB shares totaling $11.1 million as proceeds from the sale.

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Such adjustments were of a normal recurring nature. The results of operations for the three and six months ended June 30, 2012 are not necessarily indicative of the results that may be expected for the entire year or any other interim period. For additional information, refer to the financial statements and footnotes thereto of the Company included in the Company s Form 10-K for the year ended December 31, 2011 which was filed with the Securities and Exchange Commission (SEC) on March 15, 2012, and is available through the SEC s website at www.sec.gov.

In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the evaluation of goodwill for impairment, other-than-temporary impairment of securities and the valuation of deferred tax assets.

2. RECENT ACCOUNTING PRONOUNCEMENTS

In May 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS*. ASU 2011-04 clarifies and expands the disclosures pertaining to unobservable inputs used in Level 3 fair value measurements, including the disclosure of quantitative information related to (1) the valuation processes used, (2) the sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, and (3) use of a nonfinancial asset in a way that differs from the asset s highest and best use. ASU 2011-04 also requires, for public companies, disclosure of the level within the fair value hierarchy for assets and liabilities not measured at fair value in the statement of financial position but for which the fair value is disclosed. The amendments in ASU 2011-04 are to be applied prospectively. The Company adopted ASU 2011-04 during the first quarter of 2012 resulting in additional disclosures see Note 7.

In June 2011, the FASB issued ASU No. 2011-05, *Comprehensive Income (Topic 220)*, *Presentation of Comprehensive Income*. ASU No. 2011-05 amends the disclosure requirements for the presentation of comprehensive income. The amended guidance eliminates the option to present components of other comprehensive income (OCI) as part of the statement of changes in stockholders equity. Under the amended guidance, all changes in OCI are to be presented either in a single continuous statement of comprehensive income or in two separate but consecutive financial statements. The Company adopted ASU 2011-05 during the first quarter of 2012 resulting in an additional financial statement see Consolidated Statements of Comprehensive Income.

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In July 2012, the FASB issued ASU No. 2012-02, *Intangibles Goodwill and Other (Topic 350); Testing Indefinite Lived Intangible Assets for Impairment.* ASU No. 2012-02 simplifies the guidance for testing the decline in the realizable value of indefinite-lived intangible assets other than goodwill. This amendment allows an organization the option to first assess qualitative factors to determine whether it is necessary to perform the quantitative impairment test. An organization electing to perform a qualitative assessment is no longer required to calculate the fair value of an indefinite-lived intangible asset unless the organization determines, based on a qualitative assessment, that is more likely than not that the asset is impaired. The amendments in ASU 2012-02 are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The Company does not expect this pronouncement to have a material effect on its consolidated financial statements.

3. EARNINGS PER SHARE

Basic earnings per share excludes dilution and is calculated by dividing net income available to common stockholders by the weighted-average number of common shares outstanding during the period. If rights to dividends on unvested stock awards are non-forfeitable, these unvested stock awards are considered outstanding in the computation of basic earnings per share. Diluted earnings per share is computed in a manner similar to that of basic earnings per share except that the weighted-average number of common shares outstanding is increased to include the number of incremental common shares (computed using the treasury method) that would have been outstanding if all potentially dilutive common stock equivalents (such as options) were issued during the period. Unallocated common shares held by the ESOP are shown as a reduction in stockholders equity and are not included in the weighted-average number of common shares outstanding for either basic or diluted earnings per share calculations.

Basic and diluted earnings per share have been computed based on the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(Dollars in thousands, except per share amounts)			
Net income available to common stockholders	$ 5,447	$ 4,165	$ 7,603	$ 7,376
Average number of common shares outstanding	21,460,224	21,642,552	21,475,457	21,707,724
Effect of unvested stock awards	170,436	210,113	171,780	209,606
Basic weighted average shares outstanding	21,630,660	21,852,665	21,647,237	21,917,330
Effect of dilutive stock options	177,847	141,706	170,842	127,305
Diluted weighted average shares outstanding	21,808,507	21,994,371	21,818,079	22,044,635
Earnings per share:				
Basic	$ 0.25	$ 0.19	$ 0.35	$ 0.34
Diluted	$ 0.25	$ 0.19	$ 0.35	$ 0.33

Options for the exercise of 71,100 and 21,500 shares for the three months ended June 30, 2012 and 2011, respectively, and options for the exercise of 64,850 and 14,500 shares for the six months ended June 30, 2012 and 2011, respectively, were not included in the calculation of diluted earnings per share because to do so would have been anti-dilutive.

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4. SECURITIES

The following table sets forth the amortized cost and fair value of securities available for sale.

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(In thousands)		
June 30, 2012				
Debt securities:				
Corporate bonds:				
Financial services	$ 80,097	$ 1,557	$ (679)	$ 80,975
Industry and manufacturing	22,868	696	(16)	23,548
Consumer products and services	17,301	763		18,064
Technology	6,007	101		6,108
Healthcare	18,581	775		19,356
Other	2,521	70		2,591
Total corporate bonds	147,375	3,962	(695)	150,642
Government-sponsored enterprises	50,298	147	(2)	50,443
Municipal bonds	7,384	199		7,583
Residential mortgage-backed securities:				
Government-sponsored enterprises	21,235	1,265	(1)	22,499
Private label	3,651	61	(78)	3,634
Total debt securities	229,943	5,634	(776)	234,801
Marketable equity securities:				
Common stocks:				
Financial services	15,299	933	(281)	15,951
Industry and manufacturing	7,719	1,323	(261)	8,781
Consumer products and services	11,910	1,364	(200)	13,074
Technology	2,129	795	(28)	2,896
Healthcare	2,761	633		3,394
Other	4,175	1,018		5,193
Total common stocks	43,993	6,066	(770)	49,289
Money market mutual funds	14,637		(17)	14,620
Total marketable equity securities	58,630	6,066	(787)	63,909
Total securities available for sale	$ 288,573	$ 11,700	$ (1,563)	$ 298,710
December 31, 2011				
Debt securities:				
Corporate bonds:				
Financial services	$ 75,235	$ 871	$ (2,012)	$ 74,094
Industry and manufacturing	27,023	911	(11)	27,923
Consumer products and services	26,087	1,092	(15)	27,164
Technology	12,762	177	(22)	12,917
Healthcare	20,104	885		20,989
Other	2,535	82		2,617
Total corporate bonds	163,746	4,018	(2,060)	165,704

Government-sponsored enterprises	82,898	299	(2)	83,195
Municipal bonds	7,401	173		7,574
Residential mortgage-backed securities:				
Government-sponsored enterprises	25,296	1,369	(1)	26,664
Private label	7,322	77	(344)	7,055
Total debt securities	286,663	5,936	(2,407)	290,192
Marketable equity securities:				
Common stocks:				
Financial services	4,808	304	(547)	4,565
Industry and manufacturing	5,215	862	(36)	6,041
Consumer products and services	13,553	1,812	(113)	15,252
Technology	2,479	687	(23)	3,143
Healthcare	2,461	432		2,893
Other	3,304	809		4,113
Total common stocks	31,820	4,906	(719)	36,007
Money market mutual funds	9,049		(18)	9,031
Total marketable equity securities	40,869	4,906	(737)	45,038
Total securities available for sale	$ 327,532	$ 10,842	$ (3,144)	$ 335,230

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The amortized cost and fair value of debt securities by contractual maturity at June 30, 2012 are as follows. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without prepayment penalties.

	Within 1 year		Over 1 year to 5 years		Over 5 years		Total	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
				(In thousands)				
Corporate bonds:								
Financial services	$ 3,995	$ 4,002	$ 68,517	$ 69,428	$ 7,585	$ 7,545	$ 80,097	$ 80,975
Industry and manufacturing	5,020	5,089	17,848	18,459			22,868	23,548
Consumer products and services	990	1,037	16,311	17,027			17,301	18,064
Technology	2,500	2,537	3,507	3,571			6,007	6,108
Healthcare	5,513	5,592	13,068	13,764			18,581	19,356
Other	1,500	1,500	1,021	1,091			2,521	2,591
Total corporate bonds	19,518	19,757	120,272	123,340	7,585	7,545	147,375	150,642
Government-sponsored enterprises	66	66	4,120	4,143	46,112	46,234	50,298	50,443
Municipal bonds			5,914	6,046	1,470	1,537	7,384	7,583
Residential mortgage-backed securities:								
Government-sponsored enterprises			5	5	21,230	22,494	21,235	22,499
Private label					3,651	3,634	3,651	3,634
Total	$ 19,584	$ 19,823	$ 130,311	$ 133,534	$ 80,048	$ 81,444	$ 229,943	$ 234,801

For the three months ended June 30, 2012 and 2011, proceeds from sales of securities available for sale amounted to $8.6 million and $27.4 million, respectively. Gross gains of $1.4 million and $3.1 million and gross losses of $98,000 and $131,000, respectively, were realized on those sales. For the six months ended June 30, 2012 and 2011, proceeds from sales of securities available for sale amounted to $16.4 million and $31.3 million, respectively. Gross gains of $2.4 million and $3.9 million and gross losses of $98,000 and $131,000, respectively, were realized on those sales.

Information pertaining to securities available for sale as of June 30, 2012 and December 31, 2011, with gross unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
		(In thousands)		
June 30, 2012				
Debt securities:				
Corporate bonds:				
Financial services	$ 540	$ 23,789	$ 139	$ 2,805
Industry and manufacturing	16	1,975		
Total corporate bonds	556	25,764	139	2,805
Government-sponsored enterprises	2	998		
Residential mortgage-backed securities:				
Government-sponsored enterprises	1	11		
Private label			78	417

Total debt securities	559	26,773	217	3,222
Marketable equity securities:				
Common stocks:				
Financial services	240	1,751	41	1,042
Industry and manufacturing	261	1,339		
Consumer products and services	200	2,747		
Technology	28	370		
Total common stocks	729	6,207	41	1,042
Money market mutual funds			17	996
Total marketable equity securities	729	6,207	58	2,038
Total temporarily impaired securities	$ 1,288	$ 32,980	$ 275	$ 5,260

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	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
	(In thousands)			
December 31, 2011				
Debt securities:				
Corporate bonds:				
Financial services	$ 1,937	$ 39,418	$ 75	$ 923
Industry and manufacturing	11	1,937		
Consumer products and services	15	1,695		
Technology	22	2,488		
Total corporate bonds	1,985	45,538	75	923
Government-sponsored enterprises	2	998		
Residential mortgage-backed securities:				
Government-sponsored enterprises	1	212		
Private label	231	5,736	113	322
Total debt securities	2,219	52,484	188	1,245
Marketable equity securities:				
Common stocks:				
Financial services	443	2,126	104	620
Industry and manufacturing	36	688		
Consumer products and services	113	1,880		
Technology	23	737		
Total common stocks	615	5,431	104	620
Money market mutual funds			18	985
Total marketable equity securities	615	5,431	122	1,605
Total temporarily impaired securities	$ 2,834	$ 57,915	$ 310	$ 2,850

The Company determined no securities were other-than-temporarily impaired for the six months ended June 30, 2012. Management evaluates securities for other-than-temporary impairment on a quarterly basis, with more frequent evaluation for selected issuers or when economic or market concerns warrant such evaluations.

As of June 30, 2012, the net unrealized gain on the total debt securities portfolio was $4.9 million. At June 30, 2012, 24 debt securities had unrealized losses with aggregate depreciation of 2.5% from the Company s amortized cost basis. In analyzing a debt issuer s financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, industry analysts reports and, to a lesser extent given the relatively insignificant levels of depreciation in the Company s debt portfolio, spread differentials between the effective rates on instruments in the portfolio compared to risk-free rates. The unrealized losses are primarily caused by (a) recent declines in profitability and near-term profit forecasts by industry analysts resulting from a decline in the level of business activity and (b) recent downgrades by several industry analysts. The contractual terms of these investments do not permit the companies to settle the security at a price less than the par value of the investment. The Company currently does not believe it is probable that it will be unable to collect all amounts due according to the contractual terms of the investments. Therefore, it is expected that the bonds would not be settled at a price less than the par value of the investment. Because (1) the Company does not intend to sell the securities; (2) the Company does not believe it is more likely than not that the Company will be required to sell the securities before recovery of its amortized cost basis; and (3) the present value of expected cash flows is sufficient to recover the entire amortized cost basis of the securities, the Company does not consider these investments to be other-than-temporarily impaired at June 30, 2012.

As of June 30, 2012, the net unrealized gain on the total marketable equity portfolio was $5.3 million. At June 30, 2012, 22 marketable equity securities have unrealized losses with aggregate depreciation of 8.7% from the Company s cost basis. Two equity securities had a market value

decline of 25.0% or more, with net unrealized losses of $190,000. Although the issuers have shown declines in earnings as a result of the weakened economy, no credit issues have been identified that cause management to believe the decline in market value is other than temporary, and the Company has the ability and intent to hold these investments until a recovery of fair value. In analyzing an equity issuer s financial condition, management considers industry analysts reports, financial

performance and projected target prices of investment analysts within a one-year time frame. A decline of 10% or more in the value of an equity security is generally the triggering event for management to review individual securities for liquidation and/or classification as other-than-temporarily impaired. Impairment losses are recognized when management concludes that declines in the value of equity securities are other than temporary, or when they can no longer assert that they have the intent and ability to hold depreciated equity securities for a period of time sufficient to allow for any anticipated recovery in fair value. Unrealized losses on marketable equity securities that are in excess of 25% of cost and that have been sustained for more than twelve months are generally considered-other-than temporary and charged to earnings as impairment losses, or realized through sale of the security.

5. LOANS

The Company s loan portfolio consists primarily of residential real estate, commercial real estate, construction, commercial business and consumer segments. The residential real estate loans include classes for one-to four-family, multi-family and home equity lines of credit. There are no foreign loans outstanding. Interest rates charged on loans are affected principally by the demand for such loans, the supply of money available for lending purposes and the rates offered by our competitors. A summary of loans follows:

	June 30, 2012		December 31, 2011	
	Amount	%	Amount	%
	(Dollars in thousands)			
Real estate loans:				
Residential real estate:				
One-to four-family	$ 441,251	28.4%	$ 417,889	30.9%
Multi-family	179,496	11.6	176,668	13.0
Home equity lines of credit	62,534	4.0	60,989	4.5
Commercial real estate	590,923	38.0	528,585	39.0
Construction	162,106	10.4	93,158	6.9
Total real estate loans	1,436,310	92.4	1,277,289	94.3
Commercial business loans	111,659	7.2	71,544	5.3
Consumer	5,776	0.4	5,195	0.4
Total loans	1,553,745	100.0%	1,354,028	100.0%
Allowance for loan losses	(16,271)		(13,053)	
Net deferred loan origination costs	332		326	
Loans, net	$ 1,537,806		$ 1,341,301	

The Company has transferred a portion of its originated commercial real estate loans to participating lenders. The amounts transferred have been accounted for as sales and are therefore not included in the Company s accompanying balance sheets. The Company and participating lenders share ratably in any gains or losses that may result from a borrower s lack of compliance with contractual terms of the loan. The Company continues to service the loans on behalf of the participating lenders and, as such, collects cash payments from the borrowers, remits payments to participating lenders and disburses required escrow funds to relevant parties. At June 30, 2012 and December 31, 2011, the Company was servicing loans for participants aggregating $37.3 million and $25.6 million, respectively.

As a result of the Mt. Washington Co-operative Bank (Mt. Washington) acquisition in January 2010, the Company acquired loans at fair value of $345.3 million. Included in this amount was $27.7 million of loans with evidence of deterioration of credit quality since origination for which it was probable, at the time of the acquisition, that the Company would be unable to collect all contractually required payments receivable. The Company s evaluation of loans with evidence of credit deterioration as of the acquisition date resulted in a nonaccretable discount of $7.6 million, which is defined as the loan s contractually required payments receivable in excess of the amount of its cash flows expected to be collected. The Company considered factors such as payment history, collateral values, and accrual status when determining whether there was evidence of deterioration of the loan s credit quality at the acquisition date.

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The following is a summary of the outstanding balance of the acquired loans with evidence of credit deterioration:

	June 30, 2012	December 31, 2011
	(In thousands)	
Real estate loans:		
Residential real estate:		
One-to four-family	$ 7,668	$ 7,754
Multi-family	1,293	1,862
Home equity lines of credit	570	624
Commercial real estate	1,657	3,265
Construction		1,588
Total real estate loans	11,188	15,093
Commercial business loans	78	90
Consumer	4	4
	82	94
Outstanding principal balance	11,270	15,187
Discount	(2,606)	(3,167)
Carrying amount	$ 8,664	$ 12,020

A rollforward of accretable yield follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(In thousands)			
Beginning balance	$ 1,162	$	$ 1,181	$
Reclassification from nonaccretable discount				
Accretion	(18)		(37)	
Disposals				
Ending balance	$ 1,144	$	$ 1,144	$

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An analysis of the allowance for loan losses and related information follows:

	One-to four-family	Multi-family	Home equity lines of credit	Commercial real estate	Construction	Commercial business	Consumer	Unallocated	Total
					(In thousands)				
					For the Three Months Ended June 30, 2012				
Beginning balance	$ 2,090	$ 1,439	$ 158	$ 7,125	$ 2,082	$ 1,131	$ 72	$	$ 14,097
Provision (credit) for loan loss	230	13	6	12	1,501	380	28		2,170
Charge-offs	(168)				(218)		(16)		(402)
Recoveries	170				229		7		406
Ending balance	$ 2,322	$ 1,452	$ 164	$ 7,137	$ 3,594	$ 1,511	$ 91	$	$ 16,271
					For the Six Months Ended June 30, 2012				
Beginning balance	$ 1,861	$ 1,361	$ 245	$ 6,980	$ 1,430	$ 1,061	$ 115	$	$ 13,053
Provision (credit) for loan loss	650	163	(29)	(61)	2,231	446	34		3,434
Charge-offs	(367)	(72)	(52)	(9)	(298)		(75)		(873)
Recoveries	178			227	231	4	17		657
Ending balance	$ 2,322	$ 1,452	$ 164	$ 7,137	$ 3,594	$ 1,511	$ 91	$	$ 16,271
					At June 30, 2012				
Amount of allowance for loan losses for loans deemed to be impaired	$ 213	$ 48	$ 7	$ 6	$ 392	$ 4	$	$	$ 670
Amount of allowance for loan losses for loans not deemed to be impaired	2,109	1,404	157	7,131	3,202	1,507	91		15,601
	$ 2,322	$ 1,452	$ 164	$ 7,137	$ 3,594	$ 1,511	$ 91	$	$ 16,271
Amount of allowance for loan losses for loans acquired with deteriorated credit quality included above	$ 96	$	$	$	$	$ 5	$	$	$ 101
Loans deemed to be impaired	$ 3,863	$ 5,669	$ 23	$ 10,614	$ 22,892	$ 1,138	$	$	$ 44,199
Loans not deemed to be impaired	437,388	173,827	62,511	580,309	139,214	110,521	5,776		1,509,546
	$ 441,251	$ 179,496	$ 62,534	$ 590,923	$ 162,106	$ 111,659	$ 5,776	$	$ 1,553,745
					For the Three Months Ended June 30, 2011				
Beginning balance	$ 1,078	$ 1,273	$ 177	$ 5,976	$ 1,296	$ 492	$ 31	$	$ 10,323
Provision (credit) for loan loss	150	68	(2)	7	154	60	49		486
Charge-offs	(31)				(37)	(14)	(18)		(100)
Recoveries	51	41		10	36		14		152
Ending balance	$ 1,248	$ 1,382	$ 175	$ 5,993	$ 1,449	$ 538	$ 76	$	$ 10,861

	For the Six Months Ended June 30, 2011								
Beginning balance	$ 1,130	$ 1,038	$ 227	$ 5,238	$ 2,042	$ 448	$ 32	$	$ 10,155
Provision (credit) for loan loss	200	301	(26)	819	(652)	123	63		828
Charge-offs	(135)		(27)	(74)	(231)	(33)	(48)		(548)
Recoveries	53	43	1	10	290		29		426
Ending balance	$ 1,248	$ 1,382	$ 175	$ 5,993	$ 1,449	$ 538	$ 76	$	$ 10,861

	At June 30, 2011								
Amount of allowance for loan losses for loans deemed to be impaired	$ 94	$	$ 8	$ 69	$	$	$	$	$ 171
Amount of allowance for loan losses for loans not deemed to be impaired	1,154	1,382	167	5,924	1,449	538	76		10,690
	$ 1,248	$ 1,382	$ 175	$ 5,993	$ 1,449	$ 538	$ 76	$	$ 10,861
Amount of allowance for loan losses for loans acquired with deteriorated credit quality included above	$	$	$	$ 5	$	$	$	$	$ 5
Loans deemed to be impaired	$ 4,601	$ 4,191	$ 124	$ 10,995	$ 27,028	$ 616	$	$	$ 47,555
Loans not deemed to be impaired	389,058	172,134	61,964	445,398	63,563	32,725	5,613		1,170,455
	$ 393,659	$ 176,325	$ 62,088	$ 456,393	$ 90,591	$ 33,341	$ 5,613	$	$ 1,218,010

	One-to four-family	Multi-family	Home equity lines of credit	Commercial real estate	Construction	Commercial business	Consumer	Unallocated	Total
				At December 31, 2011 (In thousands)					
Amount of allowance for loan losses for loans deemed to be impaired	$ 211	$ 44	$ 8	$ 220	$ 3	$ 4	$	$	$ 490
Amount of allowance for loan losses for loans not deemed to be impaired	1,650	1,317	237	6,760	1,427	1,057	115		12,563
	$ 1,861	$ 1,361	$ 245	$ 6,980	$ 1,430	$ 1,061	$ 115	$	$ 13,053
Amount of allowance for loan losses for loans acquired with deteriorated credit quality included above	$ 79	$ 44	$	$	$ 3	$	$	$	$ 126
Loans deemed to be impaired	$ 5,352	$ 5,257	$ 124	$ 12,739	$ 34,265	$ 1,115	$	$	$ 58,852
Loans not deemed to be impaired	412,537	171,411	60,865	515,846	58,893	70,429	5,195		1,295,176
	$ 417,889	$ 176,668	$ 60,989	$ 528,585	$ 93,158	$ 71,544	$ 5,195	$	$ 1,354,028

The following table provides information about the Company s past due and non-accrual loans at the dates indicated.

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Loans on Non-accrual
			June 30, 2012 (In thousands)		
Real estate loans:					
Residential real estate:					
One-to four-family	$ 7,058	$ 2,381	$ 7,182	$ 16,621	$ 18,899
Multi-family		2,300	364	2,664	1,473
Home equity lines of credit	1,191	279	779	2,249	2,642
Commercial real estate	873	433	3,899	5,205	9,755
Construction	126		7,126	7,252	7,127
Total real estate loans	9,248	5,393	19,350	33,991	39,896
Commercial business loans	34	183	599	816	542
Consumer	524	113		637	
Total	$ 9,806	$ 5,689	$ 19,949	$ 35,444	$ 40,438

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Loans on Non-accrual
			December 31, 2011 (In thousands)		
Real estate loans:					
Residential real estate:					
One-to four-family	$ 5,399	$ 2,652	$ 6,204	$ 14,255	$ 15,795

Multi-family	2,350	659	436	3,445	1,605
Home equity lines of credit	1,695	552	892	3,139	1,765
Commercial real estate	3,834		3,641	7,475	11,588
Construction	475	2,511	16,316	19,302	22,434
Total real estate loans	13,753	6,374	27,489	47,616	53,187
Commercial business loans	51	5	266	322	508
Consumer	510	210		720	
Total	$ 14,314	$ 6,589	$ 27,755	$ 48,658	$ 53,695

At June 30, 2012 and December 31, 2011, the Company did not have any accruing loans past due 90 days or more. Delinquent loans at June 30, 2012 and December 31, 2011 included $3.5 million and $5.2 million of loans acquired with evidence of credit deterioration. At June 30, 2012 and December 31, 2011, non-accrual loans included $4.6 million and $6.8 million of loans acquired with evidence of credit deterioration.

The following tables provide information with respect to the Company s impaired loans at the dates and for the periods indicated.

	June 30, 2012			December 31, 2011		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
	(In thousands)					
Impaired loans without a valuation allowance:						
One-to four-family	$ 1,999	$ 2,165	$	$ 3,542	$ 4,044	$
Multi-family	4,273	4,885		4,821	4,849	
Home equity lines of credit				100	100	
Commercial real estate	10,396	10,513		7,624	7,988	
Construction	21,213	22,206		33,110	34,193	
Commercial business loans	542	646		514	617	
Total	38,423	40,415		49,711	51,791	
Impaired loans with a valuation allowance:						
One-to four-family	1,864	1,966	213	1,810	1,960	211
Multi-family	1,396	1,396	48	436	482	44
Home equity lines of credit	23	23	7	24	24	8
Commercial real estate	218	218	6	5,115	5,115	220
Construction	1,679	1,873	392	1,155	1,740	3
Commercial business loans	596	596	4	601	601	4
Total	5,776	6,072	670	9,141	9,922	490
Total impaired loans	$ 44,199	$ 46,487	$ 670	$ 58,852	$ 61,713	$ 490

	Three Months Ended June 30, 2012			Three Months Ended June 30, 2011		
	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized on Cash Basis	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized on Cash Basis
Impaired loans without a valuation allowance:						
One-to four-family	$ 2,126	$ 35	$ 25	$ 2,458	$ 53	$ 48
Multi-family	4,921	114	109	4,278	110	88
Home equity lines of credit				100	2	2
Commercial real estate	10,768	182	77	6,483	60	38
Construction	26,955	380	294	24,733	432	172
Commercial business loans	517	12	6	298	10	8
Total	45,287	723	511	38,350	667	356
Impaired loans with a valuation allowance:						
One-to four-family	1,867	25	24	1,452	24	18
Multi-family	1,398	29	29			
Home equity lines of credit	23			17		
Commercial real estate	220	4	4	4,744	109	71

Construction	1,876	61				
Commercial business loans	598	11	11			
Total	5,982	130	68	6,213	133	89
Total impaired loans	$ 51,269	$ 853	$ 579	$ 44,563	$ 800	$ 445

	Six Months Ended June 30, 2012			Six Months Ended June 30, 2011		
	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized on Cash Basis	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized on Cash Basis
Impaired loans without a valuation allowance:						
One-to four-family	$ 2,180	$ 75	$ 55	$ 2,547	$ 79	$ 75
Multi-family	5,033	220	202	4,096	183	176
Home equity lines of credit				100	4	4
Commercial real estate	11,425	389	241	6,650	120	103
Construction	28,700	923	548	22,641	822	377
Commercial business loans	516	22	16	255	20	12
Total	47,854	1,629	1,062	36,289	1,228	747
Impaired loans with a valuation allowance:						
One-to four-family	1,787	46	43	1,445	48	38
Multi-family	932	58	58			
Home equity lines of credit	23			17		
Commercial real estate	147	9	8	4,758	211	142
Construction	1,942	127				
Commercial business loans	599	23	23			
Total	5,430	263	132	6,220	259	180
Total impaired loans	$ 53,284	$ 1,892	$ 1,194	$ 42,509	$ 1,487	$ 927

At June 30, 2012, additional funds of $2.0 million are committed to be advanced in connection with impaired construction loans.

The following is a summary of troubled debt restructurings for the periods indicated.

	Three Months Ended June 30,					
	2012			2011		
	Number of Loans	Pre-Modification Balance	Post-Modification Balance	Number of Loans	Pre-Modification Balance	Post-Modification Balance
	(Dollars in thousands)					
Real estate loans:						
One-to four-family	1	$ 175	$ 175	1	$ 316	$ 316
Construction				2	2,237	2,237
Total	1	$ 175	$ 175	3	$ 2,553	$ 2,553

	Six Months Ended June 30,					
	2012			2011		
	Number of Loans	Pre-Modification Balance	Post-Modification Balance	Number of Loans	Pre-Modification Balance	Post-Modification Balance
	(Dollars in thousands)					

Real estate loans:									
One-to four-family	4	$	851	$	851	2	$	576	$	576
Commercial real estate						1		3,450		3,450
Construction						2		2,237		2,237
Total	4	$	851	$	851	5	$	6,263	$	6,263

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The following provides information on how loans were modified as TDRs for the periods indicated.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(In thousands)			
Adjusted interest rates	$ 175	$ 316	$ 851	$ 4,026
Combination of rate and maturity		2,237		2,237
Total	$ 175	$ 2,553	$ 851	$ 6,263

The Company generally places loans modified as TDRs on non-accrual status for a minimum period of six months. Loans modified as TDRs qualify for return to accrual status once they have demonstrated performance with the modified terms of the loan agreement for a minimum of six months. TDRs are reported as impaired loans with an allowance established as part of the allocated component of the allowance for loan losses when the discounted cash flows of the impaired loan is lower than the carrying value of that loan. TDRs may be removed from impairment disclosures in the year following the restructure if the borrower demonstrates compliance with the modified terms and the restructuring agreement specifies an interest rate equal to that which would be provided to a borrower with similar credit at the time of restructuring.

The following table is a summary of TDRs that defaulted in the first twelve months after restructure:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2012		2011		2012		2011	
	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment
	(Dollars in thousands)							
Real estate loans:								
One-to four-family		$	1	$ 342	2	$ 435	3	$ 812
Total		$	1	$ 342	2	$ 435	3	$ 812

Loans modified as TDRs with payment defaults are considered in the allocated component of the allowance for loan losses for each of the Company s loan portfolio segments. The Company s historical loss experience factors include charge-offs on loans modified as TDRs, if any, as adjusted for additional qualitative factors such as levels/trends in delinquent and non-performing loans.

The Company utilizes a nine grade internal loan rating system for multi-family residential, commercial real estate, construction and commercial loans as follows:

Loans rated 1, 2, 3 and 3A: Loans in these categories are considered pass rated loans with low to average risk.

Loans rated 4 and 4A: Loans in this category are considered special mention. These loans are starting to show signs of potential weakness and are being closely monitored by management.

Loans rated 5: Loans in this category are considered substandard. Generally, a loan is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligors and/or the collateral pledged. There is a distinct possibility that the Company will sustain some loss if the weakness is not corrected.

Loans rated 6: Loans in this category are considered doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, highly questionable and improbable.

Loans rated 7: Loans in this category are considered uncollectible (loss) and of such little value that their continuance as loans is not warranted.

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On an annual basis, or more often if needed, the Company formally reviews the ratings on all multi-family residential, commercial real estate, construction and commercial business loans. The Company also engages an independent third-party to review a significant portion of loans within these segments on at least an annual basis. Management uses the results of these reviews as part of its annual review process. For one-to four-family real estate loans, home equity lines of credit and consumer loans, management uses delinquency reports as the key credit indicator.

The following tables provide information with respect to the Company s risk rating at the dates indicated.

	June 30, 2012			
	Multi-family residential real estate	Commercial real estate	Construction	Commercial business
	(In thousands)			
Loans rated 1 - 4A	$ 167,923	$ 580,667	$ 143,260	$ 110,641
Loans rated 5	11,573	10,256	18,846	1,018
Loans rated 6				
Loans rated 7				
Total	$ 179,496	$ 590,923	$ 162,106	$ 111,659

	December 31, 2011			
	Multi-family residential real estate	Commercial real estate	Construction	Commercial business
	(In thousands)			
Loans rated 1 - 4A	$ 165,754	$ 516,059	$ 62,992	$ 70,650
Loans rated 5	10,914	12,526	30,166	894
Loans rated 6				
Loans rated 7				
Total	$ 176,668	$ 528,585	$ 93,158	$ 71,544

6. COMMITMENTS AND DERIVATIVES

In the normal course of business, there are outstanding commitments which are not reflected in the accompanying consolidated financial statements.

Loan Commitments

The Company is party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the accompanying consolidated balance sheets. The contract amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

The Company s exposure to credit loss in the event of nonperformance by the other party to the financial instrument for loan commitments is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments as it does for on-balance sheet instruments.

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A summary of outstanding financial instruments whose contract amounts represent credit risk is as follows:

	June 30, 2012	December 31, 2011
	(In thousands)	
Unadvanced portion of existing loans:		
Construction	$ 129,112	$ 83,493
Home equity line of credit	38,491	38,085
Other lines and letters of credit	40,295	33,603
Commitments to originate:		
One-to four-family	22,421	6,417
Commercial real estate	123,918	70,544
Construction	41,779	66,481
Commercial business loans	44,077	71,491
Other loans	1,129	4,725
Total loan commitments outstanding	$ 441,222	$ 374,839

Commitments to originate loans are agreements to lend to a customer provided there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since a portion of the commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. The Company evaluates each customer s credit worthiness on a case by case basis. The amount of collateral obtained, if deemed necessary by the Company for the extension of credit, is based upon management s credit evaluation of the borrower. Collateral held includes, but is not limited to, residential real estate and deposit accounts.

Unfunded commitments under lines of credit are commitments for possible future extensions of credit to existing customers. These lines of credit are collateralized if deemed necessary and usually do not contain a specified maturity date and may not be drawn upon to the total extent to which the Company is committed. Letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those letters of credit are primarily issued to support borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

Derivative Loan Commitments

Residential real estate loan commitments are referred to as derivative loan commitments if the loan that will result from exercise of the commitment will be held for sale upon funding. The Company enters into commitments to fund residential real estate loans at specified times in the future, with the intention that these loans will subsequently be sold in the secondary market. A residential loan commitment requires the Company to originate a loan at a specific interest rate upon the completion of various underwriting requirements. Outstanding derivative loan commitments expose the Company to the risk that the price of the loans arising from the exercise of the loan commitment might decline from the inception of the rate lock to funding of the loan due to increases in loan interest rates. If interest rates increase, the value of these commitments decreases. Conversely, if interest rates decrease, the value of these loan commitments increase. Derivative loan commitments with a notional amount of $55.5 million and $23.3 million were outstanding at June 30, 2012 and December 31, 2011, respectively. The fair value of such commitments was an asset of $776,000 and $536,000 at June 30, 2012 and December 31, 2011, respectively and is included in other assets.

Forward Loan Sale Commitments

To protect against the price risk inherent in derivative loan commitments, the Company utilizes both mandatory delivery and best efforts forward loan sale commitments to mitigate the risk of potential decreases in the values of loans that would result from the exercise of the derivative loan commitments. Under a mandatory delivery contract, the Company commits to deliver a certain principal amount of mortgage loans to an investor at a specified price on or before a specified date. If the Company fails to deliver the amount of mortgages necessary to fulfill the commitment by the specified date, it is obligated to pay the investor a pair-off fee, based then-current market prices, to compensate the investor for the shortfall. Under a best efforts contract, the Company commits to deliver an individual mortgage loan of a specified principal amount and quality to an investor and the investor commits to a price that it will purchase the loan from the Company if the loan to the underlying borrower closes. The Company generally enters into forward sale contracts on the same day it commits to lend funds to a potential borrower. The Company expects that these forward loan sale commitments will experience changes in fair value opposite to the change in fair value of derivative loan commitments. Forward loan sale commitments with a notional amount of $50.1 million and $10.8 million were outstanding at

June 30, 2012 and December 31, 2011, respectively. The fair value of such commitments was a liability of $381,000 and $28,000 at June 30, 2012 and December 31, 2011, respectively and is included in other liabilities.

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The following table presents the fair values of derivative instruments in the balance sheet.

	June 30, 2012			
	Assets		Liabilities	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
	(In thousands)			
Derivative loan commitments	Other assets	$ 776	N/A	$
Forward loan sale commitments	N/A		Other liabilities	381
Total		$ 776		$ 381

	December 31, 2011			
	Assets		Liabilities	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
	(In thousands)			
Derivative loan commitments	Other assets	$ 536	N/A	$
Forward loan sale commitments	N/A		Other liabilities	28
Total		$ 536		$ 28

The following table presents information pertaining to the Company s derivative instruments included in the consolidated statement of income:

		Amount of Gain/(Loss) For the Three Months Ended June 30,	
Derivative Instrument	Location of Gain/(Loss)	2012	2011
		(In thousands)	
Derivative loan commitments	Mortgage banking gains, net	$ 454	$ (8)
Forward loan sale commitments	Mortgage banking gains, net	(435)	(48)
Total		$ 19	$ (56)

		Amount of Gain/(Loss) For the Six Months Ended June 30,	
Derivative Instrument	Location of Gain/(Loss)	2012	2011
		(In thousands)	
Derivative loan commitments	Mortgage banking gains, net	$ 240	$ 50
Forward loan sale commitments	Mortgage banking gains, net	(353)	(20)
Total		$ (113)	$ 30

For the six months ended June 30, 2012, the Company recognized net mortgage banking gains of $1.2 million, consisting of $1.3 million in net gains on sale of loans and $113,000 in net derivative mortgage banking losses. For the six months ended June 30, 2011, the Company recognized net mortgage banking gains of $605,000, consisting of $575,000 in net gains on sale of loans and $30,000 in net derivative mortgage banking gains.

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7. FAIR VALUE OF ASSETS AND LIABILITIES

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The fair value of assets and liabilities is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company s various assets and liabilities. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the asset or liability.

The Company groups its assets and liabilities measured or disclosed at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1 Valuation is based on quoted prices in active markets for identical assets or liabilities. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 Valuation is based on 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 for substantially the full term of the assets or liabilities.

Level 3 Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using unobservable inputs to pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The following methods and assumptions were used by the Company in estimating fair value disclosures:

Cash and cash equivalents The carrying amounts of cash and short-term instruments approximate fair values, based on the short-term nature of the assets.

Certificates of deposit Fair values of certificates of deposit are estimated using discounted cash flow analyses based on current market rates for similar types of deposits.

Securities available for sale All fair value measurements are obtained from a third party pricing service and are not adjusted by management. Marketable equity securities are measured at fair value utilizing quoted market prices (Level 1). Corporate bonds, obligations of government-sponsored enterprises, municipal bonds and mortgage-backed securities are determined by pricing models that consider standard input factors such as observable market data, benchmark yields, reported trades, broker/dealer quotes, credit spreads, benchmark securities, as well as new issue data, monthly payment information, and collateral performance, among others (Level 2). Other debt securities are measured at fair value utilizing pricing models, discounted cash flow methodologies, or similar techniques that require significant management judgment or estimation (Level 3).

Federal Home Loan Bank stock The carrying value of Federal Home Loan Bank stock approximates fair value based on the redemption provisions of the Federal Home Loan Bank.

Loans held for sale The fair value is based on commitments in effect from investors or prevailing market prices.

Loans For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using market interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for non-performing loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

Deposits The fair values disclosed for non-certificate accounts, by definition, equal to the amount payable on demand at the reporting date which is their carrying amounts. Fair values for certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Borrowings The fair value is estimated using discounted cash flow analyses based on the current incremental borrowing rates in the market for similar types of borrowing arrangements.

Accrued interest The carrying amounts of accrued interest approximate fair value.

Forward loan sale commitments and derivative loan commitments Forward loan sale commitments and derivative loan commitments are based on fair values of the underlying mortgage loans and the probability of such commitments being exercised. Management judgment and estimation is required in determining these fair value measurements.

Off-balance sheet credit-related instruments Fair values for off-balance-sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties credit standing. The fair value of these instruments is considered immaterial.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis are summarized as follows:

	June 30, 2012			
	Level 1	Level 2	Level 3	Total Fair Value
		(In thousands)		
Assets				
Securities available for sale				
Debt securities:				
Corporate bonds	$	$ 150,642	$	$ 150,642
Government-sponsored enterprises		50,443		50,443
Municipal bonds		7,583		7,583
Residential mortgage-backed securities:				
Government-sponsored enterprises		22,499		22,499
Private label		3,634		3,634
Total debt securities		234,801		234,801
Marketable equity securities:				
Common stocks	49,289			49,289
Money market mutual funds	14,620			14,620
Total marketable equity securities	63,909			63,909
Total securities available for sale	63,909	234,801		298,710
Derivative loan commitments			776	776
Total assets	$ 63,909	$ 234,801	$ 776	$ 299,486
Liabilities				
Forward loan sale commitments	$	$	$ 381	$ 381
Total liabilities	$	$	$ 381	$ 381

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	December 31, 2011			
	Level 1	Level 2	Level 3	Total Fair Value
	(In thousands)			
Assets				
Securities available for sale				
Debt securities:				
Corporate bonds	$	$ 165,704	$	$ 165,704
Government-sponsored enterprises		83,195		83,195
Municipal bonds		7,574		7,574
Residential mortgage-backed securities:				
Government-sponsored enterprises		26,664		26,664
Private label		7,055		7,055
Total debt securities		290,192		290,192
Marketable equity securities:				
Common stocks	36,007			36,007
Money market mutual funds	9,031			9,031
Total marketable equity securities	45,038			45,038
Total securities available for sale	45,038	290,192		335,230
Derivative loan commitments			536	536
Total assets	$ 45,038	$ 290,192	$ 536	$ 335,766
Liabilities				
Forward loan sale commitments	$	$	$ 28	$ 28
Total liabilities	$	$	$ 28	$ 28

For the three and six months ended June 30, 2012 and 2011, there were no transfers in or out of Levels 1 and 2 and the changes in Level 3 assets and liabilities that are measured at fair value on a recurring basis are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(In thousands)			
Derivative loan commitments and forward sale commitments, net:				
Beginning balance	$ 376	$ 86	$ 508	$
Total realized and unrealized gains (losses) included net income	19	(56)	(113)	30
Ending balance	$ 395	$ 30	$ 395	$ 30
Total realized gain relating to instruments still held at period end	$ 395	$ 30	$ 395	$ 30

Assets Measured at Fair Value on a Non-recurring Basis

The Company may also be required, from time to time, to measure certain other assets on a non-recurring basis in accordance with generally accepted accounting principles. These adjustments to fair value usually result from the application of lower-of-cost-or market accounting or write-downs of individual assets.

The following tables summarize the fair value hierarchy used to determine each adjustment and the carrying value of the related individual assets. The gain/loss represents the amount of write-down, charge-off or specific reserve recorded during the periods noted on the assets held at period end. There were no liabilities measured at fair value on a non-recurring basis.

	June 30, 2012			Three Months Ended June 30, 2012 Total Gain/ (Loss)	Six Months Ended June 30, 2012 Total Gain/ (Loss)
	Level 1	Level 2	Level 3		
	(In thousands)				
Impaired loans	$	$	$ 5,106	$ (487)	$ (500)
Foreclosed real estate			3,012	(69)	(171)
	$	$	$ 8,118	$ (556)	$ (671)

	December 31, 2011			Three Months Ended June 30, 2011 Total Gain/ (Loss)	Six Months Ended June 30, 2011 Total Gain/ (Loss)
	Level 1	Level 2	Level 3		
	(In thousands)				
Impaired loans	$	$	$ 4,571	$ (125)	$ (99)
Foreclosed real estate			3,853		
	$	$	$ 8,424	$ (125)	$ (99)

Certain impaired loans were adjusted to fair value, less cost to sell, of the underlying collateral securing these loans resulting in losses. The loss is not recorded directly as an adjustment to current earnings, but rather as a component in determining the allowance for loan losses. Fair value was measured using appraised values of collateral and adjusted as necessary by management based on unobservable inputs for specific properties.

Certain properties in foreclosed real estate were adjusted to fair value using appraised values of collateral, less cost to sell, and adjusted as necessary by management based on unobservable inputs for specific properties. The loss on foreclosed assets represents adjustments in valuation recorded during the time period indicated and not for losses incurred on sales.

Summary of Fair Values of Financial Instruments

The estimated fair values, and related carrying amounts, of the Company s financial instruments are as follows. Certain financial instruments and all nonfinancial instruments are exempt from disclosure requirements. Accordingly, the aggregate fair value amounts presented herein do not represent the underlying fair value of the Company.

	June 30, 2012				
	Carrying Amount	Fair Value			
		Level 1	Level 2	Level 3	Total
	(In thousands)				
Financial assets:					
Cash and cash equivalents	$ 124,575	$ 124,575	$	$	$ 124,575
Securities available for sale	298,710	63,909	234,801		298,710
Federal Home Loan Bank stock	12,064			12,064	12,064

Loans and loans held for sale, net	1,549,308		1,592,508	1,592,508
Accrued interest receivable	6,828		6,828	6,828
Financial liabilities:				
Deposits	1,700,637		1,710,055	1,710,055
Borrowings	154,614	158,082		158,082
Accrued interest payable	808		808	808
On-balance sheet derivative financial instruments:				
Derivative loan commitments:				
Assets	776		776	776
Forward loan sale commitments:				
Liabilities	381		381	381

	December 31, 2011				
	Carrying	Fair Value			
	Amount	Level 1	Level 2	Level 3	Total
			(In thousands)		
Financial assets:					
Cash and cash equivalents	$ 156,685	$ 156,685	$	$	$ 156,685
Certificates of deposit	2,500		2,516		2,516
Securities available for sale	335,230	45,038	290,192		335,230
Federal Home Loan Bank stock	12,538			12,538	12,538
Loans and loans held for sale, net	1,345,493			1,382,972	1,382,972
Accrued interest receivable	7,282			7,282	7,282
Financial liabilities:					
Deposits	1,604,488			1,613,792	1,613,792
Borrowings	131,450		135,619		135,619
Accrued interest payable	972			972	972
On-balance sheet derivative financial instruments:					
Derivative loan commitments:					
Assets	536			536	536
Forward loan sale commitments:					
Liabilities	28			28	28

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ITEM 2. ***MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS***

Management s discussion and analysis of the financial condition and results of operations is intended to assist in understanding the financial condition and results of operations of Meridian Interstate Bancorp, Inc. The following discussion should be read in conjunction with the consolidated financial statements, notes and tables included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2011, filed with the Securities and Exchange Commission.

Forward Looking Statements

This report contains forward-looking statements that are based on assumptions and may describe future plans, strategies and expectations of the Company. These forward-looking statements are generally identified by use of the words believe, expect, intend, anticipate, estimate, proje similar expressions. The Company s ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on the operations of the Company and its subsidiaries include, but are not limited to:

- general economic conditions, either nationally or in our market area, that are worse than expected;
- inflation and changes in the interest rate environment that reduce our interest margins or reduce the fair value of financial instruments;
- increased competitive pressures among financial services companies;
- changes in consumer spending, borrowing and savings habits;
- our ability to enter new markets successfully and take advantage of growth opportunities, and the possible dilutive effect of potential acquisitions or *de novo* branches, if any;
- legislative or regulatory changes that adversely affect our business;
- adverse changes in the securities markets;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board or the Securities and Exchange Commission;
- inability of third-party providers to perform their obligations to us; and
- changes in our organization, compensation and benefit plans.

Management s ability to predict results or the effect of future plans or strategies is inherently uncertain. These factors include, but are not limited to, general economic conditions, changes in the interest rate environment, legislative or regulatory changes that may adversely affect our business, changes in accounting policies and practices, changes in competition and demand for financial services, adverse changes in the securities markets and changes in the quality or composition of the Company s loan or investment portfolios. Additional factors that may affect our results are discussed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011 filed with the Securities and Exchange Commission on March 15, 2012, under Risk Factors, which is available through the SEC s website at www.sec.gov, as updated by subsequent filings with the SEC. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Except as required by applicable law or regulation, the Company does not undertake, and

specifically disclaims any obligation, to release publicly the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of the statements or to reflect the occurrence of anticipated or unanticipated events.

Critical Accounting Policies

The Company s summary of significant accounting policies are described in Note 1 to the Consolidated Financial Statements included in the 2011 Annual Report on Form 10-K for the year ended December 31, 2011. The preparation of financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Management has identified accounting for the allowance for loan losses, the valuation of goodwill and analysis for impairment, other-than-temporary impairment of securities and the valuation of deferred tax assets and foreclosed real estate as the Company s critical accounting policies.

Comparison of Financial Condition at June 30, 2012 and December 31, 2011

Assets

Total assets increased $125.6 million, or 6.4%, to $2.100 billion at June 30, 2012 from $1.974 billion at December 31, 2011. Cash and cash equivalents decreased $32.1 million, or 20.5%, to $124.6 million at June 30, 2012 from $156.7 million at December 31, 2011. Securities available for sale decreased $36.5 million, or 10.9%, to $298.7 million at June 30, 2012 from $335.2 million at December 31, 2011. Net loans increased $196.5 million, or 14.7%, to $1.538 billion at June 30, 2012 from $1.341 billion at December 31, 2011. The net increase in loans for the six months ended June 30, 2012 was primarily due to increases of $62.3 million in commercial real estate loans, $68.9 million in construction loans and $40.1 million in commercial business loans.

Asset Quality

Credit Risk Management

Our strategy for credit risk management focuses on having well-defined credit policies and uniform underwriting criteria and providing prompt attention to potential problem loans.

When a borrower fails to make a required loan payment, we take a number of steps to have the borrower cure the delinquency and restore the loan to current status, including contacting the borrower by letter and phone at regular intervals. When the borrower is in default, we may commence collection proceedings. If a foreclosure action is instituted and the loan is not brought current, paid in full, or refinanced before the foreclosure sale, the real property securing the loan generally is sold at foreclosure. Management informs the Executive Committee monthly of the amount of loans delinquent more than 30 days. Management provides detailed information to the Board of Directors on loans 60 or more days past due and all loans in foreclosure and repossessed property that we own.

Delinquencies

Total past due loans decreased $13.2 million, or 27.2%, to $35.4 million at June 30, 2012 from $48.7 million at December 31, 2011, reflecting decreases of $7.8 million in loans 90 days or more past due and $5.4 million in loans 30 to 89 days past due. Delinquent loans at June 30, 2012 included $23.3 million of loans acquired in the Mt. Washington merger, including $8.0 million that were 30 to 59 days past due, $3.5 million that were 60 to 89 days past due and $9.8 million that were 90 days or more past due. At June 30, 2012, non-accrual loans exceed loans 90 days or more past due primarily due to loans which were placed on non-accrual status based on a determination that the ultimate collection of all principal and interest due was not expected and certain loans that remain on non-accrual status until they attain a sustained payment history of six months.

Non-performing Assets

Non-performing assets include loans that are 90 or more days past due or on non-accrual status and real estate and other loan collateral acquired through foreclosure and repossession. Loans 90 days or more past due may remain on an accrual basis if adequately collateralized and in the process of collection. At June 30, 2012, the Company did not have any accruing loans past due 90 days or more. For non-accrual loans, interest previously accrued but not collected is reversed and charged against income at the time a loan is placed on non-accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Real estate that we acquire as a result of foreclosure or by deed-in-lieu of foreclosure is classified as foreclosed real estate until it is sold. When property is acquired, it is initially recorded at the fair value less costs to sell at the date of foreclosure, establishing a new cost basis. Holding costs and declines in fair value after acquisition of the property result in charges against income.

The following table provides information with respect to our non-performing assets at the dates indicated.

	June 30, 2012	December 31, 2011
	(Dollars in thousands)	
Loans accounted for on a non-accrual basis:		
Real estate loans:		
Residential real estate:		
One-to four-family	$ 18,899	$ 15,795
Multi-family	1,473	1,605
Home equity lines of credit	2,642	1,765
Commercial real estate	9,755	11,588
Construction	7,127	22,434
Total real estate loans	39,896	53,187
Commercial business loans	542	508
Total non-accrual loans	40,438	53,695
Foreclosed assets	3,012	3,853
Total non-performing assets	$ 43,450	$ 57,548
Non-performing loans to total loans	2.60%	3.97%
Non-performing loans to total assets	1.93%	2.72%
Non-performing assets to total assets	2.07%	2.91%

Non-performing loans declined $13.3 million to $40.4 million, or 2.60% of total loans outstanding at June 30, 2012, from $53.7 million, or 3.97% of total loans outstanding at December 31, 2011. Non-performing assets declined $14.1 million to $43.5 million, or 2.07% of total assets, at June 30, 2012, from $57.5 million, or 2.91% of total assets, at December 31, 2011. Non-performing assets at June 30, 2012 included $21.3 million of assets acquired in the Mt. Washington merger, comprised of $20.0 million of non-performing loans and $1.3 million of foreclosed real estate. Interest income that would have been recorded for the six months ended June 30, 2012 had nonaccruing loans been current according to their original terms amounted to $660,000.

Troubled Debt Restructurings

In the course of resolving non-performing loans, the Bank may choose to restructure the contractual terms of certain loans, with terms modified to fit the ability of the borrower to repay in line with its current financial status. A loan is considered a troubled debt restructuring if, for reasons related to the debtor s financial difficulties, a concession is granted to the debtor that would not otherwise be considered.

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The following table summarizes the Company s troubled debt restructurings (TDRs) at the dates indicated.

	June 30, 2012	December 31, 2011
	(In thousands)	
TDRs on accrual status:		
One-to four-family	$ 1,788	$ 1,269
Multi-family	2,153	
Home equity lines of credit	23	
Construction	3,503	
Total TDRs on accrual status	7,467	1,269
TDRs on non-accrual status:		
One-to four-family	2,059	2,052
Commercial real estate	4,545	4,663
Construction	3,937	7,715
Total TDRs on non-accrual status	10,541	14,430
Total TDRs	$ 18,008	$ 15,699

The increase in one-to four-family TDRs on accrual was due to two residential loan modification and two one-to four-family TDRs that were returned to accrual status during the six months ended June 30, 2012. Modifications of one-to four-family TDRs consist of rate reductions, loan term extensions or provisions for interest-only payments for a specified period up to 12 months. The Company has generally been successful with the concessions it has offered to borrowers to date. The increase in multi-family TDRs on accrual was due to one multi-family TDR which was returned to accrual status during the second quarter of 2012. The increase in construction TDRs was due to one construction TDR which was returned to accrual status. The Company generally returns TDRs to accrual status when they have sustained payments for six months based on the restructured terms.

Potential Problem Loans

Certain loans are identified during the Company s loan review process that are currently performing in accordance with their contractual terms and we expect to receive payment in full of principal and interest, but it is deemed probable that we will be unable to collect all the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. This may result from deteriorating conditions, such as cash flows, collateral values or creditworthiness of the borrower. These loans are classified as impaired but are not accounted for on a non-accrual basis. There were no potential problem loans identified at June 30, 2012 other than those already classified as non-performing, impaired or troubled debt restructurings.

Allowance for Loan Losses

The allowance for loan losses is maintained at levels considered adequate by management to provide for probable loan losses inherent in the loan portfolio as of the consolidated balance sheet reporting dates. The allowance for loan losses is based on management s assessment of various factors affecting the loan portfolio, including portfolio composition, delinquent and non-accrual loans, national and local business conditions and loss experience and an overall evaluation of the quality of the underlying collateral.

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The following table sets forth the breakdown of the allowance for loan losses by loan category at the periods indicated:

	June 30, 2012			December 31, 2011		
	Amount	% of Allowance to Total Allowance	% of Loans in Category of Total Loans	Amount	% of Allowance to Total Allowance	% of Loans in Category of Total Loans
	(Dollars in thousands)					
Real estate loans:						
Residential real estate:						
One-to four-family	$ 2,322	14.2%	28.4%	$ 1,861	14.3%	30.9%
Multi-family	1,452	8.9	11.6	1,361	10.4	13.0
Home equity lines of credit	164	1.0	4.0	245	1.9	4.5
Commercial real estate	7,137	43.9	38.0	6,980	53.4	39.0
Construction	3,594	22.1	10.4	1,430	11.0	6.9
Total real estate loans	14,669	90.1	92.4	11,877	91.0	94.3
Commercial business loans	1,511	9.3	7.2	1,061	8.1	5.3
Consumer	91	0.6	0.4	115	0.9	0.4
Total loans	$ 16,271	100.0%	100.0%	$ 13,053	100.0%	100.0%
Allowance to non-accrual loans	40.24%			24.31%		
Allowance to total loans outstanding	1.05%			0.96%		
Net charge-offs to average loans outstanding (annualized)	0.03%			0.06%		

The Company s provision for loan losses was $2.2 million for the quarter ended June 30, 2012 compared to $486,000 for the quarter ended June 30, 2011. For the six months ended June 30, 2012, the provision for loan losses was $3.4 million compared to $828,000 for the six months ended June 30, 2011. The changes were based primarily on management s assessment of loan portfolio growth and composition changes, an ongoing evaluation of credit quality and current economic conditions. In addition, increases in the provision for loan losses were primarily due to growth in the commercial real estate, construction and commercial business loan categories for the second quarter and six months ended June 30, 2012 compared to the same periods in 2011. The allowance for loan losses was $16.3 million or 1.05% of total loans outstanding at June 30, 2012, compared to $13.1 million or 0.96% of total loans outstanding at December 31, 2011. The Company continues to assess the adequacy of its allowance for loan losses in accordance with established policies.

The allowance consists of general and allocated components. The general component relates to pools of non-impaired loans and is based on historical loss experience adjusted for qualitative factors. The allocated component relates to loans that are classified as impaired, whereby an allowance is established when the discounted cash flows, collateral value or observable market price of the impaired loan is lower than the carrying value of that loan.

The Company had impaired loans totaling $44.2 million and $58.9 million as of June 30, 2012 and December 31, 2011, respectively. At June 30, 2012, impaired loans totaling $5.8 million had a valuation allowance of $670,000. Impaired loans totaling $9.1 million had a valuation allowance of $490,000 at December 31, 2011. The Company s average investment in impaired loans was $53.3 million and $42.5 million for the six months ended June 30, 2012 and 2011, respectively.

A loan is considered impaired when, based on current information and events, it is probable that we will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Impairment is measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, we do not separately identify individual one-to four-family residential and consumer loans for impairment disclosures, unless such loans are subject to a troubled debt restructuring. The Company periodically may agree to modify the contractual terms of loans. When a loan is modified and a concession is made to a borrower experiencing financial difficulty, the modification is considered a TDR. All TDRs are initially classified as impaired.

We review residential and commercial loans for impairment based on the fair value of collateral, if collateral-dependent, or the present value of expected cash flows. Management has reviewed the collateral value for all impaired and non-accrual loans that were collateral-dependent as of June 30, 2012 and considered any probable loss in determining the allowance for loan losses.

For residential loans measured for impairment based on the collateral value, we will do the following:

- When a loan becomes seriously delinquent, generally 60 days past due, internal valuations are completed by our in-house appraiser who is a Massachusetts certified residential appraiser. We obtain third party appraisals, which are generally the basis for charge-offs when a loss is indicated, prior to the foreclosure sale. We generally are able to complete the foreclosure process within nine to 12 months from receipt of the internal valuation.

- We make adjustments to appraisals based on updated economic information, if necessary, prior to the foreclosure sale. We review current market factors to determine whether, in management s opinion, downward adjustments to the most recent appraised values may be warranted. If so, we use our best estimate to apply an estimated discount rate to the appraised values to reflect current market factors.

- Appraisals we receive are based on comparable property sales.

For commercial loans measured for impairment based on the collateral value, we will do the following:

- We obtain a third party appraisal at the time a loan is deemed to be in a workout situation and there is no indication that the loan will return to performing status, generally when the loan is 90 days or more past due. One or more updated third party appraisals are obtained prior to foreclosure depending on the foreclosure timeline. In general we order new appraisals every 180 days on loans in the process of foreclosure.

- We make downward adjustments to appraisals when conditions warrant. Adjustments are made by applying a discount to the appraised value based on occupancy, recent changes in condition to the property and certain other factors. Adjustments are also made to appraisals for construction projects involving residential properties based on recent sales of units. Losses are recognized if the appraised value less estimated costs to sell is less than our carrying value of the loan.

- Appraisals we receive are generally based on a reconciliation of comparable property sales and income capitalization approaches. For loans on construction projects involving residential properties, appraisals are generally based on a discounted cash flow analysis assuming a bulk sale to a single buyer.

Loans that are partially charged off generally remain on non-accrual status until foreclosure or such time that they are performing in accordance with the terms of the loan and have a sustained payment history of at least six months. The accrual of interest is generally discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectibility of principal or interest, even though the loan is currently performing. Loan losses are charged against the allowance when we believe the uncollectibility of a loan balance is confirmed, generally when appraised values (as adjusted values, if applicable) less estimated costs to sell, are less than the Company s carrying values.

Although we believe that we use the best information available to establish the allowance for loan losses, future adjustments to the allowance for loan losses may be necessary and our results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while we believe we have established our allowance for loan losses in conformity with generally accepted accounting principles in the United States of America, there can be no assurance that regulators, in reviewing our loan

portfolio, will not require us to increase our allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses may adversely affect our financial condition and results of operations.

Deposits

Deposits are a major source of our funds for lending and other investment purposes. Deposit inflows and outflows are significantly influenced by general interest rates and money market conditions. Our deposit base is comprised of demand, NOW, money market, regular savings and other deposits, and certificates of deposit. We consider demand, NOW, money market, and regular and other deposits to be core deposits. At June 30, 2012, core deposits were 63.4% of total deposits. Total deposits increased $96.1 million, or 6.0%, to $1.701 billion at June 30, 2012 from $1.604 billion at December 31, 2011, reflecting net growth in core deposits of $120.8 million or 12.6%, to $1.079 billion.

The following table summarizes the period end balance and the composition of deposits:

	June 30, 2012		December 31, 2011	
	Balance	Percent of Total Deposits	Balance	Percent of Total Deposits
	(Dollars in thousands)			
Demand deposits	$ 172,661	10.1%	$ 145,274	9.1%
NOW deposits	152,841	9.0	153,651	9.6
Money market deposits	519,875	30.6	445,868	27.8
Regular and other deposits	233,463	13.7	213,266	13.3
Certificates of deposit	621,797	36.6	646,429	40.2
Total	$ 1,700,637	100.0%	$ 1,604,488	100.0%

Borrowings

We use borrowings from the Federal Home Loan Bank of Boston to supplement our supply of funds for loans and investments. In addition, we also purchase federal funds from local banking institutions as an additional short-term funding source for the Bank. Total borrowings increased $23.2 million, or 17.6%, to $154.6 million at June 30, 2012 from $131.5 million at December 31, 2011, reflecting a $29.6 million increase in Federal Home Loan Bank of Boston advances partially offset by a $6.5 million decrease in short-term borrowings. At June 30, 2012 and December 31, 2011, Federal Home Loan Bank of Boston advances totaled $144.6 million and $114.9 million, respectively, with a weighted average rate of 2.05% and 2.61%, respectively. At June 30, 2012 and December 31, 2011, federal funds purchased totaled $10.1 million and $16.5 million, respectively, with a weighted average rate of 0.15% at the end of each of the periods. At June 30, 2012, we also had an available line of credit of $9.4 million with the Federal Home Loan Bank of Boston at an interest rate that adjusts daily, none of which was outstanding at that date.

Stockholders Equity

Total stockholders equity increased $8.8 million, or 4.0%, to $228.8 million at June 30, 2012, from $219.9 million at December 31, 2011. The increase for the six months ended June 30, 2012 was due primarily to $7.6 million in net income and a $1.5 million increase in accumulated other comprehensive income reflecting an increase in the fair value of available for sale securities, net of tax, partially offset by a $1.1 million increase in treasury stock resulting from the Company s repurchase of 86,304 shares. Stockholders equity to assets was 10.89% at June 30, 2012, compared to 11.14% at December 31, 2011. Book value per share increased to $10.36 at June 30, 2012 from $9.93 at December 31, 2011. Tangible book value per share increased to $9.74 at June 30, 2012 from $9.31 at December 31, 2011. Market price per share increased $1.47, or 11.8%, to $13.92 at June 30, 2012 from $12.45 at December 31, 2011. At June 30, 2012, the Company and the Bank continued to exceed all regulatory capital requirements.

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Average Balance Sheets and Related Yields and Rates

The following tables present information regarding average balances of assets and liabilities, the total dollar amounts of interest income and dividends from average interest-earning assets, the total dollar amounts of interest expense on average interest-bearing liabilities and the resulting annualized average yields and costs. The yields and costs for the periods indicated are derived by dividing income or expense by the average balances of assets or liabilities, respectively, for the periods presented. For purposes of this table, average balances have been calculated using daily average balances, and non-accrual loans are included in average balances but are not deemed material. Loan fees are included in interest income on loans but are not material.

	For the Three Months Ended June 30,					
	2012			2011		
	Average Balance	Interest	Yield/ Cost (5)	Average Balance	Interest	Yield/ Cost (5)
	(Dollars in thousands)					
Assets:						
Interest-earning assets:						
Loans (1)	$ 1,497,772	$ 18,565	4.99%	$ 1,193,195	$ 16,237	5.46%
Securities and certificates of deposits	314,363	2,307	2.95	394,273	3,160	3.21
Other interest-earning assets (2)	106,994	96	0.36	190,240	144	0.30
Total interest-earning assets	1,919,129	20,968	4.39	1,777,708	19,541	4.41
Noninterest-earning assets	124,549			127,554		
Total assets	$ 2,043,678			$ 1,905,262		
Liabilities and stockholders equity:						
Interest-bearing liabilities:						
NOW deposits	$ 145,731	162	0.45	$ 129,434	139	0.43
Money market deposits	502,438	1,058	0.85	363,043	872	0.96
Regular and other deposits	230,532	221	0.39	203,621	279	0.55
Certificates of deposit	620,740	2,376	1.54	706,260	3,326	1.89
Total interest-bearing deposits	1,499,441	3,817	1.02	1,402,358	4,616	1.32
Borrowings	140,651	756	2.16	148,454	791	2.14
Total interest-bearing liabilities	1,640,092	4,573	1.12	1,550,812	5,407	1.40
Noninterest-bearing demand deposits	162,520			119,346		
Other noninterest-bearing liabilities	15,268			14,641		
Total liabilities	1,817,880			1,684,799		
Total stockholders equity	225,798			220,463		
Total liabilities and stockholders equity	$ 2,043,678			$ 1,905,262		
Net interest-earning assets	$ 279,037			$ 226,896		
Net interest income		$ 16,395			$ 14,134	
Interest rate spread (3)			3.27%			3.01%
Net interest margin (4)			3.44%			3.19%

Average interest-earning assets to average interest-bearing liabilities		117.01%			114.63%	
Supplemental Information:						
Total deposits, including noninterest-bearing demand deposits	$ 1,661,961	$ 3,817	0.92%	$ 1,521,704	$ 4,616	1.22%
Total deposits and borrowings, including noninterest-bearing demand deposits	$ 1,802,612	$ 4,573	1.02%	$ 1,670,158	$ 5,407	1.30%

(1) Loans on non-accrual status are included in average balances.
(2) Includes Federal Home Loan Bank stock and associated dividends.
(3) Interest rate spread represents the difference between the yield on interest-earning assets and the cost of interest-bearing liabilities.
(4) Net interest margin represents net interest income divided by average interest-earning assets.
(5) Annualized.

	For the Six Months Ended June 30,					
	2012			2011		
	Average Balance	Interest	Yield/ Cost (5)	Average Balance	Interest	Yield/ Cost (5)
	(Dollars in thousands)					
Assets:						
Interest-earning assets:						
Loans (1)	$ 1,443,848	$ 36,553	5.09%	$ 1,193,679	$ 32,797	5.54%
Securities and certificates of deposits	319,031	4,875	3.07	383,668	6,517	3.43
Other interest-earning assets (2)	127,976	177	0.28	178,605	238	0.27
Total interest-earning assets	1,890,855	41,605	4.42	1,755,952	39,552	4.54
Noninterest-earning assets	128,023			125,521		
Total assets	$ 2,018,878			$ 1,881,473		
Liabilities and stockholders equity:						
Interest-bearing liabilities:						
NOW deposits	$ 143,705	326	0.46	$ 129,233	288	0.45
Money market deposits	481,276	2,018	0.84	349,978	1,739	1.00
Regular and other deposits	224,466	430	0.39	199,607	539	0.54
Certificates of deposit	632,120	5,046	1.61	702,714	6,623	1.90
Total interest-bearing deposits	1,481,567	7,820	1.06	1,381,532	9,189	1.34
Borrowings	137,640	1,539	2.25	152,281	1,680	2.22
Total interest-bearing liabilities	1,619,207	9,359	1.16	1,533,813	10,869	1.43
Noninterest-bearing demand deposits	158,064			116,294		
Other noninterest-bearing liabilities	16,109			12,076		
Total liabilities	1,793,380			1,662,183		
Total stockholders equity	225,498			219,290		
Total liabilities and stockholders equity	$ 2,018,878			$ 1,881,473		
Net interest-earning assets	$ 271,648			$ 222,139		
Net interest income		$ 32,246			$ 28,683	
Interest rate spread (3)			3.26%			3.11%
Net interest margin (4)			3.43%			3.29%
Average interest-earning assets to average interest-bearing liabilities		116.78%			114.48%	
Supplemental Information:						
Total deposits, including noninterest-bearing demand deposits	$ 1,639,631	$ 7,820	0.96%	$ 1,497,826	$ 9,189	1.24%
Total deposits and borrowings, including noninterest-bearing demand deposits	$ 1,777,271	$ 9,359	1.06%	$ 1,650,107	$ 10,869	1.33%

(1) Loans on non-accrual status are included in average balances.
(2) Includes Federal Home Loan Bank stock and associated dividends.

(3) Interest rate spread represents the difference between the yield on interest-earning assets and the cost of interest-bearing liabilities.
(4) Net interest margin represents net interest income divided by average interest-earning assets.
(5) Annualized.

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Rate/Volume Analysis

The following table sets forth the effects of changing rates and volumes on our net interest income. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). The net column represents the sum of the prior columns. For purposes of this table, changes attributable to changes in both rate and volume that cannot be segregated have been allocated proportionally based on the changes due to rate and the changes due to volume.

	Three Months Ended June 30, 2012 Compared to 2011 Increase (Decrease)			Six Months Ended June 30, 2012 Compared to 2011 Increase (Decrease)		
	Due to			Due to		
	Volume	Rate	Total	Volume	Rate	Total
	(In thousands)					
Interest Income:						
Loans	$ 3,833	$ (1,505)	$ 2,328	$ 6,555	$ (2,799)	$ 3,756
Securities and certificates of deposits	(608)	(245)	(853)	(1,019)	(623)	(1,642)
Other interest-earning assets	(71)	23	(48)	(69)	8	(61)
Total	3,154	(1,727)	1,427	5,467	(3,414)	2,053
Interest Expense:						
Deposits	(23)	(776)	(799)	61	(1,430)	(1,369)
Borrowings	(43)	8	(35)	(159)	18	(141)
Total	(66)	(768)	(834)	(98)	(1,412)	(1,510)
Change in net interest income	$ 3,220	$ (959)	$ 2,261	$ 5,565	$ (2,002)	$ 3,563

Results of Operations for the Three and Six Months Ended June 30, 2012 and 2011

Net Income

Our primary source of income is net interest income. Net interest income is the difference between interest income, which is the income that we earn on our loans and investments, and interest expense, which is the interest that we pay on our deposits and borrowings. Changes in levels of interest rates affect our net interest income. A secondary source of income is non-interest income, which includes revenue that we receive from providing products and services. The majority of our non-interest income generally comes from customer service fees, loan fees, bank-owned life insurance, mortgage banking gains and gains on sales of securities.

The Company recorded net income of $5.4 million, or $0.25 per diluted share, for the quarter ended June 30, 2012 compared to $4.2 million, or $0.19 per diluted share, for the quarter ended June 30, 2011. Income before income tax expense increased $1.5 million to $8.1 million, the net result of increases in net interest income of $2.3 million and non-interest income of $3.3 million, partially offset by increases in the provision for loan losses of $1.7 million and non-interest expenses of $2.3 million.

During the quarter ended June 30, 2012, the Company recognized a pre-tax gain of $4.8 million on completion of the sale of its investment in Hampshire First Bank, which was 43% owned by the Company, to NBT Bancorp, Inc. (NBTB) and NBT Bank, N.A. on June 8, 2012. On an after-tax basis, this gain increased net income by $2.9 million, or $0.13 per diluted share, for the quarter and six months ended June 30, 2012. The Company received $6.6 million of cash and 547,481 NBTB shares totaling $11.1 million as proceeds from the sale.

For the six months ended June 30, 2012, net income was $7.6 million, or $0.35 per diluted share compared to $7.4 million, or $0.33 per diluted share, for the six months ended June 30, 2011. Income before income tax expense decreased $347,000 to $11.3 million, the net result of increases in the provision for loan losses of $2.6 million and non-interest expenses of $4.9 million partially offset by increases in net interest income of $3.6 million and non-interest income of $3.6 million,.

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The Company s return on average assets was 1.07% for the quarter ended June 30, 2012 compared to 0.87% for the quarter ended June 30, 2011. For the six months ended June 30, 2012, the Company s return on average assets was 0.75% compared to 0.78% for the six months ended June 30, 2011.

The Company s return on average equity was 9.65% for the quarter ended June 30, 2012 compared to 7.56% for the quarter ended June 30, 2011. For the six months ended June 30, 2012, the Company s return on average equity was 6.74% compared to 6.73% for the six months ended June 30, 2011.

Net Interest Income

Net interest income increased $2.3 million, or 16.0%, to $16.4 million for the quarter ended June 30, 2012 from $14.1 million for the quarter ended June 30, 2011. The net interest rate spread and net interest margin were 3.27% and 3.44%, respectively, for the quarter ended June 30, 2012 compared to 3.01% and 3.19%, respectively, for the quarter ended June 30, 2011. For the six months ended June 30, 2012, net interest income increased $3.6 million, or 12.4%, to $32.2 million from $28.7 million for the six months ended June 30, 2011. The net interest rate spread and net interest margin were 3.26% and 3.43%, respectively, for the six months ended June 30, 2012 compared to 3.11% and 3.29%, respectively, for the six months ended June 30, 2011. The increases in net interest income were due primarily to strong loan growth along with declines in the cost of funds for the second quarter and six months ended June 30, 2012 compared to the same periods in 2011.

The average balance of the Company s loan portfolio increased $304.6 million, or 25.5%, to $1.498 billion, which was partially offset by the decline in the yield on loans of 47 basis points to 4.99% for the quarter ended June 30, 2012 compared to the quarter ended June 30, 2011. The Company s cost of total deposits declined 30 basis points to 0.92%, which was partially offset by the increase in the average balance of total deposits of $140.3 million, or 9.2%, to $1.662 billion for the quarter ended June 30, 2012 compared to the quarter ended June 30, 2011. The Company s yield on interest-earning assets declined two basis points to 4.39% for the quarter ended June 30, 2012 compared to 4.41% for the quarter ended June 30, 2011, while the cost of funds declined 28 basis points to 1.02% for the quarter ended June 30, 2012 compared to 1.30% for the quarter ended June 30, 2011.

Provision for Loan Losses

The Company s provision for loan losses was $2.2 million for the quarter ended June 30, 2012 compared to $486,000 for the quarter ended June 30, 2011. For the six months ended June 30, 2012, the provision for loan losses was $3.4 million compared to $828,000 for the six months ended June 30, 2011. Increases in the provision for loan losses were primarily due to growth in the commercial real estate, construction and commercial business loan categories for the second quarter and six months ended June 30, 2012 compared to the same periods in 2011. The allowance for loan losses was $16.3 million or 1.05% of total loans outstanding at June 30, 2012, compared to $13.1 million or 0.96% of total loans outstanding at December 31, 2011. For further analysis of the changes in the allowance for loan losses including the provision for loans losses refer to *Management s Discussion and Analysis of Results of Operations and Financial Condition -Allowance for Loan Losses*.

Non-Interest Income

Non-interest income increased $3.3 million, or 60.8%, to $8.7 million for the quarter ended June 30, 2012 from $5.4 million for the quarter ended June 30, 2011, primarily due to the $4.8 million gain on sale of the Hampshire First Bank affiliate and an increase of $368,000 in mortgage banking gains, net, partially offset by decreases of $1.7 million in gain on sales of securities, net, and $266,000 in equity income from the Hampshire First Bank affiliate. For the six months ended June 30, 2012, non-interest income increased $3.6 million, or 40.8%, to $12.6 million from $8.9 million for the six months ended June 30, 2011, primarily due to the gain on sale of the Hampshire First Bank affiliate and an increase of $557,000 in mortgage banking gains, net, partially offset by decreases of $1.4 million in gain on sales of securities, net, and $508,000 in equity income from the Hampshire First Bank affiliate.

Non-Interest Expenses

Non-interest expenses increased $2.3 million, or 18.5%, to $14.8 million for the quarter ended June 30, 2012 from $12.5 million for the quarter ended June 30, 2011, primarily due to increases of $1.6 million in salaries and employee benefits and $730,000 in other non-interest expenses. For the six months ended June 30, 2012, non-interest expenses increased $4.9 million, or 19.7%, to $30.1 million from $25.1 million for the six months ended June 30, 2011, primarily due to increases of $3.8 million in salaries and employee benefits and $1.2 million in other non-interest expenses. The increases in non-interest expenses were primarily associated with the

new branches opened and costs associated with the expansion of residential and commercial lending capacity in the past year. The Company s efficiency ratio was 77.98% for the quarter ended June 30, 2012, excluding the gain on sale of the Hampshire First Bank affiliate, compared to 75.23% for the quarter ended June 30, 2011. For the six months ended June 30, 2012, the efficiency ratio was 79.88%, excluding the gain on sale of the Hampshire First Bank affiliate, compared to 74.31% for the six months ended June 30, 2011.

Provision for Income Taxes

The Company recorded a provision for income taxes of $2.6 million for the quarter ended June 30, 2012, reflecting an effective tax rate of 32.6%, compared to $2.4 million, or 36.4%, for the quarter ended June 30, 2011. For the six months ended June 30, 2012, the provision for income taxes was $3.7 million, reflecting an effective tax rate of 32.7%, compared to $4.3 million, or 36.7%, for the six months ended June 30, 2011. The changes in the income tax provision were primarily due to the changes in pre-tax income.

Liquidity and Capital Management

Liquidity Management

Liquidity is the ability to meet current and future financial obligations of a short-term nature. Our primary sources of funds consist of deposit inflows, loan repayments, maturities of and payments on investment securities and borrowings from the Federal Home Loan Bank of Boston. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates, economic conditions and competition.

We regularly adjust our investments in liquid assets based upon our assessment of (1) expected loan demand, (2) expected deposit flows, (3) yields available on interest-earning deposits and securities and (4) the objectives of our asset/liability management policy.

Our most liquid assets are cash and cash equivalents. The levels of these assets depend on our operating, financing, lending and investing activities during any given period. At June 30, 2012, cash and cash equivalents totaled $124.6 million. In addition, at June 30, 2012, we had $61.8 million of available borrowing capacity with the Federal Home Loan Bank of Boston, including a $9.4 million line of credit. On June 30, 2012, we had $144.6 million of advances outstanding.

Our primary investing activities are the origination of loans and the purchase of securities. Our primary financing activities consist of activity in deposit accounts and Federal Home Loan Bank advances. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors and other factors. We generally manage the pricing of our deposits to be competitive. Occasionally, we offer promotional rates on certain deposit products to attract deposits.

Capital Management

Both the Company and the Bank are subject to various regulatory capital requirements administered by the Federal Reserve Board and Federal Deposit Insurance Corporation, respectively, including a risk-based capital measure. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. At June 30, 2012, both the Company and the Bank exceeded all of their respective regulatory capital requirements.

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The Company s and the Bank s actual capital amounts and ratios follow:

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
June 30, 2012						
Total Capital (to Risk Weighted Assets):						
Company	$ 228,152	12.8%	$ 142,683	8.0%	N/A	N/A
Bank	185,953	10.6	140,149	8.0	$ 175,186	10.0%
Tier 1 Capital (to Risk Weighted Assets):						
Company	209,498	11.7	71,342	4.0	N/A	N/A
Bank	167,611	9.6	70,074	4.0	105,112	6.0
Tier 1 Capital (to Average Assets):						
Company	209,498	10.4	80,712	4.0	N/A	N/A
Bank	167,611	8.4	79,574	4.0	99,468	5.0
December 31, 2011						
Total Capital (to Risk Weighted Assets):						
Company	$ 217,156	13.7%	$ 127,244	8.0%	N/A	N/A
Bank	177,602	11.4	125,028	8.0	$ 156,285	10.0%
Tier 1 Capital (to Risk Weighted Assets):						
Company	202,219	12.7	63,622	4.0	N/A	N/A
Bank	162,661	10.4	62,514	4.0	93,771	6.0
Tier 1 Capital (to Average Assets):						
Company	202,219	10.4	77,525	4.0	N/A	N/A
Bank	162,661	8.5	76,328	4.0	95,410	5.0

We may use capital management tools such as cash dividends and common share repurchases. Pursuant to Federal Reserve Board approval conditions imposed in connection with the formation of the Company, the Company has committed (i) to seek the Federal Reserve Board s prior approval before repurchasing any equity securities from Meridian Financial Services and (ii) that any repurchases of equity securities from stockholders other than Meridian Financial Services will be at the current market price for such stock repurchases. The Company is also subject to the Federal Reserve Board s notice provisions for stock repurchases.

In August 2011, the Company s Board of Directors voted to adopt a fourth stock repurchase program of up to 10% of its outstanding common stock not held by its mutual holding company parent, or 904,224 shares of its common stock. As of June 30, 2012, the Company had repurchased 195,366 shares of its stock at an average price of $12.83 per share as included in treasury stock, or 21.6% of the shares authorized for repurchase under the Company s fourth stock repurchase program. The Company has repurchased 1,599,294 shares since December 2008.

Off-Balance Sheet Arrangements

In the normal course of operations, we engage in a variety of financial transactions that, in accordance with generally accepted accounting principles in the United States of America are not recorded in our financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers requests for funding and take the form of loan commitments and lines of credit.

For the six months ended June 30, 2012, we engaged in no off-balance sheet transactions reasonably likely to have a material effect on our financial condition, results of operations or cash flows.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk Management

Our earnings and the market value of our assets and liabilities are subject to fluctuations caused by changes in the level of interest rates. We manage the interest rate sensitivity of our interest-bearing liabilities and interest-earning assets in an effort to minimize the adverse effects of changes in the interest rate environment. Deposit accounts typically react more quickly to changes in market interest rates than mortgage loans because of the shorter maturities of deposits. As a result, sharp increases in interest rates may adversely affect our earnings while decreases in interest rates may beneficially affect our earnings. To reduce the potential volatility of our earnings, we have sought to improve the match between asset and liability maturities and rates, while maintaining an acceptable interest rate spread. Our strategy for managing interest rate risk emphasizes: originating loans with adjustable interest rates; selling the residential real estate fixed-rate loans with terms greater than 15 years that we originate; promoting core deposit products; and gradually extending the maturity of funding sources, as borrowing and term deposit rates are historically low.

We have an Asset/Liability Management Committee to coordinate all aspects of asset/liability management. The committee establishes and monitors the volume, maturities, pricing and mix of assets and funding sources with the objective of managing assets and funding sources to provide results that are consistent with liquidity, growth, risk limits and profitability goals.

Net Interest Income Simulation Analysis

We analyze our interest rate sensitivity position to manage the risk associated with interest rate movements through the use of interest income simulation. The matching of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are interest sensitive. An asset or liability is said to be interest rate sensitive within a specific time period if it will mature or reprice within that time period.

Our goal is to manage asset and liability positions to moderate the effects of interest rate fluctuations on net interest income. Interest income simulations are completed quarterly and presented to the Asset/Liability Committee and the board of directors. The simulations provide an estimate of the impact of changes in interest rates on net interest income under a range of assumptions. The numerous assumptions used in the simulation process are reviewed by the Asset/Liability Committee and the Executive Committee on a quarterly basis. Changes to these assumptions can significantly affect the results of the simulation. The simulation incorporates assumptions regarding the potential timing in the repricing of certain assets and liabilities when market rates change and the changes in spreads between different market rates. The simulation analysis incorporates management s current assessment of the risk that pricing margins will change adversely over time due to competition or other factors.

Simulation analysis is only an estimate of our interest rate risk exposure at a particular point in time. We continually review the potential effect changes in interest rates could have on the repayment of rate sensitive assets and funding requirements of rate sensitive liabilities.

The simulation uses projected repricing of assets and liabilities on the basis of contractual maturities, anticipated repayments and scheduled rate adjustments. Prepayment rates can have a significant impact on interest income simulation. Because of the large percentage of loans we hold, rising or falling interest rates have a significant impact on the prepayment speeds of our earning assets that in turn affect the rate sensitivity position. When interest rates rise, prepayments tend to slow. When interest rates fall, prepayments tend to rise. Our asset sensitivity would be reduced if prepayments slow and vice versa. While we believe such assumptions to be reasonable, there can be no assurance that assumed prepayment rates will approximate actual future mortgage-backed security and loan repayment activity.

The following table reflects changes in estimated net interest income for the Bank due to immediate non-parallel changes in interest rates at July 1, 2012 through June 30, 2013.

	Net Interest Income		
Increase (Decrease) in Market Interest Rates	**Amount**	**Change**	**Percent**
	(Dollars in thousands)		
300	$ 57,336	$ (4,732)	(7.62)%
Flat	62,068		
-50	63,087	1,019	1.64

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ITEM 4. ***CONTROLS AND PROCEDURES***

(a) *Disclosure Controls and Procedures* The Company s management, including the Company s principal executive officer and principal financial officer, have evaluated the effectiveness of the Company s disclosure controls and procedures, as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company s disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the SEC) (1) is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms and (2) is accumulated and communicated to the Company s management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

(b) *Internal Control over Financial Reporting* There have not been any changes in the Company s internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II OTHER INFORMATION

ITEM 1. *LEGAL PROCEEDINGS*

Periodically, there have been various claims and lawsuits against us, such as claims to enforce liens, condemnation proceedings on properties in which we hold security interests, claims involving the making and servicing of real property loans and other issues incident to our business. We are not a party to any pending legal proceedings that we believe would have a material adverse effect on our financial condition, results of operations or cash flows.

ITEM 1A. *RISK FACTORS*

For information regarding our risk factors, see Risk Factors, in our 2011 Annual Report on Form 10-K, filed with the SEC on March 15, 2012, which is available through the SEC s website at www.sec.gov. As of June 30, 2012, our risk factors have not changed materially from those reported in the annual report. The risks described in our annual report are not the only risks that we face. Additional risks not presently known to us, or that we currently deem immaterial, may also adversely affect our business, financial condition or results of operations.

ITEM 2. *UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS*

(a.) Not applicable.

(b.) Not applicable.

(c.) The following table sets forth information with respect to any purchase made by or on behalf of the Company during the indicated periods:

Period	(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (1)	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
April 1 - 30, 2012	2,300	$ 13.61	2,300	782,535
May 1 - 31, 2012	48,677	$ 13.36	48,677	733,858
June 1 - 30, 2012	25,000	$ 13.03	25,000	708,858
Total	75,977	$ 13.26	75,977	708,858

(1)

In August 2011, the Company s Board of Directors voted to adopt a fourth stock repurchase program of up to 10% of its outstanding common stock not held by its mutual holding company parent, or 904,224 shares of its common stock.

ITEM 3. ***DEFAULTS UPON SENIOR SECURITIES***

Not applicable.

ITEM 4. ***MINE SAFETY DISCLOSURES***

Not applicable.

ITEM 5. ***OTHER INFORMATION***

None.

ITEM 6. *EXHIBITS*

3.1	Amended and Restated Articles of Organization of Meridian Interstate Bancorp, Inc.*
3.2	Amended and Restated Bylaws of Meridian Interstate Bancorp, Inc.****
3.3	Articles of Correction of Meridian Interstate Bancorp, Inc.***
4	Form of Common Stock Certificate of Meridian Interstate Bancorp, Inc.*
10.1	Form of East Boston Savings Bank Employee Stock Ownership Plan*
10.2	Form of East Boston Savings Bank Employee Stock Ownership Plan Trust Agreement*
10.3	East Boston Savings Bank Employee Stock Ownership Plan Loan Agreement, Pledge Agreement and Promissory Note*
10.4	Form of Amended and Restated Employment Agreement*
10.5	Form of East Boston Savings Bank Employee Severance Compensation Plan*
10.6	Form of Supplemental Executive Retirement Agreements with certain directors*
10.7	[Reserved]
10.8	[Reserved]
10.9	[Reserved]
10.10	Form of Supplemental Executive Retirement Agreement with Richard J. Gavegnano filed as an exhibit to Form 10-Q filed on May 14, 2008
10.11	Form of Employment Agreement with Richard J. Gavegnano incorporated by reference to the Form 8-K filed on January 12, 2009
10.12	Form of Employment Agreement with Deborah J. Jackson incorporated by reference to the Form 8-K filed on January 22, 2009
10.13	Form of Supplemental Executive Retirement Agreement with Deborah J. Jackson incorporated by reference to the Form 8-K filed on January 22, 2009
10.14	2008 Equity Incentive Plan**
10.15	Amendment to Supplemental Executive Retirement Agreements with Certain Directors incorporated by reference to the Form 10-K/A filed on April 8, 2009
10.16	Agreement and Plan of Merger incorporated by reference to the Form 8-K filed on July 24, 2009
10.17	Employment Agreement between Edward J. Merritt and East Boston Savings Bank***
10.18	Supplemental Executive Retirement Agreement between East Boston Savings Bank and Edward J. Merritt***
10.19	Joint Beneficiary Designation Agreement between Edward J. Merritt and Mt. Washington Co-operative Bank***
10.20	First Amendment to Joint Beneficiary Designation Agreement between Edward J. Merritt and Mt. Washington Co-operative Bank***
10.21	Change in Control Agreement between Mark Abbate and East Boston Savings Bank incorporated by reference to the Form 8-K filed on December 15, 2009
21	Subsidiaries of Registrant*
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following financial statements for the quarter ended June 30, 2012, formatted in XBRL: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Changes in Stockholders Equity, (v) Consolidated Statements of Cash Flows, and (vi) the Notes to Consolidated Financial Statements, tagged as blocks of text.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

* Incorporated by reference to the Registration Statement on Form S-1 of Meridian Interstate Bancorp, Inc. (File No. 333-146373), originally filed with the Securities and Exchange Commission on September 28, 2007.

** Incorporated by reference to Appendix A to the Company s Definitive Proxy Statement for its 2008 Annual Meeting, as filed with the Securities and Exchange Commission on July 11, 2008.

*** Incorporated by reference to the Company s Annual Report on Form 10-K as filed with the Securities and Exchange Commission on March 16, 2010.

**** Incorporated by reference to the Company s Form 8-K as filed with the Securities and Exchange Commission on May 17, 2012.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

MERIDIAN INTERSTATE BANCORP, INC.
(Registrant)

Dated: August 9, 2012

/s/ Richard J. Gavegnano
Richard J. Gavegnano
Chairman and Chief Executive Officer
(Principal Executive Officer)

Dated: August 9, 2012

/s/ Mark L. Abbate
Mark L. Abbate
Senior Vice President, Treasurer and Chief Financial Officer
(Principal Financial and Accounting Officer)