FARMERS NATIONAL BANC CORP /OH/
Form 10-Q
October 29, 2010

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
Quarterly Report Under Section 13 or 15(d) of the
Securities Exchange Act of 1934
For the Quarterly period ended September 30, 2010
Commission file number 0-12055
FARMERS NATIONAL BANC CORP.
(Exact name of registrant as specified in its charter)

OHIO	34-1371693
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No)
20 South Broad Street Canfield, OH	44406
(Address of principal executive offices)	(Zip Code)

(330) 533-3341
(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 (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 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 o No o

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o	Smaller reporting company o

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

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

Class	Outstanding at October 28, 2010
Common Stock, No Par Value	13,609,707 shares

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CONSOLIDATED BALANCE SHEETS
FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES
(Unaudited)

	(In Thousands of Dollars)	
	September 30, 2010	**December 31, 2009**
ASSETS		
Cash and due from banks	$ 20,936	$ 25,713
Federal funds sold	49,113	25,447
TOTAL CASH AND CASH EQUIVALENTS	70,049	51,160
Securities available for sale	345,298	309,368
Loans	607,649	609,395
Less allowance for loan losses	7,785	7,400
NET LOANS	599,864	601,995
Premises and equipment, net	14,138	14,193
Bank owned life insurance	11,823	11,438
Goodwill	3,709	3,709
Other intangibles	3,356	3,791
Other assets	16,077	19,154
TOTAL ASSETS	$ 1,064,314	$ 1,014,808
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits:		
Noninterest-bearing	$ 73,220	$ 68,420
Interest-bearing	687,805	709,132
TOTAL DEPOSITS	761,025	777,552
Short-term borrowings	174,999	125,912
Long-term borrowings	24,957	27,169
Other liabilities	12,232	3,547
TOTAL LIABILITIES	973,213	934,180
Commitments and contingent liabilities		

Stockholders Equity:		
Common Stock Authorized 25,000,000 shares; issued 15,662,843 in 2010 and 15,572,703 in 2009	96,014	95,650
Retained earnings	11,654	7,137
Accumulated other comprehensive income (loss)	8,936	3,344
Treasury stock, at cost; 2,053,136 shares in 2010 and 2,053,098 in 2009	(25,503)	(25,503)
TOTAL STOCKHOLDERS EQUITY	91,101	80,628
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 1,064,314	$ 1,014,808

See accompanying notes

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CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES
(Unaudited)

	(In Thousands except Per Share Data)			
	For the Three Months Ended		For the Nine Months Ended	
	Sept. 30, 2010	**Sept. 30, 2009**	**Sept. 30, 2010**	**Sept. 30, 2009**
INTEREST AND DIVIDEND INCOME				
Loans, including fees	$ 9,329	$ 9,610	$ 27,753	$ 28,003
Taxable securities	2,183	2,336	6,685	6,916
Tax exempt securities	584	632	1,759	1,831
Dividends	45	60	145	197
Federal funds sold	19	11	43	25
TOTAL INTEREST AND DIVIDEND INCOME	12,160	12,649	36,385	36,972
INTEREST EXPENSE				
Deposits	2,068	3,218	7,233	9,640
Short-term borrowings	210	463	729	1,435
Long-term borrowings	267	497	818	1,515
TOTAL INTEREST EXPENSE	2,545	4,178	8,780	12,590
NET INTEREST INCOME	9,615	8,471	27,605	24,382
Provision for loan losses	1,500	1,550	5,878	3,050
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	8,115	6,921	21,727	21,332
NONINTEREST INCOME				
Service charges on deposit accounts	556	768	1,531	2,020
Bank owned life insurance income	128	127	385	383
Trust income	1,254	1,248	3,683	2,251
Security gains (losses)	1,161	(2)	1,158	507
Impairment of equity securities	0	0	0	(74)
Insurance agency commissions	32	38	204	38
Investment commissions	132	100	372	244
Other operating income	434	330	1,421	1,001
TOTAL NONINTEREST INCOME	3,697	2,609	8,754	6,370
NONINTEREST EXPENSES				
Salaries and employee benefits	4,209	4,204	12,285	11,302
Occupancy and equipment	925	857	2,742	2,524

State and local taxes	224	238	680	689
Professional fees	379	252	1,069	695
Advertising	199	153	476	408
FDIC insurance	340	312	960	1,240
Merger related costs	0	0	0	453
Intangible amortization	145	150	435	298
Core processing charges	266	18	742	50
Other operating expenses	1,230	1,491	3,705	4,075
TOTAL NONINTEREST EXPENSES	7,917	7,675	23,094	21,734
INCOME BEFORE INCOME TAXES	3,895	1,855	7,387	5,968
INCOME TAXES	1,041	299	1,652	1,071
NET INCOME	$ 2,854	$ 1,556	$ 5,735	$ 4,897
OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX:				
Change in net unrealized gains (losses) on securities, net of reclassifications	1,537	3,216	5,592	3,064
COMPREHENSIVE INCOME (LOSS)	$ 4,391	$ 4,772	$ 11,327	$ 7,961
NET INCOME PER SHARE basic and diluted	$ 0.21	$ 0.12	$ 0.42	$ 0.37
DIVIDENDS PER SHARE	$ 0.03	$ 0.06	$ 0.09	$ 0.30

See accompanying notes

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CONSOLIDATED STATEMENTS OF CASH FLOWS
FARMERS NATIONAL BANC CORP. AND SUBSIDIARIES
(Unaudited)

	(In Thousands of Dollars) Nine Months Ended	
	Sept 30, 2010	**Sept 30, 2009**
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 5,735	$ 4,897
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	5,878	3,050
Depreciation and amortization	1,284	1,092
Net amortization of securities	1,727	306
Security (gains) losses	(1,158)	(507)
Impairment of securities	0	74
Loss on sale of other real estate owned	48	41
Increase in bank owned life insurance	(385)	(383)
Net change in other assets and liabilities	1,145	(918)
NET CASH FROM OPERATING ACTIVITIES	14,274	7,652
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities and repayments of securities available for sale	44,931	54,290
Proceeds from sales of securities available for sale	48,887	9,778
Purchases of securities available for sale	(114,231)	(106,334)
Proceeds from sale of Federal Home Loan Bank stock	0	1,414
Purchase of trust entity, net	0	(10,511)
Loan originations and payments, net	(4,101)	(61,984)
Proceeds from sale of other real estate owned	354	239
Additions to premises and equipment	(719)	(899)
NET CASH FROM INVESTING ACTIVITIES	(24,879)	(114,007)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net change in deposits	(16,527)	95,889
Net change in short-term borrowings	49,087	37,564
Repayments of Federal Home Loan Bank borrowings and other debt	(2,212)	(3,191)
Cash dividends paid	(1,218)	(3,992)
Proceeds from dividend reinvestment	364	1,188
NET CASH FROM FINANCING ACTIVITIES	29,494	127,458
NET CHANGE IN CASH AND CASH EQUIVALENTS	18,889	21,103
Beginning cash and cash equivalents	51,160	24,049
Ending cash and cash equivalents	$ 70,049	$ 45,152

Supplemental cash flow information:				
Interest paid	$	9,098	$	12,624
Income taxes paid	$	1,030	$	1,885
Supplemental noncash disclosures:				
Transfer of loans to other real estate	$	354	$	544
Security purchases not yet settled	$	7,528	$	0

Farmers National Banc Corp acquired all of the stock of Butler Wick Trust Company for $12.13 million on March 31, 2009. The assets acquired and liabilities assumed were as follows:

Fair value of assets acquired	$	12,394
Purchase price		12,125
Liabilities assumed	$	269

See accompanying notes

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Principles of Consolidation:

The consolidated financial statements include the accounts of Farmers National Banc Corp. (the Company), and its wholly-owned subsidiaries, The Farmers National Bank of Canfield (Farmers Bank), Farmers Trust Company (Farmers Trust), and Farmers National Insurance. All significant intercompany balances and transactions have been eliminated in the consolidation.

Basis of Presentation:

The unaudited condensed consolidated financial statements have been prepared in conformity with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles (U.S. GAAP) for complete financial statements. The financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s 2009 Annual Report to Shareholders included in the Company s Annual Report on Form 10-K for the year ended December 31, 2009. The interim consolidated financial statements include all adjustments (consisting of only normal recurring items) that, in the opinion of management, are necessary for a fair presentation of the financial position and results of operations for the periods presented. The results of operations for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year.

Estimates:

To prepare financial statements in conformity with U.S. GAAP, management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and future results could differ.

The allowance for loan losses, carrying amount of goodwill and fair values of financial instruments are particularly subject to change.

Segments:

The Company provides a broad range of financial services to individuals and companies in northeastern Ohio. While the Company s chief decision makers monitor the revenue streams of the various products and services, operations are managed and financial performance is primarily aggregated and reported in two lines of business, the Bank segment and the Trust segment.

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Securities:

The following table summarizes the amortized cost and fair value of the available-for-sale investment securities portfolio at September 30, 2010 and December 31, 2009 and the corresponding amounts of unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows:

(In Thousands of Dollars)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2010				
U.S. Treasury and U.S. government -sponsored entities	$ 86,508	$ 5,838	$ (6)	$ 92,340
States and political subdivisions	75,777	3,273	(66)	78,984
Mortgage-backed securities residential	147,739	4,835	(188)	152,386
Collateralized mortgage obligations	21,128	1	0	21,129
Equity securities	149	54	(15)	188
Other securities	250	21	0	271
Totals	$ 331,551	$ 14,022	$ (275)	$ 345,298

(In Thousands of Dollars)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2009				
U.S. Treasury and U.S. government -sponsored entities	$ 98,746	$ 1,424	$ (337)	$ 99,833
States and political subdivisions	62,809	1,070	(447)	63,432
Mortgage-backed securities residential	141,915	3,758	(411)	145,262
Collateralized mortgage obligations	309	9	0	318
Equity securities	149	129	(19)	259
Other securities	250	14	0	264
Totals	$ 304,178	$ 6,404	$ (1,214)	$ 309,368

Proceeds from sales of securities were $48.89 million and $9.78 million for the nine months ended September 30, 2010 and 2009, respectively. Gross gains of $1.16 million and $509 thousand were realized on these sales during the 2010 and 2009, respectively. Gross losses during the nine month periods ended September 30, 2010 and 2009 was $3 thousand and $2 thousand respectively.

Proceeds from sales of securities were $46.99 million and $250 thousand for the three months ended September 30, 2010 and 2009, respectively. Gross gains of $1.16 million were realized on these sales during the three month period ended September 30, 2010. Gross losses during the three month period ended September 30, 2009 were $2 thousand.

Included in States and political subdivisions is $7.53 million of securities which were purchased but not settled as of September 30, 2010. A corresponding obligation was included in other liabilities for the amounts due to the broker for these purchases.

The amortized cost and fair value of the debt securities portfolio are shown by expected maturity. Expected maturities may differ from contractual maturities if issuers have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage backed securities are not due at a single maturity date and are shown separately.

	September 30, 2010	
(In Thousands of Dollars)	Amortized Value	Fair Value
Maturity		
Within one year	$ 2,901	$ 2,920
One to five years	75,912	79,700
Five to ten years	48,723	52,168
Beyond ten years	34,999	36,807
Mortgage-backed and CMO securities	168,867	173,515
Total	$ 331,402	$ 345,110

	December 31, 2009	
(In Thousands of Dollars)	Amortized Value	Fair Value
Maturity		
Within one year	$ 3,538	$ 3,563
One to five years	92,162	93,357
Five to ten years	35,177	35,777
Beyond ten years	30,928	30,832
Mortgage-backed and CMO securities	142,224	145,580
Total	$ 304,029	$ 309,109

The following table summarizes the investment securities with unrealized losses at September 30, 2010 and December 31, 2009, aggregated by major security type and length of time in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or Longer		Total	
(In Thousands of Dollars)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
September 30, 2010						
Available-for-sale						
U.S. Treasury and U.S. government-sponsored entities	$ 0	$ 0	$ 325	$ (6)	$ 325	$ (6)
States and political subdivisions	0	0	885	(66)	885	(66)
Mortgage-backed securities residential	22,029	(187)	27	(1)	22,056	(188)
Equity securities	0	0	8	(15)	8	(15)
Total	$ 22,029	$ (187)	$ 1,245	$ (88)	$ 23,274	$ (275)

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(In Thousands of Dollars)	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Unrealized Losses	Total Fair Value	Total Unrealized Losses
December 31, 2009						
Available-for-sale						
U.S. Treasury and U.S. government-sponsored entities	$ 44,854	$ (330)	$ 359	$ (7)	$ 45,213	$ (337)
States and political subdivisions	13,336	(162)	3,035	(285)	16,371	(447)
Mortgage-backed securities residential	40,304	(410)	60	(1)	40,364	(411)
Equity securities	28	(3)	7	(16)	35	(19)
Total	$ 98,522	$ (905)	$ 3,461	$ (309)	$ 101,983	$ (1,214)

Other-Than-Temporary-Impairment

Management evaluates securities for other-than-temporary impairment (OTTI) at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. Investment securities are generally evaluated for OTTI under Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 320, *Investments Debt and Equity Securities*. Consideration is given to the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, whether the market decline was affected by macroeconomic conditions and whether the Company has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. In analyzing an issuer s financial condition, the Company may consider whether the securities are issued by the federal government or its agencies, or U.S. Government sponsored enterprises, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer s financial condition. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

When OTTI occurs, the amount of the OTTI recognized in earnings depends on whether an entity intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis. If an entity intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, the OTTI shall be recognized in earnings equal to the entire difference between the investment s amortized cost basis and its fair value at the balance sheet date. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment.

As of September 30, 2010, the Company s security portfolio consisted of 411 securities, 19 of which were in an unrealized loss position. The majority of the unrealized losses on the Company s securities are related to its holdings of U.S. Government-sponsored entities, state and political subdivisions, and mortgage-backed securities as discussed below.

Unrealized losses on debt securities issued by U.S. Government-sponsored entities have not been recognized into income because the securities are of high credit quality, management does not have the intent to sell these securities before their anticipated recovery and the decline in fair value is largely due to fluctuations in market interest rates and not credit quality. Consequently, the fair value of such debt securities is expected to recover as the securities approach their maturity date.

Unrealized losses on debt securities at September 30, 2010 relative to obligations of state and political subdivisions have not been recognized into income. Generally these debt securities have maintained their investment grade ratings and management does not have the intent to sell these securities before their anticipated recovery, which may be at maturity.

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All of the Company s holdings of mortgage-backed securities were issued by U.S. Government sponsored enterprises. Unrealized losses on mortgage-backed securities have not been recognized into income. Because the decline in fair value is attributable to changes in interest rates and illiquidity, and not credit quality, and because the Company does not have the intent to sell these mortgage-backed securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Company does not consider these securities to be OTTI.

Loans:

Loan balances were as follows:

(In Thousands of Dollars)	September 30, 2010	December 31, 2009
Residential real estate	$ 181,215	$ 180,877
Commercial real estate	209,654	215,917
Consumer	136,222	136,708
Commercial	80,558	75,893
Subtotal	607,649	609,395
Allowance for loan losses	(7,785)	(7,400)
Net loans	$ 599,864	$ 601,995

Activity in the allowance for loan losses was as follows:

	Three months ended September 30,		Nine months ended September 30,	
(In Thousands of Dollars)	2010	2009	2010	2009
Balance at beginning of period	$ 8,255	$ 6,640	$ 7,400	$ 5,553
Provision for loan losses	1,500	1,550	5,878	3,050
Recoveries	152	114	424	492
Loans charged off	(2,122)	(1,094)	(5,917)	(1,885)
Balance at end of period	$ 7,785	$ 7,210	$ 7,785	$ 7,210

Individually impaired loans were as follows:

(In Thousands of Dollars)	September 30, 2010	December 31, 2009
Loans with no allocated allowance for loan losses	$ 2,911	$ 425
Loans with allocated allowance for loan losses	4,108	13,071
	$ 7,019	$ 13,496
Amount of the allowance for loan losses allocated	$ 243	$ 2,058

Impaired loans decreased during the first nine months of 2010 due to loan charge-offs, partial payoffs and the sale of collateral associated with the impaired loans.

Included in the $7.02 million disclosed above at September 30, 2010 are $3.00 million of loans that have terms that have been modified under troubled debt restructuring. The Company has allocated $40 thousand of specific reserves

to those loans at September 30, 2010. At December 31, 2009, $5.44 million of loans had terms that have been modified were classified as troubled debt restructurings and were included in the $13.50 million of individually impaired loans. The Company has allocated $333 thousand of specific reserves to those loans at December 31, 2009. Interest income recognized during impairment for the periods was immaterial.

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Nonperforming loans were as follows:

(In Thousands of Dollars)	September 30, 2010	December 31, 2009
Nonaccrual loans:		
Residential real estate	$ 4,719	$ 2,281
Commercial real estate	3,610	5,677
Consumer	151	172
Commercial	411	1,504
Total Nonaccrual Loans	8,891	9,634
Loans past due over 90 days still on accrual	316	469
Total nonperforming loans	$ 9,207	$ 10,103
Other real estate owned	326	374
Total nonperforming assets	$ 9,533	$ 10,477
Percentage of nonperforming loans to gross loans	1.52%	1.66%
Percentage of nonperforming assets to total assets	.90%	1.03%
Loans delinquent 30-90 days	5,888	9,212
Percentage of loans delinquent 30-90 days to total loans	.97%	1.51%

Earnings Per Share:

The computation of basic and diluted earnings per share is shown in the following table:

(In Thousands, except Share and Per Share Data)	Three months ended September 30, 2010	Three months ended September 30, 2009	Nine months ended September 30, 2010	Nine months ended September 30, 2009
Basic EPS computation				
Numerator Net income	$ 2,854	$ 1,556	$ 5,735	$ 4,897
Denominator Weighted average shares outstanding	13,577,228	13,415,896	13,548,105	13,329,621
Basic earnings per share	$ .21	$ .12	$ .42	$ .37
Diluted EPS computation				
Numerator Net income	$ 2,854	$ 1,556	$ 5,735	$ 4,897
Denominator Weighted average shares outstanding for basic earnings per share	13,577,228	13,415,896	13,548,105	13,329,621
Effect of Stock Options	0	0	0	0
Weighted averages shares for diluted earnings per share	13,577,228	13,415,896	13,548,105	13,329,621
Diluted earnings per share	$ .21	$ .12	$ .42	$ .37

Stock options for 30,000 and 37,000 shares were not considered in the computing of diluted earnings per share for 2010 and 2009, respectively, because they were antidilutive.

Stock Based Compensation:

The Company s Stock Option Plan (the Plan), permitted the grant of share options to its directors, officers and employees. Under the terms of the Plan no additional shares can be issued. Option awards were granted with an exercise price equal to the market price of the Company s common shares at the date of grant, with a vesting period of 5 years and have 10-year contractual terms. At September 30, 2010 there were 30,000 outstanding options of which 27,000 were fully vested and are exercisable.

The fair value of each option award is estimated on the date of grant using a Black-Scholes model. Total compensation cost charged against income for the stock option plan for the three month and nine month period ended September 30, 2010 was not material. No related income tax benefit was recorded.

Comprehensive Income:

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income consists solely of the change in unrealized gains and losses on securities available for sale, net of reclassification for gains recognized in income.

Recent Accounting Pronouncements

In June 2009, the FASB issued SFAS No. 166*, Accounting for Transfers of Financial Assets, an Amendment of FASB Statement No. 140,* which is now codified under ASC 810, *Consolidation*. The new accounting requirement amends previous guidance relating to the transfers of financial assets and eliminates the concept of a qualifying special-purpose entity. ASC 810 must be applied as of the beginning of each reporting entity s first annual reporting period that began after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. ASC 810 must be applied to transfers occurring on or after the effective date. Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special-purpose entities should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance. Additionally, the disclosure provisions of ASC 810 were also amended and apply to transfers that occurred both before and after the effective date of ASC 810. The adoption of ASC 810 did not have a material effect on the Company s consolidated financial statements.

In June 2009, the FASB issued SFAS No. 167, *Amendments to FASB Interpretation No. 46(R),* now codified in ASC 810, which amended guidance for consolidation of variable interest entities by replacing the quantitative-based risks and rewards calculation for determining which enterprise, if any, has a controlling financial interest in a variable interest entity with an approach focused on identifying which enterprise has the power to direct the activities of a variable interest entity that most significantly impact the entity s economic performance and has (1) the obligation to absorb losses of the entity or (2) the right to receive benefits from the entity. This statement requires additional disclosures about an enterprise s involvement in variable interest entities. This statement became effective as of the beginning of each reporting entity s first annual reporting period that began after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. The adoption of the accounting guidance did not have an impact on the Company s consolidated financial statements.

In January 2010, FASB issued Accounting Standards Update (ASU) No. 2010-06, *Fair Value Measurements and Disclosures* (ASC 820) *Improving Disclosures About Fair Value Measurements*. The ASU requires new disclosures regarding significant transfers in and out of Level 1 and 2 fair value measurements and the reasons for the transfers. This ASU also requires that a reporting entity should present separately information about purchases, sales, issuances and settlements, on a gross basis rather than a net basis for activity in Level 3 fair value measurements using significant unobservable inputs. It also clarifies existing disclosures on the level of disaggregation, in that the reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities, and that a reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements for Level 2 and 3. The new disclosures and clarifications of existing disclosures for ASC 820 became effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The adoption of ASC 820 did not have a

material effect on the Company s consolidated financial statements.

In July 2010, FASB issued ASU No. 2010-20, Receivables (Topic 310): *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses.* ASU 2010-20 is intended to provide additional information to assist financial statement users in assessing an entity s credit risk exposures and evaluating the adequacy of its allowance for credit losses. The disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The amendments in ASU 2010-20 encourage, but do not require, comparative disclosures for earlier reporting periods that ended before initial adoption. However, an entity should provide comparative disclosures for those reporting periods ending after initial adoption. The Company is currently evaluating the impact the adoption of this guidance will have on the Company s financial position or results of operations.

Fair Value

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

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

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

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

The Company used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

Investment Securities: The fair values for investment securities are determined by quoted market prices, if available (Level 1). For securities where quoted prices are not available, fair values are calculated based on market prices of similar securities (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3).

Impaired Loans: The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

Other Real Estate Owned: Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate owned (OREO) are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

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Assets and Liabilities Measured on a Recurring Basis

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

		Fair Value Measurements at September 30, 2010 Using:		
(In Thousands of Dollars)	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets				
Investment securities available-for sale				
U.S. Treasury and U.S. Government sponsored entities	$ 92,340	$ 0	$ 92,340	$ 0
States and political subdivisions	78,984	0	78,984	0
Mortgage-backed securities-residential	152,386	0	152,374	12
Collateralized mortgage obligations	21,129	0	21,129	0
Equity securities	188	188	0	0
Other securities	271	0	271	0
Total investment securities	$ 345,298	$ 188	$ 345,098	$ 12

		Fair Value Measurements at December 31, 2009 Using:		
(In Thousands of Dollars)	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets				
Investment securities available-for sale				
U.S. Treasury and U.S. Government sponsored entities	$ 99,833	$ 0	$ 99,833	$ 0
States and political subdivisions	63,432	0	63,432	0
Mortgage-backed securities-residential	145,262	0	145,249	13
Collateralized mortgage obligations	318	0	318	0
Equity securities	259	259	0	0
Other securities	264	0	264	0
Total investment securities	$ 309,368	$ 259	$ 309,096	$ 13

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The table below presents a reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis:

	Investment Securities Available-for-sale (Level 3)	
	Three months ended Sept. 30, 2010	Nine months ended Sept. 30, 2010
Beginning balance	$ 13	$ 13
Total unrealized gains or losses:		
Included in other comprehensive income	0	0
Purchases, sales, issuances and settlements, net	(1)	(1)
Transfer in and/or out	0	0
Ending balance	$ 12	$ 12

Assets and Liabilities Measured on a Non-Recurring Basis

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

	Fair Value Measurements at September 30, 2010 Using:		
(In Thousands of Dollars)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:			
Impaired loans	0	0	2,084

	Fair Value Measurements at December 31, 2009 Using:		
(In Thousands of Dollars)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:			
Impaired loans	0	0	5,904

The following represent impairment charges recognized during the period:

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a carrying amount of $2.29 million with a valuation allowance of $203 thousand, resulting in an additional provision for loan loss of $180 thousand and $2.48 million for the three and nine month periods ending September 30, 2010. At December 31, 2009, impaired loans had a carrying amount of $7.63 million, net of a valuation allowance of $1.73 million, resulting in an additional provision for loan losses of $1.50 million for the year ending December 31, 2009.

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The carrying amounts and estimated fair values of financial instruments, at September 30, 2010 and December 31, 2009 are as follows:

(In Thousands of Dollars)	Carrying Amount	Fair Value
September 30, 2010		
Financial assets		
Cash and cash equivalents	$ 70,049	$ 70,049
Securities available-for-sale	345,298	345,298
Restricted stock	3,977	n/a
Loans, net	599,864	609,365
Accrued interest receivable	4,542	4,542
Financial liabilities		
Deposits	761,025	766,123
Short-term borrowings	174,999	174,999
Long-term borrowings	24,957	27,996
Accrued interest payable	837	837

(In Thousands of Dollars)	Carrying Amount	Fair Value
December 31, 2009		
Financial assets		
Cash and cash equivalents	$ 51,160	$ 51,160
Securities available-for-sale	309,368	309,368
Restricted stock	3,977	n/a
Loans, net	601,955	609,127
Accrued interest receivable	4,370	4,370
Financial liabilities		
Deposits	777,552	781,703
Short-term borrowings	125,912	125,912
Long-term borrowings	27,169	28,990
Accrued interest payable	1,155	1,155

The methods and assumptions used to estimate fair value are described as follows:

Carrying amount is the estimated fair value for cash and cash equivalents, interest bearing deposits, accrued interest receivable and payable, demand deposits, short-term debt, and variable rate loans or deposits that reprice frequently and fully. The methods for determining the fair values for securities were described previously. For fixed rate loans or deposits and for variable rate loans or deposits with infrequent repricing or repricing limits, fair value is based on discounted cash flows using current market rates applied to the estimated life and credit risk. Fair value of debt is based on current rates for similar financing. It was not practicable to determine the fair value of restricted stock due to restrictions placed on its transferability. The fair value of off-balance-sheet items is not considered material.

Segment Information

A reportable segment is determined by the products and services offered, primarily distinguished between banking and trust operations. They are also distinguished by the level of information provided to the chief operating decision makers in the Company, who use such information to review performance of various components of the business, which are then aggregated. Loans, investments, and deposits provide the revenues in the banking operation, and trust service fees provide the revenue in trust operations. All operations are domestic.

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Significant segment totals are reconciled to the financial statements as follows:

(In Thousands of Dollars)	Trust Segment	Bank Segment	Others	Consolidated Totals
September 30, 2010				
Assets				
Cash and due from banks	$ 1,128	$ 69,074	$ (153)	$ 70,049
Securities available for sale	2,647	342,530	121	345,298
Net loans	0	599,864	0	599,864
Premises and equipment, net	118	14,020	0	14,138
Goodwill and other intangibles	7,065	0	0	7,065
Other assets	452	27,325	123	27,900
Total Assets	$ 11,410	$ 1,052,813	$ 91	$ 1,064,314
Liabilities and Stockholders Equity				
Deposits, borrowings and other liabilities	$ 619	$ 972,938	$ (344)	$ 973,213
Stockholders equity	10,791	79,875	435	91,101
Total Liabilities and Stockholders Equity	$ 11,410	$ 1,052,813	$ 91	$ 1,064,314

(In Thousands of Dollars)	Trust Segment	Bank Segment	Others	Consolidated Totals
For the Three Months ended September 30, 2010				
Net interest income	$ 12	$ 9,615	$ (12)	$ 9,615
Provision for loan losses	0	1,500	0	1,500
Service fees, security gains and other noninterest income	1,332	2,378	(13)	3,697
Noninterest expense	1,179	6,562	176	7,917
Income before taxes	165	3,931	(201)	3,895
Income tax	57	1,052	(68)	1,041
Net Income	$ 108	$ 2,879	$ (133)	$ 2,854

(In Thousands of Dollars)	Trust Segment	Bank Segment	Others	Consolidated Totals
For the Three Months ended September 30, 2009				
Net interest income	$ 27	$ 8,443	$ 1	$ 8,471
Provision for loan losses	0	1,550	0	1,550
Service fees, security gains and other noninterest income	1,246	1,351	12	2,609
Noninterest expense	1,075	6,579	21	7,675

Income before taxes	198	1,665	(8)	1,855
Income tax	47	255	(3)	299
Net Income	$ 151	$ 1,410	$ (5)	$ 1,556

(In Thousands of Dollars)	**Trust Segment**	**Bank Segment**	**Others**	**Consolidated Totals**
For the Nine Months ended September 30, 2010				
Net interest income	$ 51	$ 27,586	$ (32)	$ 27,605
Provision for loan losses	0	5,878	0	5,878
Service fees, security gains and other noninterest income	3,818	4,604	332	8,754
Noninterest expense	3,436	19,273	385	23,094
Income before taxes	433	7,039	(85)	7,387
Income tax	150	1,531	(29)	1,652
Net Income	$ 283	$ 5,508	$ (56)	$ 5,735

(In Thousands of Dollars)	Trust Segment	Bank Segment	Others	Consolidated Totals
For the Nine Months ended September 30, 2009				
Net interest income	$ 47	$ 24,329	$ 6	$ 24,382
Provision for loan losses	0	3,050	0	3,050
Service fees, security gains and other noninterest income	2,249	4,192	(71)	6,370
Noninterest expense	2,098	19,131	505	21,734
Income before taxes	198	6,340	(570)	5,968
Income tax	27	1,238	(194)	1,071
Net Income	$ 171	$ 5,102	$ (376)	$ 4,897

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

Forward Looking Statements

Discussions in this report that are not statements of historical fact (including statements that include terms such as will, may, should, believe, expect, anticipate, estimate, project, intend, and plan) are forward-looki involve risks and uncertainties. Any forward-looking statement is not a guarantee of future performance and actual future results could differ materially from those contained in forward-looking information. Factors that could cause or contribute to such differences include, without limitation, risks and uncertainties detailed from time to time in the Company s filings with the Securities and Exchange Commission, including without limitation the risk factors disclosed in Item 1A, Risk Factors, of in the Company s 2009 Annual Report on Form 10-K.

Many of these factors are beyond the Company s ability to control or predict, and readers are cautioned not to put undue reliance on those forward-looking statements. The following list, which is not intended to be an all-encompassing list of risks and uncertainties affecting the Company, summarizes several factors that could cause the Company s actual results to differ materially from those anticipated or expected in these forward-looking statements:

- general economic conditions in market areas where we conduct business, which could materially impact credit quality trends;
- business conditions in the banking industry;
- the regulatory environment;
- fluctuations in interest rates;
- demand for loans in the market areas where we conduct business;
- rapidly changing technology and evolving banking industry standards;
- competitive factors, including increased competition with regional and national financial institutions;
- new service and product offerings by competitors and price pressures; and
- other like items.

Other factors not currently anticipated may also materially and adversely affect the Company s results of operations, cash flows and financial position. There can be no assurance that future results will meet expectations. While the Company believes that the forward-looking statements in this report are reasonable, the reader should not place undue reliance on any forward-looking statement. In addition, these statements speak only as of the date made. The Company does not undertake, and expressly disclaims, any obligation to update or alter any statements whether as a result of new information, future events or otherwise, except as may be required by applicable law.

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Overview

For the nine months ended September 30, 2010, the Company reported net income of $5.74 million, a 17.11% increase from the $4.90 million for the same period in 2009. For the nine months ended September 30, 2010, the Company reported net income of $0.42 per diluted share, a 13.51% increase from the $0.37 per diluted share for the same period of 2009. The Company s pre-tax, pre-provision income increased to $5.40 million for the third quarter of 2010, which represents a 58.44% increase over the $3.40 million reported for the third quarter of 2009. This increase was driven by a $1.14 million, or 13.50%, increase in net interest income, a result of the strategy to grow income producing assets. Farmers Bank also reported $1.16 million in gains on the sale of securities in the current three month period. The securities were sold to recognize market appreciation on existing holdings and to further diversify the security portfolio. Third quarter net income results also improved over the second and first quarters of 2010 because of a lower loan loss provision. Management initiated a strategy 27 months ago to earn the Company s way through the economic downturn by adding income producing assets, fee income and by enhancing the loan review process. The Company continues to see the benefits of this strategy through increased earnings power and asset quality trends that are better than many of our peers. The Company s strategies also include maintaining the appropriate levels of capital that are essential to remain a well-capitalized institution under all regulatory guidelines; continuing to deal with the number of issues the banking industry has been facing; closely monitor the efficiency ratio; and strategically manage interest rate risk and credit risk, specifically, the non-performing assets.

Pre-tax pre-provision income is a non-U.S.GAAP financial measure. A non-U.S.GAAP financial measure is a numerical measure of historical or future financial performance, financial position or cash flows that excludes or includes amounts that are required to be disclosed by generally accepted accounting principles in the United States (U.S.GAAP). The Company believes that non-U.S.GAAP financial measures provide both management and investors a more complete understanding of the underlying operational results and trends and the Company s marketplace performance. The presentation of this additional information is not meant to be considered in isolation or as a substitute for the numbers prepared in accordance with U.S.GAAP.

Reconciliation of Income Before Taxes to Pre-Tax Pre-Provision Income

	For the three months ended September 30,		For the nine months ended September 30,	
	2010	2009	2010	2009
Income before income taxes	$ 3,895	$ 1,855	$ 7,387	$ 5,968
Provision for loan losses	1,500	1,550	5,878	3,050
Pre-tax pre-provision income	$ 5,395	$ 3,405	$ 13,265	$ 9,018

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Results of Operations

The following is a comparison of selected financial ratios and other results at or for the three-month and nine-month periods ending September 30, 2010 and 2009:

	At or for the three months ended September 30,		At or for the nine months ended September 30,	
(In Thousands, except Per Share Data)	2010	2009	2010	2009
Total Assets	$ 1,064,314	$ 1,016,051	$ 1,064,314	$ 1,016,051
Net Income	$ 2,854	$ 1,556	$ 5,735	$ 4,897
Basic and Diluted Earnings Per Share	$ .21	$ .12	$ .42	$ .37
Return on Average Assets (Annualized)	1.08%	.62%	.74%	.69%
Return on Average Equity (Annualized)	12.95%	7.71%	9.08%	8.27%
Efficiency Ratio (tax equivalent basis)	61.70%	65.02%	62.50%	67.48%
Equity to Asset Ratio	8.56%	8.10%	8.56%	8.10%
Tangible Common Equity Ratio *	7.95%	7.40%	7.95%	7.40%
Dividends to Net Income	14.26%	51.74%	21.26%	81.54%
Net Loans to Assets	56.36%	59.53%	56.36%	59.53%
Loans to Deposits	79.85%	82.28%	79.85%	82.28%

* The tangible common equity ratio is calculated by dividing total common stockholders equity by total assets, after reducing both amounts by intangible assets. The tangible common equity ratio is not required by U.S.GAAP or by applicable bank regulatory requirements, but is a metric used by management to evaluate the adequacy of our capital levels. Since there is no authoritative requirement to

calculate the tangible common equity ratio, our tangible common equity ratio is not necessarily comparable to similar capital measures disclosed or used by other companies in the financial services industry. Tangible common equity and tangible assets are non U.S.GAAP financial measures and should be considered in addition to, not as a substitute for or superior to, financial measures determined in accordance with U.S.GAAP. With respect to the calculation of the actual unaudited tangible common equity ratio as of September 30, 2010, reconciliations of tangible common equity to U.S.GAAP total common stockholders equity and tangible assets

to U.S.GAAP
total assets are
set forth below:

	September 30, 2010	September 30, 2009
Reconciliation of Common Stockholders Equity to Tangible Common Equity		
Stockholders Equity	$ 91,101	$ 82,259
Less Goodwill and other intangibles	7,065	7,621
Tangible Common Equity	$ 84,036	$ 74,638

	September 30, 2010	September 30, 2009
Reconciliation of Total Assets to Tangible Assets		
Total Assets	$ 1,064,314	$ 1,016,051
Less Goodwill and other intangibles	7,065	7,621
Tangible Assets	$ 1,057,249	$ 1,008,430

With the improvement in net interest income for quarter ended September 30, 2010 over the same quarter in the prior year as well as the previous quarter, and security gains of $1.16 million, the three month period ended September 30, 2010 was the Company s best performing quarter in the past few years. The management team continues to actively monitor and address asset quality issues, and has made appropriate provisions to the allowance for loan losses accordingly. The Company s challenges for the future quarters will continue to be managing issues related to the general economic conditions and to develop relationships to grow core business lines.

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Net Interest Income. The following schedules detail the various components of net interest income for the periods indicated. All asset yields are calculated on a tax-equivalent basis where applicable. Security yields are based on amortized cost.

Average Balance Sheets and Related Yields and Rates
(Dollar Amounts in Thousands)

	Three Months Ended September 30, 2010			**Three Months Ended September 30, 2009**		
	AVERAGE BALANCE	INTEREST	RATE (1)	AVERAGE BALANCE	INTEREST	RATE (1)
EARNING ASSETS						
Loans (3) (5) (6)	**$ 602,312**	**$ 9,415**	**6.20%**	$ 592,634	$ 9,740	6.52%
Taxable securities (4)	**255,461**	**2,183**	**3.39**	224,323	2,336	4.13
Tax-exempt securities (4) (6)	**58,294**	**875**	**5.96**	62,337	946	6.02
Equity Securities (2) (6)	**4,126**	**45**	**4.33**	5,435	60	4.38
Federal funds sold	**45,257**	**19**	**0.17**	38,284	11	0.11
Total earning assets	**965,450**	**12,537**	**5.15**	923,013	13,093	5.63
NONEARNING ASSETS						
Cash and due from banks	**26,251**			22,772		
Premises and equipment	**14,288**			14,295		
Allowance for Loan Losses	**(8,249)**			(6,721)		
Unrealized gains (losses) on securities	**13,296**			5,086		
Other assets (3)	**40,156**			39,879		
Total Assets	**$ 1,051,192**			$ 998,324		
INTEREST-BEARING LIABILITIES						
Time deposits	**$ 277,856**	**$ 1,660**	**2.37%**	$ 330,262	$ 2,493	2.99%
Savings deposits	**308,781**	**388**	**0.50**	242,290	660	1.08
Demand deposits	**108,154**	**20**	**0.07**	101,865	65	0.25
Short term borrowings	**165,676**	**210**	**0.50**	132,957	463	1.38
Long term borrowings	**25,099**	**267**	**4.22**	43,592	497	4.52
Total Interest-Bearing Liabilities	**885,566**	**2,545**	**1.14**	850,966	4,178	1.95
NONINTEREST-BEARING LIABILITIES AND STOCKHOLDERS EQUITY						
Demand deposits	**74,731**			63,108		
Other Liabilities	**3,448**			4,147		

Stockholders equity	**87,447**			80,103		
Total Liabilities and Stockholders Equity	**$ 1,051,192**			$ 998,324		
Net interest income and interest rate spread		**$ 9,992**	**4.01%**		$ 8,915	3.68%
Net interest margin			**4.11%**			3.83%

(1) Rates are calculated on an annualized basis.

(2) Equity securities include restricted stock, which is included in other assets on the consolidated balance sheets.

(3) Non-accrual loans and overdraft deposits are included in other assets.

(4) Includes unamortized discounts and premiums. Average balance and yield are computed using the average historical amortized cost.

(5) Interest on loans includes fee income of $543 thousand and $540 thousand for 2010 and 2009

respectively and is reduced by amortization of $452 thousand and $413 thousand for 2010 and 2009 respectively.

(6) For 2010, adjustments of $86 thousand and $291 thousand respectively are made to tax equate income on tax exempt loans and tax exempt securities. For 2009, adjustments of $130 thousand and $314 thousand respectively are made to tax equate income on tax exempt loans and tax exempt securities. These adjustments are based on a marginal federal income tax rate of 35%, less disallowances.

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Average Balance Sheets and Related Yields and Rates
(Dollar Amounts in Thousands)

	Nine Months Ended September 30, 2010			Nine Months Ended September 30, 2009		
	AVERAGE BALANCE	INTEREST	RATE (1)	AVERAGE BALANCE	INTEREST	RATE (1)
EARNING ASSETS						
Loans (3) (5) (6)	**$ 600,861**	**$ 28,027**	**6.24%**	$ 572,573	$ 28,392	6.63%
Taxable securities (4)	**252,974**	**6,685**	**3.53**	214,619	6,916	4.34
Tax-exempt securities (4) (6)	**58,397**	**2,635**	**6.03**	60,795	2,741	6.03
Equity Securities (2) (6)	**4,126**	**145**	**4.70**	5,506	197	4.78
Federal funds sold	**35,847**	**43**	**0.16**	28,735	25	0.12
Total earning assets	**952,205**	**37,535**	**5.27**	882,228	38,271	5.80
NONEARNING ASSETS						
Cash and due from banks	**22,017**			22,767		
Premises and equipment	**14,359**			14,185		
Allowance for Loan Losses	**(7,795)**			(6,155)		
Unrealized gains (losses) on securities	**9,376**			5,231		
Other assets (3)	**40,992**			33,863		
Total Assets	**$ 1,031,154**			$ 952,119		
INTEREST-BEARING LIABILITIES						
Time deposits	**$ 299,421**	**$ 5,740**	**2.56%**	$ 307,424	$ 7,348	3.20%
Savings deposits	**295,018**	**1,388**	**0.63**	230,673	2,045	1.19
Demand deposits	**107,040**	**105**	**0.13**	100,843	247	0.33
Short term borrowings	**145,120**	**729**	**0.67**	119,965	1,435	1.60
Long term borrowings	**25,695**	**818**	**4.26**	47,011	1,515	4.31
Total Interest-Bearing Liabilities	**872,294**	**8,780**	**1.35**	805,916	12,590	2.09
NONINTEREST-BEARING LIABILITIES AND STOCKHOLDERS EQUITY						
Demand deposits	**71,057**			62,417		
Other Liabilities	**3,392**			4,628		
Stockholders equity	**84,411**			79,158		
	$ 1,031,154			$ 952,119		

Total Liabilities and Stockholders Equity				
Net interest income and interest rate spread	**$ 28,755**	**3.92%**	$ 25,681	3.71%
Net interest margin		**4.04%**		3.90%

(1) Rates are calculated on an annualized basis.

(2) Equity securities include restricted stock, which is included in other assets on the consolidated balance sheets.

(3) Non-accrual loans and overdraft deposits are included in other assets.

(4) Includes unamortized discounts and premiums. Average balance and yield are computed using the average historical amortized cost.

(5) Interest on loans includes fee income of $1.54 million and $1.83 million for 2010 and 2009 respectively and

is reduced by amortization of $1.34 million and $1.11 million for 2010 and 2009 respectively.

(6) For 2010, adjustments of $274 thousand and $876 thousand respectively are made to tax equate income on tax exempt loans and tax exempt securities. For 2009, adjustments of $389 thousand and $910 thousand respectively are made to tax equate income on tax exempt loans and tax exempt securities. These adjustments are based on a marginal federal income tax rate of 35%, less disallowances.

Taxable equivalent net interest income. Net interest income was $9.62 million for the third quarter of 2010, which compares to $8.47 million in the third quarter of 2009. This represents a 13.5% increase quarter over quarter. The annualized net interest margin to average earning assets on a fully taxable equivalent basis was 4.11% for the three months ended September 30, 2010, compared to 3.83% for the same period in the prior year. In comparing the two quarters, yields on earning assets decreased 48 basis points, while the cost of interest bearing liabilities decreased 81 basis points. This equates to an increase in our net interest margin of 28 basis points compared to the three months ended September 30, 2009.

On a year-to-date basis, net interest income improved to $27.61 million for the nine month period ended September 30, 2010, compared to $24.38 million in the same period in 2009. The annualized net interest margin to average earning assets on a fully taxable equivalent basis was 4.04% for the nine months ended September 30, 2010, compared to 3.90% for the same period in the prior year.

Noninterest Income. Noninterest income was $3.70 million for the third quarter of 2010, which is a $1.09 million, or 41.70%, improvement over results for the same quarter of 2009. Farmers Bank recognized security gains on sales of securities of $1.16 million in the three months ended September 30, 2010, compared to a $2 thousand security loss for the same period in the prior year. Service charges on deposit accounts were $556 thousand for the current quarter, a decline of 27.60% when compared to $768 thousand in the same quarter in the prior year. This decline was primarily a result of a decline in overdraft and return check fee income. The Company is uncertain of the future trend in reduced overdraft fees in light of new consumer regulatory provisions associated with these fees.

Noninterest income for the nine months ended September 30, 2010 was $8.75 million, compared to $6.37 million for the same period in 2009. The increase in noninterest income was primarily due to an increase in trust fee income of $1.43 million and an increase in gains on sales of securities of $651 thousand. Farmers Trust was purchased on March 31, 2009, therefore, the prior year s results included only six months of income compared to nine months year to date in 2010. The addition of Farmers Trust, and its growth from $684.55 million in trust assets at September 30, 2009 to $850.55 million in assets at September 30, 2010, complements our existing core retail and asset management services.

Noninterest Expense. Noninterest expenses totaled $7.92 million for the third quarter of 2010, which is $272 thousand or 3.56% higher than the $7.65 million in the previous quarter. This increase is spread amongst several expense categories. The current period s total noninterest expense of $7.92 million is $242 thousand or 3.15% higher than the $7.68 million reported for the same quarter in 2009. This increase is mainly the result of a $248 thousand increase in core processing charges in 2010. During 2009 these expenses were included in occupancy and equipment expense as Farmers Bank converted, during the fourth quarter of 2009, from an internal core processing system to a vendor operated system.

Noninterest expense for the nine months ended September 30, 2010 was $23.09 million, compared to $21.73 million for the same period in 2009, representing an increase of $1.36 million, or 6.26%. The increase resulted from the inclusion of expenses associated with Farmers Trust throughout the first nine months of 2010. Because Farmers Trust was acquired on March 31, 2009, results for the first nine months of 2009 included only six months of expenses associated with its operations. Farmers Trust s noninterest expenses were $3.44 million for the first nine months of 2010, an increase of 63.78% when compared to $2.10 million reported for the same period in 2009. In addition to the increase resulting from nine months of Farmers Trust operations, there was an increase of $374 thousand or 53.81% in professional fees for the first nine months of 2010 over the same nine month period in 2009. The majority of the increase is the result of increased legal and accounting fees due to capital raising activities.

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The following is a detail of non-interest expense line items classified between the Farmers Trust and the other entities in the Company for the three-month and nine-month periods ending September 30, 2010 and 2009. The Company purchased Farmers Trust on March 31, 2009:

	For the Three Months Ended					
	September 30, 2010			September 30, 2009		
(In Thousands of Dollars)	Trust Company	Bank and Others	Total Company	Trust Company	Bank and Others	Total Company
Noninterest expense						
Salaries and employee benefits	$ 666	$ 3,543	$ 4,209	$ 664	$ 3,540	$ 4,204
Occupancy and equipment	135	790	925	51	806	857
State and local taxes	30	194	224	15	223	238
Professional fees	15	364	379	15	237	252
Advertising	1	198	199	2	151	153
FDIC insurance	0	340	340	0	312	312
Intangible amortization	145	0	145	150	0	150
Other operating expenses	187	1,309	1,496	178	1,331	1,509
Total noninterest expense	$ 1,179	$ 6,738	$ 7,917	$ 1,075	$ 6,600	$ 7,675

	For the Nine Months Ended					
	September 30,2010			September 30, 2009		
(In Thousands of Dollars)	Trust Company	Bank and all Others	Total Company	Trust Company	Bank and all Others	Total Company
Noninterest expense						
Salaries and employee benefits	$ 1,946	$ 10,339	$ 12,285	$ 1,290	$ 10,012	$ 11,302
Occupancy and equipment	383	2,359	2,742	100	2,424	2,524
State and local taxes	89	591	680	30	659	689
Professional fees	45	1,024	1,069	30	1,118	1,148
Advertising	3	473	476	7	401	408
FDIC insurance	0	960	960	0	1,240	1,240
Intangible amortization	435	0	435	298	0	298
Other operating expenses	535	3,912	4,447	343	3,782	4,125
Total noninterest expense	$ 3,436	$ 19,658	$ 23,094	$ 2,098	$ 19,636	$ 21,734

The Company s tax equivalent efficiency ratio for the three month period ended September 30, 2010 was 61.70% compared to 65.02% in the prior year s same three month period. The improvement in the efficiency ratio was the result of the 12.08% improvement in net interest income, offset by a 3.15% increase in noninterest expense.

The Company s tax equivalent efficiency ratio for the nine month period ended September 30, 2010 was 62.50% compared to 67.48% in the prior year s same nine month period. The improvement in the efficiency ratio was the result of the 11.97% improvement in net interest income and a $1.73 million increase in noninterest income.

Income Taxes. Income tax expense totaled $1.04 million for the quarter ended September 30, 2010 and $299 thousand for the quarter ended September 30, 2009. The increase in the current quarter can be attributed to the reduction in tax exempt municipal securities and the increase in income before taxes.

Income tax expense was $1.65 million for the first nine months of 2010 and $1.07 million for the first nine months of 2009. The effective tax rate for the first nine months of 2010 was 22.36%, compared to 17.95% for the same period in 2009. The effective tax rate increase over the same period in 2009 was due to the increase in income before taxes.

Other Comprehensive Income. For the quarter ended September 30, 2010, the change in net unrealized gains on securities, net of reclassifications, resulted in an unrealized gain, net of tax, of $1.54 million, compared to an unrealized gain of $3.22 million for the same period in 2009.
For the first nine months of 2010, the change in net unrealized gains on securities, net of reclassifications, resulted in an unrealized gain, net of tax, of $5.59 million, compared to an unrealized gain of $3.06 million for the same period in 2009. Management believes the increase in fair value for the periods in 2010 over the same periods in 2009 is largely due to lower market interest rates.

Financial Condition

Securities. Securities available-for-sale increased by $35.93 million since December 31, 2009. Securities were purchased in an effort to increase returns on some of the cash available from the additional money market accounts and repurchase agreements sold during the period. The Company sold $46.99 million in market value of available-for-sale securities, resulting in a $1.16 million gain during the third quarter of 2010. Farmers Bank sold securities to recognize market appreciation on existing holdings and to further diversify the securities portfolio. There was a $8.56 million increase in the net unrealized gains on securities during the first nine months of 2010.
Loans. Gross loans decreased $1.75 million or 2.87% since December 31, 2009. The commercial loan category increased $4.67 million, coupled with small increases in the other loan categories and offset by a $6.26 million decrease in commercial real estate, accounted for the $1.75 million overall decrease in gross loans during the first nine months of 2010. On a fully tax equivalent basis, loans contributed 74.67% of total interest income for the nine months ended September 30, 2010 and 74.19% for the same period in 2009.
Allowance for Loan Losses. The following table indicates key asset quality ratios that management evaluates on an ongoing basis.

Asset Quality History
(In Thousands of Dollars)

	9/30/10	6/30/10	3/31/10	12/31/09	9/30/09
Nonperforming loans	$ 9,207	$ 9,954	$ 10,740	$ 10,103	$ 12,640
Nonperforming loans as a % of total loans	1.52%	1.62%	1.76%	1.66%	2.07%
Loans delinquent 30-90 days	5,888	5,652	6,076	9,212	4,599
Loans delinquent 30-90 days as a % of total loans	.97%	.92%	1.00%	1.51%	.75%
Allowance for loan losses	$ 7,785	$ 8,255	$ 8,220	$ 7,400	$ 7,210
Allowance for loan losses as a % of loans	1.28%	1.35%	1.35%	1.21%	1.18%
Allowance for loan losses as a % of nonperforming loans	84.56%	82.93%	76.54%	73.25%	57.04%
Annualized net charge-offs to average net loans outstanding	1.31%	1.04%	1.30%	1.86%	.66%
Non-performing assets	9,533	10,099	10,817	10,477	12,969
Non-performing assets as a % of total assets	.90%	1.00%	1.04%	1.03%	1.28%
Net charge-offs	1,970	1,565	1,958	2,810	980

For the three months ended September 30, 2010, management provided $1.50 million to the allowance for loan losses, a decrease of $100 thousand from the preceding quarter and a decrease of $50 thousand over the same three month period in the prior year. Net charge-offs for the quarter ending September 30, 2010 were $1.97 million, compared to $980 thousand for the same period ending September 30, 2009. The ratio of nonperforming loans to total loans decreased from 2.07% at September 30, 2009 to 1.52% at September 30, 2010. On September 30, 2010, the ratio of the allowance for loan losses (ALLL) to non-performing loans was 85%, compared to 83% in the preceding quarter and 57% at September 30, 2009.

As of September 30, 2010, the ALLL/total loan ratio was 1.28%, compared to 1.21% at December 31, 2009. The increase in this particular ratio was attributable to the increased level of charge-offs, which increased our historical loss factors being partially offset by lower specific allocations on impaired loans. On September 30, 2010, the ALLL balance was $7.79 million, up 5.20% from $7.40 million at December 31, 2009.

Based on the evaluation of the adequacy of the allowance for loan losses, management believes that the allowance for loan losses at September 30, 2010 to be adequate and reflects probable incurred losses in the portfolio. The provision for loan losses is based on management s judgment after taking into consideration all factors connected with the collectability of the existing loan portfolio. Management evaluates the loan portfolio in light of economic conditions, changes in the nature and volume of the loan portfolio, industry standards and other relevant factors. Specific factors considered by management in determining the amounts charged to operating expenses include previous credit loss experience, the status of past due interest and principal payments, the quality of financial information supplied by loan customers and the general condition of the industries in the community to which loans have been made.

Deposits. Total deposits decreased $16.53 million, or 2.13%, since December 31, 2009. Balances in the Company s time deposits decreased $57.59 million, or 17.72%, between December 31, 2009 and September 30, 2010. Money market deposit accounts increased $30.32 million, or 15.75%, during the nine month period ended September 30, 2010, as customers moved deposit dollars from time deposit seeking liquidity. The Company s focus is on core deposit growth and the Company will continue to price deposit rates to remain competitive within the market and to retain customers. At September 30, 2010, core deposits savings and money market accounts, time deposits less than $100,000, demand accounts and NOW accounts represented approximately 85% of total deposits.

Borrowings. Total borrowings increased $46.88 million, or 30.62%, since December 31, 2009. The increase in borrowings is due to the increase in securities sold under repurchase agreements, which increased $49.21 million, during the first nine months of 2010. The large increase in repurchase agreements is the result of an increase in public funds deposits and customers seeking liquidity.

Capital Resources. Total stockholders equity increased from $80.63 million at December 31, 2009 to $91.10 million at September 30, 2010. During the first nine months of 2010, the mark to market adjustment of securities increased accumulated other comprehensive income by $5.59 million and overall retained earnings increased by $4.52 million. The capital management function is a regular process that consists of providing capital for both the current financial position and the anticipated future growth of the Company. As of September 30, 2010 the Company s total risk-based capital ratio stood at 12.87%, and the Tier I risk-based capital ratio and Tier I leverage ratio were at 11.66% and 7.19%, respectively. Management believes that the Company and Farmers Bank meet all capital adequacy requirements to which they are subject, as of September 30, 2010.

In addition, due to the continuing growth in Farmers Bank s business and the increase in its allowance for loan losses associated with current economic conditions, senior management and the Board have determined that higher levels of capital are appropriate. The OCC concurred in the Board s view that additional capital would be beneficial in supporting its continued growth and operations. As a result, effective February 2, 2010, the OCC proposed and Farmers Bank accepted the following individual minimum capital requirements for Farmers Bank: Tier I Capital to Adjusted Total Assets of 7.20% and Total Capital to Risk-Weighted Assets of 11.00%. In conjunction with guidance provided by the OCC, we have targeted Farmers Bank to meet these individual minimum capital requirements by December 31, 2010. At September 30, 2010, the Bank s Tier I Capital to Adjusted Total Assets was 6.90% and Total Capital to Risk-Weighted Assets was 12.23%.

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Management believes that Farmers Bank will be able to attain its individual minimum capital requirements by December 31, 2010 from earnings generated through the normal course of operations. In order to provide additional capital necessary to support continued growth, the Company has filed a registration statement with the Securities and Exchange Commission in connection with a proposed public offering of its common shares. At present, the Company intends to contribute a portion of the net proceeds of the offering to Farmers Bank for general operating purposes, which may include among other things funding of loans, investment in securities, and payment of expenses. The proceeds of the offering which are not contributed to Farmers Bank will be used for general corporate purposes which may include, among others, payment of expenses, payment of dividends, and pursuing strategic opportunities which may be presented to us from time to time. We cannot assure you that such an offering will be completed or as to the timing of any such offering or the amount of proceeds ultimately received by the Company.

Critical Accounting Policies

The Company follows financial accounting and reporting policies that are in accordance with U.S. GAAP. These policies are presented in Note A to the consolidated audited financial statements in the Company s 2009 Annual Report to Shareholders included in the Company s Annual Report on Form 10-K. Critical accounting policies are those policies that require management s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. The Company has identified two accounting policies that are critical accounting policies and an understanding of these policies is necessary to understand our financial statements. These policies relate to determining the adequacy of the allowance for loan losses and other-than-temporary impairment of securities. Additional information regarding these policies is included in the notes to the aforementioned 2009 consolidated financial statements, Note A (Summary of Significant Accounting Policies), Note B (Securities), Note C (Loans), and the sections captioned Loan Portfolio and Investment Securities .
Management believes that the accounting for goodwill and other intangible assets also involves a higher degree of judgment than most other significant accounting policies. U.S.GAAP establishes standards for the amortization of acquired intangible assets and the impairment assessment of goodwill. Goodwill arising from business combinations represents the value attributable to unidentifiable intangible assets in the business acquired. The Company s goodwill relates to the value inherent in the banking industry and that value is dependent upon the ability of Farmers Trust subsidiary to provide quality, cost-effective trust services in a competitive marketplace. The goodwill value is supported by revenue that is in part driven by the volume of business transacted. A decrease in earnings resulting from a decline in the customer base or the inability to deliver cost-effective services over sustained periods can lead to impairment of goodwill that could adversely impact earnings in future periods. U.S.GAAP requires an annual evaluation of goodwill for impairment, or more frequently if events or changes in circumstances indicate that the asset might be impaired. The fair value of the goodwill, which resides on the books of the Company s subsidiary, Farmers Trust, is estimated by reviewing the past and projected operating results for the subsidiary and trust banking industry comparable information.

Liquidity

The Company maintains, in the opinion of management, liquidity sufficient to satisfy depositors requirements and meet the credit needs of customers. The Company depends on its ability to maintain its market share of deposits as well as acquiring new funds. The Company s ability to attract deposits and borrow funds depends in large measure on its profitability, capitalization and overall financial condition. The Company s objective in liquidity management is to maintain the ability to meet loan commitments, purchase securities or to repay deposits and other liabilities in accordance with their terms without an adverse impact on current or future earnings. Principal sources of liquidity for the Company include assets considered relatively liquid, such as federal funds sold, cash and due from banks, as well as cash flows from maturities and repayments of loans, and securities.

Along with its liquid assets, Farmers Bank has additional sources of liquidity available which help to insure that adequate funds are available as needed. These other sources include, but are not limited to, loan repayments, the ability to obtain deposits through the adjustment of interest rates and the purchasing of federal funds and borrowings on approved lines of credit at three major domestic banks. At September 30, 2010, these lines of credited totaled $21.00 million and Farmers Bank had not borrowed against these lines of credit. In addition, the Company had a $5.00 million revolving line of credit with a correspondent bank. The terms of this line were subsequently modified to reduce the limit to $1.10 million. The outstanding balance at September 30, 2010 was $1.10 million. Management feels that its liquidity position is adequate and continues to monitor the position on a monthly basis. As of September 30, 2010 Farmers Bank had outstanding balances with the Federal Home Loan Bank of Cincinnati (FHLB) of $24.75 million with additional borrowing capacity of approximately $70.81 million with the FHLB as well as access to the Federal Reserve Discount Window, which provides an additional source of funds. Farmers Bank views its membership in the FHLB as a solid source of liquidity.

The primary investing activities of the Company are originating loans and purchasing securities. During the first nine months of 2010, net cash used in investing activities amounted to $32.41 million, compared to $114.01 million used in investing activities for the same period in 2009. A $39.11 million increase in cash from the sale of available-for-sale securities and a $57.88 million reduction in cash used for loan originations accounted for the reduction in cash used in investing activities. The decrease in cash flow used for net loans during this year s first nine month period can be attributed to the reduced activity in the indirect loan portfolio.

The primary financing activities of the Company are obtaining deposits, repurchase agreements and other borrowings. Net cash provided by financing activities amounted to $29.49 million for the first nine months of 2010, compared to $127.46 million provided by financing activities for the same period in 2009. Most of this change is a result of the net change in deposits. Deposits provided $95.89 million of cash in 2009 and used $16.53 million of cash in 2010.

Recent Market and Regulatory Developments

In response to the current national and international economic recession, and in an effort to stabilize and strengthen the financial markets and banking industries, the United States Congress and governmental agencies have taken a number of significant actions over the past several years, including the passage of legislation and the implementation of a number of programs. The most recent of these actions was the passage into law, on July 21, 2010, of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). The Dodd-Frank Act is the most comprehensive change to banking laws and the financial regulatory environment since the Great Depression of the 1930s. The Dodd-Frank Act affects almost every aspect of the nation s financial services industry and mandates change in several key areas, including regulation and compliance, securities regulation, executive compensation, regulation of derivatives, corporate governance, and consumer protection. While these changes in the law will have a major impact on large financial institutions, even relatively smaller institutions such as the Company will be affected. For example, state consumer financial protection laws historically have been preempted in their application to national banking associations by the National Bank Act and rules and interpretations adopted by the Office of the Comptroller of the Currency (OCC) under that statute. Federal preemption of these laws will be diminished under the new regulatory regime. As Congress has authorized states to enact their own substantive protections and to allow state attorneys general to initiate civil actions to enforce federal consumer protections. In this respect, the Company will be subject to regulation by a new consumer protection bureau known as the Bureau of Consumer Financial Protection (the Bureau) under the Board of Governors of the Federal Reserve System (the Federal Reserve Board). The Bureau will consolidate enforcement currently undertaken by myriad financial regulatory agencies, and will have substantial power to define the rights of consumers and responsibilities of providers, including the Company.

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In addition, and among many other legislative changes that the Company will assess, the Company will:
(1) experience a new assessment model from the FDIC based on assets, not deposits; (2) be subject to enhanced executive compensation and corporate governance requirements; and (3) be able, for the first time (and perhaps competitively compelled) to offer interest on business transaction and other accounts.

The extent to which the Dodd-Frank Act and initiatives thereunder will succeed in addressing the credit markets or otherwise result in an improvement in the national economy is uncertain. In addition, because most aspects of this legislation will be subject to intensive agency rulemaking and subsequent public comment prior to implementation over the next six to 18 months, it is difficult to predict at this time the ultimate effect of the Dodd-Frank Act on the Company. It is likely, however, that the Company s expenses will increase as a result of new compliance requirements.

Various legislation affecting financial institutions and the financial industry will likely continue to be introduced in Congress, and such legislation may further change banking statutes and the operating environment of the Company in substantial and unpredictable ways, and could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance depending upon whether any of this potential legislation will be enacted, and if enacted, the effect that it or any implementing regulations, would have on the financial condition or results of operations of the Company or any of its subsidiaries. With the enactment of the Dodd-Frank Act, the nature and extent of future legislative and regulatory changes affecting financial institutions remains very unpredictable at this time.

To the extent that the previous information describes statutory and regulatory provisions applicable to the Company, it is qualified in its entirety by reference to the full text of those provisions or agreement. Also, such statutes, regulations and policies are continually under review by Congress and state legislatures and federal and state regulatory agencies and are subject to change at any time, particularly in the current economic and regulatory environment. Any such change in statutes, regulations or regulatory policies applicable to the Company could have a material effect on the business of the Company.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company s ability to maximize net income is dependent, in part, on management s ability to plan and control net interest income through management of the pricing and mix of assets and liabilities. Because a large portion of assets and liabilities of the Company are monetary in nature, changes in interest rates and monetary or fiscal policy affect its financial condition and can have significant impact on the net income of the Company. Additionally, the Company s balance sheet is currently liability sensitive and in the low interest rate environment that exists today, the Company s net interest margin should maintain current levels throughout the near future.

The Company considers the primary market exposure to be interest rate risk. Simulation analysis is used to monitor the Company s exposure to changes in interest rates, and the effect of the change to net interest income. The following table shows the effect on net interest income and the net present value of equity in the event of a sudden and sustained 200 basis point increase or decrease in market interest rates:

Changes In Interest Rate (basis points)	September 30, 2010 Result	December 31, 2009 Result	ALCO Guidelines
Net Interest Income Change			
+200	-3.69%	-6.41%	15.00%
-200	-2.66%	-2.09%	15.00%
Net Present Value Of Equity Change			
+200	-2.95%	-6.32%	20.00%
-200	-30.70%	-31.98%	20.00%

The results of the simulation indicate that in an environment where interest rates rise or fall 100 and 200 basis points over a 12 month period, using September 30, 2010 amounts as a base case, and considering the increase in deposit liabilities, and the volatile financial markets. It should be noted that the change in the net present value of equity exceeded policy when the simulation model assumed a sudden decrease in rates of 200 basis points (2%). This was primarily because the positive impact on the fair value of assets would not be as great as the negative impact on the fair value of certain liabilities. Specifically, because core deposits typically bear relatively low interest rates, their fair value would be negatively impacted as the rates could not be adjusted by the full extent of the sudden decrease in rates. Management does not believe that a 200 basis rate decline is realistic in the current interest rate environment. The remaining results of this analysis comply with internal limits established by the Company. A report on interest rate risk is presented to the Board of Directors and the Asset/Liability Committee on a quarterly basis. The Company has no market risk sensitive instruments held for trading purposes, nor does it hold derivative financial instruments, and does not plan to purchase these instruments in the near future.

Item 4. Controls and Procedures

Based on their evaluation, as of the end of the period covered by this quarterly report, the Corporation s Chief Executive Officer and Chief Financial Officer have concluded the Corporation s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934) are effective. There were no changes in the Company s internal controls over financial reporting (as defined in Rule 13a 15(f) under the Exchange Act) that occurred during the fiscal quarter ended September 30, 2010, that have materially affected, or are reasonably likely to materially affect, the Corporation s internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

In the opinion of management there are no outstanding legal actions that will have a material adverse effect on the Company s financial condition or results of operations.

Item 1A. Risk Factors

There are certain risks and uncertainties in the Company s business that could cause its actual results to differ materially from those anticipated. In ITEM 1A. RISK FACTORS of Part I of the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2009, the Company included a detailed discussion of its risk factors. The following information updates certain of the Company s risk factors and should be read in conjunction with the risk factors disclosed in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2009. These risk factors should be read carefully in connection with evaluating the Company s business and in connection with the forward-looking statements contained in this Quarterly Report on Form 10-Q. Any of the risks described below or in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2009 could materially adversely affect the Company s business, financial condition or future results and the actual outcome of matters as to which forward-looking statements are made. Additional risks and uncertainties not currently known to the Company or that

are currently deemed to be immaterial also may materially adversely affect the Company s business, financial condition and/or operating results.

The Company s indirect lending exposes it to increased credit risks.

A portion of the Company s current lending involves the purchase of consumer automobile installment sales contracts from automobile dealers located in Northeastern Ohio. These loans are for the purchase of new or late model used cars. The Company serves customers over a broad range of creditworthiness and the required terms and rates are reflective of those risk profiles. While these loans have higher yields than many of the Company s other loans, such loans involve significant risks in addition to normal credit risk. Potential risk elements associated with indirect lending include the limited personal contact with the borrower as a result of indirect lending through dealers, the absence of assured continued employment of the borrower, the varying general creditworthiness of the borrower, changes in the local economy and difficulty in monitoring collateral. While indirect automobile loans are secured, such loans are secured by depreciating assets and characterized by loan to value ratios that could result in the Bank not recovering the full value of an outstanding loan upon default by the borrower. Due to the economic slowdown in the Company s primary market area, the Company currently is experiencing higher delinquencies, charge-offs and repossessions of vehicles in this portfolio. If the economy continues to contract, the Company may continue to experience higher levels of delinquencies, repossessions and charge-offs.

The Company has significant exposure to risks associated with commercial and residential real estate.

A substantial portion of the Company s loan portfolio consists of commercial and residential real estate-related loans, including real estate development, construction and residential and commercial mortgage loans. Consequently, real estate-related credit risks are a significant concern for the Company. The adverse consequences from real estate-related credit risks tend to be cyclical and are often driven by national economic developments that are not controllable or entirely foreseeable by the Company or its borrowers. General difficulties in the Company s real estate markets have recently contributed to increases in the Company s non-performing loans, charge-offs, and decreases in the Company s income.

Commercial and industrial loans may expose the Company to greater financial and credit risk than other loans.

Commercial and industrial loans generally carry larger loan balances and can involve a greater degree of financial and credit risk than other loans. Any significant failure to pay on time by the Company s customers would hurt the Company s earnings. The increased financial and credit risk associated with these types of loans are a result of several factors, including the concentration of principal in a limited number of loans and borrowers, the size of loan balances, the effects of general economic conditions on income-producing properties and the increased difficulty of evaluating and monitoring these types of loans. In addition, when underwriting a commercial or industrial loan, the Company may take a security interest in commercial real estate, and, in some instances upon a default by the borrower, the Company may foreclose on and take title to the property, which may lead to potential financial risks for the Company under applicable environmental laws. If hazardous substances were discovered on any of these properties, the Company may be liable to governmental agencies or third parties for the costs of remediation of the hazard, as well as for personal injury and property damage. Many environmental laws can impose liability regardless of whether the Company knew of, or were responsible for, the contamination.

Changes in interest rates may negatively affect the Company s earnings and the value of its assets.

The Company s earnings and cash flows depend substantially upon its net interest income. Net interest income is the difference between interest income earned on interest-earnings assets, such as loans and investment securities, and interest expense paid on interest-bearing liabilities, such as deposits and borrowed funds. Interest rates are sensitive to many factors that are beyond the Company s control, including general economic conditions, competition and policies of various governmental and regulatory agencies and, in particular, the policies of the Federal Reserve Board. Changes in monetary policy, including changes in interest rates, could influence not only the interest the Company receives on loans and investment securities and the amount of interest it pays on deposits and borrowings, but such changes could also affect: (1) the Company s ability to originate loans and obtain deposits; (2) the fair value of the Company s financial assets and liabilities, including its securities portfolio; and (3) the average duration of the Company s interest-earning assets. This also includes the risk that interest-earning assets may be more responsive to changes in interest rates than interest-bearing liabilities, or vice versa (repricing risk), the risk that the individual interest rates or rates indices underlying various interest-earning assets and interest-bearing liabilities may not change in the same degree over a given time period (basis risk), and the risk of changing interest rate relationships across the spectrum of interest-earning asset and interest-bearing liability maturities (yield curve risk), including a prolonged flat or inverted yield curve environment. Any substantial, unexpected, prolonged change in market interest rates could have a material adverse affect on the Company s financial condition and results of operations.

The Company may be required to make further increases in its provisions for loan losses and to charge off additional loans in the future, which could materially adversely affect the Company.

There is no precise method of predicting loan losses. The Company can give no assurance that its allowance for loan losses is or will be sufficient to absorb actual loan losses. The Company maintains an allowance for loan losses, which is a reserve established through a provision for loan losses charged to expense, that represents management s best estimate of probable incurred losses within the existing portfolio of loans. The level of the allowance reflects management s evaluation of, among other factors, the status of specific impaired loans, trends in historical loss experience, delinquency trends, credit concentrations and economic conditions within the Company s market area. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and judgment and requires the Company to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of the Company s control, may require the Company to increase its allowance for loan losses. Increases in nonperforming loans have a significant impact on its allowance for loan losses.

In addition, bank regulatory agencies periodically review the Company s allowance for loan losses and may require the Company to increase the provision for loan losses or to recognize further loan charge-offs, based on judgments that differ from those of management. If loan charge-offs in future periods exceed the Company s allowance for loan losses, the Company will need to record additional provisions to increase its allowance for loan losses. Furthermore, growth in the Company s loan portfolio would generally lead to an increase in the provision for loan losses. Generally, increases in the Company s allowance for loan losses will result in a decrease in net income and stockholders equity, and may have a material adverse effect on the Company s financial condition, results of operations and cash flows. Material additions to the Company s allowance could also materially decrease the Company s net income.

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Failure to satisfy the Company s individual minimum capital requirements could result in enforcement action against the Company, which could negatively affect its results of operations and financial condition.

In conjunction with the recommendations of the OCC, effective February 2, 2010, the Company agreed to accept increased individual minimum capital requirements for Farmers Bank in excess of what would otherwise be required under applicable law. In conjunction with guidance provided by the OCC, the Company has targeted Farmers Bank to meet the following individual minimum capital requirements by December 31, 2010: Tier 1 Capital to Adjusted Total Assets of 7.20%; and Total Capital to Risk Weighted Assets of 11.00%. Failure to comply with the Company s targeted minimum capital requirements in the time frame provided, or at all, could result in enforcement orders or penalties from federal banking regulators, which could have a material adverse effect on the Company s business, financial condition and results of operations.

The Company may not be able to attract and retain skilled people.

The Company s success depends, in large part, on its ability to attract and retain key people. Competition for the best people in most activities in which the Company s engages can be intense, and the Company may not be able to retain or hire the people it wants or needs. In order to attract and retain qualified employees, the Company must compensate its employees at market levels. If the Company is unable to continue to attract and retain qualified employees, or do so at rates necessary to maintain its competitive position, the Company s performance, including its competitive position, could suffer, and, in turn, adversely affect the Company s business, financial condition and results of operations.

The Company may be adversely impacted by weakness in the local economies it serves.

The Company s business activities are geographically concentrated in Northeast Ohio and, in particular, Mahoning, Trumbull and Columbiana County, Ohio, where commercial activity has deteriorated at a greater rate than in other parts of Ohio and in the national economy. This has led to and may lead to further unexpected deterioration in loan quality, and slower asset and deposit growth, which may adversely affect the Company s business, financial condition and results of operations.

The soundness of other financial institutions could adversely affect the Company.

The Company s ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships. The Company has exposure to many different industries and counterparties, and the Company routinely executes transactions with counterparties in the financial industry. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, have led to market-wide liquidity problems and could lead to losses or defaults by the Company or by other institutions. Many of these transactions expose the Company to credit risk in the event of default of the Company s counterparty or client. In addition, the Company s credit risk may be exacerbated when the collateral that it holds cannot be realized upon or is liquidated at prices insufficient to recover the full amount of the loan. The Company cannot assure that any such losses would not materially and adversely affect the Company s business, financial condition or results of operations.

Impairment of investment securities, goodwill, other intangible assets, or deferred tax assets could require charges to earnings, which could result in a negative impact on the Company s results of operations.

In assessing the impairment of investment securities, the Company considers the length of time and extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuers, whether the market decline was affected by macroeconomic conditions and whether the Company has the intent to sell the debt security or will be required to sell the debt security before its anticipated recovery. Under current accounting standards, goodwill and certain other intangible assets with indeterminate lives are no longer amortized but, instead, are assessed for impairment periodically or when impairment indicators are present. Assessment of goodwill and such other intangible assets could result in circumstances where the applicable intangible asset is deemed to be impaired for accounting purposes. Under such circumstances, the intangible asset s impairment would be reflected as a charge to earnings in the period. Deferred tax assets are only recognized to the extent it is more likely than not they will be realized. Should management determine it is not more likely than not that the deferred tax assets will be realized, a valuation allowance with a change to earnings would be reflected in the period.

A substantial decline in the value of the Company s Federal Home Loan Bank of Cincinnati common stock may adversely affect its financial condition.

The Company owns common stock of the Federal Home Loan Bank of Cincinnati (the FHLB), in order to qualify for membership in the Federal Home Loan Bank system, which enables the Company to borrow funds under the Federal Home Loan Bank advance program. The carrying value of the Company s FHLB common stock was approximately $3.06 million as of September 30, 2010.

Published reports indicate that certain member banks of the Federal Home Loan Bank system may be subject to asset quality risks that could result in materially lower regulatory capital levels. In December 2008, certain member banks of the Federal Home Loan Bank system (other than the FHLB) suspended dividend payments and the repurchase of capital stock until further notice. In an extreme situation, it is possible that the capitalization of a Federal Home Loan Bank, including the FHLB, could be substantially diminished or reduced to zero. Consequently, given that there is no market for the Company s FHLB common stock, the Company believes that there is a risk that its investment could be deemed other-than-temporarily impaired at some time in the future. If this occurs, it may adversely affect the Company s results of operations and financial condition. If the FHLB were to cease operations, or if the Company were required to write-off its investment in the FHLB, the Company s business, financial condition, liquidity, capital and results of operations may be materially adversely affected.

The Company s business strategy includes continuing its growth plans. The Company s financial condition and results of operations could be negatively affected if the Company fails to grow or fails to manage its growth effectively.

The Company intends to continue pursuing a profitable growth strategy both within its existing markets and in new markets. The Company s prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in significant growth stages of development. The Company cannot assure that it will be able to expand its market presence in the Company s existing markets or successfully enter new markets or that any such expansion will not adversely affect the Company s results of operations. Failure to manage the Company s growth effectively could have a material adverse effect on the Company s business, future prospects, financial condition or results of operations and could adversely affect the Company s ability to successfully implement its business strategy. Also, if the Company grow more slowly than anticipated, the Company s operating results could be materially adversely affected.

The recently enacted Dodd-Frank Act may adversely affect our business, financial conditions and results of operations.

On July 21, 2010, President Obama signed into law the Dodd-Frank Act. The Dodd-Frank Act imposes new restrictions and an expanded framework of regulatory oversight for financial institutions, including depository institutions. Because the Dodd-Frank Act requires various federal agencies to adopt a broad range of regulations with significant discretion, many of the details of the new law and the effects they will have on us will not be known for months or even years.

Many of the provisions of the Dodd-Frank Act apply directly only to institutions much larger than us, and some will affect only institutions with different charters than Farmers or institutions that engage in activities in which we do not engage. Among the changes to occur pursuant to the Dodd-Frank Act that can be expected to have an effect on us are the following:

- The OTS will be merged into the OCC and the authority of the other remaining bank regulatory agencies restructured;
- A new independent consumer financial protection bureau will be established within the Federal Reserve Board, empowered to exercise broad regulatory, supervisory and enforcement authority with respect to both new and existing consumer financial protection laws;

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New capital regulations for thrift holding companies will be adopted and any new trust preferred securities will no longer count toward Tier 1 capital;

The current prohibition on the payment of interest on demand deposits will be repealed, effective July 21, 2011;

The standard maximum amount of deposit insurance per customer is permanently increased to $250,000 and non-interest bearing transaction accounts will have unlimited deposit insurance through January 1, 2013;

The deposit insurance assessment base calculation will be expanded to equal a depository institution s total assets minus the sum of its average tangible equity during the assessment period.

New corporate governance requirements applicable generally to all public companies in all industries will require new compensation practices, including, but not limited to, requiring companies to claw back incentive compensation under certain circumstances, to provide shareholders the opportunity to cast a nonbinding vote on executive compensation, to consider the independence of compensation advisors and new executive compensation disclosure requirements.

Many provisions of the Dodd-Frank Act will not be implemented immediately and will require interpretation and rule making by federal regulators. Farmers is closely monitoring all relevant sections of the Dodd-Frank Act to ensure continued compliance with laws and regulations. While the ultimate effect of the Dodd-Frank Act on Farmers cannot be determined yet, the law is likely to result in increased compliance costs and fees paid to regulators, along with possible restrictions on Farmers operations.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds Purchases of equity securities by the issuer.

On July 14, 2009, the Company announced the adoption of a stock repurchase program that authorizes the repurchase of up to 4.9% or approximately 657 thousand shares of its outstanding common stock in the open market or in privately negotiated transactions. This program expired in July 2010 and as of this filing had not been renewed. There was no treasury stock purchased by the issuer during the third quarter of 2010.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. (Removed and Reserved).

Item 5. Other Information

Not applicable.

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Item 6. Exhibits

The following exhibits are filed or incorporated by reference as part of this report:

3.1	Articles of Incorporation of Farmers National Banc Corp., as amended (incorporated by reference from Exhibit 4.1 to Farmers National Banc Corp. s Registration Statement on Form S-3 filed with the SEC on October 3, 2001 (File No. 333-70806).
3.2	Amended Code of Regulations of Farmers National Banc Corp. (incorporate by reference from Exhibit 3(ii) to Farmers National Banc Corp. s Annual Report on Form 10-K for the fiscal year ended December 31, 2009, filed with the SEC on March 16, 2010).
31.a	Certification of Chief Executive Officer (Filed herewith)
31.b	Certification of Chief Financial Officer (Filed herewith)
32.a	906 Certification of Chief Executive Officer (Filed herewith)
32.b	906 Certification of Chief Financial Officer (Filed herewith)

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FARMERS NATIONAL BANC CORP.

Dated: October 28, 2010

/s/ John S. Gulas

John S. Gulas
President and Chief Executive Officer

Dated: October 28, 2010

/s/ Carl D. Culp

Carl D. Culp
Executive Vice President and Treasurer