FARMERS NATIONAL BANC CORP /OH/
Form 10-Q
August 09, 2011

Table of Contents

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 June 30, 2011
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 þ 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 July 31, 2011
Common Stock, No Par Value	18,700,453 shares

	Page Number
PART I FINANCIAL INFORMATION	
Item 1 Financial Statements (Unaudited)	
Included in Part I of this report:	
Farmers National Banc Corp. and Subsidiaries	
Consolidated Balance Sheets	1
Consolidated Statements of Income and Comprehensive Income	2
Consolidated Statements of Cash Flows	3
Notes to Unaudited Consolidated Financial Statements	4-20
Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations	21-32
Item 3 Quantitative and Qualitative Disclosures About Market Risk	33
Item 4 Controls and Procedures	33
PART II OTHER INFORMATION	
Item 1 Legal Proceedings	34
Item 1A Risk Factors	34
Item 2 Unregistered Sales of Equity Securities and Use of Proceeds	34
Item 3 Defaults Upon Senior Securities	34
Item 4 (Removed and Reserved)	34
Item 5 Other Information	34
Item 6 Exhibits	34-35
SIGNATURES	36
10-Q Certifications	
Section 906 Certifications	

Exhibit 3.2
Exhibit 31.a
Exhibit 31.b

Exhibit 32.a
Exhibit 32.b
EX-101 INSTANCE DOCUMENT
EX-101 SCHEMA DOCUMENT
EX-101 CALCULATION LINKBASE DOCUMENT
EX-101 LABELS LINKBASE DOCUMENT
EX-101 PRESENTATION LINKBASE DOCUMENT

Table of Contents

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

	(In Thousands of Dollars)	
	June 30, 2011	**December 31, 2010**
ASSETS		
Cash and due from banks	$ 28,170	$ 30,772
Federal funds sold	16,969	6,533
TOTAL CASH AND CASH EQUIVALENTS	45,139	37,305
Securities available for sale	358,335	314,347
Loans	568,704	590,367
Less allowance for loan losses	10,876	9,307
NET LOANS	557,828	581,060
Premises and equipment, net	14,599	13,944
Bank owned life insurance	14,699	11,529
Goodwill	3,709	3,709
Other intangibles	2,956	3,211
Other assets	16,956	17,646
TOTAL ASSETS	$ 1,014,221	$ 982,751
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits:		
Noninterest-bearing	$ 81,550	$ 77,728
Interest-bearing	688,513	683,322
TOTAL DEPOSITS	770,063	761,050
Short-term borrowings	108,720	105,634
Long-term borrowings	23,572	24,733
Other liabilities	3,290	3,286
TOTAL LIABILITIES	905,645	894,703
Commitments and contingent liabilities		

Stockholders Equity:		
Common Stock Authorized 25,000,000 shares; issued 18,700,466 in 2011 and 15,699,184 in 2010	104,012	96,142
Retained (deficit) earnings	(2,155)	14,502
Accumulated other comprehensive income	6,719	2,907
Treasury stock, at cost; 13 shares in 2011 and 2,053,149 in 2010	0	(25,503)
TOTAL STOCKHOLDERS EQUITY	108,576	88,048
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 1,014,221	$ 982,751

See accompanying notes

Table of Contents

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 Six Months Ended	
	June 30, 2011	**June 30, 2010**	**June 30, 2011**	**June 30, 2010**
INTEREST AND DIVIDEND INCOME				
Loans, including fees	$ 8,354	$ 9,192	$ 16,820	$ 18,424
Taxable securities	2,048	2,261	3,917	4,502
Tax exempt securities	729	584	1,468	1,175
Dividends	53	47	99	100
Federal funds sold	10	15	19	24
TOTAL INTEREST AND DIVIDEND INCOME	11,194	12,099	22,323	24,225
INTEREST EXPENSE				
Deposits	1,684	2,420	3,382	5,165
Short-term borrowings	104	234	201	519
Long-term borrowings	249	269	500	551
TOTAL INTEREST EXPENSE	2,037	2,923	4,083	6,235
NET INTEREST INCOME	9,157	9,176	18,240	17,990
Provision for loan losses	1,075	1,600	2,950	4,378
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	8,082	7,576	15,290	13,612
NONINTEREST INCOME				
Service charges on deposit accounts	500	497	973	975
Bank owned life insurance income, including death benefits	119	131	278	257
Trust fees	1,365	1,197	2,703	2,429
Security gains (losses)	0	(3)	0	(3)
Insurance agency commissions	28	110	92	172
Investment commissions	263	129	454	240
Other operating income	419	660	811	987
TOTAL NONINTEREST INCOME	2,694	2,721	5,311	5,057
NONINTEREST EXPENSES				
Salaries and employee benefits	4,483	4,099	8,671	8,076
Occupancy and equipment	922	892	1,838	1,817

State and local taxes		238		224		485		456
Professional fees		267		381		503		690
Advertising		211		147		356		277
FDIC insurance		244		317		592		620
Intangible amortization		112		145		255		290
Core processing charges		245		237		490		476
Other operating expenses		1,370		1,203		2,716		2,475
TOTAL NONINTEREST EXPENSES		8,092		7,645		15,906		15,177
INCOME BEFORE INCOME TAXES		2,684		2,652		4,695		3,492
INCOME TAXES		567		618		888		611
NET INCOME	$	2,117	$	2,034	$	3,807	$	2,881
OTHER COMPREHENSIVE INCOME, NET OF TAX:								
Change in net unrealized gains on securities, net of reclassifications		3,769		2,988		3,812		4,055
COMPREHENSIVE INCOME	$	5,886	$	5,022	$	7,619	$	6,936
NET INCOME PER SHARE basic and diluted	$	0.11	$	0.15	$	0.21	$	0.21
DIVIDENDS PER SHARE	$	0.03	$	0.03	$	0.06	$	0.06

See accompanying notes

Table of Contents

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

	(In Thousands of Dollars) Six Months Ended	
	June 30, 2011	**June 30, 2010**
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 3,807	$ 2,881
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	2,950	4,378
Depreciation and amortization	829	861
Net amortization of securities	2,540	504
Security (gains) losses	0	3
Loss on sale of other real estate owned	29	48
Income on bank owned life insurance	(278)	(257)
Net change in other assets and liabilities	(1,139)	863
NET CASH FROM OPERATING ACTIVITIES	8,738	9,281
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities and repayments of securities available for sale	19,251	27,489
Proceeds from sales of securities available for sale	3,361	1,896
Purchases of securities available for sale	(63,277)	(39,014)
Loan originations and payments, net	19,845	(7,560)
Proceeds from sale of other real estate owned	141	354
Purchase of bank owned life insurance	(3,000)	0
Proceeds from BOLI death benefit	108	0
Additions to premises and equipment	(1,179)	(632)
NET CASH FROM INVESTING ACTIVITIES	(24,750)	(17,467)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net change in deposits	9,013	(16,873)
Net change in short-term borrowings	3,086	11,999
Repayment of Federal Home Loan Bank borrowings and other debt	(1,161)	(1,889)
Cash dividends paid	(1,119)	(813)
Proceeds from dividend reinvestment	255	240
Net proceeds from issuance of common shares	13,772	0
NET CASH FROM FINANCING ACTIVITIES	23,846	(7,336)
NET CHANGE IN CASH AND CASH EQUIVALENTS	7,834	(15,522)
Beginning cash and cash equivalents	37,305	51,160
Ending cash and cash equivalents	$ 45,139	$ 35,638

Supplemental cash flow information:		
Interest paid	$ 4,108	$ 6,435
Income taxes paid	$ 2,085	$ 50
Supplemental noncash disclosures:		
Transfer of loans to other real estate	$ 437	$ 173

See accompanying notes

Table of Contents

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Principles of Consolidation:

Farmers National Banc Corp. (the Company) is a multi-bank holding company registered under the Bank Holding Company Act of 1956, as amended. The Company provides full banking services through its nationally chartered subsidiary, The Farmers National Bank of Canfield (the Bank). The Company provides trust services through its subsidiary, Farmers Trust Company (the Trust), and insurance services through the Bank s subsidiary, Farmers National Insurance. The consolidated financial statements include the accounts of the Company, the Bank, the 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 2010 Annual Report to Shareholders included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010. 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, deferred tax assets, 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.

Shareholders Equity:

The Company successfully completed a rights and public offering of 5,000,000 common shares in January 2011. As part of this rights offering the Company issued 2,946,864 shares of authorized but unissued shares and reissued 2,053,136 shares of treasury stock. Total proceeds from the offering net of offering costs of $1.2 million were $13.8 million. Since the Company s cost basis of the treasury shares was greater than the price paid for stock issued in the rights offering, the difference of $19.3 million was recorded as a reduction to retained earnings. Other changes to retained earnings for the six months ended June 30, 2011 were net income of $3.8 million and partially offset by dividends paid to shareholders of $1.1 million. In addition to the rights and public offering, common stock increased by $255 thousand during the six months ended June 30, 2011 due to the issuance of 54,418 shares of stock through the Company s dividend reinvestment program. Accumulated other comprehensive income increased $3,8 million from December 31, 2010 to June 30, 2011 due to the after tax impact of increases in fair value of securities available for sale during that period.

Table of Contents

Securities:

The following table summarizes the amortized cost and fair value of the available-for-sale investment securities portfolio at June 30, 2011 and December 31, 2010 and the corresponding amounts of unrealized gains and losses recognized in accumulated other comprehensive income were as follows:

(In Thousands of Dollars)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2011				
U.S. Treasury and U.S. government sponsored entities	$ 87,200	$ 3,750	$ (15)	$ 90,935
State and political subdivisions	80,045	2,456	(691)	81,810
Mortgage-backed securities residential	157,505	4,620	(395)	161,730
Collateralized mortgage obligations	22,850	238	0	23,088
Equity securities	149	373	(16)	506
Other securities	250	16	0	266
Totals	$ 347,999	$ 11,453	$ (1,117)	$ 358,335

(In Thousands of Dollars)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2010				
U.S. Treasury and U.S. government sponsored entities	$ 67,376	$ 2,768	$ (166)	$ 69,978
State and political subdivisions	81,397	1,215	(2,146)	80,466
Mortgage-backed securities residential	140,681	4,099	(1,003)	143,777
Collateralized mortgage obligations	20,021	1	(362)	19,660
Equity securities	149	66	(16)	199
Other securities	250	17	0	267
Totals	$ 309,874	$ 8,166	$ (3,693)	$ 314,347

There was one security sale during the three and six month periods ended June 30, 2011. Proceeds from the sale were $3.4 million with no gain or loss recognized. Proceeds from sales of securities were $1.9 million for the three and six month periods ended June 30, 2010. Gross losses of $3 thousand were realized on these sales, during the second quarter of 2010.

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.

	June 30, 2011	
(In Thousands of Dollars)	Amortized Cost	Fair Value
Maturity		
Within one year	$ 4,300	$ 4,385
One to five years	98,306	102,048
Five to ten years	40,161	40,699
Beyond ten years	24,728	25,879

Mortgage-backed and CMO securities	180,355	184,818
Total	$ 347,850	$ 357,829

Table of Contents

The following table summarizes the investment securities with unrealized losses at June 30, 2011 and December 31, 2010, 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	Unrealized	Fair	Unrealized	Fair	Unrealized
June 30, 2011	Value	Losses	Value	Losses	Value	Losses
Available-for-sale						
U.S. Treasury and U.S. government-sponsored entities	$ 4,976	$ (10)	$ 288	$ (5)	$ 5,264	$ (15)
State and political subdivisions	22,234	(580)	851	(111)	23,085	(691)
Mortgage-backed securities residential	43,337	(395)	25	(0)	43,362	(395)
Equity securities	0	0	7	(16)	7	(16)
Total	$ 70,547	$ (985)	$ 1,171	$ (132)	$ 71,718	$ (1,117)

	Less Than 12 Months		12 Months or Longer		Total	
(In Thousands of Dollars)	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized
December 31, 2010	Value	Losses	Value	Losses	Value	Losses
Available-for-sale						
U.S. Treasury and U.S. government-sponsored entities	$ 8,458	$ (160)	$ 313	$ (6)	$ 8,771	$ (166)
State and political subdivisions	36,118	(1,981)	790	(165)	36,908	(2,146)
Mortgage-backed securities residential	45,567	(1,002)	26	(1)	45,593	(1,003)
Collateralized mortgage obligations	19,594	(362)	0	0	19,594	(362)
Equity securities	0	0	8	(16)	8	(16)
Total	$ 109,737	$ (3,505)	$ 1,137	$ (188)	$ 110,874	$ (3,693)

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.

Table of Contents

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. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income or loss. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

As of June 30, 2011, the Company s security portfolio consisted of 414 securities, 53 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 June 30, 2011 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.

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)	June 30, 2011	December 31, 2010
Commercial real estate		
Owner occupied	$ 105,743	$ 111,261
Non-owner occupied	74,464	76,592
Other	15,696	16,582
Commercial	74,800	76,635
Residential real estate		
1-4 family residential	147,318	154,132
Home equity lines of credit	22,658	23,624
Consumer		
Indirect	113,386	116,999
Direct	11,507	11,302
Other	1,464	1,485
Subtotal	567,036	588,612
Net deferred loan (fees) costs	1,668	1,755
Allowance for loan losses	(10,876)	(9,307)

Net loans	$ 557,828	$ 581,060

Table of Contents

The following tables present the activity in the allowance for loan losses by portfolio segment for the three and six months ending June 30, 2011.

Three Months Ended June 30, 2011

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
Beginning balance, April 1, 2011	$ 6,020	$ 1,878	$ 1,261	$ 842	$ 136	$ 10,137
Provision for loan losses	582	51	34	272	136	1,075
Recoveries	6	12	402	279		699
Loans charged off	(555)	(55)	(155)	(270)		(1,035)
Ending balance, June 30, 2011	$ 6,053	$ 1,886	$ 1,542	$ 1,123	$ 272	$ 10,876

Six Months Ended June 30, 2011

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Allowance for loan losses						
Beginning balance, January 1, 2011	$ 5,780	$ 1,707	$ 881	$ 875	$ 64	$ 9,307
Provision for loan losses	905	334	1,154	349	208	2,950
Recoveries	8	34	403	468		913
Loans charged off	(640)	(189)	(896)	(569)		(2,294)
Ending balance, June 30, 2011	$ 6,053	$ 1,886	$ 1,542	$ 1,123	$ 272	$ 10,876

The following table presents the activity in the allowance for loan losses for the three and six months ending June 30, 2010.

(In Thousands of Dollars)	Three Months Ended June 30, 2010	Six Months Ended June 30, 2010
Allowance for loan losses		
Beginning balance	$ 8,220	$ 7,400
Provision for loan losses	1,600	4,378
Recoveries	125	272
Loans charged off	(1,690)	(3,795)
Ending balance	$ 8,255	$ 8,225

Table of Contents

The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of June 30, 2011 and December 31, 2010. The recorded investment in loans includes the unpaid principal balance and unamortized loan origination fees and costs but excludes accrued interest receivable, which is not considered to be material:

June 30, 2011

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 348	$ 252	$	$	$	$ 600
Collectively evaluated for impairment	5,705	1,634	1,542	1,123	272	10,276
Total ending allowance balance	$ 6,053	$ 1,886	$ 1,542	$ 1,123	$ 272	$ 10,876
Loans:						
Loans individually evaluated for impairment	$ 5,152	$ 1,049	$	$	$	$ 6,201
Loans collectively evaluated for impairment	190,226	73,751	169,303	129,223		562,503
Total ending loans balance	$ 195,378	$ 74,800	$ 169,303	$ 129,223	$	$ 568,704

December 31, 2010

(In Thousands of Dollars)	Commercial Real Estate	Commercial	Residential Real Estate	Consumer	Unallocated	Total
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 572	$ 33	$	$	$	$ 605
Collectively evaluated for impairment	5,208	1,674	881	875	64	8,702
Total ending allowance balance	$ 5,780	$ 1,707	$ 881	$ 875	$ 64	$ 9,307
Loans:						
Loans individually evaluated for impairment	$ 6,045	$ 1,015	$	$	$	$ 7,060
Loans collectively evaluated for impairment	197,849	75,620	177,067	132,771		583,307

Total ending loans balance	$ 203,894	$ 76,635	$ 177,067	$ 132,771	$	$ 590,367

Interest income recognized during impairment for the three and six months ending June 30, 2011 and June 30, 2010 was immaterial.

Table of Contents

The following tables present loans individually evaluated for impairment by class of loans as of June 30, 2011 and December 31, 2010 and the average recorded investment by class for the six months ended June 30, 2011:
(In Thousands of Dollars)

June 30, 2011	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Six Months Ended Average Recorded Investment	Three Months Ended Average Recorded Investment
With no related allowance recorded:					
Commercial real estate					
Owner occupied	$ 1,203	$ 1,208	$	$ 1,236	$ 1,211
Non-owner occupied					
Other					
Commercial	641	641		671	655
Residential real estate					
1-4 family residential					
Home equity lines of credit					
Consumer					
Indirect					
Direct					
Other					
With an allowance recorded:					
Commercial real estate					
Owner occupied	2,286	2,288	99	2,405	2,375
Non-owner occupied	823	825	143	894	833
Other	830	831	106	812	802
Commercial	405	408	252	459	445
Residential real estate					
1-4 family residential					
Home equity lines of credit					
Consumer					
Indirect					
Direct					
Other					
Total	$ 6,188	$ 6,201	$ 600	$ 6,477	$ 6,321

Table of Contents

(In Thousands of Dollars)

December 31, 2010	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
With no related allowance recorded:			
Commercial real estate			
Owner occupied	$ 821	$ 818	$
Non-owner occupied	466	465	
Other	365	364	
Commercial	800	798	
Residential real estate			
1-4 family residential			
Home equity lines of credit			
Consumer			
Indirect			
Direct			
Other			
With an allowance recorded:			
Commercial real estate			
Owner occupied	3,147	3,141	134
Non-owner occupied	167	167	3
Other	1,097	1,090	435
Commercial	219	217	33
Residential real estate			
1-4 family residential			
Home equity lines of credit			
Consumer			
Indirect			
Direct			
Other			
Total	$ 7,082	$ 7,060	$ 605

The following table presents the recorded investment in nonaccrual and loans past due over 90 days still on accrual by class of loans as of June 30, 2011 and December 31, 2010:

	June 30, 2011		December 31, 2010	
(In Thousands of Dollars)	Nonaccrual	Loans Past Due over 90 Days Still Accruing	Nonaccrual	Loans Past Due over 90 Days Still Accruing
Commercial real estate				
Owner occupied	$ 1,365	$	$ 1,960	$
Non-owner occupied	421		550	
Other	885		1,462	
Commercial	408		400	

Residential real estate								
1-4 family residential		3,726		29		3,362		190
Home equity lines of credit		931		20		815		10
Consumer								
Indirect		14		51		27		53
Direct				38				48
Other								24
Total	$	7,750	$	138	$	8,576	$	325

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

Table of Contents

The following table presents the aging of the recorded investment in past due loans as of June 30, 2011 and December 31, 2010 by class of loans:

June 30, 2011

(In Thousands of Dollars)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial real estate						
Owner occupied	$ 114	$	$ 1,365	$ 1,479	$ 103,980	$ 105,459
Non-owner occupied	15		421	436	73,828	74,264
Other			885	885	14,770	15,655
Commercial	261	35	408	704	74,096	74,800
Residential real estate						
1-4 family residential	1,209	185	3,755	5,149	141,497	146,646
Home equity lines of credit	111	147	951	1,209	21,449	22,658
Consumer						
Indirect	1,221	352	65	1,638	114,613	116,251
Direct	113	18	38	169	11,338	11,507
Other	12	1		13	1,451	1,464
Total	$ 3,056	$ 738	$ 7,888	$ 11,682	$ 557,022	$ 568,704

December 31, 2010

(In Thousands of Dollars)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial real estate						
Owner occupied	$ 407	$ 91	$ 1,960	$ 2,458	$ 108,509	$ 110,967
Non-owner occupied	499	59	550	1,108	75,281	76,389
Other			1,462	1,462	15,076	16,538
Commercial	286	275	400	961	75,674	76,635
Residential real estate						
1-4 family residential	2,981	435	3,552	6,968	146,475	153,443
Home equity lines of credit	334	16	825	1,175	22,449	23,624
Consumer						
Indirect	1,668	519	80	2,267	117,716	119,983
Direct	253	91	48	392	10,911	11,303
Other	9	1	24	34	1,451	1,485
Total	$ 6,437	$ 1,487	$ 8,901	$ 16,825	$ 573,542	$ 590,367

Troubled Debt Restructurings:

Included in loans individually impaired are loans with balances of $3.4 million and $3.0 million for which the Company has modified the repayment terms at June 30, 2011 and December 31, 2010. The Company has allocated $40 thousand of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as

of June 30, 2011 and December 31, 2010. There are no commitments to lend additional amounts to borrowers with loans that are classified as troubled debt restructurings at June 30, 2011 and December 31, 2010.

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. This analysis is performed on a monthly basis. The Company uses the following definitions for risk ratings:

Special Mention. Loans classified as special mention have a potential weakness that deserves management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution s credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

Table of Contents

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

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

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. As of June 30, 2011 and December 31, 2010, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

June 30, 2011

(In Thousands of Dollars)	Pass	Special Mention	Sub-standard	Doubtful	Not Rated	Total
Commercial real estate						
Owner occupied	$ 87,297	$ 5,902	$ 12,260	$	$	$ 105,459
Non-owner occupied	62,191	1,162	10,911			74,264
Other	12,639	597	2,419			15,655
Commercial	66,646	4,302	3,852			74,800
Total	$ 228,773	$ 11,963	$ 29,442	$	$	$ 270,178

December 31, 2010

(In Thousands of Dollars)	Pass	Special Mention	Sub-standard	Doubtful	Not Rated	Total
Commercial real estate						
Owner occupied	$ 91,976	$ 3,893	$ 15,098	$	$	$ 110,967
Non-owner occupied	63,502	1,075	11,812			76,389
Other	12,005	786	3,747			16,538
Commercial	65,358	4,076	7,201			76,635
Total	$ 232,841	$ 9,830	$ 37,858	$	$	$ 280,529

The Company considers the performance of the loan portfolio and its impact on the allowance for loan losses. For residential, consumer and indirect loan classes, the Company also evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the recorded investment in residential, consumer and indirect auto loans based on payment activity as of June 30, 2011 and December 31, 2010. Nonperforming loans are loans past due 90 days and still accruing interest and nonaccrual loans.

June 30, 2011

	Residential Real Estate		Consumer		
(In Thousands of Dollars)	1-4 Family Residential	Home Equity Lines of Credit	Indirect	Direct	Other
Performing	$ 142,891	$ 21,707	$ 116,186	$ 11,469	$ 1,465

Nonperforming	3,755	951	65	38	
Total	$ 146,646	$ 22,658	$ 116,251	$ 11,507	$ 1,465

Table of Contents

December 31, 2010

(In Thousands of Dollars)	Residential Real Estate 1-4 Family Residential	Residential Real Estate Home Equity Lines of Credit	Consumer Indirect	Consumer Direct	Consumer Other
Performing	$ 149,891	$ 22,799	$ 119,903	$ 11,255	$ 1,461
Nonperforming	3,552	825	80	48	24
Total	$ 153,443	$ 23,624	$ 119,983	$ 11,303	$ 1,485

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 June 30, 2011	Three Months Ended June 30, 2010	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Basic EPS computation				
Numerator Net income	$ 2,117	$ 2,034	$ 3,807	$ 2,881
Denominator Weighted average shares outstanding	18,674,213	13,546,569	17,820,254	13,533,302
Basic earnings per share	$ .11	$ .15	$ .21	$ .21
Diluted EPS computation				
Numerator Net income	$ 2,117	$ 2,034	$ 3,807	$ 2,881
Denominator Weighted average shares outstanding for basic earnings per share	18,674,213	13,546,569	17,820,254	13,533,302
Effect of Stock Options	0	0	0	0
Weighted averages shares for diluted earnings per share	18,674,213	13,546,569	17,820,254	13,533,302
Diluted earnings per share	$ .11	$ .15	$ .21	$ .21

Stock options for 28,500 and 34,000 shares were not considered in the computing of diluted earnings per share for 2011 and 2010, 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 June 30, 2011 there were 28,500 outstanding options of which 25,500 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 six month period ended June 30, 2011 was not material. No related income tax benefit was recorded.

Comprehensive Income:

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

Table of Contents

Recent Accounting Pronouncements

ASU No. 2010-20, Receivables (Topic 310) Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. ASU 2010-20 requires entities to provide disclosures designed to facilitate financial statement users evaluation of (i) the nature of credit risk inherent in the entity s portfolio of financing receivables, (ii) how that risk is analyzed and assessed in arriving at the allowance for credit losses and (iii) the changes and reasons for those changes in the allowance for credit losses. Disclosures must be disaggregated by portfolio segment, the level at which an entity develops and documents a systematic method for determining its allowance for credit losses, and class of financing receivable, which is generally a disaggregation of portfolio segments. The required disclosures include, among other things, a rollforward of the allowance for credit losses as well as information about modified, impaired, non-accrual and past due loans and credit quality indicators. ASU 2010-20 became effective for the Company s consolidated financial statements as of December 31, 2010, as it relates to disclosures required as of the end of a reporting period. Disclosures that relate to activity during a reporting period became effective for the Company s consolidated financial statements beginning on January 1, 2011. ASU 2011-01, Receivables (Topic 310) Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20, temporarily deferred the effective date for disclosures related to troubled debt restructurings to coincide with the effective date of the then proposed ASU 2011-02, Receivables (Topic 310) A Creditor s Determination of Whether a Restructuring Is a Troubled Debt Restructuring, which is further discussed below.

ASU No. 2010-28, Intangibles Goodwill and Other (Topic 350) When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts. ASU 2010-28 modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist such as if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. ASU 2010-28 became effective for the Company on January 1, 2011 and did not have a significant impact on the Company s consolidated financial statements.

ASU No. 2011-02, Receivables (Topic 310) A Creditor s Determination of Whether a Restructuring Is a Troubled Debt Restructuring. ASU 2011-02 clarifies which loan modifications constitute troubled debt restructurings and is intended to assist creditors in determining whether a modification of the terms of a receivable meets the criteria to be considered a troubled debt restructuring, both for purposes of recording an impairment loss and for disclosure of troubled debt restructurings. In evaluating whether a restructuring constitutes a troubled debt restructuring, a creditor must separately conclude, under the guidance clarified by ASU 2011-02, that both of the following exist: (a) the restructuring constitutes a concession; and (b) the debtor is experiencing financial difficulties. ASU 2011-02 will be effective for the Company on July 1, 2011, and applies retrospectively to restructurings occurring on or after January 1, 2011. Adoption of ASU 2011-02 is not expected have a significant impact on the Company s consolidated financial statements.

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.

Table of Contents

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.

Assets Measured on a Recurring Basis

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

		Fair Value Measurements at June 30, 2011 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	$ 90,935	$ 0	$ 90,935	$ 0
State and political subdivisions	81,810	0	81,810	0
Mortgage-backed securities-residential	161,730	0	161,718	12
Collateralized mortgage obligations	23,088	0	23,088	0
Equity securities	506	506	0	0
Other securities	266	0	266	0
Total investment securities	$ 358,335	$ 506	$ 357,817	$ 12

Table of Contents

(In Thousands of Dollars)	Carrying Value	Fair Value Measurements at December 31, 2010 Using: 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	$ 69,978	$ 0	$ 69,978	$ 0
State and political subdivisions	80,466	0	80,466	0
Mortgage-backed securities-residential	143,777	0	143,765	12
Collateralized mortgage obligations	19,660	0	19,660	0
Equity securities	199	199	0	0
Other securities	267	0	267	0
Total investment securities	$ 314,347	$ 199	$ 314,136	$ 12

There were no significant transfers between level 1 and level 2 during the three and six month periods ending June 30, 2011.

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 June 30,		Six Months Ended June 30,	
(In Thousands of Dollars)	2011	2010	2011	2010
Beginning balance	$ 12	$ 13	$ 12	$ 13
Total unrealized gains or losses:				
Included in other comprehensive income or loss	0	0	0	0
Purchases, sales, issuances and settlements, net	0	0	0	0
Transfer in and/or out	0	0	0	0
Ending balance	$ 12	$ 13	$ 12	$ 13

Assets Measured on a Non-Recurring Basis

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

Fair Value Measurements at June 30, 2011 Using: Quoted Prices in Active	Significant Other	Significant

(In Thousands of Dollars)	Carrying Value	Markets for Identical Assets (Level 1)	Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Financial assets:				
Impaired loans				
Commercial real estate				
Owner occupied	$ 441	$ 0	$ 0	$ 441
Non-owner occupied	680	0	0	680
Other	724	0	0	724
Commercial	153	0	0	153

Table of Contents

(In Thousands of Dollars)	Carrying Value	Fair Value Measurements at December 31, 2010 Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial assets:				
Impaired loans				
Commercial real estate				
Owner occupied	$ 1,239	$ 0	$ 0	$ 1,239
Non-owner occupied	164	0	0	164
Other	662	0	0	662
Commercial	186	0	0	186

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a principal balance of $2.6 million with a valuation allowance of $561 thousand, resulting in an additional provision for loan loss of $66 thousand and $397 thousand for the three and six month periods ending June 30, 2011. At December 31, 2010, impaired loans had a principal balance of $2.8 million, with a valuation allowance of $565 thousand. Excluded from the fair value of impaired loans, at June 30, 2011 and December 31, 2010, discussed above are $1.8 million of loans classified as troubled debt restructurings, which are not carried at fair value.

The carrying amounts and estimated fair values of financial instruments, at June 30, 2011 and December 31, 2010 are as follows:

(In Thousands of Dollars) **June 30, 2011**	Carrying Amount	Fair Value
Financial assets		
Cash and cash equivalents	$ 45,139	$ 45,139
Securities available-for-sale	358,335	358,335
Restricted stock	4,224	n/a
Loans, net	557,828	574,353
Accrued interest receivable	4,086	4,086
Financial liabilities		
Deposits	770,063	774,535
Short-term borrowings	108,720	108,720
Long-term borrowings	23,572	26,068
Accrued interest payable	678	678

(In Thousands of Dollars) **December 31, 2010**	Carrying Amount	Fair Value
Financial assets		
Cash and cash equivalents	$ 37,305	$ 37,305
Securities available-for-sale	314,347	314,347
Restricted stock	3,977	n/a

Loans, net	581,060	590,331
Accrued interest receivable	4,125	4,125
Financial liabilities		
Deposits	761,050	764,170
Short-term borrowings	105,634	105,634
Long-term borrowings	24,733	27,080
Accrued interest payable	703	703

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, 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

The reportable segments are 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.
Significant segment totals are reconciled to the financial statements as follows:

(In Thousands of Dollars) **June 30, 2011**	**Trust Segment**	**Bank Segment**	**Others**	**Consolidated Totals**
Assets				
Cash and due from banks	$ 2,019	$ 43,147	$ (27)	$ 45,139
Securities available for sale	2,387	355,821	127	358,335
Net loans	0	557,828	0	557,828
Premises and equipment, net	109	14,490	0	14,599
Goodwill and other intangibles	6,665	0	0	6,665
Other assets	545	30,759	351	31,655
Total Assets	$ 11,725	$ 1,002,045	$ 451	$ 1,014,221
Liabilities and Stockholders Equity				
Deposits, borrowings and other liabilities	$ 613	$ 910,132	$ (5,100)	$ 905,645
Stockholders equity	11,112	91,913	5,551	108,576
Total Liabilities and Stockholders Equity	$ 11,725	$ 1,002,045	$ 451	$ 1,014,221

(In Thousands of Dollars) **December 31, 2010**	**Trust Segment**	**Bank Segment**	**Others**	**Consolidated Totals**
Assets				
Cash and due from banks	$ 1,122	$ 36,343	$ (160)	$ 37,305
Securities available for sale	2,627	311,601	119	314,347
Net loans	0	581,060	0	581,060
Premises and equipment, net	113	13,831	0	13,944
Goodwill and other intangibles	6,920	0	0	6,920
Other assets	425	28,336	414	29,175
Total Assets	$ 11,207	$ 971,171	$ 373	$ 982,751

Liabilities and Stockholders Equity				
Deposits, borrowings and other liabilities	$ 368	$ 894,052	$ 283	$ 894,703
Stockholders equity	10,839	77,119	90	88,048
Total Liabilities and Stockholders Equity	$ 11,207	$ 971,171	$ 373	$ 982,751

(In Thousands of Dollars)

For the Three Months Ended June 30, 2011	**Trust Segment**	**Bank Segment**	**Others**	**Consolidated Totals**
Net interest income	$ 11	$ 9,158	$ (12)	$ 9,157
Provision for loan losses	0	1,075	0	1,075
Service fees, security gains and other noninterest income	1,377	1,356	(39)	2,694
Noninterest expense	1,149	6,743	200	8,092
Income before taxes	239	2,696	(251)	2,684
Income taxes	82	570	(85)	567
Net Income	$ 157	$ 2,126	$ (166)	$ 2,117

(In Thousands of Dollars)

For the Six Months Ended June 30, 2011	**Trust Segment**	**Bank Segment**	**Others**	**Consolidated Totals**
Net interest income	$ 22	$ 18,243	$ (25)	$ 18,240
Provision for loan losses	0	2,950	0	2,950
Service fees, security gains and other noninterest income	2,727	2,661	(77)	5,311
Noninterest expense	2,349	13,255	302	15,906
Income before taxes	400	4,699	(404)	4,695
Income taxes	137	888	(137)	888
Net Income	$ 263	$ 3,811	$ (267)	$ 3,807

(In Thousands of Dollars)

For the Three Months Ended June 30, 2010	**Trust Segment**	**Bank Segment**	**Others**	**Consolidated Totals**
Net interest income	$ 20	$ 9,168	$ (12)	$ 9,176
Provision for loan losses	0	1,600	0	1,600
Service fees, security gains and other noninterest income	1,254	1,158	309	2,721
Noninterest expense	1,115	6,365	165	7,645
Income before taxes	159	2,361	132	2,652
Income taxes	55	518	45	618
Net Income	$ 104	$ 1,843	$ 87	$ 2,034

(In Thousands of Dollars)

For the Six Months Ended June 30, 2010	**Trust Segment**	**Bank Segment**	**Others**	**Consolidated Totals**

Net interest income	$ 39	$ 17,971	$ (20)	$ 17,990
Provision for loan losses	0	4,378	0	4,378
Service fees, security gains and other noninterest income	2,486	2,226	345	5,057
Noninterest expense	2,257	12,711	209	15,177
Income before taxes	268	3,108	116	3,492
Income taxes	93	479	39	611
Net Income	$ 175	$ 2,629	$ 77	$ 2,881

20

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 Annual Report on Form 10-K for the year ended December 31, 2010.

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.

Overview

For the three months ended June 30, 2011, the Company reported net income of $2.1 million, compared to $2.0 million for the second quarter of 2010. Net income for the six months ended June 30, 2011 was $3.8 million compared to $2.9 million for the same six month period in 2010, representing a 32% increase. Income from trust fees and investment commissions increased 18% during the same six month period. The increases reflect the continued benefit from the strategy to diversify income streams. On a per share basis, net income was $0.11 per diluted share compared $0.15 for the second quarter ended June 30, 2010. The tangible common equity ratio increased to 10.11% at June 30, 2011 as compared to 7.92% at June 30, 2010, mainly as a result of the successful common share offering completed in the first quarter of 2011. The provision for loan losses decreased from $4.4 million for the six month period ending June 30, 2010 to $3.0 million for the six months ended June 30, 2011. This 33% decrease is a result of improved credit quality, as net charge-offs have declined from $3.5 million for the first six months of 2010 to $1.4 million for the same period in 2011. There has also been a decline in 30-89 day delinquencies, from $5.7 million at June 30, 2010 to $3.8 million at June 30, 2011.

The Company s total assets reported at June 30, 2011 were $1.01 billion, which remains unchanged compared to $1.01 billion in total assets recorded at June 30, 2010. Net loans were reported at $557.8 million at June 30, 2011, versus $605.0 million at the same time in 2010, a decrease of $47.2 million, or 7.8%. The decline in loans, particularly in the first quarter of 2011, is related to seasonality in the retail lending portfolio and slow economic growth. The decline in loan balances resulted in a lower level of loan income for the current quarter. Over this same period, deposits increased $9.4 million, or 1.2%, from $760.7 million at June 30, 2010 to $770.1 million at June 30, 2011. Stockholders equity totaled $108.6 million, or 10.7% of total assets, at June 30, 2011, an increase of $21.6 million, or 24.8%, compared to $87.0 million at June 30, 2010. The increase in equity was primarily the result of the successful common share offering completed in the first quarter of 2011, adding approximately $14 million in capital. The increase is also the result of net income, offset by mark to market adjustments in the Company s investment securities and cash dividends paid to shareholders during the past twelve months. Shareholders received a $0.03 per share cash dividend on June 30, 2011 and a total of $0.12 per share cash dividends paid in the past four quarters. Book value per share decreased 9.4% from $6.41 per share at June 30, 2010 to $5.81 per share at June 30, 2011. This decrease is mainly the result of the increase in shares outstanding, which includes the 5 million shares issued in the first quarter 2011 common share offering, which were offered at $3.00 per share. The Company s tangible book value per share also decreased 7.3% from $5.88 per share at June 30, 2010 to $5.45 per share at June 30, 2011.

Results of Operations

The following is a comparison of selected financial ratios and other results at or for the three-month and six month periods ending June 30, 2011 and 2010:

	At or for the Three Months Ended June 30,		At or for the Six Months Ended June 30,	
(In Thousands, except Per Share Data)	2011	2010	2011	2010
Total Assets	$ 1,014,221	$ 1,014,804	$ 1,014,221	$ 1,014,804
Net Income	$ 2,117	$ 2,034	$ 3,807	$ 2,881
Basic and Diluted Earnings Per Share	$ .11	$ .15	$ .21	$ .21
Return on Average Assets (Annualized)	.83%	.79%	.76%	.57%
Return on Average Equity (Annualized)	8.05%	9.78%	7.69%	6.89%
Efficiency Ratio (tax equivalent basis)	64.42%	62.15%	63.50%	62.93%
Equity to Asset Ratio	10.71%	8.57%	10.71%	8.57%
Tangible Common Equity Ratio *	10.11%	7.92%	10.11%	7.92%
Dividends to Net Income	26.45%	19.96%	29.39%	28.18%
Net Loans to Assets	55.00%	59.62%	55.00%	59.62%
Loans to Deposits	73.85%	80.62%	73.85%	80.62%

* 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 the Company s capital levels. Since there is no authoritative requirement to calculate the tangible common equity ratio, the Company s tangible common equity ratio is not necessarily comparable to similar capital measures disclosed or

Table of Contents

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 June 30, 2011 and 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:

(In Thousands of Dollars)	June 30, 2011	June 30, 2010
Reconciliation of Common Stockholders Equity to Tangible Common Equity		
Stockholders Equity	$ 108,576	$ 86,991
Less Goodwill and other intangibles	6,665	7,210
Tangible Common Equity	$ 101,911	$ 79,781

(In Thousands of Dollars)	June 30, 2011	June 30, 2010
Reconciliation of Total Assets to Tangible Assets		
Total Assets	$ 1,014,221	$ 1,014,804
Less Goodwill and other intangibles	6,665	7,210
Tangible Assets	$ 1,007,556	$ 1,007,594

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.

Table of Contents

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

	Three Months Ended June 30, 2011			Three Months Ended June 30, 2010		
	AVERAGE BALANCE	INTEREST	RATE (1)	AVERAGE BALANCE	INTEREST	RATE (1)
EARNING ASSETS						
Loans (3) (5) (6)	**$ 562,446**	**$ 8,444**	**6.02%**	$ 599,884	$ 9,286	6.21%
Taxable securities (4)	**269,339**	**2,048**	**3.05**	255,423	2,261	3.55
Tax-exempt securities (4) (6)	**76,049**	**1,111**	**5.86**	58,103	875	6.04
Equity Securities (2) (6)	**4,343**	**53**	**4.89**	4,126	47	4.57
Federal funds sold	**40,287**	**10**	**0.10**	36,325	15	0.17
Total earning assets	**952,464**	**11,666**	**4.91**	953,861	12,484	5.25
NONEARNING ASSETS						
Cash and due from banks	**18,820**			22,933		
Premises and equipment	**13,794**			14,405		
Allowance for Loan Losses	**(10,563)**			(8,048)		
Unrealized gains (losses) on securities	**6,073**			8,245		
Other assets (3)	**43,244**			41,877		
Total Assets	**$ 1,023,832**			$ 1,033,273		
INTEREST-BEARING LIABILITIES						
Time deposits	**$ 248,816**	**$ 1,280**	**2.06%**	$ 300,567	$ 1,912	2.55%
Savings deposits	**332,426**	**385**	**0.46**	295,564	471	0.64
Demand deposits	**109,679**	**19**	**0.07**	107,979	37	0.14
Short term borrowings	**117,610**	**104**	**0.35**	146,094	234	0.64
Long term borrowings	**23,643**	**249**	**4.22**	25,357	269	4.26
Total Interest-Bearing Liabilities	**832,174**	**2,037**	**0.98**	875,561	2,923	1.34
NONINTEREST-BEARING LIABILITIES AND STOCKHOLDERS EQUITY						
Demand deposits	**82,715**			70,528		
Other Liabilities	**3,399**			3,733		
Stockholders equity	**105,544**			83,451		

Total Liabilities and Stockholders Equity	**$ 1,023,832**			$ 1,033,273		
Net interest income and interest rate spread		**$ 9,629**	**3.93%**		$ 9,561	3.91%
Net interest margin			**4.05%**			4.02%

(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 $401 thousand and $564 thousand for 2011 and 2010 respectively and is reduced by amortization of $441 thousand and $448 thousand for 2011 and 2010 respectively.

(6) For 2011, adjustments of $90 thousand and $382 thousand respectively are made to tax equate income on tax exempt loans and tax exempt securities. For 2010, adjustments of $94 thousand and $291 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.

Table of Contents

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

	Six Months Ended June 30, 2011			Six Months Ended June 30, 2010		
	AVERAGE BALANCE	INTEREST	RATE (1)	AVERAGE BALANCE	INTEREST	RATE (1)
EARNING ASSETS						
Loans (3) (5) (6)	**$ 567,849**	**$ 16,998**	**6.04%**	$ 600,034	$ 18,612	6.26%
Taxable securities (4)	**252,588**	**3,917**	**3.13**	248,726	4,502	3.65
Tax-exempt securities (4) (6)	**76,557**	**2,235**	**5.89**	58,449	1,760	6.07
Equity Securities (2) (6)	**4,235**	**99**	**4.71**	4,126	100	4.89
Federal funds sold	**34,920**	**19**	**0.11**	31,063	24	0.16
Total earning assets	**936,149**	**23,268**	**5.01**	942,398	24,998	5.35
NONEARNING ASSETS						
Cash and due from banks	**22,943**			22,705		
Premises and equipment	**13,840**			14,394		
Allowance for Loan Losses	**(10,064)**			(7,565)		
Unrealized gains (losses) on securities	**4,851**			7,383		
Other assets (3)	**42,412**			41,941		
Total Assets	**$ 1,010,131**			$ 1,021,256		
INTEREST-BEARING LIABILITIES						
Time deposits	**$ 250,811**	**$ 2,588**	**2.08%**	$ 310,383	$ 4,080	2.65%
Savings deposits	**328,139**	**757**	**0.47**	288,020	1,000	0.70
Demand deposits	**110,469**	**37**	**0.07**	106,474	85	0.16
Short term borrowings	**111,586**	**201**	**0.36**	134,673	519	0.78
Long term borrowings	**23,819**	**500**	**4.23**	25,999	551	4.27
Total Interest-Bearing Liabilities	**824,824**	**4,083**	**1.00**	865,549	6,235	1.45
NONINTEREST-BEARING LIABILITIES AND STOCKHOLDERS EQUITY						
Demand deposits	**82,074**			69,194		
Other Liabilities	**3,356**			2,252		
Stockholders equity	**99,877**			84,261		

Total Liabilities and Stockholders Equity	**$ 1,010,131**			$ 1,021,256		
Net interest income and interest rate spread		**$ 19,185**	**4.01%**		$ 18,763	3.90%
Net interest margin			**4.14%**			4.02%

(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 $837 thousand and $994 thousand for 2011 and 2010 respectively and is reduced by amortization of $888 thousand and $882 thousand for 2011 and 2010 respectively.

(6) For 2011, adjustments of $178 thousand and $767 thousand respectively are made to tax equate income on tax exempt loans and tax exempt securities. For 2010, adjustments of $188 thousand and $585 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.

Net interest income. Net interest income was $9.2 million for the second quarter of 2011, which compares to $9.2 million in the second quarter of 2010. The net interest margin to average earning assets on a fully taxable equivalent basis improved 3 basis points to 4.05% for the three months ended June 30, 2011, compared to 4.02% for the same period in the prior year. In comparing the quarters ending June 30, 2011 and 2010, yields on earning assets decreased 34 basis points, while the cost of interest bearing liabilities decreased 36 basis points.

On a year-to-date basis, net interest income improved to $18.2 million for the six month period ended June 30, 2011, compared to $18.0 million in the same period in 2010. The annualized net interest margin to average earning assets on a fully taxable equivalent basis was 4.14% for the six months ended June 30, 2011, compared to 4.02% for the same period in the prior year.

Noninterest Income. Noninterest income was $2.7 million for the second quarter of 2011, which compares to $2.7 million for the same quarter of 2010. Trust fees were $1.4 million for the quarter ended June 30, 2011, an increase of $168 thousand, or 14.0%, compared to the same quarter in 2010. Investment commissions also increased for the quarter ended June 30, 2011 to $263 thousand compared to $129 thousand in the same quarter in 2010. The increase in both the trust fees and investment commissions can be attributed to equity market appreciation during the current quarter, as most of the fee income is based on fair market values of invested securities.

Noninterest income for the six months ended June 30, 2011 was $5.3 million, compared to $5.1 million for the same period in 2009. The increase in noninterest income is primarily due to increases in trust fee income and investment commissions in 2011 of $274 thousand and $214 thousand, respectively. As with the current quarter, the six month increase in trust and investment commissions is related to the equity markets appreciation.

Noninterest Expense. Noninterest expense totaled $8.1 million for the second quarter of 2011, which is $447 thousand more than the $7.6 million in the same quarter in 2010. Most of this increase is a result of a $384 thousand increase in salaries and employee benefits, resulting from a higher number of employees in the current period.

Noninterest expenses for the six months ended June 30, 2011 was $15.9 million, compared to $15.2 million for the same period in 2010, representing an increase of $729 thousand, or 4.8%. The increase is mainly the result of a $595 thousand increase in salaries and employee benefits. Salaries and benefits increased as a result of added employees in the new loan production office and an accrual of salary expense from the separation agreement with a key employee.

The following is a detail of non-interest expense line items classified between the Trust and the other entities in the Company for the three month and six month periods ending June 30, 2011 and 2010:

	For the Three Months Ended					
	June 30, 2011			June 30, 2010		
(In Thousands of Dollars)	Trust Company	Bank and Others	Total Company	Trust Company	Bank and Others	Total Company
Noninterest expense						
Salaries and employee benefits	$ 704	$ 3,779	$ 4,483	$ 630	$ 3,469	$ 4,099
Occupancy and equipment	130	792	922	124	768	892
State and local taxes	24	214	238	29	195	224
Professional fees	12	255	267	15	366	381
Advertising	3	208	211	0	147	147
FDIC insurance	0	244	244	0	317	317
Intangible amortization	112	0	112	145	0	145
Core processing charges	0	245	245	0	237	237
Other operating expenses	164	1,206	1,370	172	1,031	1,203
Total noninterest expense	$ 1,149	$ 6,943	$ 8,092	$ 1,115	$ 6,530	$ 7,645

	For the Six Months Ended					
	June 30, 2011			June 30, 2010		
(In Thousands of Dollars)	Trust Company	Bank and Others	Total Company	Trust Company	Bank and Others	Total Company
Noninterest expense						
Salaries and employee benefits	$ 1,416	$ 7,255	$ 8,671	$ 1,280	$ 6,796	$ 8,076
Occupancy and equipment	269	1,569	1,838	248	1,569	1,817
State and local taxes	49	436	485	59	397	456
Professional fees	23	480	503	30	660	690
Advertising	3	353	356	2	275	277
FDIC insurance	0	592	592	0	620	620
Intangible amortization	255	0	255	290	0	290
Core processing charges	0	490	490	0	476	476
Other operating expenses	334	2,382	2,716	348	2,127	2,475
Total noninterest expense	$ 2,349	$ 13,557	$ 15,906	$ 2,257	$ 12,920	$ 15,177

The Company s tax equivalent efficiency ratio for the three month period ended June 30, 2011 was 64.42% compared to 62.15% for the same period in 2010. The decline in the efficiency ratio was the result of the $46 thousand decrease in net interest income and noninterest income, and a $447 thousand increase in noninterest expense.

The Company s tax equivalent efficiency ratio for the six month period ended June 30, 2011 was 63.50% compared to 62.93% in the prior year s same six month period. The decline in the efficiency ratio was the result of the $729 thousand increase in noninterest expense.

Income Taxes. Income tax expense totaled $567 thousand for the quarter ended June 30, 2011 and $618 thousand tax expense for the quarter ended June 30, 2010. The decrease in the current quarter can be attributed to the $145 thousand increase in tax exempt income from state and local government securities.

Income tax expense was $888 thousand for the first six months of 2011 and $611 thousand for the first six months of 2010. The effective tax rate for the first six months of 2011 was 18.91%, compared to 17.50% for the same period in 2010. The effective tax rate increase over the same period in 2010 was due to the recognition of tax benefits related to the arbitration and subsequent settlement surrounding the acquisition of the Trust company during the first six months of 2010.

Other Comprehensive Income. For the quarter ended June 30, 2011, the change in net unrealized gains on securities, net of reclassifications, resulted in an unrealized gain, net of tax, of $3.8 million, compared to an unrealized gain of $3.0 million for the same period in 2010. Management believes the increases in fair value for the three month periods ending June 30 in 2011 and 2010 are the result of the continued low interest rate environment that exists in the debt securities market.

For the first six months of 2011, the change in net unrealized gains on securities, net of reclassifications, resulted in an unrealized gain, net of tax, of $3.8 million, compared to an unrealized gain of $4.1 million for the same period in 2010. Management believes the increase in fair value for the periods in 2011 and 2010 is largely due to lower market interest rates.

Financial Condition

Cash and cash equivalents. Cash and cash equivalents increased $7.8 million during the first six months of 2011. The Company expects these levels to remain steady over the next few months. The increase is a result of management s effort to keep a larger balance in federal funds sold for unforeseen liquidity purposes

Securities. Securities available-for-sale increased by $44.0 million since December 31, 2010. Securities were purchased in an effort to increase returns on some of the cash available from the additional core deposit account balances and repurchase agreements sold during the period. There was a $5.9 million increase in the net unrealized gains on securities during the first six months of 2011.

Loans. Gross loans decreased $21.7 million, or 3.67%, since December 31, 2010. The commercial real estate loan and residential real estate loan portfolios decreased $8.5 million and $7.8 million, respectively, accounting for the majority of the decrease in gross loans during the first six months of 2011. The decline in loans is related to seasonality in the retail lending portfolio and slow economic growth in the Mahoning Valley. The decline in loan balances resulted in a lower level of loan income for the current quarter. On a fully tax equivalent basis, loans contributed 73.05% of total interest income for the six months ended June 30, 2011 and 74.45% for the same period in 2010.

Allowance for Loan Losses. The following table indicates key asset quality ratios that management evaluates on an ongoing basis. The unpaid principal balance of non-performing loans and non-performing assets was used in the calculation of amounts and ratios on the table below.

Asset Quality History
(In Thousands of Dollars)

	6/30/11	3/31/11	12/31/10	9/30/10	6/30/10
Nonperforming loans	$ 7,865	$ 11,011	$ 8,901	$ 9,207	$ 9,954
Nonperforming loans as a % of total loans	1.38%	1.91%	1.51%	1.52%	1.62%
Loans delinquent 30-89 days	3,758	3,392	7,924	5,888	5,652
Loans delinquent 30-89 days as a % of total loans	.66%	.59%	1.34%	.97%	.92%
Allowance for loan losses	$ 10,876	$ 10,137	$ 9,307	$ 7,785	$ 8,255
Allowance for loan losses as a % of loans	1.91%	1.76%	1.58%	1.28%	1.35%
Allowance for loan losses as a % of nonperforming loans	138.28%	92.06%	104.56%	84.56%	82.93%
Annualized net charge-offs to average net loans outstanding	.24%	.74%	.46%	1.31%	1.04%
Non-performing assets	8,664	11,867	9,433	9,533	10,099
Non-performing assets as a % of total assets	0.85%	1.17%	.96%	.90%	1.00%
Net charge-offs for the quarter	336	1,045	677	1,970	1,565

For six months ended June 30, 2011, management provided $3.0 million to the allowance for loan losses, a decrease of $1.4 million over the same six month period in the prior year. This 32% decrease is a result of improved credit quality, as net charge-offs have declined from $3.5 million for the first six months of 2010 to $1.4 million for the same period in 2011. There has also been a decline in the 30-89 day delinquencies, from $5.7 million at June 30, 2010 to $3.8 million at June 30, 2011. The ratio of nonperforming loans to total loans decreased from 1.62% at June 30, 2010 to 1.38% at June 30, 2011. Non-performing loans totaled $7.9 million at June 30, 2011, a decrease of

$2.1 million, compared to June 30, 2010. The decrease compared to the prior period is primarily related to lower levels of non-performing commercial and commercial real estate loans. On June 30, 2011, the ratio of the allowance for loan losses (ALLL) to non-performing loans was 138%, compared to 83% at June 30, 2010. At June 30, 2011, the ALLL/total loan ratio was 1.91% compared to 1.35% at June 30, 2010. This ALLL/total loan ratio s increase over the past twelve months is mainly the result of loan balances declining from $613.3 million at June 30, 2010 to $568.7 million at June 30, 2011. The residential and consumer portfolios have experienced some deterioration during the six month period ending June 30, 2011. In addition, real estate values have continued to depreciate, causing management to provide more to the ALLL.

For the three months ended June 30, 2011, management provided $1.1 million to the allowance for loan losses, a decrease of $800 thousand from the preceding quarter and a decrease of $525 thousand over the same three month period in the prior year. Net charge-offs for the quarter ending June 30, 2011 were $336 thousand compared to $1.0 million and $1.6 million for the first quarter of 2011 and the second quarter of 2010, respectively. The provision for loan losses exceeded net charge-offs for the three month period ended June 30, 2011 which is mainly due to an unusually high amount of recoveries during quarter ending June 30, 2011. Recoveries for the three month period ending June 30, 2011 were $699 thousand compared to $214 thousand and $125 thousand for the quarters ending March 31, 2011 and June 30, 2010, respectively.

Based on the evaluation of the adequacy of the allowance for loan losses, management believes that the allowance for loan losses at June 30, 2011 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 increased $9.0 million, or 1.18%, since December 31, 2010. Balances in the Company s non-interest bearing deposits increased $3.8 million, or 4.92%, between December 31, 2010 and June 30, 2011. Money market accounts also increased $8.4 million between December 31, 2010 and June 30, 2011. Time deposit accounts decreased $6.4 million, or 2.51%, during the six month period, as customers continued to move deposit dollars from time deposits 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 June 30, 2011, core deposits savings and money market accounts, time deposits less than $100,000 and demand deposits represented approximately 85% of total deposits.

Borrowings. Total borrowings increased $1.9 million, or 1.48%, since December 31, 2010. The increase in borrowings is the result of an increase in securities sold under repurchase agreements offset by a decrease in Federal Home Loan Bank (FHLB) advances. Repurchase agreements increased $3.1 million while federal home loan advances decreased $1.1 million during the first six months of 2011. The increase in repurchase agreements is due to an increase in public funds deposits and the decrease in FHLB advances is the result of normal pay down of the advances.

Capital Resources. Total stockholders equity increased from $88.0 million at December 31, 2010 to $108.6 million at June 30, 2011. The increase is a result of the successful completion by the Company of a 5,000,000 common share offering during January 2011, which injected approximately $14 million into the Company. The increase is also the result of net income and mark to market adjustments in the Company s investment securities partially offset by cash dividends paid to shareholders during the past twelve months. Shareholders received a $0.03 per share cash dividend on June 30, 2011 and a total of $0.06 per share cash dividends paid in the past two quarters. Book value per share decreased 9.9% from $6.45 per share at December 31, 2010 to $5.81 per share at June 30, 2011. This decrease is mainly the result of the sale of stock at less than book value.

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 June 30, 2011 the Company s total risk-based capital ratio stood at 16.94%, and the Tier I risk-based capital ratio and Tier I leverage ratio were at 15.65% and 9.41%, respectively. Management believes that the Company and the Bank meet all capital adequacy requirements to which they are subject, as of June 30, 2011.

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%. At June 30, 2011, the Bank is in compliance with these minimum capital requirements.

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 1 of the consolidated audited financial statements in the Company s Annual Report to Shareholders included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010. 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 the Company s 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 2010 consolidated financial statements, Note 1 (Summary of Significant Accounting Policies), Note 2 (Securities), Note 3 (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 the Company s 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 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, the 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 an approved line of credit at a major domestic bank. At June 30, 2011, this line of credited totaled $15.0 million and the Bank had not borrowed against this line. In addition, the Company has a $1.5 million revolving line of credit with a correspondent bank. The outstanding balance at June 30, 2011 was $1.1 million. Management feels that its liquidity position is adequate and continues to monitor the position on a monthly basis. As of June 30, 2011, the Bank had outstanding balances with the FHLB of Cincinnati of $23.4 million with additional borrowing capacity of approximately $77.6 million with the FHLB as well as access to the Federal Reserve Discount Window, which provides an additional source of funds. The 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 six months of 2011, net cash used by investing activities amounted to $24.7 million, compared to $17.5 million used in investing activities for the same period in 2010. Purchases of securities amounted to $63.3 million used during the first six months of 2011 compared to $39.0 million used during the same period in 2010. $19.8 million in net cash provided by loan originations and payments during the first six months of 2011, compared to $7.6 million used in loan originations and payments during the same period in 2010, accounted for a majority of the $7.3 million change in cash provided by investing activities. The cash provided by lending activities during this year s first six month period can be attributed to a reduction to the activity in the indirect, consumer real estate, and the commercial loan portfolios.

The primary financing activities of the Company are obtaining deposits, repurchase agreements and other borrowings. Net cash provided by financing activities amounted to $23.8 million for the first six months of 2011, compared to $7.3 million used by financing activities for the same period in 2010. $13.8 million of this change is a result of the issuance of the Company s common and treasury shares during the public offering during the first quarter of 2011. A smaller increase of $8.9 million in the short term borrowings category, compared to prior year, along with $9.0 million in cash provided by deposits in 2011 compared to $16.9 million in cash used for deposits in 2010 accounted for the remaining differences in financing activities.

Off-Balance Sheet Arrangements

In the normal course of business, to meet the financial needs of our customers, we are a party to financial instruments with off-balance sheet risk. These financial instruments generally include commitments to originate mortgage, commercial and consumer loans, and involve to varying degrees, elements of credit and interest rate risk in excess of amounts recognized in the Consolidated Balance Sheets. The Bank s maximum exposure to credit loss in the event of nonperformance by the borrower is represented by the contractual amount of those instruments. Because some commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The same credit policies are used in making commitments as are used for on-balance sheet instruments. Collateral is required in instances where deemed necessary. Undisbursed balances of loans closed include funds not disbursed but committed for construction projects. Unused lines of credit include funds not disbursed, but committed for, home equity, commercial and consumer lines of credit. Financial standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. Those guarantees are primarily used to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Total unused commitments were $82.8 million at June 30, 2011 and $68.3 million at December 31, 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 the new 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.

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 several 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.

Table of Contents

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)	**June 30, 2011 Result**	**December 31, 2010 Result**	**ALCO Guidelines**
Net Interest Income Change			
+200	-3.11%	-3.54%	15.00%
-200	-4.37%	-3.10%	15.00%
Net Present Value Of Equity Change			
+200	.89%	-2.24%	20.00%
-200	-34.87%	-32.08%	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 June 30, 2011 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 on Form 10-Q, the Company s Chief Executive Officer and Chief Financial Officer have concluded the Company 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 June 30, 2011, that have materially affected, or are reasonably likely to materially affect, the Company 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 have been no material changes to the Company s risk factors from those disclosed in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2010.

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 second quarter of 2011.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. (Removed and Reserved).

Item 5. Other Information

Not applicable.

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 the Company 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. (filed herewith).
10.1	Farmers National Banc Corp. Form of Indemnification Agreement (incorporated by reference from Exhibit 10.1 to the Company s Current Report on Form 8-K filed with the SEC on April 29, 2011).
10.2	Farmers National Banc Corp. Cash Incentive Plan (incorporated by reference from Exhibit 10.1 to the Company s Current Report on Form 8-K filed with the SEC on June 24, 2011).
10.3	Farmers National Banc Corp. Long-Term Incentive Plan (incorporated by reference from Exhibit 10.1 to the Company s Current Report on Form 8-K filed with the SEC on June 29, 2011).

10.4	Retirement Agreement by and between Farmers National Banc Corp., the Farmers National Bank of Canfield and Frank L. Paden (incorporated by reference from Exhibit 10.2 to the Company s Current Report on Form 8-K filed with the SEC on June 29, 2011).
31.1	Rule 13a-14(a)/15d-14(a) Certification of John S. Gulas, President and Chief Executive Officer of the Company (filed herewith).
31.2	Rule 13a-14(a)/15d-14(a) Certification of Carl D. Culp, Executive Vice President, Chief Financial Officer and Treasurer of the Company (filed herewith).
32.1	Certification pursuant to 18 U.S.C. Section 1350 of John S. Gulas, President and Chief Executive Officer of the Company (filed herewith).
32.2	Certification pursuant to 18 U.S.C. Section 1350 of Carl D. Culp, Executive Vice President, Chief Financial Officer and Treasurer of the Company (filed herewith).
101*	The following materials from the Company s Quarterly Report on Form 10-Q for the quarter ended June 30, 2011, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Balance Sheets; (ii) the Consolidated Statements of Income and Comprehensive Income; (iii) the Consolidated Statements of Cash Flows; and (iv) Notes to Consolidated Financial Statements, tagged as blocks of text.

* As provided in Rule 406T of Regulation S-T, this information shall not be deemed filed for purposes of Section 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934 or otherwise subject to liability under those sections.

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: August 9, 2011

/s/John S. Gulas

John S. Gulas
President and Chief Executive Officer

Dated: August 9, 2011

/s/Carl D. Culp

Carl D. Culp
Executive Vice President and Treasurer