

Hamilton Bancorp, Inc.
Form 10-Q
August 15, 2016
Table Of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2016

OR

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

For the transition period from _____ to _____

Commission File No. 001-35693

Hamilton Bancorp, Inc.

(Exact name of registrant as specified in its charter)

Maryland

(State or other jurisdiction of
incorporation or organization)

46-0543309

(I.R.S. Employer
Identification Number)

501 Fairmount Avenue, Suite 200, Towson, Maryland

(Address of Principal Executive Offices)

21286

Zip Code

(410) 823-4510

(Registrant's telephone number)

N/A

(Former name or former address, 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 requirements for the past 90 days.

YES] NO]

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

YES] NO]

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

Large accelerated filer]

Accelerated filer]

Non-accelerated filer]

Smaller reporting company]

(Do not check if smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES] NO]

3,413,646 shares of the Registrant's common stock, par value \$0.01 per share, were issued and outstanding as of August 15, 2016.

Table Of Contents

Hamilton Bancorp, Inc. and Subsidiaries

Form 10-Q

Index

	<u>Page</u>
Part I. Financial Information	
Item 1. <u>Financial Statements</u>	
<u>Consolidated Statements of Financial Condition as of June 30, 2016 (unaudited) and March 31, 2016</u>	1
<u>Consolidated Statements of Operations for the Three Months Ended June 30, 2016 and 2015 (unaudited)</u>	2
<u>Consolidated Statements of Comprehensive Income for the Three Months Ended June 30, 2016 and 2015 (unaudited)</u>	3
<u>Consolidated Statements of Changes in Shareholders' Equity for the Three Months Ended June 30, 2016 and 2015 (unaudited)</u>	4
<u>Consolidated Statements of Cash Flows for the Three Months Ended June 30, 2016 and 2015 (unaudited)</u>	5 - 6
<u>Notes to Consolidated Financial Statements (unaudited)</u>	7 – 37
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	38 – 55
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	55
Item 4. <u>Controls and Procedures</u>	55
Part II. Other Information	
Item 1. <u>Legal Proceedings</u>	56
Item 1A. <u>Risk Factors</u>	56
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	56

Item 3.	<u>Defaults upon Senior Securities</u>	56
Item 4.	<u>Mine Safety Disclosures</u>	57
Item 5.	<u>Other Information</u>	57
Item 6.	<u>Exhibits</u>	57
	<u>Signatures</u>	57

Table Of Contents**Part I. – Financial Information****Item 1. Financial Statements****HAMILTON BANCORP, INC AND SUBSIDIARY****Consolidated Statements of Financial Condition****June 30, 2016 and March 31, 2016**

	June 30,	March 31,
	2016	2016
	(Unaudited)	(Audited)
Assets		
Assets		
Cash and due from banks	\$51,189,015	\$47,101,688
Federal funds sold	13,647,738	20,346,848
Cash and cash equivalents	64,836,753	67,448,536
Certificates of deposit held as investment	3,726,067	3,968,229
Securities available for sale, at fair value	80,523,378	70,484,400
Federal Home Loan Bank stock, at cost	1,640,100	1,042,500
Loans held for sale	-	259,450
Loans and leases, net of unearned income	331,438,194	221,859,056
Allowance for loan losses	(1,896,972)	(1,702,365)
Net loans and leases	329,541,222	220,156,691
Premises and equipment, net	4,284,327	3,555,474
Premises and equipment held for sale	405,000	405,000
Foreclosed real estate	460,780	443,015
Accrued interest receivable	1,388,315	948,166
Bank-owned life insurance	17,880,474	12,709,908
Deferred income taxes	5,141,277	2,353,141
Income taxes refundable	228,920	228,920
Goodwill and other intangible assets	10,655,873	7,386,111
Other assets	2,051,298	1,527,014
Total Assets	\$522,763,784	\$392,916,555
Liabilities and Shareholders' Equity		
Liabilities		

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Noninterest-bearing deposits	\$22,132,850	\$19,747,437
Interest-bearing deposits	403,391,490	294,246,214
Total deposits	425,524,340	313,993,651
Borrowings	28,487,127	14,805,237
Advances by borrowers for taxes and insurance	3,069,417	1,079,794
Other liabilities	4,019,560	1,493,290
Total liabilities	461,100,444	331,371,972
Commitments and contingencies	-	-
Shareholders' Equity		
Common stock, \$.01 par value, 100,000,000 shares authorized. Issued: 3,413,646 shares at June 30, 2016 and March 31, 2016	34,136	34,136
Additional paid in capital	31,351,459	31,242,731
Retained earnings	32,324,247	32,659,455
Unearned ESOP shares	(2,369,920)	(2,369,920)
Accumulated other comprehensive income (loss)	323,418	(21,819)
Total shareholders' equity	61,663,340	61,544,583
Total Liabilities and Shareholders' Equity	\$522,763,784	\$392,916,555

The accompanying notes are an integral part of these consolidated financial statements.

Table Of Contents**HAMILTON BANCORP, INC AND SUBSIDIARY****Consolidated Statements of Operations (Unaudited)****Three Months Ended June 30, 2016 and 2015**

	Three Months Ended	
	June 30,	
	2016	2015
Interest revenue		
Loans, including fees	\$3,316,673	\$1,940,608
U.S. treasuries, government agencies and FHLB stock	86,574	96,708
Municipal and corporate bonds	49,026	34,806
Mortgage-backed securities	231,497	297,594
Federal funds sold and other bank deposits	66,706	5,263
Total interest revenue	3,750,476	2,374,979
Interest expense		
Deposits	611,812	372,444
Borrowed funds	42,072	4,953
Total interest expense	653,884	377,397
Net interest income	3,096,592	1,997,582
Provision for loan losses	210,000	-
Net interest income after provision for loan losses	2,886,592	1,997,582
Noninterest revenue		
Service charges	95,120	95,078
Gain on sale of loans held for sale	11,172	16,998
Gain on sale of property and equipment	-	407,188
Earnings on bank-owned life insurance	112,526	87,742
Other	50,680	22,997
Total noninterest revenue	269,498	630,003
Noninterest expenses		
Salaries	1,430,939	938,239
Employee benefits	349,334	261,837
Occupancy	215,900	174,626
Advertising	31,351	27,363
Furniture and equipment	98,323	78,440
Data processing	185,723	141,988
Legal services	50,263	22,179

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Other professional services	100,098	87,422
Merger related expenses	236,484	230,785
Branch consolidation expense	437,424	-
Deposit insurance premiums	77,200	49,864
Foreclosed real estate expense and losses	8,108	808
Other operating	487,952	309,423
Total noninterest expense	3,709,099	2,322,974
(Loss) income before income taxes	(553,009)	304,611
Income tax (benefit) expense	(217,801)	186,288
Net (loss) income	\$(335,208)	\$118,323
Net (loss) income per common share:		
Basic	\$(0.11)	\$0.04
Diluted	\$(0.11)	\$0.04

The accompanying notes are an integral part of these consolidated financial statements.

Table Of Contents**HAMILTON BANCORP, INC AND SUBSIDIARY****Consolidated Statements of Comprehensive Income (Loss) (Unaudited)****Three Months Ended June 30, 2016 and 2015**

	Three Months Ended	
	June 30,	
	2016	2015
Net income (loss)	\$(335,208)	\$118,323
Other comprehensive income (loss):		
Unrealized gain (loss) on investment securities available for sale	570,123	(1,200,479)
Reclassification adjustment for realized gain on investment securities available for sale included in net income	-	-
Total unrealized gain (loss) on investment securities available for sale	570,123	(1,200,479)
Income tax expense (benefit) relating to investment securities available for sale	224,886	(473,529)
Other comprehensive income (loss)	345,237	(726,950)
Total comprehensive income (loss)	\$10,029	\$(608,627)

The accompanying notes are an integral part of these consolidated financial statements.

Table Of Contents**HAMILTON BANCORP, INC AND SUBSIDIARY****Consolidated Statements of Changes in Shareholders' Equity (Unaudited)****Three Months Ended June 30, 2016 and 2015**

	Common stock	Additional paid-in capital	Retained earnings	Unearned ESOP shares	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balances March 31, 2015	\$ 34,177	\$ 30,832,815	\$ 32,752,071	\$(2,518,040)	\$(301,315)	) \$ 60,799,708
Net income	-	-	118,323	-	-	) 118,323
Unrealized loss on available for sale securities, net of tax effect of \$473,529	-	-	-	-	(726,950)	) (726,950)
Stock based compensation - options	-	52,302	-	-	-	) 52,302
Stock based compensation - restricted stock	-	56,147	-	-	-	) 56,147
Balances June 30, 2015	\$ 34,177	\$ 30,941,264	\$ 32,870,394	\$(2,518,040)	\$(1,028,265)	) \$ 60,299,530
Balance March 31, 2016	\$ 34,136	\$ 31,242,731	\$ 32,659,455	\$(2,369,920)	\$(21,819)	) \$ 61,544,583
Net loss	-	-	(335,208)	-	-	) (335,208)
Unrealized gain on available for sale securities, net of tax effect of \$224,886	-	-	-	-	345,237	) 345,237
Stock based compensation - options	-	52,302	-	-	-	) 52,302
Stock based compensation - restricted stock	-	56,426	-	-	-	) 56,426
Balance June 30, 2016	\$ 34,136	\$ 31,351,459	\$ 32,324,247	\$(2,369,920)	\$ 323,418	) \$ 61,663,340

The accompanying notes are an integral part of these consolidated financial statements.

Table Of Contents**HAMILTON BANCORP, INC AND SUBSIDIARY****Consolidated Statements of Cash Flows (Unaudited)****Three Months Ended June 30, 2016 and 2015**

	Three Months Ended	
	June 30,	
	2016	2015
Cash flows from operating activities		
Interest received	\$3,520,057	\$2,560,794
Fees and commissions received	145,801	526,071
Interest paid	(742,098)	(377,634)
Cash paid to suppliers and employees	(2,422,853)	(2,547,248)
Origination of loans held for sale	(675,000)	(1,095,650)
Proceeds from sale of loans held for sale	945,622	1,433,104
Income taxes paid	(1,735,421)	-
Net cash (used) provided by operating activities	(963,892)	499,437
Cash flows from investing activities		
Acquisition, net of cash acquired	(11,006,813)	-
Proceeds from maturing and called securities available for sale, including principal pay downs	7,968,235	5,252,100
Proceeds from maturing and called certificates of deposit	735,000	-
Purchase of Federal Home Loan Bank stock	185,000	-
Loans made, net of principal repayments	(1,121,745)	(9,360,001)
Purchase of premises and equipment	(75,953)	(46,282)
Proceeds from sale of foreclosed real estate	-	11,752
Proceeds from sale of premises and equipment	35,000	500,000
Net cash used by investing activities	(3,281,276)	(3,642,431)
Cash flows from financing activities		
Net increase in		
Deposits	1,643,762	731,214
Advances by borrowers for taxes and insurance	1,989,623	351,911
Proceeds from borrowings	-	2,000,000
Payments of borrowings	(2,000,000)	(2,000,000)
Net cash provided by financing activities	1,633,385	1,083,125
Net decrease in cash and cash equivalents	(2,611,783)	(2,059,869)
Cash and cash equivalents at beginning of period	67,448,536	16,643,888

Cash and cash equivalents at end of period	\$64,836,753	\$14,584,019
Supplemental Disclosures of Cash Flow Information:		
Total cash consideration paid for Fraternity Acquisition	\$25,704,871	\$-
Less cash acquired	14,698,058	-
Acquisition, net of cash acquired	\$11,006,813	\$-

The accompanying notes are an integral part of these consolidated financial statements.

Table Of Contents**HAMILTON BANCORP, INC AND SUBSIDIARY****Consolidated Statements of Cash Flows (Unaudited)****(Continued)**

	Three Months Ended	
	June 30,	
	2016	2015
Reconciliation of net (loss) income to net cash (used) provided by operating activities		
Net (loss) income	\$(335,208)	\$ 118,323
Adjustments to reconcile net (loss) income to net cash (used) provided by operating activities		
Amortization of premiums on securities	133,622	114,077
Amortization of premiums on certificates of deposit	5,162	-
Loan premium amortization	38,352	6,883
Deposit premium amortization	(102,183)	-
Borrowing premium amortization	(111,647)	-
Core deposit intangible asset amortization	26,474	7,250
Premises and equipment depreciation and amortization	81,906	60,083
Gain on disposal of premises and equipment	-	(407,188)
Loss on sale of foreclosed real estate		808
Stock based compensation	108,729	108,449
Provision for loan losses	210,000	-
Decrease (increase) in		
Accrued interest receivable	(440,149)	62,533
Loans held for sale	259,450	320,456
Cash surrender value of life insurance	(112,525)	(87,742)
Income taxes refundable and deferred income taxes	(1,953,222)	186,288
Other assets	2,446,605	180,314
Increase (decrease) in		
Accrued interest payable	125,616	(237)
Deferred loan origination fees	32,594	2,322
Other liabilities	(1,377,468)	(173,182)
Net cash (used) provided by operating activities	\$(963,892)	\$499,437
Noncash investing activity		
Real estate acquired through foreclosure	\$17,765	\$-

The accompanying notes are an integral part of these consolidated financial statements.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Form 10-Q

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2016

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Hamilton Bancorp, Inc. (the “Company”) was incorporated on September 7, 2012 to serve as the stock holding company for Hamilton Bank (the “Bank”), a federally chartered savings bank. On October 10, 2012, in accordance with a Plan of Conversion adopted by its Board of Directors and approved by its members, the Bank converted from a mutual savings bank to a stock savings bank and became the wholly owned subsidiary of the Company. In connection with the conversion, the Company sold 3,703,000 shares of common stock at a price of \$10.00 per share, through which the Company received proceeds of approximately \$35,580,000, net of offering expenses of approximately \$1,450,000. In addition, the Bank’s Board of Directors adopted an employee stock ownership plan (the “ESOP”) which subscribed for 8.0% of shares sold in the offering, or 296,240 common shares. The purchase of shares by the ESOP was funded by a loan from the Company.

In accordance with Office of the Comptroller of the Currency (the “OCC”) regulations, upon the completion of the conversion, the Bank restricted retained earnings by establishing a liquidation account. The liquidation account will be maintained for the benefit of eligible account holders who continue to maintain their accounts at the Bank after conversion. The liquidation account will be reduced annually to the extent that eligible account holders have reduced their qualifying deposits. Subsequent increases will not restore an eligible account holder’s interest in the liquidation account. In the event of a complete liquidation of the Bank, and only in such event, each account holder will be entitled to receive a distribution from the liquidation account in an amount proportionate to the adjusted qualifying account balances then held. The Bank may not pay dividends if those dividends would reduce equity capital below the required liquidation account amount.

On May 13, 2016, the Company completed its acquisition of Fraternity Community Bancorp, Inc. (“Fraternity”) through the merger of Fraternity, the parent company of Fraternity Federal Savings and Loan, with and into the Company

pursuant to the Agreement and Plan of Merger dated as of October 12, 2015, by and between the Company and Fraternity. As a result of the merger, each shareholder of Fraternity received a cash payment equal to nineteen dollars and twenty-five cents (\$19.25) for each share of Fraternity common stock, or an aggregate of approximately \$25.7 million. Immediately following the merger of Fraternity into the Company, Fraternity Federal Savings and Loan was merged with and into the Bank, with the Bank the surviving bank.

On September 11, 2015, the Company completed its acquisition of Fairmount Bancorp, Inc. (“Fairmount”) through the merger of Fairmount, the parent company of Fairmount Bank, with and into the Company pursuant to the Agreement and Plan of Merger dated as of April 15, 2015, by and between the Company and Fairmount. As a result of the merger, each shareholder of Fairmount received a cash payment equal to thirty dollars (\$30.00) for each share of Fairmount common stock, or an aggregate of approximately \$14.2 million. Immediately following the merger of Fairmount into the Company, Fairmount Bank was merged with and into the Bank, with the Bank the surviving entity.

Hamilton Bancorp is a holding company that operates a community bank with 7 branches in the Baltimore-metropolitan area. Its primary deposit products are certificates of deposit and demand, savings, NOW, and money market accounts. Its primary lending products consist of real estate mortgages, along with commercial and consumer loans. Hamilton Bancorp’s primary source of revenue is derived from loans to customers, who are predominately small and middle-market business and middle-income individuals.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial reporting and with instructions for Form 10-Q and Regulation S-X as promulgated by the Securities and Exchange Commission (the “SEC”). Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the preceding unaudited consolidated financial statements contain all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the financial condition and results of operations for the periods presented. We derived the balances as of March 31, 2016 from audited financial statements. Operating results for the three months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ending March 31, 2017, or any other period. For further information, refer to the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended March 31, 2016. Certain amounts from prior period financial statements have been reclassified to conform to the current period’s presentation.

Summary of Significant Accounting Policies

The accounting and reporting policies of Hamilton Bancorp, Inc. and Subsidiary (“Hamilton”) conform to accounting principles generally accepted in the United States of America (“U.S. GAAP”) and to general practices in the banking industry. The more significant policies follow:

Principles of Consolidation. The accompanying consolidated financial statements include the accounts of the parent company and its wholly owned subsidiary, Hamilton Bank. All significant intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, deferred income tax valuation allowances, the fair value of investment securities and other temporary impairment of investment securities.

Loans Receivable. The Bank makes mortgage, commercial, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout the Baltimore metropolitan area. The ability of the Bank's debtors to repay their loans is dependent upon the real estate and general economic conditions in this area.

Loans are reported at their outstanding unpaid principal balance adjusted for the allowance for loan loss, premiums on loans acquired, and/or any deferred fees or costs on originated loans. Interest revenue is accrued on the unpaid principal balance. Loan origination fees and the direct costs of underwriting and closing loans are recognized over the life of the related loan as an adjustment to yield using a method that approximates the interest method. Any differences that arise from prepayment will result in a recalculation of the effective yield.

Loans are generally placed on nonaccrual status when they are 90 days past due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual status at an earlier date if the collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual status are reversed against interest revenue. The interest on nonaccrual loans is accounted for on the cash basis method, until the loans qualify for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and, in management's judgment, future payments are reasonably assured.

Loans are considered impaired when, based on current information, management considers it unlikely that collection of principal and interest payments will be made according to contractual terms. If collection of principal is evaluated as doubtful, all payments are applied to principal. Impaired loans are measured: (i) at the present value of expected cash flows discounted at the loan's effective interest rate; (ii) at the observable market price; or (iii) at the fair value of the collateral if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, an impairment is recognized through an allocation of the allowance for loan losses and corresponding provision for loan losses. Generally, identified impairments are charged-off against the allowance for loan losses.

Troubled debt restructurings are loans for which Hamilton, for legal or economic reasons related to a debtor's financial difficulties, has granted a concession to the debtor that it otherwise would not have considered. Concessions that result in the categorization of a loan as a troubled debt restructuring include:

Reduction of the stated interest rate;

Extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk;

Reduction of the face amount or maturity amount of the debt as stated in the instrument or other agreement; or

Reduction of accrued interest

Accounting for Certain Loans or Debt Securities Acquired in a Transfer. The loans acquired from the Company's acquisition of Fraternity on May 13, 2016 (see Note 3 "Acquisition of Fraternity Community Bancorp, Inc.") were recorded at fair value at the acquisition date and no separate valuation allowance was established. The initial fair values were determined by management, with the assistance of an independent valuation specialist, based on estimated expected cash flows discounted at appropriate rates. The discount rates were based on market rates for new originations of comparable loans and did not include a separate factor for loan losses as that was included in the estimated cash flows.

Accounting Standards Codification ("ASC") Topic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*, applies to loans acquired in a transfer with evidence of deterioration of credit quality for which it is probable, at acquisition, that the investor will be unable to collect all contractually required payments receivable. If both conditions exist, the Company determines whether to account for each loan individually or whether such loans will be assembled into pools based on common risk characteristics such as credit score, loan type, and origination date.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The Company considered expected prepayments and estimated the total expected cash flows, which included undiscounted expected principal and interest. The excess of that amount over the fair value of the loan is referred to as accretable yield. Accretable yield is recognized as interest income on a constant yield basis over the expected life of the loan. The excess of the contractual cash flows over expected cash flows is referred to as nonaccretable difference and is not accreted into income. Over the life of the loan, the Company continues to estimate expected cash flows. Subsequent decreases in expected cash flows are recognized as impairments in the current period through the allowance for loan losses. Subsequent increases in cash flows to be collected are first used to reverse any existing valuation allowance and any remaining increase are recognized prospectively through an adjustment of the loan's yield over its remaining life.

ASC Topic 310-20, *Nonrefundable Fees and Other Costs*, was applied to loans not considered to have deteriorated credit quality at acquisition. Under ASC Topic 310-20, the difference between the loan's principal balance at the time of purchase and the fair value is recognized as an adjustment of yield over the life of the loan.

Allowance for Loan Losses. The allowance for loan losses represents an amount which, in management's judgment, will be adequate to absorb probable future losses on existing loans. The allowance for loan losses is established, as loan losses are estimated to have occurred, through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Recoveries on previously charged-off loans are credited to the allowance for loan losses.

The allowance for loan losses is increased by provisions charged to income and reduced by charge-offs, net of recoveries. Management's periodic evaluation of the adequacy of the allowance is based on the Bank's past loan loss experience, known and inherent risks in the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and current economic conditions. The look back period for historical losses consists of reviewing both a 36 and 48 month look back period for net charge-offs. Both of these periods are used individually to develop a range in which the allowance for loan losses should be within.

Management considers a number of factors in estimating the required level of the allowance. These factors include: historical loss experience in the loan portfolios; the levels and trends in past-due and nonaccrual loans; the status of nonaccrual loans and other loans identified as having the potential for further deterioration; credit risk and industry concentrations; trends in loan volume; the effects of any changes in lending policies and procedures or underwriting standards; and a continuing evaluation of the economic environment.

Accumulated Other Comprehensive Income. The Bank records unrealized gains and losses on available for sale securities in accumulated other comprehensive income, net of taxes. Unrealized gains and losses on available for sale securities are reclassified into earnings as the gains or losses are realized upon sale of the securities. The credit component of unrealized losses on available for sale securities that are determined to be other-than-temporarily impaired are reclassified into earnings at the time the determination is made.

Stock Based Compensation. Compensation cost is recognized for stock options and restricted stock awards issued to employees and directors, based on the fair value of these awards at the date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options, while the market price of the Company's common stock at the date of grant is used for restricted stock awards. Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.

Note 2: New Accounting Pronouncements

Recent Accounting Pronouncements

ASU 2016-13, Financial Instruments – Credit Losses. The ASU sets forth a “current expected credit loss” (CECL) model which requires the Company to measure all expected credit losses for financial instruments held at the reporting date based on historical experience, current conditions and reasonable supportable forecasts. This replaces the existing incurred loss model and is applicable to the measurement of credit losses on financial assets measured at amortized cost and applies to some off-balance sheet credit exposures. This ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently assessing the impact of the adoption of this ASU on its consolidated financial statements.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

ASU 2016-09, Improvements to Employee share-Based Payment Accounting (Topic 718). This ASU includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. Some of the key provisions of this new ASU include: (1) companies will no longer record excess tax benefits and certain tax deficiencies in additional paid-in capital (“APIC”). Instead, they will record all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement, and APIC pools will be eliminated. The guidance also eliminates the requirement that excess tax benefits be realized before companies can recognize them. In addition, the guidance requires companies to present excess tax benefits as an operating activity on the statement of cash flows rather than as a financing activity; (2) increase the amount an employer can withhold to cover income taxes on awards and still qualify for the exception to liability classification for shares used to satisfy the employer’s statutory income tax withholding obligation. The new guidance will also require an employer to classify the cash paid to a tax authority when shares are withheld to satisfy its statutory income tax withholding obligation as a financing activity on its statement of cash flows (current guidance did not specify how these cash flows should be classified); and (3) permit companies to make an accounting policy election for the impact of forfeitures on the recognition of expense for share-based payment awards. Forfeitures can be estimated, as required today, or recognized when they occur. ASU No. 2016-09 is effective for interim and annual reporting periods beginning after December 15, 2016. Early adoption is permitted, but all of the guidance must be adopted in the same period. The Company is currently evaluating the provisions of ASU No. 2016-09 to determine the potential impact the new standard will have on the Company's Consolidated Financial Statements.

ASU 2016-02, Leases (Topic 842). This ASU guidance requires lessees to recognize lease assets and lease liabilities related to certain operating leases on the balance sheet by lessees and disclose key information about leasing arrangements. This guidance is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. The Company is currently evaluating this guidance to determine the impact on its consolidated financial statements.

ASU No. 2016-01, Financial Instruments – Recognition and Measurement of Financial Assets and Liabilities. This ASU requires equity investments to be measured at fair value with changes in fair value recognized in net income, excluding equity investments that are consolidated or accounted for under the equity method of accounting. The amendment allows equity investments without readily determinable fair values to be measured at cost minus impairment, with a qualitative assessment required to identify impairment. The amendment also requires public companies to use exit prices to measure the fair value of financial instruments purposes; requiring separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statement; it eliminates the disclosure requirements related to measurement assumptions for the fair value of instruments measured at amortized cost. In addition, for liabilities

measured at fair value under the fair value option, to present in other comprehensive income changes in fair value due to changes in instrument specific credit risk. ASU No. 2016-01 is effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. The Company is currently evaluating the impact of adopting the new guidance on its consolidated financial statements.

ASU No. 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period

Adjustments. This update eliminates the requirement to retrospectively adjust the provisional amounts recognized at the acquisition date with a corresponding adjustment to goodwill. These adjustments are required when new information is obtained about facts and circumstances that existed as of the acquisition date that if known, would have affected the measurement of the amounts initially recognized or would have resulted in the recognition of additional assets or liabilities. The update also requires the nature of and reason for the business combination, to be disclosed in the consolidated financial statements. ASU 2015-16 became effective for fiscal years beginning after December 15, 2015, and were not material to the consolidated financial statements. All measurement period adjustments related to the acquisition of Fairmount were recorded in the period in which the adjustments were determined.

ASU 2014-09, Revenue from Contracts with Customers (Topic 606). ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective on January 1, 2017 and is not expected to have a significant impact on our financial statements.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Note 3: Acquisitions

Fraternity Community Bancorp, Inc.

On May 13, 2016, Hamilton Bancorp acquired Fraternity Community Bancorp, Inc. (“Fraternity”), the parent company of Fraternity Federal Savings and Loan. Under the terms of the Merger Agreement, shareholders of Fraternity received a cash payment equal to nineteen dollars and twenty-five cents (\$19.25) for each share of Fraternity common stock. The total merger consideration was \$25.7 million.

In connection with the acquisition, Fraternity Federal Savings and Loan was merged with and into Hamilton Bank, with Hamilton Bank as the surviving bank. The results of the Fraternity acquisition are included with Hamilton’s results as of and from May 13, 2016.

As required by the acquisition method of accounting, we have adjusted the acquired assets and liabilities of Fraternity to their estimated fair value on the date of acquisition and added them to those of Hamilton Bancorp. Based on management’s preliminary valuation of the fair value of tangible and intangible assets acquired and liabilities assumed, which we have based on level 3 valuation estimates and assumptions that are subject to change, we have allocated the preliminary purchase price for Fraternity as follows:

	As recorded by Fraternity Community Bancorp, Inc.	Fair Value Adjustments	As recorded by Hamilton Bancorp, Inc.
Identifiable assets:			
Cash and cash equivalents	\$ 15,196,058	\$ -	\$ 15,196,058

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Investment securities available for sale	17,570,712	-		17,570,712
FHLB Bank Stock	782,600	-		782,600
Loans	108,872,041	(310,544	) A	108,561,497
Allowance For Loan Loss	(1,550,000	)	1,550,000	A -
Premises and equipment	691,095	78,711	B	769,806
Bank-Owned Life Insurance	5,058,041	-		5,058,041
Deferred income taxes	1,470,177	(410,377	) C	1,059,800
Other assets	2,877,665	-		2,877,665
Total identifiable assets	\$ 150,968,389	\$ 907,790		\$ 151,876,179
Identifiable liabilities:				
Non-interest bearing deposits	1,242,187	-		1,242,187
Interest bearing deposits	107,648,792	1,098,131	D	108,746,923
Borrowings	15,000,000	793,537	E	15,793,537
Other liabilities	3,778,122	-		3,778,122
Total identifiable liabilities	\$ 127,669,101	\$ 1,891,668		\$ 129,560,769
Net tangible assets acquired	23,299,288	(983,878	)	22,315,410
Definite lived intangible assets acquired	-	242,020		242,020
Goodwill	-	3,147,441		3,147,441
Net intangible assets acquired	-	3,389,461		3,389,461
Total cash consideration	\$ 23,299,288	\$ 2,405,583		\$ 25,704,871

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Explanation of fair value adjustments:

- A - Adjustment reflects the fair value adjustments based on Hamilton Bancorp's evaluation of the acquired loan portfolio and excludes the allowance for losses recorded by Fraternity Community Bancorp, Inc.
- B - Adjustment reflects the fair value adjustments based on Hamilton Bancorp's evaluation of the acquired premises and equipment.
- C - Adjustment to record deferred tax asset related to fair value adjustments at 39.45% income tax rate.
- D - Adjustment arises since the rates on interest-bearing deposits are higher than rates available on similar deposits as of the acquisition date.
- E - Adjustment reflects the fair value of Fraternity's borrowings acquired on acquisition date.

Prior to the end of the measurement period, if information becomes available which indicates the purchase price allocations require adjustments, we will include such adjustments in the purchase price allocation retrospectively.

Of the total estimated purchase price, we have allocated an estimate of \$22.3 million to net tangible assets acquired and we have allocated \$242,020 to the core deposit intangible which is a definite lived intangible asset. We have allocated the remaining purchase price to goodwill, which is deductible for income tax purposes. We will amortize the core deposit intangible on a straight-line basis over its estimated useful life of 8 years. We will evaluate goodwill annually for impairment.

Pro forma Condensed Combined Financial Information. The following schedule includes consolidated statements of operations data for the unaudited pro forma results for the three month periods ended June 30, 2016 and 2015 as if the Fraternity acquisition had occurred as of the beginning of the periods presented.

	Three Months Ended June 30,	
	2016	2015
Net interest income	\$3,764,707	\$3,309,172
Other non-interest revenue	266,058	686,489

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Total revenue	4,030,765	3,995,661
Provision expense	210,000	-
Other non-interest expense	3,538,536	3,390,202
Income before income taxes	282,229	605,459
Income tax expense	93,301	224,127
Net income	\$188,928	\$381,332
Basic earning per share	\$0.06	\$0.12
Diluted earnings per share	\$0.06	\$0.12

We have not included any provision for loan losses during the period for loans acquired from Fraternity. In accordance with accounting for business combinations, we included the credit losses evident in the loans in the determination of the fair value of loans at the date of acquisition and eliminated the allowance for loan losses maintained by Fraternity at acquisition date. Also excluded are an estimated \$3.0 million in merger related expenses associated with completing the actual acquisition. This expense includes expenses incurred by both the buyer and the seller.

We have presented the pro forma financial information for illustrative purposes only and it is not necessarily indicative of the financial results of the combined companies if we had actually completed the acquisition at the beginning of the periods presented, nor does it indicate future results for any other interim or full year period. Pro forma basic and diluted earnings per common share were calculated using Hamilton Bancorp's actual weighted average shares outstanding for the periods presented, assuming the acquisition occurred at the beginning of the periods presented.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The following table outlines the contractually required payments receivable, cash flows we expect to receive, non-accretable credit adjustments and the accretable yield for all Fraternity loans as of the acquisition date.

	Contractually Required Payments Receivable	Non-Accretable Credit Adjustments	Cash Flows Expected To Be Collected	Accretable FMV Adjustments	Carrying Value of Loans Receivable
Performing loans acquired	\$ 107,474,993	\$ -	\$ 107,474,993	\$ 58,986	\$ 107,533,979
Impaired loans acquired	1,397,048	(314,484)	1,082,564	(55,046)	1,027,518
Total	\$ 108,872,041	\$ (314,484)	\$ 108,557,557	\$ 3,940	\$ 108,561,497

At our acquisition of Fraternity, we recorded all loans acquired at the estimated fair value on the purchase date with no carryover of the related allowance for loan losses. On the acquisition date, we segregated the loan portfolio into two loan pools, performing and nonperforming loans, to be retained in our portfolio.

We had an independent third party determine the fair value of cash flows on \$107,474,993 of performing loans. The valuation took into consideration the loans' underlying characteristics, including account types, remaining terms, annual interest rates, interest types, past delinquencies, timing of principal and interest payments, current market rates, loan to value ratios, loss exposures, and remaining balances. These performing loans were segregated into pools based on loan and payment type and in some cases, risk grade. The effect of this fair valuation process was a net accretable premium adjustment of \$58,986 at acquisition.

We also individually evaluated 23 impaired loans totaling \$1,397,048 to determine the fair value as of the May 13, 2016 measurement date. In determining the fair value for each individually evaluated impaired loan, we considered a

number of factors including the remaining life of the acquired loans, estimated prepayments, estimated loss ratios, estimated value of the underlying collateral and net present value of cash flows we expect to receive, among others.

We established a credit risk related non-accretable difference of \$314,484 relating to these acquired, credit impaired loans, reflected in the recorded net fair value. We further estimated the timing and amount of expected cash flows in excess of the estimated fair value and established an accretable discount adjustment of \$55,046 at acquisition relating to these impaired loans.

Fairmount Bancorp, Inc.

On September 11, 2015, Hamilton Bancorp acquired Fairmount Bancorp, Inc. (“Fairmount”), the parent company of Fairmount Bank. Under the terms of the Merger Agreement, shareholders of Fairmount received a cash payment equal to thirty dollars (\$30.00) for each share of Fairmount common stock. The total merger consideration was \$14.2 million.

In connection with the acquisition, Fairmount Bank was merged with and into Hamilton Bank, with Hamilton Bank as the surviving bank. The results of the Fairmount acquisition are included with Hamilton’s results as of and from September 11, 2015.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

As required by the acquisition method of accounting, we have adjusted the acquired assets and liabilities of Fairmount to their estimated fair value on the date of acquisition and added them to those of Hamilton Bancorp. Based on management's preliminary valuation of the fair value of tangible and intangible assets acquired and liabilities assumed, which we have based on level 3 valuation estimates and assumptions that are subject to change, we have allocated the preliminary purchase price for Fairmount as follows:

	As recorded by	Fair Value Adjustments		As recorded by
	Fairmount Bancorp, Inc.			Hamilton Bancorp, Inc.
Identifiable assets:				
Cash and cash equivalents	\$1,468,499	\$-		\$1,468,499
Certificates of deposit	4,467,825	27,772	A	4,495,597
Investment securities available for sale	9,729,405	-		9,729,405
Loans	55,454,414	(1,876,502)	B	53,577,912
Allowance For Loan Loss	(591,070)	591,070	B	-
Premises and equipment	2,975,587	(726,997)	C	2,248,590
Core Deposit Intangible	22,802	(22,802)	D	-
Deferred income taxes	976,956	596,675	E	1,573,631
Other assets	1,031,755	-		1,031,755
Total identifiable assets	\$75,536,173	\$(1,410,784)		\$74,125,389
Identifiable liabilities:				
Non-interest bearing deposits	909,669	-		909,669
Interest bearing deposits	52,123,868	433,429	F	52,557,297
Borrowings	10,500,000	389,147	G	10,889,147
Other liabilities	120,351	-		120,351
Total identifiable liabilities	\$63,653,888	\$822,576		\$64,476,464
Net tangible assets acquired	11,882,285	(2,233,360)		9,648,925
Definite lived intangible assets acquired	-	542,540		542,540
Goodwill	-	4,000,904		4,000,904
Net intangible assets acquired	-	4,543,444		4,543,444

Total cash consideration	\$11,882,285	\$2,310,084	\$14,192,369
--------------------------	--------------	-------------	--------------

Explanation of fair value adjustments:

- A - Adjustment reflects marking the certificates of deposit portfolio to fair value as of the acquisition date.
- B - Adjustment reflects the fair value adjustments based on Hamilton Bancorp's evaluation of the acquired loan portfolio and excludes the allowance for losses recorded by Fairmount Bancorp, Inc.
- C - Adjustment reflects the fair value adjustments based on Hamilton Bancorp's evaluation of the acquired premises and equipment.
- D - Adjustment reflects the elimination of core deposit intangible recorded by Fairmount Bancorp, Inc. from an acquisition prior.
- E - Adjustment to record deferred tax asset related to fair value adjustments at 39.45% income tax rate.
- F - Adjustment arises since the rates on interest-bearing deposits are higher than rates available on similar deposits as of the acquisition date.
- G - Adjustment reflects the fair value of Fraternity's borrowings acquired on acquisition date.

Prior to the end of the measurement period, if information becomes available which indicates the purchase price allocations require adjustments, we will include such adjustments in the purchase price allocation retrospectively.

Of the total estimated purchase price, we have allocated an estimate of \$9.6 million to net tangible assets acquired and we have allocated approximately \$543,000 to the core deposit intangible which is a definite lived intangible asset. We have allocated the remaining purchase price to goodwill, which is deductible for income tax purposes. We will amortize the core deposit intangible on a straight-line basis over its estimated useful life of 8 years. We will evaluate goodwill annually for impairment.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Pro forma Condensed Combined Financial Information. The following schedule includes consolidated statements of operations data for the unaudited pro forma results for the three month periods ended June 30, 2016 and 2015 as if the Fairmount acquisition had occurred as of the beginning of the periods presented.

	Three Months Ended	
	June 30,	
	2016	2015
Net interest income	\$3,096,592	\$2,794,670
Other non-interest revenue	269,498	693,532
Total revenue	3,366,090	3,488,202
Provision expense	210,000	-
Other non-interest expense	3,709,099	2,796,255
Income before income taxes	(553,009)	691,947
Income tax expense	(217,801)	330,760
Net income	\$(335,208)	\$361,187
Basic earnings per share	\$(0.11)	\$0.11
Diluted earnings per share	\$(0.11)	\$0.11

The pro forma condensed financial information in the table above for the three months ending June 30, 2016, includes the revenue and expenses associated with the acquisition of Fraternity Community Bancorp, Inc. on May 13, 2016 through the end of the period, including \$674,000 in acquisition related and branch consolidation expenses.

We have not included any provision for loan losses during the period for loans acquired from Fairmount. In accordance with accounting for business combinations, we included the credit losses evident in the loans in the determination of the fair value of loans at the date of acquisition and eliminated the allowance for loan losses maintained by Fairmount at acquisition date. Also excluded are an estimated \$3.1 million in merger related expenses associated with completing the actual acquisition. This expense includes expenses incurred by both the buyer and the seller.

We have presented the pro forma financial information for illustrative purposes only and it is not necessarily indicative of the financial results of the combined companies if we had actually completed the acquisition at the beginning of the periods presented, nor does it indicate future results for any other interim or full year period. Pro forma basic and diluted earnings per common share were calculated using Hamilton Bancorp's actual weighted average shares outstanding for the periods presented, assuming the acquisition occurred at the beginning of the periods presented.

Fraternity and Fairmount acquisition expenses. In connection with the acquisition of Fraternity and Fairmount, the Company incurred merger related costs. These expenses were primarily related to legal, other professional services and system conversions. The following table details the expenses included in the consolidated statements of operations for the periods shown.

	Three months Ended June 30, 2016			Three Months Ended June 30, 2015		
	Fairmount	Fraternity	Total	Fairmount	Fraternity	Total
Legal	\$7,200	\$39,219	\$46,419	\$129,033	\$6,455	\$135,488
Professional services	-	135,383	135,383	80,000	7,673	87,673
Advertising	-	-	-	2,779	-	2,779
Other	-	54,682	54,682	4,701	144	4,845
Total merger related expenses	\$7,200	\$229,284	\$236,484	\$216,513	\$14,272	\$230,785

Note 4: Earnings per Share

Basic earnings per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Weighted average shares exclude unallocated ESOP shares. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Both the basic and diluted earnings per share for the three months ended June 30, 2016 and 2015 are summarized below:

	Three Months ended	Three Months ended
	June 30, 2016	June 30, 2015
Net income (loss)	\$(335,208)	\$ 118,323
Weighted average common shares outstanding - basic	3,176,654	3,165,909
Weighted average common shares outstanding - diluted	3,177,033	3,166,901
Income (loss) per common share - basic and diluted	\$(0.11)	\$0.04
Anti-dilutive shares	N/A	992

During the three months ending June 30, 2016, none of the common stock equivalents were dilutive due to the loss reported during that period.

Note 5: Investment Securities Available for Sale

The amortized cost and fair value of securities at June 30, 2016 and March 31, 2016, are summarized as follows:

<u>June 30, 2016</u>	Amortized	Gross	Gross	Fair
-----------------------------	-----------	-------	-------	------

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

	cost	unrealized gains	unrealized losses	value
U.S. government agencies	\$10,761,723	\$39,745	\$-	\$10,801,468
Municipal bonds	6,783,780	189,313	-	6,973,093
Corporate bonds	2,000,000	-	88,976	1,911,024
Mortgage-backed securities	60,443,783	509,325	115,315	60,837,793
	\$79,989,286	\$738,383	\$204,291	\$80,523,378

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
<u>March 31, 2016</u>				
U.S. government agencies	\$10,519,126	\$20,622	\$6,752	\$10,532,996
Municipal bonds	4,061,599	51,105	140	4,112,564
Corporate bonds	2,000,000	-	101,360	1,898,640
Mortgage-backed securities	53,939,706	300,731	300,237	53,940,200
	\$70,520,431	\$372,458	\$408,489	\$70,484,400

There were no sales of investment securities during the three months ended June 30, 2016 or 2015.

As of June 30, 2016 and March 31, 2016, all mortgage-backed securities are backed by U.S. Government-Sponsored Enterprises (GSE's), except one private label mortgage-backed security that was acquired in the Fraternity acquisition in May 2016 with a book value of \$118,154 and fair value of \$117,596 as of June 30, 2016.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

As of June 30, 2016 and March 31, 2016, the Company had one pledged security to the Federal Reserve Bank with a book value of \$744,186 and \$2,000,000 and a fair value of \$744,202 and \$1,993,266, respectively.

The amortized cost and estimated fair value of debt securities by contractual maturity at June 30, 2016 and March 31, 2016 follow. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations.

	Available for Sale		March 31, 2016	
	June 30, 2016		Amortized	Fair
	Amortized	Fair	Amortized	Fair
	cost	value	cost	value
Maturing				
Within one year	\$250,447	\$250,495	\$731,217	\$731,060
Over one to five years	3,267,090	3,302,116	3,268,217	3,287,589
Over five to ten years	11,122,044	11,089,369	9,830,135	9,751,610
Over ten years	4,905,922	5,043,605	2,751,156	2,773,941
Mortgage-backed, in monthly installments	60,443,783	60,837,793	53,939,706	53,940,200
	\$79,989,286	\$80,523,378	\$70,520,431	\$70,484,400

The following table presents the Company's investments' gross unrealized losses and the corresponding fair values by investment category and length of time that the securities have been in a continuous unrealized loss position at June 30, 2016 and March 31, 2016.

	Less than 12 months	12 months or longer	Total	
	Gross	Gross	Gross	Fair
	Fair	Fair		
<u>June 30, 2016</u>	Unrealized	Unrealized	Unrealized losses	
	value	value	losses	
	losses	losses		

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

U.S. government agencies	\$-	\$-	\$-	\$-	\$-	\$-
Municipal bonds	-	-	-	-	-	-
Corporate bonds	-	-	88,976	1,911,024	88,976	1,911,024
Mortgage-backed securities	20,355	5,605,839	94,960	13,849,211	115,315	19,455,050
	\$20,355	\$5,605,839	\$183,936	\$15,760,235	\$204,291	\$21,366,074

	Less than 12 months		12 months or longer		Total	
	Gross		Gross		Gross	
	Fair		Fair		Fair	
<u>March 31, 2016</u>	Unrealized		Unrealized		Unrealized	
	value		value		value	
	losses		losses		losses	
U.S. government agencies	\$6,752	\$2,244,157	\$-	\$-	\$6,752	\$2,244,157
Municipal bonds	140	480,168	-	-	140	480,168
Corporate bonds	-	-	101,360	1,898,640	101,360	1,898,640
Mortgage-backed securities	33,080	4,367,962	267,157	20,274,037	300,237	24,641,999
	\$39,972	\$7,092,287	\$368,517	\$22,172,677	\$408,489	\$29,264,964

The gross unrealized losses on debt securities are not considered by management to be other-than-temporary impairments. Management has the intent and ability to hold these securities until recovery of their value. In most cases, temporary impairment is caused by market interest rate fluctuations.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Note 6: Loans Receivable and Allowance for Loan Losses

Loans receivable, excluding loans held for sale, consist of the following at June 30, 2016 and March 31, 2016:

	June 30, 2016			% of Total	March 31, 2016			% of Total
	Legacy (1)	Acquired	Total Loans		Legacy (1)	Acquired	Total Loans	
Real estate loans:								
One-to-four-family:								
Residential	\$45,442,299	\$97,700,552	\$143,142,851	43 %	\$46,263,709	\$23,036,569	\$69,300,278	31 %
Residential construction	5,524,789	844,287	6,369,076	2 %	4,304,189	965,440	5,269,629	2 %
Investor (2)	11,825,433	23,606,757	35,432,190	11 %	12,076,911	15,783,008	27,859,919	13 %
Commercial	81,155,633	17,875,858	99,031,491	30 %	75,225,984	2,889,219	78,115,203	35 %
Commercial construction	2,348,741	1,615,922	3,964,663	1 %	1,982,571	1,274,148	3,256,719	2 %
Total real estate loans	146,296,895	141,643,376	287,940,271	87 %	139,853,364	43,948,384	183,801,748	83 %
Commercial business	15,985,673	2,714,738	18,700,411	6 %	17,773,967	2,621,625	20,395,592	9 %
Home equity loans	12,293,585	9,495,334	21,788,919	7 %	12,222,688	2,168,073	14,390,761	6 %
Consumer	2,875,534	1,031,516	3,907,050	1 %	3,072,677	1,106,434	4,179,111	2 %
Total Loans	177,451,687	154,884,964	332,336,651	100 %	172,922,696	49,844,516	222,767,212	100 %
Net deferred loan origination fees and costs	(171,916)	-	(171,916)		(139,321)	-	(139,321)	

Loan premium (discount)	68,307	(794,848)	(726,541)	77,983	(846,818)	(768,835)
	\$177,348,078	\$154,090,116	\$331,438,194	\$172,861,358	\$48,997,698	\$221,859,056

As a result of the acquisition of Fraternity Community Bancorp, Inc., the parent company of Fraternity Federal Savings and Loan, in May 2016 and Fairmount Bancorp, Inc., the parent company of Fairmount Bank, in (1) September 2015, we have segmented the portfolio into two components, loans originated by Hamilton Bank "Legacy" and loans acquired from Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc. "Acquired".

(2) "Investor" loans are residential mortgage loans secured by non-owner occupied one- to four-family properties.

Residential lending is generally considered to involve less risk than other forms of lending, although payment experience on these loans is dependent on economic and market conditions in the Bank's lending area. Construction loan repayments are generally dependent on the related properties or the financial condition of its borrower or guarantor. Accordingly, repayment of such loans can be more susceptible to adverse conditions in the real estate market and the regional economy.

A substantial portion of the Bank's loan portfolio is real estate loans secured by residential and commercial real estate properties located in the Baltimore metropolitan area. Loans are extended only after evaluation of a customer's creditworthiness and other relevant factors on a case-by-case basis. The Bank generally does not lend more than 90% of the appraised value of a property and requires private mortgage insurance on residential mortgages with loan-to-value ratios in excess of 80%. In addition, the Bank generally obtains personal guarantees of repayment from borrowers and/or others for construction loans and disburses the proceeds of those and similar loans only as work progresses on the related projects.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The following table details activity in the allowance for loan losses by portfolio segment for both the three months ended June 30, 2016 and 2015 and for the year ended March 31, 2016. The allowance for loan losses allocated to each portfolio segment is not necessarily indicative of future losses in any particular portfolio segment and does not restrict the use of the allowance to absorb losses in other portfolio segments.

Three months ended:	Legacy				Acquired					
	Allowance	Provision for	Charge	Recoveries	Allowance	Provision for	Charge	Recoveries	Allowance	
<u>June 30, 2016</u>	3/31/2016	loan losses	offs		6/30/2016	3/31/2016	offs		6/30/2016	
Real estate loans:										
One-to four-family	\$428,027	\$260,081	\$-	\$-	\$688,108	\$-	\$28,700	\$28,700	\$-	\$-
Commercial	901,768	8,992	-	-	910,760	-	-	-	-	-
Commercial construction	42,377	(14,544)	-	-	27,833	-	-	-	-	-
Commercial business	228,199	(54,562)	1,521	15,319	187,435	-	-	-	-	-
Home equity loans	82,012	(954)	-	-	81,058	-	-	-	-	-
Consumer	19,982	(17,369)	1,280	445	1,778	-	(345)	-	345	-
	\$1,702,365	\$181,644	\$2,801	\$15,764	\$1,896,972	\$-	\$28,355	\$28,700	\$345	\$-

Three months ended:	Legacy				Acquired					
	Allowance	Provision for	Charge	Recoveries	Allowance	Provision for	Charge	Recoveries	Allowance	
<u>June 30, 2015</u>	3/31/2015	loan losses	offs		6/30/2015	3/31/2015	offs		6/30/2015	

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Real estate loans:

One-to four-family	\$433,570	\$59,327	\$60,000	\$ 848	\$433,745	\$-	\$ -	\$ -	\$ -	\$ -
Commercial	585,817	76,988	-	-	662,805	-	-	-	-	-
Commercial construction	67,835	33,202	-	-	101,037	-	-	-	-	-
Commercial business	473,127	(164,574)	10,533	66,239	364,259	-	-	-	-	-
Home equity loans	98,983	(8,392)	6,000	-	84,591	-	-	-	-	-
Consumer	727	33,626	7,565	-	26,788	-	-	-	-	-
Unallocated	30,177	(30,177)	-	-	-	-	-	-	-	-
	\$1,690,236	\$-	\$84,098	\$ 67,087	\$1,673,225	\$-	\$ -	\$ -	\$ -	\$ -

Year Ended:	Legacy				Acquired					
	Allowance	Provision for	Charge	Recoveries	Allowance	Provision for loan losses	Charge	Recoveries	Allowance	
<u>March 31, 2016</u>	3/31/2015	Loan Losses	offs		3/31/2016	3/31/2015	offs		3/31/2016	

Real estate loans:

One-to four-family	\$433,570	\$164,809	\$171,200	\$848	\$428,027	\$-	\$95,703	\$120,538	\$24,835	\$ -
Commercial	585,817	883,852	567,901	-	901,768	-	-	-	-	-
Commercial construction	67,835	(262,362)	-	236,904	42,377	-	-	-	-	-
Commercial business	473,127	(426,731)	10,533	192,336	228,199	-	-	-	-	-
Home equity loans	98,983	(10,971)	6,000	-	82,012	-	-	-	-	-
Consumer	727	25,877	16,337	9,715	19,982	-	-	-	-	-
Unallocated	30,177	(30,177)	-	-	-	-	-	-	-	-
	\$1,690,236	\$344,297	\$771,971	\$439,803	\$1,702,365	\$-	\$95,703	\$120,538	\$24,835	\$ -

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The following table provides additional information on the allowance for loan losses and loan balances with respect to evaluation for impairment by segment:

	Legacy Allowance		Loan Balance		Acquired Allowance		Loan Balance	
	Individually	Collectively	Individually	Collectively	Individually	Collectively	Individually	Collectively
Three months ended:	evaluated	evaluated	evaluated	evaluated	evaluated	evaluated	evaluated	evaluated
<u>June 30, 2016</u>	for	for	for	for	for	for	for	for
	impairment	impairment	impairment	impairment	impairment	impairment	impairment	impairment
Real estate loans:								
One-to four-family	\$293,992	\$394,116	\$2,474,968	\$60,317,552	\$-	\$-	\$2,624,486	\$119,527,111
Commercial	-	910,760	2,673,131	78,482,502	-	-	369,422	17,506,436
Commercial construction	-	27,833	-	2,348,741	-	-	-	1,615,922
Commercial business	9,657	177,778	1,000,250	14,985,423	-	-	-	2,714,738
Home equity loans	-	81,058	56,977	12,236,608	-	-	10,663	9,484,671
Consumer	-	1,778	-	2,875,534	-	-	73,835	957,681
	\$303,649	\$1,593,323	\$6,205,326	\$171,246,360	\$-	\$-	\$3,078,406	\$151,806,559

	Legacy Allowance		Loan Balance		Acquired Allowance		Loan Balance	
	Individually	Collectively	Individually	Collectively	Individually	Collectively	Individually	Collectively
Three months ended:	evaluated	evaluated	evaluated	evaluated	evaluated	evaluated	evaluated	evaluated
<u>June 30, 2015</u>	for	for	for	for	for	for	for	for
	impairment	impairment	impairment	impairment	impairment	impairment	impairment	impairment

Real estate loans:

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

One-to four-family	\$92,054	\$ 341,691	\$2,135,316	\$64,325,672	\$-	\$ -	\$ -	\$ -
Commercial	-	662,805	3,358,431	62,789,930	-	-	-	-
Commercial construction	-	101,037	1,330,559	1,536,105	-	-	-	-
Commercial business	-	364,259	1,687,697	16,273,627	-	-	-	-
Home equity loans	-	84,591	20,136	12,287,920	-	-	-	-
Consumer	-	26,788	-	3,872,597	-	-	-	-
	\$92,054	\$ 1,581,171	\$8,532,139	\$ 161,085,851	\$-	\$ -	\$ -	\$ -

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Year Ended:	Legacy Allowance		Loan Balance		Acquired Allowance		Loan Balance	
	Individually	Collectively	Individually	Collectively	Individually	Collectively	Individually	Collectively
	Evaluated	Evaluated	Evaluated	Evaluated	evaluated	evaluated	evaluated	evaluated
<u>March 31, 2016</u>	for	for	for	for	for	for	for	for
	Impairment	Impairment	Impairment	Impairment	impairment	impairment	impairment	impairment
Real estate loans:								
One-to four-family	\$59,571	\$368,456	\$1,918,527	\$60,726,282	\$-	\$-	\$1,210,306	\$38,574,711
Commercial	-	901,768	2,717,144	72,508,840	-	-	211,239	2,677,980
Commercial construction	-	42,377	-	1,982,571	-	-	-	1,274,148
Commercial business	-	228,199	1,279,233	16,494,734	-	-	-	2,621,625
Home equity loans	-	82,012	59,169	12,163,519	-	-	-	2,168,073
Consumer	-	19,982	-	3,072,677	-	-	42,488	1,063,946
	\$59,571	\$1,642,794	\$5,974,073	\$166,948,623	\$-	\$-	\$1,464,033	\$48,380,483

Past due loans, segregated by age and class of loans, as of and for the three months ended June 30, 2016 and as of and for the year ended March 31, 2016, were as follows:

<u>June 30, 2016</u>	Loans	Loans	Loans	Total past due loans	Current loans	Totals loans	Accruing	Nonaccrual
	30-59 days past due	60-89 days past due	90 or more days past due				loans 90 or more days past due	Nonaccrual loans	interest not accrued

Legacy**Loans:**

Real estate

loans:

One-to four-family	\$438,973	\$261,332	\$298,902	\$999,207	\$61,793,314	\$62,792,521	\$-	\$680,471	\$21,192
Commercial	-	-	2,673,132	2,673,132	78,482,501	81,155,633	-	2,673,132	-
Commercial construction	101,080	-	-	101,080	2,247,661	2,348,741	-	-	-
Commercial business	-	-	-	-	15,985,673	15,985,673	-	-	-
Home equity loans	-	41,947	-	41,947	12,251,638	12,293,585	-	5,718	95
Consumer	12,903	-	-	12,903	2,862,631	2,875,534	-	-	-
	\$552,956	\$303,279	\$2,972,034	\$3,828,269	\$173,623,418	\$177,451,687	\$-	\$3,359,321	\$21,287

	Loans 30-59 days past due	Loans 60-89 days past due	Loans 90 or more days past due	Total past due loans	Current loans	Totals loans	Accruing		
							loans 90 or more days past due	Nonaccrual loans	Nonaccrual interest accrued

**June 30,
2016****Acquired****Loans:**

Real estate

loans:

One-to four-family	\$1,005,916	\$70,960	\$845,309	\$1,922,185	\$120,229,411	\$122,151,596	\$16,977	\$1,037,358	\$117,513
Commercial	-	-	8,640	8,640	17,867,218	17,875,858	-	8,640	-
Commercial construction	-	-	-	-	1,615,922	1,615,922	-	-	-
Commercial business	19,149	-	-	19,149	2,695,589	2,714,738	-	-	-
Home equity loans	-	-	11,511	11,511	9,483,823	9,495,334	-	11,511	-
Consumer	31,325	3,063	-	34,388	997,128	1,031,516	-	-	-
	\$1,056,390	\$74,023	\$865,460	\$1,995,873	\$152,889,091	\$154,884,964	\$16,977	\$1,057,509	\$117,513

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

	Loans 30-59 days past due	Loans 60-89 days past due	Loans 90 or more days past due	Total past due loans	Current loans	Totals loans	Accruing loans 90 or more days past due	Nonaccrual loans	Nonacc interest not accrued
<u>March 31, 2016</u>									
<u>Legacy</u>									
<u>Loans:</u>									
Real estate loans:									
One-to four-family	\$468,887	\$99,360	\$388,104	\$956,351	\$61,688,458	\$62,644,809	\$165,701	\$511,939	\$18,490
Commercial	-	-	2,717,144	2,717,144	72,508,840	75,225,984	-	2,717,144	-
Commercial construction	-	-	-	-	1,982,571	1,982,571	-	-	-
Commercial business	-	-	121,760	121,760	17,652,207	17,773,967	-	121,760	47,640
Home equity loans	20,753	-	43,073	63,826	12,158,862	12,222,688	-	49,462	1,007
Consumer	-	-	-	-	3,072,677	3,072,677	-	-	-
	\$489,640	\$99,360	\$3,270,081	\$3,859,081	\$169,063,615	\$172,922,696	\$165,701	\$3,400,305	\$67,140

	Loans 30-59 days past due	Loans 60-89 days past due	Loans 90 or more days past due	Total past due loans	Current loans	Totals loans	Accruing loans 90 or more days past due	Nonaccrual loans	Nonaccrual interest not accrued
<u>March 31, 2016</u>									
<u>Acquired</u>									
<u>Loans:</u>									

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Real estate
loans:

One-to four-family	\$42,800	\$-	\$1,480,508	\$1,523,308	\$38,261,709	\$39,785,017	\$542,236	\$938,272	\$118,381
Commercial	-	-	-	-	2,889,219	2,889,219	-	-	-
Commercial construction	-	-	-	-	1,274,148	1,274,148	-	-	-
Commercial business	-	-	-	-	2,621,625	2,621,625	-	-	-
Home equity loans	-	-	-	-	2,168,073	2,168,073	-	-	-
Consumer	-	-	3,535	3,535	1,102,899	1,106,434	-	3,535	178
	\$42,800	\$-	\$1,484,043	\$1,526,843	\$48,317,673	\$49,844,516	\$542,236	\$941,807	\$118,559

Impaired Loans as of and for the three months ended June 30, 2016 and as of and for the year ended March 31, 2016, was as follows:

	Unpaid contractual principal balance	Recorded investment with no allowance	Recorded investment with allowance	Total recorded investment	Related allowance	Average recorded investment	Interest recognized
<u>June 30, 2016</u>							
<u>Legacy Loans:</u>							
Real estate loans:							
One-to four-family	\$2,786,045	\$1,112,496	\$1,362,471	\$2,474,967	\$293,992	\$2,456,954	\$25,145
Commercial	3,433,621	2,673,131	-	2,673,131	-	2,694,891	987
Commercial construction	-	-	-	-	-	-	-
Commercial business	1,484,294	387,432	612,818	1,000,250	9,657	1,148,591	34,752
Home equity loans	80,916	56,977	-	56,977	-	58,136	1,046
Consumer	6,625	-	-	-	-	-	-
	\$7,791,501	\$4,230,036	\$1,975,289	\$6,205,325	\$303,649	\$6,358,572	\$61,930

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

	Unpaid	Recorded	Recorded	Total	Related	Average	Interest
<u>June 30, 2016</u>	contractual	investment	investment	recorded	allowance	recorded	recognized
	principal	with no	with	investment		investment	
	balance	allowance	allowance				
<u>Acquired Loans:</u>							
Real estate loans:							
One-to four-family	\$4,583,803	\$2,624,486	\$ -	\$2,624,486	\$ -	\$2,311,600	\$ 34,831
Commercial	2,774,763	369,422	-	369,422	-	316,478	11,814
Commercial construction	-	-	-	-	-	-	-
Commercial business	-	-	-	-	-	-	-
Home equity loans	142,633	10,663	-	10,663	-	5,480	1,254
Consumer	110,310	73,835	-	73,835	-	75,781	3,090
	\$7,611,509	\$3,078,406	\$ -	\$3,078,406	\$ -	\$2,709,339	\$ 50,989
	Unpaid	Recorded	Recorded	Total	Related	Average	Interest
<u>March 31, 2016</u>	contractual	investment	investment	recorded	allowance	recorded	recognized
	principal	with no	with	investment		investment	
	balance	allowance	allowance				
<u>Legacy Loans:</u>							
Real estate loans:							
One-to four-family	\$2,116,820	\$626,719	\$1,291,808	\$1,918,527	\$ 59,571	\$1,865,000	\$ 63,498
Commercial	3,433,621	2,717,144	-	2,717,144	-	3,298,855	99,599
Commercial construction	-	-	-	-	-	-	-
Commercial business	1,884,258	1,279,233	-	1,279,233	-	1,557,871	147,101
Home equity loans	82,740	59,169	-	59,169	-	18,817	331
Consumer	-	-	-	-	-	-	-
	\$7,517,439	\$4,682,265	\$1,291,808	\$5,974,073	\$ 59,571	\$6,740,543	\$ 310,529
<u>March 31, 2016</u>	Unpaid	Recorded	Recorded	Total	Related	Average	Interest

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

	contractual principal balance	investment with no allowance	investment with no allowance	recorded investment	allowance	recorded investment	recognized
<u>Acquired Loans:</u>							
Real estate loans:							
One-to four-family	\$2,444,002	\$1,210,306	\$ -	\$1,210,306	\$ -	\$1,387,353	\$ 86,587
Commercial	261,239	211,239	-	211,239	-	212,806	9,978
Commercial construction	-	-	-	-	-	-	-
Commercial business	-	-	-	-	-	-	-
Home equity loans	-	-	-	-	-	-	-
Consumer	72,358	42,488	-	42,488	-	43,233	7,086
	\$2,777,599	\$1,464,033	\$ -	\$1,464,033	\$ -	\$1,643,392	\$ 103,651

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The following table documents changes in the carrying amount of acquired impaired loans (Purchased Credit Impaired or "PCI") for the three months ended June 30, 2016, along with the outstanding balance at the end of the period:

	June 30, 2016
Recorded investment at March 31, 2016	\$919,729
Fair value of loans acquired during the year	1,027,518
Accretion	6,527
Reductions of payments	(11,670)
Recorded investment at June 30, 2016	\$1,942,104
Outstanding principal balance at June 30, 2016	\$2,643,930

A summary of changes in the accretable yield for PCI loans for the three months ended June 30, 2016 is as follows:

	June 30, 2016
Accretable yield at March 31, 2016	\$32,629
Addition from acquisition	55,046
Accretion	(6,527)
Reclassification from nonaccretable difference	-
Accretable yield at June 30, 2016	\$81,148

Impaired loans also include certain loans that have been modified in troubled debt restructurings (TDRs) where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Bank's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Generally, nonaccrual loans that are modified and considered TDRs are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

A summary of TDRs at June 30, 2016 and March 31, 2016 follows:

<u>June 30, 2016</u>	Number of	Performing	Nonperforming	Total
	contracts			
Real estate loans:				
One-to four-family	23	\$1,284,370	\$ 543,978	\$1,828,348
Commercial	2	-	2,673,132	2,673,132
Commercial construction	-	-	-	-
Commercial business	2	643,767	-	643,767
Home equity loans	-	-	-	-
Consumer	-	-	-	-
	27	\$1,928,137	\$ 3,217,110	\$5,145,247

<u>March 31, 2016</u>	Number of	Performing	Nonperforming	Total
	contracts			
Real estate loans:				
One-to four-family	12	\$1,457,552	\$ 101,449	\$1,559,001
Commercial	2	-	2,717,144	2,717,144
Commercial construction	-	-	-	-
Commercial business	2	647,654	-	647,654
Home equity loans	-	-	-	-
Consumer	-	-	-	-
	16	\$2,105,206	\$ 2,818,593	\$4,923,799

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The following table presents the number of contracts and the dollar amount of TDR's that were added during the three month period ended June 30, 2016. The amount shown reflects the outstanding loan balance at the time of the modification.

<u>Three months ended June 30, 2016</u>	Number of contracts	Outstanding recorded investment
Real estate loans:		
One-to four-family	11	\$ 712,786
Commercial	-	-
Commercial construction	-	-
Commercial business	-	-
Home equity loans	-	-
Consumer	-	-
	11	\$ 712,786

The following table represents loans that were modified as TDRs within the previous 12 months and have subsequently defaulted in the three months ended June 30, 2016. There were no TDRs that defaulted in the three months ended June 30, 2015. Payment default under a TDR is defined as any TDR that is 90 days or more past due since the loan was modified or the inability of the TDR to make the required payment subsequent to the modification.

TDR Loan Type	Defaulted During The Three Months Ended June 30, 2016 Number of Investment

Contracts

One-to four-family **11** **\$ 261,563**

The one-to four-family TDR loans that defaulted as of June 30, 2016 represent several loans to one borrower for non-owner occupied residential real estate properties. The recorded investment reflects a write-down of the recorded investment amounts of \$451,223 during the quarter ended June 30, 2016. This write-down was recorded through an adjustment to goodwill based upon information that we were unaware of at time of acquisition. Had we been aware of the information at acquisition, we would have identified these loans as impaired at the time of acquisition.

Credit quality indicators

As part of the ongoing monitoring of the credit quality of the Bank's loan portfolio, management tracks certain credit quality indicators including trends related to the risk grade of loans, the level of classified loans, net charge offs, nonperforming loans, and the general economic conditions in the Bank's market.

The Bank utilizes a risk grading matrix to assign a risk grade to each of its loans. A description of the general characteristics of loans characterized as watch list or classified is as follows:

Pass

A pass loan is considered of sufficient quality to preclude a special mention or an adverse rating. Pass assets generally are well protected by the current net worth and paying capacity of the obligor or by the value of the asset or underlying collateral.

Special Mention

A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in the Bank's credit position at some future date. Special mention loans are not adversely classified and do not expose the Bank to sufficient risk to warrant adverse classification.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Loans that would primarily fall into this notational category could have been previously classified adversely, but the deficiencies have since been corrected. Management should closely monitor recent payment history of the loan and value of the collateral.

Borrowers may exhibit poor liquidity and leverage positions resulting from generally negative cash flow or negative trends in earnings. Access to alternative financing may be limited to finance companies for business borrowers and may be unavailable for commercial real estate borrowers.

Substandard

A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard loans have a well defined weakness, or weaknesses, that jeopardize the collection or liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. This will be the measurement for determining if a loan is impaired.

Borrowers may exhibit recent or unexpected unprofitable operations, an inadequate debt service coverage ratio, or marginal liquidity and capitalization. These loans require more intense supervision by Bank management.

Doubtful

A doubtful loan has all the weaknesses inherent as a substandard loan 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. A loan classified as doubtful exhibits loss potential. However, there is still sufficient reason to permit the loan to remain on the books. A doubtful classification could reflect the deterioration of the primary source of repayment and serious doubt exists as to the quality of the secondary source of repayment.

Doubtful classifications should be used only when a distinct and known possibility of loss exists. When identified, adequate loss should be recorded for the specific assets. The entire asset should not be classified as doubtful if a partial recovery is expected, such as liquidation of the collateral or the probability of a private mortgage insurance payment is likely.

Loss

Loans classified as loss are considered uncollectable and of such little value that their continuance as loans is unjustified. A loss classification does not mean a loan has absolutely no value; partial recoveries may be received in the future. When loans or portions of a loan are considered a loss, it will be the policy of the Bank to write-off the amount designated as a loss. Recoveries will be treated as additions to the allowance for loan losses.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The following tables present the June 30, 2016 and March 31, 2016, balances of classified loans based on the risk grade. Classified loans include Special Mention, Substandard, and Doubtful loans. The Bank had no loans classified as Doubtful or Loss as of June 30, 2016 or March 31, 2016.

<u>June 30,</u> <u>2016</u>	Legacy				Total	Acquired		
	Pass	Special Mention	Substandard			Pass	Special Mention	Substandard
Real estate loans:								
One-to four-family	\$59,917,740	\$2,090,307	\$784,474	\$62,792,521	\$116,864,791	\$3,332,605	\$1,954,200	
Commercial	75,219,651	3,262,850	2,673,132	81,155,633	15,787,419	1,491,896	596,543	
Commercial construction	2,348,741	-	-	2,348,741	1,615,922	-	-	
Commercial business	14,832,111	898,687	254,875	15,985,673	2,714,738	-	-	
Home equity loans	12,236,608	41,947	15,030	12,293,585	9,344,607	140,064	10,663	
Consumer	2,875,534	-	-	2,875,534	1,031,516	-	-	
	\$167,430,385	\$6,293,791	\$3,727,511	\$177,451,687	\$147,358,993	\$4,964,565	\$2,561,406	
Percentage of total loans	94.4	% 3.5	% 2.1	% 100	% 95.1	% 3.2	% 1.7	%

<u>March 31,</u> <u>2016</u>	Legacy				Total	Acquired		
	Pass	Special Mention	Substandard			Pass	Special Mention	Substandard
Real estate loans:								

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

One-to four-family	\$59,969,105	\$2,272,150	\$403,554	\$62,644,809	\$38,039,563	\$535,148	\$1,210,306	\$39,000,000
Commercial	66,824,956	5,683,884	2,717,144	75,225,984	2,677,980	-	211,239	2,000,000
Commercial construction	1,982,571	-	-	1,982,571	1,274,148	-	-	1,000,000
Commercial business	13,629,957	3,477,579	666,431	17,773,967	2,621,625	-	-	2,000,000
Home equity loans	12,163,519	-	59,169	12,222,688	2,168,073	-	-	2,000,000
Consumer	3,072,677	-	-	3,072,677	1,063,946	-	42,488	1,000,000
	\$157,642,785	\$11,433,613	\$3,846,298	\$172,922,696	\$47,845,335	\$535,148	\$1,464,033	\$49,000,000
Percentage of total loans	91.2	% 6.6	% 2.2	% 100	% 96.0	% 1.1	% 2.9	% 100

In the normal course of business, the Bank has various outstanding commitments and contingent liabilities that are not reflected in the accompanying financial statements. Loan commitments and lines of credit are agreements to lend to a customer as long as there is no violation of any condition to the contract. Mortgage loan commitments generally have fixed interest rates, fixed expiration dates, and may require payment of a fee. Other loan commitments generally have fixed interest rates. Lines of credit generally have variable interest rates. Such lines do not represent future cash requirements because it is unlikely that all customers will draw upon their lines in full at any time.

The Bank's maximum exposure to credit loss in the event of nonperformance by the customer is the contractual amount of the credit commitment. Loan commitments, lines of credit, and letters of credit are made on the same terms, including collateral, as outstanding loans. Management is not aware of any accounting loss to be incurred by funding these loan commitments.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The Bank had the following outstanding commitments and unused lines of credit as of June 30, 2016 and March 31, 2016:

	June 30,	March 31,
	2016	2016
Unused commercial lines of credit	\$10,588,489	\$9,845,571
Unused home equity lines of credit	23,488,650	16,004,725
Unused consumer lines of credit	36,388	29,656
Residential mortgage loan commitments	9,721,431	-
Residential construction loan commitments	964,550	8,166,473
Commercial construction loan commitments	5,966,798	1,384,932
Home equity loan commitments	166,502	536,000
Commercial loan commitments	1,000,000	411,500
Standby letters of credit	230,052	273,981

Note 7: Goodwill and Other Intangible Asset

The Company's intangible assets (goodwill and core deposit intangible) at June 30, 2016 consist of assets recorded in December 2009 associated with the acquisition of a branch office in Pasadena, Maryland, the acquisition Fairmount in September 2015, and the acquisition of Fraternity in May 2016. The goodwill is deductible for tax purposes. We evaluate goodwill and other intangible assets for impairment on an annual basis. The core deposit intangible asset is being amortized straight-line over a life of 8 years.

The following table presents the changes in the net book value of intangible assets for the three months ended June 30, 2016 and 2015:

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

	Goodwill	Core deposit intangible
Balance March 31, 2015	\$2,664,432	\$138,333
Amortization expense	-	(7,250)
Balance June 30, 2015	\$2,664,432	\$131,083

	Goodwill	Core deposit intangible
Balance March 31, 2016	\$6,767,811	\$618,300
Additions (1)	3,147,441	242,020
Post acquisition adjustments	(93,226)	
Amortization expense	-	(26,473)
Balance June 30, 2016	\$9,822,026	\$833,847

(1) - Additions to intangible assets are related to acquisition of Fraternity Community.

The post acquisition adjustment to goodwill shown in the table above represents a \$451,000 write-down of several owner-occupied residential investor loans to one borrower that were acquired in the Fairmount acquisition and recording of a \$544,000 net operating loss (NOL) from Fairmount's final tax return. With regards to the investor loans, information we were not aware of at the time of the acquisition became available during the recent quarter ended June 30, 2016. Had we known this information at the time of the acquisition, we would have deemed these loans as impaired and valued them accordingly.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

At June 30, 2016, future expected annual amortization associated with the core deposit intangible is as follows:

<u>Year ending March 31,</u>	<u>Amount</u>
2017	\$94,554
2018	126,070
2019	126,070
2020	123,737
2021	98,070
2022	98,070
2023	98,070
2024	64,163
2025	5,043
	\$833,847

Note 8: Derivative – Interest Rate Swap Agreement

Derivative instruments are entered into primarily as a risk management tool of the Company. The derivative position relates to a transaction in which the Bank entered into an interest rate swap with another financial institution using a fixed rate commercial real estate loan as an offset. The Bank agrees to pay the other financial institution a fixed interest rate on a notional amount based upon the commercial real estate loan and in return receive a variable interest rate on the same notional amount. This transaction allows the Bank to effectively convert a fixed rate loan to a variable rate. Because the terms of the swap with the other financial institution and the commercial real estate loan offset each other, with the only difference being credit risk associated with the loan, changes in the fair value of the underlying derivative contract and the commercial real estate loan are not materially different and do not significantly impact the Bank's results of operations.

During the second quarter of fiscal 2016, the Company entered into the interest rate swap agreement with a \$3.3 million notional amount to convert a fixed rate commercial real estate loan at 3.99% into a variable rate for a term of approximately 10 years. The notional amounts of the interest rate swap and the offsetting commercial real estate loan were \$3.2 million at June 30, 2016. The derivative is designated as a fair value hedge.

Credit risk arises from the possible inability of counterparties to meet the terms of their contracts. The Bank's exposure is limited to the replacement value of the contract rather than the notional amount, principal, or contract amount. There are provisions in the agreement with the counterparty that allow for certain unsecured credit exposure up to an agreed threshold. Exposures in excess of the agreed threshold are collateralized. In addition, the Bank minimizes credit risk through credit approvals, limits, and monitoring procedures.

The fair value hedge is summarized below:

	June 30, 2016		
	Notional	Principal	Fair
	Amount	Amount	Value
Included in Loans and Leases:			
Commercial real estate loan	\$-	\$3,235,507	\$3,502,060
Included in Other Liabilities:			
Interest Rate Swap	\$3,235,507	\$-	\$266,553

No gain or loss was recognized in earnings for the three months ending June 30, 2016 related to the interest rate swap. The Company posted \$290,422 under collateral arrangements as of June 30, 2016 to satisfy collateral requirements associated with the credit risk exposure.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Note 9: Deposits

The following table details the composition of deposits and the related percentage mix of total deposits, respectively:

	June 30, 2016		March 31, 2016	
	Amount	% of Total	Amount	% of Total
Savings	\$45,282,733	11 %	\$33,010,962	11 %
Noninterest-bearing checking	22,132,850	5 %	19,747,437	6 %
Interest-bearing checking	17,089,730	4 %	13,298,677	4 %
Money market accounts	58,479,057	14 %	52,576,567	17 %
Time deposits	281,215,426	66 %	195,031,411	62 %
	424,199,796	100 %	\$313,665,054	100 %
Premium on deposits assumed	1,324,544		328,597	
Total deposits	\$425,524,340		\$313,993,651	

Note 10: Lines of Credit and Federal Home Loan Bank Advances

The Bank may borrow up to \$5,000,000 from a correspondent bank under a secured federal funds line of credit and \$1,000,000 under an unsecured federal funds line of credit. The Bank would be required to pledge investment securities to draw upon the secured line of credit. There were no borrowings under these lines of credit at June 30, 2016 and March 31, 2016.

Borrowings consist of advances from the Federal Home Loan Bank (FHLB). The Bank may borrow up to 20 percent of its assets under a line of credit agreement with the FHLB. Advances under the line of credit are secured by investments and certain loans owned by the Bank. As of June 30, 2016 and March 31, 2016, the Bank had \$49,912,200 and \$57,987,800 respectively, of available credit from the FHLB. Advances would be limited by the balance of investment securities and loans available for pledge. As a condition of obtaining the line of credit from the FHLB, the FHLB also requires the Bank purchase shares of capital stock in the FHLB. Information relating to

borrowings at June 30, 2016 and March 31, 2016 is presented below.

	June 30, 2016			March 31, 2016		
	Amount	Rate	Maturity Date	Amount	Rate	Maturity Date
FHLB advance	\$ -			\$ 2,000,000	0.43 %	6/3/2016
FHLB advance	2,000,000	0.60 %	9/3/2016	2,000,000	0.60 %	9/3/2016
FHLB advance	1,500,000	0.75 %	3/31/2017	1,500,000	0.75 %	3/31/2017
FHLB advance	1,000,000	4.24 %	7/31/2017	1,000,000	4.24 %	7/31/2017
FHLB advance	1,000,000	4.01 %	8/21/2017	1,000,000	4.01 %	8/21/2017
FHLB advance	1,000,000	0.91 %	8/31/2017	1,000,000	0.91 %	8/31/2017
FHLB advance	1,500,000	3.23 %	11/24/2017	1,500,000	3.23 %	11/24/2017
FHLB advance	1,500,000	3.40 %	11/27/2017	1,500,000	3.40 %	11/27/2017
FHLB advance	1,000,000	2.60 %	7/2/2018	1,000,000	2.60 %	7/2/2018
FHLB advance	1,000,000	3.05 %	7/3/2018	1,000,000	3.05 %	7/3/2018
FHLB advance	1,000,000	2.60 %	7/31/2017	1,000,000	2.60 %	10/2/2018
FHLB advance	5,000,000	4.28 %	7/23/2018	-		
FHLB advance	5,000,000	3.94 %	9/19/2018	-		
FHLB advance	5,000,000	3.38 %	10/2/2018	-		
	27,500,000			14,500,000		
Premium on borrowings assumed	987,127			305,237		
Total borrowings	\$ 28,487,127			\$ 14,805,237		

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

Note 11: Regulatory Capital Ratios

Banks and bank holding companies are subject to various regulatory capital requirements administered by state and federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors.

The Basel III Capital Rules became effective for Hamilton Bank on January 1, 2015 (subject to a phase-in period for certain provisions). Quantitative measures established by the Basel III Capital Rules to ensure capital adequacy require the maintenance of minimum amounts and ratios (set forth in the table below) of Common Equity Tier 1 capital, Tier 1 capital and Total capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital to adjusted quarterly average assets (as defined).

In connection with the adoption of the Basel III Capital Rules, we elected to opt-out of the requirement to include accumulated other comprehensive income in Common Equity Tier 1. Common Equity Tier 1 for Hamilton Bank is reduced by goodwill and other intangible assets, net of associated deferred tax liabilities and subject to transition provisions.

Under the revised prompt corrective action requirements, as of January 1, 2015, insured depository institutions are required to meet the following in order to qualify as “well capitalized:” (1) a common equity Tier 1 risk-based capital ratio of 6.5%; (2) a Tier 1 risk-based capital ratio of 8%; (3) a total risk-based capital ratio of 10% and (4) a Tier 1 leverage ratio of 5%. As of June 30, 2016, the Bank met all capital adequacy requirements under the Basel III Capital Rules to be considered “well capitalized” under prompt corrective action rules.

The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level and is being phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5% on January 1, 2019). The Basel III Capital Rules also provide for a “countercyclical capital buffer” that is applicable to only certain covered institutions and does not have any current applicability to Hamilton Bank.

The aforementioned capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of Common Equity Tier 1 capital to risk-weighted assets above the minimum but below the conservation buffer (or below the combined capital conservation buffer and countercyclical capital buffer, when the latter is applied) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

The following table presents actual and required capital ratios as of June 30, 2016 and March 31, 2016 for Hamilton Bank under the Basel III Capital Rules. The minimum required capital amounts presented include the minimum required capital levels as of January 1, 2015 based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered well capitalized are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

	Actual		Minimum Capital Required - Basel III Phase-In Schedule		Minimum Capital Required - Basel III Fully Phased-In		To be well capitalized (1)		
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio	
			<i>(dollars in thousands)</i>		<i>(dollars in thousands)</i>				
<u>June 30, 2016</u>									
Common equity tier 1 capital (to risk-weighted assets)	\$37,614	11.84 %	\$16,286	5.125 %	\$22,244	7.000 %	\$20,655	6.50 %	
Total risk-based capital (to risk-weighted assets)	39,553	12.45 %	27,408	8.625 %	33,366	10.500 %	31,777	10.00 %	
Tier 1 capital (to risk-weighted assets)	37,614	11.84 %	21,052	6.625 %	27,011	8.500 %	25,422	8.00 %	
Tier 1 capital (to adjusted total assets)	37,614	8.49 %	17,714	4.000 %	17,714	4.000 %	22,142	5.00 %	
<u>March 31, 2016</u>									
Common equity tier 1 capital (to risk-weighted assets)	\$44,518	19.06 %	\$11,971	5.125 %	\$16,350	7.00 %	\$15,182	6.50 %	
Total risk-based capital (to risk-weighted assets)	46,262	19.81 %	20,146	8.625 %	24,525	10.50 %	23,357	10.00 %	
Tier 1 capital (to risk-weighted assets)	44,518	19.06 %	15,474	6.625 %	19,854	8.50 %	18,686	8.00 %	
Tier 1 capital (to adjusted total assets)	44,518	11.78 %	15,114	4.00 %	15,114	4.00 %	18,892	5.00 %	

(1) - Under prompt corrective action

Tier 1 capital consists of total shareholders' equity less goodwill and intangible assets. Total capital includes a limited amount of the allowance for loan losses and a portion of any unrealized gain on equity securities. In calculating risk-weighted assets, specified risk percentages are applied to each category of asset and off-balance-sheet items.

Failure to meet the capital requirements could affect, among other things, the Bank's ability to accept brokered deposits and may significantly affect the operations of the Bank.

In its regulatory report filed as of June 30, 2016, the Bank exceeded all regulatory capital requirements and was considered "well capitalized" under regulatory guidelines. Management is not aware of any events that would have caused this classification to change. Management has no plans that should change the classification of the capital adequacy.

Note 12: Stock Based Compensation

In November 2013, the Company's shareholders approved a new Equity Incentive Plan (the "2013 Equity Incentive Plan"). The 2013 Equity Incentive Plan allows for up to 148,120 shares to be issued to employees, executive officers or Directors in the form of restricted stock, and up to 370,300 shares to be issued to employees, executive officers or Directors in the form of stock options. At June 30, 2016, there were 81,900 restricted stock awards issued and outstanding and 219,650 stock option awards granted under the 2013 Equity Incentive Plan.

Stock Options:

Under the above plan, the exercise price for stock options is the market price at date of grant. The maximum option term is ten years and the options granted shall vest in five equal annual installments of 20% with the first installment becoming exercisable on the first anniversary of the date of grant, or February 3, 2015, and succeeding installments on each anniversary thereafter, through February 3, 2019. The Company plans to issue new shares to satisfy share option exercises. The total cost that has been incurred for the stock option plan was \$52,301 for the three months ended June 30, 2016 and 2015, respectively.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

The fair value of each option award is estimated on the date of grant using a closed form option valuation (Black-Scholes) model that uses the assumptions noted in the table below. Expected volatilities are based on historical data. The Company uses historical data to estimate option exercise and post-vesting termination behavior. The expected term of options granted represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury rate equal to the expected term of the option in effect at the time of the grant.

The fair value of options granted during the fiscal year ended March 31, 2014 was determined using the following weighted-average assumptions as of grant date.

	February 3, 2014	
	(Grant Date)	
Risk free interest rate	2.07	%
Expected term (years)	7.0	
Expected stock price volatility	27.30	%
Dividend yield	0.00	%

The fair value of the options granted at grant date was \$4.65

A summary of stock option activity for the three months ended June 30, 2016 is as follows:

Three Months Ended June 30, 2016: Shares Weighted Weighted

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

		Average Exercise Price	Average Remaining Contractual Term (years)
Outstanding at beginning of period	219,650	\$ 13.85	7.6
Granted	-	-	-
Exercised	-	-	-
Forfeited, exchanged or expired	-	-	-
Outstanding at end of year	219,650	\$ 13.85	7.6
Vested at end of year	87,860	\$ 13.85	7.6

As of June 30, 2016 there was \$540,458 of total unrecognized compensation cost related to nonvested stock options granted under the Plan. The cost is expected to be recognized over a weighted-average period of 2.6 years. The intrinsic value of a stock option is the amount that the market value of the underlying stock exceeds the exercise price of the option. Based upon a fair market value of \$13.91 at June 30, 2016, the options outstanding had an intrinsic value of \$13,179.

Restricted Stock:

The specific terms of each restricted stock award are determined by the Compensation Committee at the date of the grant. Compensation expense is recognized over the vesting period of the awards based on the fair value of the stock at the grant date. Restricted stock awards granted shall vest in five equal annual installments of 20% with the first installment becoming vested on the first anniversary of the date of grant and succeeding installments on each anniversary thereafter.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

A summary of changes in the Company's nonvested shares for the three months ended June 30, 2016 is as follows:

	Shares	Weighted-Average Grant-Date Fair Value
Nonvested at March 31, 2016	50,600	\$ 13.76
Granted	-	-
Vested	-	-
Forfeited	-	-
Nonvested at June 30, 2016	50,600	\$ 13.76
Fair Value of shares vested	\$435,383	

The Company recorded restricted stock awards expense of \$56,426 and \$56,146 during the three months ended June 30, 2016 and 2015, respectively. As of June 30, 2016, there was \$600,091 of total unrecognized compensation cost related to nonvested shares granted under the 2013 stock incentive plan. The cost is expected to be recognized over a weighted-average period of 2.7 years.

Note 13: Fair Value Measurements

Generally accepted accounting principles define fair value, establish a framework for measuring fair value, and establish a hierarchy for determining fair value measurement. The hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities. The three levels are as follows:

Level 1: Valuation is based on quoted prices (unadjusted) for identical assets or liabilities in active markets;

Level 2: Valuation is determined from quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar instruments in markets that are not active or by model-based techniques in which all significant inputs are observable in the market; and

Level 3: Valuation is derived from model-based techniques in which at least one significant input is unobservable and based on the Company's own estimates about the assumptions that market participants would use to value the asset or liability.

The following is a description of the valuation methods used for instruments measured at fair value as well as the general classification of such instruments pursuant to the applicable valuation method.

Fair value measurements on a recurring basis

Securities available for sale – If quoted prices are available in an active market for identical assets, securities are classified within Level 1 of the hierarchy. If quoted market prices are not available, then fair values are estimated using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. As of June 30, 2016 and March 31, 2016, the Bank has categorized its investment securities available for sale as follows:

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total
<u>June 30, 2016</u>				
U.S. government agencies	\$ -	\$10,801,468	\$-	\$10,801,468
Municipal bonds	-	6,973,093	-	6,973,093
Corporate bonds	-	-	1,911,024	1,911,024
Mortgage-backed	-	60,837,793	-	60,837,793
Total investment securities available for sale	\$ -	\$78,612,354	\$1,911,024	\$80,523,378

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total
<u>March 31, 2016</u>				
U.S. government agencies	\$ -	\$10,532,996	\$-	\$10,532,996
Municipal bonds		4,112,564		4,112,564
Corporate bonds	-	-	1,898,640	1,898,640
Mortgage-backed	-	53,940,200	-	53,940,200
Total investment securities available for sale	\$ -	\$68,585,760	\$1,898,640	\$70,484,400

Derivative – Interest rate swap agreement – Our methodology consists of a discounted cash flow model where all future floating cash flows are projected and both floating and fixed cash flows are discounted to the valuation date. The curve utilized for discounting and projecting is built by obtaining publicly available third party market quotes. As of June 30, 2016, the bank has categorized its interest rate swap and related loan as follows:

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total
<u>June 30, 2016</u>				
Loans - Commercial real estate loan	\$ -	\$3,502,060	\$ -	\$3,502,060
Derivative - Interest rate swap agreement	\$ -	\$(266,553)	\$ -	\$(266,553)

The following table presents the valuation and unobservable inputs for Level 3 assets measured at fair value on a recurring basis at June 30, 2016:

Description	Fair Value	Valuation	Unobservable	Range of
-------------	------------	-----------	--------------	----------

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

		Methodology	Inputs	Inputs
Corporate bonds	\$ 1,911,024	3rd party valuation	Discount to reflect current market conditions	0.00% - 10.00%

Fair value measurements on a nonrecurring basis

Impaired Loans - The Bank has measured impairment generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values. As of June 30, 2016 and March 31, 2016, the fair values consist of loan balances of \$9,283,731 and \$7,438,106 that have been written down by \$303,649 and \$59,571, respectively, as a result of specific loan loss allowances.

Foreclosed real estate – The Bank's foreclosed real estate is measured at fair value less estimated cost to sell. As of June 30, 2016 and March 31, 2016, the fair value of foreclosed real estate was estimated to be \$460,780 and \$443,015, respectively. Fair value was determined based on offers and/or appraisals. Cost to sell the assets was based on standard market factors. The Company has categorized its foreclosed assets as Level 3.

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total
June 30, 2015				
Impaired loans	\$ -	\$ -	\$8,980,082	\$8,980,082
Foreclosed real estate	-	-	460,780	460,780
Premises and equipment held for sale	-	-	405,000	405,000
Loans held for sale	-	-	-	-
Total fair value of assets on a nonrecurring basis	\$ -	\$ -	\$9,845,862	\$9,845,862

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

	Level 1 inputs	Level 2 inputs	Level 3 inputs	Total
<u>March 31, 2016</u>				
Impaired loans	\$ -	\$-	\$7,378,535	\$7,378,535
Foreclosed real estate	-	-	443,015	443,015
Premises and equipment held for sale	-	-	405,000	405,000
Loans held for sale	-	266,176	-	266,176
Total fair value of assets on a nonrecurring basis	\$ -	\$266,176	\$8,226,550	\$8,492,726

The following table presents the valuation and unobservable inputs for Level 3 assets measured at fair value on a nonrecurring basis at June 30, 2016:

Description	Fair Value	Valuation Methodology	Unobservable Inputs	Range of Inputs
Impaired loans, net of allowance	\$ 8,980,082	Appraised value	Discount to reflect current market conditions	0.00% - 25.00%
		Discounted cash flows	Discount rates	2.63% - 7.25%
Foreclosed real estate	\$ 460,780	Appraised value	Discount to reflect current market conditions	0.00% - 25.00%
Premises and equipment held for sale	\$ 405,000	Appraised Value	Discount to reflect current	0.00% - 10.00%

market
conditions

The following table summarizes changes in foreclosed real estate for the three months ended June 30, 2016, which is measured on a nonrecurring basis using significant unobservable, level 3, inputs.

Balance, March 31, 2016	\$443,015
Transfer to foreclosed real estate	17,765
Proceeds from sale of foreclosed real estate	-
Loss on sale of foreclosed real estate	-
Balance, June 30, 2016	\$460,780

The remaining financial assets and liabilities are not reported on the balance sheets at fair value on a recurring basis. The calculation of estimated fair values is based on market conditions at a specific point in time and may not reflect current or future fair values.

Table Of Contents

HAMILTON BANCORP, INC AND SUBSIDIARY

Notes to Consolidated Financial Statements (unaudited)

	June 30, 2016		March 31, 2016	
	Carrying	Fair	Carrying	Fair
	amount	value	amount	value
<u>Financial assets</u>				
Level 1 inputs:				
Cash and cash equivalents	\$64,836,753	\$64,836,753	\$67,448,536	\$67,448,536
Level 2 inputs:				
Loans held for sale	-	-	259,450	266,176
Federal Home Loan Bank stock	1,640,100	1,640,100	1,042,500	1,042,500
Bank-owned life insurance	17,880,474	17,880,474	12,709,908	12,709,908
Level 3 inputs:				
Certificates of deposit held as investment	3,726,067	3,688,643	3,968,229	3,911,474
Loans receivable, net	328,202,687	331,149,847	218,604,150	220,671,409
<u>Financial liabilities</u>				
Level 3 inputs:				
Deposits	425,524,340	425,730,247	313,993,651	314,095,055
Advance payments by borrowers for taxes and insurance	3,069,417	3,069,417	1,079,794	1,079,794
Borrowings	28,487,127	29,912,592	14,805,237	15,146,307

The fair values of cash and cash equivalents and advances by borrowers for taxes and insurance are estimated to equal the carrying amount.

The fair value of loans held for sale is based on commitments from investors.

The fair value of Federal Home Loan Bank stock and bank-owned life insurance are estimated to equal carrying amounts, which are based on repurchase prices of the FHLB stock and the insurance company.

The fair value of fixed-rate loans is estimated to be the present value of scheduled payments discounted using interest rates currently in effect. The fair value of variable-rate loans, including loans with a demand feature, is estimated to equal the carrying amount. The valuation of loans is adjusted for estimated loan losses.

The fair value of certificates of deposit held as investments is estimated based on interest rates currently offered for borrowings of similar remaining maturities.

The fair value of interest-bearing checking, savings, and money market deposit accounts is equal to the carrying amount. The fair value of fixed-maturity time deposits is estimated based on interest rates currently offered for deposits of similar remaining maturities.

The fair value of borrowings is estimated based on interest rates currently offered for borrowings of similar remaining maturities.

The fair value of outstanding loan commitments and unused lines of credit are considered to be the same as the contractual amounts, and are not included in the table above. These commitments generate fees that approximate those currently charged to originate similar commitments.

Table Of Contents

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

Statements included in this management's discussion and analysis include non-GAAP financial measures and should be read along with the accompanying tables which provide a reconciliation of non-GAAP financial measures to GAAP financial measures. The Company's management uses these non-GAAP financial measures, including: (i) net income pre-acquisition related expenses; and (ii) tangible common equity, in its analysis of the Company's performance. The net income pre-acquisition related expenses and tangible common equity non-GAAP reconciliations, which include tangible book value per share, are presented within the “Summary of Recent Performance and Other Activities” section below.

Management believes that non-GAAP financial measures provide additional useful information that allows readers to evaluate the ongoing performance of the Company without regard to transactional activities. Non-GAAP financial measures should not be considered as an alternative to any measure of performance or financial condition as promulgated under GAAP, and investors should consider the Company's performance and financial condition as reported under GAAP and all other relevant information when assessing the performance or financial condition of the Company. Non-GAAP financial measures have limitations as analytical tools, and investors should not consider them in isolation or as a substitute for analysis of the Company's results or financial condition as reported under GAAP.

Safe Harbor Statement for Forward-Looking Statements

This report may contain forward-looking statements within the meaning of the federal securities laws. These statements are not historical facts; rather they are statements based on the Company’s current expectations regarding its business strategies and their intended results and its future performance. Forward-looking statements are preceded by terms such as “expects”, “believes”, “anticipates”, “intends”, and similar expressions.

Forward-looking statements are not guarantees of future performance. Numerous risks and uncertainties could cause or contribute to the Company’s actual results, performance, and achievements being materially different from those expressed or implied by the forward-looking statements. Factors that may cause or contribute to these differences include, without limitation, general economic conditions, including changes in market interest rates and changes in monetary and fiscal policies of the federal government, legislative and regulatory changes, the quality and composition of the loan and investment securities portfolio, loan demand, deposit flows, competition, and changes in accounting principles and guidelines. Additional factors that may affect our results are discussed in Part II, Item 1A of this form 10-Q and Item 1A of Hamilton Bancorp, Inc.’s Annual Report on Form 10-K filed June 29, 2016 with the Securities and Exchange Commission under the sections titled “*Risk Factors*”. These factors should be considered in evaluating the forward-looking statements, and undue reliance should not be placed on such statements. Except as required by applicable law or regulation, the Company assumes no obligation and disclaims any obligation to update

any forward-looking statements.

General

Hamilton Bancorp, Inc. (the “Company”) is a Maryland corporation incorporated on June 7, 2012 by Hamilton Bank (the “Bank”) to be its holding company following the Bank’s conversion from the mutual to the stock form of organization (the “Conversion”). The Conversion was completed on October 10, 2012. On that same date, the Company completed its public stock offering and issued 3,703,000 shares of its common stock for aggregate proceeds of \$37,030,000, and net proceeds of \$35,580,000. The Company’s business is the ownership of the outstanding capital stock of the Bank. The Company does not own or lease any property but instead uses the premises, equipment and other property of the Bank.

Founded in 1915 and recently celebrating its 100th year anniversary, the Bank is a community-oriented financial institution, dedicated to serving the financial service needs of consumers and businesses within its geographic area, which consists of Baltimore City, Baltimore County, Howard County, and Anne Arundel County in Maryland. We offer a variety of deposit products and provide loans secured by real estate located in our market area. Our real estate loans consist primarily of one-to four-family mortgage loans, as well as commercial real estate loans, and home equity loans and lines of credit. We also offer commercial term and line of credit loans and, to a limited extent, consumer loans. We currently operate out of our corporate headquarters in Towson, Maryland and our seven full-service branch offices located in Baltimore City, Cockeysville, Towson, Rosedale, Ellicott City and Pasadena, Maryland. The Bank is subject to extensive regulation, examination and supervision by the Office of the Comptroller of the Currency, its primary federal regulator, and the Federal Deposit Insurance Corporation, its deposit insurer. The Company is subject to regulation and supervision by the Board of Governors of the Federal Reserve System.

Table Of Contents

On May 13, 2016, the Company acquired Fraternity Community Bancorp, Inc. (“Fraternity”), the parent company of Fraternity Federal Savings and Loan in an all cash transaction for \$25.7 million. In addition, the Company acquired Fairmount Bancorp, Inc. (“Fairmount”), the parent company of Fairmount Bank on September 11, 2015 in an all cash transaction for \$14.2 million. Both acquisitions combined added three branches to our already existing branch structure in the Baltimore area.

The Company and the Bank maintain an Internet website at <http://www.hamilton-bank.com>. Information on our website should not be considered a part of this Quarterly Report on Form 10-Q.

Summary of Recent Performance and Other Activities

The Company and its wholly owned subsidiary, Hamilton Bank, continue to show improvement in net interest income, as well as loan growth and consistent asset quality during the three months ending June 30, 2016 compared to the same period a year ago. Net interest income improved \$1.1 million to \$3.1 million during the first three months of fiscal 2016 compared to the same period a year ago as the Company continued to show strong loan demand, closed on its acquisition of Fraternity and integrated its acquisition of Fairmount from last year. Non-interest expense increased \$1.4 million in the three months ending June 30, 2016 compared to the same period a year ago. Included in non-interest expense for the three months ending June 30, 2016 is \$674,000 in expenses relating to the acquisition of Fraternity and branch consolidation. Along with these expenses, there were additional expenses associated with operating as a larger institution. Management has diligently worked at monitoring and improving efficiencies to reduce our overall operating expenses and improve our efficiency ratio going forward.

The following highlights contain additional financial data and events that have occurred during the three months ended June 30, 2016:

Successfully completed the acquisition of Fraternity . As a result of the acquisition, total assets grew to \$522.8 million at June 30, 2016, representing growth of \$129.8 million or 33% compared to \$392.9 million in assets at March 31, 2016.

Total gross loans grew to \$332.3 million at June 30, 2016, up \$109.6 million, or 49%, compared to \$222.8 million at March 31, 2016. Growth in loans was attributable to both the acquisition of Fraternity and organic loan growth. Total deposits grew to \$425.5 million, up \$111.5 million, or 36%, compared to \$314 million over that same period. This growth included \$108.9 million in acquired Fraternity deposits

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Net interest income for the three months ended June 30, 2016 was \$3.1 million, an increase of \$1.1 million, or 55%, compared to \$2.0 million for the same period a year ago.

For the three months ending June 30, 2016, the Company reported a net loss of \$335,000 (loss of \$0.11 per common share) compared to net income of \$118,000 (earnings of \$0.04 per common share) for the same period a year ago. The comparative results were impacted by the acquisition and branch consolidation related expenses in the current period and the sale of our Towson branch in the first quarter of last year. Excluding these factors would result in adjusted net income and earnings per share as follows:

Net Income Excluding Acquisition and Branch Consolidation Related Expenses and Non-Recurring Revenue - (Non-GAAP)

	Three months ended June 30,		
	2016	2015	Difference
	(dollars in thousands)		
Reported pre-tax income (loss)	\$ (553)	\$ 305	\$ (858)
Add: Merger related expenses	237	231	6
Add: Branch consolidation expense	437	-	437
Less: Gain on sale of branch	-	(407)	407
Adjusted pre-tax income - (Non-GAAP)	121	129	(8)
Reported income tax expense (benefit)	(218)	186	(404)
Tax adjustment	266	(69)	336
Adjusted net income (loss) - Non-GAAP	\$ 73	\$ 13	\$ 60
Adjusted basic earnings per common share - Non-GAAP	\$ 0.02	\$ 0.00	\$ 0.03

- The non-GAAP financial measures shown above should not be viewed as a substitute for net income (loss) or earnings (loss) per share in accordance with GAAP. The Company's management believes that the presentation of net income on a non-GAAP basis, excluding acquisition related and other non-recurring expenses and gains, provides useful information for evaluating the Company's operating results and any related trends that may be affecting the Company's business.

Table Of Contents

Nonperforming loans as a percentage of gross loans declined to 1.35% at June 30, 2016 from 2.27% at March 31, 2016.

The allowance for loan losses as a percentage of nonperforming loans increased to 42.4% at June 30, 2016 from 33.7% at March 31, 2016.

Net charge-offs over the first three months ending June 30, 2016 were \$15,000 or 0.02% of average loans, on an annualized basis, compared to 0.22% for the twelve months ended March 31, 2016.

As a result of the acquisition of Fraternity, the Company acquired one branch that serviced the same area as an existing Hamilton branch. Based upon due diligence and the expense savings forecasted out, management chose to close the existing Hamilton branch and maintain the acquired Fraternity branch in that area. As part of closing the existing Hamilton branch, the Company recognized a \$437,000 expense that reflected the remaining term of the lease. This expense is reported as branch consolidation expense for the three months ending June 30, 2016.

The Company ended June 30, 2016 with a book value of \$18.06 per common share and a tangible book value of \$14.85 per common share compared to \$18.03 and \$15.87, respectively, at March 31, 2016. Tangible book value declined as a result of the goodwill and other intangible assets created in the Fraternity acquisition. Tangible book value, a non-GAAP measure, was determined as follows:

	June 30, 2016	March 31, 2016
Tangible book value per common share:		
Total shareholders' equity	\$61,663,340	\$61,544,583
Add: Other Comprehensive (Income) loss	(323,418)	21,819
Less: Goodwill and other intangible assets	(10,655,873)	(7,386,111)
Tangible common equity	\$50,684,049	\$54,180,291
Outstanding common shares	3,413,646	3,413,646
Book value per common share	\$18.06	\$18.03
Tangible book value per common share	\$14.85	\$15.87

Table Of Contents

The Company maintained strong liquidity and at June 30, 2016 the Bank was deemed “well capitalized” under federal regulations.

Pursuant to the merger agreement with Fraternity, the Fraternity stockholders received cash consideration of \$25.7 million or \$19.25 per common share outstanding. Included in Note 3 to the consolidated financial statements is additional discussion about the Fraternity acquisition.

Strategic Plan

We have based our 2017-2019 strategic plan on the objective of improving stockholder value and growth through creating sustainable and profitable growth given the current and expected economic and competitive environment in the financial industry. Our short-term goals include continuing the growth of our loan portfolio, changing the mix of our deposits base to be more concentrated in lower costing core deposits, collecting payments on non-accrual and past due loans, enhancing and improving credit quality, expanding fee income, maintaining a sensible branch network, and using technology to improve efficiencies and enhance the customer experience.

We identified several strategic priorities in our three year Strategic Plan. Those priorities included focusing on the following core areas:

Efficient Operating Revenue Growth – Generating sustainable, profitable operating revenue through smart growth of earning assets that are funded by low-cost core deposits and growth of noninterest income. In addition, focus on efficient utilization of the Bank’s assets. This strategic priority includes prudent loan growth, sales strategies to attract and grow small business deposit and other fee income services, strategic marketing campaigns, studying and benchmarking efficiency and productivity, and focusing on ways to utilize technology to drive earnings.

Well-defined and integrated delivery channels – Create and support delivery channels and branch strategy that leverages technology and optimizes efficiencies.

Acquisition strategy and planning - It is expected that the banking industry will continue to consolidate over the coming years due to a competitive market and the cost of regulatory compliance. Hamilton Bancorp is well positioned to take advantage of strategic opportunities that present themselves either through potential mergers or acquisitions in our marketplace. This may include other financial institutions, individual branches, or loan purchases. The focus will be on proactive evaluation and contact with potential targets and the implementation of a capital strategy to fund such acquisitions, including investor relations. These opportunities, however, will be aligned with

our strategic vision and goal of creating shareholder value and growth. We currently have no agreements or arrangements relating to any merger or acquisition.

Although the current economic climate continues to present significant challenges for the financial industry, management feels that based on our strategic initiatives we have positioned the Company to capitalize on the opportunities that may become available in the current economy, as well as a healthier economy going forward.

Critical Accounting Policies

The discussion and analysis of the financial condition and results of operations are based on our consolidated financial statements, which are prepared in conformity with generally accepted accounting principles used in the United States of America. The preparation of these consolidated financial statements requires management to make estimates and assumptions affecting the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and the reported amounts of income and expenses. We consider the accounting policies discussed below to be critical accounting policies. The estimates and assumptions that we use are based on historical experience and various other factors and are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions, resulting in a change that could have a material impact on the carrying value of our assets and liabilities and our results of operations.

Table Of Contents

For a discussion of significant accounting policies, see *Note 1—Nature of Operations and Summary of Significant Accounting Policies* in the Notes to our Consolidated Financial Statements. The following are the accounting policies that we believe require the most subjective or complex judgments, and as such could be most subject to revision as new information becomes available:

Allowance for Loan Losses. The allowance for loan losses is the estimated amount considered necessary to cover inherent credit losses in the loan portfolio at the balance sheet date. The allowance is established through the provision for losses on loans which is charged against income. In determining the allowance for loan losses, management makes significant estimates and has identified this policy as one of our most critical accounting policies.

Management, at a minimum, performs a quarterly evaluation of the allowance for loan losses. Consideration is given to historical losses in conjunction with a variety of other factors including, but not limited to, current economic conditions, delinquency statistics, geographic and industry concentrations, the adequacy of the underlying collateral, the financial strength of the borrower, results of internal loan reviews and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change.

The analysis has two components, specific and general allocations. Specific allocations can be made for estimated losses related to loans that are determined to be impaired. Impairment is measured by determining the present value of expected future cash flows or, for collateral-dependent loans, the fair value of the collateral adjusted for market conditions and selling expenses. If the fair value of the loan is less than the loan's carrying value, a charge is recorded for the difference. The general allocation is determined by segregating the remaining loans by type of loan, risk weighting (if applicable) and payment history. We also analyze historical loss experience, delinquency trends, general economic conditions and geographic and industry concentrations. This analysis establishes factors that are applied to the loan groups to determine the amount of the general reserve.

We cannot predict with certainty the amount of loan charge-offs that we will incur. Our regulatory agencies, as an integral part of their examination processes, periodically review our allowance for credit losses. Such agencies may require that we recognize additions to the allowance for credit losses based on their judgments about information available to them at the time of their examination. To the extent that actual outcomes differ from management's estimates, additional provisions to the allowance for credit losses may be required that would adversely impact earnings in future periods.

Securities Valuation and Impairment. We classify our investments in debt and equity securities as either held to maturity or available for sale. Securities classified as held to maturity are recorded at cost or amortized cost. Available-for-sale securities are carried at fair value. We obtain our fair values from a third party service. This service's fair value calculations are based on quoted market prices when such prices are available. If quoted market prices are not available, estimates of fair value are computed using a variety of techniques, including extrapolation

from the quoted prices of similar instruments or recent trades for thinly traded securities, fundamental analysis, or through obtaining purchase quotes. Due to the subjective nature of the valuation process, it is possible that the actual fair values of these investments could differ from the estimated amounts, thereby affecting our financial position, results of operations and cash flows.

If the estimated value of investments is less than the cost or amortized cost, we evaluate whether an event or change in circumstances has occurred that may have a significant adverse effect on the fair value of the investment. If such an event or change has occurred and we determine that the impairment is other-than-temporary, we record the impairment of the investment in the period in which the event or change occurred. We also consider how long a security has been in a loss position in determining if it is other than temporarily impaired. Management also assesses the nature of the unrealized losses taking into consideration factors such as changes in risk-free interest rates, general credit spread widening, market supply and demand, creditworthiness of the issuer, and quality of the underlying collateral. At June 30, 2016, all of our securities were either issued by U.S. government agencies, U.S. government-sponsored enterprises, municipalities, or corporations.

Table Of Contents

Goodwill Impairment. Goodwill represents the excess purchase price paid for Fairmount and our Pasadena branch over the fair value of the net assets acquired. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The Company is considered the Reporting Unit for purposes of impairment testing. Impairment testing requires that the fair value of the Company be compared to the carrying amount of the Company's net assets, including goodwill. If the fair value of the Company exceeds the book value, no write-down of recorded goodwill is required. If the fair value of the Company is less than book value, an expense may be required to write-down the related goodwill to the proper carrying value. We test for impairment of goodwill during February of each year. We estimate the fair value of the Company utilizing four valuation methods including the Comparable Transactions Approach, the Control Premium Approach, the Public Market Peers Approach, and the Discounted Cash Flow Approach.

Based on our impairment testing as of February 2016, there was no evidence of impairment of the Company's goodwill or intangible assets.

Business Combinations. GAAP requires that the acquisition method of accounting, formerly referred to as purchase method, be used for all business combinations and that an acquirer be identified for each business combination. Under GAAP, the acquirer is the entity that obtains control of one or more businesses in the business combination, and the acquisition date is the date the acquirer achieves control. GAAP requires that the acquirer recognize the fair value of assets acquired, liabilities assumed, and any non-controlling interest in the acquired entity at the acquisition date

Income Taxes. We account for income taxes under the asset/liability method. We recognize deferred tax assets for the future consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as operating loss and tax credit carry-forwards. We measure deferred tax assets and liabilities using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. We recognize the effect on deferred tax assets and liabilities of a change in tax rates in income in the period indicated by the enactment date. We establish a valuation allowance for deferred tax assets when, in the judgment of management, it is more likely than not that such deferred tax assets will not become realizable. The judgment about the level of future taxable income is dependent to a great extent on matters that may, at least in part, be beyond our control. It is at least reasonably possible that management's judgment about the need for a valuation allowance for deferred tax assets could change in the near term.

Comparison of Financial Condition at June 30, 2016 and March 31, 2016

Assets. Total assets increased \$129.8 million, or 33.0%, to \$522.8 million at June 30, 2016 from \$392.9 million at March 31, 2016. The increase is primarily attributable to \$151.9 million in identifiable assets acquired in the Fraternity acquisition, along with \$3.4 million in intangible assets that were created.

Cash and Cash Equivalents. Cash and cash equivalents decreased by \$2.6 million, or 3.9%, to \$64.8 million at June 30, 2016 from \$67.4 million at March 31, 2016. The decrease in cash is a result of the \$25.7 million in cash paid for the Fraternity acquisition, partially offset by the \$15.2 million in cash acquired in the transaction, along with growth in our deposit base and a decrease in our investment portfolio due to normal principal pay-down of our mortgage backed securities.

Certificates of Deposit Held as Investment. Certificates of deposit declined \$242,000 from \$4.0 million at March 31, 2016 to \$3.7 million at June 30, 2016. The decline resulted from \$735,000 in certificates of deposit that matured, partially offset by \$498,000 in certificates of deposit that were acquired in the Fraternity acquisition that are held as investments. The certificates of deposit held consist of individual amounts that are equal to or less than \$250,000 and fully insured by the FDIC. The weighted average term of the portfolio is 1.6 years.

Investment Securities. Our investment portfolio consists primarily of investment grade securities including U.S. government agency and government-sponsored entity securities, securities issued by states, counties and municipalities, corporate bonds, and mortgage-backed securities. At June 30, 2016, all securities are classified as available for sale. While we usually intend to hold investment securities until maturity, this classification provides us the opportunity to divest of securities that may no longer meet our liquidity objectives. During the three months ending June 30, 2016, we did not purchase or sell any securities.

Table Of Contents

Investment securities increased \$10.0 million, or 14.2%, to \$80.5 million at June 30, 2016, from \$70.5 million at March 31, 2016. The increase is attributable to \$17.6 million in securities acquired in the Fraternity acquisition, partially offset by \$1.7 million in agency and municipal securities that were called and \$4.8 million in monthly principal pay-downs associated with collateralized mortgage obligations and mortgage-backed securities issued by GSEs (Government Sponsored Enterprise). The fair value of the investment portfolio increased \$570,000 from an unrealized loss position of \$36,000 at March 31, 2016 to an unrealized gain position of \$534,000 at June 30, 2016. The increase in fair value of the investment portfolio is a result of the decrease in interest rates over the past three months.

We have evaluated securities with unrealized losses for an extended period of time and determined that these losses are temporary because, at this point in time, we have the ability to hold them until maturity. Currently, we have no intent to sell these securities, however, if market conditions or funding needs change, we may sell securities if needed. As the maturity date moves closer and/or interest rates decline, we expect that any unrealized losses for individual securities in the portfolio will decline or dissipate. As a result, we have not identified any portion of the unrecorded loss as being attributed to credit deterioration in the issuer of the security.

Loans. Excluding loans held for sale and loan origination fees and costs, gross loans receivable increased by \$109.6 million, or 49.2%, to \$332.3 million at June 30, 2016 from \$222.8 million at March 31, 2016. Included in loans and leases at June 30, 2016 is \$108.6 million in loans associated with the Fraternity acquisition (included in the “acquired” loan column of the table below, along with loans acquired from the Fairmount acquisition). At June 30, 2016, gross loans receivable represented 63.6% of total assets compared to 56.7% of total assets at March 31, 2016.

The following table details the composition of loans, excluding loans held for sale, and the related percentage mix and growth of total loans:

	June 30, 2016			Percent of Total	March 31, 2016			Percent of Total	Ye Gr An
	Legacy	Acquired	Total		Legacy	Acquired	Total		
Real estate loans:									
One-to four-family:									
Residential	\$45,442,298	\$97,700,553	\$143,142,851	43 %	\$46,263,709	\$23,036,569	\$69,300,278	31 %	7
Residential construction	5,524,789	844,287	6,369,077	2 %	4,304,189	965,440	5,269,629	2 %	1
Investor	11,825,432	23,606,757	35,432,189	11 %	12,076,911	15,783,008	27,859,919	13 %	7
Commercial	81,155,633	17,875,858	99,031,491	30 %	75,225,984	2,889,219	78,115,203	35 %	2

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Commercial construction	2,348,741	1,615,922	3,964,663	1 %	1,982,571	1,274,148	3,256,719	2 %	7
Total real estate loans	146,296,893	141,643,377	287,940,271	87 %	139,853,364	43,948,384	183,801,748	83 %	1
Commercial business	15,985,673	2,714,738	18,700,411	6 %	17,773,967	2,621,625	20,395,592	9 %	(
Home equity loans	12,293,585	9,495,334	21,788,919	6 %	12,222,688	2,168,073	14,390,761	6 %	7
Consumer	2,875,534	1,031,516	3,907,050	1 %	3,072,677	1,106,434	4,179,111	2 %	(
Total loans	\$ 177,451,685	\$ 154,884,965	\$ 332,336,651	100 %	\$ 172,922,696	\$ 49,844,516	\$ 222,767,212	100 %	\$ 1

Approximately \$74.9 million, or 69%, of the \$108.6 million in loans acquired in the Fraternity acquisition consisted of one-to four-family residential loans, while \$9.2 million, or 8.5%, of those loans acquired consisted of investor real estate loans. Investor real estate loans represent funds advanced to borrowers for the purchase or refinance of non-owner occupied one- to four-family properties. These loans make up \$23.6 million, or 15.2%, of the \$154.9 million in acquired loans as of June 30, 2016. In addition, \$14.2, or 13.1%, in commercial real estate loans and \$7.4, or 6.8%, million in home equity loans were also acquired from Fraternity.

Table Of Contents

Organically, the Bank continues to focus on growing both commercial real estate and commercial business loans as these loans offer higher rates of return and shorter maturity periods than typical retail lending. The largest increase organically in loans over the first three months of fiscal 2017, as shown in the previous table under “legacy”, is a \$5.9 million, or 7.9%, increase in commercial real estate loans from \$75.2 million at March 31, 2016 to \$81.2 million at June 30, 2016. Commercial business loans declined \$1.8 million, or 10.1%, to \$16.0 million at June 30, 2016 from \$17.8 million at March 31, 2016. This decrease is related to a borrower that was asked to obtain alternative financing as they were no longer a good fit for the bank from a credit risk perspective. The Bank continues to see the benefits of our new commercial lending platform that has been restructured with new personnel and improved underwriting and monitoring procedures from both an origination and credit quality perspective.

The Bank continues to originate traditional one-to four-family residential loans and sell them in the secondary market at a premium in order to manage interest rate risk in a rising rate environment. Beginning in fiscal 2015, the Bank began to promote its one- to four-family residential construction lending program. During the first three months of fiscal 2017, the Bank has originated roughly \$7.6 million in residential construction loans. As a result, at June 30, 2016 we had \$13.3 million in residential construction commitments, of which \$5.9 million in funds have been advanced; compared to \$7.9 million in residential construction commitments at March 31, 2016 of which \$2.6 million in funds had been advanced. The construction period on residential homes is typically nine to twelve months, at which time Hamilton Bank is often repaid through permanent financing by a third party.

Deposits. Total deposits (excluding premiums on acquired deposits) increased \$110.5 million, or 35.2%, to \$424.2 million at June 30, 2016 from \$313.7 million at March 31, 2016, including \$110.0 million in deposits assumed in the Fraternity acquisition. Approximately \$22.4 million, or 20.4%, of the acquired deposits from Fraternity were core deposits (which we consider to be all deposits other than certificates of deposit). The Company continues to focus on changing its deposit mix to rely less on time deposits as a primary funding source and attract lower costing core deposits, including money market accounts. With the Fraternity acquisition, core deposits increased \$24.3 million, or 20.5%, to \$143.0 million at June 30, 2016 compared to \$118.6 million at March 31, 2016.

The following table details the composition of deposits and the related percentage mix and growth of total deposits.

	June 30, 2016		March 31, 2016		Year-To-Date Growth	
	Total	Percent of Total	Total	Percent of Total	Amount	Growth Percent
Savings	\$45,282,733	11 %	\$33,010,962	11 %	\$12,271,771	37 %
Noninterest-bearing checking	22,132,850	5 %	19,747,437	6 %	2,385,413	12 %
Interest-bearing checking	17,089,730	4 %	13,298,677	4 %	3,791,053	29 %
Money market accounts	58,479,057	14 %	52,576,567	17 %	5,902,490	11 %

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Time deposits	281,215,426	66	%	195,031,411	62	%	86,184,015	44	%
	\$424,199,796	100	%	\$313,665,054	100	%	\$110,534,742	35	%
Premium on deposits assumed	1,324,544			328,597			995,947		
Total deposits	\$425,524,340			\$313,993,651			\$111,530,689		

Our strategy with respect to deposits has been to maintain or shrink our current certificates of deposit base, based upon liquidity needs, and focus on growing our core deposits at a faster pace to reduce our overall cost of funds.

Borrowings. Borrowings consist of both short and long-term advances from the Federal Home Loan Bank (FHLB). At June 30, 2016, the Company had \$28.9 million in FHLB borrowings outstanding compared to \$14.8 million at the beginning of the year. The increase over the first three months of fiscal 2017 is attributable to \$15.0 million in FHLB advances assumed in the Fraternity acquisition. These borrowings were longer term borrowings and are coming due in one to three years and carry rates of 3.4% to 4.3%. As a result of these higher stated rates, we were able to record a discount of \$794,000 when accounting for the borrowings at fair value at acquisition. At June 30, 2016 the discount is at \$724,000. The accretion of this discount will offset the higher stated rate of these borrowings. Partially offsetting this increase in advances was a \$2.0 million advance that matured during the most recent quarter with a stated interest rate of 0.43%.

Table Of Contents

At June 30, 2016, \$3.5 million of the total advances are considered short-term and mature in less than one year, while the remaining \$24.0 million are considered long-term; maturing in a year or more. The longest outstanding borrowing is for \$5.0 million and matures in October 2018.

The FHLB borrowings provide an alternative means to support the cash outflow needed to fund new loan originations in coordination with deposit growth. FHLB borrowings can provide a less expensive means to support cash outflow when compared to selling higher yielding investment securities. These obligations are secured by our residential and home equity loan portfolios. At June 30, 2016, we had the ability to borrow approximately \$49.9 million in additional funds from the FHLB, subject to our pledging sufficient assets. These obligations will be repaid as our cash position strengthens.

Equity. Total equity increased \$119,000, or 0.2%, to \$61.6 million at June 30, 2016 from \$61.5 million at March 31, 2016. Overall equity was not materially impacted by the acquisition of Fraternity due to the acquisition being an all cash transaction. The increase is primarily attributable to the \$345,000 increase in accumulated other comprehensive income associated with an increase in the fair value of the investment portfolio from declining interest rates over the first quarter. Additional paid in capital also increased \$109,000 as a result of the expense derived from equity awards granted in prior periods. These increases were partially offset by the net loss of \$355,000 that was recorded for the quarter ending June 30, 2016. The Company's book value per share was \$18.06 at June 30, 2016 compared to \$18.03 at March 31, 2016.

Comparison of Asset Quality at June 30, 2016 and March 31, 2016

The Bank's asset quality remains a primary focus of management and the Board of Directors. Nonperforming assets at June 30, 2016, were \$4.9 million, a decrease of \$598,000 from March 31, 2016 and a \$1.8 million increase from June 30, 2015. Nonperforming assets to total assets decreased from 1.40% at March 31, 2016 to 0.94% at June 30, 2016. Nonperforming assets for the respective periods were as follows:

	At	At	At
	June	March	June
	30,	31,	30,
	2016	2016	2015
	(dollars in thousands)		
Nonaccruing loans	\$4,417	\$4,342	\$2,094

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Accruing loans delinquent more than 90 days	17	708	600
Foreclosed real estate	461	443	443
Total nonperforming assets	\$4,895	\$5,493	\$3,137

Asset Quality Ratios:

Nonperforming loans to gross loans	1.33 %	2.27 %	1.59 %
Nonperforming assets to total assets	0.94 %	1.40 %	1.08 %
Net charge-offs (annulized) to average loans	0.02 %	0.22 %	0.04 %

Included in nonperforming loans are accruing loans delinquent more than 90 days. These loans represent loans that are on accrual status and paying under the contractually agreed upon terms of the note, however, such loans are 90 days past their contractual maturity date, and therefore reported as nonperforming. At March 31, 2016 these loan balances were elevated as they related to many smaller investor (residential non-owner occupied) loans that matured at the same time. The Bank's credit department has diligently worked through many of these loans over the past quarter and have either renewed or extended them accordingly.

Nonaccrual loans increased slightly to \$4.4 million at June 30, 2016 compared to \$4.3 million at March 31, 2016. A large portion of the non-accrual loans reported at June 30, 2016 and March 31, 2016 consist of two commercial real estate loans that are related. Together these loans have a contractual principal balance of \$3.4 million and a recorded investment balance of \$2.7 million, including \$567,000 charge-off to date. The loans were placed on non-accrual in October 2015 due to legal issues and the concern of collectability. The borrower is classified as a Trouble Debt Restructure ("TDR") and continues to make interest only payments as agreed, which are being applied by the Bank as a principal reduction to the loans. The property is currently listed for sale by a broker. As of June 30, 2016, there was no other commercial real estate or business loans on nonaccrual.

Table Of Contents

Nonaccrual loans also consisted of \$930,000 in non-owner occupied investor loans as of June 30, 2016, the majority of which were acquired through the acquisition of Fairmount Bank. This group of loans primarily consists of three separate borrowers/investors that have individual loans on multiple properties. The remaining balance of nonaccrual loans at June 30, 2016 consist of traditional one- to four-family residential mortgages. Nonaccrual loans attributable to the acquisition of Fraternity included one home equity line of credit for \$12,000.

Foreclosed real estate increased \$18,000 from \$443,000 at March 31, 2016 to \$461,000 at June 30, 2016 and consisted of two properties. The first property represents semi-developed land in the amount of \$443,000. The property is listed for sale and is participated with another financial institution, with Hamilton being the lead lender. The second property was added to foreclosed real estate during the current quarter in the amount of \$18,000. This property is residential real estate that represented a participation bought by Hamilton. Hamilton participated in 20% of the original loan amount with another financial institution, who is the lead lender.

The Bank recorded a \$210,000 provision for loan loss during the first quarter of fiscal 2017 compared to no provision for loan loss for the same period a year ago. The provision for loan loss for the recent quarter was a result of an increase in organic loan growth and the granting of a concession to two already existing one-to four-family residential TDRs. The allowance for loan losses at June 30, 2016 totaled \$1.9 million, or 0.57% of total gross loans, compared to \$1.7 million, or 0.76% of total gross loans, at March 31, 2016. This decrease in percentage is related to the increase in overall loan balances associated with the Fraternity acquisition in May 2016. As outlined in note 3 to our consolidated financial statements, loans acquired in an acquisition are recorded at estimated fair value on their purchase date with no carryover of the related allowance for loan and lease losses. We continue to monitor and manage the acquired loan portfolio to determine if additional provisions are necessary in relation to the estimated fair value placed on those loans as determined by management.

The activity in the allowance for loan losses for the three month period ending June 30, 2016 includes \$32,000 in charge-offs, offset by \$16,000 in recoveries and a \$210,000 provision for loan losses. We currently review the adequacy of the allowance for loan losses on a monthly basis and are proactively managing problem assets. Based upon our analysis, we believe this allowance appropriately reflects the inherent risk of loss in our loan portfolio at June 30, 2016. We estimate the allowance for loan losses within a range based upon our historical charge-off history and certain environmental factors.

Results of Operations for the Three Months Ended June 30, 2016 and 2015 (unaudited)

General. Net loss available to common shareholders was \$335,000 or \$(0.11) per basic and diluted common share for the three month period ended June 30, 2016 compared to net income available to common shareholders of \$118,000 or \$0.04 per basic and diluted common share for the same period in fiscal 2016, a decline of \$453,000 in earnings. The decrease in net results of operations resulted primarily from a \$210,000 increase in the provision for loan loss, a

\$1.4 million increase in noninterest expense, and a \$360,000 decrease in noninterest revenue, partially offset by a \$1.1 million increase in net interest income and a \$404,000 decrease in income tax expense.

Net Interest Income. Net interest income increased \$1.1 million, or 55.0%, to \$3.1 million for the three months ended June 30, 2016 compared to \$2.0 million for the three months ended June 30, 2015. The increase in net interest income was due to a \$1.4 million increase in interest revenue, partially offset by a \$276,000 increase in interest expense. The increase in interest revenue was due to an increase in the average balance of interest-earning assets, particularly higher yielding loans, as well as a slight increase in average yield on interest-earning assets. The average balance in interest-earning assets increased \$152.8 million, or 56.2%, for the quarter ended June 30, 2016 compared to the same period in fiscal 2016, while the average yield increased 3 basis points to 3.53% from 3.50%, respectively. The average balances increased quarter-over-quarter due to the acquisitions of Fairmount and Fraternity which occurred subsequent to the June 30, 2015 quarter. Over this period, the Bank was able to also increase organically the average balance of higher interest-earning assets, particularly loans, which grew a net of \$7.8 million, excluding the effect of our acquisitions.

Table Of Contents

The increase in the average balance of interest-earning assets for the quarter ended June 30, 2016 was offset by a \$161.7 million increase in the average balance of interest-bearing liabilities for the same period. The increase is attributable to deposits and borrowings acquired in the Fairmount and Fraternity acquisitions, as well as management's focus on increasing our deposit base to fund organic loan growth. The average cost of interest-bearing liabilities for the comparative periods remained relatively flat, declining 1 basis point from 0.71% for the quarter ended June 30, 2015 to 0.70% for the quarter ended June 30, 2016. Our net interest margin decreased 2 basis points from 2.94% for the three months ended June 30, 2015 to 2.92% for the three months ended June 30, 2016.

Interest Revenue. Interest revenue increased \$1.4 million, or 57.9% to \$3.8 million during the three months ended June 30, 2016 compared to the three months ended June 30, 2015, as a result of increases in interest and fees on loans, partially offset by a decrease in revenue from investment securities.

Interest and fees on loans increased \$1.4 million, or 70.9%, to \$3.3 million for the three months ended June 30, 2016, compared to \$1.9 million for the three months ended June 30, 2015. The increase in interest and fees on loans is due to a \$115.8 million increase in the average balance of net loans from \$162.4 million to \$278.2 million quarter-over-quarter. The increase in average loans is attributable to the loans acquired in both the Fairmount and Fraternity acquisitions that were completed subsequent to June 30, 2015, as well as our new commercial lending platform and staff that was put in place at the beginning of fiscal 2015. The average yield earned on loans remained relatively unchanged, decreasing 1 basis point from 4.78% for the three months ended June 30, 2015 to 4.77% for the three months ending June 30, 2016. The yield on average loans, although relatively unchanged in comparing the June 30, 2016 and 2015 quarters, continues to be impacted by the extended low interest rate environment and the competitive pressure relating to pricing.

Interest revenue on investment securities decreased \$62,000 to \$367,000 during the three months ended June 30, 2016 from \$429,000 during the three months ended June 30, 2015. The average balance of investment securities decreased by \$13.0 million, or 14.2%, to \$78.6 million during the three months ended June 30, 2016 from \$91.5 million during the same period last year, while the average yield remained unchanged at 1.87%. The largest decrease in investment securities was in mortgage-backed securities, which declined \$12.0 million to \$57.2 million for the three months ended June 30, 2016 from \$69.2 million for the same period last year. The proceeds from the decrease in mortgage-backed securities have been used to fund the increase in the average loans associated with organic growth over the same period, as well as to assist in building up cash reserves for the \$25.7 million, all cash acquisition of Fraternity that closed on May 13, 2016.

Interest Expense. Interest expense increased \$276,000, or 73.3%, to \$654,000 for the three months ended June 30, 2016 compared to \$377,000 for the same period in fiscal 2016, due to the increase in the average balance of both interest-bearing deposits and borrowings. Average interest-bearing deposits increased \$145.2 million, or 70.8%, to \$350.3 million for the three months ended June 30, 2016 from \$205.1 million for the three months ended June 30, 2015. The average cost of deposits declined slightly from 0.73% to .070% over those same periods, a 3 basis point decline. A significant portion of our time deposits have already repriced in today's low interest rate environment, as a

result, the change in interest expense is more attributable to the increase in average balances than to interest rates.

For the three month period ended June 30, 2016, average interest-bearing deposit balances increased for all types of deposits when compared to the same period last year as a result of both the Fraternity and Fairmount acquisitions, as well as promotional efforts to raise funds for new loan growth. We remain focused on changing the mix of our deposit portfolio by maintaining our maturing certificates of deposits and growing lower cost core deposits, including savings, interest-bearing checking and money market accounts. The average balance of time deposits increased \$92.3 million, or 62.3%, to \$240.3 million for the quarter ended June 30, 2016 compared to \$148.1 million for the quarter ended June 30, 2015. Over this same period, core interest bearing deposits increased \$52.9 million, or 92.9%, to \$109.9 million for the three months ended June 30, 2016 compared to \$57.0 million for the three months ended June 30, 2015. The growth in core deposits was primarily a result of the continued efforts by our cash management and financial service teams, as well as those core deposits assumed in the Fraternity and Fairmount acquisitions.

Noninterest-bearing deposits allow us to fund growth in interest-earning assets at minimal cost. As a result of the growth generated from the efforts of our cash management personnel, commercial loan officers working with commercial clients to move their deposit relationship to Hamilton Bank and the acquisitions of Fraternity and Fairmount, average noninterest-bearing deposits increased \$2.8 million, or 14.7%, to \$22.0 million for the three months ended June 30, 2016, compared to \$19.1 million for the three months ended June 30, 2015.

Table Of Contents

For the three month period ended June 30, 2016, the average interest-bearing borrowings were \$22.5 million compared to an average balance of \$6.0 million for the same period a year ago. The borrowings consisted entirely of advances from the Federal Home Loan Bank (“FHLB”). At June 30, 2016, the Bank had \$27.5 million in outstanding advances from the FHLB, including \$25.5 million in borrowings assumed through the Fraternity and Fairmount acquisitions. These borrowings carried an average rate of 0.75% for the three months ended June 30, 2016. Borrowing from the FHLB in today’s low interest rate environment can be a more cost effective means to obtain funds if deposits are not growing compared to selling investment securities that were earning a higher yield.

Average Balances, Interest and Yields. The following table presents information regarding average balances of assets and liabilities, the total dollar amounts of interest revenue from average interest-earning assets, the dollar amounts of interest expense on average interest-bearing liabilities, and the resulting annualized average yields and costs. The yields and costs for the periods indicated are derived by dividing revenue or expense by the average balances of assets or liabilities, respectively, for the periods presented. Average balances have been calculated using average daily balances. No tax-equivalent adjustments were made. Nonaccrual loans have been included in the table as loans carrying a zero yield.

Table Of Contents

	Three Months Ended June 30, (dollars in thousands)					
	2016			2015		
	Average	Yield/ Interest	Yield/ Cost	Average	Yield/ Interest	Yield/ Cost
	Balance			Balance		
Interest-earning assets:						
Cash and cash equivalents	\$67,668	\$ 67	0.40%	\$17,698	\$ 5	0.11%
Investment securities (1)	21,393	136	2.54%	22,346	131	2.34%
Mortgage-backed securities	57,177	231	1.62%	69,203	298	1.72%
Loans receivable, net (2)	278,202	3,316	4.77%	162,443	1,941	4.78%
Total interest-earning assets	424,440	3,750	3.53%	271,690	2,375	3.50%
Noninterest-earning assets	35,325			21,449		
Total assets	\$459,765			\$293,139		
Interest-bearing liabilities:						
Certificates of deposit	\$240,336	\$ 565	0.94%	\$148,059	\$ 361	0.98%
Money Market	54,358	31	0.23%	27,679	8	0.12%
Statement savings	39,442	15	0.15%	17,560	2	0.05%
NOW accounts	16,139	1	0.02%	11,764	1	0.03%
Total interest-bearing deposits	350,275	612	0.70%	205,062	372	0.73%
Borrowings	22,479	42	0.75%	6,000	5	0.33%
Total interest-bearing liabilities	372,754	654	0.70%	211,062	377	0.71%
Noninterest-bearing liabilities and equity:						
Noninterest-bearing deposits	21,950			19,142		
Other noninterest-bearing liabilities	5,701			1,886		
Total liabilities	400,405			232,090		
Total shareholders' equity	59,360			61,049		
Total liabilities and shareholders' equity	\$459,765			\$293,139		
Net interest income		\$ 3,096			\$ 1,998	
Net interest rate spread (3)			2.83%			2.78%
Net interest-earning assets (4)	\$51,686			\$60,628		
Net interest margin (5)			2.92%			2.94%
Average interest-earning assets to average interest-bearing liabilities	113.87 %			128.73 %		

(1) Includes U.S agency and treasury securities, municipal and corporate bonds and to a much lesser extent, Federal Home Loan Bank equity securities.

(2) Loans on non-accrual status are included in average loans carrying a zero yield.

(3) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.

- (4) Net interest-earning assets represents total interest-earning assets less total interest-bearing liabilities.
- (5) Net interest margin represents net interest income divided by average total interest-earning assets.

Provision for Loan Losses. We establish provisions for loan losses that are charged to operations in order to maintain the allowance for loan losses at a level believed, to the best of management's knowledge, to cover all known and inherent losses in the portfolio both probable and reasonable to estimate at each reporting date. There was \$210,000 charged to the provision for loan losses for the three months ended June 30, 2016 compared to no provision for the three months ended June 30, 2015. In the current quarter, a \$170,000 of the \$210,000 charged to the provision for loan loss is related to two performing TDRs that were charged a risk adjusted rate of interest when their modified rate period expired. The remaining provision is related to organic loan growth and not necessarily a product of charge-offs, as reflected in the table below. Management identified probable losses in the loan portfolio and recorded net charge-offs of \$15,000 for the three months ended June 30, 2016, compared to \$17,000 for the comparable period a year ago.

Table Of Contents

The allowance for loan losses was \$1.9 million, or 42.4% of non-performing loans at June 30, 2016 compared to \$1.7 million, or 62.1% of non-performing loans at June 30, 2015. The decrease in the percentage is due to two related commercial real estate loans with a recorded investment balance of \$2.7 million that were placed on non-accrual in October 2015. We charged-off \$567,000 of this loan in March 2016.

During the three months ended June 30, 2016, loan charge offs totaled \$31,000 with recoveries of \$16,000, compared to \$84,000 in charge offs and \$67,000 in recoveries during the three months ended June 30, 2015. During fiscal year 2017, we expect that we will continue our emphasis in growing commercial real estate and commercial business loans, which have higher interest rates than one-to four-family mortgage loans, but are generally considered to bear higher risk than one-to four-family mortgage loans and could contribute to higher provisions going forward.

Summary of Allowance for Loan Losses Activity. The following table sets forth an analysis of the allowance for loan losses for the periods indicated.

	Three Months Ended June 30, 2016 2015	
	(dollars in thousands)	
Allowance for loan losses at beginning of period	\$1,702	\$1,690
Charge-offs:		
Real estate loans:		
One-to four-family	28	60
Commercial	-	-
Construction	-	-
Commercial	2	10
Home equity	-	6
Consumer	1	8
Total charge-offs	31	84
Recoveries	16	67
Net charge-offs	15	17
Provision for loan losses	210	-
Allowance for loan losses at end of period	\$1,897	\$1,673
Allowance for loan losses to non-performing loans	42.44 %	62.12 %
Allowance for loan losses to total loans outstanding at the end of the period	0.57 %	0.98 %
Net charge-offs to average loans outstanding during the period (annualized)	0.02 %	0.04 %

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Noninterest Revenue. Noninterest revenue decreased \$361,000, or 57.2%, to \$269,000 for the three months ended June 30, 2016, compared to \$630,000 for the three months ended June 30, 2015. The following table outlines the changes in noninterest revenue for the three month periods.

	Three months ended June 30,		\$ Change	% Change
	2016	2015		
Service charges	\$95,120	\$95,078	\$42	-
Gain on sale of loans held for sale	11,172	16,998	(5,826)	(34.3)
Gain on sale of property and equipment	-	407,188	(407,188)	N/A
Earnings on bank-owned life insurance	112,526	87,742	24,784	28.2
Other fees and commissions	50,680	22,997	27,683	120.4
Total noninterest revenue	\$269,498	\$630,003	\$(360,505)	(57.2)

Table Of Contents

Noninterest revenue decreased in large part due to a \$407 thousand gain on the sale of the Towson branch property in the 2015 period, which closed in early May 2015. Excluding this gain, non-interest revenue increased \$47 thousand, or 21.0%, compared to the comparable period last year.

The increase in earnings on bank-owned life insurance (BOLI) is associated with \$5.1 million in BOLI assumed by Hamilton in the Fraternity acquisition. The revenue earned from BOLI is exempt for tax purposes. Other fees and commissions are related to loan fees charged to customers, including \$26,000 in extension fees to commercial loan borrowers.

Offsetting these increases in noninterest revenue was a decrease in gains on the sale of loans held for sale. The decrease is attributable to the revenues earned on loans sold in the secondary and premiums associated with such sales. We sell a majority of our newly originated one-to four-family residential mortgage loans with a maturity greater than 10 years to the secondary market with service released to assist in managing our interest rate risk in anticipation of rising interest rates.

Service charges associated with retail deposit products remained unchanged quarter-over-quarter. We have continued to focus on growing our core deposits, particularly checking accounts, which typically generate more service fee income. We continually review our fee structure on transactional accounts so that we may be more aligned with our market. Customers, however, have become more cost conscious of fees and better manage their deposit relationship with the Bank. There was also no change with respect to gain on sale of investment securities as a result of there being no sale of securities in either quarter.

Noninterest Expense. Noninterest expense increased \$1.4 million, or 59.7%, to \$3.7 million for the three months ended June 30, 2016 compared to the three months ended June 30, 2015. The following table outlines the changes in noninterest expense for the three month periods.

	Three months ended			% Change
	June 30,			
	2016	2015	\$ Change	
Salaries and benefits	\$1,780,273	\$1,200,422	\$579,851	48.3
Occupancy	215,900	174,626	41,274	23.6
Advertising	31,351	27,363	3,988	14.6
Furniture and equipment	98,323	78,440	19,883	25.3
Data processing	185,723	141,988	43,735	30.8
Legal services	50,263	28,634	21,629	75.5
Other professional services	100,098	95,094	5,004	5.3

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

Merger related expenses	236,484	216,312	20,172	9.3
Branch consolidation expense	437,424	-	437,424	N/A
Deposit insurance premiums	77,200	49,864	27,336	54.8
Foreclosed real estate expense and losses	8,108	808	7,300	903.5
Other operating	487,952	309,423	178,529	57.7
Total noninterest expense	\$3,709,099	\$2,322,974	\$1,386,125	59.7

The \$1.4 million increase in noninterest expense during the three months ended June 30, 2016, as compared to the same period of 2016, was attributable to \$674,000 in acquisition and branch consolidation related costs pertaining primarily to the Fraternity acquisition that closed in May 2016, as well as the acquisition related costs associated with Fairmount in the prior quarter. The merger expenses include fees paid to attorneys, investment bankers and accountants, data conversion, as well as other related costs, while the branch consolidation expense includes \$437,424 in expense associated with the closing of our Cockeyville branch office due to branch overlap from the Fraternity acquisition. A breakdown of the acquisition related expenses is shown in the following table.

Table Of Contents

	Three months Ended June 30, 2016			Three Months Ended June 30, 2015		
	Fairmount	Fraternity	Total	Fairmount	Fraternity	Total
Legal	\$7,200	\$39,219	\$46,419	\$129,033	\$6,455	\$135,488
Professional services	-	135,383	135,383	80,000	7,673	87,673
Advertising	-	-	-	2,779	-	2,779
Other	-	54,682	54,682	4,701	144	4,845
Total merger related expenses	\$7,200	\$229,284	\$236,484	\$216,513	\$14,272	\$230,785

In addition to acquisition related expenses, several other categories, including occupancy, furniture and equipment, deposit insurance, and data processing all increased as a result of the Bank operating as a larger institution. Certain costs are naturally inherited after acquiring another financial institution, including additional personnel, branch costs, additional equipment, increased FDIC insurance, and an increase in the core data base resulting from the addition of acquired customers.

The largest increase in noninterest expenses quarter-over-quarter was in salaries and benefits. The Company went from 53 full-time equivalent employees at June 30, 2015 to 75 full-time equivalent employees at June 30, 2016. The additional personnel are related to the retention of certain employees from the Fraternity and Fairmount acquisitions and internal growth within our loan area. Also included in salaries and benefits is payment to the executives of Fraternity under a non-compete agreement. The expense associated with this agreement is \$860,000 and will be recognized over the contractual period of the agreements, including \$48,000 that was recognized in the quarter ending June 30, 2016. Lastly, for the three months ending June 30, 2016 and 2015, \$79,000 in expense was recognized relating to equity awards granted to officers under the Company's Equity Incentive Plan. The equity awards provide for management to have a vested interest in the performance of the company and share in the benefit of an increase in shareholder value. Similarly, other operating expenses for the same periods include \$30,000 in expense associated with equity awards granted to Directors.

Legal expense for the quarter ending June 30, 2016 increased over the same quarter a year ago due to the problem assets acquired in the Fairmount acquisition, particularly the non-owner occupied residential investor loans. Management is diligently working through these problem assets and has engaged legal counsel to assist with the collection and foreclosure process, as well as consult on how to proceed with certain borrowers.

The increase in other operating expense consists of several items, including adjustments to the deferral of Director fees associated with loan origination costs, new costs associated with non-owner residential investor loans acquired from Fairmount and the management of those properties, additional amortization expense associated with the core deposit intangible created in the Fraternity and Fairmount acquisitions, increased regulatory filing expenses, and other miscellaneous items such telephone and dues and subscriptions.

Management actively explores ways to cut costs and improve efficiency. We monitor our costs associated with daily operations and review existing vendor contracts for additional savings and/or seek alternative vendors. These actions, along with efficiencies achieved through the acquisitions of Fraternity and Fairmount, continue to improve our efficiency ratio.

Income Tax Expense. We recorded a tax benefit of \$218,000 for the three months ended June 30, 2016 after pre-tax net loss of \$553,000, compared to tax expense of \$186,000 for the three months ended June 30, 2015 after pre-tax net income of \$305,000. The effective income tax rate was a negative 39.4% for the three months ending June 30, 2016 due to the net loss before income taxes and the impact from tax-exempt revenue compared to an effective tax rate of 61.2% for the three months ended June 30, 2015. The effective tax rate for the quarter ending June 30, 2015 was higher as a result of \$231,000 in acquisition related expenses. The respective acquisition related costs associated with each quarter are not tax deductible.

Table Of Contents

Liquidity and Capital Resources

Liquidity describes our ability to meet current and future financial obligations that arise in the ordinary course of business. Liquidity is primarily needed to meet the borrowing and deposit withdrawal requirements of our customers and to fund current and planned expenditures. Our primary sources of funds are deposits, scheduled amortization and prepayments of loan principal and mortgage-backed securities, maturities and calls of investment securities and funds provided by our operations. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates, economic conditions, and competition. We regularly adjust our investments in liquid assets available to meet short-term liquidity needs based upon our assessment of (i) expected loan demand, (ii) expected deposit flows, (iii) yields available on interest-earning deposits and securities, and (iv) the objectives of our asset/liability management policy.

We also have the ability to borrow from the Federal Home Loan Bank Atlanta (FHLB) to meet our liquidity needs. At June 30, 2016, we had \$28.5 million in borrowings from the FHLB, of which \$26.5 million were assumed through acquisitions, and the capacity to borrow approximately \$49.9 million more, subject to our pledging sufficient assets. Historically we have not used borrowings to fund operations.

Hamilton Bank may also borrow up to \$5.0 million from a correspondent bank under a secured federal funds line of credit, and \$1.0 million under an unsecured line of credit. We would be required to pledge investment securities to draw upon the secured line of credit.

We normally carry balances with correspondent banks that exceed the federally insured limit. We currently conduct a quarterly review of each correspondent bank's financial information, including the banks' capital ratios, balance sheet, income statement, allowance for loans losses, and other performance ratios, to determine if the bank is financially stable.

Our most liquid assets are cash and cash equivalents and investment securities. The level of these assets depends on our operating, financing, lending, and investing activities during any given period. At June 30, 2016, cash and cash equivalents totaled \$64.8 million and securities classified as available-for-sale amounted to \$80.5 million.

Total deposits, excluding those acquired in the Fraternity acquisition, increased \$546,000 over the three months ended June 30, 2016, while total deposits increased \$733,000 over the same period a year ago. Deposit flows are affected by the level of interest rates, the interest rates and products offered by competitors and other factors. In the second half of fiscal 2016, we made a conscious effort to grow and retain maturing certificates of deposits through various promotions to assist in funding organic loan growth. Certificates of deposit allowed us to lock in those funds for an

extended period of time based upon current interest rates. This strategy began to change over the first quarter of fiscal 2017 due to the excess liquidity that has built up in the form of cash from the acquisition of Fraternity. We discontinued our promotional efforts with certificates of deposit in hope of maintaining these deposits as they mature and continued to focus more on generating lower costing core deposits (considered to be all deposits other than certificates of deposit). At June 30, 2016, certificates of deposit scheduled to mature within one year totaled \$143.7 million, or 51.1% of certificates of deposit. We believe the large percentage of certificates of deposit that mature within one year reflects customers' hesitancy to invest their funds for longer periods due to the current low interest rate environment and local competitive pressures. Whether we retain these deposits will be determined in part by the interest rates we are willing to pay on such deposits. If these maturing deposits do not remain with us, we will be required to seek other sources of funds, including other certificates of deposit and borrowings. Depending on market conditions, we may be required to pay higher rates on such deposits or other borrowings than we currently pay on certificates of deposit due on or before June 30, 2017.

In the normal course of operations, we engage in a variety of financial transactions that, in accordance with generally accepted accounting principles, are not recorded in our financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments, unused lines of credit and letters of credit. At June 30, 2016, we had \$52.2 million in commitments to extend credit outstanding.

Table Of Contents

We are committed to maintaining a strong liquidity position. We monitor our liquidity position on a daily basis. We anticipate that we will have sufficient funds to meet our current funding commitments. Based on our deposit retention experience and current pricing strategy, we anticipate that a significant portion of maturing time deposits will be retained.

At June 30, 2016, we exceeded all of the applicable regulatory capital requirements for the Bank, including the new requirement under Basel III to obtain a minimum common equity core (Tier 1) capital to risk-weighted assets ratio of 5.125%. To be classified as a well-capitalized bank, we must have a common equity core (Tier 1) capital to risk-weighted assets ratio of at least 6.5%. For the year ended June 30, 2016, our common equity to Tier 1 capital was \$37.6 million, or 11.84%, of total risk-weighted assets compared to \$44.5 million, or 19.06% of total risk-weighted assets for the year ended March 31, 2016.

Our core (Tier 1) capital was \$37.6 million and \$44.5 million, or 8.49% and 11.78% of adjusted total assets, at June 30, 2016 and March 31, 2016, respectively. In order to be classified as “well-capitalized” under federal banking regulations, we were required to have core capital of at least \$22.1 million, or 5.0% of adjusted assets, as of June 30, 2016. To be classified as a well-capitalized bank, we must also have a ratio of total risk-based capital to risk-weighted assets of at least 10.0%, and a Tier 1 risk-based capital to risk-weighted assets of at least 8%. At June 30, 2016 and March 31, 2016, we had total risk-based capital ratios of 12.45% and 19.81%, respectively, and Tier 1 risk-based capital ratios of 11.84% and 19.06%, respectively. Our regulatory risk weighted capital ratios decreased during the first quarter of fiscal 2017 as a result of our risk-weighted assets increasing due to the Fraternity acquisition and to a lesser extent, increases in commercial loans due to organic growth.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

For a discussion of our market risk, please refer to the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended March 31, 2016 filed on June 29, 2016. The Company’s market risk has not changed materially from that disclosed in the annual report.

Item 4. Controls and Procedures

As of the end of the period covered by this report, management of the Company carried out an evaluation, under the supervision and with the participation of the Company’s principal executive officer and principal financial officer, of the effectiveness of the Company’s disclosure controls and procedures as that term is defined in Rule 13a-15(e). Based on this evaluation, the Company’s principal executive officer and principal financial officer concluded that the Company’s disclosure controls and procedures are effective in ensuring that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission’s

rules and forms and is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

It should be noted that the design of the Company's disclosure controls and procedures is based in part upon certain reasonable assumptions about the likelihood of future events, and there can be no reasonable assurance that any design of disclosure controls and procedures will succeed in achieving its stated goals under all potential future conditions, regardless of how remote, but the Company's principal executive and financial officers have concluded that the Company's disclosure controls and procedures are, in fact, effective at a reasonable assurance level.

During the period covered by this report, there have been no changes in the Company's internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Securities and Exchange Commission Rule 13a-15 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Table Of Contents

Part II – Other Information

Item 1. Legal Proceedings

The Bank and Company are subject to various legal actions arising in the normal course of business. In the opinion of management, the resolution of these legal actions is not expected to have a material adverse effect on the Bank's or the Company's financial condition or results of operations.

Item 1A. Risk Factors

For information regarding the Company's risk factors, see "Risk Factors" in the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission on June 29, 2016. As of June 30, 2016, except for the additional risk factors set forth below, the risk factors of the Company have not changed materially from those disclosed in the annual report.

Our acquisitions of Fairmount Bancorp, Inc. and Fraternity Community Bancorp, Inc. may not produce the anticipated benefits.

Acquisitions involve a number of risks and challenges including: our ability to integrate the branches and operations we acquire, and the associated internal controls and regulatory functions, into our current operations; our ability to limit the outflow of deposits held by our new customers in the acquired branches and our ability to monitor, manage and properly reserve for the loans we acquire; our ability to attract new deposits and to generate new interest-earning assets in local markets we have not previously served. Additionally, no assurance can be given that the operation of acquired branches and performance of the acquired loan portfolio would not adversely affect our existing profitability; that we would be able to achieve results in the future similar to those achieved by our existing banking business; that we would be able to compete effectively in the market areas served by acquired branches; or that we would be able to manage any growth resulting from the transaction effectively. We face the additional risk that the anticipated benefits of the acquisition may not be realized fully or at all, or within the time period expected.

A new accounting standard will likely require us to increase our allowance for loan losses and may have a material adverse effect on our financial condition and results of operations.

The Financial Accounting Standards Board has adopted a new accounting standard that will be effective for Hamilton Bancorp, Inc. and Hamilton Bank for our first fiscal year after December 15, 2019. This standard, referred to as Current Expected Credit Loss, or CECL, will require financial institutions to determine periodic estimates of lifetime expected credit losses on loans, and recognize the expected credit losses as allowances for loan losses. This will change the current method of providing allowances for loan losses that are probable, which would likely require us to increase our allowance for loan losses, and to greatly increase the types of data we would need to collect and review to determine the appropriate level of the allowance for loan losses. Any increase in our allowance for loan losses or expenses incurred to determine the appropriate level of the allowance for loan losses may have a material adverse effect on our financial condition and results of operations.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Table Of Contents

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*

Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Consolidated Statements of Financial Condition as of June 30, 2016 (unaudited) and March 31, 2016; (ii) the Consolidated Statements of Operations for the three months ended June 30, 2016 and 2015 (unaudited); (iii) the Consolidated Statements of Comprehensive Income for the three months ended June 30, 2016 and 2015 (unaudited); (iv) the Consolidated Statements of Equity for the three months ended June 30, 2016 and 2015 (unaudited); (v) the Consolidated Statement of Cash Flows for the three months ended June 30, 2016 and 2015 (unaudited); and (vi) Notes to Consolidated Financial Statements (unaudited).

* This information is furnished and not filed for purposes of Section 18 of the Securities Exchange Act of 1934, and shall not be deemed incorporated into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934 unless specifically incorporated therein.

SIGNATURES

Edgar Filing: Hamilton Bancorp, Inc. - Form 10-Q

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.

HAMILTON BANCORP, INC.

Date: August 15, 2016 /s/ Robert A. DeAlmeida
Robert A. DeAlmeida
President and Chief Executive Officer

Date: August 15, 2016 /s/ John P. Marzullo
John P. Marzullo
Senior Vice President, Chief Financial Officer and
Treasurer