FORM 10KSB40

Annual and transition reports of small business issuers [Section 13 or 15(d), S-B Item 405]

Filing Date: **1996-12-30** | Period of Report: **1996-09-30**
SEC Accession No. 0000946275-96-000444

(HTML Version on secdatabase.com)

FILER

BEDFORD BANCSHARES INC

CIK:**921435**| IRS No.: **541709924** | State of Incorp.:**VA** | Fiscal Year End: **0930**
Type: **10KSB40** | Act: **34** | File No.: **000-24330** | Film No.: **96687544**
SIC: **6035** Savings institution, federally chartered

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB

(Mark One):

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934 [NO FEE REQUIRED] For the fiscal year ended September 30, 1996, OR

|_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [NO FEE REQUIRED] For the transition period from to ____________________ to _________________

Commission File Number: 0-24330

BEDFORD BANCSHARES, INC.
(Exact name of registrant as specified in its charter)

Virginia	54-1709924
(State or other jurisdiction of incorporation or organization)	I.R.S. Employer Identification No.
125 West Main Street, Bedford, Virginia	24523
(Address of principal executive offices	(Zip Code)
Registrant's telephone number, including area code:	(540) 586-2590
Securities registered pursuant to Section 12(b) of the Act:	None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, par value $0.10 per share
(Title of Class)

Check whether the issuer: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES X NO .

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-B is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. [X]

State issuer's revenues for its most recent fiscal year. $9,999,000.

As of December 6, 1996, there were issued and outstanding 1,143,669 shares of the registrant's Common Stock.

The registrant's voting stock is traded over-the-counter under the symbol "BFSB." The aggregate market value of the voting stock held by non-affiliates of the registrant, based on the closing price of the registrant's common stock as reported by the Nasdaq National Market on December 6, 1996, was $16,207,987.

Transition Small Business Disclosure Format (check one)
YES NO X

DOCUMENTS INCORPORATED BY REFERENCE

1. Portions of Annual Report to Stockholders for the Fiscal Year ended September 30, 1996. (Parts I, II and IV)

2. Portions of Proxy Statement for the 1997 Annual Meeting of stockholders. (Part III)

PART I

Item 1. Business

The Company

Bedford Bancshares, Inc. (the "Company") is a Virginia corporation organized in March of 1994 at the direction of Bedford Federal Savings Bank ("Bedford Federal" or the "Savings Bank") to acquire all of the capital stock that the Savings Bank issued in its conversion from the mutual to stock form of ownership (the "Conversion"). On August 19, 1994, the Savings Bank completed the Conversion and became a wholly owned subsidiary of the Company. The Company is a unitary savings and loan company which, under existing laws, generally is not restricted in the types of business activities in which it may engage provided that the Savings Bank retains a specified amount of its assets in housing related investments.

The Savings Bank

Bedford Federal, a wholly owned subsidiary of the Company, was founded in 1935 and is primarily engaged in attracting deposits from the general public and using those funds to originate real estate loans on one- to four- family residences and, to a lesser extent, multi-family, commercial real estate and consumer loans. The Savings Bank has offices in the city of Bedford and in Forest and Moneta, which are located in Bedford County, Virginia. In addition, the Savings Bank invests in investment securities and mortgage-backed securities. The Savings Bank offers its customers fixed-rate, and adjustable-rate mortgage loans, as well as consumer loans, including home equity and savings account loans. Adjustable-rate mortgage loans are originated for retention in the Savings Bank's portfolio while fixed-rate mortgage loans are generally sold upon origination into the secondary market. All consumer loans are retained in the Savings Bank's portfolio.

The principal sources of funds for the Savings Bank's lending activities are deposits, the amortization, repayment and maturity of loans and investment securities and advances from the Federal Home Loan Bank ("FHLB") of Atlanta. Primary sources of income are interest and fees on loans and investment securities and customer service fees and commissions. The Savings Bank's primary expense is interest paid on deposits.

Market Area/Competition

The City and County of Bedford are the Savings Bank's primary market area. The Bedford City/County area consists of over 770 square miles and is located in the west-central portion of Virginia known as the Piedmont Plateau. The Savings Bank's main office is located at 125 West Main Street in the City of Bedford, Virginia, and two other offices are located at opposite ends of Bedford County. An office in Forest serves the eastern part of the county, as well as parts of the City of Lynchburg, Campbell and Amherst Counties. The office located in Moneta serves the southern and western parts of Bedford County, as well as the area surrounding Smith Mountain Lake which includes portions of Franklin and Roanoke Counties.

The City of Bedford is located approximately 25 miles west of the City of Lynchburg and 30 miles east of Roanoke. The City of Bedford serves as the county seat and the commercial and retail hub of the area with a market of over 55,000 persons. The Bedford area enjoys a diversified economy comprised of manufacturing, wholesale, retail, service, agriculture and tourism.

The Savings Bank is the only financial institution headquartered in Bedford City/County. This area is also served by branch offices of five regional commercial banks and a branch office of a thrift headquartered in Lynchburg. The Savings Bank encounters strong competition both in the attraction of deposits and origination of real estate and other loans. Competition for deposits comes primarily from commercial banks and competition for loans comes primarily from branches of commercial banks and thrifts, as well as mortgage companies that operate in the areas which comprise the Savings Bank's primary market area. Due to their size, many of the Savings Bank's competitors possess greater financial and marketing resources.

Lending Activities

General. The Savings Bank's loan portfolio predominantly consists of adjustable-rate mortgage loans or short-term fixed-rate loans secured by one-to four family residences and to a lesser extent, commercial real estate, construction and consumer loans. Fixed rate mortgage loans with maturities exceeding 15 years generally are sold with servicing rights retained by the Savings Bank in the secondary market.

The following table sets forth the composition of the Savings Bank's loan portfolio in dollar amounts and in percent of the respective portfolios at the dates indicated.

<TABLE>
<CAPTION>

	1996 Amount	1996 Percent of Total	1995 Amount	1995 Percent of Total
	(Dollars in Thousands)			
Real estate:				
Residential:				
<S>	<C>	<C>	<C>	<C>
One- to four-family...........	$ 84,235	74.53%	$ 75,341	74.08%
Multi-family..................	1,000	.88	223	.22
Commercial......................	4,998	4.42	4,379	4.31
Construction....................	9,783	8.66	9,732	9.56
Land............................	4,127	3.65	3,588	3.53
Consumer and commercial business...	8,878	7.86	8,436	8.30
Total loans.................	113,021	100.00%	101,699	100.00%
Less:				
Unearned discounts, premium, deferred loan fees, net........	299		396	
Loans-in-process................	3,199		2,994	
Allowance for credit losses......	650		640	
Total loans, net..............	$108,873		$ 97,669	

</TABLE>

The following table sets forth the maturity of the Savings Bank's loan portfolio at September 30, 1996. The table does not include prepayments or scheduled principal repayments. Prepayments and scheduled principal repayments on loans totalled $23.6 million for the year ended September 30, 1996. Adjustable-rate mortgage loans are shown as maturing based on contractual maturities.

<TABLE>
<CAPTION>

	At September 30, 1996						
	One- to Four-Family	Multi-Family	Commercial Real Estate	Construction	Land	Consumer and Commercial Business	Total Loans Receivable
	(In thousands)						
Amounts due:							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
One year or less	$ 38	$ 1	$ 1,956	$ 7,736	$ 21	$ 2,229	$ 11,981
After one year:							
More than one year to three years..	260	--	54	866	170	2,212	3,562
More than three years to five years	669	--	288	717	1,853	2,996	6,523
More than five years to 10 years...	6,337	300	828	47	1,181	1,348	10,041
More than 10 years to 20 years.....	26,871	699	1,872	352	902	87	30,783
More than 20 years	50,060	--	--	65	--	6	50,131
Total due after one year	84,197	999	3,042	2,047	4,106	6,649	101,040
Total amounts due	84,235	1,000	4,998	9,783	4,127	8,878	113,021
Less:							
Loans-in-process	--	--	--	3,199	--	--	3,199
Unearned discounts, premiums and deferred loan fees, net	239	3	14	28	12	3	299
Allowance for credit losses	445	1	50	40	25	89	650

Loans, net	$ 83,551	$ 996	$ 4,934	$ 6,516	$4,090	$ 8,786	$108,873
	======	======	=======	=======	=====	=======	=======

</TABLE>

The following table sets forth the dollar amount of all loans due after September 30, 1997, which have fixed interest rates and which have floating or adjustable interest rates.

	Fixed Rates	Floating or Adjustable Rates	Total
		(In thousands)	
Real estate loans:			
One- to four-family....	$10,645	$75,599	$ 86,244
Multi-family...........	171	828	999
Commercial real estate	955	2,087	3,042
Land...................	2,856	1,250	4,106
Consumer and commercial business................	3,174	3,475	6,649
Total...................	$17,801	$83,239	$101,040

One- to Four-Family Residential Loans. The Savings Bank's primary lending activity consists of the origination of one-to four-family, owner-occupied, residential mortgage loans secured by property located in the Savings Bank's primary market area. Management believes that its policy of focusing on

one- to four-family lending has been effective in contributing to net interest income while reducing credit risk by keeping loan delinquencies and losses to a minimum.

The Savings Bank currently offers adjustable-rate mortgage loans ("ARMS") that adjust every one or three years, some have a fixed rate for seven years before adjusting annually and have terms from 10 to 30 years. Generally, the interest rates on ARMs are based on treasury bill indices and are adjustable once a year with certain limitations on adjustments per period and over the life of the loan. All ARMs have a "floor rate", whereby interest charged on such loans cannot be reduced below the rate set forth in the loan documents, thereby insulating the Savings Bank from lower yields due to further reductions in interest rates. The Savings Bank considers the market factors and competitive rates on loans as well as its own cost of funds when determining the rates on the loans that it offers. The Savings Bank does not originate loans with negative amortization.

Bedford Federal originated $19.0 million and $16.8 million of adjustable-rate, one- to four-family permanent and construction mortgage loans during the fiscal years ended September 30, 1996 and 1995, respectively. The Savings Bank's total one- to four-family ARM portfolio amounted to $75.6 million of the Savings Bank's gross loans receivable at September 30, 1996.

The retention of ARMs in the Savings Bank's portfolio greatly helps to reduce the Savings Bank's exposure to changes in interest rates. However, there are unquantifiable credit risks which would result from potential increased payments to the borrower as a result of repricing of ARMs. It is possible that during periods of rapidly rising interest rates, the risk of default on ARMs may increase due to the upward adjustment of interest cost to the borrower. Additionally, the ARMs originated by the Savings Bank historically have provided for initial rates of interest below the fully indexed rates that would prevail were the index used for repricing applied initially. These loans are subject to increased risk of delinquency or default when the higher, fully-indexed rate of interest subsequently comes into effect and replaces the lower initial rate. The Savings Bank attempts to limit such potential risk by placing limitations on the interest rate adjustments. Although the potential exists for a higher rate of delinquency on ARMs versus fixed-rate loans, Bedford Federal has not experienced a disproportionate share of delinquencies or defaults in its ARM portfolio.

Generally, during periods of rising interest rates, the risk of default on ARMs is considered to be greater than the risk of default on a fixed-rate loan due to the upward adjustment of interest costs to the borrower. To help reduce such risk, the Savings Bank qualifies the loan at the fully indexed accrual rate, as opposed to the original interest rate. ARMs may be made at up to 95% of the loan to value ratio. Although ARMs allow the Savings Bank to increase the sensitivity of its asset base to changes in interest rates, the extent of this interest sensitivity is limited by the periodic and lifetime interest rate adjustment limitations. Accordingly, there can be no assurance that yields on the Savings Bank's ARMs will adjust sufficiently to compensate for increases in the Savings Bank's cost of funds.

The Savings Bank also offers conventional fixed-rate one- to four-family mortgage loans with terms from 10 to 30 years. Fixed-rate loans are generally underwritten either according to the Federal Home Loan Mortgage Corporation ("FHLMC")or Federal National Mortgage Association ("FNMA") guidelines, utilizing their approved documents so that the loans qualify for sale in the secondary mortgage market. The Savings Bank originates and holds its fixed-rate mortgage loans with maturities not exceeding 15 years in its portfolio. Bedford Federal originated $2.2 million and $3.0 million in permanent fixed-rate, one- to four-family mortgage loans during the years ended September 30, 1996 and 1995, respectively. The Savings Bank sold $152,000 and $184,000 of the loans originated during the fiscal years ended September 30, 1996 and 1995, respectively. In addition, the Savings Bank originated $167,000 and $262,000 in fixed-rate one-to four-family mortgage loans for the Virginia Housing Development Authority ("VHDA") in fiscal 1996 and 1995, respectively.

While one- to four-family residential real estate loans are normally originated with terms from 10 to 30 years, such loans typically remain outstanding for substantially shorter periods. This is because borrowers often prepay their loans in full upon sale of the property pledged as security or upon refinancing the original loan. In addition, substantially all of the mortgage loans in the Savings Bank's loan portfolio contain due-on-sale clauses providing that the Savings Bank may declare the unpaid amount due and payable upon the sale of the property securing the loan. The Savings Bank enforces these due-on-sale clauses to the extent permitted by law. Thus, average loan maturity is a function of, among other factors, the level of purchase and sale activity in the real estate market, prevailing interest rates and the interest rates payable on outstanding loans.

Construction Lending. The Savings Bank engages in construction lending involving loans to qualified borrowers for construction of one- to four-family residential properties and, on a limited basis, involving commercial and multi-family properties. These properties are located in the Savings Bank's market area.

Construction loans are made to builders on a speculative basis and to owners for construction of their primary residence on a construction/permanent basis. Loans for speculative housing construction are made to area builders only after a thorough background check has been made. This background check includes an analysis of the builder's financial statements, credit report and reference checks with subcontractors and suppliers. The Savings Bank usually will have no more than three construction loans outstanding at any time to any builder. Construction loans on speculative properties are limited to a maximum loan-to-value ratio of 80% and have a maximum maturity of 12 months. Loan proceeds are disbursed in increments as construction progresses. Accrued interest on loan disbursements is paid monthly. At September 30, 1996, the Savings Bank had $1.2 million in construction loans outstanding secured by unsold properties, with $271,000 in loans-in-process (funds being held for construction progress) outstanding and attributed to these loans. The Savings Bank has experienced increased residential construction lending in its market area, primarily in the Forest, Virginia area. This increased lending is a result of the recruitment by the Savings Bank of several financially strong small builders as customers in the Forest area.

Construction/permanent loans to owner/borrowers have either fixed or adjustable rates and are underwritten in accordance with the same terms and requirements as the Savings Bank's permanent mortgages on existing properties except that the builder must qualify as a Savings Bank approved contractor, and the loans generally provide for disbursement of loan proceeds in stages during a construction period of up to six months. Borrowers are required to pay accrued interest on the outstanding balance monthly during the construction phase. At September 30, 1996, there was $9.8 million outstanding in construction loans to owner/borrowers with $3.2 million outstanding loans-in-process allocated to these projects. Construction loans originated on commercial and multi-family properties amounted to $0 and $385,000 during fiscal 1996 and 1995, respectively. The Savings Bank originated $9.9 million and $10.8 million in construction loans on one- to four-family properties during fiscal years 1996 and 1995, respectively.

Construction financing is generally considered to involve a higher degree of risk of loss than long-term financing on improved occupied real estate. Risk of loss on a construction loan is dependent largely upon the accuracy of the initial estimate of the property's value at completion of construction or development and the estimated cost (including interest) of construction. During the construction phase, a number of factors could result in delays and cost overruns. If the estimate of construction costs proves to be inaccurate, it may be necessary for the Savings Bank to advance funds beyond the amount originally committed to permit completion of the construction. If the estimate of value proves to be inaccurate, the Savings Bank may be confronted, at or prior to the maturity of the loan, with collateral having a value

which is insufficient to assure full repayment. As a result of the foregoing, construction lending often involves the disbursement of substantial funds with repayment dependent, in part, on the success of the construction. If the Savings Bank is forced to foreclose on a property prior to or at completion due to a default, there can be no assurance that the Savings Bank will be able to recover all of the unpaid balance of, and accrued interest on, the loan as well as related foreclosure and holding costs. The Savings Bank has sought to minimize this risk by limiting construction loans to qualified borrowers on properties located in the Savings Bank's market area and by limiting the number of construction loans for speculative purposes outstanding at any time.

Multi-Family and Commercial Real Estate Loans. The Savings Bank offers multi-family and commercial real estate loans, however, this type of lending represents a small portion of the Savings Bank's lending activities. Commercial real estate loans consist of permanent loans secured by small office buildings, churches, shopping centers and other non-residential buildings on real estate located in the west-central Virginia area.

Loans secured by multi-family and commercial real estate generally involve a greater degree of risk than one- to four-family residential mortgage loans and carry larger loan balances. This increased credit risk is a result of several factors, including the concentration of principal in a limited number of loans and borrowers, the effects of general economic conditions on income producing properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by commercial and multi-family real estate is typically dependent upon the successful operation or management of the related real estate project. If the cash flow from the project is reduced, the borrower's ability to repay the loan may be impaired. The Savings Bank seeks to minimize these risks in a variety of ways, including limiting the size of such loans and strictly scrutinizing the financial condition of the borrower, the quality of the collateral and the management of the property securing the loan. In certain instances, the Savings Bank will require personal guarantees. Substantially all of the properties securing the Savings Bank's commercial and multi-family real estate loans are inspected by the Savings Bank's lending personnel before the loan is made. The Savings Bank also obtains appraisals on each property. At September 30, 1996, the largest commercial or multi-family real estate loan had a balance of $1.6 million and was performing.

Land Lending. Land loans are made primarily to individuals on developed residential lots located in the Savings Bank's market area. Land lending generally involves additional risks to the lender as compared with residential mortgage lending. These risks are attributable to the fact that loan funds are advanced upon the security of unimproved and developed lots or land under development, predicated on the future value of the property upon completion of development. Loans on undeveloped land may run the risk of adverse zoning changes, environmental or other restrictions on future use. Because of these factors, the analysis of land loans requires an expertise that is different in significant respects from that which is required for residential mortgage lending.

Consumer and Commercial Business Loans. The Savings Bank views consumer lending as an important component of its lending operations because consumer loans generally have shorter terms and higher yields, thus reducing exposure to changes in interest rates. In addition, the Savings Bank believes that offering consumer loans helps to expand and create stronger ties to its customer base. Consequently, the Savings Bank has recently focused on consumer lending by marketing consumer loans to existing and potential customers. All branches are now able to originate consumer loans. Regulations permit federally chartered savings associations to make secured and unsecured consumer loans up to 35% of the Savings Bank's assets, with no limit for credit cards and educational loans. In addition, the Savings Bank has lending authority above the 35% limit for certain consumer loans, such as home improvement loans and loans secured by savings accounts.

Consumer loans consist of automobile loans, savings account loans, home equity, personal secured and unsecured loans and home improvement loans. As of September 30, 1996, $1.5 million of such loans consisted of automobile loans.

The underwriting standards employed by the Savings Bank for consumer loans include a determination of the applicant's payment history on other debts and an assessment of ability to meet existing obligations and payments on the proposed loan. In addition, the stability of the applicant's monthly income from primary employment is considered during the underwriting process. Creditworthiness of the applicant is of primary consideration, however, the underwriting process also includes a comparison of the value of the security, if any, in relation to the proposed loan amount.

Consumer loans entail greater credit risk than do residential mortgage loans, particularly in the case of consumer loans which are unsecured or secured by assets that depreciate rapidly, such as automobiles, mobile homes, boats and recreational vehicles. In such cases, repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and the remaining deficiency often does not warrant further substantial collection efforts against the borrower. In particular, amounts realizable on the sale of repossessed automobiles may be significantly reduced based upon the condition of the automobiles and the lack of demand for used automobiles. The Savings Bank adds a general provision to its consumer loan loss allowance, based on general economic conditions, prior loss experience and management's periodic evaluation. See "--Loan Delinquencies and Non-Performing Assets and Classified Assets" for information regarding the Savings Bank's loan loss experience and reserve policy.

Regulations authorize the Savings Bank to make secured and unsecured loans for commercial, corporate, business and agricultural purposes. The aggregate amount of such loans outstanding may not exceed 20% of the Savings Bank's assets. Any loans in excess of 10% of assets must be made to qualifying small businesses and farms. In addition, another 10% of total assets may be invested in commercial equipment leasing. The Savings Bank has offered limited commercial business loans since the early 1980s, primarily to existing customers. Generally, the Savings Bank's commercial business loans are secured by real estate or other assets.

It is the policy of Bedford Federal annually to request financial statements from commercial loan borrowers. The financial statements are reviewed as received by management to detect any conditions or trends which may affect the ability of the borrower and/or cash flows of the project to repay the debt.

Loan Solicitation and Processing. The Savings Bank's sources of mortgage loan applications are referrals from existing or past customers, real estate brokers, builders, call-in and walk-in customers and also the result of advertising.

All loans are underwritten and approved by the loan committee. Any loan up to $300,000 is reviewed and approved by two members of the loan committee. Any loan over $300,000 is reviewed and approved by three members of the loan committee. All loan approvals are ratified by the Board of Directors on a monthly basis.

The Savings Bank uses independent fee appraisers on all real estate related transactions. Each fee appraiser used must be state licensed or state certified and approved by Bedford Federal's Board of Directors. It is the Savings Bank's policy to obtain title insurance or an attorney's opinion and certification of title and fire and casualty insurance for all mortgage loans. If appropriate, flood insurance is also required.

Loan Originations, Purchases, Sales and Repayments. The following table sets forth the Savings Bank's loan originations, sales, and principal repayments for the periods indicated. The Savings Bank did not purchase any loans during these periods.

	For the Year Ended September 30,	
	1996	1995
	(In thousands)	
Gross loans:		
Beginning balance....................	$97,669	$ 89,309
Loans originated:		
One- to four-family...............	15,473	8,159
Multi-family......................	--	130
Commercial real estate............	126	315
Construction......................	11,559	11,233
Land..............................	2,393	1,566
Consumer and commercial business.......................	8,616	7,003
Total loans originated.........	38,167	28,406
Less:		
Transfer to foreclosed real estate.	--	--

Principal repayments	23,612	16,868
Sales of loans	152	184
Loans-in-process	3,199	2,994
Net loan activity	11,204	8,360
Ending balance	$108,873	$ 97,669

Loan Sales. The Savings Bank generally underwrites fixed-rate one- to four-family mortgage loans pursuant to FHLMC and FNMA guidelines to facilitate sale in the secondary market. However, all fixed-rate mortgage loans with terms not exceeding 15 years are retained in the Savings Bank's portfolio. Loans with maturities exceeding 15 years generally are sold with servicing rights retained by the Savings Bank unless the loan was originated for community reinvestment purposes. Prior to 1992, the Savings Bank retained all fixed-rate mortgage loans originated as management sought to increase its mortgage loan holdings to a desired level. See also "--One- to Four-Family Residential Loans."

Loan Commitments. The Savings Bank issues written, formal commitments as to interest rate to prospective borrowers on all real estate loans at the date of application. The interest rate commitment is good for 60 days from the date of the application. Upon receipt of loan approval, the borrower has the balance of the 60 day period to close the loan at the interest rate committed. At September 30, 1996, the Savings Bank had $1.8 million of commitments to originate mortgage loans, $2.0 million in unfunded home equity loans and $.4 million in unfunded commercial lines of credit.

Loan Processing and Servicing Fees. In addition to interest earned on loans, the Savings Bank recognizes fees and service charges which consist primarily of fees charged for loan originations and loans serviced for others and late charges. The Savings Bank recognized loan servicing fees of $403,000 and $345,000 for the years ended September 30, 1996 and 1995, respectively. As of September 30, 1996, loans serviced for others totalled $2.7 million. To the extent possible, the Savings Bank intends to expand the amount of loans serviced for others through the continued sale of fixed-rate, long-term loans to others and through the VHDA.

Loans to One Borrower. Current regulations limit loans-to-one borrower to an amount equal to 15% of unimpaired capital and retained income on an unsecured basis and an additional amount equal to 10% of unimpaired capital and retained income if the loan is secured by readily marketable collateral (generally, financial instruments, not real estate) or $500,000, whichever is greater. Under such regulations, the Savings Bank's maximum loan-to-one borrower limit was approximately $2.4 million as of September 30, 1996. See " -- Classified Assets."

The Savings Bank's largest loan to one borrower is a loan originated jointly in May 1988 by three financial institutions in the amount of $3.5 million of which Bedford Federal loaned approximately $1.2 million. During fiscal 1996 the three financial institutions loaned an additional $1.2 million of which Bedford Federal loaned $400,000, for remodeling to accommodate the relocation of a national chain grocer within the shopping center. The balance of the amount due Bedford Federal was $1.6 million at September 30, 1996. This loan is secured by a shopping center located in the City of Bedford and was performing at September 30, 1996.

Loan Delinquencies and Non-performing Assets. The Savings Bank's collection procedures provide that when a mortgage loan is 15 days past due, a computer printed delinquency notice is sent. If payment is still delinquent at the end of that month, within five days a telephone call is made to the borrower. If the delinquency continues, subsequent efforts are made to eliminate the delinquency. If the loan continues in a delinquent status for 90 days or more, the Board of Directors of the Savings Bank generally approves the initiation of foreclosure proceedings unless other repayment arrangements are made and a specific reserve for 100% of uncollected interest is established, thus effecting non-accrual status. Collection procedures for non-mortgage loans generally begin after a loan is 10 days delinquent.

Real estate acquired by the Savings Bank as a result of foreclosure or by deed in lieu of foreclosure is classified as foreclosed real estate until such time as it is sold. When foreclosed real estate is acquired, it is recorded at the lower of fair value or cost. Valuations are periodically performed by management and subsequent charges to specific loss allowances are taken when it is determined that the carrying value of the property exceeds the fair value less estimated costs to sell. See "-- Foreclosed Real Estate."

At September 30, 1996 and 1995, delinquencies in the Savings Bank's loan portfolio were as follows:

<TABLE>
<CAPTION>

	At September 30,							
	1996				1995			
	60-89 Days		90 Days or More		60-89 Days		90 Days or More	
	Number of Loans	Principal Balance of Loans	Number of Loans	Principal Balance of Loans	Number of Loans	Principal Balance of Loans	Number of Loans	Principal Balance of Loans
One- to four- <S> family.......	<C> 9	<C> $651	<C> 4	<C> $ 510	<C> 5	<C> $465	<C> 4	<C> $ 266
Multi-family....	--	--	--	--	--	--	--	--
Commercial real estate..	--	--	1	54	--	--	1	1,042
Land...........	--	--	--	--	1	17	--	--
Consumer and commercial business.......	8	83	6	120	4	21	2	4
Total........	17	$734	11	$684	10	$503	7	$1,312
Delinquent loans to total loans		.67%		.63%		.52%		1.34%

</TABLE>

Uncollectible interest on loans that are contractually past due is charged off, or an allowance is established based on management's periodic evaluation of its portfolio. The allowance is established by a charge to interest income equal to all interest previously accrued, and income is subsequently recognized only to the extent that cash payments are received until, in management's judgment, the borrower has the ability to make periodic interest and principal payments or is no longer delinquent, and the loan is returned to accrual status. The Savings Bank ceases the accrual of interest on delinquent loans upon foreclosure. At September 30, 1996, the Bank had no restructured loans within the meaning of Statement of Financial Accounting Standard ("SFAS") 15. The following table sets forth information regarding loans which are 90 days or more delinquent.

	At September 30,	
	1996	1995
	(In thousands)	
Loans 90 days or more delinquent..........	$684	$1,312
Foreclosed real estate....................	--	-
Total non-performing assets...........	$684	$1,312

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(1) A 100% reserve is established for interest on loans 90 days or more delinquent. At September 30, 1996 and 1995, the balance of the reserve for accrued interest on loans delinquent 90 days or more was $168,000 and $122,000, respectively. At September 30, 1996, the Savings Bank had no loans accounted for on a nonaccrual basis which were less than 90 days past due.

Classified Assets. OTS regulations provide for a classification system for problem assets of insured institutions. Under this classification system, problem assets of insured institutions are classified as "substandard," "doubtful," or "loss." An asset is considered "substandard" if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any.

"Substandard" assets include those characterized by the "distinct possibility" that the insured institution will sustain "some loss" if the deficiencies are not corrected. Assets classified as "doubtful" have all of the weaknesses inherent in those classified "substandard," with the added characteristic that the weaknesses present make "collection or liquidation in full," on the basis of currently existing facts, conditions and values, "highly questionable and improbable." Assets classified as "loss" are those considered "uncollectible" and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. Assets designated "special mention" by management are assets included on the Savings Bank's internal watchlist because of potential weakness but which do not currently warrant classification in one of the aforementioned categories.

When an insured institution classifies problem assets as either substandard or doubtful, it may establish general allowances for credit losses in an amount deemed prudent by management. General allowances represent loss allowances which have been established to recognize the inherent risk associated with lending activities, but which, unlike specific allowances, have not been allocated to particular problem assets. When an insured institution classifies problem assets as "loss," it is required either to establish a specific provision for losses equal to 100% of that portion of the asset so classified or to charge off such amount. An institution's determination as to the classification of its assets and the amount of its valuation allowances is subject to review by the OTS, which may order the establishment of additional general or specific loss allowances. A portion of general loss allowances established to cover possible losses related to assets classified as substandard or doubtful may be included in determining an institution's regulatory capital, while specific valuation allowances for credit losses generally do not qualify as regulatory capital.

At September 30, 1996, the Savings Bank's problem assets were as follows: $83,000 were designated special mention, $670,000 were classified as substandard and none were classified as doubtful or loss.

Foreclosed Real Estate. Real estate acquired by the Savings Bank as a result of foreclosure, judgment or by deed in lieu of foreclosure is classified as foreclosed real estate until it is sold. When property is acquired it is recorded at the lower of fair value less estimated selling costs, or the balance of the loan on the property at the date of foreclosure. The Savings Bank held no foreclosed real estate at September 30, 1996.

Provision for Credit and Foreclosed Real Estate Losses. It is management's policy to provide for losses on unidentified loans in its loan portfolio and foreclosed real estate. A provision for credit losses is charged to operations based on management's evaluation of the potential losses that may be incurred in the Savings Bank's loan portfolio. Such evaluation, which includes a review of all loans of which full collectibility of interest and principal may not be reasonably assured, considers, among other matters, perceived risks, delinquency ratios, economic conditions and the estimated net realizable value of the underlying collateral. During the years ended September 30, 1996 and 1995, the Savings Bank charged $22,000 and $20,000, respectively, to the provision for credit losses. There were no charges to the provision for losses on foreclosed real estate for either fiscal 1996 or 1995.

Management will continue to review the entire loan portfolio to determine the extent, if any, to which further additional loss provisions may be deemed necessary. There can be no assurance that the allowance for losses will be adequate to cover losses which may in fact be realized in the future and that additional provisions for losses will not be required.

Allowance Analysis. The following table sets forth the Savings Bank's allowance for credit losses, allowance for losses on foreclosed real estate and related ratios.

	At or For the Year Ended September 30,	
	1996	1995
	(Dollars in thousands)	
Allowance for credit losses:		
Balance at beginning of period...............	$640	$636
Charge-offs:		
One- to four-family.......................	--	--
Multi-family..............................	--	--

Commercial real estate	--	--
Construction and land	--	--
Consumer and commercial business	12	18
Total charge-offs	12	18
Recoveries	--	2
Provisions charged to income	22	20
Balance at end of period(1)	$ 650	$640
Allowance for losses on foreclosed real estate:		
Balance at beginning of period	$ --	$ --
Provision charged to income	--	--
Charge-offs	--	--
Recoveries	--	--
Balance at end of period	$ --	$ --
Ratios of net charge-offs during the period to average loans outstanding during the period	.01%	.02%
Ratio of allowance for losses to total loans at the end of the period(2)	.60%	.63%
Ratio of allowance for losses to non-performing assets at the end of the period(2)	95.03%	48.78%

----
(1) Includes reserves attributable to loans classified as "loss," which totalled $-0- at September 30, 1996 and 1995.
(2) Allowance for losses includes valuation allowances on loans and foreclosed real estate.

Allowance by Loan Category. The following table sets forth the Savings Bank's allocation of the allowance for credit losses by loan category and the percent of loans in each category to total loans receivable at the dates indicated. The portion of the allowance for credit losses allocated to each loan category does not represent the total available for future losses which may occur within the loan category.

<TABLE>
<CAPTION>

	At September 30,			
	1996		1995	
	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans
	(Dollars in Thousands)			
<S>	<C>	<C>	<C>	<C>
One- to four-family	$445	68.46%	$469	74.08%
Multi-family	1	.15	1	.22
Commercial real estate	50	7.69	44	4.31
Construction	40	6.15	39	9.57
Land	25	3.85	22	3.52
Consumer and commercial business	89	13.70	65	8.30
Total valuation allowances(1)(2)	$650	100.00%	$640	100.00%

</TABLE>

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(1) Includes reserves attributable to loans classified as "loss," which totalled $-0- at September 30, 1996 and 1995.
(2) Includes $-0- of allowance for losses on foreclosed real estate at both September 30, 1996 and 1995.

Investment and Mortgage-backed Securities Activities

Investment Securities. The Savings Bank is required under federal regulations to maintain a minimum amount of liquid assets which may be invested in specified short-term securities and certain other investments. The Savings Bank has generally maintained a liquidity portfolio well in excess of regulatory requirements. Liquidity levels may be increased or decreased depending upon the yields on investment alternatives and upon management's judgment as to the attractiveness of the yields then available in relation to other opportunities and its expectation of future yield levels, as well as management's projections as to the short-term demand for funds to be used in the Savings Bank's loan origination and other activities. At September 30, 1996, the Savings Bank had an investment securities portfolio of approximately $11.5 million, consisting primarily of U.S. government and agency obligations, Federal Home Loan Bank ("FHLB") stock and marketable equity securities. Marketable equity securities consist of the Asset Management Fund for Financial Institutions, Inc. ("AMF Fund"), a mutual fund that invests in securities eligible for direct investment by savings associations and a $48,000 investment in corporate common stock. The Savings Bank uses this fund to increase its short-term yield, primarily on overnight funds. The AMF Fund consists primarily of adjustable-rate mortgage-related securities. These funds are marked to the lower of cost or market at the end of each month with all adjustments in value reported to the Board of Directors monthly. At September 30, 1996, the Savings Bank had $3.8 million or 30.2% of its investment securities portfolio in the AMF Fund. Bedford Federal will continue to seek high quality investment securities with short to intermediate maturities and durations from one to five years.

Mortgage-backed Securities. The Savings Bank purchased additional mortgage-backed securities during fiscal 1996. The mortgage-backed securities are participation certificates issued and guaranteed by the FHLMC and secured by an interest in pools of conventional mortgages originated by other financial institutions.

Mortgage-backed securities provide for monthly payments of principal and interest and generally have contractual maturities ranging from five to 30 years. However, due to expected repayment terms being significantly less than the underlying mortgage loan pool contractual maturities, the estimated lives of these securities could be significantly shorter.

The Savings Bank did not sell any mortgage-backed securities during the years ended September 30, 1996 and 1995.

As of September 30, 1996, mortgage-backed securities amounted to $482,000 or .38% of total assets. All mortgage-backed securities were fixed-rate.

Investment Carrying and Market Values. The following table sets forth certain information regarding the carrying and market values of the Savings Bank's federal funds sold and other short-term investments, investment securities, securities held for sale and mortgage-backed securities at the dates indicated:

<TABLE>
<CAPTION>

	At September 30,			
	1996		1995	
	Carrying Value	Market Value	Carrying Value	Market Value
	(In thousands)			
<S>	<C>	<C>	<C>	<C>
Federal funds sold and other short-term investments	$ 223	$ 223	$ 725	$ 725
Investment securities:				
Held for investment:				
FHLB stock..................................	932	932	932	932
U.S. Government and agency obligations.......	5,214	5,161	5,420	5,377
Total held for investment.................	6,369	6,316	7,077	7,034
Held for sale:				
U.S. Government and agency obligations.......	1,860	1,860	1,409	1,409
Marketable equity securities................	3,879	3,879	3,660	3,660
Total held for sale........................	5,739	5,739	5,069	5,069
Total	$12,178	$12,055	$12,146	$12,103
Mortgage-backed securities:				
Held for investment...........................	$ 25	$ 25	31	$ 31
Held for sale.................................	457	457	--	--
Total.....................................	$ 482	$ 482	$ 31	$ 31

</TABLE>

Investment Yields and Maturities. The table below sets forth certain information regarding the carrying value, weighted average yields and contractual maturities of the Savings Bank's federal funds sold and other short-term investments, investment securities, securities held for sale and mortgage-backed securities as of September 30, 1996.

<TABLE>
<CAPTION>

	As of September 30, 1996										
	One Year or Less		One to Five Years		Five to Ten Years		More Than Ten Years		Total Investment Securities		
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Market Value
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Federal funds sold and other short-term investments.	$ 223	5.15%	$ --	--%	$ --	--%	$ --	--%	$ 223	5.15%	$ 223
Held for investment:											
Investment securities:											
FHLB Stock...........	932	7.19	--	--	--	--	--	--	932	7.19	932
U.S. government and federal agency obligations.	--	--	3,481	5.87	1,733	7.80	--	--	5,214	6.51	5,161
Total investment securities held for investment....	$1,155	6.79	$ 3,481	5.87	$ 1,733	7.80	$ --	--	$6,369	6.56	$6,316
Total mortgage-backed securities held for investment	$ --	--	$ 25	8.43	$ --	--	$ --	--	$ 25	8.43	$ 25
Held for sale:											
U.S. Government and agencies	--	--	$ 1,391	6.49	$ 469	5.82	$ --	--	$1,860	6.32	$1,860
Marketable equity securities	3,879	6.05	--	--	--	--	--	--	3,879	6.05	3,879
Total investment securities held for sale..........	$ 3,879	6.05	$ 1,391	6.49	$ 469	5.82	$ --	--	$5,739	6.14	$5,739
Total mortgage-backed securities held for sale..........	$	--	$ --	--	$ --	--	$ 457	6.50	$ 457	6.50	$ 457

</TABLE>

Sources of Funds

General. Deposits are the major source of the Savings Bank's funds for lending and other investment purposes. The Savings Bank also derives funds from amortization and prepayment of loans, maturities of investment securities and operations and utilizes advances from the FHLB of Atlanta. Scheduled loan principal repayments are a relatively stable source of funds, while deposit inflows and outflows and loan prepayments are significantly influenced by general interest rates and market conditions. The Savings Bank does not have any brokered deposits.

Deposits. Customer deposits are attracted principally from within the Savings Bank's primary market area through the offering of a broad selection of deposit instruments including negotiable order of withdrawal accounts ("NOW") (including interest-bearing and noninterest-bearing), passbook and statement savings, money market deposit, term certificate accounts and Individual

Retirement Accounts. Deposit account terms vary according to the minimum balance required, the time period the funds must remain on deposit and the interest rate.

The interest rates paid by the Savings Bank on deposits are set at the direction of the asset/liability committee. The asset/liability committee consists of senior management. The interest rates on deposit account products are determined by evaluating the following factors: (i) the interest rates offered by other local financial institutions and the degree of competition the Savings Bank wishes to maintain; (ii) the Savings Bank's anticipated need for cash and the timing of that desired cash flow; (iii) the cost of borrowing from other sources versus the cost of acquiring funds through customer deposits; and (iv) the Savings Bank's anticipation of future economic conditions and related interest rates.

NOW accounts (including noninterest-bearing), money market accounts, passbook and statement savings accounts constituted $32.9 million, or 34.52% of the Savings Bank's deposit portfolio at September 30, 1996. Certificates of deposit constituted $62.5 million or 65.48% of the deposit portfolio, including certificates of deposit, with principal amounts of $100,000 or more, which constituted $7.0 million or 7.34% of the deposit portfolio at September 30, 1996. The Savings Bank has no brokered deposits.

Deposit Account Composition. The following table sets forth the distribution of the Savings Bank's deposit accounts for the periods indicated and the weighted average interest rates on each category presented.

<TABLE>
<CAPTION>

	For the Year Ended September 30,					
	1996			1995		
	Average Balance	Percent of Total Average Deposits	Weighted Average Rate	Average Balance	Percent of Total Average Deposits	Weighted Average Rate
	(Dollars in thousands)					
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Money market deposits.......	$ 5,011	5.39%	3.07	$ 5,957	6.91%	3.04%
Passbook and statement deposits	15,400	16.57	2.97	17,045	19.77	3.03
NOW and other demand deposits	7,316	7.87	2.77	5,971	6.92	2.81
Noninterest bearing deposits	5,131	5.52	--	4,717	5.47	--
Total.................	32,858	35.35	2.48	33,690	39.07	2.57
Certificate accounts:						
Three months or less.....	10,775	11.59	5.37	6,588	7.64	4.31
Over three through six month	8,437	9.08	5.34	7,914	9.18	5.05
Over six through 12 months	13,335	14.35	5.22	17,878	20.74	5.05
Over one to three years..	25,083	26.99	5.46	16,474	19.11	5.48
Over three to five years.	2,463	2.64	6.34	3,675	4.26	5.63
Total certificates....	60,093	64.65	5.41	52,529	60.93	5.13
Total deposits........	$92,951	100.00%		$86,219	100.00%	

</TABLE>

Deposit Account Rate Analysis. The following table presents, by various rate categories, the amount of certificate accounts outstanding at the dates indicated and the periods to maturity of the certificate accounts outstanding at September 30, 1996.

<TABLE>
<CAPTION>

At September 30, Period to Maturity from September 30, 1996

Over

	1996	1995	Within One Year	One To Three Years	Over Three Years	Total
			(In thousands)			
Certificate Accounts:						
<S>	<C>	<C>	<C>	<C>	<C>	<C>
3.00% or less......	$ --	$ 19	$ --	$ --	$ --	$ --
3.01% to 4.00%.....	75	572	75	--	--	75
4.01% to 5.00%.....	16,239	16,808	14,692	1,547	--	16,239
5.01% to 6.00%.....	36,025	25,667	14,009	21,010	1,006	36,025
6.01% to 7.00%.....	9,486	13,902	5,051	3,511	924	9,486
7.01% to 8.00%.....	627	755	--	--	627	627
8.01% to 9.00%.....	--	15	--	--	--	--
9.01% to 10.00%....	--	--	--	--	--	--
Over 10.01%........	--	--	--	--	--	--
Total...........	$62,452	$57,738	$33,827	$26,068	$2,557	$62,452

</TABLE>

Certificates of Deposit of $100,000 or More. The following table indicates the amount of the Savings Bank's certificates of deposit and other time deposits of $100,000 or more by time remaining until maturity as of September 30, 1996.

Maturity Period	Amount (In thousands)
Within three months............................	$ 742
Three through six months.......................	757
Six through twelve months......................	2,005
Over twelve months.............................	3,474
Total.....................................	$6,978

Deposit Activity. The following table presents the deposit activity of the Savings Bank for the periods indicated.

	For the Year Ended September 30, 1996	1995
	(Dollars in thousands)	
Opening balance....................	$90,063	$84,841
Net deposits (withdrawals).........	1,210	1,660
Interest credited on deposits......	4,105	3,562
Ending balance.....................	$95,378	$90,063
Total increase (decrease) deposits	$ 5,315	$ 5,222
Percentage increase (decrease)...	5.90%	6.16%

Borrowings. While deposits are the primary source of funds for the Savings Bank's lending and investment activities and for its general business purposes, the Savings Bank also obtains advances from the FHLB of Atlanta to supplement its supply of lendable funds. Advances from the FHLB of Atlanta are secured by the Savings Bank's first mortgage loans. The Savings Bank, if the need arises, may also access the Federal Reserve Bank discount window to supplement its supply of lendable funds and to meet deposit withdrawal requirements. At September 30, 1996 and 1995, the Savings Bank had $12.0 million and $5.0 million, respectively, of advances outstanding from the FHLB of Atlanta.

Personnel

As of September 30, 1996, the Savings Bank had 37 full-time employees. None of the Savings Bank's employees are represented by a collective bargaining group. The Savings Bank believes that its relationship with its employees is good.

Regulation

Set forth below is a summary description of certain laws which relate to the regulation of the Company and the Savings Bank. The description does not purport to be complete and is qualified in its entirety by reference to applicable laws and regulations.

Company Regulation

General. The Company is a unitary savings and loan holding company subject to regulatory oversight by the OTS and the SEC. As such, the Company is required to register and file reports with the OTS and the SEC and is subject to regulation and examination by the OTS. In addition, the OTS has enforcement authority over the Company and its non-savings association subsidiaries, should such subsidiaries be formed, which also permits the OTS to restrict or prohibit activities that are determined to be a serious risk to the subsidiary savings association.

Qualified Thrift Lender Test. As a unitary savings and loan holding company, the Company generally will not be subject to activity restrictions, provided the Savings Bank satisfies the QTL test. If the Company acquires control of another savings association as a separate subsidiary, it would become a multiple savings and loan holding company, and the activities of the Company and any of its subsidiaries (other than the Savings Bank or any other SAIF-insured savings association) would become subject to restrictions applicable to bank holding companies unless such other associations each also qualify as a QTL and were acquired in a supervisory acquisition. See "-- Savings Bank Regulation -- Qualified Thrift Lender Test."

Savings Bank Regulation

General. As a federally chartered, Savings Association Insurance Fund ("SAIF")-insured savings association, the Savings Bank is subject to extensive regulation by the OTS and the Federal Deposit Insurance Corporation ("FDIC"). Lending activities and other investments must comply with various federal statutory and regulatory requirements. The Savings Bank is also subject to certain reserve requirements promulgated by the Federal Reserve Board.

The OTS, in conjunction with the FDIC, regularly examines the Savings Bank and prepares reports for the consideration of the Savings Bank's Board of Directors on any deficiencies that they find in the Savings Bank's operations. The Savings Bank's relationship with its depositors and borrowers is also regulated to a great extent by federal law, especially in such matters as the ownership of savings accounts and the form and content of the Savings Bank's mortgage documents.

The Savings Bank must file reports with the OTS and the FDIC concerning its activities and financial condition, in addition to obtaining regulatory approvals prior to entering into certain transactions such as mergers with or acquisitions of other savings institutions. This regulation and supervision establishes a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of the SAIF and depositors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulations, whether by the OTS, the FDIC or the Congress could have a material adverse impact on the Company, the Savings Bank and their operations.

Insurance of Deposit Accounts. The Savings Bank's deposit accounts are insured by the SAIF to a maximum of $100,000 for each insured member (as defined by law and regulation).

Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or the institution's primary regulator.

Pursuant to the Economic Growth and Paperwork Reduction Act of 1996 (the "Act"), the FDIC imposed a special assessment on SAIF members to capitalize the SAIF at the designated reserve level of 1.25% as of October 1, 1996. Based on the Savings Bank's deposits as of March 31, 1995, the date for measuring the amount of the special assessment pursuant to the Act, the Savings Bank paid a special assessment of approximately $555,000 on November 27, 1996 to recapitalize the SAIF. The FDIC is expected to lower the premium for deposit insurance to a level necessary to maintain the SAIF at its required reserve level; however, the range of premiums has not been determined at this time.

Pursuant to the Act, the Savings Bank will pay, in addition to its normal deposit insurance premium as a member of the SAIF, an amount equal to approximately 6.4 basis points toward the retirement of the Financing Corporation bonds ("Fico Bonds") issued in the 1980's to assist in the recovery of the savings and loan industry. Members of the Bank Insurance Fund ("BIF"), by contrast, will pay, in addition to their normal deposit insurance premium, approximately 1.3 basis points. Based on total deposits as of September 30, 1996, had the Act been in effect, the Savings Bank's Fico Bond premium would have been approximately $61,000 in addition to its normal deposit insurance premium. Beginning no later than January 1, 2000, the rate paid to retire the Fico Bonds will be equal for members of the BIF and the SAIF. The Act also provides for the merging of the BIF and the SAIF by January 1, 1999 provided there are no financial institutions still chartered as savings associations at that time. Should the insurance funds be merged before January 1, 2000, the rate paid by all members of this new fund to retire the Fico Bonds would be equal.

Recent Tax Treatment Changes. The Bank computed income tax by application of Section 593(b)2 of the U.S. Internal Revenue Code which provided a special deduction for bad debts. The benefits of Section 593(b)2 were repealed by 1996 federal tax legislation. The Bank will now compute its tax bad debt deduction by use of the "experience method" which is based on a moving five-year average of actual loss experience. According to the legislation that "applicable excess reserves" must be recaptured as taxable income over five years beginning in fiscal 1997. The amount to be recaptured is the excess of the accumulated reserves since 1987 over the amount allowed by use of the experience method for those years. The Bank has been computing deferred taxes and therefore does not believe it will have a material effect on its reportable earnings.

Regulatory Capital Requirements. Set forth below is the Savings Bank's regulatory capital requirements applicable to it as of September 30, 1996:

	Amount	Percent of Adjusted Assets
	(Dollars in Thousands)	
Tangible Capital:		
Regulatory requirement............	$ 1,918	1.5%
Actual capital....................	15,844	12.4
Excess..........................	$13,926	10.9%
Core Capital:		
Regulatory requirement............	$ 3,835	3.0%
Actual capital....................	15,844	12.4
Excess..........................	$12,009	9.4%
Risk-Based Capital:		
Regulatory requirement(1).........	$ 5,677	8.0%
Actual capital....................	16,417	23.1
Excess..........................	$10,740	15.1%

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(1) Based on risk-weighted assets of $70,966.

Net Portfolio Value. In recent years, the Savings Bank has measured its interest rate sensitivity by computing the "gap" between the assets and liabilities which were expected to mature or reprice within certain periods, based on assumptions regarding loan prepayment and deposit decay rates formerly provided by the OTS. However, the OTS now requires the computation of amounts by which the net present value of an institution's cash flows from assets, liabilities and off balance sheet items (the institution's net portfolio value, or "NPV") would change in the event of a range of assumed changes in market interest rates. The OTS also requires the computation of estimated changes in net interest income over a four-quarter period. These computations estimate the effect of an institution's NPV and net interest income of instantaneous and permanent 1% to 4% increases and decreases in market interest rates. In the Savings Bank's interest rate sensitivity policy, the Board of Directors has established a maximum decrease in net interest income and maximum decreases in NPV given these instantaneous changes in interest rates.

In order to encourage associations to reduce their interest rate risk, the OTS adopted a final rule in August 1993 incorporating an interest rate risk ("IRR") component into the risk-based capital rules. The new rule was effective January 1, 1994, with institutions first required to meet the new standards at September 30, 1995. The IRR component is a dollar amount that will be deducted from total capital for the purpose of calculating an institution's risk-based capital requirement and is measured in terms of the sensitivity of its NPV to changes in interest rates. NPV is the difference between incoming and outgoing discounted cash flows from assets, liabilities, and off-balance sheet contracts. An institution's IRR is measured as the change to its NPV as a result of a hypothetical 200 basis point change in market interest rates. A resulting change in NPV of more than 2% of the estimated market value of its assets will require the institution to maintain additional capital. The rules provide that the OTS will calculate the IRR component quarterly for each institution.

The following table sets forth the interest rate risk capital component for the Savings Bank at September 30, 1996 given a hypothetical 200 basis point rate change in market interest rates. See "-- Regulatory Capital Requirements."

	As of September 30, 1996
	(Dollars in thousands)
RISK MEASURES:	
200 Basis Point Rate Shock	
Pre-Shock NPV Ratio: NPV as % of Present Value of Assets............	15.21%
Exposure Measure: Post-Shock NPV Ratio............................	13.38%
Sensitivity Measure: Change in NPV Ratio................................	-183 bp
CALCULATION OF CAPITAL COMPONENT:	
Change in NPV as % of Present Value of Assets............................	2.26%
Interest Rate Risk Capital Component....	$2,988

Computations of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates, loan prepayments and deposit run-offs, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions the Savings Bank may undertake in response to changes in interest rates.

Certain shortcomings are inherent in the method of analysis presented in both the computation of NPV and in the analysis presented in prior tables setting forth the maturing and repricing of interest-earning assets and interest-bearing liabilities. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in differing degrees to changes in market interest rates. The interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain assets, such as adjustable rate loans, which represent the Savings Bank's primary loan product, have features which restrict changes in interest rates on a short-term basis and over the life of the asset. In addition, the proportion of adjustable rate loans in the Savings Bank's portfolios could decrease in future periods if market interest rates remain at or decrease below current levels due to refinance activity. Further, in the event of a change in interest rates, prepayment and early withdrawal levels would likely deviate significantly from those assumed in the tables. Finally, the ability of many borrowers to service their adjustable-rate debt may decrease in the event of an interest rate increase.

Pursuant to the Financial Institutions Reform, Recovery and Enforcement Act of 1991 ("FIRREA"), the OTS must revise the risk-based capital regulations to include a credit risk component and a nontraditional activities component, the purpose of which will be to increase the minimum capital requirements for savings associations with higher credit risks.

Prompt Corrective Action. The FDICIA established a system of prompt corrective action to resolve the problems of undercapitalized institutions. Under this system, the banking regulators are required to take certain supervisory actions against undercapitalized institutions, the severity of which depends upon the institution's degree of capitalization. Under the OTS final rule implementing the

prompt corrective action provisions, an institution shall be deemed to be (i) "well capitalized" if it has total risk-based capital of 10.0% or more, has a Tier I risk-based capital ratio (core or leverage capital to risk-weighted assets) of 6.0% or more, has a leverage capital of 5.0% or more and is not subject to any order or final capital directive to meet and maintain a specific capital level for any capital measure, (ii) "adequately capitalized" if it has a total risk-based capital ratio of 8.0% or more, a Tier I risked-based ratio of 4.0% or more and a leverage capital ratio of 4.0% or more (3.0% under certain circumstances) and does not meet the definition of "well capitalized," (iii) "undercapitalized" if it has a total risk-based capital ratio that is less than 6.0%, a Tier I risk-based capital ratio that is less than 4.0% or a leverage capital ratio that is less than 4.0% (3.0% in certain circumstances), (iv) "significantly undercapitalized" if it has a total risk-based capital ratio that is less than 6.0%, a Tier I risk-based capital ratio that is less than 3.0% or a leverage capital ratio that is less than 3.0% and (v) "critically undercapitalized" if it has a ratio of tangible equity to total assets that is equal to or less than 2.0% In addition, under certain circumstances, a federal banking agency may reclassify a well capitalized institution as adequately capitalized and may require an adequately capitalized institution or an undercapitalized institution to comply with supervisory actions as if it were in the next lower category (except that the FDIC may not reclassify a significantly undercapitalized institution as critically undercapitalized).

Dividend and Other Capital Distribution Limitations. OTS regulations require the Savings Bank to give the OTS 30 days' advance notice of any proposed declaration of dividends to the Company, and the OTS has the authority under its supervisory powers to prohibit the payment of dividends to the Company. In addition, the Savings Bank may not declare or pay a cash dividend on its capital stock if the effect thereof would be to reduce the regulatory capital of the Savings Bank below the amount required for the liquidation account to be established pursuant to the Savings Bank's Plan of Conversion.

OTS regulations impose limitations upon all capital distributions by savings institutions, such as cash dividends, payments to repurchase or otherwise acquire its shares, payments to shareholders of another institution in a cash-out merger and other distributions charged against capital. The rule establishes three tiers of institutions, based primarily on an institution's capital level. An institution that exceeds all fully phased-in capital requirements before and after a proposed capital distribution ("Tier 1 institution") and has not been advised by the OTS that it is in need of more than the normal supervision can, after prior notice but without the approval of the OTS, make capital distributions during a calendar year equal to the greater of (i) 100% of its net income to date during the calendar year plus the amount that would reduce by one-half its "surplus capital ratio" (the excess capital over its fully phased-in capital requirements) at the beginning of the calendar year, or (ii) 75% of its net income over the most recent four quarter period. Any additional capital distributions require prior regulatory approval. As of September 30, 1996, the Savings Bank was a Tier 1 institution. In the event the Savings Bank's capital fell below its fully phased-in requirement or the OTS notified it that it was in need of more than normal supervision, the Savings Bank's ability to make capital distributions could be restricted. In addition, the OTS could prohibit a proposed capital distribution by any institution, which would otherwise be permitted by the regulation, if the OTS determines that such distribution would constitute an unsafe or unsound practice.

Finally, a savings association is prohibited from making a capital distribution if, after making the distribution, the savings association would be "undercapitalized" (not meet any one of its minimum regulatory capital requirements).

Qualified Thrift Lender Test. Savings institutions must meet a QTL test. If the Savings Bank maintains an appropriate level of Qualified Thrift Investments (primarily residential mortgages and related investments, including certain mortgage-related securities) ("QTIs") and otherwise qualifies as a QTL, it will continue to enjoy full borrowing privileges from the FHLB of Atlanta. The required percentage of QTIs is 65% of portfolio assets (defined as all assets minus intangible assets, property used by the institution in conducting its business and liquid assets equal to 10% of total assets). Certain assets are subject to a percentage limitation of 20% of portfolio assets. In addition, savings associations may include shares of stock of the FHLBs, FNMA and FHLMC as qualifying QTIs. An association must be in compliance with the QTL test on a monthly basis in nine out of every 12 months. As of September 30, 1996, the Savings Bank was in compliance with its QTL requirement with 81.15% of its assets invested in QTIs.

Federal Home Loan Bank System. The Bank is a member of the FHLB of Atlanta, which is one of 12 regional FHLBs that administers the home financing credit function of savings associations. Each FHLB serves as a reserve or central bank for its members within its assigned region. It is funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB System. It makes loans to members (i.e., advances) in accordance with policies and procedures established by the Board of Directors of the FHLB.

As a member, the Bank is required to purchase and maintain stock in the FHLB of Atlanta in an amount equal to at least 1% of its aggregate unpaid residential mortgage loans, home purchase contracts or similar obligations at the beginning of each year.

Federal Reserve System. The Federal Reserve Board requires all depository institutions to maintain non-interest bearing reserves at specified levels against their transaction accounts (primarily checking, NOW, and Super NOW checking accounts) and non-personal time deposits. The balances maintained to meet the reserve requirements imposed by the Federal Reserve Board may be used to satisfy the liquidity requirements that are imposed by the OTS. At September 30, 1996, the Bank was in compliance with these Federal Reserve Board requirements.

Subsidiary Activity

In August 1994, the Company acquired all of the capital stock of the Savings Bank. The officers of the Company consist of the officers of the Savings Bank. The Company is organized as a holding company. As of September 30, 1996, the net book value of the Company's investment in the Savings Bank amounted to $15.9 million.

The Savings Bank has one subsidiary, First Financial Enterprises, Inc. ("FFE") which was incorporated in the State of Virginia and is engaged in the sale of mortgage life insurance.

Item 2. Description of Property.

(a) The Savings Bank conducts its business through a main office located in Bedford, Virginia and two branch offices. The Savings Bank installed three freestanding ATM's during fiscal 1995; all were in operation at September 30, 1996. The Savings Bank believes that the current facilities are adequate to meet its present and immediately foreseeable needs.

<TABLE>
<CAPTION>

Location	Leased or Owned	Original Date Leased or Acquired	Date of Lease Expiration	Net Book Value of Property or Leasehold Improvements at September 30, 1996
				(In thousands)
<S>	<C>	<C>	<C>	<C>
125-133 W. Main Street Bedford, VA 24523	Owned	12/70 - Main Office 12/84 -Drive thru 3/89 - Annex	N/A	$557,000
655 at 122 Moneta, VA 24121	Land Leased	8/86	8/01(1)	N/A
	Building Owned	1/87	N/A	133,000
ATM Route 122	Land			

Moneta, VA 24121	Leased	7/95	8/01(1)	
	Building Owned	8/95		29,000
Forest Village Square including ATM Forest, VA 24551	Owned	12/78	N/A	215,000
Longwood Avenue (ATM) Bedford, VA 24523	Owned	1/85	N/A	80,000

</TABLE>

----
(1) Lease is renewable for one five-year term.

At September 30, 1996, the Bank had a total investment in its land, buildings and improvements, and fixtures, furniture and equipment of $2,283,000, less accumulated depreciation of $1,045,000, or a net carrying value of $1,238,000.

The Bank owns various bookkeeping and accounting equipment and is on-line with an outside data processing company, BISYS, Inc.

(b) Investment Policies. See "Item 1. Business" for a general description of the Company's investment policies and any regulatory or Board of Directors' percentage of assets limitations regarding certain investments. All of the Company's investment policies are reviewed and approved by the Board of Directors of the Company or the Savings Bank, and such policies, subject to regulatory restrictions (if any), can be changed without a vote of stockholders. The Company's investments are primarily acquired to produce income, and to a lesser extent, possible capital gain.

(1) Investments in Real Estate or Interests in Real Estate. See "Item 1. Business -- Lending Activities" and "Item 2. Properties."

(2) Investments in Real Estate Mortgages. See "Item 1. Business -- Lending Activities" and "Item 1. Business -- Regulation."

(3) Investments in Securities of or Interests in Persons Primarily Engaged in Real Estate Activities. See "Item 1. Business -- Lending Activities," "Item 1. Business -- Regulation" and "Item 1. Business -- Subsidiary Activity."

(c) Description of Real Estate and Operating Data.

Not Applicable.

Item 3. Legal Proceedings

Neither the Corporation nor the Bank are engaged in any legal proceedings of a material nature at the present time. From time to time, the Bank is a party to legal proceedings in the ordinary course of business wherein it enforces its security interest in mortgage loans made by it.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

PART II

Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters

The information contained under the sections captioned "Stock Market Information" in the Corporation's Annual Report to Stockholders for the Fiscal Year Ended September 30, 1996 (the "Annual Report") is incorporated herein by reference. The Annual Report is included as Exhibit 13 to this Form 10-KSB.

Item 6. Management's Discussion and Analysis of Financial Condition and Results of Operations

The required information is contained in the section captioned "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report and is incorporated herein by reference.

Item 7. Financial Statements

The Corporation's consolidated financial statements required herein are incorporated herein by reference.

Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

Not applicable.

Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(b) of the Exchange Act

The required information is on pages 3-9 of the Registrant's definitive proxy statement for Registrant's 1997 Annual Meeting of Stockholders filed with the Commission on December 17, 1996 (the "Proxy Statement") is incorporated herein by reference.

Item 10. Executive Compensation

The required information is contained under the section captioned "Management Remuneration and Other Information - Executive Compensation" on pages 10-12 in the Proxy Statement is incorporated herein by reference.

Item 11. Security Ownership of Certain Beneficial Owners and Management

(a) Security Ownership of Certain Beneficial Owners

Information required by this item is incorporated herein by reference to the Section captioned "Voting Securities and Principal Holders Thereof" on pages 2-3 of the Proxy Statement.

(b) Security Ownership of Management

Information required by this item is incorporated herein by reference to the section captioned "Information with Respect to Nominees for Director; Directors Whose Term Continues; and Executive Officers -- Election of Directors" on pages 4-6 of the Proxy Statement.

(c) Management of the Corporation knows of no arrangements, including any pledge by any person of securities of the Corporation, the operation of which may at a subsequent date result in a change in control of the registrant.

Item 12. Certain Relationships and Related Transactions

The information required by this item is incorporated herein by reference to the section captioned "-- Certain Transactions with Management and Others" on page 15 of the Proxy Statement.

Item 13. Exhibits, List and Reports on Form 8-K

a. Exhibits

3.1 Restated Articles of Incorporation of Bedford Bancshares, Inc.*

3.2 Bylaws of Bedford Bancshares, Inc.*

4 Specimen Stock Certificate*

10.1 1994 Stock Option Plan*

10.2 Recognition and Retention Plan and Trust Agreement*

10.3 Employment Agreement with Harold K. Neal*

11 Computation of Earnings Per Share

13 Annual Report to Stockholders for Fiscal Year Ended September 30, 1996

21 Subsidiaries of the Registrant (See Item 1 - Business -- Subsidiary Activity)

23 Independent Auditors' Consents

27 Financial Data Schedule **

99 Prior Accountant's Independent Auditor's Report

* Included as an exhibit to the Registrant's Form 10-KSB filed with the SEC on December 19, 1994, and is incorporated by reference herein.

** Only included in electronic filing.

b. Reports on Form 8-K

No reports on Form 8-K were filed by the Registrant during the last quarter of the period covered by this report.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BEDFORD BANCSHARES, INC.

Date: December 30, 1996

By /s/ Harold K. Neal
Harold K. Neal, President and
Chief Executive Officer
(Duly Authorized Representative)

Pursuant to the requirement of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By: /s/ Harold K. Neal Harold K. Neal President, Chief Executive Officer and Director (Principal Executive Officer)	/s/ Hugh H. Bond Hugh H. Bond Chairman of the Board
Date: December 30, 1996	Date: December 30, 1996
By: /s/ James W. Smith James W. Smith Vice President, Treasurer and Comptroller (Principal Financial and Accounting Officer)	/s/ George N. Cooper George N. Cooper Director
Date: December 30, 1996	Date: December 30, 1996
By: /s/ Macon C. Putney Macon C. Putney Director	/s/ Harry W. Garrett, Jr. Harry W. Garrett, Jr. Director
Date: December 30, 1996	Date: December 30, 1996
By: /s/ W. Henry Walton, Jr. W. Henry Walton, Jr. Director	/s/ William P. Pickett William P. Pickett Director
Date: December 30, 1996	Date: December 30, 1996

By: /s/ William T.Powell

William T. Powell
Director

Date: December 30, 1996

EXHIBIT 11

Computation of Earnings Per Share

STATEMENT REGARDING COMPUTATION OF EARNINGS PER SHARE

	Three Months Ended September 30, 1996	Twelve Months Ended September 30, 1996
Net Income............................	$ 125,000	$1,302,000
Primary and Fully Diluted		
Average Shares Outstanding Net of Unallocated ESOP Shares (70,667).....	1,079,715	1,112,697
Per Share Amount.....................	$ .12	$ 1.17

Earnings per share of common stock for the three months and twelve months ended September 30, 1996 have been determined by dividing net income for the periods by the weighted average number of shares of common stock outstanding net of unallocated ESOP shares.

EXHIBIT 13

Annual Report to Stockholders for Fiscal Year
Ended September 30, 1996

[CORPORATE LOGO]

BEDFORD BANCSHARES, INC.

1996 ANNUAL REPORT

BEDFORD BANCSHARES, INC. - 1996 ANNUAL REPORT

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Corporate Profile and Related Information

Bedford Bancshares, Inc. (the "Company") is the parent company of Bedford Federal Savings Bank ("Bedford Federal" or the "Savings Bank"). The Company is a unitary savings and loan holding company which, under existing laws, generally is not restricted in the types of business activities in which it may engage, provided that the Savings Bank retains a specified amount of its assets in housing-related investments. At the present time, since the Company does not conduct any active business, the Company does not intend to employ any persons other than officers, but utilizes the support staff and facilities of the Savings Bank from time to time.

Bedford Federal, a federally-chartered stock savings bank headquartered in Bedford, Virginia, was originally chartered in 1935 under the name "Bedford Federal Savings and Loan Association." The Savings Bank has operated as a federally-chartered stock savings bank since its mutual-to-stock conversion on August 19, 1994. Deposits have been federally insured since 1935 and are currently insured up to the maximum amount allowable by the Federal Deposit Insurance Corporation (the "FDIC"). The Savings Bank is a community oriented savings institution offering a variety of financial services to meet the needs of the communities that it serves. Bedford Federal conducts its business from its main office in Bedford, Virginia, two full service branch offices located in Bedford County, Virginia, and three Automated Teller Machines ("ATMs").

The Savings Bank attracts deposits from the general public and uses such deposits, together with borrowings and other funds, primarily to originate loans secured by first mortgages on owner-occupied, one-to-four family residences in its market area and to invest in mortgage-backed and investment securities. To a lesser extent, Bedford Federal also originates construction loans, commercial real estate and consumer loans.

Stock Market Information

The Company's common stock trades on the Nasdaq National Market under the trading symbol of "BFSB". The daily stock quotation for Bedford Bancshares, Inc., is published in The Wall Street Journal and in other local newspapers under the trading symbol of "BFSB" or "Bedford Bc". The following table reflects the stock price as published by the Nasdaq National Market statistical report.

<TABLE>
<CAPTION>

Quarter Ended	High	Low	Volume	Dividends Per Share Declared	Dividends Per Share Paid
<S>	<C>	<C>	<C>	<C>	<C>
December 1994	$11.75	$10.25	153,965	--	--
March 1995	$13.00	$10.75	90,995	$.15	--
June 1995	$16.25	$12.25	298,726	--	$.15
September 1995	$18.75	$15.50	209,914	$.15	--
December 1995	$18.75	$17.50	93,376	$.09	$.15
March 1996	$18.25	$16.75	120,970	$.09	$.09
June 1996	$17.75	$15.75	189,406	$.10	$.09
September 1996	$17.25	$16.50	85,591	$.11	$.10

</TABLE>

On September 30, 1996, there were approximately 651 shareholders of record with approximately 51.6% of the 1,143,669 outstanding shares held in nominee or "street" name through various brokerage firms. There were seven firms making a market in the Company's common stock during the month of September 1996.

The Savings Bank may not declare or pay a cash dividend on its stock if the effect thereof would cause the regulatory capital of the Savings Bank to be reduced below (1) the amount required for the liquidation account established in connection with the Savings Bank's conversion from mutual to stock form, or (2) the regulatory capital requirements imposed by the Office of Thrift Supervision ("OTS").

Letter from the Chief Executive Officer

To Our Stockholders:

I am pleased to report that Bedford Bancshares, Inc. experienced solid performance and growth during fiscal 1996. The year was highlighted by a record level of loan closings, strong growth of core earnings, a 30% increase in dividends declared and the resolution of the deposit insurance premium disparity between the Savings Association Insurance Fund ("SAIF") and the Bank Insurance Fund ("BIF").

During the fourth quarter of fiscal 1996, federal legislation was passed imposing a one-time assessment on all members of the SAIF, including Bedford Federal, in order to recapitalize the SAIF to the congressionally mandated ratio of 1.25%. The assessment, based on the level of an institution's domestic deposits at March 31, 1995, amounted to approximately $555,000 ($344,000 on an after-tax basis) for Bedford Federal. As a result of the one-time assessment, we anticipate a reduction in future SAIF premiums.

Reflecting the impact of the one-time assessment, net income for fiscal 1996 amounted to $1.3 million compared to $1.4 million for fiscal 1995. On a per share basis, earnings for fiscal 1996 and 1995 were $1.17 and $1.20, respectively. The return on average assets for the year ended September 30, 1996, was 1.10% compared to a return of 1.28% for the previous year. The returns on average equity were 6.98% and 7.31% for fiscal 1996 and 1995, respectively. Without the one-time assessment, net income for fiscal 1996 would have exceeded $1.6 million, or $1.48 per share.

Total assets were $127.2 million on September 30, 1996, up 10.5% from the level one year earlier. The asset growth was focused in net loans receivable, which increased 11.5% in fiscal 1996 over fiscal 1995. During fiscal 1996, a record $29.6 million of mortgage loans were closed representing a 38.1% increase over fiscal 1995. As a result, total mortgage loans at September 30, 1996, were 9.40% above the level at the end of fiscal 1995. In addition, home equity loans were up 46.4% and installment loans were up 23.6% from fiscal year end 1995 to fiscal year end 1996. These increases reflect the fairly stable interest rate environment experienced during fiscal 1996, as well as the continuing growth in the markets served by Bedford Federal.

Stockholders' equity ended fiscal 1996 at $18.2 million, down 2.5% from the $18.6 million on September 30, 1995. The modest decrease primarily reflects the repurchase of 65,390 shares of the Corporation's common stock at an aggregate price of $1.1 million and dividend declarations of $457,000 (.$39 per share), mostly offset by net income of $1.3 million.

We were deeply saddened by the death of T. Glenn Bradley on September 23, 1996. Mr. Bradley had served as a director for 30 years and as Chairman of the Board since 1983. Mr. Bradley was a valuable asset to Bedford Bancshares, Inc., and we will all miss his keen insight, wisdom and kindness. Mr. Hugh Bond was elected Chairman of the Board to fill the vacancy left by Mr. Bradley's death. Mr. Bond has been a director for 33 years and had served as president since 1970.

This report provides details of our progress in fiscal 1996. The successes we enjoyed reflect the loyalty and support of our customers and stockholders, and the dedication, commitment and pride of your Board of Directors, management and staff. We thank you and look forward to continued success in the future.

Sincerely,

/s/ Harold K. Neal
Harold K. Neal
President and Chief Executive Officer
December 16, 1996

<TABLE>
<CAPTION>

SELECTED FINANCIAL AND OTHER DATA

Financial Condition (Dollars in Thousands)

At September 30,	1996	1995	1994	1993	1992
<S>	<C>	<C>	<C>	<C>	<C>
Total assets......................	$127,201	115,054	$105,217	$96,933	$94,723
Loans receivable, net.............	108,873	97,669	89,309	80,995	77,211
Investment securities.............	8,006	7,761	7,651	5,915	5,867
Marketable equity securities.......	3,879	3,660	3,360	3,289	3,091
Mortgage-backed securities.........	482	31	37	47	59
Foreclosed real estate, net........	--	--	--	31	329
Deposits..........................	95,378	90,063	84,841	89,187	88,745
FHLB advances.....................	12,000	5,000	1,000	1,000	--
Retained earnings.................	8,739	8,263	7,519	6,144	5,219
Total stockholders equity.........	18,227	18,685	18,659	--	--

Summary of Operations (Dollars in Thousands)

Year Ended September 30,	1996	1995	1994	1993	1992
Interest income....................	$9,264	$8,137	$6,964	$7,095	$7,905
Interest expense...................	4,492	3,778	3,478	3,740	4,929
Net interest income................	4,772	4,359	3,486	3,355	2,976
Provision for credit losses........	22	20	51	234	182
Non-interest income................	735	543	554	497	508
Non-interest expense...............	3,429(1)	2,620	2,238	2,089	2,081
Net income before income taxes and cumulative effect of change in accounting principle.............	2,056	2,262	1,751	1,529	1,221
Net income.........................	1,302	1,401	1,445	925	677

Other Selected Data

Year Ended September 30,	1996	1995	1994(2)	1993	1992
Return on average assets...........	1.10%	1.28%	1.12%	.97%	.72%
Return on average equity...........	6.98	7.31	12.89	16.25	13.82
Average equity to average assets...	15.69	17.49	8.71	5.98	5.25
Net interest rate spread...........	3.34	3.26	3.28	3.39	3.07
Non-performing assets to total assets	.54	1.14	1.07	.40	.88
Non-performing loans to total loans	.63	1.34	1.26	.44	.66
Allowance for loan losses to total loans	.60	.63	.71	.73	1.02

Per Share Data

Year Ended September 30,	1996	1995	1994(2)	1993	1992
Net income per share...............	$ 1.17	$ 1.20	$ 1.23	N/A	N/A
Book value per share...............	16.95	16.81	15.84	N/A	N/A
Cash dividends declared per share..	.39	.30	--	N/A	N/A

</TABLE>

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(1) Includes a one-time, special assessment of $555,000 to recapitalize the SAIF.

(2) Income and related ratios exclude the cumulative effect of a change in accounting principle of $323,000 in fiscal year 1994.

Total Assets [Graphics Omitted - Plotting Points Below]

Bar graph showing Total Assets in thousands of dollars for the year ended September 30. The horizontal axis shows the years 1992 to 1996 and the vertical axis shows amounts from $0 to $140,000. Graph values are $94,723, $96,933, $105,217, $115,054, $127,201 for 1992, 1993, 1994, 1995, and 1996, respectively.

Loan Portfolio Composition [Graphics Omitted - Plotting Points Below]

Pie Chart showing Loan Portfolio Composition identifying the type of loan and in percentages At September 30, 1996. 1-4 Family Residential (76.7%), Commercial & Multi-Family Real Estate (5.4%), Consumer/Commercial Business (8.1%), Construction (6.0%), Land (3.8%).

Deposit Portfolio Composition [Graphics Omitted - Plotting Points Below]

Pie Chart showing Deposit Portfolio Composition identifying the type of deposit and in percentages At September 30, 1996. Certificates (65.5%), Checking (13.7%), Savings (16.0%), Money Market (4.8%).

Net Interest Incom [Graphics Omitted - Plotting Points Below]

Bar graph showing Net Interest Income in thousands of dollars for the year ended September 30. The horizontal axis shows the years 1992 to 1996 and the vertical axis shows amounts from $0 to $5000. Graph values are $2,976, $3,355, $3,486, $4,359, $4,772 for 1992, 1993, 1994, 1995, and 1996, respectively.

Net Income [Graphics Omitted - Plotting Points Below]

Bar graph showing Net Income in thousands of dollars for the year ended September 30. The horizontal axis shows the years 1992 to 1996 and the vertical axis shows amounts from $0 to $1500. Graph values are $677, $925, $1,445, $1,401, $1,302 for 1992, 1993, 1994, 1995, and 1996, respectively.

Return on Average Assets [Graphics Omitted - Plotting Points Below]

Bar graph showing Return On Average Assets stated in percentages for the year ended September 30. The horizontal axis shows the years 1992 to 1996 and the vertical axis shows amounts from 0.00% to 1.50%. Graph values are 0.72%, 0.97%, 1.12%, 1.28%, 1.10% for 1992, 1993, 1994, 1995, and 1996, respectively.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management Strategy

The Company's management strategy is to maintain profitability and a strong capital position through controlled growth. This has been accomplished in the past by the Savings Bank's focus upon the origination of traditional one- to four-family, adjustable rate mortgage loans which are retained in its loan portfolio. To a lesser extent, the Savings Bank originates 10 to 15 year, fixed-rate mortgage loans, and consumer loans, including home equity, automobile and personal loans. This strategy, along with prudent underwriting standards, is designed to reduce the risk of loss in the Savings Bank's loan portfolio as well as to reduce the interest risk exposure.

Management has increased the interest rate sensitivity of Bedford Federal's earning assets to better match the sensitivity of its interest bearing liabilities, while maintaining high asset quality. This has been accomplished by: (1) originating adjustable-rate mortgage loans and shorter term consumer loans for its portfolio, (2) emphasizing the solicitation and retention of core deposits from within the Savings Bank's market area, (3) investing in short- and intermediate-term investments, (4) adhering to sound underwriting and investment standards, and (5) effectively managing interest rates paid on deposits.

In its efforts to manage the interest rates it pays on deposits, the Savings Bank focuses on maintaining a stable deposit base while providing efficient and quality service to its customers. Historically, Bedford Federal has relied primarily upon the cash flows from its deposits and mortgage payments as its major sources of funds, however, in recent years the bank has utilized borrowings from the Federal Home Loan Bank ("FHLB") to meet increased lending requirements.

General

Net interest income is the primary source of the Company's earnings. Net interest income is affected by the levels of average earning assets and average interest bearing liabilities, and the respective interest rates earned and paid. The difference between average rates of interest earned on interest earning assets and average rates paid on interest bearing liabilities is the "interest rate spread." The "net interest margin" relates net interest income to average earning assets and serves as an indication of the effectiveness of funds allocation.

The Savings Bank also receives income from service charges and other fees primarily related to credit and deposit services. Bedford Federal incurs expenses in its day-to-day operations including salaries and benefits, deposit insurance, facilities expense, marketing and other related business expenses.

Interest Rate Sensitivity Analysis

As rates on sources of funds have become deregulated and subject to competitive pressures, financial institutions have become increasingly concerned with the extent to which they are able to match maturities of interest-earning assets and interest-bearing liabilities. Such matching is facilitated by examining the extent to which such assets and liabilities are "interest rate sensitive" and by monitoring the interest rate sensitivity "gap." The "gap" represents the difference between interest-earning assets and interest-bearing liabilities maturing or repricing within a specific time period. The following table sets forth the amounts of interest earning assets and interest bearing liabilities outstanding at September 30, 1996, which are expected to reprice or mature in each of the future time periods shown. It is important to note that certain shortcomings are inherent in the method of analysis presented in the table. For example, although certain assets and liabilities may have similar maturities or periods of repricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain assets, such as adjustable-rate mortgage loans have features which restrict changes in interest rates on a short-term basis over the life of the assets. Further in the event of a change in interest rates, prepayment levels and decay rates on core deposits may deviate significantly from those assumed in calculating the table.

The following table indicates the time periods in which interest-earning assets and interest bearing liabilities will mature or reprice in accordance with their contractual terms. The table assumes prepayments and scheduled principal amortization of fixed-rate loans and mortgage-backed securities, and assumes that adjustable rate mortgage loans will reprice at contractual repricing intervals. There has been no adjustment for the impact of future commitments and loans in process.

<TABLE>
<CAPTION>

	At September 30, 1996						
	Three Months or Less	More than 3 Months to 6 Months	More than 6 Months to 1 Year	More than 1 Year to 3 Years	More than 3 Years to 5 Years	More Than 5 Years	Total
	(Dollars in Thousands)						
Interest-earning assets:							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Mortgage loans(1)(2)	$ 7,409	$ 8,506	$ 64,760	$ 8,541	$ 3,152	$ 9,259	$101,627
Other loans(1)	3,830	526	957	5,238	843	--	11,394
Marketable equity securities(3)	3,879	--	--	--	--	--	3,879
Federal funds sold and other short- .. term investments	223	--	--	--	--	--	223
Investment securities	--	--	--	2,708	1,883	2,483	7,074
Mortgage-backed securities(2)	--	--	--	25	--	457	482
FHLB stock	932	--	--	--	--	--	932
Total interest-earning assets	16,273	9,032	65,717	16,512	5,878	12,199	125,611
Less:							
Loans in process	1,600	1,599	--	--	--	--	3,199
Unearned discount and deferred fees(2)	26	20	179	38	11	25	299
Allowance for credit losses	56	43	390	82	24	55	650
Net interest-earning assets	14,591	7,370	65,148	16,392	5,843	12,119	121,463
Interest-bearing liabilities:							
Money market deposits	1,479	1,001	1,137	504	240	218	4,579
Passbook deposits	679	648	1,209	4,225	2,511	6,018	15,290
NOW and other demand deposits	829	738	1,244	2,573	689	1,525	7,598
Certificate accounts	11,197	--	22,624	26,071	2,560	--	62,452
Borrowed funds	2,000	--	10,000	--	--	--	12,000
Total interest-bearing liabilities	16,184	2,387	36,214	33,373	6,000	7,761	101,919
Interest sensitivity gap(4)	$ (1,593)	$ 4,983	$ 28,934	$(16,981)	$ (157)	$ 4,358	$ 19,544
Cumulative interest sensitivity	$ (1,593)	$ 3,390	$ 32,324	$ 15,343	$ 15,186	$ 19,544	
Cumulative interest sensitivity gap as a percent of total assets	(1.25)%	2.67%	25.41%	12.06%	11.94%	15.36%	
Cumulative net interest-bearing assets as a percent of interest-bearing liabilities	90.16 %	118.25%	159.00%	117.40%	116.13%	119.18%	

</TABLE>

----
(1) For purposes of the gap analysis, mortgage and other loans are reduced for nonperforming loans but are not reduced for the allowance for credit

losses.
(2) For purposes of the gap analysis, unearned discount and deferred fees are pro rated for mortgage loans and mortgage backed securities.
(3) Includes assets held for sale.

Analysis of Net Interest Income

The following table sets forth certain information relating to the Savings Bank's average balance sheet and reflects the interest earned on assets and interest expense of liabilities for the periods indicated and the average yields earned and rates paid. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods presented. Average balances are derived from daily balances.

<TABLE>
<CAPTION>

	For the Year Ended September 30,					
	1996			1995		
	Average Balance	Interest	Yield/ Average Cost	Average Balance	Interest	Yield/ Average Cost
	(Dollars in Thousands)					
Assets:						
Interest-earning assets:						
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Mortgage loans(1)	$ 91,605	$ 7,408	8.09%	$ 86,126	$ 6,632	7.70%
Other loans(1)	9,305	972	10.45	7,413	736	9.93
Interest-earning deposits(2)	3,718	225	6.05	3,472	211	6.08
Federal funds sold and other short-term investments	1,050	93	8.86	924	58	6.28
Investment securities	7,112	479	6.74	6,743	430	6.38
Mortgage-backed securities, net	287	20	6.97	35	3	8.57
FHLB stock	932	67	7.19	932	67	7.19
Total interest-earning assets	114,009	9,264	8.13	105,645	8,137	7.70
Noninterest earning assets	4,807			3,886		
Total assets	$118,816			$109,531		
Liabilities and equity:						
Interest-bearing liabilities:						
Money market deposits	$ 5,011	$ 154	3.07%	$ 5,957	$ 181	3.04%
Passbook deposits	15,400	458	2.97	17,045	516	3.03
NOW and other demand deposits	7,316	203	2.77	5,971	168	2.81
Certificate accounts	60,093	3,313	5.51	52,529	2,697	5.13
Total savings accounts	87,820	4,128	4.70	81,502	3,562	4.37
Borrowed funds	6,018	364	6.05	3,596	216	6.01
Total interest-bearing liabiliies	93,838	4,492	4.79	85,098	3,778	4.44
Noninterest-bearing liabilities	6,336			5,278		
Equity	18,642			19,155		
Total liabilities and equity	$118,816			$109,531		
Net interest income		$ 4,772			$ 4,359	
Interest rate spread(3)			3.34%			3.26%
Net interest margin(4)			4.19%			4.13%
Ratio of interest-earning assets interest-bearing liabilities	121.50%			124.15%		

</TABLE>

----
(1) Amount is net of deferred loan fees and discounts, loans in process and

allowance for credit losses and includes accrued interest.
(2) Includes assets held for sale.
(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 margin represents net interest income divided by average interest-earning assets.

The following table sets forth certain information regarding changes in interest income and expense of the Savings Bank for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes due to (1) changes in volume (change in average volume times the old rate); (2) changes in rate (changes in rate times the old average volume); and (3) net change. The change attributable to the combined impact of volume and rate have been allocated proportionately to the changes due to volume and the changes due to rate.

<TABLE>
<CAPTION>

	Year Ended September 30,					
	1995 vs. 1996			1994 vs. 1995		
	Increase (Decrease) Due to			Increase (Decrease) Due to		
	Volume	Rate	Net	Volume	Rate	Net
	(Dollars In Thousands)					
Interest-earning assets:						
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Mortgage loans	$ 432	$ 344	$ 776	$ 501	$ 324	$ 825
Other loans	195	41	236	190	16	206
Interest-earning deposits	15	(1)	14	6	60	66
Federal funds sold and other short-term investments	9	26	35	11	(13)	(2)
Investment securities, net	24	25	49	73	(8)	65
Mortgage-backed securities, net	18	(1)	17	(1)	--	(1)
FHLB stock	--	--	--	--	14	14
Total interest-earning assets	693	434	1,127	780	393	1,173
Interest-bearing liabilities:						
Money market deposits	(29)	2	(27)	--	4	4
Passbook deposits	(49)	(9)	(58)	(119)	--	(119)
NOW and other demand deposits	38	(3)	35	9	(7)	2
Certificate accounts	406	210	616	(35)	273	238
Borrowed funds	146	2	148	140	35	175
Total interest-bearing liabilities..	512	202	714	(5)	305	300
Net change in interest income	$ 181	$ 232	$ 413	$ 785	$ 88	$ 873

</TABLE>

Comparison of Financial Condition for Fiscal Years Ended September 30, 1996 and 1995.

The Corporation's total assets were $127.2 million at September 30, 1996, an increase of 10.5% from the $115.1 million on September 30, 1995. The asset growth was primarily due to a 11.47% rise in loans receivable, net, from $97.7 million at fiscal year-end 1995 to $108.9 at fiscal year-end 1996.

An increase in new home construction within the markets Bedford Federal serves combined with the stable interest rate environment that continued during fiscal 1996 were the major factors in the expansion of loans. This increase was funded primarily by principal repayments of the loan portfolio, increased deposits, and FHLB advances. Because lending is directly affected by interest rates, a rise in interest rates could cause a slow down in new loan originations. Investment securities increased $245,000, marketable equity securities rose $219,000 and mortgage-backed securities were up $451,000 in 1996 over 1995.

At September 30, 1995 and 1996, the Corporation's total investments in loans receivable, net, and securities equalled 94.8% and 95.3% of total assets, respectively. Effective October 1, 1994, the Corporation adopted SFAS 115, "Accounting for Certain Investments in Debt 3 and Equity Securities." SFAS 115 requires that all investments in debt securities and all investments in equity securities that have readily determinable fair values be classified into three categories. Securities that management has positive intent and ability to hold until maturity will be classified as held to maturity. Securities that are purchased and held specifically for the purpose of selling in the near future will be classified as trading securities. All other securities will be classified as available for sale. Securities

classified as trading and available for sale will be carried at market value. Unrealized holding gains and losses for trading securities will be included in current income. Unrealized holding gains and losses for available for sale securities will be reported as a net amount in a separate component of stockholders' equity until realized. At September 30, 1996, Bedford Bancshares had $5.2 million of securities held to maturity and $6.2 million of securities available for sale. In addition, at September 30, 1996, the Bank had $932,000 invested in Federal Home Loan Bank ("FHLB") stock.

Deposits totaled $95.4 million at September 30, 1996, an increase of $5.3 million from $90.1 million at September 30, 1995. The increase was partially attributable to the higher rates paid on deposits during fiscal 1996 combined with the healthy economic environment in the areas served by Bedford Federal. Advances from the FHLB totaled $12 million at September 30, 1996, an increase of $7 million from $5 million at September 30, 1995. The increase was primarily used to fund the increase in the loan portfolio.

Total stockholders' equity was $18.2 million on September 30, 1996, down $458,000 from the $18.7 million one year previous. This planned reduction reflects the acquisition of 65,390 shares of the Corporation's common stock at an aggregate cost of $1.1 million under the stock buy back program conducted during 1996. In addition, the Corporation declared $457,000 of dividends during fiscal 1996 and realized net income of $1.3 million. The equity-to-asset ratio at September 30, 1996 stood at 14.3% down from 16.2% one year earlier.

Comparison of Operating Results for Years Ended September 30, 1996 and 1995

Net Income. Net income decreased $99,000 in fiscal 1996 from fiscal 1995. During the fourth quarter of fiscal 1996, the FDIC imposed a one-time assessment on all members of the SAIF in order to recapitalize the SAIF to the federally mandated level of 1.25%. The assessment amounted to approximately $555,000 for Bedford Federal ($344,000 on an after tax basis). Excluding the impact of the assessment, net income would have been $1.6 million, or 14.2% higher than fiscal 1995.

Interest Income. Interest income totaled $9.3 million for the fiscal year ended September 30, 1996, a 13.9% increase from the $8.1 million recorded for fiscal 1995. The $1.2 million expansion of interest income is due to the 7.9% growth of average earning assets, primarily loans, coupled with the overall improvement in the rate earned on average earning assets. The table on page 9 provides a detailed analysis of the changes in interest income due to volume and rate.

Interest Expense. Interest expense increased $714,000 from $3.8 million for the year ended September 30, 1995 to $4.5 million for the fiscal year ended September 30, 1996. Both the level and cost of average interest-bearing liabilities rose in fiscal 1996 over fiscal 1995. Average interest-bearing liabilities rose 10.2% and the cost increased 35 basis points in fiscal 1996 over fiscal 1995, primarily due to a 38 basis point increase in certificate accounts due to more aggressive pricing and a larger balance of FHLB advances which tend to have higher costs than deposit accounts. The table on the previous page provides a detailed analysis of the change in interest expense due the changes in volume and rate.

Net Interest Income. Net interest income totaled $4.8 million for the year ended September 30, 1996, up 9.5% from the $4.4 million realized in fiscal 1995. An 8 basis point improvement in the interest rate spread and a more favorable mix of earning assets contributed to the improved level of net interest income. The growth of net interest income was somewhat restrained by the increase in average borrowed funds and the rise in the cost of interest-bearing liabilities. A detailed analysis of net interest income is presented earlier in this report.

Provisions for Credit Losses. Provisions for credit losses for the year ended September 30, 1996 increased $2,000 to $22,000 compared to the provisions recorded in fiscal 1995. The amount of the

provisions reflects management's assessment of loan loss reserves on non-classified loans. At September 30, 1996, the allowance for credit losses was $650,000, representing .60% of loans receivable,net, and 95.03% of non-performing loans. Based upon the quality of the Savings Bank's loan portfolio, the relatively stable local economy, and favorable interest rate environment, management presently believes the Savings Bank's allowance for credit losses is adequate to absorb any anticipated credit losses. Management currently expects future provisions for credit losses to be based primarily upon growth in the loan portfolio and other factors. However, assessment of the adequacy of the allowance for credit loss involves subjective judgments regarding future events and thus there can be no assurance that additional provisions for credit losses will not be required in future periods.

Noninterest Income. For the year ended September 30, 1996, noninterest income amounted to $735,000, up 35.4% from the $543,000 earned in fiscal 1995. Service charges and fees on loans were up $58,000 due to an increase in the number and dollar volume of loan originations. Other customer service fees and commissions reflected a $77,000 rise primarily due to an increase in customer deposit activity. In addition, the Savings Bank realized a gain of $27,000 on the sale of foreclosed property during fiscal 1996 compared to a loss of $4,000 in fiscal 1995.

Noninterest Expense. Noninterest expense totaled $3.4 million for the year ended September 30, 1996 compared to $2.6 million for fiscal 1995. This change was primarily due to the imposition by the FDIC on members of the SAIF of the one-time assessment designed to recapitalize the SAIF. The charge to Bedford Federal was approximately $555,000. Compensation and employee benefits were up $87,000 due primarily to merit increases and higher benefits costs. In addition, occupancy and equipment expense increased $77,000 due primarily to expenses related to the installation and operation of three ATMs.

Income Taxes. The provision for income taxes decreased $107,000 to $754,000 in fiscal 1996 from $861,000 in fiscal 1995 due to the lower level of taxable income.

Liquidity and Capital Resources

Under applicable federal regulations, Bedford Federal is required to maintain specified levels of "liquid investments" in qualifying types of U.S. Government, federal agency and other investments, having maturities of five years or less. Current OTS regulations require that a savings association maintain liquid assets of not less than 5% of its average daily balance of net withdrawable deposit accounts and borrowings payable in one year or less, of which short-term liquid assets must consist of not less than 1%. At September 30, 1996, the Savings Bank's liquidity, as measured for regulatory purposes, was 8.55% which was $3.3 million in excess of the minimum OTS requirement. The Savings Bank adjusts its liquidity as appropriate to meet its asset/liability objectives.

Primary funding sources for the Savings Bank are deposits, amortization and prepayments of loans, FHLB advances, maturities of investment securities and funds provided from operations. While scheduled loan repayments are a relative predictable source of funds, deposit flows and loan prepayments are significantly influenced by general interest rates, economic conditions and competition. In addition, Bedford Federal invests excess funds in overnight deposits which provide liquidity to meet funding requirements.

The Savings Bank's most liquid assets are cash and cash equivalents, which include investments in highly liquid short-term investments. The level of these assets is dependent on the Savings Bank's operating, financing and investing activities during any given period. At September 30, 1996, cash and cash equivalents totaled $3.1 million.

Bedford Federal has other sources of liquidity if the need for funds exceeds the level generated from normal operations. Included in these other sources are additional FHLB advances and the ability to borrow against securities. At September 30, 1996, the Savings Bank had $12.0 million in advances outstanding from the FHLB of Atlanta. At September 30, 1996, the Savings Bank had commitments to fund loans of $1.8 million, $3.2 million of loans in process, and $2.0 million and $362,000 of unfunded home equity lines of credit and commercial credit loans, respectively.

Certificates of deposit scheduled to mature within one year totaled $33.8 million September 30, 1996. Based on historical deposit withdrawals and outflows, and on internal monthly deposit reports monitored by management, management believes that a majority of such maturing deposits will remain in the Savings Bank.

As of September 30, 1996, Bedford Federal exceeded its tangible, core and risk-based capital requirements by 10.9%, 9.4% and 15.1%, respectively. See Note 14 to the Company's Consolidated Financial Statements included in this Annual Report.

Impact of Inflation and Changing Prices

The financial statements and related data in this report have been prepared in accordance with generally accepted accounting principles which require the measurement of financial position and operating results in terms of historical dollars, without consideration for changes in the relative purchasing power of money over time caused by inflation.

Unlike industrial companies, nearly all of the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution's performance than general levels of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the price of goods and services, since such goods and services are affected by inflation. In the current interest rate environment, liquidity and the maturity structure of the Savings Bank's assets and liabilities are critical to the maintenance of acceptable performance levels.

Recent Developments

The Savings Bank's deposits are insured up to the legal maximum by the SAIF as administered by the FDIC. In the past, Bedford Federal and most other SAIF members have paid an annual insurance premium between .23% and .31% of total deposits held. On the other hand, a vast majority of members of the BIF, primarily commercial banks, paid insurance premiums on deposits at or near the legal minimum of $2,000 per year. Recent federal legislation required the FDIC to impose a one-time assessment on all members of SAIF in order to recapitalize the SAIF to the federally mandated level of 1.25%. The assessment equalled .65% of an institution's domestic deposits as of March 31, 1995 and was approximately $555,000 for Bedford Federal. It is anticipated that future SAIF premiums will be lowered which will reduce somewhat the competitive advantage commercial banks have had regarding deposit insurance premiums.

On August 20, 1996, The Small Business Job Protection Act of 1996 was signed into law. Under this law the tax bad debt reserve method that had been available to thrift institutions was repealed for tax years beginning after 1995. Upon repeal, a small thrift (under $500 million in assets) is required to recapture into income the portion of its bad debt reserves that exceeds the greater of (1) the experience method reserve computed as if the thrift had always been a small bank, or (2) the lesser of the base year reserve or the contracted base year reserve. The impact of this change was immaterial on Bedford Federal.

Consolidated Financial Statements
As of September 30, 1996 and 1995 and
For the Years Ended September 30, 1996, 1995 and 1994
Bedford Bancshares, Inc. and Subsidiaries

[BDO SEIDMAN LETTERHEAD]

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Fax: (804) 330-7753

Report of Independent Certified Public Accountants

The Board of Directors and Stockholders
Bedford Bancshares, Inc.
Bedford, Virginia

We have audited the consolidated balance sheet of Bedford Bancshares, Inc. and subsidiaries (the "Company") as of September 30, 1996, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The consolidated financial statements of Bedford Bancshares, Inc. and subsidiaries as of September 30, 1995 and 1994, were audited by other auditors whose report dated October 27, 1995, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 1996 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Bedford Bancshares, Inc. and subsidiaries as of September 30, 1996, and the results of their operations and their cash flows for the year then ended in conformity with generally accepted accounting principles.

As discussed in the Summary of Accounting Policies to the consolidated financial statements, the Company changed its method of accounting for income taxes by adopting Statement of Financial Accounting Standards No. 109, effective October 1, 1993. The Company also changed its method of accounting for debt and equity securities by adopting Statement of Financial Accounting Standards No. 115, effective October 1, 1994.

/s/ BDO Seidman, LLP

October 29, 1996

Bedford Bancshares, Inc. and Subsidiaries

Consolidated Balance Sheets
(in thousands)

September 30,	1996	1995
Assets		
Cash (including interest bearing deposits of approximately $223 and $725)	$ 3,075	$ 3,337
Securities (Notes 1 and 6)	11,435	10,520
Investment in Federal Home Loan Bank stock, at cost (Note 6)	932	932
Loans receivable, net (Notes 2, 6 and 14)	108,873	97,669
Property and equipment, net (Note 4)	1,238	1,313
Accrued interest receivable	662	713
Deferred income taxes (Note 9)	438	214
Refundable income taxes	-	103
Other assets	548	253
	$127,201	$115,054

Bedford Bancshares, Inc. and Subsidiaries

Consolidated Balance Sheets
(in thousands)

September 30,	1996	1995
Liabilities and Stockholders' Equity		
Liabilities		
Deposits (Note 5)	$ 95,378	$ 90,063
Advances from Federal Home Loan Bank (Note 6)	12,000	5,000
Advances from borrowers for taxes and insurance	539	545
Dividends payable	126	186
Other liabilities (Note 8)	931	575
Total liabilities	108,974	96,369
Commitments and contingencies (Notes 11 and 12)		
Stockholders' equity		
Preferred stock, par value $.10, authorized 250,000 shares, none outstanding	-	-
Common stock, par value $.10, authorized 2,750,000 shares, 1,143,669 and 1,204,875 shares, issued and outstanding	114	121
Additional paid-in capital	10,773	11,366
Retained earnings, substantially restricted (Note 10)	8,739	8,263

Unrealized loss on securities available for sale (Note 1)	(33)	(9)
Less stock acquired by ESOP and RRP (Note 11)	(1,366)	(1,056)
Total stockholders' equity	18,227	18,685
	$127,201	$115,054

See accompanying summary of accounting policies and notes to consolidated financial statements.

Bedford Bancshares, Inc. and Subsidiaries

Consolidated Statements of Operations
(in thousands)

Year Ended September 30,	1996	1995	1994
Interest income			
Loans	$8,380	$7,368	$6,337
U.S. government obligations, including agencies	748	708	563
Other investments	136	61	64
Total interest income	9,264	8,137	6,964
Interest expense			
Deposits (Note 5)	4,128	3,562	3,437
Borrowed money	364	216	41
Total interest expense	4,492	3,778	3,478
Net interest income	4,772	4,359	3,486
Provision for loan losses (Note 2)	22	20	51
Net interest income after provision for loan losses	4,750	4,339	3,435
Noninterest income			
Service charges and fees on loans	403	345	362
Other customer service fees and commissions	257	180	169
Gain (loss) on sale of loans, investments and foreclosed real estate	30	(4)	8
Other	45	22	15
Total noninterest income	735	543	554
Noninterest expense			
Compensation and employee benefits	1,467	1,380	1,197
Occupancy and equipment	336	259	254
Data processing	311	302	260
Federal insurance of accounts	207	197	202
Advertising	87	85	73
Professional fees	115	149	84
BIF/SAIF premium disparity assessment (Note 8)	555	-	-
Other	351	248	168

Total noninterest expense	3,429	2,620	2,238

continued...

Bedford Bancshares, Inc. and Subsidiaries

Consolidated Statements of Operations
(in thousands)
(continued)

Year Ended September 30,	1996	1995	1994
Income before income taxes and cumulative effect of change in accounting principle	$2,056	$2,262	$1,751
Provision for income taxes (Note 9)	754	861	629
Net income before cumulative effect of change in accounting principle	1,302	1,401	1,122
Cumulative effect at October 1, 1993, of change in accounting for income taxes	-	-	323
Net income	$1,302	$1,401	$1,445
Primary and fully diluted earnings per common share			
Income before cumulative effect	$1.17	$ 1.20	$ .95
Cumulative effect of change in accounting principle	-	-	.28
Net income	$1.17	$ 1.20	$ 1.23

See accompanying summary of accounting policies and notes to consolidated financial statements.

Bedford Bancshares, Inc. and Subsidiaries

Consolidated Statements of Stockholders' Equity
(in thousands)

<TABLE>
<CAPTION>

	Common Stock	Additional Paid-in Capital	Retained Earnings	Unrealized Gain/(Loss) on Securities	Acquired By ESOP and RRP	Total

<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance, September 30, 1993	$ --	$ --	$ 6,144	$ --	$ --	$ 6,144
Net income	--	--	1,445	--	--	1,445
Change in unrealized loss on marketable equity securities	--	--	--	(70)	--	(70)
Sale of stock (1,256,375 shares)	126	11,814	--	--	(800)	11,140
Balance, September 30, 1994	126	11,814	7,589	(70)	(800)	18,659
Net income	--	--	1,401	--	--	1,401
Cumulative effect of change in accounting principle	--	--	--	35	--	35
Change in unrealized loss on securities available for sale (Note 1)	--	--	--	26	--	26
Allocated/earned ESOP shares (Note 10)	--	62	--	--	93	155
Purchase of RRP shares (Note 10)	--	--	--	--	(349)	(349)
Repurchase of stock (51,500 shares)	(5)	(510)	(370)	--	--	(885)
Dividends declared ($.30 per share)	--	--	(357)	--	--	(357)

</TABLE>

continued...

Bedford Bancshares, Inc. and Subsidiaries

Consolidated Statements of Stockholders' Equity
(in thousands)
(continued)

<TABLE>
<CAPTION>

	Common Stock	Additional Paid-in Capital	Retained Earnings	Unrealized Gain/(Loss) on Securities	Acquired By ESOP and RRP	Total
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Balance, September 30, 1995	$121	$ 11,366	$ 8,263	$ (9)	$(1,056)	$18,685
Net income	--	--	1,302	--	--	1,302
Change in unrealized loss on securities available for sale (Note 1)	--	--	--	(24)	--	(24)
Allocated/earned ESOP shares (Note 11)	--	55	88	--	26	169
Purchase of RRP shares (Note 11)	--	--	--	--	(483)	(483)
Repurchase of stock (65,390 shares)	(7)	(647)	(461)	--	--	(1,115)
Dividends declared ($.39 per share)	--	--	(457)	--	--	(457)
Exercise of options (Note 11)	--	41	4	--	--	45
RRP vesting (Note 11)	--	(42)	--	--	147	105

Balance, September 30, 1996	$114	$ 10,773	$ 8,739	$ (33)	$(1,366)	$18,227

</TABLE>

See accompanying summary of accounting policies and notes to consolidated financial statements.

Bedford Bancshares, Inc. and Subsidiaries

Consolidated Statements of Cash Flows
(in thousands)

<TABLE>
<CAPTION>

Year Ended September 30,	1996	1995	1994
Operating activities			
<S>	<C>	<C>	<C>
Net income	$ 1,302	$ 1,401	$ 1,445
Adjustments to reconcile net income to net cash provided by operating activities			
Cumulative effect of change in accounting for income taxes	--	--	(323)
Provision for loan losses	22	20	51
Provision for depreciation and amortization	163	120	97
(Increase) decrease in deferred income taxes	(121)	116	67
(Gain) loss on sale of loans and securities	(2)	4	(8)
(Gain) loss on sale of foreclosed real estate	(28)	--	(4)
Loans originated for sale	(152)	(184)	(301)
Proceeds from sale of loans originated for sale	153	188	309
(Increase) decrease in interest receivable	51	(128)	(50)
(Increase) decrease in other assets	(295)	(84)	46
Increase (decrease) in other liabilities	356	331	92
Net cash provided by operating activities	1,449	1,784	1,421
Investing activities			
Proceeds from maturities of investments	2,200	1,200	1,700
Proceeds from sales of investments	872	394	--
Principal collected on mortgage-backed securities	26	7	10
Purchases of investment securities	(4,035)	(1,955)	(3,579)
Net increase in loans to customers	(11,311)	(8,380)	(8,365)
Net proceeds from sales of foreclosed real estate	113	--	113
Purchases of foreclosed real estate	--	--	(78)
Purchases of premises, equipment and leasehold improvements	(88)	(298)	(69)
Net cash absorbed by investing activities	(12,223)	(9,032)	(10,268)

</TABLE>

continued...

Consolidated Statements of Cash Flows
(in thousands)
(continued)

<TABLE>
<CAPTION>

Year Ended September 30,	1996	1995	1994
Financing activities			
<S>	<C>	<C>	<C>
Net increase (decrease) in customer deposits	$ 5,315	$ 5,222	$ (4,346)
Net increase (decrease) in advance payments from borrowers	(6)	72	23
Proceeds from advances and other borrowed money	11,000	5,000	--
Principal payments of advances	(4,000)	(1,000)	--
Proceeds from sale of stock	--	--	11,940
Purchase of stock by ESOP and RRP	(483)	(349)	(800)
Allocation of ESOP and RRP shares	274	155	--
Repurchase of stock	(1,115)	(885)	--
Dividends paid	(518)	(183)	--
Issuance of common stock	45	--	--
Net cash provided by financing activities	10,512	8,032	6,817
Increase (decrease) in cash and cash equivalents	(262)	784	(2,030)
Cash and cash equivalents - beginning of year	3,337	2,553	4,583
Cash and cash equivalents - end of year	$ 3,075	$ 3,337	$ 2,553
Supplemental Disclosures of Cash Flow Information			
Cash payments of interest expense	$ 4,503	$ 3,777	$ 3,480
Cash payments of income taxes	$ 817	$ 718	$ 616

</TABLE>

See accompanying summary of accounting policies and notes to consolidated financial statements.

Summary of Accounting Policies

Nature of Business and Regulatory Environment

Bedford Bancshares, Inc. (the "Parent Company") is a unitary thrift holding company whose principal asset is its wholly-owned subsidiary, Bedford Federal Savings Bank (the "Savings Bank"). The Savings Bank is a federally chartered stock savings bank that provides a full range of banking services to individual and corporate customers. In these financial statements the consolidated group is referred to collectively as "the Company".

The Office of Thrift Supervision ("OTS") is the primary regulator for federally chartered savings associations, as well as savings and loan holding companies.

The Federal Deposit Insurance Corporation ("FDIC") is the federal deposit insurance administrator for both banks and savings associations. The FDIC has specified authority to prescribe and enforce such regulations and issue such orders as it deems necessary to prevent actions or practices by savings associations that pose a serious threat to the Savings Association Insurance Fund ("SAIF").

Principles of Consolidation

The consolidated financial statements include the accounts of Bedford Bancshares, Inc. and Bedford Federal Savings Bank, its wholly-owned subsidiary, and First Financial Enterprises, Inc., the wholly-owned subsidiary of the Savings Bank. All material intercompany accounts and transactions have been eliminated in the consolidation. Prior year accounts are reclassified when necessary to conform to current year classifications.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Investment Securities

The Company adopted Statement of Financial Accounting Standards No. 115 (SFAS 115), "Accounting for Certain Investments in Debt and Equity Securities", as of October 1, 1994. This statement requires certain securities to be classified as "held to maturity", "trading" or "available for sale", according to management's intent and ability.

Debt securities for which the Bank has the positive intent and ability to hold to maturity are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period to maturity.

Investment Securities (continued)

Trading securities, if any, are carried at fair value. Realized gains and losses on sales and unrealized changes in fair values are included in noninterest income.

Investments classified as "available for sale" are carried at fair value with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity. Realized gains and losses on these sales are included in noninterest income and are computed under the specific identification method.

Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate. Net unrealized losses are recognized through a valuation allowance by charges to income.

Loans Receivable

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding principal balance adjusted for any charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans.

Loans receivable consists primarily of long-term real estate loans secured by first deeds of trust on single family residences, other residential property, commercial property and land located primarily in the state of Virginia. Interest income on mortgage loans is recorded when earned and is recognized based on the level yield method. The Company provides an allowance for accrued interest deemed to be uncollectible, which is netted against accrued interest receivable in the consolidated balance sheets.

The Company defers loan origination and commitment fees, net of certain direct loan origination costs, and the net deferred fees are amortized into interest income over the lives of the related loans as yield adjustments. Any unamortized net fees on loans fully repaid or sold are recognized as income in the year of repayment or sale.

The Company places loans on nonaccrual status after being delinquent greater than 90 days or earlier if the Company becomes aware that the borrower has entered bankruptcy proceedings, or in situations in which the loans have developed inherent problems prior to being 90 days delinquent that indicate payments of principal or interest will not be made in full. Whenever the accrual of interest is stopped, previously accrued but uncollected interest income is reversed. Thereafter, interest is recognized only as cash is received until the loan is reinstated.

Loans Receivable (continued)

The allowance for loan losses is maintained at a level considered by management to be adequate to absorb future loan losses currently inherent in the loan portfolio. Management's assessment of the adequacy of the allowance is based upon type and volume of the loan portfolio, past loan loss experience, existing and anticipated economic conditions, and other factors which deserve current recognition in estimating future loan losses. Additions to the allowance are charged to operations. Loans are charged-off partially or wholly at the time management determines collectibility is not probable. Management's assessment of the adequacy of the allowance is subject to evaluation and adjustment by the Company's regulators.

Effective October 1, 1995, the Company adopted Statement of Financial Accounting Standards No. 114 (SFAS 114), "Accounting by Creditors for Impairment of a Loan" (as amended by SFAS No. 118, "Accounting by Creditors for Impairment of a Loan-Income Recognition and Disclosures"). The effect of adopting these new accounting standards was immaterial to the operating results of the Company for the year ended September 30, 1996.

Under the new accounting standard, a loan is considered to be impaired when it is probable that the Company will be unable to collect all principal and interest amounts according to the contractual terms of the loan agreement. The allowance for loan losses related to loans identified as impaired is primarily based on the excess of the loan's current outstanding principal balance over the estimated fair market value of the related collateral. For a loan that is not collateral-dependent, the allowance is recorded at the amount by which the outstanding principal balance exceeds the current best estimate of the future cash flows on the loan discounted at the loan's original effective interest rate. Prior to October 1, 1995, the allowance for loan losses for all loans which would have qualified as impaired under the new accounting standards was primarily based upon the estimated fair market value of the related collateral.

For impaired loans that are on nonaccrual status, cash payments received are generally applied to reduce the outstanding principal balance. However, all or a portion of a cash payment received on a nonaccrual loan may be recognized as interest income to the extent allowed by the loan contract, assuming management expects to fully collect the remaining principal balance on the loan.

As of September 30, 1996, the Company had no loans that were considered as impaired.

Real Estate Owned

Real estate acquired through foreclosure is initially recorded at the lower of fair value, less estimated selling costs, or the balance of the loan on the property at date of foreclosure. Costs relating to the development and improvement of property are capitalized, whereas those relating to holding the property are charged to expense.

Real Estate Owned (continued)

Valuations are periodically performed by management, and an allowance for losses is established by a charge to operations if the carrying value of a property exceeds its estimated fair value.

Sale of Loans, Participations in Loans

The Company is able to generate funds by selling loans and participations in loans to the Federal Home Loan Mortgage Corporation and other investors. Under participation service agreements, the Company continues to service the loans and the participant is paid its share of principal and interest collections.

Gain or loss on loan participations is recognized at the time of the sale. The gain or loss recorded is equal to the present value of the estimated future interest receipts, net of allowance for estimated servicing costs and a normal servicing profit on the portion sold less the present value of interest payments to be remitted to the buyers. The resulting deferred premium or discount is amortized or accreted to income using the level yield method. Loan servicing income is recorded when earned. Loan servicing costs are charged to expense as incurred.

Property, Equipment and Depreciation

The various classes of property are stated at cost and are depreciated by accelerated and straight-line methods over their estimated useful lives of 30 to 40 years for office buildings, 15 to 20 years for land improvements, 15 years for ATM facilities, 5 to 10 years for furniture and equipment and 5 years for automobiles. Additions and improvements are capitalized, while repairs are expensed as incurred. The cost and accumulated depreciation on property are eliminated from the accounts upon disposal, and any resulting gain or loss is included in the determination of net income.

Income Taxes

During the year ended September 30, 1994, the Company adopted Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes", which required a change from the deferred method to the asset and liabilities method of accounting for income taxes.

Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

Income Taxes (continued)

In computing Federal income taxes, savings banks that meet certain definitional tests and other conditions prescribed by the Internal Revenue Code are allowed, within limitations, to deduct from taxable income an allowance for bad debts based on actual loss experience, a percentage of taxable income (8%) before such deduction or an amount based on a percentage of eligible loans. The cumulative bad debt reserve, upon which no taxes have been paid, was approximately $212,000 as of September 30, 1996.

As a result of 1996 tax legislation, the Company will compute its tax bad debt deduction by use of the "experience method", which is based on a moving five-year average of actual charge-offs, for tax years beginning with fiscal year 1997. According to the legislation, "applicable excess reserves" must be recaptured as taxable income over five years beginning with fiscal year 1997. The amount to be recaptured is the excess of the accumulated reserves since fiscal year 1987 over the amount allowed by use of the experience method for those years. Management does not believe that the legislation will have a material effect on the Company's financial statements.

The Company has reported the cumulative effect of change in the method of accounting for income taxes as of the beginning of the 1994 fiscal year in the consolidated statement of operations.

Accounting Pronouncements

In March 1995, the Financial Accounting Standards Board issued its Statement of Financial Accounting Standards No. 121 (SFAS 121), "Accounting for the Impairment of Long-Lived Assets and For Long-Lived Assets to Be Disposed Of". SFAS 121 requires that long-lived assets and certain intangibles to be held and used by an entity be reviewed for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. In addition, SFAS 121 requires long-lived assets and certain intangibles to be disposed of to be reported at the lower of carrying amount or fair value less costs to sell. SFAS 121 is effective for fiscal years beginning after December 15, 1995. Management does not expect the application of this pronouncement to have a material effect on the Company's financial statements.

In May 1995, the Financial Accounting Standards Board issued its Statement of Financial Accounting Standards No. 122 (SFAS 122), "Accounting for Mortgage Servicing Rights an Amendment of FASB Statement No. 65". SFAS 122 requires entities to allocate the cost of acquiring or originating mortgage loans between the mortgage servicing rights and the loans, based on their relative fair values, if the bank sells or securitizes the loans and retains the mortgage servicing rights. In addition, SFAS 122 requires entities to assess its capitalized mortgage servicing rights for impairment based on the fair value of those rights. SFAS 122 is effective for fiscal years beginning after December 15, 1995. Management does not expect the application of this pronouncement to have a material effect on the Company's financial statements.

Accounting Pronouncements (continued)

In October 1995, the FASB issued SFAS No. 123 "Accounting for Stock-Based Compensation." SFAS No. 123 allows companies to continue to account for their stock option plans in accordance with APB Opinion 25 but encourages the adoption of a new accounting method based on the estimated fair value of employee stock options. Companies electing not to follow the new fair value based method are required to provide expanded footnote disclosures, including pro forma net income and earnings per share, determined as if the company had applied the new method. SFAS No. 123 is required to be adopted by the Company prospectively beginning October 1, 1996. Management does not expect the application of this pronouncement to have a material effect on the Company's financial statements.

In June 1996, the Financial Accounting Standards Board issued its Statement of Financial Accounting Standards No. 125 (SFAS 125), "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". This Statement provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities. After a transfer of financial assets, an entity recognizes the financial and servicing assets it controls and the liabilities it has incurred, derecognizes financial assets when control has been surrendered, and derecognizes liabilities when extinguished. In addition, a transfer of financial assets in which the transferor surrenders control over those assets is accounted for as a sale to the extent that consideration other than beneficial interests in the transferred assets is received in exchange. SFAS 125 is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after December 31, 1996, and is to be applied prospectively. Management does not expect the application of this pronouncement to have a material effect on the financial statements of the Company.

Earnings Per Share

Earnings per share of Common Stock for the years ended September 30, 1996 and 1995 have been determined by dividing the net income for the twelve month period by the calculated weighted average number of shares of Common Stock and common stock equivalents. The September 30, 1994 calculation was computed as if the conversion from mutual ownership to stock ownership had occurred on the first day of the fiscal year rather than on August 19, 1994. Shares acquired by the employee stock benefit plans are accounted for in accordance with AICPA Statement of Position 93-6 and are not considered in the weighted average shares outstanding until the shares have been earned by the employees and/or committed to be released. The weighted average number of shares of Common Stock outstanding for the years ending September 30, 1996, 1995 and 1994, including common stock equivalents, were 1,112,697, 1,165,381 and 1,176,375, respectively.

Statement of Cash Flows

For purposes of the statements of cash flows the Company considers all highly liquid debt instruments with maturities, when purchased, of three months or less, to be cash equivalents. Cash and cash equivalents include cash on hand, funds due from banks, and federal funds sold.

Conversion to Stock Ownership

At a special meeting on August 2, 1994, the members of the Savings Bank approved management's plan to convert the Savings Bank from a Federal Mutual to a Federal Stock Savings Bank. The plan called for the formation of Bedford Bancshares, Inc. which would own the stock of the Savings Bank upon its conversion to a stock form of ownership. The stock of the Parent Company would then be offered through a Subscription and Community Offering to the Savings Bank's tax-qualified employee stock plans, eligible account holders and others. The transaction was accounted for as a pooling of interests.

On August 19, 1994, the Parent Company issued 1,256,375 shares of $.10 par value Common Stock at $10 per share and became the parent company of the Savings Bank. Net proceeds, after deducting conversion expenses and underwriters' discounts of $624,000, were $11,940,000 and are reflected as Common Stock and additional paid-in capital in the accompanying consolidated financial statements.

1. Investment Securities

A summary of the amortized cost and estimated market values of investment securities, in thousands, is as follows:

<TABLE>
<CAPTION>

September 30, 1996

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Held to Maturity				
United States government and agency obligations	$5,214	$24	$ 77	$ 5,161
Mortgage-backed securities	25	-	-	25
	5,239	24	77	5,186
Available for Sale				
United States government and agency obligations	1,900	8	48	1,860
Mortgage-backed securities	490	-	33	457
Marketable Equity securities	3,909	-	30	3,879
	6,299	8	111	6,196
	$11,538	$32	$188	$11,382

</TABLE>

1. Investment Securities (continued)

<TABLE>
<CAPTION>

September 30, 1995

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Held to Maturity				
United States government and agency obligations	$ 5,420	$64	$107	$ 5,377
Mortgage-backed securities	31	-	-	31
	5,451	64	107	5,408
Available for Sale				
United States government and agency obligations	1,400	9	-	1,409
Marketable equity securities	3,684	-	24	3,660
	5,084	9	24	5,069
	$10,535	$73	$131	$10,477

</TABLE>

Proceeds from the sale of securities available for sale during the years ended September 30, 1996 and 1995 were $802,000 and $394,000, respectively. A gain of $2,000 was realized on the 1996 sale while a loss of $8,000 was realized on the 1995 sale.

1. Securities (continued)

The amortized cost and estimated market value of debt securities, in thousands, at September 30, 1996, by contractual maturity, were as follows:

<TABLE>
<CAPTION>

September 30, 1996

	Amortized Cost	Estimated Market Value

Held to Maturity

Due in one year or less	$ -	$ -
Due in one through five years	3,481	3,407
Due after five years	1,733	1,754
	5,214	5,161
Mortgage-backed securities	25	25
	5,239	5,186
Available for Sale		
Due in one year or less	-	-
Due in one through five years	1,400	1,391
Due after five years	500	469
	1,900	1,860
Mortgage-backed securities	490	457
	2,390	2,317
	$7,629	$7,503

Expected maturities can differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

2. Loans Receivable

Loans receivable, in thousands, are summarized as follows:

September 30,	1996	1995
First mortgage loans	$ 91,386	$ 83,532
Construction loans	10,121	9,732
Home equity loans	2,636	1,800
Loans to depositors, secured by savings	551	799
Installment loans	5,169	4,183
Term notes	3,158	1,653

	113,021	101,699
Less		
Undisbursed loans in process	3,199	2,994
Unearned discount resulting from add-on interest	15	60
Deferred loan fees and costs, net	284	336
Allowance for credit losses	650	640
	$108,873	$ 97,669

</TABLE>

Activity in the allowance for credit losses, in thousands, is summarized as follows:

<TABLE>
<CAPTION>

Year Ended September 30,	1996	1995	1994
<S>	<C>	<C>	<C>
Balance at beginning of year	$640	$636	$595
Provision charged to operations	22	20	51
Charge offs net of recoveries	(12)	(16)	(10)
Balance at end of year	$650	$640	$636

</TABLE>

3. Loan Servicing

Mortgage loans serviced for others are not included in the accompanying statements of financial condition. The unpaid principal balances of those loans, in thousands, are summarized as follows:

<TABLE>
<CAPTION>

Year Ended September 30,	1996	1995	1994
<S>	<C>	<C>	<C>
Federal Home Loan Mortgage Corporation (FHLMC)	$1,472	$1,511	$1,387
Virginia Housing Development Authority (VHDA)	1,245	1,197	1,016
	$2,717	$2,708	$2,403

</TABLE>

Custodial escrow balances maintained in connection with the foregoing loan servicing at September 30, 1996, 1995 and 1994 were approximately $18,000, $24,000 and $17,000, respectively.

4. Property and Equipment

Property and equipment, in thousands, are summarized as follows:

September 30,	1996	1995
Land	$ 251	$ 251
Office buildings	1,190	1,161
Rental buildings	48	48
Furniture, fixtures and equipment	755	841
Automobile	16	16
Leasehold improvements	23	25
	2,283	2,342
Less accumulated depreciation	1,045	1,029
	$1,238	$1,313

5. Deposits

Deposits, in thousands, are summarized as follows:

<TABLE>
<CAPTION>

September 30,	1996		1995	
	Amount	Percent	Amount	Percent
<S>	<C>	<C>	<C>	<C>
NOW accounts	$13,057	13.69%	$10,967	12.18%
Money market accounts	4,579	4.80	5,630	6.25
Savings accounts	15,290	16.03	15,728	17.46
Time deposits	62,452	65.48	57,738	64.11
	$95,378	100.00%	$90,063	100.00%

</TABLE>

The aggregate amount of certificates of deposit of $100,000 or more was approximately $6,978,000 and $4,563,000 at September 30, 1996 and 1995, respectively.

At September 30, 1996, the scheduled maturities of time deposits, in thousands, are as follows:

Year ending September 30,	
1997	$33,827
1998	21,669
1999	4,399
2000	1,944
2001 and thereafter	613
	$62,452

Interest expense on deposits, in thousands, is summarized as follows:

September 30,	1996	1995	1994
NOW accounts	$ 197	$ 185	$ 166
Money market account	160	182	177
Savings account	458	517	635
Time deposits	3,313	2,678	2,459
	$4,128	$3,562	$3,437

6. Advances from Federal Home Loan Bank

Borrowings ("advances") from the Federal Home Loan Bank ("FHLB"), in thousands, are scheduled to mature as follows:

September 30,	1996	1995
Within one year	$12,000	$4,000
One to two years	-	1,000
	$12,000	$5,000

The weighted average interest rate on advances at September 30, 1996 and 1995 was 5.77% and $6.40%, respectively. These advances are collateralized by the Company's investment in FHLB stock and qualifying real estate loans under a blanket collateral agreement.

7. Fair value of Financial Instruments

The estimated fair values of the Company's financial instruments, in thousands, as of September 30, 1996, are as follows:

	Carrying Amount	Fair Value
Financial assets		
Cash and short-term investments	$ 3,075	$ 3,075

Securities	11,435	11,382
Loans, net of allowance for loan losses	108,873	109,601
Financial liabilities		
Deposits	95,378	95,388
Advances from Federal Home Loan Bank	12,000	12,000

	Notional Amount	Fair Value
Unrecognized financial instruments		
Commitments to extend credit	$4,187	$4,187

---

7. Fair Value of Financial Instruments (continued)

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value.

Cash and short-term investments

For those short-term investments, the carrying amount is a reasonable estimate of fair value.

Securities

Fair values are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loan receivables

The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar remaining maturities. This calculation ignores loan fees and certain factors affecting the interest rates charged on various loans such as the borrower's creditworthiness and compensating balances and dissimilar types of real estate held as collateral.

Deposit liabilities

The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the balance sheet date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities.

Advances from Federal Home Loan Bank

For advances that mature within one year of the balance sheet date, carrying value is considered a reasonable estimate of fair value.

The fair values of all other advances are estimated using discounted cash flow analysis based on the Company's current incremental borrowing rate for similar types of advances.

Commitments to extend credit

The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the borrowers. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. Because of the competitive nature of the marketplace loan fees vary greatly with no fees charged in many cases.

8. BIF/SAIF Premium Disparity Assessment

Pursuant to the Economic Growth and Paperwork Reduction Act of 1996 (the "Act"), the FDIC imposed a special assessment on SAIF members to capitalize the SAIF at the designated reserve level of 1.25% as of September 30, 1996. Based on the Company's deposits as of March 31, 1995, the date for measuring the amount of the special assessment pursuant to the Act, the Company will pay of special assessment of $555,000 on November 27, 1996 to capitalize the SAIF. The FDIC is expected to lower the premium for deposit insurance to a level necessary to maintain the SAIF at its required reserve level; however, the range of premiums has not been determined.

9. Income Taxes

The provision for income taxes, in thousands, is summarized as follows:

Year Ended September 30,	1996	1995	1994
Current			
Federal	$816	$656	$495
State	97	89	67
	913	745	562
Deferred tax expense (benefit)	(159)	116	67
Total provision for income taxes	$754	$861	$629

Differences between the statutory and effective tax rates are summarized as follows:

	Percent of Pretax Income		
Year Ended September 30,	1996	1995	1994
Tax at statutory rate	34.0%	34.0%	34.0%
Increases (decreases) in taxes resulting from:			
State income taxes, net of federal benefit	3.6	2.6	2.5
Other	(.9)	1.5	(.6)
	36.7%	38.1%	35.9%

9. Income Taxes (continued)

The components of the net deferred tax asset, in thousands, were as follows:

September 30,	1996	1995
Deferred tax asset		
Bad debts	$ 81	$141
Loan fees	66	117
Pension expense	-	15
Unrealized loss on securities, available for sale	61	5
BIF/SAIF assessment	211	-
Other	21	-
Total deferred tax asset	440	278
Deferred tax liability		
Accelerated depreciation	(2)	(64)
Net deferred tax asset	$438	$214

10. Restricted Retained Earnings

In accordance with the current regulations concerning conversion from a mutual to a stock organization, the Savings Bank was required to establish a liquidation account equal to its net worth as of the latest balance sheet contained in the final offering circular. Such liquidation account is to be maintained for the benefit of depositors, as of the eligibility record date (September 30, 1993) who continue to maintain their deposits in the Savings Bank after the conversion, in the event of a complete liquidation of the Savings Bank. If, however, on any annual closing date of the Savings Bank subsequent to September 30, 1993, the amount in any deposit account is less than the amount in such deposit account on September 30, 1993, then the interest in the liquidation account relating to such deposit account would be reduced by the amount of such reduction, and such interest will cease to exist if such deposit account is closed. The Savings Bank may not declare or pay a cash dividend or repurchase any of its capital stock if the effect thereof would cause the net worth of the Savings Bank to be reduced below either the amount required for the liquidation account or the minimum regulatory capital requirements. At September 30, 1996, the liquidation account, unadjusted for customer withdrawals, totaled $6,144,000.

11. Retirement Plans and Employee Benefit Programs

The Savings Bank has a retirement plan under Internal Revenue Code Section 401(k) covering all full-time employees who have completed one or more years of continuous service and have reached age 21. Each employee has an option to voluntarily contribute to this plan up to 10% of their salary and the Savings Bank will match $.50 for every $1 up to 4% of salary. During fiscal 1993, the plan also provided for the Savings Bank to pay into the plan an amount equal to 10% of each employee's salary, subject to Department of Labor and income tax limitations. Effective October 1, 1993, this 10% contribution was eliminated and a new money purchase plan was adopted which provides for a fixed percentage contribution for each employee's salary. This percentage was 5%, 5% and 10% for the years ended September 30, 1996, 1995 and 1994, respectively. The total expense for the plan was $54,000, $59,000 and $118,000 for the years ended September 30, 1996, 1995 and 1994, respectively.

Employee Stock Ownership Plan

At the time of the stock conversion, the Savings Bank established an Employee Stock Ownership Plan (ESOP) covering all full-time employees, over the age of 21, with at least one year of service. The ESOP borrowed funds from the Parent Company to purchase a total of 80,000 shares of the Parent Company's Common Stock, the loan being collateralized by the Common Stock. Contributions by the Savings Bank, along with dividends received on unallocated shares, are used to repay the loan with shares being released from the Parent Company's lien proportional to the loan repayments. Annually on September 30, the released shares are allocated to the participants in the same proportion that their wages bear to the total compensation of all of the participants. The Company has released and allocated 17,333 and 9,333 shares of Common Stock as of September 30, 1996 and 1995, respectively. The Company recognized $135,000 and $146,000 of compensation cost for the years ended September 30, 1996 and 1995. The fair value of unearned ESOP shares totaled $1,042,000 at September 30, 1996. There were no commitments to repurchase ESOP shares.

Shares pledged as collateral are reported as a reduction of stockholders' equity in the consolidated balance sheets. As shares are released from collateral, the Company reports compensation expense equal to the current market price of the shares, and the shares become outstanding for earnings per share computations. Dividends on allocated ESOP shares are recorded as a reduction of retained earnings, and dividends on unallocated ESOP shares are recorded as a reduction of debt.

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11. Retirement Plans and Employee Benefit Programs (continued)

Recognition and Retention Plan

The Board of Directors approved the establishment of a Recognition and Retention Plan ("RRP") on January 25, 1995. The plan states that the Trust, established under the plan, shall not purchase more than 4% of the aggregate shares of Common Stock issued by the Parent Company in the mutual-to-stock conversion of the Savings Bank (50,255 shares). During 1996 and 1995, the Company purchased 27,650 and 22,600 shares, respectively, of the Company's Common Stock at an average price of $17.50 and $15.50 per share, respectively, to be awarded to directors, officers and employees in accordance with the provisions of the RRP. The costs of the shares awarded under these plans are recorded as unearned compensation, a contra equity account, and are recognized as an expense in accordance with the vesting requirements under the various plans. For the years ended September 30, 1996 and 1995, the amount included in compensation expense was $72,000 and $122,000, respectively. The status of the shares in this plan is summarized as follows:

	Per Share Price	Unawarded Shares	Awarded Shares
Total established by plan	$ -	50,255	-
Granted	11.00	(41,058)	41,058
Vested	-	-	-

Balance at September 30, 1995	11.00	9,197	41,058
Granted	16.75	(2,600)	2,600
Vested	11.00 - 16.75	-	(11,277)
Balance at September 30, 1996	$11.00 - 16.75	6,597	32,381

11. Retirement Plans and Employee Benefit Programs (continued)

Stock Option Plans

The Company established two stock option plans during 1995, as part of the stock conversion, for directors, officers and employees. The exercise price under both plans is the fair market price on the date of the grant. One is a non-incentive stock option plan and the other is an incentive stock option plan. Rights to exercise options granted vest at the rate of 20% per year, beginning on the first anniversary of the grant. A summary of the stock option activity is as follows:

<TABLE>
<CAPTION>

	Option Price	Available for Grant	Options Outstanding	Vested and Exercisable
<S>	<C>	<C>	<C>	<C>
At inception	$ -	125,637	-	-
Granted	11.00	(102,640)	102,640	-
Vested	-	-	-	-
Balance at September 30, 1995	$ 11.00	22,997	102,640	-
Granted	$ 16.75	(6,250)	6,250	-
Vested	11.00 - 16.75	-	(28,185)	28,185
Exercised	11.00	-	-	(4,187)
Balance at September 30, 1996	$11.00 - 16.75	16,747	80,705	23,998

</TABLE>

12. Commitments and Contingencies

The Savings Bank is lessee under a five-year operating lease expiring August 18, 2001 for the land at its Moneta branch at an annual rental of $4,800 for five years. The Savings Bank also leases ATM space in Moneta, under a five year lease expiring in August 18, 2001 at an annual rental of $2,400.

Bedford Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements
(continued)

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12. Commitments and Contingencies (continued)

The current minimum annual rental commitments under non-cancelable operating leases in effect at September 30, 1996 are as follows:

Year Ending September 30,	Amount
1997	$7,200
1998	7,200
1999	7,200
2000	7,200
Thereafter	6,600
	$35,400

Rent expense was approximately $6,100, $4,400 and $3,600 for the years ended September 30, 1996, 1995 and 1994, respectively.

The Savings Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments consist of commitments to extend credit. These instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the statements of financial position. The contract or notional amounts of those instruments reflect the extent of involvement the Savings Bank has in a particular class of financial instruments.

The Savings Bank's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit is represented by the contractual notional amount (in thousands) of those instruments at September 30, 1996 and 1995. The Savings Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

<TABLE>
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September 30,	1996	1995
Financial instruments, in thousands, whose contract amounts represent credit risk		
<S>	<C>	<C>
Unfunded commercial credit line	$ 362	$ 274
Unfunded home equity lines of credit	2,027	1,443
Commitments to finance real estate acquisitions and construction	1,798	1,704
	$4,187	$3,421

</TABLE>

---

12. Commitments and Contingencies (continued)

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to be drawn upon, the total commitment amounts generally represent future cash requirements. The Savings Bank evaluates each customer's credit-worthiness on a case-by-case basis. The amount of collateral, if deemed necessary by the Savings Bank upon extension of credit, is based on management's credit evaluation of the credit applicant. Collateral normally consists of real property.

13. Concentrations of Credit Risk

The Savings Bank grants residential, commercial, and installment loans to customers in the Central Southwest region of Virginia, principally Bedford County. The Savings Bank has a loan portfolio consisting principally of residential mortgage loans, and is not dependent upon any particular economic sector, although the portfolio as a whole may be affected by general economic factors in its lending area.

14. Related Party Transactions

The Company has made loans in the ordinary course of business to various officers and directors generally collateralized by the individual's personal residences or by savings accounts in the Savings Bank. The aggregate balances of such loans which exceed $60,000 in aggregate outstanding amount to any executive officer or director, in thousands, is summarized as follows:

Year Ended September 30,	1996	1995	1994
Beginning balance	$457	$410	$395
Additions	205	127	128
Repayments	(21)	(80)	(113)
Ending balance	$641	$457	$410

---

15. Regulatory Capital of the Savings Bank

The Office of Thrift Supervision's capital regulations require thrift institutions to maintain capital at least sufficient to meet three requirements: tangible capital, core capital, and risk-based capital. Management has determined that the Savings Bank's capital meets and exceeds all three capital requirements (in thousands) as follows as of September 30, 1996 and 1995, in thousands. Tangible and core capital levels are shown as a percentage of adjusted total assets, and risk-based capital levels are shown as a percentage of risk-weighted assets.

<TABLE>
<CAPTION>

	September 30, 1996			
	GAAP	Tangible	Core	Risk-Based

	Capital	Capital		Capital		Capital	
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
GAAP capital before adjustments	$15,815						
Adjustments							
Other	29						
GAAP capital as adjusted	$ 15,844	$ 15,844		$ 15,844		$ 15,844	
General credit loss allowance		--		--		650	
Land loans greater than 80%		--		--		(77)	
Regulatory capital computed		15,844	12.4%	15,844	12.4%	16,417	23.1%
Minimum capital requirement		1,918	1.5	3,835	3.0	5,677	8.0
Regulatory capital excess		$ 13,926	10.9	$ 12,009	9.4%	$ 10,740	15.1%

</TABLE>

<TABLE>
<CAPTION>

	September 30, 1995						
	GAAP Capital	Tangible Capital		Core Capital		Risk-Based Capital	
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
GAAP capital before adjustments	$13,648						
Adjustments							
Unpaid ESOP debt and unrealized securities loss	1,065						
GAAP capital as adjusted	$14,713	$14,713		$14,713		$14,713	
General credit loss allowance		-		-		640	
Land loans greater than 80%		-		-		(687)	
Regulatory capital computed		14,713	12.8%	14,713	12.8%	14,666	23.7%
Minimum capital requirement		1,729	1.5	3,458	3.0	4,942	8.0
Regulatory capital excess		$12,984	11.3%	$11,255	9.8%	$ 9,724	15.7%

</TABLE>

16. Condensed Parent Company Information

Condensed financial information is shown for the Parent Company as follows:

Balance Sheets
(in thousands)

Year Ended September 30,	1996	1995
Assets		
Cash and cash equivalents	$ 149	$ 526

Securities	42	48
Investment in Savings Bank subsidiary	15,855	13,648
Loan to Savings Bank ESOP	627	707
Loan to Savings Bank subsidiary	3,000	4,000
Other assets	83	80
Total assets	$19,756	$ 19,009
Liabilities and stockholders' equity		
Accounts payable	$ 8	$ 138
Dividends payable	126	186
Stockholders' equity	19,622	18,685
Total liabilities and stockholders' equity	$19,756	$ 19,009

16. Condensed Parent Company Information (continued)

Condensed Statements of Operations
(in thousands)

<TABLE>
<CAPTION>

Year Ended September 30,	1996	1995	1994
Income			
<S>	<C>	<C>	<C>
Interest from			
Savings Bank's ESOP loan	$ 44	$ 51	$ 8
Loan to Savings Bank subsidiary	292	416	23
Other	23	--	--
Total income	359	467	31
Expenses			
Professional fees	44	66	--
Other operating expenses	40	33	--
Total expenses	84	99	--
Net income before income taxes and equity in undistributed net income of Savings Bank subsidiary	275	368	31
Provision for income taxes	104	140	13
Equity in undistributed net income of Savings Bank subsidiary	1,131	1,173	1,427
Net income	$1,302	$1,401	$1,445

</TABLE>

Bedford Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements
(continued)

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16. Condensed Parent Company Information (continued)

Condensed Statements of Cash Flows
(in thousands)

<TABLE>
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Year Ended September 30,	1996	1995	1994
Operating activities			
<S>	<C>	<C>	<C>
Net income	$ 1,302	$ 1,401	$ 1,445
Adjustments			
Equity in undistributed net income of Savings Bank subsidiary	(1,131)	(1,173)	(1,427)
(Increase) decrease in other assets	(3)	37	(41)
Increase (decrease) in other liabilities	(130)	102	35
Net cash provided by operating activities	38	367	12
Investing activities			
Loans originated, net of principal repayments	1,080	1,093	(5,000)
Purchase of Savings Bank subsidiary stock	--	--	(5,970)
Purchase of investment securities	--	(48)	--
Net cash provided (absorbed) by investing activities	1,080	1,045	(10,970)
Financing activities			
Proceeds from sale of stock	--	--	11,940
Purchase of stock, by ESOP	--	--	(800)
Dividends paid	(518)	(183)	--
Repurchase of stock	(1,115)	(885)	--
RRP vesting	(42)	--	--
ESOP note payment	135	--	--
Exercise of option	45	--	--
Net cash provided (absorbed) by financing activities	(1,495)	(1,068)	11,140
Increase (decrease) in cash and cash equivalents	(377)	344	182
Cash and cash equivalents, beginning of year	526	182	--
Cash and cash equivalents, end of year	$ 149	$ 526	$ 182

</TABLE>

Bedford Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements
(continued)

17. Selected Quarterly Financial Data (Unaudited)

Condensed quarterly consolidated financial data, in thousands (except per share data), is shown as follows:

Year Ended September 30, 1996	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Total interest income	$2,252	$2,283	$2,323	$2,406
Total interest expense	1,106	1,083	1,115	1,188
Net interest income	1,146	1,200	1,208	1,218
Provision for credit losses	-	-	-	22
Net interest income after provision for credit losses	1,146	1,200	1,208	1,196
Noninterest income	155	162	191	227
Noninterest expense	728	721	715	1,265
Income before income taxes	573	641	684	158
Provision for income taxes	218	243	260	33
Net income	$ 355	$ 398	$ 424	$ 125
Net income per share	$ .32	$ .35	$ .38	$ .12
Cash dividends declared per share	$ .09	$ .09	$ .10	$ .11

17. Selected Quarterly Financial Data (Unaudited) (continued)

Year Ended September 30, 1995	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Total interest income	$1,885	$1,977	$2,105	$2,170
Total interest expense	832	884	984	1,078
Net interest income	1,053	1,093	1,121	1,092
Provision for credit losses	-	7	8	5

Net interest income after provision for credit losses	1,053	1,086	1,113	1,087
Other noninterest income	147	131	137	128
Noninterest expense	624	631	657	708
Income before income taxes	576	586	593	507
Provision for income taxes	219	223	233	186
Net income	$ 357	$ 363	$ 360	$ 321
Net income per share	$ .30	$ .31	$ .31	$ .28
Cash dividends declared per share	$ -	$ .15	$ -	$ .15

OFFICE LOCATIONS

CORPORATE OFFICE
Bedford Bancshares, Inc. and Bedford Federal Savings Bank
125 W. Main Street
Bedford, VA 24523
(540) 586-2590

BRANCH OFFICES - BEDFORD FEDERAL SAVINGS BANK

Moneta Office
Rt 655 at Rt 122
Moneta, VA 24121
(540) 297-1233

Forest Office
Forest Village Square
Forest, VA 24551
(804) 525-2000

Board of Directors of Bedford Bancshares, Inc. and Bedford Federal Savings Bank

Hugh H. Bond
Chairman of the Board

George N. Cooper

Harry W. Garrett, Jr.

Harold K. Neal

William P. Pickett

William T. Powell

Macon C. Putney

W. Henry Walton, Jr.

Executive Officers of Bedford Bancshares, Inc. and Bedford Federal Savings Bank

Harold K. Neal
President and Chief Executive Officer

James W. Smith
Vice President, Treasurer and Chief Financial Officer

Russell E. Millner
Vice President

Nancy T. Snyder
Secretary

Corporate Counsel
Garrett and Garrett
116 East Main Street
Bedford, VA 24523

Independent Auditors
B.D.O. Seidman LLP
300 Arboretum Place
Suite 520
Richmond, VA 23236

Special Counsel
Malizia, Spidi, Sloane & Fisch, P.C.
One Franklin Square
1301 K Street, N.W., Suite 700 East
Washington, D.C. 20005

Transfer Agent and Registrar
Registrar & Transfer Company
10 Commerce Drive
Cranford, NJ 07016
(908) 272-8511

Bedford Bancshares, Inc.'s Annual Report for the year ended September 30, 1996, filed with the Securities and Exchange Commission on Form 10-KSB without exhibits is available without charge upon written request. For a copy of the Form 10-KSB or any other investor information, please write or call Harold K. Neal, Chief Executive Officer at the Company's Corporate Office in Bedford, Virginia. The Annual Meeting of Stockholders will be held on January 22, 1997 at 2:00 p.m. at the Olde Liberty Station, 515 Bedford Avenue, Bedford, Virginia.

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EXHIBIT 23

Independent Auditor's Consent

[Cherry,Bekaert & Holland Letterhead]

[Logo]

INDEPENDENT ACCOUNTANTS' CONSENT

Board of Directors
Bedford Bancshares, Inc.
125 West Main Street
Bedford, Virginia 24523

We consent to incorporation by reference in this Registration Statement on Form S-8 related to the Bedford Bancshares, Inc. 1994 Stock Option Plan of our report dated October 27, 1995 on the consolidated financial statements of Bedford Bancshares, Inc. for the fiscal years ended September 30, 1995 and 1994, included in the Form 10-KSB of Bedford Bancshares, Inc. for the fiscal year ended September 30, 1996.

/s/Cherry, Bekaert & Holland, L.L.P.
Cherry, Bekaert & Holland, L.L.P.

Lynchburg, Virginia
December 27, 1996

Cherry, Bekaert & Holland, L.L.P.
1700 Central Fidelity Bank Building o 828 Main Street (24504) o
P.O. Box 1119 o Lynchburg, VA 24505 o (804) 847-6643 o Fax (804) 528-3605
Offices Throughout The Southeast o Represented Internationally Through Summit International Associates, Inc.

CONSENT OF INDEPENDENT
CERTIFIED PUBLIC ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statement on Form S-8 related to the Bedford Bancshares, Inc. 1994 Stock Option Plan of our report dated October 29, 1996, relating to the consolidated financial statements of Bedford Bancshares, Inc. appearing in the Company's Annual Report on Form 10-KSB for the year ended September 30, 1996.

/s/BDO Seidman,LLP
BDO Seidman, LLP

Richmond, Virginia
December 30, 1996

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</TABLE>

Exhibit 99

Prior Accountant's Auditor's Report

[Cherry,Bekaert & Holland Letterhead]
[Logo]

Report of Independent Auditors

The Board of Directors and Stockholders
Bedford Bancshares, Inc.
Bedford, Virginia

We have audited the accompanying consolidated statements of financial condition of Bedford Bancshares, Inc. and Subsidiaries (the "Company") as of September 30, 1994 and 1995, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for each of the three years in the period ended September 30, 1995. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Bedford Bancshares, Inc. and Subsidiaries as of September 30, 1994 and 1995, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 1995 in conformity with generally accepted accounting principles.

As discussed in Notes 1 and 10 to the consolidated financial statements, the Company changes its method of accounting for income taxes by adopting Statement of Financial Accounting Standards No. 109, effective October 1, 1993. The Company also changed its method of accounting for debt and equity securititites by adopting Statement of Financial Accounting Standards No. 115, effective October 1, 1994.

/s/Cherry, Bekaert & Holland, L.L.P.

Lynchburg, Virginia
October 27, 1995