FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

Filing Date: **1995-05-10** | Period of Report: **1995-03-31**
SEC Accession No. 0000950159-95-000042

FILER

NATIONAL PENN BANCSHARES INC

CIK:**700733**| IRS No.: **232215075** | State of Incorp.:**PA** | Fiscal Year End: **1231**
Type: **10-Q** | Act: **34** | File No.: **000-10957** | Film No.: **95536004**
SIC: **6021** National commercial banks

Mailing Address
POST OFFICE BOX 547
POST OFFICE BOX 547
BOYERTOWN PA 19512

Business Address
POST OFFICE BOX 547
BOYERTOWN PA 19512
6103696341

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: March 31, 1995

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from: __________________ to __________________

Commission file number: 0-10957

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

Pennsylvania	23-2215075
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Philadelphia and Reading Avenues, Boyertown, PA 19512
(Address of principal executive offices) (Zip Code)

(610) 367-6001
(Registrant's telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No

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

Class	Outstanding at May 5, 1995
Common Stock ($2.50 par value)	(No.) 7,136,930 Shares

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

NATIONAL PENN BANCSHARES, INC. AND SUBSIDIARIES

<TABLE>
CONSOLIDATED CONDENSED BALANCE SHEET
<CAPTION>

(Dollars in thousands, except per share data)	March 31 1995 (Unaudited)	Dec. 31 1994 (Note)
<S>	<C>	<C>
ASSETS		
Cash and due from banks	$34,084	$33,195
Interest bearing deposits in banks	1,584	964
Federal funds sold	---	---
	-------	-------

Total cash and cash equivalents	35,668	34,159
Securities held to maturity (approximate market of $92,933 and $97,459 at 1995 and 1994, respectively)	92,704	99,229
Securities available for sale at market value	145,388	138,873
Total Investment Securities	238,092	238,102
Loans, net of unearned discount	848,954	830,612
Less allowance for possible loan losses	(19,577)	(19,310)
Net loans	829,377	811,302
Other assets	52,320	53,611
Total Assets	$1,155,457	$1,137,174
LIABILITIES AND SHAREHOLDERS' EQUITY		
Non-interest bearing deposits	$116,280	$121,273
Interest bearing deposits (Includes certificates of deposit in excess of $100: 1995 - $93,828; 1994- $65,630)	788,673	743,367
Total deposits	904,953	864,640
Securities sold under repurchase agreements and federal funds purchased	63,961	50,274
Short-term borrowings	2,156	47,967
Long-term obligations	77,777	77,777
Accrued interest and other liabilities	15,021	11,645
Total Liabilities	1,063,868	1,052,303
Commitments and contingent liabilities	---	---
Shareholders' equity		
Preferred stock, no stated par value; authorized 1,000,000 shares, none issued	---	---
Common stock, par value $2.50 per share; 20,000,000 shares authorized; 7,234,507 shares issued and 7,136,930 outstanding at March 31, 1995; 7,234,126 shares issued and 7,135,347 shares outstanding at December 31, 1994	18,084	18,083
Additional paid-in-capital	57,136	57,263
Retained earnings	19,016	16,598
Valuation adjustment for securities available for sale, net of tax	229	(4,011)
Treasury stock (97,577 shares at cost at March 31, 1995 and 98,779 shares at cost at December 31, 1994)	(2,876)	(3,062)
Total Shareholders' Equity	91,589	84,871
Total Liabilities and Shareholders' Equity	$1,155,457	$1,137,174

</TABLE>

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

Note: The Balance Sheet at Dec. 31, 1994 has been derived from the audited financial statements at that date.

NATIONAL PENN BANCSHARES, INC. AND SUBSIDIARIES
<TABLE>
UNAUDITED CONSOLIDATED CONDENSED STATEMENTS OF INCOME
<CAPTION>

(Dollars in thousands, except per share data)	Three Months Ended March 31	
	1995	1994
<S>	<C>	<C>
INTEREST INCOME		
Loans, including fees	$19,258	$16,375
Deposits in banks	15	32
Federal funds sold	2	5
Investment securities	3,975	2,805
	------	------
Total interest income	23,250	19,217
	------	------
INTEREST EXPENSE		
Deposits	7,403	4,795
Federal funds purchased, borrowed funds and securities sold under repurchase agreements	2,387	1,233
	------	------
Total interest expense	9,790	6,028
	------	------
Net interest income	13,460	13,189
Provision for loan losses	750	750
	------	------
Net interest income after provision for loan losses	12,710	12,439
	------	------
OTHER INCOME		
Trust Services	424	325
Service charges on deposit accounts	640	646
Net gains (losses) on sale of securities and mortgages	256	(221)
Other	748	396
	------	------
Total other income	2,068	1,146
	------	------
OTHER EXPENSES		
Salaries, wages and employee benefits	4,981	4,253
Net premises and equipment	1,389	1,197
Other operating	2,837	2,530
	------	------
Total other expenses	9,207	7,980
	------	------
Income before income taxes	5,571	5,605
Applicable income tax expense	1,654	1,802
	------	------

Net income	$3,917	$3,803
	======	======
PER SHARE OF COMMON STOCK		
Net income	0.55	0.53
Dividends paid in cash	0.21	0.17

</TABLE>

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

NATIONAL PENN BANCSHARES, INC. AND SUBSIDIARIES

<TABLE>

UNAUDITED CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

<CAPTION>

(Dollars in thousands)	Three Months Ended March 31, 1995	1994
<S>	<C>	<C>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$3,917	$3,803
Adjustments to reconcile net income to net cash provided by (used in) operating activities		
Provision for loan losses	750	750
Depreciation and amortization	628	437
Net gains (losses) on sale of securities and mortgages	256	(221)
Mortgage loans originated for resale	(1,279)	(7,913)
Sale of mortgage loans originated for resale	1,279	7,913
Other	2,029	(823)
	------	------
Net cash provided by (used in) operating activities	7,580	3,946
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales of investment securities - available for sale	2,525	---
Proceeds from maturities of investment securities - held to maturity	6,525	8,284
Proceeds from maturities of investment securities - available for sale	11	---
Purchase of investment securities - available for sale	(2,527)	(31,013)
Proceeds from sales of loans	---	---
Net increase in loans	(18,825)	(13,662)
Purchases of premises & equipment	(657)	(1,151)
	------	------
Net cash provided by (used in) investing activities	(12,948)	(37,542)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase (decrease) in:		

Deposits	40,313	2,319
Repurchase agreements, fed funds & short-term borrowings	(32,124)	34,080
Long-term borrowings	---	---
(Increase) decrease in treasury stock	186	(250)
Issuance of common stock under dividend reinvestment plan	---	9
Cash dividends	(1,498)	(1,301)
Net cash provided by (used in) financing activities	6,877	34,857
Net increase (decrease) in cash and cash equivalents	1,509	1,261
Cash and cash equivalents at January 1	34,159	29,767
Cash and cash equivalents at March 31	$35,668	$31,028

</TABLE>

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

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (UNAUDITED)

1. The accompanying unaudited condensed financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information. The financial information included herein is unaudited; however, such information reflects all adjustments (consisting solely of normal recurring adjustments) which are, in the opinion of management, necessary to a fair statement of the results for the interim periods. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 1994.

2. The results of operations for the three month period ended March 31, 1995 are not necessarily indicative of the results to be expected for the full year.

3. Per share data are based on the weighted average number of shares outstanding of 7,139,680 and 7,165,367 for 1995 and 1994, respectively, and are computed after giving retroactive effect to a 5% stock dividend paid October 31, 1994.

4. On January 1, 1995 the Company adopted Statement of Financial Accounting Standards (SFAS) No. 114, "Accounting for Creditors for Impairment of a Loan," as amended by SFAS No. 118, "Accounting for Creditors for Impairment of a Loan - Income Recognition and Disclosures." SFAS No. 114 requires that a creditor measure impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, a creditor may measure impairment based on a loan's observable market price, or the fair value of collateral if the loan is collateral dependent.

Regardless of the measurement method, a creditor must measure impairment based on the fair value of the collateral when the creditor determines that foreclosure is probable. SFAS No. 118 allows creditors to use existing methods for recognizing interest income on impaired loans.

The Company has identified a loan as impaired when it is probable that interest and principal will not be collected according to the contractual terms of the loan agreement. The accrual of interest is discontinued in such loans and no income is recognized until all recorded amounts of interest and principal are recovered in full.

Loan impairment is measured by estimating the expected future cash flows and discounting them at the respective effective interest rate or by valuing the underlying collateral. The recorded investment in these loans and the valuation for credit losses related to loan impairment are as follows:

	March 31, 1995
Principal amount of impaired loans	$8,853,000
Accrued interest	---
Deferred loan costs	---

	8,853,000
Less valuation allowance	1,721,000

	$7,132,000
	==========

On January 1, 1995 a valuation for credit losses related to impaired loans was established. The activity in this allowance for the quarter ending March 31, 1995 is as follows:

Valuation allowance at beginning of period	$1,913,000
Provision for loan impairment	125,000
Direct charge-offs	(485,000)
Recoveries	168,000

Valuation allowance at end of period	$1,721,000
	==========

Total cash collected on impaired loans during the quarter ended March 31, 1995 was $178,000, of which $168,000 was credited to the principal balance outstanding on such loans and $10,000 was recognized as interest income. Interest that would have been accrued on impaired loans during the quarter was $196,000. Interest income recognized during the quarter was $10,000.

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

The following discussion and analysis is intended to assist in understanding and evaluating the major changes in the financial condition and earnings performance of the Company with a primary focus on an analysis of operating results.

FINANCIAL CONDITION

Total assets increased to $1.155 billion, an increase of $18.3 million or 1.6% over the $1.137 billion at December 31, 1994. This increase is reflected primarily in the loan category, the result of the investment of deposits, the Company's primary source of funds.

Total cash and cash equivalents increased $1.5 million or 4.4% at March 31, 1995 when compared to December 31, 1994. This increase was primarily due to interest bearing deposits in banks.

Loans increased to $849.0 million at March 31, 1995. The increase of $18.3 million or 2.2% compared to December 31, 1994 was primarily the result of the investment of deposits. In addition, loans originated for immediate resale during the first quarter amounted to $1.3 million. The Company's credit quality is reflected by the annualized ratio of net charge-offs to average total loans of .23% for the first quarter and the level of non-accrual loans to total loans of 1.04% at March 31, 1995. The Company has no significant exposure to energy and agricultural-related loans. Non-accrual loans at December 31, 1994 were 1.12% of total loans.

Investments, the Company's secondary use of funds, remained stable through March 31, 1995.

As the primary source of funds, aggregate deposits of $905.0 million at March 31, 1995 increased $40.3 million or 4.7% compared to December 31, 1994. There was a shift in deposit mix during the first three months of 1995 as interest bearing deposits increased $45.3 million and non-interest bearing deposits decreased $5.0 million. Certificates of deposit in excess of $100,000 increased $28.2 million. In addition to deposits, earning assets are funded to some extent through purchased funds and borrowings. These include securities sold under repurchase agreements, federal funds purchased, short-term borrowings, and long-term obligations. In aggregate, these funds totaled $159.0 million at March 31, 1995 and $187.7 million at December 31, 1994. The decrease of $28.8 million represents an decrease in short-term borrowings, primarily securities sold under repurchase agreements and federal funds purchased.

Shareholders' equity increased $6.7 million or 7.9% at March 31, 1995 to $91.6 million compared to the $84.9 million at December 31, 1994. This increase was due to the retention of earnings and the change in valuation adjustment for securities available for sale. Cash dividends paid during the first three months of 1995 increased $268,000 or 21.8% compared to the cash dividends paid during the first three months of 1994. Earnings retained during the first three months of 1995 were 61.8% compared to 67.7% during the first three months of 1994.

RESULTS OF OPERATIONS

Net income for the quarter ended March 31, 1995 was $3.9 million, 3.0% more than the $3.8 million reported for the same period in 1994. The Company's performance has been and will continue to be in part influenced by the strength of the economy and conditions in the real estate market.

Net interest income is the difference between interest income on assets and interest expense on liabilities. Net interest income increased $.3 million or 2.1% to $13.5 million during the first quarter of 1995 from $13.2 million in the first quarter 1994. The increase was due primarily to an increase in interest income, as a result of growth in loan outstandings and higher rates on loans, partially offset by growth in deposits and higher rates on deposits and borrowings. Interest rate risk is a major concern in forecasting earnings potential. The Company's prime rate from January 1, 1995 to January 31, 1995 was 8.5%. On February 1, 1995, the prime rate changed to 9.0%. The Company's prime rate from January 1 to March 23, 1994 was 6.0%. On March 24, 1994, the prime rate changed to 6.25%. Interest expense during the first three months of 1995 increased $3.8 million or 62.4% compared to the prior year three month period. In addition to the current increasing rate environment, the cost of attracting and holding deposited funds is an ever-increasing expense in the banking industry. These increases are the real costs of deposit accumulation and retention, including FDIC insurance costs and branch overhead expenses. Such costs are necessary for continued growth and to maintain and increase market share of available deposits.

The provision for loan losses is determined by periodic reviews of loan quality, current economic conditions, loss experience and loan growth. Based on these factors, the provision for loan losses remained constant when compared to the first quarter of 1994. The allowance for loan losses of $19.6 million at March 31, 1995 and $19.3 million at December 31, 1994 as a percentage of gross loans was 2.3% for both time periods. Net charge-offs of $483,000 and $717,000 during the first three months of 1995 and 1994, continues to be comparable to that of the

Company's peers, as reported in the Bank Holding Company Performance Report.

"Total other income" increased $922,000 or 80.5% during the first quarter of 1995 as the result of gains on the sale of securities and mortgages of $477,000, other income of $352,000 and trust income of $99,000. "Total other expenses" increased $1,227,000 or 15.4% during the quarter ended March 31, 1995. Of this amount, salaries and benefits increased $728,000 or 17.1% over the first quarter of 1994. Other operating expenses increased $307,000 and premises and equipment increased $192,000.

Income before income taxes decreased by $34,000 or .6% compared to the first quarter of 1994. Income taxes decreased $148,000, or 8.2%, for the quarter due to a higher level of tax advantaged assets than for the same period in 1994.

LIQUIDITY AND INTEREST RATE SENSITIVITY

The primary functions of asset/liability management are to assure adequate liquidity and maintain an appropriate balance between interest-earning assets and interest-bearing liabilities. Liquidity management involves the ability to meet the cash flow requirements of customers who may be either depositors wanting to withdraw funds or borrowers needing assurance that sufficient funds will be available to meet their credit needs. Funding affecting short-term liquidity, including deposits, repurchase agreements, federal funds purchased, and short-term borrowings, increased in the aggregate $8.2 million from year end 1994. Long-term borrowings remained constant through the first quarter of 1995.

The goal of interest rate sensitivity management is to avoid fluctuating net interest margins, and to enhance consistent growth of net interest income through periods of changing interest rates. Such sensitivity is measured as the difference in the volume of assets and liabilities in the existing portfolio that are subject to repricing in a future time period.

The following table shows separately the interest rate sensitivity of each category of interest-earning assets and interest-bearing liabilities at March 31, 1995:

	Repricing Periods (1)		
	Within One Year	One Year Through Five Years	Over Five Years
		(In Thousands)	
Assets			
Interest bearing deposits at banks	$ 1,584	$ --	$ --
Investment securities	54,129	114,750	69,213
Loans and leases	346,203	337,608	165,143
Other assets	4,369	--	82,035
	406,285	452,358	316,391
Liabilities and equity			
Non-interest bearing deps.	116,280	--	--
Interest bearing deposits	290,983	224,552	273,138
Borrowed funds	117,305	14,089	12,500
Other liabilities	--	--	34,598
Hedging instruments	100,000	(70,000)	(30,000)
Shareholders' equity	--	--	91,589
	624,568	168,641	381,825

Interest sensitivity gap	(218,283)	283,717	(65,434)
Cumulative interest rate sensitivity gap	($218,283)	$65,434	$ --

(1) Savings and NOW deposits are scheduled for repricing based on historical deposit decay rate analyses, as well as historical moving averages of run-off for the Company's deposits in these categories.

Interest rate sensitivity is a function of the repricing characteristics of the Company's assets and liabilities. These characteristics include the volume of assets and liabilities repricing, the timing of the repricing, and the relative levels of repricing. Attempting to minimize the interest rate sensitivity gaps is a continual challenge in a changing rate environment. Based on the Company's gap position as reflected in the above table, current accepted theory would indicate that net interest income would increase in a falling interest rate environment and would decrease in a rising rate environment. An interest rate gap table does not, however, present a complete picture of the impact of interest rate changes on net interest income. First, changes in the general level of interest rates do not affect all categories of assets and liabilities equally or simultaneously. Second, assets and liabilities which can contractually reprice within the same period may not, in fact, reprice at the same time or to the same extent. Third, the table represents a one-day position; variations

occur daily as the Company adjusts its interest sensitivity throughout the year. Fourth, assumptions must be made to construct such a table. For example, non-interest bearing deposits are assigned a repricing interval of within one year, although history indicates a significant amount of these deposits will not move into interest bearing categories regardless of the general level of interest rates. Finally, the repricing distribution of interest sensitive assets may not be indicative of the liquidity of those assets.

The Company anticipates volatile interest rate levels for the remainder of 1995, with no clear indication of sustainable rising or falling rates. Given this assumption, the Company's asset/liability strategy for 1995 is to move toward a smaller negative gap (interest-bearing liabilities subject to repricing greater than rising interest-earning assets subject to repricing) for periods up to a year. The impact of a volatile interest rate environment on net interest income is not expected to be significant to the Company's results of operations. Effective monitoring of these interest sensitivity gaps is the priority of the Company's asset/liability management committee.

CAPITAL ADEQUACY

The following table sets forth certain capital performance ratios.

	Mar. 31, 1995	Dec. 31, 1994
CAPITAL LEVELS		

Tier 1 leverage ratio	7.41%	7.35%
Tier 1 risk-based ratio	11.09	10.85
Total risk-based ratio	12.36	12.11
CAPITAL PERFORMANCE		
Return on average assets(annualized)	1.38	1.41
Return on average equity(annualized)	18.20	17.30
Earnings retained	61.76	63.50
Internal capital growth(annualized)	31.66	11.32

The Company's capital ratios above compare favorably to the minimum required amounts of Tier 1 and total capital to "risk-weighted" assets and the minimum Tier 1 leverage ratio, as defined by banking regulators. At March 31, 1995, the Company was required to have minimum Tier 1 and total capital ratios of 4.0% and 8.0%, respectively, and a minimum Tier 1 leverage ratio of 3.0%. In order for the Company to be considered "well capitalized", as defined by banking regulators, the Company must have Tier 1 and total capital ratios of 6.0% and 10.0%, respectively, and a minimum Tier 1 leverage ratio of 5.0%. The Company currently meets the criteria for a well capitalized institution, and management

believes that, under current regulations, the Company will continue to meet its minimum capital requirements in the foreseeable future. At present, the Company has no commitments for significant capital expenditures.

The Company is not under any agreement with regulatory authorities nor is the Company aware of any current recommendations by the regulatory authorities which, if such recommendations were implemented, would have a material effect on liquidity, capital resources or operations of the Company.

FUTURE OUTLOOK

On March 1, 1995, the Company opened its first supermarket branch banking facility. The Company considers supermarket branches to be a strategic delivery system for banks in the future and anticipates opening four more during the remainder of 1995.

The Company will continue its work on the installation of platform automation during 1995. Through platform automation, the Company expects to increase efficiencies and re-focus its efforts to improve productivity, in order to provide faster and improved service to our customers, at the same time reducing costs to contribute to improved profitability. The platform automation project may lead to in excess of $1 million in capital expenditures in 1995.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

None

Item 2. Changes in Securities.

None

Item 3. Defaults Upon Senior Securities.

None

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

None

Item 5. Other Information.

On March 1, 1995, the Registrant's banking subsidiary, National Penn Bank, opened its first full-service supermarket branch in Muhlenberg Weis Market, Berks County, Pennsylvania. The Registrant anticipates that in 1995 National Penn Bank will open four more supermarket branches, located in Schnecksville (Lehigh County), Cedar Crest (Lehigh County), Coopersburg (Lehigh County), and Bethlehem (Northampton County). The Registrant also anticipates that National Penn Bank will close its Fairview Village branch (Montgomery County) in June 1995.

In February 1994, the Registrant's Board of Directors approved the repurchase of up to 200,000 shares of its common stock in open market or negotiated transactions. At March 31, 1995, a total of 152,440 shares have been repurchased at an aggregate cost of $4,737,000.

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits.

Exhibit 27 - Financial Data Schedule.

(b) Reports on Form 8-K. The Registrant did not file any report on Form 8-K during the quarterly period ended March 31, 1995.

SIGNATURES

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the Registrant has caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

NATIONAL PENN BANCSHARES, INC.
(Registrant)

Dated: May 5, 1995

By /s/ Lawrence T. Jilk, Jr.

Lawrence T. Jilk, Jr., President and Chief Executive Officer

Dated: May 5, 1995

By /s/ Gary L. Rhoads

Gary L. Rhoads, Principal Financial Officer

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