

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

BANCORP RHODE ISLAND INC  
Form 10-Q  
August 09, 2002

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C.

FORM 10-Q

Quarterly Report Under Section 13 of the Securities Exchange Act of 1934  
For quarter ended: June 30, 2002

Commission File No. 001-16101

BANCORP RHODE ISLAND, INC.

-----  
(Exact Name of Registrant as Specified in Its Charter)

RHODE ISLAND

05-0509802

-----  
(State or Other Jurisdiction  
of Incorporation or Organization)

(IRS Employer  
Identification No.)

ONE TURKS HEAD PLACE, PROVIDENCE, RI 02903

-----  
(Address of Principal Executive Offices)

(401) 456-5000

-----  
(Issuer's Telephone Number, Including Area Code)

Not Applicable

-----  
(Former Name, Former Address and Former Fiscal Year,  
if Changed Since Last Report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 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 Registrant's classes of common stock, as of August 5, 2002:

Common Stock - Par Value \$0.01

3,776,150 shares

-----  
(class)

-----  
(outstanding)

BANCORP RHODE ISLAND, INC.

# Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

FORM 10-Q

## INDEX

	PAGE NUMBER	
	-----	
Cover Page	1	
Index	2	
PART I - FINANCIAL INFORMATION		
Item 1	Financial Statements	
	Consolidated Balance Sheets	3
	Consolidated Statements of Operations	4
	Consolidated Statements of Changes in Shareholders' Equity	5
	Consolidated Statements of Cash Flows	6
	Notes to Consolidated Financial Statements	7 - 8
Item 2	Management's Discussion and Analysis	9 - 20
Item 3	Quantitative and Qualitative Disclosures About Market Risk	21 - 22
PART II - OTHER INFORMATION		
Item 1	Legal Proceedings	23
Item 2	Changes in Securities	23
Item 3	Default upon Senior Securities	23
Item 4	Submission of Matters to a Vote of Security Holders	23 - 24
Item 5	Other Information	24
Item 6	Exhibits and Reports on Form 8-K	24
	Signature Page	25

2

BANCORP RHODE ISLAND, INC.  
Consolidated Balance Sheets

June 30,      Decemb  
2002            20

-----  
(Dollars in thous

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

ASSETS:

Cash and due from banks	\$ 22,094	\$ 24
Overnight investments	9,377	4
Investment securities available for sale (amortized cost of \$71,249 and \$49,193 at June 30, 2002 and December 31, 2001, respectively)	71,800	49
Mortgage-backed securities available for sale (amortized cost of \$188,288 and \$149,549 at June 30, 2002 and December 31, 2001, respectively)	189,464	150
Stock in Federal Home Loan Bank of Boston	7,683	5
Loans receivable:		
Residential mortgage loans	291,495	310
Commercial loans	259,502	239
Consumer and other loans	64,581	61
	-----	-----
Total loans	615,578	610
Less allowance for loan losses	(9,266)	(8)
	-----	-----
Net loans	606,312	602
Premises and equipment, net	7,717	7
Other real estate owned	--	
Excess of cost over net assets acquired, net	10,184	10
Accrued interest receivable	6,059	5
Investment in bank-owned life insurance	10,237	
Prepaid expenses and other assets	3,067	
	-----	-----
Total assets	\$943,994	\$862
	=====	=====

LIABILITIES:

Deposits:		
Demand deposit accounts	\$116,377	\$112
NOW accounts	64,482	44
Money market accounts	9,956	9
Savings accounts	268,747	254
Certificate of deposit accounts	241,627	248
	-----	-----
Total deposits	701,189	670
Overnight and short-term borrowings	18,003	13
Federal Home Loan Bank of Boston borrowings	150,802	113
Company-obligated mandatorily redeemable capital securities	8,000	3
Other liabilities	4,074	3
	-----	-----
Total liabilities	882,068	803
	-----	-----

SHAREHOLDERS' EQUITY:

Common stock, par value \$0.01 per share, authorized 11,000,000 shares:		
Voting: Issued and outstanding 3,762,850 shares in 2002 and 3,753,550 in 2001	38	
Additional paid-in capital	39,970	39
Retained earnings	20,778	18
Accumulated other comprehensive income (loss), net	1,140	
	-----	-----
Total shareholders' equity	61,926	59
	-----	-----
Total liabilities and shareholders' equity	\$943,994	\$862
	=====	=====

See accompanying notes to consolidated financial statements

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

3

BANCORP RHODE ISLAND, INC.  
Consolidated Statements of Operations

	Three Months Ended June 30,		Six
	2002	2001	200
	(Dollars in thousands, except per		
Interest and dividend income:			
Residential mortgage loans	\$ 4,845	\$ 5,485	\$ 9,
Commercial loans	4,443	4,568	8,
Consumer and other loans	959	1,199	1,
Mortgage-backed securities	2,348	1,954	4,
Investment securities	821	705	1,
Overnight investments	43	215	
Federal Home Loan Bank of Boston stock dividends	80	77	
Total interest and dividend income	13,539	14,203	26,
Interest expense:			
NOW accounts	86	58	
Money market accounts	31	60	
Savings accounts	1,282	1,785	2,
Certificate of deposit accounts	2,101	3,566	4,
Overnight and short-term borrowings	53	116	
Federal Home Loan Bank of Boston borrowings	1,888	1,373	3,
Other borrowings	--	68	
Company-obligated mandatorily redeemable capital securities	81	79	
Total interest expense	5,522	7,105	11,
Net interest income	8,017	7,098	15,
Provision for loan losses	450	352	
Net interest income after provision for loan losses	7,567	6,746	14,
Noninterest income:			
Service charges on deposit accounts	912	894	1,
Loan related fees	82	51	
Commissions on loans originated for others	58	71	
Commissions on nondeposit investment products	173	73	
Gain on sale of mortgage-backed securities	--	4	
Income from bank-owned life insurance	142	--	
Other income	151	213	
Total noninterest income	1,518	1,306	3,
Noninterest expense:			
Salaries and employee benefits	3,207	2,665	6,

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

Occupancy	496	438	
Equipment	246	208	
Data processing	485	463	
Marketing	385	369	
Professional services	416	185	
Loan servicing	236	242	
Other real estate owned expense	16	21	
Amortization of excess of cost over net assets acquired	291	291	
Other	759	766	1,
	-----		
Total noninterest expense	6,537	5,648	12,
	-----		
Income before income taxes	2,548	2,404	5,
Income tax expense	834	832	1,
	-----		
Net income	\$ 1,714	\$ 1,572	\$ 3,
	=====		

Per share data:			
Basic earnings per common share	\$ 0.46	\$ 0.42	\$ 0
Diluted earnings per common share	\$ 0.43	\$ 0.40	\$ 0
Average common shares outstanding - basic	3,751,054	3,729,879	3,749,
Average common shares outstanding - diluted	4,012,159	3,888,868	3,995,

See accompanying notes to consolidated financial statements

4

BANCORP RHODE ISLAND, INC.  
Consolidated Statements of Changes in Shareholders' Equity

Six months ended June 30,	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Compre- hensive Income (Loss), Net
	-----	-----	-----	-----
	(In thousands)			
2002				
----				
Balance at December 31, 2001	\$37	\$39,826	\$18,336	\$ 898
Net income	--	--	3,419	--
Other comprehensive income, net of tax:				
Unrealized holding gains on securities available for sale, net of taxes of \$132				257
Realized gain on securities available for sale, net of taxes of \$8				(15)
Comprehensive income				

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

Proceeds from exercise of options	1	128	--	--
Common stock issued for incentive stock award, net	--	16	--	--
Dividends on common stock	--	--	(977)	--
-----				
Balance at June 30, 2002	\$38	\$39,970	\$20,778	\$1,140
=====				
2001				
----				
Balance at December 31, 2000	\$37	\$39,621	\$13,815	\$ (181)
Net income	--	--	3,132	--
Other comprehensive income, net of tax:				
Unrealized holding gains on securities available for sale, net of taxes of \$1,156				763
Realized gain on securities available for sale, net of taxes of \$1				(3)
Comprehensive income				
Proceeds from exercise of options	--	16	--	--
Common stock issued for incentive stock award, net	--	11	--	--
Dividends on common stock	--	--	(896)	--
-----				
Balance at June 30, 2001	\$37	\$39,648	\$16,051	\$ 579
=====				

See accompanying notes to consolidated financial statements

5

BANCORP RHODE ISLAND, INC.  
Consolidated Statements of Cash Flows

	Six Months Ended June 30,	
	2002	2001
	----	----
	(In thousands)	
Cash flows from operating activities:		
Net income	\$ 3,419	\$ 3,132
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	1,792	1,511
Provision for loan losses	850	840
Gain on mortgage-backed securities	(23)	(4)
Gain on sale of other real estate owned	(29)	(14)
Income from bank-owned life insurance	(237)	--
Compensation expense from restricted stock grant	16	11
(Increase) decrease in:		

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

Accrued interest receivable	(256)	(534)
Prepaid expenses and other assets	(2,342)	(656)
Increase (decrease) in:		
Other liabilities	732	(244)
Other, net	53	9
	-----	-----
Net cash provided (used) by operating activities	3,975	4,051
	-----	-----
Cash flows from investing activities:		
Origination of:		
Residential mortgage loans	(4,915)	(7,082)
Commercial loans	(33,845)	(24,813)
Consumer loans	(12,313)	(9,398)
Purchase of:		
Investment securities available for sale	(41,074)	(34,026)
Mortgage-backed securities available for sale	(73,017)	(33,000)
Residential mortgage loans	(62,318)	(105,689)
Consumer loans	--	(5,045)
Federal Home Loan Bank of Boston stock	(2,015)	(1,211)
Principal payments on:		
Investment securities available for sale	19,006	23,000
Mortgage-backed securities available for sale	30,359	18,017
Residential mortgage loans	85,614	55,454
Commercial loans	13,619	19,407
Consumer loans	8,949	10,342
Proceeds from sale of mortgage-backed securities	3,766	3,885
Proceeds from sale of other real estate owned	293	84
Proceeds from sale of premises and equipment	--	18
Capital expenditures for premises and equipment	(1,122)	(739)
Purchase of bank-owned life insurance	(10,000)	--
	-----	-----
Net cash provided (used) by investing activities	(79,013)	(90,796)
	-----	-----
Cash flows from financing activities:		
Net increase in deposits	30,776	26,988
Net increase in overnight and short-term borrowings	4,970	3,277
Proceeds from long-term borrowings	45,351	71,000
Repayment of long-term borrowings	(2,914)	(7,755)
Proceeds from exercise of stock options	129	16
Dividends on common stock	(977)	(896)
	-----	-----
Net cash provided (used) by financing activities	77,335	92,630
	-----	-----
Net increase (decrease) in cash and cash equivalents	2,297	5,885
Cash and cash equivalents at beginning of period	29,174	34,453
	-----	-----
Cash and cash equivalents at end of period	\$ 31,471	\$ 40,338
	=====	=====
Supplementary Disclosures:		
Cash paid for interest	\$ 10,901	\$ 13,249
Cash paid for income taxes	2,582	2,690
Non-cash transactions:		
Additions to other real estate owned in settlement of loans	--	62
Change in other comprehensive income, net of taxes	242	760

See accompanying notes to consolidated financial statements

BANCORP RHODE ISLAND, INC.  
Notes to Consolidated Financial Statements

(1) Basis of Presentation

Bancorp Rhode Island, Inc. (the "Company"), a Rhode Island corporation, was organized by Bank Rhode Island (the "Bank") on February 15, 2000, to be a bank holding company and to acquire all of the capital stock of the Bank. The reorganization of the Bank into the holding company form of ownership was completed on September 1, 2000. The Company has no significant assets other than the common stock of the Bank. For that reason, substantially all of the discussion in this Quarterly Report on Form 10-Q relates to the operations of the Bank and its subsidiaries.

The consolidated financial statements include the accounts of the Company and its wholly-owned direct subsidiaries, the Bank, BRI Statutory Trust I and BRI Statutory Trust II (issuers of trust preferred securities), and its indirect subsidiaries, BRI Investment Corp. (a Rhode Island passive investment company), BRI Realty Corp. (a real estate holding company) and Acorn Insurance Agency, Inc. (a licensed insurance agency). All significant intercompany accounts and transactions have been eliminated in consolidation.

The interim results of consolidated operations are not necessarily indicative of the results for any future interim period or for the entire year. These interim consolidated financial statements do not include all disclosures associated with annual financial statements and, accordingly, should be read in conjunction with the annual consolidated financial statements and accompanying notes included in the Company's Annual Report to Shareholders filed with the Securities and Exchange Commission.

In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to change relate to the determination of the allowance for loan losses.

The unaudited interim consolidated financial statements of the Company have been prepared in accordance with Accounting Principles Generally Accepted in the United States of America ("GAAP") and prevailing practices within the banking industry and include all necessary adjustments (consisting of only normal recurring adjustments), that, in the opinion of management, are required for a fair presentation of the results and financial condition of the Company.

(2) Earnings Per Share

Basic earnings per share ("EPS") excludes dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted EPS reflects the potential dilution that could occur if options, warrants or other contracts to issue common stock were exercised and resulted in the issuance of additional common stock that then shared in the earnings of the entity.



## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

### (3) Recent Accounting Developments

On July 20, 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Account Standards 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 142 addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, "Intangible Assets". Under SFAS 142, goodwill and intangible assets that have indefinite useful lives are no longer be amortized, but rather are tested at least annually for impairment. The Statement applies to existing goodwill, as well as goodwill arising subsequent to the effective date of the Statement. Intangible assets that have finite useful lives will continue to be amortized over their useful lives, but without the constraint of the 40-year maximum life required by APB Opinion No. 17. The provisions of SFAS 142 must be applied for fiscal years beginning after December 15, 2001 and may not be adopted earlier.

On October 17, 2001, FASB issued Action Alert No. 01-37. That Action Alert reported a conclusion reached by FASB at its October 10, 2001 meeting regarding the application of SFAS 142 and Statement of Financial Accounting Standards 141, Business Combinations ("SFAS 141") with respect to goodwill accounting for bank branch acquisitions. The conclusion set forth in the October 17th Action Alert states that paragraph 5 of Statement of Financial Standards 72, Accounting for Certain Acquisitions of Banking or Thrift Institutions (SFAS 72), "applies to all acquisitions of financial institutions (or branches thereof) whether "troubled" or not, in which the fair value of the liabilities assumed exceeds the fair value of tangible and intangible assets acquired." SFAS 72 was originally issued in 1983, in the context of the savings and loan crisis and the acquisition of so-called "troubled" financial institutions. The branch acquisitions associated with the formation of the Company's banking subsidiary in March 1996 were such that the fair value of the liabilities assumed appear to exceed the fair value of tangible and intangible assets acquired. Thus, the March 1996 transaction gave rise to a type of intangible that, unlike goodwill, will continue to be amortized under current accounting guidelines.

Based upon the conclusion set forth in the October 17th Action Alert, the Company is required to continue amortizing its intangible attributable to its March 1996 bank branch acquisition during the Fleet Financial Group, Inc. divestiture. Current amortization of this intangible is \$1.2 million annually. Accordingly, the Company anticipates that there will continue to be a difference between its GAAP and cash basis presentations.

The October 17th Action Alert also states that FASB will reconsider its new guidance during future deliberations. The conclusion reached by FASB regarding the need to continue amortization of an unidentifiable intangible asset, therefore, may be overturned at a later date. The Company, however, can give no assurance that FASB will vary from its current position. Regardless of its final outcome, this goodwill accounting issue will not have any material impact on the Company's financial condition. At June 30, 2002, the Company had \$10.2 million of excess of cost over net assets acquired remaining on its balance sheet.

8

BANCORP RHODE ISLAND, INC.  
Management's Discussion and Analysis

ITEM 2. Management's Discussion and Analysis

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

Certain statements contained herein are "Forward Looking Statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Forward Looking Statements may be identified by reference to a future period or periods or by the use of forward looking terminology such as "may," "believes," "intends," "expects," and "anticipates" or similar terms or variations of these terms. Actual results could differ materially from those set forth in Forward Looking Statements as a result of certain risks and uncertainties, including but not limited to, changes in political and economic conditions, interest rate fluctuations, competitive product and pricing pressures, equity and bond market fluctuations, credit risk, inflation, as well as other risks and uncertainties detailed from time to time in filings with the Securities and Exchange Commission ("SEC").

### GENERAL

-----

The Company's principal subsidiary, Bank Rhode Island, is a commercial bank chartered as a financial institution in the State of Rhode Island. The Bank pursues a community banking mission and is principally engaged in providing banking products and services to individuals and businesses in Providence and Kent counties. The Bank is subject to competition from a variety of traditional and nontraditional financial service providers both within and outside of Rhode Island. The Bank offers its customers a wide range of deposit products, nondeposit investment products, commercial, residential and consumer loans, and other traditional banking products and services, designed to meet the needs of individuals and small- to mid-sized businesses. The Bank also has introduced both commercial and consumer on-line banking products and maintains a web site at <http://www.bankri.com>. The Company and Bank are subject to regulation by a number of federal and state agencies and undergo periodic examinations by certain of those regulatory authorities. The Bank's deposits are insured by the Federal Deposit Insurance Corporation ("FDIC"), subject to regulatory limits. The Bank is also a member of the Federal Home Loan Bank of Boston ("FHLB").

### NON-GAAP MEASURES OF FINANCIAL PERFORMANCE

-----

The Bank's formation in 1996 resulted in the generation of \$17.5 million of intangibles that are being amortized over a 15-year period. The amortization of these intangibles reduces the Bank's pre-tax income \$1.2 million annually. Because of the impact of this amortization, certain measures of financial performance have been calculated excluding such amortization and any related income taxes.

These measures are identified as "cash" or "cash basis" and have been provided to assist the reader in evaluating the core performance of the Company. Information presented on a cash basis is not in accordance with GAAP, but management believes it to be beneficial to gaining an understanding of the financial performance of the Company.

9

The following table sets forth selected financial measures in accordance with GAAP and on a cash basis:

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

	Three Months Ended June 30,		Six Months Ended June 30,	
	2002	2001	2002	2001
Basic earnings per share	\$ 0.46	\$ 0.42	\$ 0.91	\$ 0.84
Diluted earnings per share	\$ 0.43	\$ 0.40	\$ 0.86	\$ 0.81
Basic cash earnings per share	\$ 0.51	\$ 0.47	\$ 1.01	\$ 0.94
Diluted cash earnings per share	\$ 0.48	\$ 0.45	\$ 0.95	\$ 0.91
Return on average assets	0.74%	0.77%	0.76%	0.80%
Cash basis return on average assets	0.84%	0.88%	0.85%	0.91%
Return on average equity	11.37%	11.40%	11.43%	11.58%
Cash Basis Return on average equity	12.67%	12.78%	12.71%	12.97%
Efficiency ratio	68.56%	67.21%	67.77%	66.04%
Cash basis efficiency ratio	65.51%	63.74%	64.66%	62.56%

OVERVIEW

Total assets increased \$81.7 million, or 9.5%, to \$944.0 million at June 30, 2002 from \$862.3 million at December 31, 2001. The increase was predominantly in overnight investments, US Agency securities, mortgage-backed securities ("MBSs"), commercial loans and consumer loans. Funding of this growth was primarily from increases in total deposits and borrowings from the FHLB, coupled with repayments of residential mortgage loans. Since the end of 2001, commercial loans increased \$20.1 million, or 8.4%, consumer loans increased \$3.2 million, or 5.2%, total deposits increased \$30.8 million, or 4.6%, and FHLB borrowings increased \$37.4 million, or 33.0%. Shareholders' equity was \$61.9 million at June 30, 2002, and represented 6.6% of total assets.

In June 2002, the Company through its subsidiary, BRI Statutory Trust II, issued \$5.0 million of trust preferred securities. These securities qualify as Tier I capital for regulatory purposes and can be used to support continued growth of the Company.

FINANCIAL CONDITION

-- Investments. Total investments (consisting of overnight investments, investment securities, MBSs and stock in the FHLB) totaled \$278.3 million, or 29.5% of total assets, at June 30, 2002, compared to \$210.7 million, or 24.4% of total assets, at December 31, 2001. All \$261.3 million of investment securities and MBSs at June 30, 2002 were classified as available for sale and carried a total of \$1.7 million in net unrealized gains. The increase of \$67.6 million, or 32.1%, in total investments was associated with the growth in total deposits and FHLB borrowings.

-- Loans. Total loans were \$615.6 million, or 65.2% of total assets, at June 30, 2002, compared to \$611.0 million, or 70.9% of total assets, at December 31, 2001. In response to low market interest rates, the Company experienced a sharp increase in residential mortgage loan prepayments during the first quarter of 2002. This led to the residential mortgage loan portfolio decreasing \$18.7 million, or 6.0%, during the first six months of 2002, as prepayments exceeded new loan purchases.

The commercial loan portfolio (consisting of commercial & industrial, small business, commercial real estate, multi-family real estate and construction loans) increased \$20.1 million, or 8.4%, during the first half of 2002. Particular emphasis is placed on the generation of small- to medium-sized commercial relationships (those relationships with \$5.0 million or less in loan commitments). The Bank is also active in small business lending (loans of \$250,000 or less) in which it utilizes credit scoring, in conjunction with traditional review standards, and employs streamlined documentation. The Bank is a participant in the U.S. Small Business Administration ("SBA") Preferred Lender Program in Rhode Island and the 7a Guarantee Loan Program in Massachusetts.

The consumer loan portfolio increased \$3.2 million, or 5.2%, reaching \$64.6 million at June 30, 2002. This increase was predominantly in home equity lines of credit, which grew \$5.1 million, or 18.0%, since December 31, 2001. While the origination efforts continue to be concentrated on commercial and consumer loan opportunities, the Bank also originates residential mortgage loans on a limited basis for its customers. Additionally, until such time as the Company can generate sufficient commercial and consumer loans to utilize available cash flow, or to otherwise meet investment objectives, it also intends to continue purchasing residential mortgage and automobile loans as opportunities develop.

The following is a breakdown of loans receivable:

	June 30, 2002	December 31, 2001
	-----	-----
	(In thousands)	
Residential mortgage loans:		
One- to four-family adjustable rate	\$270,450	\$285,589
One- to four-family fixed rate	19,879	23,306
	-----	-----
Subtotal	290,329	308,895
Premium on loans acquired	1,232	1,381
Net deferred loan origination fees	(66)	(64)
	-----	-----
Total residential mortgage loans	\$291,495	\$310,212
	=====	=====
Commercial loans:		
Commercial real estate - nonowner occupied	\$ 80,024	\$ 73,369
Commercial and industrial	57,436	53,677
Commercial real estate - owner occupied	48,722	46,698
Small business	26,466	24,122
Multi-family real estate	16,472	14,927
Construction	15,885	14,027
Leases and other	14,715	12,715
	-----	-----
Subtotal	259,720	239,535
Net deferred loan origination fees	(218)	(171)

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

Total commercial loans	\$259,502	\$239,364
Consumer loans:		
Home equity - lines of credit	\$ 33,584	\$ 28,460
Home equity - term loans	23,280	22,930
Automobile	4,760	6,335
Installment	1,074	1,240
Savings secured	624	656
Unsecured and other	663	1,153
Subtotal	63,985	60,774
Premium on loans acquired	143	192
Net deferred loan origination costs	453	422
Total consumer loans	\$ 64,581	\$ 61,388

11

-- Deposits and Borrowings. Total deposits increased by \$30.8 million, or 4.6%, during the first half of 2002, from \$670.4 million, or 77.8% of total assets, at December 31, 2001, to \$701.2 million, or 74.3% of total assets, at June 30, 2002. The decrease in the relative percentage of total assets resulted from first quarter total asset growth being primarily funded by FHLB borrowings. In addition, the composition of total deposits also changed since the end of 2001. Core deposit accounts (checking and savings accounts) increased \$37.4 million, or 8.9%, while certificates of deposit decreased \$6.6 million, or 2.7%. The Bank continues its strategy of emphasizing core deposit growth over certificate of deposit growth. The decline in certificates of deposits also reflects customer movement away from extended term deposits in response to the current low interest rate environment. At June 30, 2002, core deposit accounts comprised 65.5% of total deposits, compared to 63.0% of total deposits at December 31, 2001.

The following table sets forth certain information regarding deposits:

	June 30, 2002			December 31, 2001	
	Amount	Percent of Total	Weighted Average Rate	Amount	Percent of Total
(Dollars in thousands)					
NOW accounts	\$ 64,482	9.2%	0.98%	\$ 44,445	6.6%
Money market accounts	9,956	1.4%	1.34%	9,914	1.5%
Savings accounts	268,747	38.3%	1.87%	254,861	38.0%
Certificate of deposit accounts	241,627	34.5%	3.48%	248,268	37.0%
Total interest bearing deposits	584,812	83.4%	2.43%	557,488	83.1%
Noninterest bearing accounts	116,377	16.6%	--	112,925	16.9%

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

Total deposits	\$701,189	100.0%	2.02%	\$670,413	100.0%
=====					

The Company, through the Bank's membership in the FHLB, has access to a variety of borrowing alternatives, and management will from time to time take advantage of these opportunities to fund asset growth. During the first half of 2002, FHLB borrowings increased \$37.4 million, or 33.0%, as the Company sought to take advantage of lower, long-term borrowing rates to fund its asset growth. The proceeds from these new borrowings were primarily reinvested in hybrid ARM MBSs and allowed the Company to control the duration match of its balance sheet. However, on a long-term basis, the Company intends to concentrate on increasing its core deposits.

Asset Quality

-----

The definition of nonperforming assets includes nonperforming loans and other real estate owned ("OREO"). OREO consists of real estate acquired through foreclosure proceedings and real estate acquired through acceptance of a deed in lieu of foreclosure. Nonperforming loans are defined as nonaccrual loans, loans past due 90 days or more, but still accruing, and impaired loans. Under certain circumstances the Company may restructure the terms of a loan as a concession to a borrower. These restructured loans are considered impaired loans.

-- Nonperforming Assets. At June 30, 2002, the Company had nonperforming assets of \$902,000, which represented 0.10% of total assets. This compares to nonperforming assets of \$1.0 million, or .12% of total assets, at December 31, 2001. The level of nonperforming assets remains at a low level, but as the loan portfolio continues to grow and mature, or if economic conditions worsen, management believes it highly likely that the level of nonperforming assets will increase, as

12

will its level of charged-off loans. Nonperforming assets at June 30, 2002, consisted of nonaccrual commercial loans aggregating \$457,000, nonaccrual residential mortgage loans aggregating \$379,000 and nonaccrual consumer loans aggregating \$66,000. Included in nonaccrual loans were \$232,000 of impaired loans at June 30, 2002. There were no impaired loans at December 31, 2001. The Company maintained reserves of \$202,000 against impaired loans at June 30, 2002. The Company evaluates the underlying collateral of each nonperforming loan and continues to pursue the collection of interest and principal.

Delinquencies. At June 30, 2002, loans with an aggregate balance of \$106,000 were 60 to 89 days past due, a decrease of \$25,000, or 19.1%, from \$131,000 reported at December 31, 2001. The majority of these loans at both dates were residential mortgage loans and are secured.

The following table sets forth information regarding nonperforming assets and loans 60-89 days past due as to interest at the dates indicated.

	June 30,	December 31,
	2002	2001
	-----	-----

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

(Dollars in thousands)

Loans accounted for on a nonaccrual basis	\$ 902	\$ 753
Loans past due 90 days or more, but still accruing	--	--
Impaired loans (not included in nonaccrual loans)	--	--
	-----	-----
Total nonperforming loans	902	753
Other real estate owned	--	264
	-----	-----
Total nonperforming assets	\$ 902	\$1,017
	=====	=====
Delinquent loans 60-89 days past due	\$ 106	\$ 131
Nonperforming loans as a percent of total loans	.15%	.12%
Nonperforming assets as a percent of total assets	.10%	.12%
Delinquent loans 60-89 days past due as a percent of total loans	.02%	.02%

Adversely Classified Assets. The Company's management adversely classifies certain assets as "substandard," "doubtful" or "loss" based on criteria established under banking regulations. An asset is considered substandard if 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 existing 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.

At June 30, 2002, the Company had \$8.6 million of assets that were classified as substandard. This compares to \$8.7 million of assets that were classified as substandard at December 31, 2001. The Company had no assets that were classified as doubtful or loss at either date. Performing loans may or may not be adversely classified depending upon management's judgment with respect to each individual loan. At June 30, 2002, included in the \$8.6 million of assets that were classified as substandard, were \$7.7 million of performing loans. This compares to \$7.9 million of adversely classified performing assets as of December 31, 2001. Adversely classified assets are a reflection of commercial credit quality. An increase in adversely classified assets may lead to an increase in nonperforming assets and an increase in the provision for loan losses in future periods.

13

Allowance for Loan Losses

-----

During the first six months of 2002, the Company made provisions to the allowance for loan losses totaling \$850,000 and had \$108,000 of net charge-offs, bringing the balance in the allowance to \$9.3 million at June 30, 2002, compared to \$8.5 million at December 31, 2001. The allowance, expressed as a percentage of total loans, was 1.51% as of June 30, 2002,

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

compared to 1.40% at the prior year-end and stood at 1027.3% of nonperforming loans at June 30, 2002, compared to 1132.0% of nonperforming loans at December 31, 2001.

Assessing the adequacy of the allowance for loan losses involves substantial uncertainties and is based upon management's evaluation of the amounts required to meet estimated charge-offs in the loan portfolio after weighing various factors. Among these factors are the risk characteristics of the loan portfolio, the quality of specific loans, the level of nonaccruing loans, current economic conditions, trends in delinquencies and charge-offs, and the value of underlying collateral, all of which can change frequently. Based on this evaluation, management believes that the allowance for loan losses, as of June 30, 2002, is adequate.

While management evaluates currently available information in establishing the allowance for loan losses, future adjustments to the allowance may be necessary if conditions differ substantially from the assumptions used in making the evaluations. In addition, various regulatory agencies, as an integral part of their examination process, periodically review a financial institution's allowance for loan losses and carrying amounts of other real estate owned. Such agencies may require the financial institution to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

### RESULTS OF OPERATIONS

-----

The Company's operating results depend primarily on its "net interest income," or the difference between its interest income and its cost of money, and on the quality of its assets. Interest income depends on the average amount of interest-earning assets outstanding during the period and the interest rates earned thereon. Cost of money is a function of the average amount of deposits and borrowed money outstanding during the period and the interest rates paid thereon. Earnings are further influenced by the quality of assets, through the amount of interest income lost on nonaccrual loans, the amount of additions to the allowance for loan losses and the amount of expenses incurred as a result of resolving troubled assets.

### Three Months Ended June 30, 2002 and 2001

-----

-- Overview. The Company reported net income for the second quarter of 2002 of \$1.7 million, up \$142,000, or 9.0%, from the second quarter of 2001. Diluted earnings per common share were \$0.43 for the second quarter of 2002, compared to \$0.40 for the second quarter of 2001. Diluted cash earnings per common share were \$0.48 for the 2002 period, compared to \$0.45 for the 2001 period.

The Company reported a return on average assets of 0.74% and a return on average equity of 11.37% for the 2002 period, as compared to a return on average assets of 0.77% and a return on average equity of 11.40% for the 2001 period. Cash basis return on average assets and cash basis

14

return on average equity were 0.84% and 12.67% for the 2002 period, and 0.88% and 12.78% for the 2001 period, respectively.



## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

-- Net Interest Income. For the quarter ended June 30, 2002, net interest income was \$8.0 million, compared to \$7.1 million for the 2001 period. The net interest margin for the second quarter of 2002 was 3.66% compared to a net interest margin of 3.64% for the 2001 period. The increase in net interest income of \$919,000, or 12.9%, was primarily attributable to the continued growth of the Company. Average earnings assets were \$97.3 million, or 12.4%, higher and average interest-bearing liabilities were \$85.7 million, or 12.9%, higher than the comparable period a year earlier. The slight increase of 2 basis points in the net interest margin was primarily attributable to a drop in the average rate paid on certificates of deposit that occurred over the past year.

-- Interest Income. Investments. Total investment income was \$3.3 million for the quarter ended June 30, 2002, compared to \$3.0 million for the second quarter of 2001. This increase in total investment income of \$341,000, or 11.6%, was primarily attributable to an increase of \$57.9 million, or 44.6%, in the average balance of MBSs. The Company's investments are primarily comprised of US Agency securities or MBSs with remaining maturities or repricing periods of less than five years. In addition to assisting in overall tax planning, management believes that this composition, along with a structured maturity ladder, provides more stable earnings and predictable cash flows from the portfolio.

-- Interest Income. Loans. Interest from loans was \$10.2 million for the three months ended June 30, 2002, and represented a yield on total loans of 6.78%. This compares to \$11.3 million of interest, and a yield of 7.73%, for the second quarter of 2001. Declining market interest rates, coupled with residential mortgage loan prepayment activity, resulted in lower interest from the loan portfolio. Interest from residential mortgage loans decreased \$640,000, or 11.7%, commercial loan income decreased \$125,000, or 2.7%, and consumer and other loan income decreased \$240,000, or 20.0%, between the two quarters. Since its inception, the Bank has concentrated its origination efforts on commercial and consumer loan opportunities, while purchasing residential mortgage loans, and more recently automobile loans, as cash flows dictated. The average balance of the various components of the loan portfolio changed from the second quarter of 2001 as follows: commercial loans increased \$28.2 million, or 12.8%, and consumer and other loans increased \$2.5 million, or 4.0%, while residential mortgage loans decreased \$8.6 million, or 2.9%. As a result of declining market interest rates, the yields on the various loan portfolio components changed as follows: commercial loans decreased 115 basis points, to 7.19%; consumer and other loans decreased 180 basis points, to 5.98%, and residential mortgage loans decreased 66 basis points, to 6.61%.

-- Interest Expense. Interest paid on deposits and borrowings decreased \$1.6 million, or 22.3%, to \$5.5 million for the three months ended June 30, 2002, from \$7.1 million paid during the second quarter of 2001. The decrease in total interest expense was primarily attributable to a decrease in market interest rates, partially offset by an increase in the average balance of deposits and borrowings. The overall average cost for interest-bearing liabilities decreased 134 basis points from 4.30% for the second quarter of 2001 to 2.96% for the second quarter of 2002. Average costs for the various components of interest-bearing liabilities changed from the second quarter of 2001 as follows: money market accounts decreased 89 basis points, to 1.32%, savings accounts decreased 123 basis points, to 1.87%, certificate of deposit accounts decreased 203 basis points, to 3.51%, and borrowings decreased 66 basis points to 4.75%, while NOW accounts increased 8 basis points, to 0.66%. Meanwhile, the average balance of interest-bearing liabilities increased \$85.7 million, from

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

\$662.1 million in the second quarter of 2001 to \$747.8 million in the second quarter of 2002, as savings account growth and borrowings were utilized to fund much of the asset growth. Liability costs are dependent on a number of factors including general economic conditions, national and local interest rates, competition in the local deposit marketplace, interest rate tiers offered and the Company's cash flow needs.

-- Provision for Loan Losses. The provision for loan losses was \$450,000 for the quarter ended June 30, 2002, up \$98,000, or 27.8%, from the same quarter last year. Growth in the commercial loan portfolio increased at an annualized rate of 28.7% during the second quarter of 2002. As the loan portfolio continues to grow and mature, or if economic conditions worsen, management believes it highly likely that the level of nonperforming assets will increase, which in turn may lead to increases in the provision for loan losses in future periods. Management evaluates several factors including new loan originations, actual and estimated charge-offs, the risk characteristics of the loan portfolio and general economic conditions when determining the provision for each quarter. Also see discussion under "Allowance for Loan Losses."

-- Noninterest Income. Total noninterest income increased \$212,000, or 16.2%, to \$1.5 million for the second quarter of 2002, from \$1.3 million for the 2001 quarter. The Bank's purchase of \$10.0 million of bank-owned life insurance during the first quarter of 2002 resulted in \$142,000 of noninterest income during the second quarter. This income was not present during the second quarter of 2001. In addition, Commissions on Nondeposit Investment Products increased \$100,000, or 137.0%, compared to the second quarter of 2001 as a result of efforts begun in 2001 to revitalize the program. Partially offsetting these increases was a decrease of \$62,000, or 29.1%, in Other Income that resulted primarily from a decrease in card services income following the termination of a student travel card program with FirstDebit Corporation. Service Charges on Deposit Accounts, which represent the largest source of noninterest income for the Company, remained steady, rising \$18,000, or 2.0%, from \$894,000 for the quarter ended June 30, 2001, to \$912,000 for the same period in 2002, as core deposit accounts continued to grow.

-- Noninterest Expense. Total noninterest expense for the second quarter of 2002 increased \$889,000, or 15.7%, to \$6.5 million from \$5.6 million in 2001. This increase occurred primarily in the following areas: Salaries and Benefits (up \$542,000, or 20.3%), Occupancy and Equipment (up \$96,000, or 14.9%) and Professional Services (up \$231,000, or 124.9%). During 2001 the Bank experienced substantial growth in both loans and core deposits that resulted in the increased operating costs evidenced in the second quarter of 2002. In addition, the Bank has retained professional assistance to evaluate its data processing alternatives and to develop and test software being deployed in conjunction with its CampusMate(TM) product. As a result, the Company's cash basis efficiency ratio increased 177 basis points, from 63.74% for the second quarter of 2001 to 65.51% for the second quarter of 2002.

-- Income Tax Expense. Income tax expense of \$834,000 was recorded for the quarter ended June 30, 2002, compared to \$832,000 for the 2001 period. This represented total effective tax rates of 33.0% and 34.6%, respectively. Tax-favored income from U.S. Agency securities, along with the utilization of a Rhode Island passive investment company, has reduced the Company's effective tax rate from the 39.9% combined statutory federal and state tax rates. The 2002 period also benefited from the tax-favored status of the Company's investment in bank-owned life insurance.

Six Months Ended June 30, 2002 and 2001  
-----

-- Overview. Net income for the first half of 2002, increased \$287,000, or 9.2%, to \$3.4 million, or \$0.86 per diluted common share, from \$3.1 million, or \$0.81 per diluted common share, for the first half of 2001. Diluted cash earnings per common share were \$0.95 for the 2002 period, compared to \$0.91 for the 2001 period.

This performance represented a return on average assets of 0.76% and a return on average equity of 11.43% for the 2002 period, as compared to a return on average assets of 0.80% and a return on average equity of 11.58% for the 2001 period. Cash basis return on average assets and cash basis return on average equity were 0.85% and 12.71% for the 2002 period, and 0.91% and 12.97% for the 2001 period, respectively.

-- Net Interest Income. For the six months ended June 30, 2002, net interest income was \$15.6 million, compared to \$14.3 million for the first half of 2001. The net interest margin for the first six months of 2002 was 3.64% compared to a net interest margin of 3.81% for the 2001 period. The increase in net interest income of \$1.3 million, or 9.3%, was primarily attributable to the overall growth of the Company. Average earning assets increased \$108.3 million, or 14.3%, and average interest-bearing liabilities increased \$94.1 million, or 14.7%, over the comparable period a year earlier. The decrease of 17 basis points in the net interest margin was primarily caused by the dramatic drop in market interest rates occurring in 2001, coupled with the asset-sensitive nature of the Company's balance sheet.

-- Interest Income. Investments. Total investment income was \$6.2 million for the six months ended June 30, 2002, compared to \$5.9 million for the first half of 2001. This increase in total investment income of \$324,000, or 5.5%, was primarily attributable to a \$53.1 million, or 42.3%, increase in the average balance of MBSs. Meanwhile, the overall yield on investments decreased 146 basis points, from 6.26% in 2001, to 4.80% in 2002, in response to dramatically lower market interest rates.

-- Interest Income. Loans. Interest from loans was \$20.4 million for the six months ended June 30, 2002, and represented a yield on total loans of 6.79%. This compares to \$22.4 million of interest, and a yield of 7.96%, for the first half of 2001. This decrease of \$2.0 million, or 9.1%, in interest on loans was due primarily to a decrease in the average yield on loans resulting from the dramatic drop in market interest rates over the past year. The average yield on the various components of the loan portfolio changed as follows: residential mortgage loans decreased 81 basis points, to 6.61%; commercial loans decreased 140 basis points, to 7.20%; and consumer and other loans decreased 213 basis points, to 6.07%. The effect of the decreases in average yield was partially offset by increase in the average balance of loans. The average balance of the various components of the loan portfolio changed as follows: residential mortgage loans increased \$7.4 million, or 2.5%, commercial loans increased \$27.0 million, or 12.4%, and consumer and other loans increased \$2.3 million, or 3.8%. The Company has continued to concentrate its origination efforts on commercial and consumer loan opportunities, but also originates residential mortgage loans for its portfolio on a limited basis.

-- Interest Expense. Interest paid on deposits and borrowings decreased \$3.1 million, or 21.7%, to \$11.0 million for the six months ended

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

June 30, 2002, compared to \$14.1 million for the same period during 2001. The decrease in total interest was also primarily attributable to the dramatic drop in market interest rates over the past year and was partially offset by growth in checking and

17

savings deposits, along with the use of borrowings to fund the overall growth of the Company. The overall average cost for interest-bearing liabilities decreased 141 basis points from 4.43% for the first half of 2001, to 3.02% for the first half of 2002. Deposit costs are dependent on a number of factors including general economic conditions, national and local interest rates, competition in the local marketplace, interest rate tiers offered, and the Company's cash flow needs. Partially offsetting the effect of the decline in market interest rates, the average balance of interest-bearing liabilities increased \$94.1 million, from \$640.3 million in 2001, to \$734.4 million in 2002. The Company continued to experience strong average balance growth in core deposit accounts, specifically noninterest bearing demand deposit accounts (up \$16.2 million, or 16.8%) and savings accounts (up \$46.1 million, or 20.6%). In addition, the Company increased its utilization of FHLB borrowings (up \$58.5 million, or 66.9%).

-- Provision for Loan Losses. The provision for loan losses was \$850,000 for the six months ended June 30, 2002, compared to \$840,000 for the same period last year. The allowance, expressed as a percentage of total loans, was 1.51% as of June 30, 2002, compared to 1.40% at the prior year-end and stood at 1027.3% of nonperforming loans at June 30, 2002, compared to 1132.0% of nonperforming loans at December 31, 2001. Management evaluates several factors including new loan originations, actual and estimated charge-offs, and the risk characteristics of the loan portfolio when determining the provision for the quarter. Also see discussion under "Allowance for Loan Losses."

-- Noninterest Income. Total noninterest income increased \$676,000, or 28.1%, from the first half of 2001, to \$3.1 million for the first six months of 2002. Service charges on deposit accounts, which represents the largest source of noninterest income, rose \$107,000, or 6.4%, from \$1.7 million for the six months ended June 30, 2001, to \$1.8 million for the same period in 2002, primarily as a result of continued growth in core deposit accounts. Commissions on Nondeposit Investment Products increased \$276,000, or 189.0%, in response to rejuvenation efforts begun in 2001. Additionally, the Bank's purchase of \$10.0 million of bank-owned life insurance during the first quarter of 2002, resulted in \$237,000 of noninterest income for the six month period.

-- Noninterest Expense. Noninterest expenses for the first half of 2002 increased a total of \$1.6 million, or 14.9%, to \$12.7 million. This increase occurred primarily as a result of the overall growth of the Company, along with development of new products, and was centered in the following areas: Salaries and Benefits (up \$939,000, or 17.7%), Occupancy and Equipment (up \$151,000, or 11.6%), Marketing (up \$124,000, or 22.3%) and Professional Services (up \$398,000, or 99.5%). Partially offsetting these increases was a decrease in: Other Real Estate Owned Expense (down \$57,000, or 89.1%). The Company's cash basis efficiency ratio increased to 64.66% for the 2002 period, from 62.56% for the 2001 period.

-- Income Tax Expense. The Company recorded income tax expense of \$1.8 million for the first half of 2002, compared to \$1.7 million for the same period during 2001. This represented total effective tax rates of

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

34.0% and 35.2%, respectively. Tax-favored income from U.S. Agency securities and bank-owned life insurance, along with its utilization of a Rhode Island passive investment company, has reduced the Company's effective tax rate from the 39.9% combined statutory federal and state tax rates.

18

### LIQUIDITY AND CAPITAL RESOURCES

-----

-- Liquidity. Liquidity is defined as the ability to meet current and future financial obligations of a short-term nature. The Company further defines liquidity as the ability to respond to the needs of depositors and borrowers, as well as to earnings enhancement opportunities, in a changing marketplace.

The primary source of funds for the payment of dividends and expenses by the Company is dividends paid to it by the Bank. Bank regulatory authorities generally restrict the amounts available for payment of dividends if the effect thereof would cause the capital of the Bank to be reduced below applicable capital requirements. These restrictions indirectly affect the Company's ability to pay dividends. The primary sources of liquidity for the Bank consist of deposit inflows, loan repayments, borrowed funds, maturity of investment securities and sales of securities from the available for sale portfolio. Management believes that these sources are sufficient to fund the Bank's lending and investment activities.

Management is responsible for establishing and monitoring liquidity targets as well as strategies and tactics to meet these targets. In general, the Company maintains a high degree of flexibility. At June 30, 2002, overnight investments, investment securities and MBSs available for sale amounted to \$270.6 million, or 28.7% of total assets. This compares to \$205.0 million, or 23.8% of total assets at December 31, 2001. The Bank is a member of the FHLB and, as such, has access to both short- and long-term borrowings. In addition, the Bank maintains a line of credit at the FHLB as well as a line of credit with a correspondent bank. There have been no adverse trends in the Company's liquidity or capital reserves. Management believes that the Company has adequate liquidity to meet its commitments.

-- Capital Resources. Total shareholders' equity of the Company at June 30, 2002 was \$61.9 million, as compared to \$59.1 million at December 31, 2001. This increase of \$2.8 million was the result of net income for the period of \$3.4 million, less dividends of \$977,000 and changes in unrealized gains on investment securities of \$257,000.

All FDIC-insured institutions must meet specified minimal capital requirements. These regulations require banks to maintain a minimum leverage capital ratio. In addition, the FDIC has adopted capital guidelines based upon ratios of a bank's capital to total assets adjusted for risk. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. These regulations require banks to maintain minimum capital levels for capital adequacy purposes and higher capital levels to be considered "well capitalized."

Capital guidelines have also been issued by the Federal Reserve Board

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

("FRB") for bank holding companies. These guidelines require the Company to maintain minimum capital levels for capital adequacy purposes. In general, the FRB has adopted substantially identical capital adequacy guidelines as the FDIC. Such standards are applicable to bank holding companies and their bank subsidiaries on a consolidated basis.

19

As of June 30, 2002, the Company and the Bank met all applicable minimum capital requirements and were considered "well capitalized" by both the FRB and the FDIC. The Company's and the Bank's actual and required capital amounts and ratios are as follows:

	Actual		Minimum Required For Capital Adequacy Purposes		Minimum Re To Be Cons "Well Capit
	Amount	Ratio	Amount	Ratio	Amount
At June 30, 2002:					
Bancorp Rhode Island, Inc.					
Tier I capital (to average assets)	\$58,602	6.39%	\$27,505	3.00%	\$45,841
Tier I capital (to risk weighted assets)	58,602	10.39%	22,554	4.00%	33,830
Total capital (to risk weighted assets)	65,672	11.65%	45,107	8.00%	56,384
Bank Rhode Island					
Tier I capital (to average assets)	\$52,614	5.75%	\$27,456	3.00%	\$45,760
Tier I capital (to risk weighted assets)	52,614	9.34%	22,537	4.00%	33,806
Total capital (to risk weighted assets)	59,684	10.59%	45,074	8.00%	56,343
At December 31, 2001:					
Bancorp Rhode Island, Inc.					
Tier I capital (to average assets)	\$50,433	5.93%	\$25,508	3.00%	\$42,513
Tier I capital (to risk weighted assets)	50,433	9.86%	20,462	4.00%	30,694
Total capital (to risk weighted assets)	56,803	11.10%	40,925	8.00%	51,156
Bank Rhode Island					
Tier I capital (to average assets)	\$49,702	5.84%	\$25,526	3.00%	\$42,544
Tier I capital (to risk weighted assets)	49,702	9.72%	20,458	4.00%	30,687
Total capital (to risk weighted assets)	56,121	10.97%	40,916	8.00%	51,145

20

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

### ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

#### INTEREST RATE RISK

-----

The principal market risk facing the Company is interest rate risk. The Company's objective regarding interest rate risk is to manage its assets and funding sources to produce results which are consistent with its liquidity, capital adequacy, growth and profitability goals, while minimizing the vulnerability of its operations to changes in market interest rates. The Bank's Asset/Liability Committee ("ALCO") manages the Company's interest rate risk position using both income simulation and interest rate sensitivity "gap" analysis. The ALCO has established internal parameters for monitoring the income simulation and gap analysis. These guidelines serve as benchmarks for evaluating actions to balance the current position against overall strategic goals. The ALCO monitors current exposures and reports these to the Board of Directors.

Simulation is used as the primary tool for measuring the interest rate risk inherent in the Company's balance sheet at a given point in time by showing the effect on net interest income, over a 24-month period, of interest rate ramps of up to 200 basis points. These simulations take into account repricing, maturity and prepayment characteristics of individual products. The ALCO reviews simulation results to determine whether the downside exposure resulting from changes in market interest rates remains within established tolerance levels over both a 12-month and 24-month horizon, and develops appropriate strategies to manage this exposure. The Company's limits on interest rate risk specify that if interest rates were to shift up or down 200 basis points over a 12-month period, estimated net interest income for those 12 months and the subsequent 12 months, should decline by no more than 5.0% or 10.0%, respectively. As of June 30, 2002, net interest income simulation indicated that the Company's exposure to changing interest rates was outside of the 10% tolerance level established for the second year of a 200 basis point decline. This exposure primarily results from the unusually low current rates paid on deposit accounts and the extremely high prepayment speeds anticipated for mortgage-related assets if market rates declined 200 basis points. The current rates on many deposit accounts are so low, that they cannot decline 200 basis points without becoming negative. This results in a floor of zero percent for these deposit accounts, and this floor causes compression of the net interest margin for modeling purposes. The ALCO reviews the methodology utilized for calculating interest rate risk exposure and may, from time to time, adopt modifications to this methodology. While the ALCO reviews simulation assumptions and methodology to ensure that they reflect historical experience, it should be noted that income simulation may not always prove to be an accurate indicator of interest rate risk because the actual repricing, maturity and prepayment characteristics of individual products may differ from the estimates used in the simulations.

21

The following table presents the estimated impact of interest rate ramps on the Company's estimated net interest income over a 24-month period beginning July 1, 2002:

Estimated Exposure  
to Net Interest Income

## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

	Dollar Change	Percent Change
	-----	-----
(Dollars in thousands)		
Initial 12-Month Period:		
Up 200 basis points	\$ 577	1.85%
Up 100 basis points	370	1.19%
Down 100 basis points	(451)	(1.44%)
Down 200 basis points	(969)	(3.11%)

Subsequent 12-Month Period:

Up 200 basis points	\$ 817	2.73%
Up 100 basis points	747	2.50%
Down 100 basis points	(1,468)	(4.91%)
Down 200 basis points	(3,764)	(12.59%)

The Company also uses interest rate sensitivity gap analysis to provide a more general overview of its interest rate risk profile. The interest rate sensitivity gap is defined as the difference between interest-earning assets and interest-bearing liabilities maturing or repricing within a given time period. At June 30, 2002, the Company's one year cumulative gap was a positive \$90.9 million, or 9.63% of total assets.

For additional discussion on interest rate risk see the section titled "Asset and Liability Management" contained on pages 39 to 41 of the Company's 2001 Annual Report to Shareholders.

22

BANCORP RHODE ISLAND, INC.  
Other Information

PART II. Other Information

ITEM 1. LEGAL PROCEEDINGS

There are no material pending legal proceedings to which the Company or its subsidiaries are a party, or to which any of their property is subject, other than ordinary routine litigation incidental to the business of banking.

ITEM 2. CHANGE IN SECURITIES

No information to report.

ITEM 3. DEFAULT UPON SENIOR SECURITIES

No defaults upon senior securities have taken place.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF THE SECURITY HOLDERS

At the Annual Meeting of Shareholders, held May 15, 2002, holders of Common Stock elected the Board's nominees to the Board of Directors, approved the 2002 Incentive and Nonqualified Stock Option Plan, amended the Non-Employee Director Stock Option Plan



## Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

and ratified the appointment of independent public accountants.

The vote for Class III director nominees with terms expiring in 2005 was:

	FOR	WITHHELD
Anthony F. Andrade	3,508,110	27,780
Malcolm G. Chace	3,509,110	26,780
Ernest J. Chorneyei, Jr.	3,507,960	27,930
Edward J. Mack, II	3,507,510	28,380
Merrill W. Sherman	3,507,570	28,320

The vote for Class I director nominee with a term expiring in 2003 was:

	FOR	WITHHELD
Karen Adams	3,504,820	31,070

The vote for approving the 2002 Incentive and Nonqualified Stock Option Plan was:

FOR	AGAINST	ABSTAIN
2,724,208	122,703	26,240

23

#### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF THE SECURITY HOLDERS (continued)

The vote for amending the Non-Employee Director Stock Plan was:

FOR	AGAINST	ABSTAIN
2,782,023	62,289	28,840

The vote for ratifying the appointment of KPMG LLP as independent public accountants for the Company was:

FOR	AGAINST	ABSTAIN
3,524,830	8,200	2,860

#### ITEM 5. OTHER INFORMATION

No information to report.

#### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

##### (a) Exhibits

- 10.6(a) Amendment to Amended and Restated Non-Employee Director Stock Plan.
- 10.13 2002 Incentive and Nonqualified Stock Option Plan.
- 99.1 Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

##### (b) Reports on Form 8-K

Edgar Filing: BANCORP RHODE ISLAND INC - Form 10-Q

No information to report.

24

BANCORP RHODE ISLAND, INC.

SIGNATURES

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

Bancorp Rhode Island, Inc.

August 7, 2002

-----

(Date)

By: /s/ Merrill W. Sherman

-----

Merrill W. Sherman  
President and  
Chief Executive Officer

August 7, 2002

-----

(Date)

By: /s/ Albert R. Rietheimer

-----

Albert R. Rietheimer  
Chief Financial Officer  
and Treasurer

25