HINGHAM INSTITUTION FOR SAVINGS

ANNUAL REPORT

1997

A vision for the future. Values rooted in the past.

Technology is dramatically changing the way we live. At an astonishing pace, we have become computer literate. Banking by Automated Teller Machines (ATMs) is a basic example of these changes. Not so long ago, few among us were comfortable making deposits or withdrawals by pushing buttons on a machine. Now it's second nature and an expected convenience.

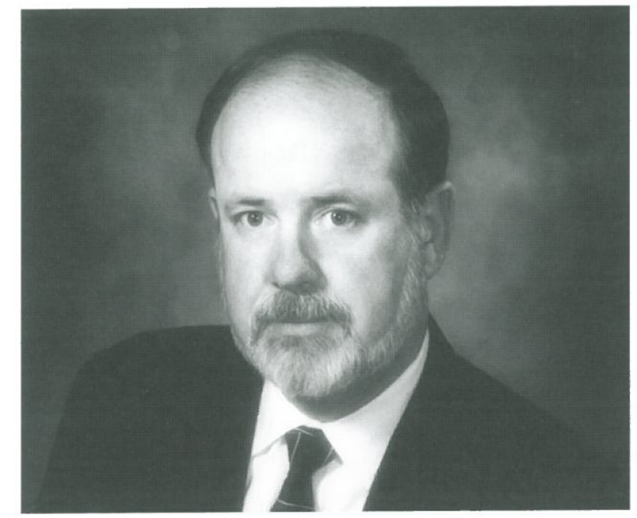
Yet within this age of lightening-fast change, it serves us well to pause for a moment and reflect. Yes, electronics are helping to improve our quality of life, but impersonal machines can never replace basic human interaction.

Our humanity, after all, is what distinguishes us. How we talk, smile, care about, and relate to one another makes us companions and friends. It is what allows us to enjoy the company of workmates, family members, and customers.

As we present our 1997 Annual Report, we are proud to elaborate on our vision for the future and the technological advances we are introducing to better serve you.

At the same time, we wish to celebrate the values that have built the reputation of Hingham Institution for Savings over the past 163 years. To do this credibly, we must acknowledge and commend the people who work here. Without our friendly, helpful, and caring staff, this bank would not be the success it is today. Nor would it be able to look forward confidently to continued growth tomorrow.

From the President



To Our Stockholders

During 1997 we not only achieved record financial success but also invested heavily in technological improvements that will position us for future success.

Our net income for 1997 was $2.7 million, a 30% increase over that of 1996. These are the highest earnings in our 163 year history. All other indicia of success were equally impressive. The increase in earnings was fueled principally by the vigorous growth rate of our assets, in excess of 10%, and the effective control of operating expenses. Our total assets increased from $202 million to $223 million. Our efficiency ratio (non-interest operating expenses as a percent of operating income) of 49.67% compares quite favorably with that of our competitors. We were successful in increasing our loan portfolio by 14% and, at the same time, increasing the yield on that portfolio. Our Return on Assets increased from 1.10% to 1.26%, and our Return on Equity increased from 11.06% to 13.00%. Our earnings per share increased from $1.57 to $2.04.

These achievements translated into concrete and immediate benefits to our stockholders. We were able to improve the declared dividends to stockholders from $0.45 per share to $0.59 per share, a 31% increase. The market value of our stock increased by over 50%, far outpacing all of the major indexes.

While our accomplishments of the past year are noteworthy, we are fully cognizant of the increasing intensity of competition. We realize that continued progress will require continued improvement. This can only be achieved by the blending of our traditional personal service with an increased utilization of state-of-the-art technology. During 1997 we invested heavily in efforts to upgrade our technology. We completed a conversion of our data processing to a data center which is capable of supporting the most sophisticated applications. We installed new wide and local area networks as well as new hardware in all of our locations. This platform is allowing us to implement a number of product improvements. This improvement entailed a major investment of time and attention from all of our staff as well as a significant financial commitment. These efforts have positioned us to credibly claim a level of product sophistication that when combined with our level of personal service, make us the most attractive banking alternative in our local market. We are confident that consumers will continue to prefer a local institution to a national chain if the local bank can offer both technological competence and individual attention.

Our rightful pride in the accomplishments of 1997 is muted by the deep sadness we all experienced with the loss of Robert H. Gaughen, Sr. in November. My father's courage and persistence were critical elements in our bank's survival and success during turbulent times. His great enthusiasm for work and for life remains an inspiration for his family, his fellow board members, and for all of us who work at the bank. We will honor his memory by renewing our efforts to develop a bank that uniquely provides for the needs of our stockholders, employees, and community well into the next century.

Thanking you for your continued support,

I am,

Very truly yours,

Robert H. Gaughen, Jr.
President and C.E.O.

Technology with a purpose.

Hingham Institution for Savings won't invest in new technology if the end result isn't better service for our customers. To that end, we are introducing new electronics in a sensible and practical manner.

For instance, we now have a MasterMoney® ATM/Debit Card. It's a Hingham Institution for Savings bank card that's as simple to use as a credit card but works like a check. It allows you to access cash at any ATM machine where you see the NYCE® and CIRRUS® network symbols. In addition, you can pay for purchases where you see the MasterCard® symbol. Your account at Hingham is automatically debited, eliminating the need to write a check. This makes banking and shopping easier and more convenient.

On the commercial side, our new technology means we can offer local businesses a Commercial Sweep Account. With this capability, allocated funds in business customers' accounts can be moved each night into higher earning accounts such as Money Market accounts. The great benefit is that the process is automatic, and business customers' money is working hard for them while they sleep.

Banking with a personality.

Savings bank passbooks have been around for as long as there have been savings banks. At Hingham, we're happy to say that many still find them invaluable and use them on a regular basis. For our customers, it's an excellent way to keep track of their savings and to encourage a new generation to develop the savings habit. For us, it's a great way to keep in touch with our customers.

Personal contact is important. It means we can put a face to the account, a name to the transaction, and show neighborly concern when appropriate. The essence of community banking, after all, is people, not dollars and cents. It is reflected in the gratitude of the senior citizen we protect from a scam and the enthusiasm of the grammar school students that we visit each week.

Our customers look to the trusted relationship they have built with us. They know, for example, that our passbooks come with no fees, that rates are always fair, and our loan terms are flexible.

We recently introduced a "Completely Free Checking" service and, unlike many big banks, we return your canceled checks. You can still buy Savings Bonds in any branch. If this sounds like friendly, caring banking, then it has served our purpose admirably. We wouldn't have it any other way.

Reaching out across the branches.

Our data processing system, which at one time was considered quite sophisticated, has now been replaced with a state-of-the-art data processing center that makes us more efficient and more productive.

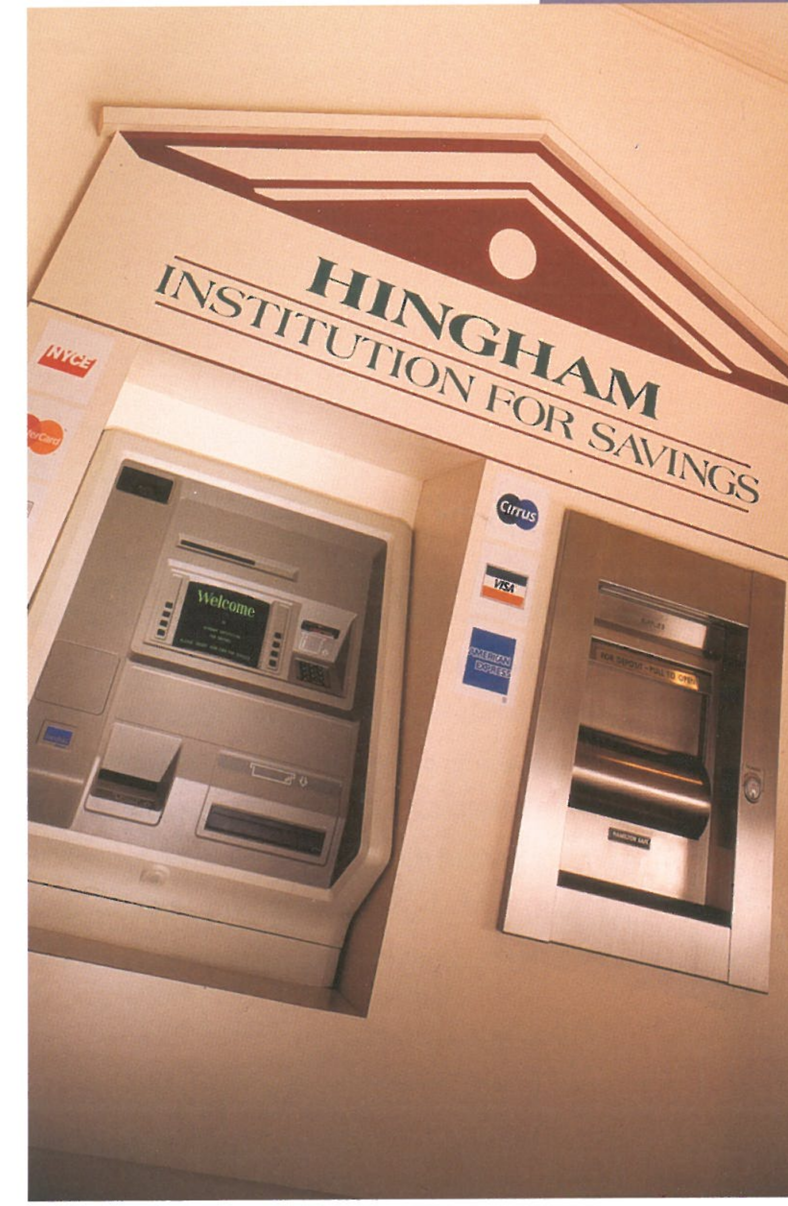
We have improved our computer systems by having Local Area Networks and Wide Area Networks installed to link our departments internally and allow us to communicate instantly and seamlessly with our branch offices. So whichever branch you visit, we will have the relevant information right at our fingertips, resulting in faster and more accurate transactions.

We also have the technology in place to offer combined, easy-to-follow statement listings of your monthly account balances and transactions. At a glance, you'll know the status of your savings, checking, CDs, loans, and other bank accounts.

Thanks to sophisticated technology, we now are capable of implementing a signature verification program which is virtually foolproof and provides excellent protection for every customer.

Soon we will be introducing Telephone Banking, allowing customers to transfer funds, get account information, and make loan payments without writing checks. All you do is make one convenient phone call any time day or night.

Reaching out across the harbor.



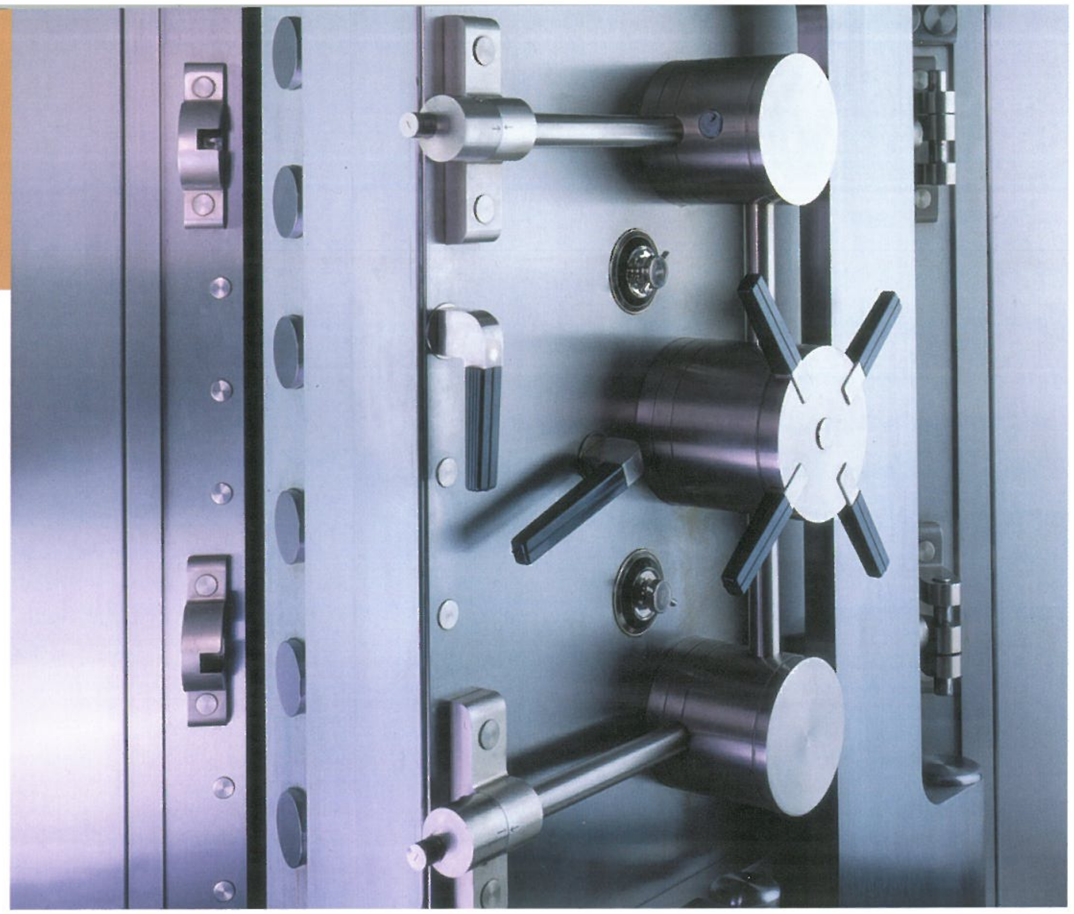
Large, multinational financial institutions can boast of their global reach. Our claims are more modest in scope but more personal in focus. We are aggressively working to better serve our customers wherever we can.

Those who travel back and forth to Boston by the Hingham commuter boats will have noticed the Hingham Institution for Savings ATM machine at the dockside. Judging by the transaction records, it has proven to be a terrific convenience for many.

It is said that if a bank makes a point of thoroughly understanding the community, it can successfully meet its needs. This is one instance where that has proven to be correct. As an added benefit, we never surcharge for using our ATMs – a welcome difference from many of the large national chains.

Our continued emphasis on residential mortgages is also in keeping with our determination to reach out to our neighbors. We continue to be a leader in financing home ownership in neighborhoods throughout our area.

What's more, a mortgage from Hingham Institution for Savings is likely to stay here and not be sold to an out-of-state bank or investor. Our customers tell us that there is nothing more frustrating than dealing with an out-of-area loan servicer with an impenetrable voice mail system. If our loan customers have a question, they can call us or stop by for a visit. In either case, they get a human response. It's that easy.



Toward a stronger community.

As regional banks continue to consolidate into even larger institutions which place greater emphasis on self-described efforts to become "broadly integrated and diversified financial service providers on a global scale," we provide an excellent alternative.

We believe, for instance, that one of the best ways to serve our community is to help build the businesses within it. At Hingham Institution for Savings we have a very active commercial lending program.

No bank on the South Shore knows the local commercial real estate climate better or is more current on expansion and development opportunities. We will continue to reach out to area businesses so that we can better understand their needs and goals.

While commerce is fundamentally important, we understand that there are other sectors that are vital to the life of our community. Hingham Institution for Savings is proud to be associated in a meaningful way with many area not-for-profit organizations such as Habitat for Humanity, The Thayer House Assisted Living Facility, Glastonbury Abbey, the Montessori School, and the South Shore Conservatory.

We are convinced that our bank can thrive and grow only to the extent that all of our community thrives and grows. Neither can succeed independent of the other. This is a philosophy we live by every day.

Toward a brighter future.

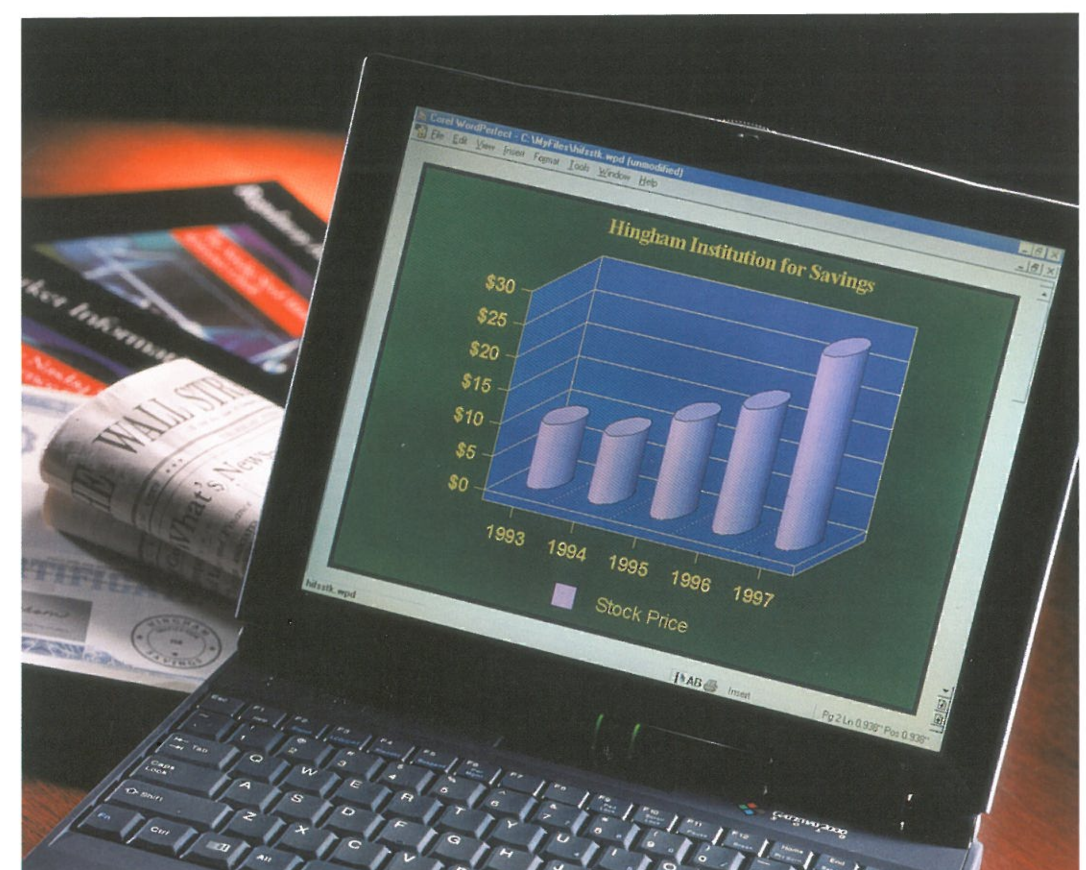
Hingham Institution will continue to deliver quality financial services to our customers, including new technology, as it becomes available. This past year we have installed the necessary technological platform on which to build. In the immediate future we anticipate the introduction of electronic banking products such as Home Banking through PCs and Voice Response Banking via a 24-hour direct phone link.

Sophisticated services such as these will allow the bank to remain competitive and be attractive to an ever-increasing customer base. In fact, as a computer-literate younger generation matures, it expects such services.

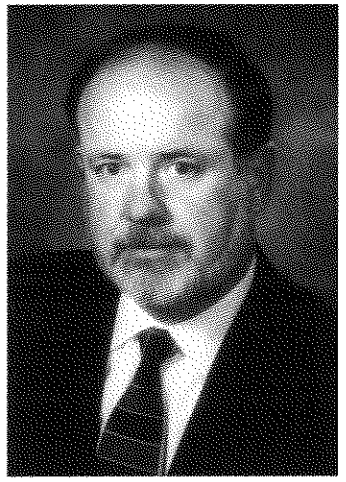
We will also remain true to our commitment to provide friendly, personable service on all levels throughout the bank. We feel we know our regular customers by name, and every member of our staff is accessible to answer questions and help with applications and forms.

Innovative services are not possible without a dedicated and thoroughly professional staff, and we consider ourselves extremely fortunate in this area. Not only are they skilled, they have many years of experience and loyalty to the bank.

As a local bank, we are extremely proud of the role we play in our communities. While information technology will change the way we deliver services, it won't change the neighborly spirit that characterizes Hingham Institution for Savings.

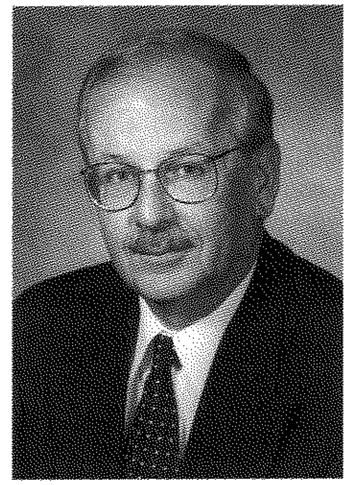


Senior Officers

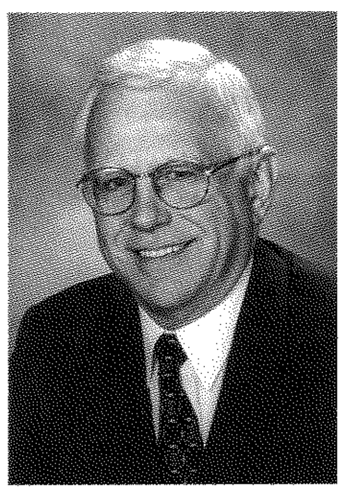


Robert H. Gaughen, Jr.
President and C.E.O.

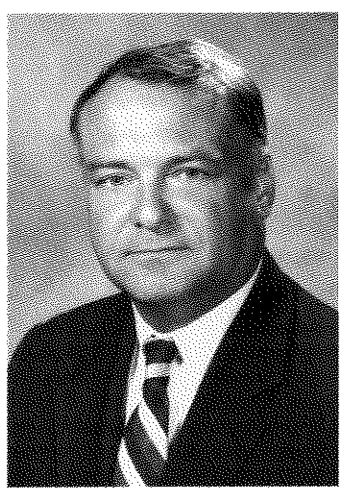
Deborah J. Jackson
Sr. Vice President and Treasurer



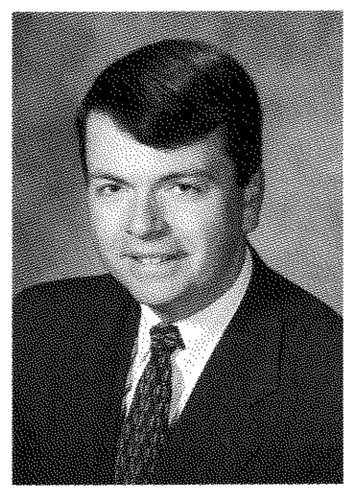
William M. Donovan, Jr.
Vice President-Administration



Edward P. Zec
Vice President-Branch Operations

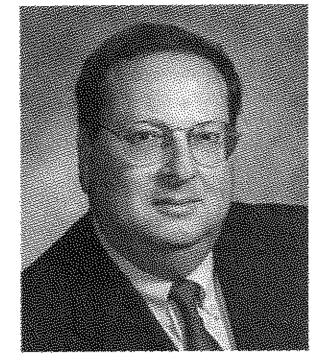


Peter R. Smollett
Vice President-Lending

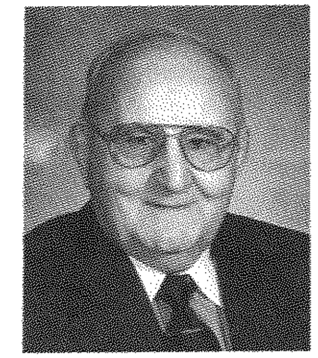


Michael J. Sinclair
Retail Lending Officer

Directors

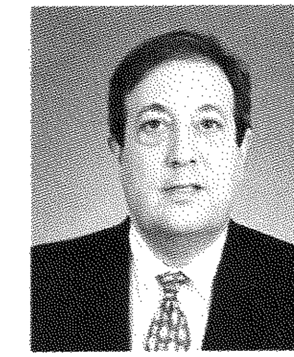


Howard M. Berger, Esq.*

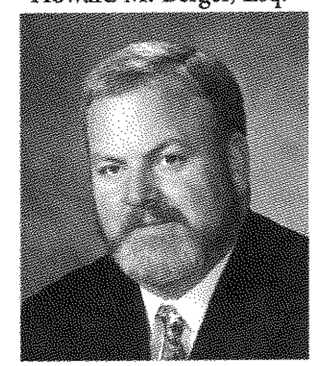


James V. Consentino

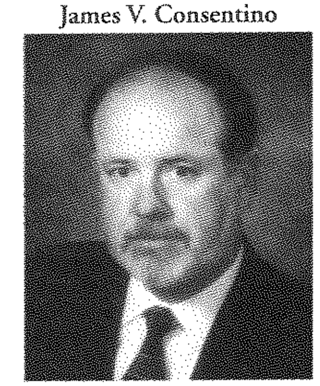
Marion J. Fahey



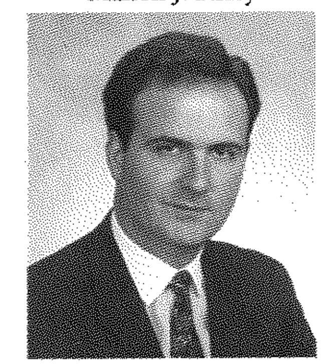
Ronald D. Falcione



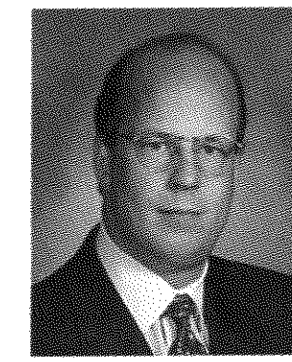
Kevin W. Gaughen, Esq.



Robert H. Gaughen, Jr., Esq.

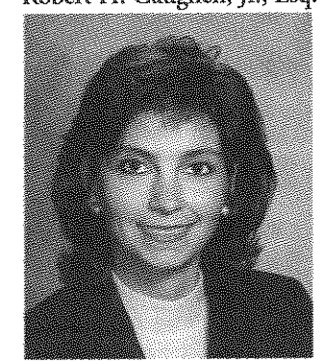


Julio R. Hernando, Esq.



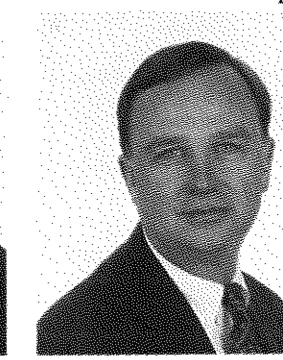
Robert A. Lane, Esq.

Warren B. Noble



Stacy M. Page

Edward L. Sparda



Donald E. Staszko

Donald M. Tardiff, M.D.

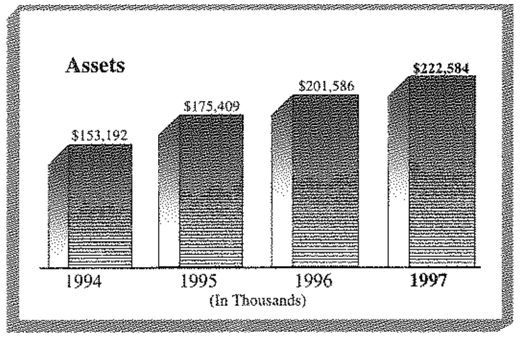
James R. White

Geoffrey C. Wilkinson, Sr.

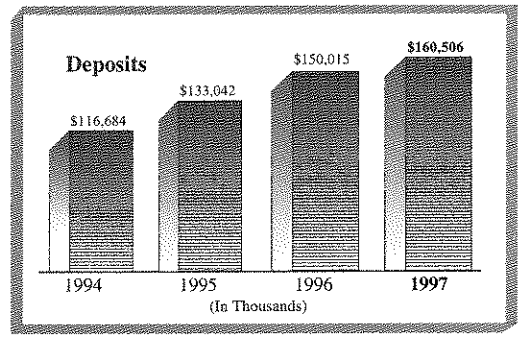
Jacqueline M. Youngworth

** Nominee*

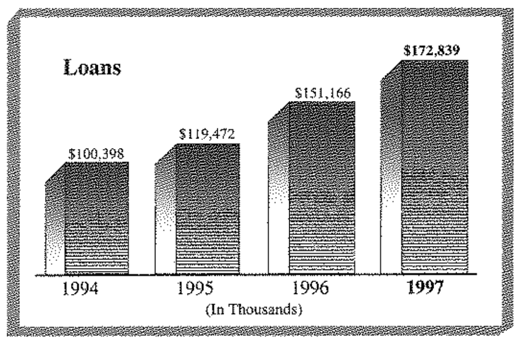
Financial Highlights



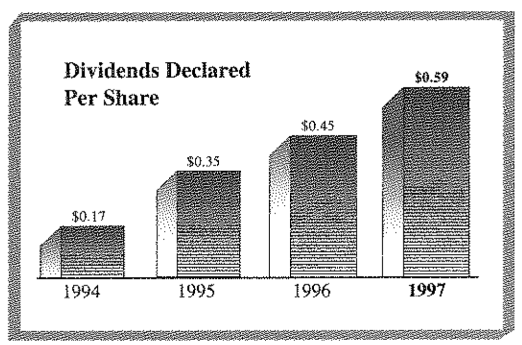
Solid asset growth continued in 1997 with the loan portfolio accounting for nearly 78% of total assets. Meanwhile, the bank continued to surpass all regulatory capital maintenance requirements and reported capital to assets of 9.60%.



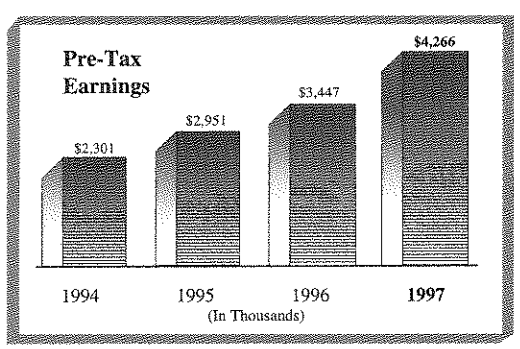
1997 marks the third consecutive year for deposit growth with more than a $10.0 million increase over 1996. A recent system upgrade will allow the Bank to improve its existing deposit products and offer complementary services to customers.



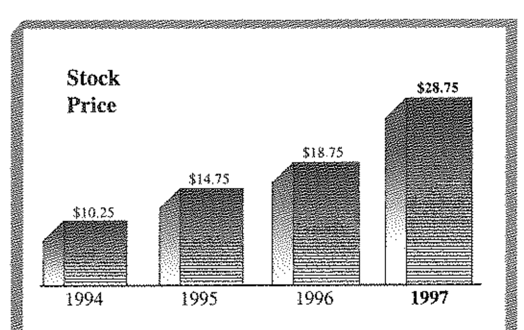
Nearly $56.0 million loans were originated in 1997, resulting in a remarkable 14% growth over 1996. More than 99% of the loan portfolio is secured by mortgages.



Quarterly dividends continue to show steady improvement with the dividend payout ratio approaching 30%. Special dividends were declared in each of the past three years culminating in a $0.13 per share special dividend in the fourth quarter of 1997.



The results for 1997 represent the fourth consecutive year of double-digit increases in pre-tax earnings. Pre-tax earnings for 1997 rose 24% over those of 1996.



The Bank's stock price has risen dramatically over the past three years, improving by $10 per share, or more than 50%, during 1997 alone.

Selected Consolidated Financial Data

The following information does not purport to be complete and is qualified in its entirety by the more detailed information contained elsewhere herein.

	At December 31,				
	1997	1996	1995	1994	1993
	(In Thousands)				
Balance Sheet Data:					
Total assets	$222,584	$201,586	$175,409	$153,192	$147,889
Investment securities	35,369	32,321	39,152	42,930	58,904
Loans:					
Residential Mortgage	84,092	79,418	69,872	61,607	54,222
Commercial Mortgage	84,362	67,008	44,667	34,651	20,600
Construction, net	4,857	5,421	5,437	4,649	1,951
Other	1,209	938	1,066	1,116	1,525
Allowance for loan losses	1,560	1,393	1,277	1,338	1,191
Foreclosed real estate, net	—	—	34	439	2,384
Deposits	160,506	150,015	133,042	116,684	117,717
Federal Home Loan Bank advances	38,147	29,754	22,000	19,000	15,000
Other borrowed funds	319	188	—	—	—
Stockholders' equity	21,377	19,212	17,819	15,981	14,074

	Years Ended December 31,				
	1997	1996	1995	1994	1993
	(In Thousands, Except Per Share Amounts)				
Income Statement Data:					
Total interest and dividend income	$ 16,405	$ 13,962	$ 12,074	$ 9,963	$ 9,232
Total interest expense	8,160	6,956	5,871	4,324	4,593
Net interest income	8,245	7,006	6,203	5,639	4,639
Provision for loan losses	174	107	120	120	63
Other income	653	614	509	642	1,484
Operating expenses	4,458	4,066	3,641	3,860	6,340
Income (loss) before income taxes	4,266	3,447	2,951	2,301	(280)
Income tax provision (benefit)	1,607	1,403	1,045	(255)	(469)
Net income	$ 2,659	$ 2,044	$ 1,906	$ 2,556	$ 189
Earnings per share	$ 2.04	$ 1.57	$ 1.47	$ 1.99	$ 0.15
Earnings per share - assuming dilution for stock options	$ 2.00	$ 1.56	$ 1.46	$ 1.98	$ 0.15
Financial Ratios:					
Return on average assets	1.26%	1.10%	1.17%	1.70%	0.13%
Return on average equity	13.00	11.06	11.11	17.09	1.34
Average equity to average assets	9.67	9.94	10.54	9.94	9.52
Interest rate spread	3.48	3.38	3.42	3.55	3.06
Net yield on average earning assets	4.02	3.90	3.96	3.92	3.34
Dividend payout ratio	28.92	28.66	23.81	8.54	—
Cash dividends declared per share	$ 0.59	$ 0.45	$ 0.35	$ 0.17	$ —

Founded in 1834, Hingham Institution for Savings has served the local community for more than 163 years. On December 20, 1988, the Bank converted its ownership from mutual to stock form. Banking services are provided through branch offices in Hingham, South Hingham, Hull, Scituate and Cohasset.

The following information should be read in conjunction with the Consolidated Financial Statements and Notes contained in this report.

COMPARISON OF THE YEARS 1997, 1996, and 1995

RESULTS OF OPERATIONS

For the year ended December 31, 1997, the Bank earned $2.7 million, as compared to $2.0 million in 1996 and $1.9 million in 1995. Earnings per share were $2.04 in 1997, $1.57 in 1996, and $1.47 in 1995. On a dilutive basis, which assumes that certain stock options have been exercised, earnings per share were $2.00 in 1997, $1.56 in 1996, and $1.46 in 1995.

Net interest income increased nearly 18% when comparing 1997 to 1996, and increased nearly 13% when comparing 1996 to 1995. Customer service fees have risen gradually over the past three years resulting from growth in deposit accounts and transactions and a modest increase in the Bank's fee schedule. When comparing 1997 to 1996, operating expenses increased $392,000, resulting primarily from salary and employee benefit expenses, costs incurred during a data center conversion and computer system upgrade. Operating expenses increased $425,000 when comparing 1996 to 1995, resulting primarily from the addition of two branch offices in late 1995.

Net Interest Income

The Bank reported $8.2 million in net interest income for 1997 as compared to $7.0 million in 1996, and $6.2 million in 1995. This positive trend was primarily the result of significant growth in loans which averaged $163.0 million for 1997 as compared to $136.8 million for 1996 and $109.8 million for 1995.

The following table presents information regarding changes in interest and dividend income and interest expense of the Bank for the years indicated. For each category, information is provided with respect to changes attributable to changes in rate (change in rate multiplied by old volume) and changes in volume (change in volume multiplied by old rate). The change attributable to both volume and rate is allocated proportionately to the changes due to volume and rate.

	Years Ended December 31,					
	1997 Compared to 1996 Increase (Decrease)			1996 Compared to 1995 Increase (Decrease)		
	Due to			Due to		
	Volume	Rate	Total	Volume	Rate	Total
	(In Thousands)					
Interest and dividend income:						
Total loans	$ 2,226	$ 216	$ 2,442	$ 2,263	$ (144)	$ 2,119
Investment securities and Federal Home Loan Bank stock	(41)	43	2	(326)	48	(278)
Interest-bearing deposits	(8)	7	(1)	72	(25)	47
Total interest and dividend income	2,177	266	2,443	2,009	(121)	1,888
Interest expense:						
Deposits	694	(57)	637	946	41	987
Borrowings	569	(2)	567	141	(43)	98
Total interest expense	1,263	(59)	1,204	1,087	(2)	1,085
Net interest income	$ 914	$ 325	$ 1,239	$ 922	$ (119)	$ 803

The following table details changes in net interest income and net yield on average earning assets.

	Years Ended December 31,								
	1997			1996			1995		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
	(Dollars in Thousands)								
Assets:									
Loans:									
Real estate loans	$161,156	$13,752	8.53%	$134,775	$11,283	8.37%	$107,842	$9,157	8.49%
Commercial loans	764	71	9.29	1,080	105	9.72	1,062	112	10.55
Other loans	1,075	93	8.65	994	86	8.65	944	86	9.11
Total loans (1) (2)	162,995	13,916	8.54	136,849	11,474	8.38	109,848	9,355	8.52
Investment securities (3) (4)	36,537	2,197	6.01	37,218	2,195	5.90	42,759	2,473	5.78
Interest-bearing deposits	5,414	292	5.39	5,564	293	5.27	4,232	246	5.81
Total earning assets	204,946	16,405	8.00	179,631	13,962	7.77	156,839	12,074	7.70
Other assets	6,481			6,277			5,884		
Total assets	$211,427			$185,908			$162,723		
Liabilities and stockholders' equity:									
Interest-bearing deposits:									
NOW accounts (5)	$ 13,173	169	1.28	$ 12,980	184	1.42	$ 10,581	157	1.48
Money market deposits	20,600	621	3.01	20,269	606	2.99	20,392	603	2.96
Regular	31,257	783	2.51	31,292	783	2.50	30,956	775	2.50
Term certificates	83,257	4,690	5.63	71,153	4,053	5.70	55,213	3,104	5.62
Total interest-bearing deposits	148,287	6,263	4.22	135,694	5,626	4.15	117,142	4,639	3.96
Borrowings	32,212	1,897	5.89	22,557	1,330	5.90	20,181	1,232	6.10
Total interest-bearing liabilities	180,499	8,160	4.52	158,251	6,956	4.40	137,323	5,871	4.28
Demand deposits	9,291			7,854			6,572		
Other liabilities	1,188			1,323			1,672		
Stockholders' equity	20,449			18,480			17,156		
Total liabilities and stockholders' equity	$211,427			$185,908			$162,723		
Net interest income		$8,245			$ 7,006			$6,203	
Weighted average rate spread			3.48%			3.37%			3.42%
Net yield on average earning assets (6)			4.02%			3.90%			3.96%

(1) Gross of allowance for loan losses.
(2) Includes average non-accrual loans.
(3) Excludes the impact of the average unrealized gain (loss) on securities available for sale.
(4) Includes Federal Home Loan Bank stock.
(5) Includes mortgagors' escrow accounts.
(6) Net interest income divided by average total earning assets.

Interest income is derived from residential and commercial mortgages, home equity, installment and commercial loans, and the investment portfolio. The Bank earned an average yield of 8.0% on these assets in 1997, as compared to 7.77% in 1996 and 7.70% in 1995. For 1997, 1996 and 1995, interest income totaled $16.4 million, $14.0 million and $12.1 million, respectively. Average total earning assets increased $25.3 million, or 14%, in 1997 over 1996 and $22.8 million, or 15%, in 1996 over 1995. The Bank achieved this growth by continuing to focus on real estate lending and decreasing its emphasis on the investment portfolio.

Average deposit and borrowing balances increased in 1997 and 1996 as the Bank employed these sources to fund its loan growth. As a result, interest expense, which is incurred on certificates of deposit, NOW, savings and money market deposit accounts, Federal Home Loan Bank ("FHLB") advances and other borrowings, collectively increased in these periods.

The average rate paid on interest-bearing deposit accounts was 4.22% during 1997, as compared to 4.15% for 1996 and 3.96% for 1995 resulting primarily from a continuing shift in the Bank's deposit mix. Certificates of deposit comprised 56% of average interest-bearing deposits for 1997, at an average rate of 5.63%. Comparably, certificates of deposit comprised 52% of average interest-bearing deposits in 1996 and 47% in 1995 at an average rate of 5.70% and 5.62% in 1996 and 1995, respectively.

Interest expense on borrowings continued to rise during 1997 resulting primarily from an increase in FHLB advances. However, the average rate paid on borrowings declined from 6.10% in 1995 and 5.90% in 1996 to 5.89% in 1997 due to the downturn in market interest rates. Also, during 1997, the Bank continued as a note option depository for treasury, tax and loan deposits which allowed it to borrow short-term funds at a preferred interest rate.

Provision for Loan Losses

The provision for loan losses is based on management's assessment of the adequacy of the allowance for loan losses. Management considers the size of the loan portfolio, the risks associated with certain loan types, and the underlying collateral values of individual loans as well as other factors. During 1997, the Bank originated $56.0 million in residential, commercial, and personal loans combined, increasing the loan portfolio to a total of $172.8 million at December 31, 1997. The provision for loan losses for 1997 was $174,000 as compared to $107,000 in 1996 and $120,000 in 1995. In 1996 recoveries of previously charged-off loans enabled the Bank to maintain an adequate level of allowance for loan losses while lowering its annual provision.

Other Income

Other income is comprised of customer service fees, net gains or losses on sales of investments, and other miscellaneous items. The most significant component of other income was fees earned on customer accounts with $443,000 reported for 1997, $409,000 for 1996, and $346,000 for 1995. These increases reflect a higher volume of transactions along with a modest rise in the fee schedule. In 1995, the Bank reported $49,000 in net losses on sales of securities classified as available for sale. The securities were earning below-market rates of interest and were sold to obtain liquidity to fund growth in the loan portfolio.

Operating Expenses

There were $4.5 million in operating expenses in 1997 as compared to $4.1 million in 1996, and $3.6 million in 1995. The rise in expenses in 1997 is primarily attributable to salary and employee benefit expenses and a Bank-wide computer system upgrade and data center conversion, which resulted in an increase in various operating expenses. The rise in expenses in 1996 is primarily attributable to the addition of two branch offices which opened in the fourth quarter of 1995. As a percentage of average total assets, expenses declined steadily from 2.24% in 1995 to 2.19% in 1996 to 2.11% in 1997.

Salaries and employee benefits were the largest component of operating expenses at $2.5 million for 1997, $2.3 million for 1996, and $1.8 million for 1995. In the fourth quarter of 1995, the Bank hired eight employees to staff the two new branches. This increased expense continued throughout 1996 and 1997. Annual merit-based raises also contributed to the increase in salary expenses.

Occupancy and equipment expenses increased over the three periods. In 1997, the increase was primarily the result of a Bank-wide computer system upgrade. The Bank replaced approximately 50 outdated terminals with state-of-the-art personal computers, installed local-area networks and a wide-area network, and upgraded its data

communication lines. The result of these improvements will be the ability to meet customer needs, enhance administrative efficiency, and lower maintenance expenses.

Deposit insurance expense, comprised of federal and state deposit insurance premiums, increased when comparing 1997 to 1996 and declined when comparing 1996 and 1995. In 1995, the Federal Deposit Insurance Corporation ("FDIC") awarded the Bank its lowest premium rate due to the Bank's improved financial condition and then, effective June 1995 reduced this premium rate by 85% to only $0.04 per hundred dollars of average deposits. In 1996, the FDIC further reduced the annual premium to $2,000 for well-capitalized banks. Effective January 1, 1997, in accordance with the Deposit Insurance Fund Act, the Financing Corporation (FICO) debt service assessment became applicable to all insured institutions. This resulted in an additional expense of $17,000 in 1997 over 1996.

Other operating expenses including data processing, legal, and other were $1.4 million combined for 1997 as compared to $1.3 million in each of 1996 and 1995. Data processing expenses rose in each of the three periods as a result of an increase in the number of deposit accounts and their associated transaction volume.

Income Taxes

In 1995, the Bank was able to utilize net operating loss carryforwards to offset current taxable income and recognize deferred tax assets. As a result, the Bank recognized a net provision for income taxes in the amount of $1.0 million for 1995, at an effective tax rate of 35.4%. There were no further tax benefits available in 1996, and as a result, the Bank reported a provision for income taxes of $1.4 million at an effective tax rate of 40.7%. In 1997, the Bank employed strategies with respect to its securities portfolio which reduced its effective tax rate to 37.7%.

COMPARISON OF THE YEARS 1997 AND 1996

BALANCE SHEET ANALYSIS

The Bank had total assets of $222.6 million at December 31, 1997, an increase of $21.0 million, or 10%, from the $201.6 million level at year end 1996.

Loans

At December 31, 1997, the Bank reported net loans of $172.8 million, or 78% of total assets. Comparably at December 31, 1996, net loans were $151.2 million, or 75% of total assets. This growth of $21.7 million, or 14%, was achieved through the origination of nearly $56.0 million in mortgage and other loan products. A stringent underwriting policy continues to complement this lending strategy. At December 31, 1997 and 1996, mortgage loans accounted for more than 99% of gross loans with commercial mortgages representing approximately 49% of the mortgage portfolio in 1997 and 44% in 1996.

The Bank's lending strategy during 1997 and 1996 has been to provide commercial property, residential, and multifamily loans at an initial fixed rate for three to five years with a floating rate thereafter. Residential mortgages are generally underwritten to conform to Federal National Mortgage Association or Federal Home Loan Mortgage Corporation guidelines. The Bank also offers home equity loans tied to the prime lending rate.

The Bank's loan portfolio is reported net of the allowance for loan losses. At December 31, 1997 and 1996, the allowance had a balance of $1.6 million and $1.4 million, respectively. The allowance is maintained at a level to absorb possible losses. Loan losses are charged against the allowance when the collectibility of loan principal becomes unlikely. Recoveries are recorded as additional reserves when received. There were $13,000 in charge-offs and $6,000 in recoveries in 1997. Comparably in 1996 there were $48,000 in charge-offs and $57,000 in recoveries.

Non-accrual loans totaled $1.7 million, or 0.77% of total assets, at December 31, 1997, as compared to $1.2 million, or 0.58% of total assets, at year end 1996. The increase in non-accrual loans is primarily the result of two mortgage borrowers, with whom the Bank is working to resolve the delinquency. No significant write-offs related to these mortgages are anticipated.

The following table presents information regarding the Bank's non-accrual loans:

At December 31,	1997	1996
	(In Thousands)	
Residential Mortgages (1)	$1,200	$1,168
Commercial Mortgages	502	—
Commercial Loans	5	—
Installment Loans	1	—
Total Non-accrual Loans	$1,708	$1,168

(1) Includes home equity loans.

Investments

The purpose of the Bank's investment portfolio is to supplement the Bank's lending activities by generating income and providing liquidity through the receipt of principal and interest payments. At December 31, 1997, the portfolio was comprised of mortgage-backed and agency issues for a total of $35.4 million, or 16% of total assets, as compared to $32.3 million, or 16% of total assets, at year end 1996. All securities in the portfolio are issued or guaranteed by U.S. Government agencies or U.S. Government sponsored agencies and, as such, carry a relatively low risk-weighting under Federal Deposit Insurance Corporation ("FDIC") risk-based capital guidelines.

At December 31, 1997, $17.3 million, or 49% of the Bank's investment portfolio, was comprised of mortgage-backed securities, a decline of $6.0 million from the $23.3 million held at December 31, 1996. These securities are subject to declines in principal balances due to principal prepayments. Prepayments tend to increase as market interest rates fall and the individual underlying mortgages are refinanced at lower rates. Conversely, prepayments tend to decrease as market interest rates rise. The decrease in the amount of mortgage-backed securities held, offset by the decline in interest rates in 1997, resulted in $4.5 million in principal prepayments received during 1997 as compared to $6.1 million during 1996.

At year end 1997 and 1996, the entire investment portfolio was classified as available for sale and was carried at fair value with unrealized gains or losses reported as a separate component of stockholders' equity. The unrealized loss on the investment portfolio amounted to $50,000, net of tax effects, at December 31, 1997 as compared to $244,000 at year end 1996, reflecting an improvement in market conditions. The fair value of securities fluctuates with the movement of interest rates. Generally, during periods of decreasing interest rates, the fair values increase whereas the opposite may hold true during a rising interest rate environment.

Deposits

At December 31, 1997, the Bank held a total of $160.5 million in deposits, an increase of $10.5 million, or 7%, from the $150.0 million in deposits at year end 1996. The Bank offers a wide range of products, competitively priced, accompanied by quality service. During the fourth quarter of 1995 the Bank opened branch offices in the towns of Scituate and Cohasset which have assisted in the growth of the deposit base.

Primary competition for deposits are other banks and credit unions in the Bank's market area and mutual funds. The Bank's ability to attract and retain deposits depends upon satisfaction of depositors' requirements with respect to rate, liquidity, risk, and service. The Bank offers competitive rates, convenient branch locations, and the added convenience of automated teller machines. Deposits are insured in full through the Federal Deposit Insurance Corporation and Deposit Insurance Fund of Massachusetts. This insurance, combined with the Bank's strong capital position, provides an advantage in allaying customer concerns regarding the safety of deposits.

Core deposits, comprised of savings, NOW, and money market accounts were $73.6 million at December 31, 1997 as compared to $71.3 million at year end 1996, an increase of $2.3 million. Certificates of deposit were $86.9 million, or 54% of total deposits, at December 31, 1997 as compared to $78.7 million, or 52% of total deposits, at year end 1996, an increase of $8.2 million. This continued growth in certificates of deposit has resulted in increased deposit interest expense.

Borrowings

The Bank had $38.1 million in FHLB advances at December 31, 1997, as compared to $29.8 million at year end 1996. The Bank borrowed an additional $8.4 million in 1997 to fund growth in the loan portfolio and to effectively manage its interest rate sensitivity position. During 1996, the Bank became a note option depository for treasury, tax and loan deposits, which provides the Bank with an additional source of short-term funding at a preferred interest rate. At December 31, 1997 and 1996, there were $319,000 and $188,000, respectively, in such borrowings.

Liquidity and Capital Resources

The Bank's primary sources of liquidity are its available-for-sale securities portfolio, principal and interest payments on loans and investment securities, net increases in deposit balances, and FHLB advances.

As a member of the Federal Home Loan Bank of Boston, the Bank is eligible to obtain both short and long-term credit advances. The Bank can borrow up to approximately $62.8 million to meet its borrowing needs, based on the Bank's available qualified collateral which consists primarily of 1-4 family residential mortgages. Upon specific approval from the FHLB, the Bank may also pledge securities and other mortgages as collateral to secure as much as $51.7 million in additional borrowings. At December 31, 1997, the Bank had $38.1 million in advances with original maturities of up to three years.

The Bank can also enter into repurchase agreement transactions if the need for additional liquidity arises. At December 31, 1997, the Bank had no repurchase agreements outstanding.

At December 31, 1997, the Bank had capital of $21.4 million, or 9.60% of total assets, as compared to $19.2 million, or 9.53%, at December 31, 1996. Total capital is adjusted by the unrealized gains or losses in the Bank's available-for-sale securities portfolio, and as such it is subject to fluctuations resulting from changes in the market values of its investment securities. At December 31, 1997 the Bank's entire securities portfolio was classified as available for sale, which had the effect of reducing capital by $50,000. In comparison, at year end 1996 capital was reduced by $244,000.

Massachusetts-chartered savings banks that are insured by the FDIC are subject to minimum capital maintenance requirements. Regulatory guidelines define the minimum amount of qualifying capital an institution must maintain as a percentage of risk-weighted assets (Risk-Based Capital Ratios) and average total assets (Leverage Ratio). The Bank's ratios exceeded these regulatory capital requirements in both 1997 and 1996, as follows:

December 31,	1997	1996	Minimum Regulatory Ratios
Risk-Based Capital Ratios:			
Tier One Capital	14.60%	15.04%	4%
Total Capital	15.66	16.12	8
Leverage Ratio	9.80	9.90	3-5

These high capital levels were maintained despite a more aggressive dividend policy. During 1997 the Bank declared dividends of $0.59 per share, which included a $0.13 per share special dividend which was declared in the fourth quarter. In comparison, in 1996, the Bank declared dividends of $0.45 per share, which included a $0.10 per share special dividend. The Bank's dividend payout ratio, which is calculated by dividing dividends per share into earnings per share, increased to 28.9% for 1997 as compared to 28.7% for 1996.

IMPACT OF THE YEAR 2000 ISSUE

The Year 2000 Issue is the result of computer programs being written using two digits rather than four to define the applicable year. Any of a bank's computer programs that have date-sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000. This could result in a system failure or miscalculations causing disruptions of operations, including, among other things, a temporary inability to process transactions or engage in normal business activities.

The Bank has assessed the potential impact of the Year 2000 Issue on its key operational areas. Virtually all of the Bank's deposit and loan data processing is supplied by one vendor, who, thus far, has been adhering to a schedule which anticipates Year 2000 readiness by June 30, 1998. The Bank is also working with its other vendors who provide software, hardware, and other date-sensitive equipment to ensure that all systems will remain operational in the Year 2000 and beyond. Also under consideration are the Bank's loan customers, whose operations may be impacted by Year 2000 problems and may subsequently impair their ability to meet their financial obligations to the Bank. It is the Bank's belief that all key systems are, or will be, Year 2000 compliant in advance of the millennium, and anticipated expenditures will not be material.

IMPACT OF INFLATION AND CHANGING PRICES

The consolidated financial statements and related consolidated financial data presented herein have been prepared in accordance with generally accepted accounting principles which generally require the measurement of financial position and operating results in terms of historical dollars without considering the changes in the relative purchasing power of money over time due to inflation. The primary impact of inflation on operations of the Bank is reflected in increased operating costs. Unlike most industrial companies, virtually all 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 the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the price of goods and services.

Management's Discussion and Analysis

ASSET/LIABILITY MANAGEMENT

The earnings of most banking institutions are exposed to interest rate risk because their balance sheets, both assets and liabilities, are predominantly interest bearing. It is the Bank's objective to minimize, to the degree prudently possible, its exposure to interest rate risk, bearing in mind that the Bank, by its very nature, will always be in the business of taking on interest rate risk. Interest rate risk is monitored on a quarterly basis by the Asset Liability Committee of the Bank. The primary tool used by the Bank in managing interest rate risk is income simulation modeling. Income simulation modeling measures changes in net interest income by projecting the future composition of the Bank's balance sheet and applying different interest rate scenarios. Management incorporates numerous assumptions into the simulation model, such as prepayment speeds, balance sheet growth and deposit elasticity. Rates are assumed to rise, or decline, steadily over a twelve month period, then remain constant over the remaining period.

Assuming an upward shift in the yield curve resulting in a 200 basis point increase in short rates and an approximate 54 basis point increase in longer rates, management estimates a .69% decrease in net interest income over a 24 month period. Conversely, management estimates a 1.63% increase in net interest income over a 24 month period assuming a downward shift in the yield curve resulting in a 200 basis point decrease in short rates and an approximate 74 basis point decrease in longer rates.

The Bank's interest rate risk exposure is believed to be managed and well within pre-defined limits.

To a significantly lesser degree, the Bank also utilizes GAP analysis which involves comparing the difference between interest-rate sensitive assets and liabilities that mature or reprice during a given period of time. However, GAP analysis does not measure the financial impact of mismatched assets to liabilities, nor does it measure the velocity at which assets and liabilities reprice.

FORWARD-LOOKING STATEMENTS

This annual report may contain statements relating to future results of the Bank (including certain projections and business trends) that are considered "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those projected 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 within the Bank's market, bond market fluctuations, personal and corporate customers' bankruptcies, and inflation, as well as other risks and uncertainties.

The following table presents, as of December 31, 1997, interest-rate sensitive assets and liabilities categorized by expected maturity (or interest rate adjustment date, if earlier) and weighted average rate. Expected maturities are contractual maturities adjusted for amortization and prepayment of principal. Prepayment speeds range from 4% to 24% depending upon the particular asset category. Generally, adjustable rate loans are indexed to Prime or Treasury rates and can reprice as much as 200 basis points per year and 600 basis points over the life of the loan. Non-certificate deposits do not have contractual maturities. The table reflects management's assumptions about the repricing characteristics of such deposits.

Maturing or repricing within:	One Year	1-2 Years	2-3 Years	3-4 Years	4-5 Years	Thereafter	Total
	(Dollars in Thousands)						
Interest-earning assets:							
Investments, at cost	$ 9,663	$ 9,113	$ 9,187	$ 1,150	$ 656	$ 5,685	$35,454
	6.41%	6.45%	6.44%	6.82%	7.13%	6.52%	6.47%
Loans:							
Fixed rate	$23,013	$22,281	$10,931	$ 6,969	$4,890	$24,595	$92,679
	8.63%	8.41%	8.28%	8.03%	7.71%	7.64%	8.18%
Adjustable rate	$46,542	$13,443	$16,981	$ 2,716	$1,108	$ 1,051	$81,841
	9.03%	8.31%	8.71%	8.61%	8.49%	8.48%	8.82%
Interest-bearing liabilities:							
Deposits:							
Non-certificate accounts	$20,359	$20,359	$23,973	$ —	$ —	$ —	$64,691
	2.75%	2.75%	1.80%	—	—	—	2.40%
Term certificates	$63,632	$13,793	$ 7,781	$ 1,262	$ 408	$ —	$86,876
	5.73%	6.01%	6.67%	5.87%	6.21%	—	5.87%
Borrowings	$33,466	$ 5,000	$ —	$ —	$ —	$ —	$38,466
	5.84%	5.96%	—	—	—	—	5.85%

Independent Auditors' Report

To the Board of Directors and Stockholders of
Hingham Institution for Savings

We have audited the consolidated balance sheets of Hingham Institution for Savings and subsidiaries as of December 31, 1997 and 1996, and the related consolidated statements of income, changes in stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 1997. These consolidated financial statements are the responsibility of the Bank'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 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 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 Hingham Institution for Savings and subsidiaries as of December 31, 1997 and 1996, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1997 in conformity with generally accepted accounting principles.

Wolf + Company, P.C

Boston, Massachusetts
January 23, 1998

Consolidated Balance Sheets

ASSETS

	December 31, 1997	December 31, 1996
	(In Thousands)	
Cash and due from banks (Note 2)	$ 3,804	$ 3,323
Interest-bearing deposits	3,464	8,317
Cash and cash equivalents	7,268	11,640
Securities available for sale (Note 3)	35,369	32,321
Loans, net of allowance for loan losses of $1,560,000 in 1997 and $1,393,000 in 1996 (Notes 4 and 7)	172,839	151,166
Banking premises and equipment, net (Note 5)	2,633	2,418
Accrued interest receivable	1,243	1,060
Deferred income tax asset, net (Note 8)	994	1,106
Federal Home Loan Bank stock, at cost (Note 7)	1,900	1,450
Other assets	338	425
	$222,584	$201,586

LIABILITIES AND STOCKHOLDERS' EQUITY

	1997	1996
Deposits (Note 6)	$160,506	$150,015
Federal Home Loan Bank advances (Note 7)	38,147	29,754
Other borrowed funds	319	188
Mortgagors' escrow accounts	451	292
Accrued interest payable	205	582
Other liabilities (Note 12)	1,579	1,543
Total liabilities	201,207	182,374
Commitments and contingencies (Note 9)		
Stockholders' equity (Notes 10 and 11):		
Preferred stock, $1.00 par value, 2,500,000 shares authorized; none issued	—	—
Common stock, $1.00 par value, 5,000,000 shares authorized; 1,303,500 and 1,297,500 shares issued and outstanding in 1997 and 1996, respectively	1,304	1,298
Additional paid-in capital	8,693	8,616
Undivided profits	11,430	9,542
	21,427	19,456
Net unrealized loss on securities available for sale, after tax effect (Notes 3 and 8)	(50)	(244)
Total stockholders' equity	21,377	19,212
	$222,584	$201,586

See accompanying notes to consolidated financial statements.

Consolidated Statements of Income

	Years Ended December 31, 1997	1996	1995
	(In Thousands, Except Per Share Data)		
Interest and dividend income:			
Loans	$13,916	$11,474	$ 9,355
Investment securities	2,197	2,195	2,473
Interest-bearing deposits	292	293	246
Total interest and dividend income	16,405	13,962	12,074
Interest expense:			
Deposits (Note 6)	6,263	5,626	4,639
Borrowed funds	1,897	1,330	1,232
Total interest expense	8,160	6,956	5,871
Net interest income	8,245	7,006	6,203
Provision for loan losses (Note 4)	174	107	120
Net interest income, after provision for loan losses	8,071	6,899	6,083
Other income:			
Customer service fees on deposits	443	409	346
Other	210	205	163
Total other income	653	614	509
Operating expenses:			
Salaries and employee benefits (Note 12)	2,467	2,268	1,838
Data processing	339	331	298
Occupancy and equipment (Note 5)	539	485	372
Legal	29	10	66
Deposit insurance	22	4	159
Other	1,062	968	908
Total operating expenses	4,458	4,066	3,641
Income before income taxes	4,266	3,447	2,951
Income tax provision (Note 8)	1,607	1,403	1,045
Net income	$ 2,659	$ 2,044	$ 1,906
Weighted average shares outstanding	1,302	1,298	1,294
Weighted average shares outstanding - assuming dilution for stock options	1,331	1,311	1,302
Earnings per share	$ 2.04	$ 1.57	$ 1.47
Earnings per share - assuming dilution for stock options	$ 2.00	$ 1.56	$ 1.46

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Stockholders' Equity

Years Ended December 31, 1997, 1996 and 1995

	Common Stock	Additional Paid-in Capital	Undivided Profits	Net Unrealized Loss on Securities Available for Sale	Total Stockholders' Equity
			(In Thousands)		
Balance at December 31, 1994	$ 1,293	$ 8,584	$ 6,629	$ (525)	$15,981
Net income	—	—	1,906	—	1,906
Change in net unrealized loss on securities available for sale, after tax effect	—	—	—	370	370
Stock options exercised, after tax effect	2	13	—	—	15
Cash dividends declared ($.35 per share)	—	—	(453)	—	(453)
Balance at December 31, 1995	1,295	8,597	8,082	(155)	17,819
Net income	—	—	2,044	—	2,044
Change in net unrealized loss on securities available for sale, after tax effect	—	—	—	(89)	(89)
Stock options exercised, after tax effect	3	19	—	—	22
Cash dividends declared ($.45 per share)	—	—	(584)	—	(584)
Balance at December 31, 1996	1,298	8,616	9,542	(244)	19,212
Net income	—	—	2,659	—	2,659
Change in net unrealized loss on securities available for sale, after tax effect	—	—	—	194	194
Stock options exercised, after tax effect	6	77	—	—	83
Cash dividends declared ($.59 per share)	—	—	(771)	—	(771)
Balance at December 31, 1997	$ 1,304	$ 8,693	$11,430	$ (50)	$21,377

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

	Years Ended December 31,		
	1997	1996	1995
	(In Thousands)		
Cash flows from operating activities:			
Net income	$2,659	$2,044	$1,906
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	174	107	120
Provision for losses on foreclosed and other real estate	—	—	20
Amortization of premium on investment securities, net of accretion	151	242	288
Amortization of deferred loan origination fees, net	(52)	(73)	(62)
Depreciation	248	195	133
Loss on sale of securities available for sale, net	—	—	49
Gain on sale of foreclosed and other real estate	—	(31)	(4)
Deferred tax (benefit) provision	(20)	(16)	249
Changes in operating assets and liabilities:			
Accrued interest receivable	(183)	(12)	(213)
Other assets	87	(49)	(17)
Accrued interest payable and other liabilities	(402)	(164)	843
Net cash provided by operating activities	2,662	2,243	3,312
Cash flows from investing activities:			
Proceeds from sale of securities available for sale	—	—	1,463
Purchase of securities available for sale	(10,996)	(3,991)	(4,882)
Purchase of securities held to maturity	—	—	(2,183)
Proceeds from maturities of securities available for sale	3,576	4,324	4,000
Proceeds from maturities of securities held to maturity	—	—	2,000
Principal payments received on mortgage-backed securities	4,547	6,122	3,676
Loans originated, net of payments received	(21,795)	(31,694)	(18,832)
Additions to foreclosed and other real estate, net of payments	—	—	(110)
Proceeds from sale of foreclosed and other real estate	—	31	279
Increase in Federal Home Loan Bank stock	(450)	(250)	(206)
Additions to banking premises and equipment	(463)	(117)	(930)
Net cash used in investing activities	(25,581)	(25,575)	(15,725)

(continued)

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(Concluded)

	Years Ended December 31,		
	1997	1996	1995
		(In Thousands)	
Cash flows from financing activities:			
Increase in deposits, net	$10,491	$16,973	$16,358
Increase in mortgagors' escrow accounts	159	5	35
Proceeds from stock options exercised	63	11	8
Cash dividends paid on common stock	(690)	(545)	(310)
Proceeds (repayments) from borrowings with maturities of less than three months	(2,976)	3,442	—
Proceeds from Federal Home Loan Bank advances with maturities of three months or more	38,500	24,000	50,500
Repayment of Federal Home Loan Bank advances with maturities of three months or more	(27,000)	(19,500)	(47,500)
Net cash provided by financing activities	18,547	24,386	19,091
Net increase (decrease) in cash and cash equivalents	(4,372)	1,054	6,678
Cash and cash equivalents at beginning of year	11,640	10,586	3,908
Cash and cash equivalents at end of year	$ 7,268	$11,640	$10,586
Supplementary information:			
Interest paid on deposit accounts	$ 6,684	$ 5,579	$ 4,499
Interest paid on borrowed funds	1,853	1,300	1,225
Income taxes paid	1,658	1,734	72
Financed sales of foreclosed real estate	—	34	171
Foreclosed real estate transferred to loans	—	—	129
Securities held to maturity transferred to available for sale	—	—	26,301

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

December 31, 1997, 1996 and 1995

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation and consolidation

The consolidated financial statements include the accounts of Hingham Institution for Savings ("Bank") and its wholly owned subsidiaries, Hingham Securities Corporation and Hingham Motel Corporation. Hingham Securities Corporation holds title to securities available for sale and Hingham Motel Corporation is presently inactive. All intercompany accounts and transactions have been eliminated in consolidation. The accounting and reporting policies of the Bank conform to generally accepted accounting principles and prevailing practices within the banking industry.

Use of estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation reserve against deferred tax assets.

Business

The Bank provides a variety of financial services to individuals and small businesses through its five offices in southeastern Massachusetts. Its primary deposit products are savings, checking and term certificate accounts, and its primary lending products are residential and commercial mortgage loans.

Reclassification

Certain amounts have been reclassified in the 1996 and 1995 consolidated financial statements to conform to the 1997 presentation.

Cash and cash equivalents

Cash and cash equivalents include amounts due from banks and interest-bearing deposits.

Interest-bearing deposits

Interest-bearing deposits mature within ninety days and are carried at cost, which approximates fair value.

Securities Available for Sale

Investments are classified as available for sale and reflected at fair value, with unrealized gains and losses, after tax effect, excluded from earnings and reported as a separate component of stockholders' equity.

Federal Home Loan Bank of Boston stock is reflected at cost.

Purchased premiums and discounts are amortized to earnings by a method which approximates the interest method over the terms of the investments. Declines in the value of investments that are deemed to be other than temporary are reflected in earnings when identified. Gains and losses on disposition of investments are computed by the specific identification method.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Loans

The Bank grants mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans in the southeastern Massachusetts area. The ability of the Bank's debtors to honor their contracts is dependent upon the real estate, construction and general economic sectors.

Loans, as reported, have been reduced by unadvanced loan funds, net deferred interest and loan origination fees and the allowance for loan losses.

Interest on loans is recognized on a simple interest basis and is not accrued on loans which are ninety days or more past due or for which collection is not assured. Interest income previously accrued on such loans is reversed against current period interest income. Interest income on all non-accrual loans is recognized only to the extent of interest payments received.

Net deferred interest and loan origination fees are amortized as an adjustment of the related loan yields using the level-interest method.

Allowance for loan losses

The allowance for loan losses is established through a provision for loan losses charged to earnings and is maintained at a level considered adequate to provide for reasonably foreseeable loan losses.

The provision and the level of the allowance are evaluated on a regular basis by management and are based upon management's periodic review of the collectibility of the loans in light of historical experience, known and inherent risks in the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant change. Ultimately losses may vary from current estimates, and future additions to the allowance may be necessary.

Loan losses are charged against the allowance when management believes the collectibility of the loan balance is unlikely. Subsequent recoveries, if any, are credited to the allowance.

A loan is considered impaired when, based on current information and events, it is probable that a creditor will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Substantially all of the Bank's loans which are identified as impaired are measured by the fair value of existing collateral.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer loans for impairment disclosures.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Banking premises and equipment

Land is carried at cost. Buildings and equipment are carried at cost, less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets. It is general practice to charge the cost of maintenance and repairs to earnings when incurred; major expenditures for betterments are capitalized and depreciated.

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 accordingly through the provision for income taxes. The Bank's base amount of its federal income tax reserve for loan losses is a permanent difference for which there is no recognition of a deferred tax liability. However, the loan loss allowance maintained for financial reporting purposes is a temporary difference with allowable recognition of a related deferred tax asset, if it is deemed realizable. The Bank and its subsidiaries file state and consolidated federal income tax returns based on an October 31 year end.

Retirement plan

The compensation cost of an employee's pension benefit is recognized on the net periodic pension cost method over the employee's approximate service period. The aggregate cost method is utilized for funding purposes.

Stock Compensation Plans

In accordance with the provisions of Statement of Financial Accounting Standards ("SFAS") No.123, "Accounting for Stock-Based Compensation," issued by the Financial Accounting Standards Board ("FASB"), the Bank has elected to continue to measure compensation cost for those plans using the intrinsic value-based method of accounting prescribed by APB Opinion No. 25, "Accounting for Stock Issued to Employees." Compensation cost is the excess, if any, of the quoted market price of the stock at the grant date (or other measurement date) over the amount an employee must pay to acquire the stock. Stock options issued under the Bank's stock option plans have no intrinsic value at the grant date, and under Opinion No. 25 no compensation cost is recognized for them. The Bank has elected to continue with the accounting methodology in Opinion No. 25 and, as a result, must make pro forma disclosures of net income and earnings per share and other disclosures, as if the fair value based method of accounting had been applied. The pro forma disclosures required by SFAS No.123 include the effects of all awards granted on or after January 1, 1995. (See Note 11.)

Earnings per share

In February 1997, FASB issued SFAS No. 128, "Earnings per Share," which requires that earnings per share be calculated on a basic and a dilutive basis. Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed conversion. Potential common shares that may be issued by the Bank relate solely to outstanding stock options, and are determined using the treasury stock method. The assumed conversion of outstanding dilutive stock options would increase the shares outstanding but would not require an adjustment to income as a result of the conversion. The Statement is effective for interim and annual periods ending after December 15, 1997, and requires the restatement of all prior-period earnings per share data presented. Accordingly, the Bank has restated all earnings per share data presented herein.

For the year ended December 31, 1995, options applicable to 28,000 shares were anti-dilutive and excluded from the diluted earnings per share computations. There were no such anti-dilutive shares for the years ended December 31, 1997 and 1996.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (concluded)

Recent Accounting Pronouncement

In June 1997, FASB issued SFAS No. 130, "Reporting Comprehensive Income," effective for fiscal years beginning after December 15, 1997. Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain FASB statements, however, require entities to report specific changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, as a separate component of the equity section of the balance sheet. Such items, along with net income, are components of comprehensive income. SFAS No.130 requires that all items of comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements. Additionally, SFAS No. 130 requires that the accumulated balance of other comprehensive income be displayed separately from retained earnings and additional paid-in capital in the equity section of the balance sheet. The Bank will adopt these disclosure requirements beginning in the first quarter of 1998.

2. CASH AND DUE FROM BANKS

The Bank is required to maintain cash reserve balances with the Federal Reserve Bank based upon a percentage of certain deposits. At December 31, 1997 and 1996, cash and due from banks included $531,000 and $228,000, respectively, to satisfy such reserve requirements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

3. SECURITIES AVAILABLE FOR SALE

The amortized cost and estimated fair value of securities available for sale, with gross unrealized gains and losses, follows:

	December 31, 1997			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
U.S. Government and federal agency obligations	$ 18,001	$ 83	$ (12)	$ 18,072
Mortgage-backed - FHLMC	7,656	22	(57)	7,621
Mortgage-backed - FNMA	7,897	12	(82)	7,827
REMIC's - FNMA	1,900	—	(51)	1,849
Total securities available for sale	$ 35,454	$ 117	$ (202)	$ 35,369

	December 31, 1996			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
U.S. Government and federal agency obligations	$ 9,030	$ 11	$ (62)	$ 8,979
Mortgage-backed - FHLMC	12,134	26	(165)	11,995
Mortgage-backed - FNMA	9,669	18	(154)	9,533
REMIC's - FNMA	1,899	—	(85)	1,814
Total securities available for sale	$ 32,732	$ 55	$ (466)	$ 32,321

At December 31, 1997, the Bank has pledged U.S. Government obligations with an amortized cost of $1,000,000 and a fair value of $998,000 as collateral against its treasury, tax and loan account.

SECURITIES AVAILABLE FOR SALE (concluded)

The amortized cost and estimated fair value of debt securities by contractual maturity at December 31, 1997 are shown below. Expected maturities will differ from contractual maturities because of prepayments and scheduled payments on mortgage-backed securities. Further, certain obligors have the right to call bonds and obligations without prepayment penalties.

	Amortized Cost	Fair Value
	(In Thousands)	
Bonds and obligations:		
Within 1 year	$ 4,005	$ 4,004
Over 1 year to 5 years	12,996	13,070
Over 5 years to 10 years	1,000	998
	18,001	18,072
Mortgage-backed securities:		
Within 1 year	1,331	1,323
Over 1 year to 5 years	7,458	7,416
Over 5 years to 10 years	709	708
Over 10 years	7,955	7,850
	17,453	17,297
Total debt securities	$ 35,454	$ 35,369

For the year ended December 31, 1995, proceeds from the sale of securities available for sale amounted to $1,463,000 resulting in gross realized losses of $49,000. There were no sales of securities during 1997 or 1996.

4. LOANS

A summary of the balances of loans follows:

	December 31, 1997	December 31, 1996
	(In Thousands)	
Mortgage loans:		
Residential	$ 76,414	$ 71,409
Commercial	84,362	67,008
Construction	8,071	9,252
Equity lines of credit	7,108	7,842
Second mortgages	570	167
	176,525	155,678
Less unadvanced loan funds	(3,214)	(3,831)
Total mortgage loans, net	173,311	151,847
Other loans:		
Personal installment	885	819
Commercial	247	48
Education	10	14
Revolving credit	67	57
Total other loans	1,209	938
Total loans	174,520	152,785
Less: Allowance for loan losses	(1,560)	(1,393)
Net deferred interest and loan origination fees	(121)	(226)
Loans, net	$172,839	$151,166

The Bank has sold mortgage loans in the secondary mortgage market and has retained the servicing responsibility and receives fees for the services provided. Loans sold and serviced for others amounted to $5,615,000, $6,667,000 and $8,787,000 at December 31, 1997, 1996 and 1995, respectively. All loans serviced for others were sold without recourse provisions and are not included in the accompanying consolidated balance sheets.

LOANS (concluded)

An analysis of the allowance for loan losses follows:

	Years Ended December 31, 1997	1996	1995
		(In Thousands)	
Balance at beginning of year	$1,393	$1,277	$1,338
Provision for loan losses	174	107	120
	1,567	1,384	1,458
Loans charged-off	(13)	(48)	(188)
Recoveries on loans previously charged-off	6	57	7
Balance at end of year	$1,560	$1,393	$1,277

The following is a summary of information pertaining to impaired and non-accrual loans:

	December 31, 1997	1996
	(In Thousands)	
Impaired loans without a valuation allowance	$ 189	$1,075
Impaired loans with a valuation allowance	639	93
Total impaired loans	$ 828	$1,168
Valuation allowance allocated to impaired loans	$ 71	$ 46
Non-accrual loans	$1,708	$1,168

	Years Ended December 31, 1997	1996	1995
		(In Thousands)	
Average investment in impaired loans	$754	$992	$556
Interest income recognized on impaired loans	$103	$ 53	$ 41
Interest income recognized on a cash basis on impaired loans	$103	$ 53	$ 41

At December 31,1997 there is $82,000 committed to be advanced in connection with impaired loans.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

5. BANKING PREMISES AND EQUIPMENT

A summary of the cost and accumulated depreciation of banking premises and equipment and their estimated useful lives follows:

	December 31, 1997	1996	Estimated Useful Lives
	(In Thousands)		
Banking premises:			
Land	$ 548	$ 548	
Buildings	2,217	2,155	3 - 40 years
Equipment	1,694	1,293	3 - 25 years
	4,459	3,996	
Less accumulated depreciation	(1,826)	(1,578)	
	$2,633	$2,418	

Depreciation expense for the years ended December 31, 1997, 1996 and 1995 amounted to $248,000, $195,000 and $133,000, respectively.

6. DEPOSITS

A summary of deposit balances, by type, is as follows:

	December 31, 1997	1996
	(In Thousands)	
Non-certificate accounts:		
Regular	$ 31,285	$ 30,989
Money market deposits	20,070	20,991
NOW	13,336	12,589
Demand	8,939	6,732
Total non-certificate accounts	73,630	71,301
Term certificates less than $100,000	64,065	59,126
Term certificates $100,000 or more	22,811	19,588
Total certificate accounts	86,876	78,714
Total deposits	$160,506	$150,015

DEPOSITS (concluded)

The maturity distribution of term certificates is as follows:

	December 31, 1997		December 31, 1996	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate
	(Dollars in Thousands)			
Within 1 year	$63,632	5.73%	$60,233	5.47%
Over 1 year to 2 years	13,793	6.01	7,320	5.92
Over 2 years to 3 years	7,781	6.67	4,581	5.70
Over 3 years to 5 years	1,670	5.96	6,580	6.51
	$86,876	5.87%	$78,714	5.61%

A summary of interest expense on deposits is as follows:

	Years Ended December 31, 1997	1996	1995
	(In Thousands)		
Regular	$ 783	$ 783	$ 775
Money market deposits	621	606	603
NOW	169	184	157
Term certificates	4,690	4,053	3,104
	$6,263	$5,626	$4,639

7. FEDERAL HOME LOAN BANK ADVANCES

A summary of advances from the Federal Home Loan Bank of Boston follows:

Maturing During the Year Ending December 31,	December 31, 1997 Amount	Weighted Average Rate	December 31, 1996 Amount	Weighted Average Rate
	(Dollars in Thousands)			
1997	$ —	—%	$22,754	5.76%
1998	33,147	5.84	7,000	5.82
1999	5,000	5.96	—	—
	$38,147	5.86%	$29,754	5.78%

All borrowings from the Federal Home Loan Bank of Boston are secured by stock in the Federal Home Loan Bank of Boston and a blanket lien on "qualified collateral" defined principally as 75% of the carrying value of first mortgage loans on owner-occupied residential property.

The Bank also has an available line of credit with the Federal Home Loan Bank of Boston at an interest rate that adjusts daily. Borrowings under this line are limited to $4,031,000 at December 31, 1997.

8. INCOME TAXES

Allocation of federal and state income taxes between current and deferred portions is as follows:

	Years Ended December 31, 1997	1996	1995
	(In Thousands)		
Current tax provision:			
Federal	$1,343	$1,094	$ 868
State	284	325	310
Utilization of operating loss carryforwards	—	—	(382)
	1,627	1,419	796
Deferred tax provision (benefit):			
Federal	(17)	(5)	397
State	(3)	(11)	41
	(20)	(16)	438
Change in valuation reserve realization assumptions	—	—	(189)
	$1,607	$1,403	$1,045

The reasons for the differences between the statutory federal income tax rate and the effective tax rates are summarized as follows:

	Years Ended December 31, 1997	1996	1995
Statutory rate	34.0%	34.0%	34.0%
Increase (decrease) resulting from:			
State taxes, net of federal tax benefit	4.3	6.0	7.8
Change in valuation allowance	—	—	(6.4)
Other, net	(.6)	.7	—
Effective tax rates	37.7%	40.7%	35.4%

INCOME TAXES (continued)

The components of the net deferred tax asset are as follows:

	December 31, 1997	December 31, 1996
	(In Thousands)	
Deferred tax asset:		
Federal	$ 834	$ 897
State	358	395
	1,192	1,292
Valuation reserve on asset	(55)	(57)
	1,137	1,235
Deferred tax liability:		
Federal	(111)	(101)
State	(32)	(28)
	(143)	(129)
Net deferred tax asset	$ 994	$1,106

The tax effects of each type of income and expense item that give rise to deferred taxes are as follows:

	December 31, 1997	December 31, 1996
	(In Thousands)	
Allowance for loan losses	$ 610	$ 524
Employee benefits	239	223
Other accrued expenses	193	218
Net unrealized loss on securities available for sale	35	167
Other	(28)	31
	1,049	1,163
Valuation reserve	(55)	(57)
Net deferred tax asset	$ 994	$1,106

A summary of the change in the net deferred tax asset is as follows:

	Years Ended December 31, 1997	1996	1995
	(In Thousands)		
Balance at beginning of year	$1,106	$1,045	$1,557
Deferred tax benefit (provision)	20	16	(249)
Net unrealized loss on securities available for sale	(132)	45	(263)
Balance at end of year	$ 994	$1,106	$1,045

INCOME TAXES (concluded)

A summary of the change in the valuation reserve applicable to the net deferred tax asset is as follows:

	Years Ended December 31, 1997	1996	1995
	(In Thousands)		
Balance at beginning of year	$ 57	$ 65	$ 254
Benefits expired	(2)	(8)	—
Change in assumptions due to anticipation of future income	—	—	(189)
Balance at end of year	$ 55	$ 57	$ 65

Tax reserve for loan losses

The federal income tax reserve for loan losses at the Bank's base year was $3,780,000. If any portion of the reserve is used for purposes other than to absorb loan losses, approximately 150% of the amount actually used, limited to the amount of the reserve, will be subject to taxation in the fiscal year in which used. As the Bank intends to use the reserve only to absorb loan losses, a deferred tax liability of approximately $1,550,000 has not been provided. (See Note 1)

9. COMMITMENTS AND CONTINGENCIES

In the normal course of business, there are outstanding commitments and contingencies which are not reflected in the consolidated financial statements.

Loan commitments

The 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 include unused lines of credit, commitments to originate loans, and standby letters of credit. The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets.

The Bank's exposure to credit loss in the event of non-performance by the other party to its financial instruments is represented by the contractual amount of these commitments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

COMMITMENTS AND CONTINGENCIES (concluded)

At December 31, 1997 and 1996, the following financial instruments were outstanding with contract amounts representing credit risk:

	Contract Amount 1997	Contract Amount 1996
	(In Thousands)	
Unused lines of credit	$8,483	$7,782
Commitments to originate loans:		
Commercial Mortgages	6,583	5,830
Residential Mortgages	3,695	3,149
Standby letters of credit	30	80

Commitments to extend credit are agreements to lend to a customer provided 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 may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. The commitments to originate loans and the majority of unused lines of credit are secured by real estate.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

Employment agreements

The Bank has entered into employment agreements with certain senior executives. The original terms of the agreements are for three or two years and automatically extend unless either party gives notice to the contrary. The agreements generally provide for certain lump sum severance payments under certain circumstances, within a one-year period following a "change in control," as defined in the agreements.

Other contingencies

Various legal claims arise from time to time in the normal course of business, which, in the opinion of management, will have no material effect on the Bank's consolidated financial position.

10. STOCKHOLDERS' EQUITY

Minimum regulatory capital requirements

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of its assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

STOCKHOLDERS' EQUITY (concluded)

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 1997 and 1996, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31,1997 and 1996, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, it must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following table. There are no conditions or events since the notification that management believes have changed the Bank's category. The Bank's actual capital amounts and ratios as of December 31, 1997 and 1996 are also presented in the table.

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in Thousands)			
December 31,1997						
Total Capital to Risk-Weighted Assets	$22,987	15.66%	$11,741	8.0%	$14,676	10.0%
Tier 1 Capital to Risk-Weighted Assets	21,427	14.60	5,870	4.0	8,806	6.0
Tier 1 Capital to Average Assets	21,427	9.80	6,559 to 10,932	3.0 to 5.0	10,932	5.0
December 31,1996						
Total Capital to Risk-Weighted Assets	$20,849	16.12%	$10,347	8.0%	$12,934	10.0%
Tier 1 Capital to Risk-Weighted Assets	19,456	15.04	5,173	4.0	7,760	6.0
Tier 1 Capital to Average Assets	19,456	9.90	5,894 to 9,824	3.0 to 5.0	9,824	5.0

Liquidation account

At the time of conversion from mutual to stock form, the Bank established a liquidation account for the benefit of eligible account holders. The liquidation account is reduced annually to the extent that eligible account holders reduce their qualifying deposit. In the event of a complete liquidation, eligible account holders will be entitled to receive a distribution from the liquidation account to the extent that funds are available. According to the Bank's transfer agent, the balance of the liquidation account at December 31, 1997 amounted to $731,000 (unaudited).

11. STOCK OPTION PLANS

At December 31,1997, the Bank has two fixed stock option plans as described below. The Bank applies APB Opinion 25 and related Interpretations in accounting for the plans. Accordingly, no compensation cost has been recognized for the plans. Had compensation cost for the plans been determined based on the fair value at the grant dates for awards under the plans consistent with the method prescribed by SFAS No. 123, "Accounting for Stock-Based Compensation," the Bank's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

	Years Ended December 31,		
	1997	1996	1995
	(In Thousands, except per share amounts)		
Net Income:			
As reported	$2,659	$2,044	$1,906
Pro forma	2,651	1,966	1,827
Earnings per share:			
As reported	$ 2.04	$ 1.57	$ 1.47
Pro forma	2.04	1.51	1.41
Earnings per share-assuming dilution for stock options:			
As reported	$ 2.00	$ 1.56	$ 1.46
Pro forma	1.99	1.50	1.40

Under the Bank's 1988 and 1996 stock option plans, options may be granted to officers, other employees and certain directors as the Stock Option Committee of the Board may determine. A total of 125,000 shares of common stock were reserved for issuance pursuant to options granted under the 1988 plan, and a total of 60,000 shares of common stock were reserved for issuance pursuant to options granted under the 1996 plan. Both "incentive options" and "non-qualified options" may be granted under the plans. All options under both plans will have an exercise price per share equal to, or in excess of, the fair market value of a share of common stock at the date the option is granted and will have a maximum option term of 10 years. Non-qualified stock options granted during 1997, 1996, 1995 and 1993 are immediately exercisable, and options granted prior to 1993 vest over a five-year period.

The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option pricing model with the following assumptions:

	Years Ended December 31,		
	1997	1996	1995
Dividend yield	3.27%	3.27%	2.75%
Expected life	10 years	10 years	10 years
Expected volatility	13.57%	25.79%	27.06%
Risk-free interest rate	6.93%	6.11%	6.28%

STOCK OPTION PLANS (concluded)

Stock option activity is as follows:

	Years Ended December 31,					
	1997		1996		1995	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Shares under option:						
Outstanding at beginning of year	100,000	$11.47	70,500	$10.17	44,500	$ 8.27
Granted	3,000	18.38	32,000	13.75	28,000	12.75
Exercised	(6,000)	10.50	(2,500)	4.00	(2,000)	4.00
Outstanding at end of year	97,000	$11.75	100,000	$11.47	70,500	$10.17
Options exercisable at end of year	97,000	$11.75	100,000	$11.47	70,500	$10.17
Weighted average fair value of options granted during the year		$ 4.51		$ 4.11		$ 4.36

Options outstanding consist of the following:

	December 31,			
	1997		1996	
Option price	Shares	Weighted Average Remaining Contractual Life in Years	Shares	Weighted Average Remaining Contractual Life In Years
$18.375	3,000	10	—	—
13.750	29,000	9	32,000	10
12.750	28,000	8	28,000	9
8.875	37,000	6	39,000	7
4.000	—	—	1,000	4
	97,000		100,000	

12. EMPLOYEE BENEFIT PLANS

Pension Plan

The Bank provides pension benefits for all of its eligible officers and employees through membership in a defined benefit plan of the Savings Banks Employees Retirement Association ("SBERA"). Each employee reaching the age of 21 and having completed at least one year of continuous service and 1,000 hours of service during each twelve-month period beginning with such employee's date of employment becomes a Participant of the Plan. All Participants become fully vested after three years of service or age 62 if earlier. Under the Plan, retirement benefits are based on years of credited service, the highest average compensation (as defined), and the primary social security benefit. In addition, employees may make optional, voluntary contributions to the Plan under several methods. The optional contributions provide retirement benefits to the employee in addition to those otherwise available under the Bank's Plan. Annual contributions by the Bank are based on assessments from SBERA.

Net periodic pension cost is as follows:

	Plan Years Ended October 31,		
	1997	1996	1995
	(In Thousands)		
Service cost - benefits earned during year	$128	$123	$ 82
Interest cost on projected benefits	107	95	87
Actual return on plan assets	(273)	(210)	(221)
Net amortization and deferral	3	3	3
Amortization of net loss	83	66	99
Net periodic pension cost	$ 48	$ 77	$ 50

EMPLOYEE BENEFIT PLANS (concluded)

Pension expense for the years ended December 31, 1997, 1996 and 1995 amounted to $49,000, $89,000, and $54,000, respectively.

According to SBERA, a reconciliation of the funded status of the plan is as follows:

	October 31, 1997	October 31, 1996
	(In Thousands)	
Plan assets at fair value	$2,054	$1,808
Actuarial present value of projected benefit obligation	1,660	1,424
Plan assets greater than projected benefit obligation	394	384
Unamortized net obligation since adoption of SFAS No. 87	26	29
Unrecognized net gain	(999)	(944)
Pension liability	$ (579)	$ (531)

The accumulated benefit obligation (substantially all vested) at October 31, 1997 amounted to $1,157,000.

For the plan years ended October 31, 1997, 1996 and 1995, actuarial assumptions include an assumed discount rate on benefit obligations of 7.25%, 7.50% and 7.00%, respectively. An expected long-term rate of return on plan assets of 8.00%, and an annual salary increase of 6.00% was utilized for all years.

401(k) Plan

Effective August 1, 1996, the Bank adopted a 401(k) Plan whereby each employee reaching the age of 21 and having completed at least 1,000 hours of service in a twelve-month period, beginning with date of employment, becomes eligible to participate in the Plan. Employees may contribute up to 15% of their compensation subject to certain limits based on federal tax laws. The Bank does not make matching contributions to the Plan.

13. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Bank has granted loans to principal officers and directors and their affiliates amounting to $21,000 at December 31, 1997 and $22,000 at December 31, 1996. In 1993, the Bank established a policy whereby new loans (excluding passbook loans) cannot be granted to employees, officers or directors.

14. FAIR VALUE OF FINANCIAL INSTRUMENTS

SFAS No. 107, "Disclosures about Fair Value of Financial Instruments," requires disclosure of estimated fair values of all financial instruments where it is practicable to estimate such values. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. Statement No. 107 excludes certain financial instruments and all non-financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Bank.

The following methods and assumptions were used by the Bank in estimating fair value disclosures for financial instruments:

Cash and cash equivalents: The carrying amounts of cash, due from banks and interest-bearing deposits approximate fair values.

FAIR VALUE OF FINANCIAL INSTRUMENTS (concluded)

Securities available for sale: Fair values for securities available for sale are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

Loans: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for non-performing loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

Federal Home Loan Bank stock: The carrying value of Federal Home Loan Bank stock is deemed to approximate fair value based on the redemption provisions of the Federal Home Loan Bank of Boston.

Deposits: The fair values of non-certificate accounts are, by definition, equal to the amount payable on demand at the reporting date which is their carrying amount. Fair values for certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Federal Home Loan Bank advances: The fair values of the Bank's borrowings are estimated using discounted cash flow analyses based on the Bank's current incremental borrowing rates for similar types of borrowing arrangements.

Other borrowed funds: The carrying amounts of other borrowed funds approximate fair value.

Accrued interest: The carrying amounts of accrued interest approximate fair value.

Off-balance-sheet instruments: Fair values for off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. At December 31, 1997 and 1996, the fair value of commitments outstanding is not significant since fees charged are not material.

The carrying amounts and estimated fair values of the Bank's financial instruments are as follows:

	December 31, 1997		1996	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(In Thousands)			
Financial assets:				
Cash and cash equivalents	$ 7,268	$ 7,268	$ 11,640	$ 11,640
Securities available for sale	35,369	35,369	32,321	32,321
Loans, net	172,839	174,668	151,166	152,381
Accrued interest receivable	1,243	1,243	1,060	1,060
Federal Home Loan Bank stock	1,900	1,900	1,450	1,450
Financial liabilities:				
Deposits	160,506	160,852	150,015	150,328
Federal Home Loan Bank advances	38,147	38,139	29,754	29,767
Other borrowed funds	319	319	188	188
Accrued interest payable	205	205	582	582

15. QUARTERLY FINANCIAL DATA (UNAUDITED)

Quarterly results of operations for the years ended December 31, 1997 and 1996 are as follows:

	Years Ended December 31,							
	1997				1996			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
	(In Thousands, Except Per Share Data)							
Interest and dividend income	$ 4,268	$4,214	$ 4,059	$ 3,864	$ 3,734	$3,587	$ 3,387	$ 3,254
Interest expense	2,143	2,102	1,995	1,920	1,844	1,778	1,679	1,655
Net interest income	2,125	2,112	2,064	1,944	1,890	1,809	1,708	1,599
Provision for loan losses	48	48	39	39	38	30	30	9
Net interest income, after provision for loan losses	2,077	2,064	2,025	1,905	1,852	1,779	1,678	1,590
Other income	173	144	157	179	180	141	157	136
Operating expenses	1,149	1,103	1,108	1,098	1,063	1,010	999	994
Income before income taxes	1,101	1,105	1,074	986	969	910	836	732
Income tax provision	420	424	411	352	369	382	349	303
Net income	$ 681	$ 681	$ 663	$ 634	$ 600	$ 528	$ 487	$ 429
Earnings per share	$ 0.52	$ 0.52	$ 0.51	$ 0.49	$ 0.46	$ 0.40	$ 0.38	$ 0.33
Earnings per share-assuming dilution for stock options	$ 0.51	$ 0.51	$ 0.50	$ 0.48	$ 0.46	$ 0.40	$ 0.37	$ 0.33
Cash dividends declared per share	$ 0.25(1)	$ 0.12	$ 0.12	$ 0.10	$ 0.19(2)	$ 0.09	$ 0.09	$ 0.08

(1) Includes a special dividend of $0.13 per share declared on December 1, 1997.

(2) Includes a special dividend of $0.10 per share declared on December 2, 1996.

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Form 10-K
A copy of the Bank's Annual Report on Form 10-K for the fiscal year ended December 31, 1997 as filed with the Federal Deposit Insurance Corporation, may be obtained without charge by any stockholder of the Bank upon written request addressed to the Investor Relations Department.

STOCK DATA

Hingham Institution for Savings common shares are listed and traded on The Nasdaq Stock Market under the symbol HIFS.

As of December 31, 1997 there were approximately 506 stockholders of record, holding 644,344 outstanding shares of common stock. These shares do not include the number of persons who hold their shares in nominee or street name through various brokerage firms.

The following table presents the quarterly high and low bid prices for the Bank's common stock reported by Nasdaq.

	High	Low
1997		
First Quarter	$19 1/4	$18 1/4
Second Quarter	21 3/4	18
Third Quarter	28 5/8	20 3/4
Fourth Quarter	29	26 3/4
1996		
First Quarter	$15	$13
Second Quarter	14 3/4	13 3/4
Third Quarter	15 1/2	14
Fourth Quarter	18 3/4	15

The closing sale price of the Bank's common stock at December 31, 1997 was $28.75 per share.

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