FEDERAL DEPOSIT INSURANCE CORPORATION

Washington, D.C., 20429
FORM 10-Q

(Mark one)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2019

OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period ________ to ________.

Commission File Number: FDIC Certificate No. 90211

HINGHAM INSTITUTION FOR SAVINGS

(Exact name of registrant as specified in its charter)

Massachusetts	**04-1442480**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
55 Main Street, Hingham, Massachusetts	**02043**
(Address of principal offices)	**(Zip Code)**

(781) 749-2200
(Registrant's telephone number, including area code)
Securities Registered pursuant to Section 12(b) of the Act:

Common Stock, $1.00 par value per share	**NASDAQ Stock Market, LLC**
(Title of Class)	**(Name of exchange on which registered)**

Securities registered under Section 12(g) of the Act: None

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer	☐	Accelerated filer	☒
Non-accelerated filer	☐	Smaller reporting company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

The number of shares outstanding of each of the Bank's classes of Common Stock, as of the latest practicable date is:

Class: Common Stock $1.00 par value per share
Outstanding as of May 8, 2019: 2,133,750 shares

Table of Contents

PART I – FINANCIAL INFORMATION

Item 1 – Financial Statements

HINGHAM INSTITUTION FOR SAVINGS AND SUBSIDIARIES

Consolidated Balance Sheets

	December 31, 2018	March 31, 2019
(Unaudited)	(In Thousands)	
ASSETS		
Cash and due from banks	$ 8,004	$ **7,433**
Federal Reserve and other short-term investments	287,971	**286,333**
Cash and cash equivalents	295,975	**293,766**
Securities available for sale, at fair value	14	**13**
Equity securities, at fair value	38,446	**42,711**
Federal Home Loan Bank stock, at cost	28,696	**30,617**
Loans, net of allowance for loan losses of $13,808,000 at December 31, 2018 and $14,232,000 at March 31, 2019	2,009,288	**2,092,313**
Bank-owned life insurance	12,476	**12,542**
Premises and equipment, net	14,553	**14,388**
Accrued interest receivable	4,581	**5,180**
Deferred income tax asset, net	2,258	**1,626**
Other assets	2,300	**4,233**
Total assets	$ 2,408,587	$ **2,497,389**
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Interest-bearing	$ 1,359,581	$ **1,327,451**
Demand	213,573	**227,872**
Total deposits	1,573,154	**1,555,323**
Federal Home Loan Bank advances	606,600	**702,100**
Mortgage payable	751	**735**
Mortgagors' escrow accounts	7,402	**7,201**
Accrued interest payable	2,187	**2,086**
Other liabilities	5,917	**8,263**
Total liabilities	2,196,011	**2,275,708**
Stockholders' equity:		
Preferred stock, $1.00 par value, 2,500,000 shares authorized; none issued	—	**—**
Common stock, $1.00 par value, 5,000,000 shares authorized; 2,132,750 shares issued and outstanding at December 31, 2018 and 2,133,750 and shares issued and outstanding at March 31, 2019	2,133	**2,134**
Additional paid-in capital	11,863	**11,954**
Undivided profits	198,580	**207,593**
Total stockholders' equity	212,576	**221,681**
Total liabilities and stockholders' equity	$ 2,408,587	$ **2,497,389**

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

HINGHAM INSTITUTION FOR SAVINGS AND SUBSIDIARIES

Consolidated Statements of Net Income and Comprehensive Income

	Three Months Ended March 31,	
	2018	2019
(Unaudited)	(In Thousands, except per share amounts)	
Interest and dividend income:		
Loans	$ 20,417	$ **23,080**
Equity securities	479	**489**
Federal Reserve and other short-term investments	1,241	**1,560**
Total interest and dividend income	22,137	**25,129**
Interest expense:		
Deposits	3,567	**6,146**
Federal Home Loan Bank advances	2,093	**3,128**
Mortgage payable	12	**11**
Total interest expense	5,672	**9,285**
Net interest income	16,465	**15,844**
Provision for loan losses	285	**425**
Net interest income, after provision for loan losses	16,180	**15,419**
Other income:		
Customer service fees on deposits	206	**186**
Increase in cash surrender value of bank-owned life insurance	68	**66**
Gain on equity securities, net	966	**2,869**
Miscellaneous	44	**41**
Total other income	1,284	**3,162**
Operating expenses:		
Salaries and employee benefits	3,212	**3,147**
Occupancy and equipment	466	**454**
Data processing	341	**434**
Deposit insurance	273	**243**
Marketing	167	**132**
Foreclosure	5	**23**
Other general and administrative	639	**709**
Total operating expenses	5,103	**5,142**
Income before income taxes	12,361	**13,439**
Income tax provision	3,449	**3,615**
Net income and comprehensive income	$ 8,912	$ **9,824**
Weighted average common shares outstanding:		
Basic	2,133	**2,133**
Diluted	2,186	**2,182**
Earnings per share:		
Basic	$ 4.18	$ **4.61**
Diluted	$ 4.08	$ **4.50**

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

HINGHAM INSTITUTION FOR SAVINGS AND SUBSIDIARIES
Consolidated Statements of Changes in Stockholders' Equity
For the Three Months Ended
March 31, 2018 and 2019

(Unaudited)	Common Stock	Additional Paid-In Capital	Undivided Profits	Accumulated Other Comprehensive Income	Total Stockholders' Equity
			(In Thousands)		
Balance at December 31, 2017	$ 2,133	$ 11,750	$ 165,596	$ 6,679	$ 186,158
Cumulative effect of change in accounting principle (Note 5)	—	—	6,679	(6,679)	—
Comprehensive income	—	—	8,912	—	8,912
Share-based compensation expense	—	44	—	—	44
Cash dividends declared – common ($0.34 per share)	—	—	(726)	—	(726)
Balance at March 31, 2018	$ 2,133	$ 11,794	$ 180,461	$ —	$ 194,388
Balance at December 31, 2018	**$ 2,133**	**$ 11,863**	**$ 198,580**	**$ —**	**$ 212,576**
Comprehensive income	**—**	**—**	**9,824**	**—**	**9,824**
Share-based compensation expense	**—**	**21**	**—**	**—**	**21**
Stock options exercised	**1**	**70**	**—**	**—**	**71**
Cash dividends declared – common ($0.38 per share)	**—**	**—**	**(811)**	**—**	**(811)**
Balance at March 31, 2019	**$ 2,134**	**$ 11,954**	**$ 207,593**	**$ —**	**$ 221,681**

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

HINGHAM INSTITUTION FOR SAVINGS AND SUBSIDIARIES
Consolidated Statements of Cash Flows

(Unaudited)	Three Months Ended March 31, 2018	Three Months Ended March 31, 2019
	(In Thousands)	
Cash flows from operating activities:		
Net income	$ 8,912	**$ 9,824**
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	285	**425**
Amortization of deferred loan origination costs, net	146	**147**
Share-based compensation expense	44	**21**
Deferred income tax provision	198	**632**
Depreciation and amortization of premises and equipment	157	**163**
Increase in cash surrender value of bank-owned life insurance	(68)	**(66)**
Gain on equity securities	(966)	**(2,869)**
Changes in operating assets and liabilities:		
Accrued interest receivable and other assets	(669)	**(2,532)**
Accrued interest payable and other liabilities	2,014	**3,288**
Net cash provided by operating activities	10,053	**9,033**
Cash flows from investing activities:		
Activity in securities available for sale:		
Maturities, payments and calls	—	**1**
Activity in equity securities:		
Proceeds from sales	124	**26**
Purchases	(2,684)	**(1,422)**
Purchase of Federal Home Loan Bank stock	—	**(10,380)**
Proceeds from redemption of Federal Home Loan Bank stock	2,572	**8,459**
Loans originated, net of payments received	(38,558)	**(83,597)**
Additions to premises and equipment	(36)	**2**
Net cash used in investing activities	(38,582)	**(86,911)**

(continued)

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

HINGHAM INSTITUTION FOR SAVINGS AND SUBSIDIARIES
Consolidated Statements of Cash Flows (concluded)

	Three Months Ended March 31,	
	2018	2019
(Unaudited)	(In Thousands)	
Cash flows from financing activities:		
Increase (decrease) in deposits	25,946	**(17,831)**
Increase (decrease) in mortgagors' escrow accounts	127	**(201)**
Cash dividends paid on common stock	(1,450)	**(1,854)**
Proceeds from stock options exercised	—	**71**
Net change in Federal Home Loan Bank advances with maturities of three months or less	(50,000)	**(125,000)**
Proceeds from Federal Home Loan Bank advances with maturities of more than three months	—	**224,700**
Repayment of Federal Home Loan Bank advances with maturities of more than three months	(30,040)	**(4,200)**
Repayment of mortgage payable	(15)	**(16)**
Net cash provided by (used in) financing activities	(55,432)	**75,669**
Net change in cash and cash equivalents	(83,961)	**(2,209)**
Cash and cash equivalents at beginning of period	355,229	**295,975**
Cash and cash equivalents at end of period	$ 271,268	$ **293,766**
Supplementary information:		
Interest paid on deposit accounts	$ 3,400	$ **6,482**
Interest paid on Federal Home Loan Bank advances and mortgage payable	2,073	**2,904**
Income taxes paid	2,005	**1,602**
Non-cash activities:		
Real estate acquired through foreclosure	$ —	$ **—**

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

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated interim financial statements of Hingham Institution for Savings (the "Bank") have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial statements and with the instructions to SEC Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements.

Financial information as of March 31, 2019, and for the three months ended March 31, 2018 and 2019, is unaudited and, in the opinion of management, reflects all adjustments necessary for a fair presentation of such information. Such adjustments were of a normal recurring nature. Interim results are not necessarily indicative of results to be expected for the entire year. The unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements of the Bank for the year ended December 31, 2018 filed on Form 10-K.

Earnings per common share

Basic earnings per share represent income available to common stockholders divided by the weighted-average number of shares outstanding during the period. Diluted earnings per share reflect additional shares that would have been outstanding if dilutive potential shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential shares that may be issued by the Bank relate solely to outstanding stock options and are determined using the treasury stock method. The amount of excess tax benefit that would be credited to additional paid-in capital assuming exercise of the options is not considered in the proceeds when applying the treasury stock method.

Earnings per common share have been computed based on the following:

	Three Months Ended March 31,	
	2018	**2019**
	(In Thousands)	
Average number of shares outstanding used to calculate basic earnings per share	2,133	**2,133**
Effect of dilutive options	53	**49**
Average number of shares outstanding used to calculate diluted earnings per share	2,186	**2,182**

There were no antidilutive options for the quarters ended March 31, 2018 or 2019.

Fair value hierarchy

The Bank groups its assets measured at fair value in three levels, based on the markets in which the assets are traded and the reliability of the assumptions used to determine fair value, as follows:

Level 1 – Valuation is based on quoted prices in active markets for identical assets. Level 1 assets generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets.

Level 2 – Valuation is based on observable inputs other than Level 1 prices, such as quoted prices for similar assets; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets.

Level 3 – Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets. Level 3 assets include those whose value is determined using unobservable inputs to pricing models, discounted cash flow methodologies, or similar techniques, as well as assets for which the determination of fair value requires significant management judgment or estimation.

Loans

The Bank's loan portfolio includes residential real estate, commercial real estate, construction, home equity, commercial and consumer segments. A substantial majority of the loan portfolio is secured by real estate in the southeastern Massachusetts area. The remainder of the real estate loan portfolio is located in the Washington D.C. metropolitan area ("WMA"). The ability of the Bank's debtors to honor their contracts is dependent upon the real estate, construction, and general economic conditions in these markets.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and net deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on mortgage and commercial loans is discontinued at the time a loan is 90 days past due (the loan is in default) unless the credit is well-secured and in process of collection. Personal loans are typically charged off no later than becoming 180 days past due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on non-accrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on non-accrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for loan losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance when collected.

The allowance for loan losses is evaluated on a regular basis by management. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance consists of general and allocated loss components, as further discussed below.

General component

The general component of the allowance for loan losses is based on historical loss experience adjusted for qualitative factors stratified by loan segment. Management uses a rolling average of historical losses based on a time frame (currently two years) appropriate to capture relevant loss data for each loan segment. This historical loss factor is adjusted for the following qualitative factors: levels/trends in delinquencies; trends in volume and terms of loans; effects of changes in risk selection and underwriting standards and other changes in lending policies, procedures and practices; experience/ability/depth of lending management and staff; national and local economic trends and conditions; industry conditions and effects of changes in credit concentrations. There were no changes in the Bank's policies or methodology pertaining to the general component of the allowance for loan losses during the three months ended March 31, 2019.

The qualitative factors are determined based on the various risk characteristics of each loan segment. Risk characteristics relevant to each portfolio segment are as follows:

Residential real estate – The Bank generally does not originate loans with a loan-to-value ratio greater than 80 percent (without private mortgage insurance). All loans in this segment are collateralized by residential real estate that is owner-occupied at the time of origination and repayment is dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality in this segment. The Bank only originates these loans in Massachusetts.

Commercial real estate – Loans in this segment are primarily secured by income-producing properties throughout Massachusetts. Beginning in late 2016, the Bank also originates loans on income producing commercial real estate in the greater Washington D.C. metropolitan area. Underwriting and portfolio management policies are the same for both markets. Generally, loan amounts do not exceed 75% of the appraised value of the collateral. The underlying cash flows generated by the properties are adversely impacted by a downturn in the economy as evidenced by increased vacancy rates which, in turn, will have an effect on the credit quality in this segment. Management obtains rent rolls annually and regularly monitors the cash flows of these loans.

Construction – Loans in this segment include both owner-occupied and speculative real estate development loans for which payment is derived from sale of the property. Credit risk is affected by cost overruns, time to sell at an adequate price, the overall health of the economy and market conditions. The Bank only originates these loans in Massachusetts.

Home equity – Loans in this segment include equity lines of credit and second mortgage loans, and are generally collateralized by second liens on residential real estate. Repayment is dependent on the credit quality of the individual borrower. The Bank generally does not originate loans with combined loan-to-value ratios greater than 70% when taking into account both the balance of the home equity loans and the first mortgage loan. Similar to residential real estate, the overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality in this segment. The Bank only originates these loans in Massachusetts.

Commercial – Loans in this segment are made to businesses and are generally secured by assets of the business. Repayment is expected from the cash flows of the business. A weakened economy, and resultant decreased consumer spending, will have an effect on the credit quality in this segment. These loans are not a focus of the Bank's origination program, and are originated only in Massachusetts.

Consumer – Loans in this segment are generally unsecured and repayment is dependent on the credit quality of the individual borrower. These loans are not a focus of the Bank's origination program, and are originated only in Massachusetts.

<u>Allocated component</u>

The allocated component relates to loans that are classified as impaired. Impairment is measured on a loan-by-loan basis for residential real estate, commercial real estate, construction, home equity and commercial loans. 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. Impaired loans are generally maintained on a non-accrual basis. 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, or the fair value of the collateral if the loan is collateral dependent. An allowance is established when the discounted cash flows (or collateral value) of the impaired loan is lower than the carrying amount of that loan. Large groups of smaller balance homogeneous loans, such as consumer loans, are collectively evaluated for impairment.

The Bank periodically may agree to modify the contractual terms of loans. When a loan is modified and a concession is made to a borrower experiencing financial difficulty, the modification is considered a troubled debt restructuring ("TDR"). All TDRs are initially classified as impaired.

Leases

On January 1, 2019, the Bank adopted Financial Accounting Standards Board ("FASB") Accounting Standards Update ("ASU") 2016-02, *Leases (Topic 842*), and ASU 2018-11, *Leases (Topic 842): Targeted Improvements*. As a result of the adoption of ASU 2016-02, the Bank recorded operating lease right-of-use ("ROU") assets and operating lease liabilities amounting to $1.7 million effective January 1, 2019 relating to operating leases for some of its banking offices. The ROU asset is included in other assets and the operating lease liability is included in other liabilities on the Bank's Consolidated Balance Sheets. At March 31, 2019, both the ROU asset and the corresponding operating lease liability were $1.6 million. Operating lease costs for the quarter ended March 31, 2019 were $87,000.

ROU assets represent the Bank's right to use an underlying asset for the lease term and lease liabilities represent the Bank's obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. As most of the Bank's leases do not provide an implicit rate, the Bank uses the Bank's incremental borrowing rate, which is generally the Federal Home Loan Bank classic advance rate, based on the information available at commencement date in determining the present value of lease payments. The Bank will use the implicit rate when readily determinable. The weighted average discount rate for operating leases as of March 31, 2019 was 2.9%. The Bank's lease terms may include options to extend when it is reasonably certain that the Bank will exercise that option. The initial term of these lease agreements is five years, and the agreements contain up to three extension options for subsequent five year terms. Management considered options that have been exercised or are reasonably certain to be exercised in the recognition of the operating lease ROU asset. The weighted average remaining lease term for operating leases as of March 31, 2019 is 5.9 years. For operating leases, lease expense is recognized on a straight-line basis over the lease term.

The Bank has lease agreements with lease and non-lease components, which are generally accounted for separately. The Bank has not elected the practical expedient to account for lease and non-lease components as one lease component.

The Bank has elected to adopt the lease guidance retrospectively at the beginning of 2019. The adoption did not result in any cumulative-effect adjustment to beginning retained earnings. The Bank has elected certain practical expedients upon adoption and therefore has not reassessed whether any expired or existing contracts contain leases, has not reassessed the lease classification for any expired or existing leases and has not reassessed initial direct costs for any existing leases.

The maturities of lease liabilities are as follows at March 31, 2019:

Years	Amount (In Thousands)
2019 (remaining nine months)	$ **247**
2020	**336**
2021	**256**
2022	**245**
2023	**253**
Thereafter	**423**
Total lease payments	**1,760**
Imputed interest	**(151)**
Total lease liability	$ **1,609**

Reclassification

Certain amounts in the 2018 consolidated financial statements have been reclassified to conform to the 2019 presentation.

NOTE 2: COMMITMENTS

At December 31, 2018 and March 31, 2019, outstanding loan commitments were as follows:

	December 31, 2018	March 31, 2019
	(In Thousands)	
Unused lines of credit	$ 127,535	$ **128,505**
Commitments to originate loans	26,865	**91,754**
Unadvanced funds on construction loans	104,484	**95,895**
Standby letters of credit	25	**25**
Total	$ 258,909	$ **316,179**

At March 31, 2019, the Bank had the following contractual obligations outstanding:

	Payments Due by Year				
	Total	Less Than One Year	One to Three Years	Three to Five Years	More than Five Years
	(In Thousands)				
Certificates of deposit	$ **731,188**	$ **609,327**	$ **112,986**	$ **8,875**	$ **—**
Federal Home Loan Bank advances	**702,100**	**667,100**	**35,000**	**—**	**—**
Mortgage payable (1)	**735**	**65**	**142**	**161**	**367**
Data processing agreements (2)	**3,959**	**880**	**1,829**	**1,250**	**—**

(1) Under the mortgage agreement, the balance of the note may be paid off at any date after January 2020 without penalty.

(2) Estimated payments are subject to change based on transaction volume.

NOTE 3: DIVIDEND DECLARATION

On March 27, 2019, the Board of Directors declared a cash dividend of $0.38 per share to all stockholders of record as of April 8, 2019, payable April 17, 2019.

NOTE 4: FAIR VALUES OF ASSETS AND LIABILITIES

Determination of Fair Value

The Bank uses fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Bank's assets and liabilities. 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 fair value estimates may not be realized in an immediate settlement of the asset or liability.

Assets Measured at Fair Value on a Recurring Basis

Assets measured at fair value on a recurring basis are summarized below. There are no liabilities measured at fair value on a recurring basis.

	Level 1	Level 2	Level 3	Total Fair Value
	(In Thousands)			
December 31, 2018				
Securities available for sale	$ —	$ 14	$ —	$ 14
Equity securities	35,730	2,716	—	38,446
Total	$ 35,730	$ 2,730	$ —	$ 38,460
March 31, 2019				
Securities available for sale	**$ —**	**$ 13**	**$ —**	**$ 13**
Equity securities	**39,873**	**2,838**	**—**	**42,711**
Total	**$ 39,873**	**$ 2,851**	**$ —**	**$ 42,724**

Assets Measured at Fair Value on a Non-recurring Basis

The Bank may also be required, from time to time, to measure certain other assets on a non-recurring basis in accordance with generally accepted accounting principles. These adjustments to fair value usually result from application of lower-of-cost-or-market accounting or write-downs of individual assets.

There are no assets or liabilities measured at fair value on a non-recurring basis at December 31, 2018 and March 31, 2019.

Notes to Unaudited Consolidated Financial Statements (continued)

Summary of Fair Values of Financial Instruments

The estimated fair values, determined using the exit price notion, and related carrying amounts, of the Bank's financial instruments are as follows. Certain financial instruments and all nonfinancial instruments are exempt from disclosure requirements. Accordingly, the aggregate fair value amounts presented herein do not represent the underlying fair value of the Bank.

	Carrying Amount	Fair Value		
		Level 1	Level 2	Level 3
	(In Thousands)			
December 31, 2018				
Financial assets:				
Cash and cash equivalents	$ 295,975	$ 295,975	$ —	$ —
Debt securities available for sale	14	—	14	—
Equity securities	38,446	35,730	2,716	—
Federal Home Loan Bank stock	28,696	—	—	28,696
Loans, net	2,009,288	—	—	2,018,874
Accrued interest receivable	4,581	—	—	4,581
Financial liabilities:				
Deposits	$ 1,573,154	$ —	$ —	$ 1,576,359
Federal Home Loan Bank advances	606,600	—	606,568	—
Mortgage payable	751	—	—	776
Mortgagors' escrow accounts	7,402	—	—	7,402
Accrued interest payable	2,187	—	—	2,187
March 31, 2019				
Financial assets:				
Cash and cash equivalents	**$ 293,766**	**$ 293,766**	**$ —**	**$ —**
Debt securities available for sale	**13**	**—**	**13**	**—**
Equity securities	**42,711**	**39,873**	**2,838**	**—**
Federal Home Loan Bank stock	**30,617**	**—**	**—**	**30,617**
Loans, net	**2,092,313**	**—**	**—**	**2,102,447**
Accrued interest receivable	**5,180**	**—**	**—**	**5,180**
Financial liabilities:				
Deposits	**$ 1,555,323**	**$ —**	**$ —**	**$ 1,558,881**
Federal Home Loan Bank advances	**702,100**	**—**	**702,105**	**—**
Mortgage payable	**735**	**—**	**—**	**756**
Mortgagors' escrow accounts	**7,201**	**—**	**—**	**7,201**
Accrued interest payable	**2,086**	**—**	**—**	**2,086**

NOTE 5: SECURITIES

Securities available for sale

At December 31, 2018 and March 31, 2019, all securities available for sale were residential mortgage-backed securities. Both the amortized cost and fair value of the residential mortgage-backed securities were $14,000 and $13,000 at December 31, 2018 and March 31, 2019, respectively. There were no gross unrealized gains or gross unrealized losses at either December 31, 2018 or March 31, 2019.

At December 31, 2018 and March 31, 2019, all debt securities were pledged to secure Federal Home Loan Bank advances. There were no sales of securities available for sale during the quarter ended March 31, 2018 or 2019.

Equity securities

At March 31, 2019, equity securities include a $7.8 million investment in the Community Reinvestment Act Qualified Investment Fund and $34.9 million investment in equity securities in the banking, insurance, ratings, payments, technology and industrial sectors.

Effective January 1, 2018, the Bank adopted FASB ASU 2016-01, *Financial Instruments – Overall, (Subtopic 825-10).* Consequently, beginning January 1, 2018, equity securities (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) are measured at fair value with changes in fair value recognized in net income. As a result, net unrealized gains and losses are reflected in the Consolidated Statements of Net Income, regardless of whether such gains and losses are realized. The cumulative effect of adopting this standard was to increase undivided profits and decrease accumulated other comprehensive income by $6.7 million on January 1, 2018.

For the three months ended March 31, 2018 and 2019, proceeds from sales of equity securities amounted to $124,000 and $26,000, respectively. Unrealized gains recognized during the first quarter of 2018 and 2019 on equity securities still held at March 31, 2018 and 2019 totaled $953,000 and $2.9 million, respectively.

NOTE 6: LOANS

A summary of the balances of loans is as follows:

	December 31, 2018	March 31, 2019
	(In Thousands)	
Real estate loans:		
Residential	$ 709,982	**$ 713,352**
Commercial	1,150,535	**1,206,009**
Construction	127,274	**151,905**
Home equity	31,859	**31,799**
Total real estate loans	2,019,650	**2,103,065**
Other loans:		
Commercial	128	**194**
Consumer	414	**371**
Total other loans	542	**565**
Total loans	2,020,192	**2,103,630**
Allowance for loan losses	(13,808)	**(14,232)**
Net deferred loan origination costs	2,904	**2,915**
Loans, net	$ 2,009,288	**$ 2,092,313**

Notes to Unaudited Consolidated Financial Statements (continued)

A blanket lien on "qualified collateral," defined principally as 67-78% of the carrying value of first mortgage loans on certain owner-occupied residential property, 77% of the carrying value of first mortgage loans on certain non-owner-occupied residential property, 74% of the carrying value of first mortgage loans on certain multi-family residential property and 62% of the carrying value of loans on certain commercial property, is used to secure borrowings from the Federal Home Loan Bank of Boston. In addition, qualified collateral includes 93% of the fair value of all debt securities. Additionally, a blanket lien on home equity and second mortgage loans is used to secure borrowing from the Federal Reserve Bank of Boston through its discount window.

The following is a summary of past due and non-accrual loans at December 31, 2018 and March 31, 2019:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Loans on Non-accrual
			(In Thousands)		
December 31, 2018					
Residential real estate	$ 9,200	$ 89	$ —	$ 9,289	$ —
Commercial real estate	1,104	—	484	1,588	484
Home equity	171	—	—	171	—
Commercial	2	—	—	2	—
Total loans	$ 10,477	$ 89	$ 484	$ 11,050	$ 484
March 31, 2019					
Residential real estate	**$ 2,451**	**$ —**	**$ —**	**$ 2,451**	**$ 472**
Commercial real estate	**—**	**—**	**—**	**—**	**152**
Home equity	**198**	**—**	**—**	**198**	**—**
Consumer	**3**	**—**	**—**	**3**	**—**
Total loans	**$ 2,652**	**$ —**	**$ —**	**$ 2,652**	**$ 624**

At December 31, 2018 and March 31, 2019, there were no loans past due 90 days or more and still accruing interest.

An analysis of the activity in the allowance for loan losses, by segment, for the periods ended March 31, 2018 and 2019 follows:

	Residential Real Estate	Commercial Real Estate	Construction	Home Equity	Commercial	Consumer	Total
				(In Thousands)			
Three months ended March 31, 2018							
Balance December 31, 2017	$ 2,607	$ 8,508	$ 1,301	$ 113	$ 2	$ 6	$ 12,537
Provision (credit) for loan losses	110	218	(26)	(15)	—	(2)	285
Loans charged off	—	—	—	—	—	—	—
Recoveries of loans previously charged off	1	—	—	—	—	—	1
Balance March 31, 2018	$ 2,718	$ 8,726	$ 1,275	$ 98	$ 2	$ 4	$ 12,823
Three months ended March 31, 2019							
Balance December 31, 2018	**$ 2,674**	**$ 9,687**	**$ 1,337**	**$ 105**	**$ 1**	**$ 4**	**$ 13,808**
Provision (credit) for loan losses	**(66)**	**249**	**245**	**(3)**	**1**	**(1)**	**425**
Loans charged off	**—**	**(3)**	**—**	**—**	**—**	**—**	**(3)**
Recoveries of loans previously charged off	**1**	**—**	**—**	**—**	**—**	**1**	**2**
Balance March 31, 2019	**$ 2,609**	**$ 9,933**	**$ 1,582**	**$ 102**	**$ 2**	**$ 4**	**$ 14,232**

An analysis of the allowance for loan losses, by segment, as of December 31, 2018 and March 31, 2019 follows:

	Residential Real Estate	Commercial Real Estate	Construction	Home Equity	Commercial	Consumer	Total
				(In Thousands)			
December 31, 2018							
Allowance for impaired loans	$ 118	$ —	$ —	$ —	$ —	$ —	$ 118
Allowance for non-impaired loans	2,556	9,687	1,337	105	1	4	13,690
	$ 2,674	$ 9,687	$ 1,337	$ 105	$ 1	$ 4	$ 13,808
Impaired loans	$ 1,397	$ 484	$ —	$ —	$ —	$ —	$ 1,881
Non-impaired loans	708,585	1,150,051	127,274	31,859	128	414	2,018,311
	$ 709,982	$ 1,150,535	$ 127,274	$ 31,859	$ 128	$ 414	$ 2,020,192
March 31, 2019							
Allowance for impaired loans	**$ 115**	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**	**$ 115**
Allowance for non-impaired loans	**2,494**	**9,933**	**1,582**	**102**	**2**	**4**	**14,117**
	$ 2,609	**$ 9,933**	**$ 1,582**	**$ 102**	**$ 2**	**$ 4**	**$ 14,232**
Impaired loans	**$ 1,862**	**$ 152**	**$ —**	**$ —**	**$ —**	**$ —**	**$ 2,014**
Non-impaired loans	**711,490**	**1,205,857**	**151,905**	**31,799**	**194**	**371**	**2,101,616**
	$ 713,352	**$ 1,206,009**	**$ 151,905**	**$ 31,799**	**$ 194**	**$ 371**	**$ 2,103,630**

The following is a summary of impaired loans at December 31, 2018 and March 31, 2019:

	December 31, 2018			March 31, 2019		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
			(In Thousands)			
Impaired loans without a valuation allowance:						
Residential real estate	$ 362	$ 415		**$ 833**	**$ 886**	
Commercial real estate	484	484		**152**	**152**	
Total	846	899		**985**	**1,038**	
Impaired loans with a valuation allowance:						
Residential real estate	1,035	1,035	$ 118	**1,029**	**1,029**	**$ 115**
Total impaired loans	$ 1,881	$ 1,934	$ 118	**$ 2,014**	**$ 2,067**	**$ 115**

The following is information pertaining to impaired loans for periods ended March 31, 2018 and 2019:

	Three Months Ended March 31, 2018			Three Months Ended March 31, 2019		
	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized on Cash Basis	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized on Cash Basis
			(In Thousands)			
Impaired loans:						
Residential real estate	$ 2,835	$ 18	$ 20	**$ 1,709**	**$ 16**	**$ 9**
Commercial real estate	477	4	2	**373**	**—**	**15**
Home equity	262	—	6	**—**	**—**	**—**
Total impaired loans	$ 3,574	$ 22	$ 28	**$ 2,082**	**$ 16**	**$ 24**

No additional funds are committed to be advanced in connection with impaired loans.

In the course of resolving non-performing loans, the Bank may choose to restructure the contractual terms of certain loans, with terms modified to fit the ability of the borrower to repay in line with its current financial status. A loan is considered a troubled debt restructure if, for reasons related to the debtor's financial difficulties, a concession is granted to the debtor that would not otherwise be considered. For the three months ended March 31, 2018 and 2019, troubled debt restructurings were not considered material.

Credit Quality Information

The Bank uses a seven-grade internal rating system for residential real estate, commercial real estate, construction and commercial loans as follows:

Loans rated 1-3B: Loans in this category are considered "pass" rated with low to average risk.

Loans rated 4: Loans in this category are considered "special mention." These loans are currently protected, but exhibit conditions that have the potential for weakness. The borrower may be affected by unfavorable economic, market or other external conditions that may affect their ability to repay the debt. These may also include credits where there is deterioration of the collateral or have deficiencies which may affect our ability to collect on the collateral. This rating is consistent with the "Other Assets Especially Mentioned" category used by the FDIC.

Loans rated 5: Loans in this category are considered "substandard." Generally, a loan is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligors and/or the collateral pledged. There is a distinct possibility that the Bank will sustain some loss if the weakness is not corrected.

Loans rated 6: Loans in this category are considered "doubtful." Loans classified as doubtful have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, highly questionable and improbable.

Loans rated 7: Loans in this category are considered uncollectible ("loss") and of such little value that their continuance as loans is not warranted.

Commercial loans are assigned an initial grade at the origination of the loan. After origination, the Bank has a quality control program performed by an independent third party. On a rolling quarterly basis, all commercial, construction and residential loan relationships with individual loans of $500,000 or more are assigned a risk rating. An in-depth review is performed on all commercial real estate relationships with exposure in excess of $850,000, new credits in excess of $500,000 and all the loans on the Bank's Watch List. Watch List loans are those loans that are more than two payments past due at the end of the quarter, loans for which the borrowing entity or sponsor has filed bankruptcy, loans rated four or higher in a previous review, impaired loans, troubled debt restructurings and loans past contractual maturity. Results of the independent loan review are reported to the Bank's Audit Committee on a quarterly basis and become the mechanism for monitoring the overall credit quality of the portfolio.

The following table presents the Bank's loans by risk rating as of December 31, 2018 and March 31, 2019:

Rating	Residential Real Estate	Commercial Real Estate	Construction	Commercial
	(In Thousands)			
December 31, 2018				
1- 3B	$ 708,421	$ 1,148,094	$ 127,274	$ 128
4	1,199	2,110	—	—
5	362	331	—	—
	$ 709,982	$ 1,150,535	$ 127,274	$ 128
March 31, 2019				
1- 3B	**$ 712,122**	**$ 1,203,909**	**$ 151,905**	**$ 194**
4	**869**	**2,100**	—	—
5	**361**	—	—	—
	$ 713,352	**$ 1,206,009**	**$ 151,905**	**$ 194**

For home equity and consumer loans, management uses delinquency reports as the key credit quality indicator.

NOTE 7: RECENT ACCOUNTING PRONOUNCEMENTS

Accounting Standards Issued But Yet Not Adopted

The following identifies ASUs applicable to the Bank that have been issued but are not yet effective:

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*. This Update requires entities to measure expected credit losses based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. Credit losses on available for sale debt securities should be measured in a manner similar to current GAAP. However, the amendments in this Update require that credit losses be presented as an allowance rather than as a write down. The Update will be effective for fiscal years beginning after December 15, 2019, including interim periods. The Bank has completed the model selection, defined the data framework and is currently evaluating the model’s results and qualitative adjustment factors. Management will continue to monitor developments and additional guidance to determine the potential impact on the Bank's consolidated financial statements.

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

Cautionary Note Regarding Forward-Looking Statements

The following discussion of the financial condition and results of operations of the Bank should be read in conjunction with the Consolidated Financial Statements and Notes thereto included elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2018. Matters discussed in this Quarterly Report on Form 10-Q and in our public disclosures, whether written or oral, relating to future events or our future performance, including any discussion, expressed or implied, of our anticipated growth, operating results, future earnings per share, plans and objectives, contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements are often identified by the words "believe," "plan," "estimate," "project," "target," "continue," "intend," "expect," "future," "anticipate," and similar expressions that are not statements of historical fact. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict, including changes in political and economic climate, interest rate fluctuations and competitive product and pricing pressures within the Bank's market, bond market fluctuations, personal and corporate customers' bankruptcies and inflation. Our actual results and timing of certain events could differ materially from those anticipated in these forward-looking statements as a result of certain factors including, but not limited to, those set forth under "Risk Factors" and elsewhere in this Quarterly Report on Form 10-Q and in our other public filings with the FDIC. It is routine for internal projections and expectations to change as the year or each quarter in the year progresses and, therefore, it should be clearly understood that all forward-looking statements and the internal projections and beliefs upon which we base our expectations included in this Quarterly Report on Form 10-Q are made only as of the date of this Quarterly Report on Form 10-Q and may change. While we may elect to update forward-looking statements at some point in the future, we do not undertake any obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.

Note on Core Return on Average Equity and Core Return on Average Assets

Effective January 1, 2018, the Bank adopted FASB ASU 2016-01, *Financial Instruments – Overall, (Subtopic 825-10)*. Consequently, beginning January 1, 2018, equity securities (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) are measured at fair value with changes in fair value recognized in the Consolidated Statements of Net Income, regardless of whether such gains and losses are realized, and included in the other income category. This change affects the Bank's portfolio of marketable equity securities, which includes common equity securities and a mutual fund which invests in securities which qualify for Community Reinvestment Act securities test. This portfolio primarily includes common equity investments, which the Bank views as long-term partnership interests in operating companies. Consequently the Bank does not view the quarterly fluctuation in market value as indicative of the change in the intrinsic value of these portfolio holdings. The performance of these holdings should be evaluated on the basis of their contribution to growth in book value per share over time, not via quarterly adjustments to net income. Consistent with this view, beginning the first quarter of 2018, "Management's Discussion and Analysis of Financial Condition and Results of Operations" incorporates core net income, core return on average equity and core return on average assets, which are non-GAAP measurements that exclude the after-tax effect of gain on equity securities, both realized and unrealized.

INTRODUCTION

Net income for the quarter ended March 31, 2019 was $9,824,000 or $4.61 per share basic and $4.50 per share diluted, as compared to $8,912,000 or $4.18 per share basic and $4.08 per share diluted in earnings for the first quarter of 2018. The Bank's annualized return on average equity for the first quarter of 2019 was 17.98%, and the annualized return on average assets was 1.64%, compared to 18.56% and 1.56% for the same period in 2018. Excluding the after-tax gains on equity securities, both realized and unrealized, core net income for the first quarter of 2019 was $7,587,000 or $3.56 per share basic and $3.48 per share diluted, representing an annualized core return on average equity of 13.89% and an annualized core return on average assets of 1.26%. This compares to core net income of $8,159,000 or $3.83 per share basic and $3.73 per share diluted, representing an annualized core return on average equity of 16.99% and an annualized core return on average assets of 1.43% for the same period in 2018.

Balance sheet growth was mixed in the first quarter of 2019, with a decline in total deposits combined with strong loan growth. Total deposits decreased by $17.8 million from December 31, 2018, representing a 5% annualized decline year-to-date, but increased by $23.5 million from March 31, 2018, representing 2% growth. Net loans increased by $83.0 million from December 31, 2018 and $220.2 million from March 31, 2018, representing 17% annualized growth year-to-date and 12% growth from March 31, 2018. Total assets increased by $88.8 million from December 31, 2018 and $257.3 million from March 31, 2018, representing a 15% annualized growth year-to-date and 11% growth from March 31, 2018. Stockholders' equity increased to $221.7 million as of March 31, 2019, representing 17% annualized growth year-to-date and a 14% increase from March 31, 2018. Book value per share increased to $103.89 per share at March 31, 2019, from $99.67 per share at December 31, 2018 and $91.14 per share at March 31, 2018.

Since March 31, 2018, the Bank declared dividends of $1.96 per share, which included a $0.50 special dividend declared in the fourth quarter of 2018.

Key credit and operational metrics remained strong in the first quarter of 2019. At March 31, 2019, non-performing assets totaled 0.02% of total assets, compared with 0.02% at December 31, 2018 and 0.08% at March 31, 2018. Non-performing loans as a percentage of the total loan portfolio totaled 0.03% at March 31, 2019, as compared to 0.02% at December 31, 2018 and 0.10% at March 31, 2018. The efficiency ratio increased to 31.86% for the first quarter of 2019, as compared to 30.41% in the same period last year. Operating expenses (annualized) as a percentage of average assets fell to 0.86% for the first quarter of 2019, as compared to 0.89% for the same period last year. These figures reflect the Bank's continued focus on credit quality and disciplined expense control.

The Bank continues to exceed all of the minimum regulatory capital requirements.

RESULTS OF OPERATIONS
COMPARISON OF THE THREE MONTHS ENDED MARCH 31, 2019 AND 2018

General

The Bank reported net income of $9.8 million for the quarter ended March 31, 2019 as compared to $8.9 million for the quarter ended March 31, 2018. Net income was $4.61 per share basic and $4.50 per share diluted for the quarter ended March 31, 2019 as compared to $4.18 per share basic and $4.08 per share diluted for the same period in 2018. Earnings for the quarter ended March 31, 2019 were positively impacted by an increase of $1.9 million in other income, partially offset by a decrease of $621,000 in net interest income, a $140,000 increase in the provision for loan losses, an increase of $166,000 in the income tax provision and a $39,000 increase in operating expenses. The Bank's annualized return on average equity for the quarter ended March 31, 2019 was 17.98%, and the annualized return on average assets was 1.64%, compared to 18.56% and 1.56%, respectively, for the same period in 2018.

Excluding the after-tax gains on equity securities, both realized and unrealized, core net income for the first quarter of 2019 was $7.6 million or $3.56 per share basic and $3.48 per share diluted, representing an annualized core return on average equity of 13.89% and an annualized core return on average assets of 1.26%. This compares to core net income of $8.2 million or $3.83 per share basic and $3.73 per share diluted, representing an annualized core return on average equity of 16.99% and an annualized core return on average assets of 1.43% for the same period in 2018.

Net Interest Income

Net interest income was $15.8 million for the first quarter of 2019 and $16.5 million for the first quarter of 2018. The $621,000 decrease was due to a 39 basis point decline in the weighted average spread, partially offset by a $117.4 million, or 5%, increase in average interest-earning assets in the three months ended March 31, 2019, as compared to the same period in 2018. For the quarter ended March 31, 2019, the weighted average rate spread and net interest margin were 2.36% and 2.68%, respectively, compared to 2.75% and 2.93%, respectively, for the quarter ended March 31, 2018. Average interest-bearing liabilities increased by $54.6 million, or 3%, and the rate paid on interest-bearing liabilities increased by 70 basis points during the same period.

In recent years long-term rates have increased slightly from recent historic lows; while, starting in December 2015, the Federal Reserve began gradually increasing the overnight rate, impacting many short-term rates. In this environment, the Bank's cost of funds has increased in tandem with short-term rates over the last two years, while the yield on earning assets has increased at a slower pace, as the Federal Reserve has increased interest on excess reserves and the Bank has been gradually increasing the interest rate on certain loan products, particularly in 2018. To mitigate the negative effect of these market conditions on its net interest margin, the Bank began using brokered time deposits in 2017 as an alternative to other wholesale funding sources, such as FHLB borrowings or Internet listing services certificates of deposit. In 2018, the Bank shifted a portion of its wholesale funding mix from FHLB advances to brokered deposits, to take advantage of their lower cost and/or longer duration. At the same time, the Bank reduced the balance of excess reserves held at the Federal Reserve Bank, in order to minimize the carrying cost of its on-balance sheet liquidity. In the first quarter of 2019, the Bank continued to use these strategies opportunistically.

Interest and dividend income increased by $3.0 million to $25.1 million for the first quarter of 2019, as compared to $22.1 million for the first quarter of 2018. The yield on total interest-earning assets was 4.25% for the quarter ended March 31, 2019, as compared to 3.94% for the quarter ended March 31, 2018.

Interest income on loans increased by $2.7 million when comparing the two periods, primarily resulting from a 10% increase in average loan balances combined with a 13 basis point increase in yield.

Securities and short-term investments accounted for 13% of the total average interest-earning assets for the quarter ended March 31, 2019, as compared to 17% for the same period in 2018. This includes the Bank's cash holdings at the Federal Reserve. Income for these categories combined increased $329,000 when comparing the two periods, primarily due to a combined higher yield partially offset by a $64.8 million decline in average balances. During the last three quarters of 2018 and the first quarter of 2019, the Bank purchased additional marketable equity securities, some of which pay cash dividends. Additionally, the Federal Home Loan Bank ("FHLB") has continued to pay an elevated dividend on the Bank's stock investment. At the same time, the interest on excess reserves paid by the Federal Reserve has increased over this period.

The average rate on interest-bearing liabilities increased to 1.89% for the first quarter of 2019 from 1.19% for the comparable quarter of 2018. Total interest expense increased by $3.6 million when comparing the quarters ended March 31, 2019 and 2018 due to increases in the combined average balances and higher interest rates on deposits and borrowings.

Interest expense on deposits increased by $2.6 million due to an increase of $123.0 million in average interest-bearing deposits combined with a 60 basis point increase in the weighted average rate. Beginning in 2015, the Bank has seen increasing market pressure to raise rates on term deposits and some core deposits, driven largely by strong loan demand in the Bank's market area, changes in the economic environment and increasing short-term rates. The Bank has increased certain core product rates and continued to use wholesale time deposits to provide an efficient means for balanced growth. Given the current economic environment, management believes it is likely that deposit market rates may continue to increase in 2019. This approach has allowed the Bank to maintain deposit balances to fund lending activity and operate with an elevated level of liquidity.

Interest expense on borrowed funds for the first quarter of 2019 increased $1.0 million, as compared to the same quarter in 2018, primarily due to a 109 basis point increase in the weighted average rate, partially offset by a $68.4 million decrease in average outstanding balances. The increase in FHLB borrowings rate was primarily driven by the higher short-term market rates. Also, in the first quarter of 2018, the FHLB called a $20 million option advance taken during the first quarter of 2017, which had favorable interest rate and was replaced by shorter term advances at higher rates.

The following tables detail components of net interest income and yields/rates on average earning assets/liabilities.

	Three Months Ended March 31,					
	2018			2019		
	AVERAGE BALANCE	INTEREST	YIELD/ RATE (8)	AVERAGE BALANCE	INTEREST	YIELD/ RATE (8)
	(In Thousands)					
Loans (1) (2)	$ 1,866,138	$ 20,417	4.38 %	**$ 2,048,387**	**$ 23,080**	**4.51** %
Securities (3) (4)	53,517	479	3.58	**54,873**	**489**	**3.56**
Federal Reserve and other short-term investments	326,375	1,241	1.52	**260,176**	**1,560**	**2.40**
Total interest-earning assets	2,246,030	22,137	3.94	**2,363,436**	**25,129**	**4.25**
Other assets	38,003			**39,122**		
Total assets	$ 2,284,033			**$ 2,402,558**		
Interest-bearing deposits (5)	$ 1,362,569	3,567	1.05	**$ 1,485,540**	**6,146**	**1.65**
Borrowed funds	543,607	2,105	1.55	**475,213**	**3,139**	**2.64**
Total interest-bearing liabilities	1,906,176	5,672	1.19	**1,960,753**	**9,285**	**1.89**
Demand deposits	180,375			**215,115**		
Other liabilities	5,381			**8,128**		
Total liabilities	2,091,932			**2,183,996**		
Stockholders' equity	192,101			**218,562**		
Total liabilities and stockholders' equity	$ 2,284,033			**$ 2,402,558**		
Net interest income		$ 16,465			**$ 15,844**	
Weighted average spread			2.75 %			**2.36** %
Net interest margin (6)			2.93 %			**2.68** %
Average interest-earning assets to average interest-bearing liabilities (7)	117.83 %			**120.54 %**		

(1) Before allowance for loan losses.
(2) Includes non-accrual loans.
(3) Excludes the impact of the average net unrealized gain or loss on securities.
(4) Includes Federal Home Loan Bank stock.
(5) Includes mortgagors' escrow accounts.
(6) Net interest income divided by average total interest-earning assets.
(7) Total interest-earning assets divided by total interest-bearing liabilities.
(8) Annualized.

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

	Three Months Ended March 31, 2019 Compared to the Three Months Ended March 31, 2018 Increase (Decrease)		
	Due to		
	Volume	Rate	Total
	(In Thousands)		
Interest and dividend income:			
Loans	$ 2,040	$ 623	$ 2,663
Securities and FHLB stock	12	(2)	10
Federal Reserve and other short-term investments	(289)	608	319
Total interest and dividend income	1,763	1,229	2,992
Interest expense:			
Deposits	347	2,232	2,579
Borrowed funds	(293)	1,327	1,034
Total interest expense	54	3,559	3,613
Net interest income	$ 1,709	$ (2,330)	$ (621)

Provision for Loan Losses

At March 31, 2019, management's review of the allowance for loan losses concluded that a balance of $14.2 million was adequate to provide for losses based upon evaluation of risk in the loan portfolio. During the first quarter of 2019, management provided $425,000 to achieve such a loan loss allowance balance at March 31, 2019. Comparably, at March 31, 2018, management’s evaluation of the balance of the allowance for loan losses indicated the need for a quarterly provision of $285,000. The increase in provision is due to higher loan growth in the quarter ended March 31, 2019 compared to the quarter ended March 31, 2018. The Bank recorded net charge-offs of $1,000 during the first quarter of 2019 as compared to net recoveries of $1,000 during the first quarter of 2018.

See Notes 1 and 6 to the accompanying interim consolidated financial statements and “Loans and Foreclosed Real Estate” included in this Management’s Discussion and Analysis for additional information pertaining to the allowance for loan losses.

Other Income

Other income is comprised of gains on equity securities, net, customer service fees on deposits, increases in the cash surrender value of bank-owned life insurance policies and miscellaneous income. As previously discussed, beginning in 2018, unrealized gains or losses resulting from changes in fair value of the Bank’s equity securities are recognized in other income, included in gain on equity securities, net. Total other income was $3.2 million for the quarter ended March 31, 2019 compared to $1.3 million for the same period in 2018. In the first three months of 2019, the Bank recorded gains totaling $2.9 million on equity securities, including $2.9 million of unrealized gains on equity securities held at the end of the period and $1,000 of gains recognized on equity securities sold during the period. In the first three months of 2018, the Bank recorded gains totaling $966,000 on equity securities, including $953,000 of unrealized gains on equity securities held at the end of the period and $13,000 gains recognized on equity securities sold during the period.

Customer service fees on deposits decreased by $20,000 in the first quarter of 2019 compared to the same period in 2018. Over the last few years, there has been a slight decline in deposit account transaction fees as the Bank has eliminated many fees on deposit products to simplify offerings and enhance the value proposition of our consumer and business checking accounts to customers. There has been an offsetting trend in debit card interchange fees, as the size of the Bank’s checking account base has increased and the Bank has benefited from a secular trend towards increasing use of debit cards in payments. The Bank’s strategy does not rely on generating substantial non-interest fee-based revenue from our deposit accounts.

An increase in the cash surrender value of bank-owned life insurance also contributed to other income during the first quarter of 2019 and 2018. The Bank held $12.5 million in life insurance policies at March 31, 2019 as compared to $12.3 million at March 31, 2018. The policies accrete at a variable rate of interest with minimum stated guaranteed rates and income remained stable when comparing the two periods.

Operating Expenses

Operating expenses include salaries and employee benefits, data processing, occupancy and equipment, deposit insurance, foreclosure, marketing and other general and administrative expenses. Total operating expenses were $5.1 million for both quarters ended March 31, 2019 and 2018, or an annualized 0.86% and 0.89% of average total assets, respectively.

Salaries and employee benefits expenses decreased $65,000, or 2%, primarily due to a reduction in staffing levels, partially offset by annual merit-based salary increases.

Occupancy and equipment expenses decreased $12,000 to $454,000, primarily due to lower utility, maintenance and service equipment expenses, partially offset by higher depreciation expenses. This line also includes income collected from two rental properties held by the Bank. When the Bank developed its Nantucket location in 2013, it built a residential apartment unit on the 2nd floor for rental purposes. In 2016, the Bank completed a residential apartment unit on the 3rd floor of the building for rental purposes. The Bank continues to analyze how to maximize value in its real estate portfolio.

Data processing expenses for the first quarter of 2019 increased by $93,000, or 27%, when compared to the same period in 2018, driven primarily by a one-time conversion fee and secondarily by higher data processing charges associated with improvements made to the Bank's systems and volume increases. Expense for the first quarter of 2019 includes a $62,000 fee paid to Elan, related to the conversion of the Bank’s debit card platform from Elan to Fiserv. This fee, plus additional fees expected to be incurred in the second quarter of 2019, will be recovered through credits Fiserv will issue upon conversion. Technology spending at the Bank remains focused on three primary objectives: delivering new or improved customer experience, reducing costs through simplification and automation of internal processes, and securing customer and Bank confidential information.

Deposit insurance expense decreased by $30,000, or 11%, when compared to the same period in 2018. The decrease in expense is due to a lower assessed rate, partially offset by an increase in the size of the balance sheet, as this charge is calculated based on total assets. The assessment rate is determined based on several factors, including capitalization, asset growth, earnings, use of brokered deposits and level of non-performing assets, among others. The Bank carefully manages its balance sheet to control the insurance expense associated with excess liquidity.

Beginning in 2019, the Bank reclassified charitable contributions from other general and administrative expenses to marketing expense. Expenses for the prior year were also reclassified accordingly. Marketing expenses decreased by $35,000, or 21%, to $132,000 for the first quarter of 2019, as the Bank continues to carefully manage these expenses and focus marketing efforts on the Bank’s Commercial Real Estate and Specialized Deposit Groups.

Foreclosure related expenses increased by $18,000 when comparing the quarter ended March 31, 2019 to the same period in 2018. The increase is primarily due to an increase in costs associated with real estate taxes paid for a delinquent loan. At March 31, 2019, December 31, 2018 and March 31, 2018, the Bank had no properties in foreclosed assets. This category includes expenses associated with the foreclosure process, such as legal, appraisal, insurance and other related foreclosure expenses. These expenses may be recovered when the loan returns to performing status or when the Bank exercises its remedies, as they are generally secured by the Bank’s mortgages. Such recoveries, if any, are reflected in future periods as contra-expense. The Bank continues to manage credit quality energetically.

Other general and administrative expenses, which include director fees, supplies, deposit related losses and audit-related expenses, among others, increased $70,000, or 11%, when comparing the two periods, reflecting higher loan related expenses and an increase in miscellaneous expenses.

Income Taxes

The Bank recognizes income taxes under the asset and liability method in which deferred tax assets and liabilities are established for the temporary difference between the accounting basis and the tax basis of the Bank's assets and liabilities at enacted tax rates expected to be in effect when the amounts related to such temporary differences are realized or settled. The Bank's deferred tax asset is reviewed quarterly by management as to the realizability of such asset.

During the first quarter of 2019, the Bank recorded $3.6 million, or 26.9% of pre-tax income, in tax expense as compared to $3.4 million, or 27.9%, for the same quarter in 2018. The lower effective tax rate in the first quarter of 2019 was driven by higher unrealized gains on equity securities recognized during the first quarter of 2019 as compared to the same quarter in the prior year, as these securities are held at a tax-advantaged subsidiary. An excess tax benefit recognized on the exercise of stock options during the first quarter of 2019 also contributed to the lower effective tax rate.

BALANCE SHEET ANALYSIS
COMPARISON AT MARCH 31, 2019 TO DECEMBER 31, 2018

Assets totaled $2.497 billion at March 31, 2019, as compared to $2.409 billion at December 31, 2018, an increase of $88.8 million, or 15% annualized. Since early 2018, the Bank been carefully managing the balance of excess reserves held at the Federal Reserve Bank, in order to minimize the carrying cost of its on-balance sheet liquidity.

Securities, Short-term Investments and FHLB Stock

Securities were $42.7 million at March 31, 2019, an increase of $4.2 million when compared to $38.5 million at December 31, 2018, reflecting equity security purchases completed during the last three quarters of 2018 and the first quarter of 2019, partially offset by sales. There were no sales, maturities or calls of debt securities and principal paydowns were immaterial.

Beginning January 1, 2018, equity securities (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) are measured at fair value with changes in fair value recognized in net income. On January 1, 2018, $6.7 million of unrealized gains on equity securities available for sale held at December 31, 2017 were reclassified from accumulated other comprehensive income ("AOCI") to undivided profits as a cumulative-effect adjustment. At December 31, 2018 and March 31, 2019, there were no unrealized gains or losses on debt securities available for sale reported in AOCI. The fair value of securities fluctuates with the movement of interest rates and equity markets. The primary driver in net unrealized gain on the securities portfolio is the fair value of the Bank's equity holdings.

At March 31, 2019, less than 1% of the securities were debt securities issued or guaranteed by government-sponsored enterprises. For the most part, these securities are offered at a fixed rate and term and at spreads above comparable U.S. Treasury issues.

At March 31, 2019, equity securities accounted for approximately 100% of the investment portfolio. At March 31, 2019, the Bank held a $7.8 million investment in the Community Reinvestment Act ("CRA") Fund, a mutual fund which invests in securities which qualify under the CRA securities test. Additionally, the portfolio included $34.9 million in common equity securities. The Bank's common equity securities are not viewed as a source of liquidity and are managed to produce superior returns on capital over a longer time horizon. The Bank's process is focused on identifying businesses with strong returns on capital, owner-oriented management teams, good reinvestment opportunities or capital discipline, and reasonable valuations. The portfolio is concentrated in a relatively small number of investees in the financial services and technology areas, including other banks, diversified and specialized insurance companies, credit rating agencies, payment networks, technology companies and one industrial company. The Bank receives two sources of advantageous tax treatment through these investments. First, dividend distributions from these companies to the Bank are partially excluded from the Bank's taxable income due to the Dividends Received Deduction ("DRD"). Second, to the extent that these companies are capable of internal reinvestment at high rates of return or deploy capital via tax-advantaged repurchases, the deferred tax liability associated with any long-term unrealized gains on our investments constitutes an interest-free source of financing.

As a member of the Federal Home Loan Bank of Boston ("FHLB"), the Bank is required to hold a Membership Stock Investment plus an Activity-based Stock Investment in the FHLB, which is based primarily on the amount of FHLB borrowings. The Bank recorded dividends totaling $354,000 for the three months ended March 31, 2019, as compared to $338,000 for the same period in 2018. At March 31, 2019, the Bank held $30.6 million in FHLB stock compared to $28.7 million at December 31, 2018. The increase was driven by the growth in FHLB borrowings during the first quarter of 2019, as the Bank allowed Internet listing services time deposits to run off the balance sheet replacing them with more attractively priced FHLB advances.

Loans and Foreclosed Real Estate

During the first three months of 2019, net loans outstanding increased by $83.0 million to $2.092 billion, from $2.009 billion at December 31, 2018, attributable primarily to originated loans of $126.7 million offset by payoffs and amortization. This includes $9.5 million of commercial real estate loans originated in the Washington D.C. metropolitan area ("WMA"). Comparably, loan originations for the same period in 2018 were $121.1 million, including $10.5 million of commercial real estate loans originated in the WMA. Loans outstanding in the WMA at March 31, 2019 and December 31, 2018 were $118.8 million and $112.3 million, respectively. At March 31, 2019 and December 31, 2018, net loans outstanding represented 84% and 83% of assets, respectively. Mortgage loans continue to account for more than 99% of the loan portfolio.

WMA: In 2017, the Bank began lending to commercial real estate borrowers in the Washington, D.C. metropolitan area, after two years of research and preparation. The Bank identified the WMA as an attractive opportunity for three reasons. First, the region has favorable economic characteristics that will support long-term investments in commercial real estate. It is the capital of the world's largest economy, it is an international economic gateway, it has the highest household median income of any of the nation's major metropolitan areas, and it has a relatively high concentration of young people. Second, the commercial real estate product in the market bears significant similarity to Boston, characterized by high density, urban infill development, transit-oriented multifamily, and scarcity imposed by land supply and restrictions on vertical development. Third, we believe that the banking market in Washington, D.C. has experienced a level of consolidation and disruption that has left smaller and mid-sized real estate investors underserved as compared to the Boston market. Although we are relatively new to this marketplace, we believe that our history as one of America's oldest banks and our family management team provide stability and surety of execution that is valued by our customers. We view this as an attractive opportunity for internal capital allocation and superior to geographically proximate, product-adjacent businesses like wealth management, insurance, or commercial-industrial lending in our home marketplace. The Bank is not making any residential owner-occupied or commercial construction loans in the WMA at this time.

The Bank approaches prospective borrowers directly via advertising programs, and indirectly via intermediaries such as attorneys, accountants and mortgage brokers. The Bank also has existing Boston-based customers with real estate investment holdings in both the Massachusetts and WMA markets. The Bank currently utilizes existing staff in the Commercial Real Estate Group with experience in the WMA, on a fly-away basis from our Main Office.

All underwriting and approval processes are identical to those utilized in the Boston marketplace and all loans are reviewed and approved by the Bank's Executive Committee and when larger than $1.5 million, by the Bank's full Board of Directors. A member of the Executive Committee performs a site visit for every collateral property and the full Executive Committee performs collateral site visits at least twice annually. The Bank uses one Arlington, VA-based law firm to advise on all of its transactional needs, with oversight on each individual transaction by the Bank's primary real estate counsel in Boston. The Bank uses the same environmental assessment firm in Boston and Washington, D.C. to ensure quality of execution and manage risk. Once closed, these loans are subject to all of the Bank's regular quality control and portfolio management processes.

The Bank has made inroads into developing deposit relationships with WMA borrowers and services these customers remotely through the Bank's Specialized Deposit Group in Hingham. The Bank's Specialized Deposit Group is now servicing multiple WMA deposit customers that do not have a lending relationship with the Bank. The Bank is actively planning for a physical presence in the WMA, likely in the District of Columbia.

Loans are carried net of the allowance for loan losses. The allowance is maintained at a level to absorb losses within the loan portfolio. At March 31, 2019, the allowance had a balance of $14.2 million, as compared to $13.8 million at December 31, 2018. The allowance for loan losses represented 0.68% of gross loans as of both March 31, 2019 and December 31, 2018.

At March 31, 2019, the Bank allocated $115,000 to loans classified as impaired. At December 31, 2018, $118,000 was allocated to impaired loans. The Bank works closely with delinquent mortgagors to bring their loans current and commences foreclosure proceedings if the mortgagor is unable to satisfy their outstanding obligation. Although regulatory changes have slowed the foreclosure process in recent years, the Bank continues to pursue delinquencies vigorously.

At March 31, 2019, there were two loans classified as non-accrual totaling $624,000, as compared to two non-accrual loans totaling $484,000 at December 31, 2018. At March 31, 2019 and December 31, 2018, there were no foreclosed properties. At both March 31, 2019 and December 31, 2018, non-performing assets were 0.02% of total assets. Management believes that its loans classified as non-accrual are significantly collateralized, pose minimal risk of loss to the Bank, and the allowance for loan loss reserves allocated to these loans is sufficient to absorb such losses, if any. However, management continues to monitor the loan portfolio and additional reserves will be recorded if necessary.

Below is a summary of non-accrual loans and foreclosed real estate:

	December 31, 2018	March 31, 2019
	(Dollars in Thousands)	
Non-accrual loans:		
Residential mortgages	$ —	**$ 472**
Commercial mortgages	484	**152**
Total non-accrual loans	484	**624**
Foreclosed real estate	—	**—**
Total non-performing assets	$ 484	**$ 624**
Percent of non-accrual loans to:		
Total loans	0.02 %	**0.03 %**
Total assets	0.02 %	**0.02 %**
Percent of non-performing assets to:		
Total loans and foreclosed real estate	0.02 %	**0.03 %**
Total assets	0.02 %	**0.02 %**
Allowance for loan losses to total loans	0.68 %	**0.68 %**

Other Assets

The Bank held $12.5 million in bank-owned life insurance at both March 31, 2019 and December 31, 2018. The $66,000 increase during the first three months of 2019 is due to increases in the cash surrender value of policies insuring the life of a current Bank executive. The policies accrete at a variable rate of interest with minimum stated guaranteed rates. The Bank monitors the financial strength and counterparty credit ratings of the policy issuers and has determined that at March 31, 2019, two of three issuers were rated at or above Bank guidelines. The third issuer retained a rating from A.M. Best at or above Bank guidelines, while the issuer's

Standard and Poor ("S&P") rating was below Bank guidelines at BBB (Good) with a stable outlook.

On January 1, 2019, the Bank adopted FASB ASU 2016-02, *Leases (Topic 842)*. As a result of the adoption of ASU 2016-02, the Bank recorded a right-of-use asset and corresponding lease liability of $1.7 million, effective January 1, 2019. As of March 31, 2019, the right-of-use asset and corresponding lease liability was $1.6 million. The right-of-use asset is included in other assets and the lease liability is included in other liabilities in the Consolidated Balance Sheets.

Deposits

Deposits decreased by $17.8 million to $1.555 billion at March 31, 2019, from $1.573 billion at December 31, 2018. Certificate balances decreased by $20.0 million from December 31, 2018 to March 31, 2019 and non-certificate accounts, which include regular, money market, NOW and demand deposits, increased by $2.2 million during the same period. Non-certificate accounts represent 53.0% of total deposits at March 31, 2019, as compared to 52.2% at December 31, 2018.

Other banks and credit unions in the Bank's market areas, banking services through the Internet, and mutual funds make up the Bank's primary competition for deposits. The Bank's ability to attract and retain deposits depends upon satisfaction of depositors' requirements with respect to insurance, product, rate and service. The Bank offers traditional deposit products, competitive rates, convenient branch locations, ATMs, debit cards and Internet-based banking for consumers and commercial account holders. The Bank offers limited certificate of deposit products using national Internet listing services and brokered deposits. These alternatives provide the Bank with a source of funding across different maturities at lower cost and/or longer duration than may be available via retail or other wholesale channels. At March 31, 2019, the Bank had $292.6 million in deposits from these sources, as compared to $321.1 million at December 31, 2018. During 2018, the Bank shifted a portion of its wholesale funding mix from FHLB advances and Internet listing services deposits to brokered deposits to mitigate the negative effect of increasing short-term market rates on the Bank's cost on interest-bearing liabilities and net interest margin. In the first quarter of 2019, the Bank continued to carefully manage its wholesale funding mix allocation based on market conditions. This resulted in declining wholesale time deposits, as maturing Internet listing services time deposits were partially replaced by brokered time deposits.

Deposits are insured in full through the combination of the Federal Deposit Insurance Corporation and the Deposit Insurance Fund of Massachusetts ("DIF"). Generally, separately insured deposit accounts are insured up to $250,000 by the FDIC and deposit balances in excess of this amount are insured by the DIF. DIF insurance provides an advantage for the Bank as some competitors cannot offer this coverage.

Below is a summary of deposits:

	Deposit Balances by Type			
	December 31, 2018	**% of Total**	**March 31, 2019**	**% of Total**
	(Dollars in Thousands)			
Non-certificate accounts				
Regular	$ 87,173	5.5 %	**$ 87,990**	**5.7 %**
Money market deposits	516,107	32.8	**503,031**	**32.3**
NOW	5,064	0.3	**5,242**	**0.3**
Demand	213,573	13.6	**227,872**	**14.7**
Total non-certificate accounts	821,917	52.2	**824,135**	**53.0**
Term certificates of less than $250,000	555,266	35.3	**537,835**	**34.6**
Term certificates of $250,000 or more	195,971	12.5	**193,353**	**12.4**
Total certificate accounts	751,237	47.8	**731,188**	**47.0**
Total deposits	$ 1,573,154	100.0 %	**$ 1,555,323**	**100.0 %**

Borrowings

FHLB advances were $702.1 million, or 28% of total assets, at March 31, 2019, as compared to $606.6 million, or 25% of total assets, at December 31, 2018. The Bank continued to manage its wholesale funding mix opportunistically during the first three months of 2019. During this period, borrowings increased by $95.5 million, as the Bank used FHLB advances to fund strong balance sheet growth and to replace maturing Internet listing services time deposits. These advances are fixed rate in nature with 95% scheduled to mature in the next twelve months.

Liquidity and Capital Resources

The Bank regularly assesses its liquidity position by forecasting incoming and outgoing cash flows. In some cases, contractual maturity dates are used to anticipate cash flows. However, when an asset or liability is subject to early repayment or redemption at the discretion of the issuer or customer, cash flows can be difficult to predict. Generally, these prepayment rights are exercised when it is most financially favorable to the issuer or customer.

The Bank's initial source of liquidity is cash and cash equivalents which comprised 12% of total assets at March 31, 2019. A significant portion of this consists of overnight cash balances at the Federal Reserve Bank of Boston, which are immediately accessible for liquidity. The Bank reduced these overnight cash balances during 2018 to minimize the carrying cost of on-balance sheet liquidity and continued to manage these balances carefully in the first quarter of 2019.

Mortgage-backed securities, which comprise less than 1% of the portfolio, are subject to repayment at the discretion of the underlying borrower and are not considered material to the overall balance sheet or liquidity targets.

Marketable common equity holdings, although liquid, are not viewed as a source of liquidity and are managed to produce superior returns on capital over a longer time horizon.

Investment in FHLB stock is illiquid.

Residential loans are susceptible to principal repayment at the discretion of the borrower. Commercial mortgage loans, while subject to significant penalties for early repayment in most cases, can also prepay at the borrower's discretion. In the first quarter of 2019, prepayment rates were lower when compared to the previous year.

The Bank invests in key executive life insurance policies that are illiquid during the life of the executive. Such policies total $12.5 million, or less than 1% of total assets, at March 31, 2019.

Non-certificate deposit balances can generally be withdrawn from the Bank at any time. Retail certificates of deposit, with predefined maturity dates and subject to early redemption penalties, can also be withdrawn subject to the discretion of the Bank. Internet listing service certificates are offered on the same terms as retail certificates, although the Bank generally does not permit early withdrawal. Brokered certificates generally may not be withdrawn before the stated maturity. The Bank estimates the volatility of its deposits in light of the general economic climate and recent actual experience. Over the past 10 years, deposits have exceeded withdrawals resulting in net cash inflows from depositors.

All of the Bank's borrowings were fixed in terms of rate and maturity at March 31, 2019. None of the advances can be called for earlier repayment at the discretion of the issuer.

The Bank also monitors its off-balance sheet items. See "Commitments" appearing in Note 2 within the "Notes to Unaudited Consolidated Financial Statements" section of this document. At March 31, 2019, the Bank had $316.2 million in commitments to extend credit, as compared to $258.9 million at December 31, 2018.

The Bank takes each of these preceding issues into consideration when measuring its liquidity position. Specific measurements include the Bank's cash flow position from the 30-day to 90-day horizon, the level of volatile liabilities to earning assets and loan to deposit ratios. Additionally, the Bank "shocks" its cash flows by assuming significant cash outflows in both non-certificate and certificate deposit balances. At March 31, 2019, each measurement was within predefined Bank guidelines, with the exception of the net loans to deposits ratio, which was 135%.

To supplement its liquidity position, should the need arise, the Bank maintains its membership in the FHLB where it is eligible to obtain both short and long-term credit advances. As of March 31, 2019, the Bank can borrow up to approximately $1.183 billion to meet its borrowing needs, based on the Bank's available qualified collateral which consists primarily of one-to-four family residential mortgage loans, certain multifamily residential property and commercial mortgage loans. The Bank can pledge other mortgage loans and assets as collateral to secure additional borrowings. Additionally, through the Federal Reserve Bank of Boston ("FRBB"), the Bank can borrow up to $20.4 million through the discount window based on the Bank pledging its home equity loan portfolio. The Bank can pledge other mortgage loans and assets as collateral to secure additional borrowings with the FRBB. At March 31, 2019, the Bank had $702.1 million in advances outstanding from the FHLB and had $480.4 million in available unused capacity (net of accrued interest on outstanding advances). This compares to an unused capacity of $538.7 million at December 31, 2018. The FHLB unused capacity decreased in the first quarter of 2019 as a result of the increase in borrowings. However, total FHLB capacity increased by $37.4 million from December 31, 2018 as the Bank continued to pledge collateral. At March 31, 2019, the Bank did not have any advances outstanding at the FRBB.

At March 31, 2019, the Bank had capital of $221.7 million, or 8.9% of total assets, as compared to $212.6 million, or 8.8% of total assets, at December 31, 2018. During the three months ended March 31, 2019, stockholders' equity increased by $9.1 million due primarily to net income for the period of $9.8 million, partially offset by the declaration of dividends of $0.38 per share, which reduced capital by $811,000.

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 and average total assets. The Bank's ratios exceeded these regulatory capital requirements at March 31, 2019 and December 31, 2018.

The following table details the Bank's actual capital ratios and minimum regulatory ratios as of December 31, 2018 and March 31, 2019.

	Actual		Minimum Capital Requirement*		Minimum To Be Well Capitalized Under Prompt Corrective Actions Provisions	
	Amounts	Ratio	Amounts	Ratio	Amounts	Ratio
			(Dollars in Thousands)			
December 31, 2018						
Total Capital to Risk-Weighted Assets	$ 226,384	13.27 %	$ 168,417	9.875 %	$ 170,548	10.00 %
Common Equity Tier 1 Capital to Risk-Weighted Assets	212,576	12.46	108,725	6.375	110,856	6.50
Tier 1 Capital to Risk-Weighted Assets	212,576	12.46	134,307	7.875	136,439	8.00
Tier 1 Capital to Average Assets	212,576	9.09	93,503	4.000	116,879	5.00
March 31, 2019						
Total Capital to Risk-Weighted Assets	**$ 235,913**	**13.10 %**	**$ 189,146**	**10.50 %**	**$ 180,139**	**10.00 %**
Common Equity Tier 1 Capital to Risk-Weighted Assets	**221,681**	**12.31**	**126,097**	**7.00**	**117,090**	**6.50**
Tier 1 Capital to Risk-Weighted Assets	**221,681**	**12.31**	**153,118**	**8.50**	**144,111**	**8.00**
Tier 1 Capital to Average Assets	**221,681**	**9.23**	**96,102**	**4.00**	**120,128**	**5.00**

* Minimum risk-based regulatory capital ratios and amounts at December 31, 2018 and March 31, 2019 include the applicable minimum risk-based capital ratios and capital conservation buffer of 1.875% and 2.5%, respectively.

Item 3 – Quantitative and Qualitative Disclosures About Market Risk

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 (the "ALCO") and Board of Directors of the Bank. The ALCO is comprised of members of Bank Management and the Executive Committee of the Board. The ALCO establishes and monitors the various components of the balance sheet including volume, maturities, pricing and mix of assets along with funding sources. The goal is to balance liquidity, interest rate risk and profitability. The primary tool used 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 asset prepayment speeds, balance sheet growth and non-maturity deposits elasticity. Management believes that there has been no material changes in the interest rate risk reported in the Bank's Annual Report on Form 10-K for the fiscal year ended December 31, 2018, filed with the Federal Deposit Insurance Corporation. The information is contained in the Form 10-K within the section "Quantitative and Qualitative Disclosures About Market Risk."

Item 4 – Controls and Procedures

(a) Disclosure Controls and Procedures

An evaluation was carried out under the supervision and with the participation of the Bank's management, including the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), of the effectiveness, as of March 31, 2019, of the Bank's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of the Bank's disclosure controls and procedures as of March 31, 2019, the CEO and CFO concluded that, as of such date, the Bank's disclosure controls and procedures were effective at the reasonable assurance level.

(b) Changes in Internal Control

There were no significant changes in the Bank's internal control over financial reporting, as defined in Rules 13a-15(e) and 15d-15(e), during the quarter ended March 31, 2019 that have materially affected, or are reasonably likely to materially affect, the Bank's internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1 – Legal Proceedings

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 statements.

Item 1A – Risk Factors

There have been no material changes to the risk factors previously disclosed in the Bank's most recently filed Form 10-K.

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

None.

Item 3 – Defaults Upon Senior Securities

None.

Item 4 – Mine Safety Disclosures

Not applicable.

Item 5 – Other Information

None.

Item 6 – Exhibits

Exhibit No.	
31.1	Certifications – Chief Executive Officer
31.2	Certifications – Chief Financial Officer
32.1	Certification Pursuant to 18 U.S.C. §1350 – Chief Executive Officer
32.2	Certification Pursuant to 18 U.S.C. §1350 – Chief Financial Officer

SIGNATURES

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

HINGHAM INSTITUTION FOR SAVINGS

Date: May 8, 2019

/s/
Robert H. Gaughen, Jr.
Chief Executive Officer
(Principal Executive Officer)

Date: May 8, 2019

/s/
Cristian A. Melej
Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

CERTIFICATIONS

EXHIBIT 31.1

I, Robert H. Gaughen, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of the Hingham Institution for Savings;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 8, 2019

/s/
Robert H. Gaughen, Jr.
Chief Executive Officer
(Principal Executive Officer)

CERTIFICATIONS

EXHIBIT 31.2

I, Cristian A. Melej, certify that:

1. I have reviewed this quarterly report on Form 10-Q of the Hingham Institution for Savings;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 8, 2019

/s/
Cristian A. Melej
Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

EXHIBIT 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. §1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Hingham Institution for Savings (the “Bank”) for the fiscal quarter ended March 31, 2019, as filed with the Federal Deposit Insurance Corporation on the date hereof (the “Report”), the undersigned Robert H. Gaughen, Jr., Chief Executive Officer of the Bank, hereby certifies pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

/s/
Robert H. Gaughen, Jr.
Chief Executive Officer
(Principal Executive Officer)

Date: May 8, 2019

EXHIBIT 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. §1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Hingham Institution for Savings (the "Bank") for the fiscal quarter ended March 31, 2019, as filed with the Federal Deposit Insurance Corporation on the date hereof (the "Report"), the undersigned Cristian A. Melej, Chief Financial Officer of the Bank, hereby certifies pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents in all material respects, the financial condition and results of operations of the Bank.

/s/
Cristian A. Melej
Chief Financial Officer
(Principal Financial Officer
and Principal Accounting Officer)

Date: May 8, 2019