STURGIS BANCORP INC
Form 10-Q
August 13, 2003

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SECURITIES AND EXCHANGE COMMISSION

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 June 30, 2003

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

For the transition period from _________ to _________

STURGIS BANCORP, INC.

(Exact name of registrant as specified in its charter)

MICHIGAN
(State of incorporation or organization)

0-49613	38-3609814
(Commission File No.)	(I.R.S. Employer Identification No.)

113-125 E. Chicago Road, Sturgis, Michigan 49091

(Address of principal executive offices)
(269) 651-9345

(Issuer s telephone number)

(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange of 1934 Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

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

Class	Outstanding at August 12, 2003
Common Stock, $1.00 par value	2,808,535

Transitional Small Business Disclosure Format (check one); Yes [ ] No [X]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule

12b-2 of the Exchange Act). Yes [ ] No [X]

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STURGIS BANCORP, INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Throughout this Form 10-Q, Sturgis Bancorp, Inc. will be referred to as Bancorp and Sturgis Bank and Trust Company and its subsidiaries will be referred to as the Bank. Bancorp is a financial holding company under the Bank Holding Company Act of 1956, as amended. The Bank is a wholly owned subsidiary of Bancorp.

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ITEM 1. FINANCIAL STATEMENTS

STURGIS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL CONDITION

	June 30 2003	December 31, 2002
ASSETS		
Cash and due from banks	$ 11,626,132	$ 13,064,101
Short-term interest-bearing deposits	298,970	7,183
Total cash and cash equivalents	11,925,102	13,071,284
Interest-bearing deposits in banks	18,726,557	23,018,375
Securities - Available-for-sale	9,083,004	
Securities - Held-to-maturity	11,610,076	12,590,709
Federal Home Loan Bank stock, at cost	4,169,900	4,115,400
Loans held for sale	8,981,083	7,437,506
Loans, net	204,013,697	212,043,350
Real estate owned	1,080,092	1,358,759
Bank owned life insurance	6,487,487	6,335,429
Accrued interest receivable	1,684,161	1,731,948
Investment in limited partnership	1,195,480	161,080
Premises and equipment, net	6,846,893	6,641,980
Intangible assets		
Goodwill, net of accumulated amortization	5,109,419	5,109,419
Originated mortgage servicing rights	1,770,242	1,501,922
Other intangible assets	103,609	105,601
Other assets	1,774,069	1,461,695
Total assets	$294,560,871	$296,684,457
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Deposit accounts:		
Noninterest-bearing	$ 17,660,829	$ 12,747,121
Interest-bearing	187,835,663	189,816,675
Borrowings from Federal Home Loan Bank	58,206,084	64,381,396
Accrued interest payable	683,189	935,954
Other liabilities	1,794,924	1,350,783
Total liabilities	266,180,689	269,231,929
Stockholders equity:		
Common stock	2,808,535	2,799,535
Additional paid-in capital	17,805,688	17,732,617
Retained earnings	7,765,960	6,920,376
Total stockholders equity	28,380,183	27,452,528
Total liabilities and stockholders equity	$294,560,871	$296,684,457

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STURGIS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF INCOME

	Three Months Ended June 30,	
	2003	**2002**
Interest income		
Loans	$3,496,154	$3,859,065
Mortgage-backed securities	67,754	50,564
Investments	190,659	139,457
Interest-bearing deposits	159,697	235,875
Overnight deposits at FHLB	8,239	8,461
Total interest income	3,922,503	4,293,422
Interest expense		
Deposits	1,087,956	1,222,707
FHLB advances	704,797	815,776
Total interest expense	1,792,753	2,038,573
Net interest income	2,129,750	2,254,849
Provision for loan losses	710,787	235,125
Net interest income after provision for loan losses	1,418,963	2,019,724
Noninterest income:		
Service charges and other fees	362,697	372,278
Commission income	303,179	282,656
Mortgage banking activities	989,221	274,659
Trust fee income	126,949	93,239
Increase in cash surrender value of life insurance	76,486	75,231
Other income	24,060	18,956
Total noninterest income	1,882,592	1,117,019
Noninterest expenses:		
Salaries and employee benefits	1,347,243	1,183,373
Office occupancy and equipment	342,780	313,828
Deposit account expenses	48,595	46,267
Service bureau expense	238,800	157,206
Professional fees and services	87,872	113,012
Other	460,812	477,386
Total noninterest expenses	2,526,102	2,291,072
Income before provision for federal income tax	775,453	845,671
Provision for federal income tax	217,394	239,385
Net income	$ 558,059	$ 606,286
Basic earnings per share	$ 0.20	$ 0.20
Diluted earnings per share	$ 0.20	$ 0.20
Dividends declared per share	$ 0.09	$ 0.07

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STURGIS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF INCOME

	Six Months Ended June 30, 2003	Six Months Ended June 30, 2002
Interest income		
Loans	$7,174,172	$7,937,154
Mortgage-backed securities	139,865	64,510
Investments	341,103	256,118
Interest-bearing deposits	337,042	400,559
Overnight deposits at FHLB	21,028	41,130
Total interest income	8,013,210	8,699,471
Interest expense		
Deposits	2,244,890	2,455,535
FHLB advances	1,453,595	1,727,988
Total interest expense	3,698,485	4,173,523
Net interest income	4,314,725	4,525,948
Provision for loan losses	1,029,476	815,257
Net interest income after provision for loan losses	3,285,249	3,710,691
Noninterest income:		
Service charges and other fees	714,643	741,379
Commission income	542,142	492,653
Mortgage banking activities	1,723,700	859,302
Trust fee income	247,781	250,778
Increase in cash surrender value of life insurance	152,058	163,998
Other income	24,048	23,621
Total noninterest income	3,404,372	2,531,731
Noninterest expenses:		
Salaries and employee benefits	2,517,824	2,299,621
Office occupancy and equipment	675,888	627,278
Deposit account expenses	98,721	94,603
Service bureau expense	444,113	315,260
Professional fees and services	185,950	200,137
Other	893,883	908,970
Total noninterest expenses	4,816,378	4,445,869
Income before provision for federal income tax	1,873,243	1,796,553
Provision for federal income tax	550,209	518,269
Net income	$1,323,024	$1,278,284
Basic earnings per share	$ 0.47	$ 0.42
Diluted earnings per share	$ 0.47	$ 0.42
Dividends declared per share	$ 0.17	$ 0.14

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STURGIS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

	Six Months Ended June 30,	
	2003	2002
	(Unaudited)	(Unaudited)
Cash Flows from Operating Activities		
Net Income	$ 1,323,034	$ 1,278,284
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	318,672	294,484
Amortization of intangibles	572,431	252,322
Provision for loan losses	1,029,476	815,287
Premiums and discounts on investment securities	47,678	13,574
Gain on sale of loans	(1,043,880)	(429,214)
Gain on sale of real estate owned	(22,629)	(18,400)
Proceeds from the sale of loans held for sale	81,567,684	38,289,024
Loans originated for sale	(82,067,381)	(34,056,040)
Loss of equity in limited partnership	15,600	9,000
Increase in cash value of bank owned life insurance	(152,058)	(163,998)
Changes in assets and liabilities:		
Increase in accrued interest and other assets	(1,103,327)	(1,051,750)
Increase in accrued interest and other liabilities	192,447	2,509,104
Net cash provided by operating activities	677,728	7,741,677
Cash Flows from Investing Activities		
Net decrease (increase) in interest-bearing deposits in banks	4,291,818	(21,480,822)
Proceeds from maturities of securities held-to-maturity	932,955	1,242,719
Purchase of securities held-to-maturity		(10,213,698)
Proceeds (purchase) of other securities	(9,083,004)	(1,334,573)
Stock dividend on FHLB stock	(54,500)	
Purchase of investment in limited partnership	(1,050,000)	
Net decrease in loans	6,673,910	6,212,141
Proceeds from sale of real estate owned	627,564	125,511
Purchases of premises and equipment	(523,586)	(217,342)
Net cash provided by (used in) investing activities	1,815,157	(25,666,064)
Cash Flows from Financing Activities		
Net increase in demand and savings account deposits	10,500,059	4,613,937
Net increase (decrease) in certificates of deposits	(7,567,363)	18,896,712
Repayment of FHLB advances	(10,349,373)	(20,401,560)
Proceeds from FHLB advances	4,174,061	16,016,768
Dividends paid	(477,451)	(424,668)
Exercise of stock options	81,000	
Stock Redemption		(1,316,846)
Net cash (used in) provided by financing activities	(3,639,067)	17,384,343
Net (decrease) increase in Cash and Cash Equivalents	(1,146,182)	(540,044)
Cash and Cash Equivalents - Beginning of Period	13,071,284	10,629,027
Cash and Cash Equivalents - End of Period	$ 11,925,102	$ 10,088,983

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note A: FINANCIAL STATEMENTS.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of Management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month and six-month periods ended June 30, 2003 are not necessarily indicative of the results that may be expected for the year ended December 31, 2003. For further information, refer to the consolidated financial statements and footnotes thereto included in the Bancorp s Annual Report on Form 10-K for the year ended December 31, 2002.

Note B: ORGANIZATION AND ACCOUNTING POLICIES.

The following is a summary of the significant accounting policies followed in the preparation of the consolidated financial statements of Sturgis Bancorp and subsidiaries (individually and collectively referred to as Bancorp).

Organization

Bancorp is chartered as a financial holding company. Bancorp s primary asset is Sturgis Bank & Trust Company (Bank), a Michigan savings bank. The Bank, as a state-chartered stock savings bank and as a member of the Federal Home Loan Bank System (FHLB), is required to maintain an investment in the capital stock of the FHLB.

The Federal Deposit Insurance Corporation (FDIC) insures deposit accounts within certain limitations. A premium is required by the FDIC for the insurance of such accounts.

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note B: ORGANIZATION AND ACCOUNTING POLICIES, Continued.

Principles of Consolidation

The consolidated financial statements include the accounts of Bancorp, the Bank and all wholly-owned subsidiaries. All significant inter-company accounts and transactions are eliminated in consolidation.

Use of Estimates in the Preparation of Financial Statements

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

The allowance for loan losses is a material estimate that is particularly susceptible to change in the near term. While management uses available information to recognize losses on loans, future additions to the allowance or write-downs may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the allowance for loan losses. Such agencies could require Bancorp to recognize additions to the allowance or write-downs based on their judgment of information available to them at the time of their examination.

Securities

Debt securities that management has the positive intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost. Securities not classified as held to maturity or trading are classified as available for sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported as other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held to maturity and available for sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note B: ORGANIZATION AND ACCOUNTING POLICIES, Continued.

Loans

Substantially all of Bancorp s loan activity is with customers located in southwestern and south-central, lower Michigan with a major concentration in single-family residential lending.

Generally, loans are collateralized by real estate. Bancorp expects loans to be repaid from cash flow or proceeds from the sale of selected assets of the borrower. Bancorp s policy for requiring collateral is dependent upon management s credit evaluation of the borrower.

Interest on loans is accrued and credited to income based upon the principal amount outstanding. The accrual of interest income is generally discontinued when a loan becomes 90 days past due as to principal or interest or when, in the opinion of management, full collection of principal or interest is unlikely. When a loan is in non-accrual status, interest income is recognized only to the extent of cash received and when the full collection of principal is not in doubt. Management may elect to continue the accrual of interest when the estimated fair value of collateral is sufficient to cover the principal balance and accrued interest.

Loan origination fees and certain direct loan origination costs are deferred and the net amount amortized as an adjustment of the related loan yield over the contractual life of the loans.

Loans Held for Sale

The Bank sells a portion of its mortgage loan production into the secondary market. Loans held for sale are carried at the lower of cost or market until sold. Whenever loan costs exceed market value on a net aggregate basis, a valuation allowance is recorded.

Allowance For Loan Losses

The allowance for loan losses is maintained at a level considered by management to be adequate to absorb losses inherent in existing loans and commitments. The adequacy of the allowance is based on evaluations that take into consideration such factors as prior loss experience, changes in the nature and volume of the portfolio, overall portfolio quality, loan concentrations, specific impaired or problem loans and commitments, and current economic conditions that may affect the borrower s ability to pay.

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note B: ORGANIZATION AND ACCOUNTING POLICIES, Continued.

Office Properties and Equipment

Office properties and equipment are carried at cost, less accumulated depreciation. Depreciation is computed on the straight-line method based on the estimated useful lives of the related assets.

Real Estate Owned

Real estate owned includes properties acquired through foreclosure proceedings or by acceptance of a deed in lieu of foreclosure. Real estate owned is recorded at the lower of its cost or the estimated fair market value (as determined by recent appraisals) less estimated selling costs. Any write-down of the loan balance to estimated fair market value (less estimated selling costs) when the property is foreclosed is charged to the allowance for loan losses. Subsequent market write-downs, operating expenses and gains or losses on disposition of real estate owned are charged to current earnings.

Investment In Limited Partnership

The Bank has an investment in an Indiana limited partnership and First Michiana Development Corporation, a wholly-owned subsidiary of the Bank, has an investment in a Michigan limited partnership, which are structured to generate low-income housing tax credits. These investments are accounted for using the equity method, whereby Bancorp annually records its proportionate share of partnership losses as an adjustment to the carrying value of the investment.

Goodwill

Until adoption of FAS 142 in January of 2002, goodwill was amortized using accelerated methods over fifteen years. Beginning in January of 2002, the Bank no longer amortizes goodwill in accordance with FAS 142. On an ongoing basis, management assesses the recoverability of the goodwill. If an assessment of the goodwill indicates that its recoverability is impaired, a charge to expense is recorded for the amount of the impairment.

Servicing Rights

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Capitalized servicing rights are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost.

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note B: ORGANIZATION AND ACCOUNTING POLICIES, Continued.

Impairment is determined by stratifying rights by predominant characteristics, such as interest rates and terms. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance for an individual stratum, to the extent that fair value is less than the capitalized amount for the stratum. The Bank carried a valuation allowance associated with capitalized servicing rights of approximately $170,000 at June 30, 2003 and $275,000 at December 31, 2002.

Federal Income Taxes

Deferred tax assets and liabilities are recognized for temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized.

Statement of Cash Flows

For the purposes of the consolidated statements of cash flows, Bancorp considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

	Six Months Ended June 30,	
	2003	**2002**
Supplemental cash flow information:		
Cash paid during the periods for:		
Interest	$3,951,250	$4,322,707
Income taxes	690,000	520,071
Noncash investing and financing activities:		
Loans transferred to real estate owned	325,668	504,812

Earnings Per Share

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding. For the three and six month periods ended June 30, 2003 the weighted average number of common shares used in the computation of basic earnings per share was 2,808,535 and 2,808,387, respectively. The weighted average number of common shares for the three and six month periods ended June 30, 2002 was 2,968,462 and 3,017,311, respectively.

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note B: ORGANIZATION AND ACCOUNTING POLICIES, Continued.

Diluted earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding plus the dilutive effect of outstanding stock options. For the three and six month periods ended June 30, 2003 the weighted average number of common shares used in the computation of diluted earnings per share was 2,810,774 and 2,810,044, respectively. The weighted average number of common shares for the three and six month periods ended June 30, 2002 was 2,970,732 and 3,018,640, respectively.

Stock Options

Bancorp applies APB Opinion 25 and related Interpretations in accounting for the stock option plan. Accordingly, no compensation cost has been recognized. Had compensation cost for the stock option plan been determined based on the fair value at the grant dates for awards under the plan consistent with the method prescribed by FASB Statement No. 123, Bancorp s net income and earnings per share would have been adjusted to the pro forma amounts indicated below:

	Three Month Periods Ended June 30,	
	2003	**2002**
	(Unaudited)	
Net income, as reported	$558,059	$606,286
Deduct: Total stock-based compensation expense determined under fair value methods for all awards	(3,655)	(23,472)
Proforma net income	$554,404	$582,814
Reported income per common share:		
Basic	$ 0.20	$ 0.20
Diluted	0.20	0.20
Proforma income per common share:		
Basic	0.20	0.20
Diluted	0.20	0.20

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note B: ORGANIZATION AND ACCOUNTING POLICIES, Continued.

	Six Month Periods Ended June 30,	
	2003	2002
	(Unaudited)	
Net income, as reported	$ 1,323,024	$ 1,278,284
Deduct: Total stock-based compensation expense determined under fair value methods for all awards	(7,310)	(46,944)
Proforma net income	$ 1,315,714	$ 1,231,298
Reported income per common share:		
Basic	$ 0.47	$ 0.42
Diluted	0.47	0.42
Proforma income per common share:		
Basic	0.47	0.41
Diluted	0.47	0.41

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note B: ORGANIZATION AND ACCOUNTING POLICIES, Continued.

Recent Accounting Pronouncements

In June 2001, Statement of Financial Accounting Standards No. 142 (FAS 142), *Goodwill and Other Intangible Assets* was issued and is effective for fiscal years beginning after December 15, 2001. Under FAS 142, identifiable intangible assets that meet certain criteria will continue to be amortized over their estimated useful lives. However, goodwill and non-identifiable intangible assets will no longer be amortized. Instead, these assets will be evaluated for impairment on an annual basis. If an asset is deemed to be impaired, the asset will be written down through an adjustment to current earnings. As a result of adopting FAS 142 effective January 1, 2002, Bancorp no longer amortizes goodwill.

Note C: LOANS RECEIVABLE, NET.

A summary of the balances of loans follows:

	June 30, 2003	December 31, 2002
	(Unaudited)	
Mortgage loans on real estate:		
Residential 1-4 family	$116,695,687	$127,770,040
Commercial	58,281,467	50,440,340
Construction loans residential	9,097,781	11,844,367
	184,074,935	190,054,747
Commercial nonmortgage loans	16,328,100	15,072,501
Consumer and installment loans:		
Consumer and installment	10,137,994	11,354,651
Other	1,208,459	569,566
	11,346,453	11,924,217
Subtotal	211,749,488	217,051,465
Less:		
Allowance for possible loan losses	2,681,018	1,920,037
Unearned interest	12,505	16,925
Undisbursed portion of loans in process	5,283,382	3,167,369
Deferred loan fees	(241,114)	(96,216)
Loans receivable, net	$204,013,697	$212,043,350

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued.

Note D: DEPOSITS.

Interest-bearing deposits are summarized as follows:

	June 30 2003	December 31, 2002
	(Unaudited)	
Statement savings	$ 44,935,447	40,890,720
NOW accounts	54,404,154	50,724,071
Time:		
$100,000 and over	28,821,238	34,452,825
Under $100,000	59,674,824	63,749,059
Total interest-bearing deposits	$187,835,663	$189,816,675

Note E: ADVANCES FROM FEDERAL HOME LOAN BANK.

Advances from the Federal Home Loan Bank of Indianapolis (FHLB) are collateralized by FHLB stock and all non-employee residential mortgage loans.

Bancorp had $58.2 million and $64.4 million in advances from FHLB at June 30, 2003 and December 31, 2002, respectively. Interest rates range from 1.36% to 7.34% with maturities ranging from July 2003 to February 2012.

Annual principal payments of FHLB advances are as follows:

Twelve Months Ending June 30,	Amount	Weighted Rate
2004	$11,302,801	4.56%
2005	2,557,211	6.73%
2006	3,346,072	5.70%
2007		
2008	10,000,000	5.50%
2009 and thereafter	31,000,000	4.51%
Total	$58,206,084	4.85%

Note F: CASH DIVIDENDS

Bancorp paid a cash dividend of $.08 per share on its issued and outstanding common stock on March 13, 2003 to shareholders of record February 13, 2003. Total dividends paid on March 13, 2003 were $224,683.

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STURGIS BANCORP, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Concluded.

Bancorp paid a cash dividend of $.09 per share on its issued and outstanding common stock on June 16, 2003 to shareholders of record May 15, 2003. Total dividends paid on June 16, 2003 were $252,768.

Note G: EMPLOYEE BENEFIT PLANS

The Bank has a Defined Contribution Plan/401(k). The plan permits eligible employees to contribute a percentage of their compensation with the Bank contributing 25% of the employee s pre-tax contribution, not to exceed 10% of the employee s total compensation, as defined in the agreement. The plan also permits the Bank to make discretionary contributions.

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward Looking Statements

This report contains statements that constitute forward-looking statements. These statements appear in several places in this report and include statements regarding intent, belief, outlook, objectives, efforts, estimates or expectations of Bancorp, primarily with respect to future events and the future financial performance of the Bancorp. Any such forward-looking statements are not guarantees of future events or performance and involve risks and uncertainties, and actual results may differ materially from those in the forward-looking statement. Factors that could cause a difference between an ultimate actual outcome and a preceding forward-looking statement include, but are not limited to, changes in interest rates and interest rate relationships; demand for products and services; the degree of competition by traditional and non-traditional competitors; changes in banking laws and regulations; changes in tax laws; changes in prices, levies, and assessments; the impact of technological advances; government and regulatory policy changes; the outcome of any pending and future litigation and contingencies; trends in consumer behavior and ability to repay loans; and changes of the world, national and local economies. Bancorp undertakes no obligation to update, amend or clarify forward-looking statements as a result of new information, future events, or otherwise.

Financial Condition

Assets. Bancorp s total assets at June 30, 2003 were $294.6 million compared to $296.7 million at December 31, 2002, a decrease of $2.1 million or 0.7%. Decreases in interest-bearing deposits and loans were redeployed into securities available for sale.

Loans. The Bank s net loans decreased to $204.0 million at June 30, 2003 from $212.0 million at December 31, 2002. This decrease was primarily due to residential loans refinanced with the decrease in market rates. Adjustable-rate mortgage loans were refinanced into fixed rate mortgages to lock in low rates. The Bank sells long-term, fixed rate, residential mortgages in the secondary market, so the residential mortgages decreased to $116.7 million at June 30, 2003 from $127.8 million at December 31, 2002. Commercial mortgage loans increased to $58.3 million, or 28.2% of gross loans, at June 30, 2003 from $50.4 million, or 23.2% of gross loans at December 31, 2002. The demand for fixed-rate mortgage loans in 2003 was strong due to lower average interest rates during the period. The mortgage loans originated for sale were primarily funded by the secondary mortgage market sales. At June 30, 2003, outstanding loan commitments were $34.4 million, which included $18.5 million of home equity lines of credit. These loan commitments will be funded by interest-bearing deposits, maturing assets, and additional FHLB borrowings, if needed. The decision to sell fixed-rate mortgages with original maturities of 10 years or greater protects the Bank from the interest rate risks inherent in holding these longer fixed-rate loans and provides a source of liquidity to fund loan demand. Bank Management does not view the decrease in loan balances as a continuing trend. An increase in market interest rates

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will decelerate the pace of refinance in the residential loan portfolio and the Bank is continuing its growth in commercial loans.

Loans serviced for others increased by $23.4 million to $201.9 million at June 30, 2003 from $178.5 million at December 31, 2002. This servicing portfolio consists of loans originated by the Bank and sold in the secondary mortgage market with servicing retained by the Bank. Bancorp has no purchased mortgage servicing portfolio. The originated mortgage servicing rights asset had a valuation allowance at June 30, 2003 and December 31, 2002 of approximately $170,000 and $275,000, respectively. This allowance was established to recognize the measured impairment of the asset. The Bank will continue to monitor the valuation of the servicing rights asset. If subsequent analysis shows reductions in the impairment, the valuation allowance will be reduced.

Allowance for loan losses. The Bank makes provisions for loan losses in accordance with the changes in the credit risk of the loan portfolio. The provisions are based on the historic loss experience of the Bank, adjusted for the increasing credit risk inherent in the growing commercial loan portfolio. The Bank makes general provisions by loan category; residential mortgages, nonresidential mortgages, commercial loans, home equity loans, second mortgages, consumer loans and deposit account loans. Commercial loans and nonresidential mortgages are graded on an 8-point scale, based on the credit quality. Loan grades are reviewed at least annually. The grade of the loan determines the allowance for losses. Loans graded 6 or higher are reviewed for specific reserves, determined by management s assessment of risk.

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The following table provides an analysis of the allowance for loan losses:

	Six Months Ended June 30,		Year Ended December, 31,		
	2003	2002	2002	2001	2000
Balance at the beginning of the period	$1,920,037	$1,300,000	$1,300,000	$ 803,744	$730,000
Charge-offs:					
Residential mortgages	102,923	275,729	448,217	226,230	117,403
Commercial mortgages	91,507		121,053	42,900	
Construction loans residential					
Construction loans commercial					
Commercial nonmortgage loans	43,121	130,717	130,718	175,675	25,061
Loans secured by deposits					
Other consumer and installment loans	59,362	32,870	250,118	162,412	188,219
Total charge-offs	296,913	439,316	950,106	607,217	330,683
Recoveries					
Residential mortgages	640			21,344	54,261
Commercial mortgages	636		2,966		
Construction loans residential					
Construction loans commercial					
Commercial nonmortgage loans		16,548	16,548	3,021	2,044
Loans secured by deposits					
Other consumer and installment loans	27,143	22,922	55,713	22,914	39,122
Total recoveries	28,419	39,470	75,227	47,279	95,427
Net charge-offs	268,494	(399,846)	874,879	559,938	235,256
Provision for loan losses	1,029,476	815,257	1,494,916	1,056,194	309,000
Balance at the end of the period	$2,681,019	$1,715,411	$1,920,037	$1,300,000	$803,744
Ratio of net charge-offs during the period to Average loans outstanding during the period	0.13%	0.19%	0.40%	0.25%	0.11%
Allowance for loan losses to total loans	1.27%	0.79%	0.88%	0.58%	0.36%
Nonperforming assets to total assets	1.42%	1.74%	1.76%	1.55%	0.86%
Allowance for loan losses to nonperforming assets	64.05%	32.75%	36.82%	29.91%	34.50%

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The following table shows the allocation of the allowance for loan losses at the dates indicated by loan type:

	June 30, 2003		December 31, 2002	
	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans
Residential mortgages	$ 446,216	55.99%	$ 491,171	58.87%
Commercial mortgages	1,410,952	27.52%	956,217	23.24%
Construction loans residential	27,176	4.30%	8,651	3.70%
Construction loans commercial	34,856	1.12%	16,914	1.75%
Commercial nonmortgage loans	644,790	7.71%	314,963	6.94%
Loans secured by deposits		0.57%		0.26%
Other consumer and installment	117,029	4.79%	132,121	5.23%
Total allowance for loan losses	$2,681,019	100.00%	$1,920,037	100.00%

[Additional columns below]

[Continued from above table, first column(s) repeated]

	December 31, 2001		December 31, 2000	
	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans
Residential mortgages	$ 304,503	67.13%	$391,768	71.96%
Commercial mortgages	470,459	15.92%	189,927	11.73%
Construction loans residential	35,014	3.62%	23,871	2.14%
Construction loans commercial		0.20%		0.14%
Commercial nonmortgage loans	165,188	5.89%	92,594	5.72%
Loans secured by deposits		0.26%		0.19%
Other consumer and installment	324,836	6.98%	105,584	8.14%
Total allowance for loan losses	$1,300,000	100.00%	$803,744	100.00%

Loans in nonaccrual status at June 30, 2003 of $2.8 million consisted primarily of residential and commercial real estate loans, for which foreclosure has begun or full collection of the loan is questionable. The following table presents the aggregate amount of troubled asset categories as of the dates indicated:

	June 30, 2003	2002	December 31, 2001	2000

Past due 90 days or greater	$ 277,138	$ 899,975	$1,073,625	$1,314,288
Nonaccrual loans	2,828,513	2,955,666	2,821,965	911,610
Real estate owned	1,080,092	1,358,759	451,173	103,500
Total nonperforming assets	4,185,743	5,214,400	4,346,763	2,329,398
Restructured assets	798,419	626,882	1,381,920	1,030,858
Total troubled assets	$4,984,162	$5,841,282	$5,728,683	$3,360,256
Ratio of troubled assets to total loans	2.44%	2.75%	2.56%	1.50%
Ratio of troubled assets to total assets	1.69%	1.97%	2.05%	1.24%

Interest-bearing Deposits in Banks. Interest-bearing deposits in banks were $18.7 million at June 30, 2003, compared to $23.0 million at December 31, 2002, a decrease of $4.3 million, due to maturity.

Securities Available for sale. Investment securities available for sale of $9.1 million at June 30, 2003 consisted primarily of shares in a mutual fund that invests in mortgage-related securities.

Securities Held-to-maturity. Investment securities held-to-maturity consisting

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of municipal obligations, trust preferred and mortgage-backed securities were $11.6 million at June 30, 2003, compared to $12.6 million at December 31, 2002 a decrease of $1.0 million. The decrease was primarily due to principal payments on mortgage-backed securities.

Investments in Limited Partnerships. Investments in limited partnerships increased to $1.2 million at June 30, 2003 from $161,080 at December 31, 2002. This increase is due to an investment in North Lake Apartments in Elkhart, Indiana. North Lake Apartments is a 192-unit apartment community which utilizes tax exempt financing along with federal tax credits to provide affordable housing to residents with less than 60% of the area s median income. Bancorp s investment of $1.1 million in the six months ended June 30, 2003 fully fund s Bancorp s 25% partnership position.

Deposits and Borrowed Funds. Deposits were $205.5 million at June 30, 2003, compared to $202.6 million at December 31, 2002, an increase of $2.9 million or 1.4%. The increase is primarily in noninterest-bearing custodial accounts for mortgage investors and commercial checking accounts. Custodial accounts increased due to payoff activity not yet remitted to investors.

The Bank has an available line of credit with the Federal Home Loan Bank of Indianapolis (FHLB) which provides for advances up to $10.0 million and matures in March 2004. All borrowings from FHLB are collateralized by FHLB stock and non-employee mortgage loans. Short-term advances were $4.2 million at June 30, 2003 compared to $6.7 million at December 31, 2002.

Long-term advances were $54.0 million at June 30, 2003 compared to $57.7 million at December 31, 2002.

Capital

The stockholders equity of Bancorp was $28.4 million at June 30, 2003 compared to $27.5 million at December 31, 2002, an increase of $0.9 million or 3.4%. The primary component of this increase was net income. Cash dividends during the first six months of 2003 of $0.17 per share reduced retained earnings by $477,451. The stockholders equity was 9.8% of total assets at June 30, 2003.

The Federal Reserve Board (FRB) has adopted risk-based capital guidelines applicable to Bancorp. These guidelines require that financial holding companies, such as Bancorp, maintain capital commensurate with both on and off balance sheet credit risks of their operations. Under the guidelines, a financial holding company must have a minimum ratio of total capital to risk-weighted assets of 8.0%.

In addition, a financial holding company must maintain a minimum ratio of Tier 1 capital equal to 4.0% of risk-weighted assets. Tier 1 capital includes common stockholders equity, qualifying perpetual preferred stock and minority interest in equity accounts of consolidated subsidiaries less goodwill.

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As a supplement to the risk-based capital requirements, the FRB has also adopted leverage capital ratio requirements. The leverage ratio requirements establish a minimum ratio of Tier 1 capital to total assets, less goodwill, of 3% for the most highly rated financial holding companies. All other financial holding companies are required to maintain additional Tier 1 capital yielding a leverage ratio of 4%-5%, depending on the particular circumstances and risk profile of the institution.

The following table summarizes the capital ratios of Bancorp at the dates indicated:

		June 30, 2003	December 31, 2002
Equity to assets		9.6%	9.2%
Tier I leverage		7.9%	7.5%
Risk-based:	Tier I capital	11.3%	11.1%
	Total capital	12.6%	12.0%

Asset/Liability Management

A significant component of the Bank s earnings is net interest income. The Bank s asset/liability management strategy is to maximize net interest income over time by reducing the impact of fluctuating interest rates. This is accomplished by matching the mix and maturities of its assets and liabilities. At the same time the Bank s asset/liability strategies for managing interest rate risk must also accommodate customer demands for particular types of deposit and loan products. The Bank uses various asset/liability management techniques in an attempt to maintain a profitable mix of financial assets and liabilities, provide deposit and loan products that meet the needs of its market area, and maintain control over interest rate risk resulting from changes in interest rates.

Net interest income is derived from the difference or spread between the yield on interest-earning assets and the cost of interest-bearing liabilities. The Bank has sought to reduce its exposure to changes in interest rates by matching more closely the effective maturities and repricings of its interest-sensitive assets and liabilities. At the same time, the Bank s asset/liability management strategies must also accommodate customer demands for particular types of deposit and loan products.

While much of the Bank s asset/liability management efforts involve strategies that increase the rate sensitivity of its loans and investments, such as the sale of long-term fixed rate loans, originations of adjustable rate loans and purchases of adjustable rate mortgage-backed securities or relatively short average life fixed-rate investments, it also uses certain techniques to reduce the rate sensitivity of its deposits and borrowed money. Those techniques include attracting longer-term certificates of deposit when the market will permit, emphasizing core deposits, which are less sensitive to changes in interest rates, and borrowing through long-term FHLB advances. The Bank s asset/liability management strategy will appropriately change when market rates change.

The Bank measures its exposure to interest rate fluctuations primarily by using a

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computer modeling system designed for savings institutions such as the Bank. The model uses assumptions which management believes are reasonable for the analysis. These assumptions include (but are not limited to) prepayment and decay rates based on nine interest rate scenarios. It allows the Bank to adjust its asset-liability mix based on the interest rate risk identified. The analysis estimates the changes in the market value of the Bank s equity using interest rate change scenarios ranging from +4% to - 4%, in 1% increments from current market rates. At June 30, 2003, the following table illustrates the interest rate sensitivity of Bancorp s equity to changes in market interest rates.

(in Thousands of Dollars)	
Book value of stockholders equity	$28,380
4% increase in market rates	44,562
3% increase in market rates	44,490
2% increase in market rates	45,973
1% increase in market rates	44,856
No change (current market value of equity)	43,507
1% decrease in market rates	40,699
2% decrease in market rates	37,694
3% decrease in market rates	34,102
4% decrease in market rates	29,633

As the table shows, Bancorp s book value of equity is less than estimated market value in all of the scenarios. That indicates that Bancorp is able to withstand fluctuations in market interest rates without posting a significant threat to either Bancorp s stockholders equity or the federal deposit insurance system and, therefore, Bancorp can be deliberate in its actions to adjust the asset-liability mix. Bancorp would meet the regulatory minimum capital requirements in all of the interest-rate scenarios.

Bancorp has an Asset-Liability Management Committee (ALCO) that meets as needed. The purpose of this Committee is to communicate, coordinate, and monitor asset-liability management procedures. The Committee establishes and monitors the volume and mix of both assets and funding sources. The objective is to manage assets and funding sources to produce results consistent with Bancorp s liquidity requirements, capital adequacy, growth, and profitability goals. To accomplish this objective, the ALCO uses internal budget variance reports, forecasts for changes in interest rates and consumer deposit activity, as well as forecasts of loan demand in each of Bancorp s loan types, investment maturities and new investment alternatives, and various other internal and external reports.

Simulation: Bancorp uses a computer-based earnings simulation model to estimate the effects of various interest rate environments on the balance sheet structure

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and net interest income. These simulation techniques involve changes in interest rate relationships, asset and liability mixes, and prepayment options inherent in financial instruments, as well as interest rate levels in order to quantify risk. Bancorp s sensitivity is estimated by first forecasting the next twelve months of net interest income under an assumed environment of constant market interest rates. Next, immediate parallel interest rate shocks are constructed in the model. The rate shocks reflect changes of equal magnitude to all market interest forecast under each of the rate shock scenarios. The resulting change in net interest income is an indication of the sensitivity change in net earnings to directional changes in market interest rates. This model is based solely on parallel changes in market rates and does not reflect the levels of interest rate risk that may arise from other factors such as changes in the spreads between key market rates or in the shape of the Treasury yield curve. The net interest income simulation model includes on-balance sheet loan, investment, deposit, and debt instruments.

Bancorp s Board of Directors compares net interest income sensitivity and has established tolerance limits for fluctuation. At June 30, 2003, the forecasted exposure was within Bancorp s established policy limits, except in falling rate change scenarios. Bancorp s Board of Directors and Management consider further significant rate decreases from June 30, 2003 as unlikely.

Net Interest Income Sensitivity: Change in Projected Results vs. Constant Rates

12 Month Projection July 2003 through June 2004

	Rate Shock Amount				
	(2.00%)	**(1.00%)**	**0.00%**	**1.00%**	**2.00%**
Percent Change in net interest income vs constant rates	(16.11%)	(7.99%)	0.00%	6.64%	15.95%
ALCO Policy	(6.00%)	(3.00%)	0.00%	(4.00%)	(8.00%)

Effect of Interest Rate Fluctuations

Bancorp s consolidated results of operations depend to a large extent on Bancorp s level of net interest income, which is the difference between interest income earned on its loan and investment portfolios versus the interest paid on deposits and borrowed funds. If the cost of funds increases faster than the yield on its interest-earning assets, net interest income will be reduced.

Bancorp measures its interest rate risk primarily using simulation analysis. This analysis is prepared by the Chief Financial Officer and reviewed by the Asset/Liability Management Committee. The ALCO is comprised of the Chief Executive Officer, Chief Financial Officer and other representatives from operations, branch

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administration, lending, trust, private banking, and marketing. Bancorp s Board of Directors reviews quarterly reports that estimate Bancorp s sensitivity to changes in interest rates. Sensitivity is estimated for net interest income and market value of portfolio equity.

While Bancorp uses various tools to monitor interest rate risk, it is unable to predict future fluctuations in interest rates or the specific impact thereof. The market value of most of Bancorp s financial assets is sensitive to fluctuations in market interest rates. Fixed-rate investments including mortgage loans and mortgage-backed securities decline in value as interest rates rise. Adjustable-rate loans and securities generally have less market value volatility than do fixed-rate products.

Liquidity

Bancorp maintains certain levels of liquid assets (the most liquid of which are cash and cash equivalents and investment securities) in order to meet demands from loan commitments, savings withdrawals and other obligations. Bancorp manages liquidity by maintaining a portion of its liquid assets in overnight accounts and by keeping various maturities in its portfolio of investment securities. The primary sources of liquidity are loan repayments and sales, maturing investments, deposit accounts, and FHLB borrowings.

Two factors contributed to the increased liquidity at June 30, 2003; low interest rates for residential mortgages and decreased confidence in equity markets. The residential mortgages that have refinanced into low fixed-rate terms have been sold to the secondary mortgage market, providing funds for Bancorp to redeploy. Bancorp originated commercial mortgage and commercial nonmortgage loans, so the percentage of commercial loans to total loans increased. Decreased investor confidence in equity markets has increased bank deposits nationally, including deposits at Bancorp. This increase in deposits provided additional funds Bancorp invested in securities and interest-bearing deposits in other banks. Either an increase in loan rates or investor confidence in equity markets could significantly reduce Bancorp s liquidity position.

Cash Flows

Operating. Cash flows from operating activities are most significantly affected by net income and mortgage banking activities. Net income was $1,323,034 and $1,278,284 for the six months ended June 30, 2003 and 2002, respectively. The increase in the gain on sale of loans to $1,043,880 in the six months ended June 30, 2003 from $429,214 in the six months ended June 30, 2002 is significantly offset by the increase in amortization of intangibles (originated mortgage servicing rights). Loans originated for sale and proceeds from the sale of loans also increased with the historically low mortgage loan rates. Loans originated for sale were $82.1 million and $34.1 million for the six months ended June 30, 2003 and 2002, respectively. This increase in loans originated for sale is primarily due to low residential mortgage rates. Proceeds from the sales of loans were $81.6 million and $38.3 million for the six months ended June 30, 2003 and 2002, respectively. Because

Bancorp generally has a policy of selling long-term fixed rate mortgage loans, the volume of loan sales varies with customer demand for these loans.

Investing. Cash flows from investing activities are most significantly affected by loans made to customers net of principal payments, changes in Bancorp s investment portfolio, and increases in interest-bearing deposits in banks. For the six months ended June 30 2003 and 2002 there were decreases in loans of $6.7 million and $6.2 million, respectively, primarily due to refinanced loans. Investment purchases and maturities also affect cash flows from investing activities. Bancorp s management maintains investments at levels that provide Bancorp with optimal return, risk and liquidity. In the six months ended June 30, 2003, Bancorp decreased its holdings in interest-bearing deposits in banks by $4.3 million to $18.7 million. This decrease in interest-bearing deposits is due to Bancorp s positioning for rising interest rates. In contrast, for the six months ended June 30, 2002, Bancorp increased interest-bearing deposits in banks by $21.5 million to securely lock in interest rates as short-term market rates decreased. Bancorp also purchased $9.1 million and $1.1 million of other securities and an investment in a limited partnership, respectively, during the six months ended June 30, 2003.

Financing. Cash flows from financing activities are mostly affected by changes in deposits and FHLB advances. Deposits increased $2.9 million and $23.5 million in the six months ended June 30, 2003 and 2002, respectively. Deposit increases in the six months ended June 30, 2002 included jumbo certificates of deposit, which the Bank used as an alternative to additional FHLB advances. Bancorp also used FHLB advances for financing its operating and investing activities. The FHLB advances decreased $6.2 million and $4.4 million during the six months ended June 30, 2003 and 2002, respectively. Bancorp generally does not borrow funds from FHLB without a specific investment strategy, such as funding specific loan commitments, holding (rather than selling) selected loans, or increasing leverage of Bancorp through investments in interest-bearing deposits in banks.

Contractual Obligations

	Payments Due by Period				
	Total	Less than 1 year	1 - 3 years	4 - 5 years	After 5 years
Certificates of deposit	$ 88,496,063	$ 36,870,091	$23,864,802	$ 22,590,392	$ 5,170,777
FHLB advances	$ 54,144,253	$ 11,302,801	$ 5,903,283	$ 10,000,000	$ 31,000,000
Total contractual cash obligations	$142,640,316	$ 48,155,287	$29,768,085	$ 32,590,392	$ 36,170,777

The long-term debt obligations consist of certificates of deposit and advances from the Federal Home Loan Bank. The above schedule represents principal payments only and does not include interest.

Results of Operations

Bancorp reported net income of $558,059 or $0.20 per share for the three months

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ended June 30, 2003 compared to net income of $606,286 or $0.20 per share for the three months ended June 30, 2002. The decrease in net income was primarily due to an increase in the provision for loan losses. Bancorp reported net income of $1,323,024 or $0.47 per share for the six months ended June 30, 2003 compared to net income of $1,278,284 or $0.42 per share for the six months ended June 30, 2002. The increase in net income was primarily due to an increase in mortgage banking activities.

Interest Income

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002. Interest income decreased $0.4 million to $3.9 million from $4.3 million. This decrease is primarily due to decreases in the average interest rates earned to 6.09% in 2003 from 6.77% in 2002. The decrease in interest income is likely to reverse when interest rates increase.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002. Interest income decreased $0.7 million to $8.0 million from $8.7 million. This decrease is primarily due to decreases in the average interest rates earned to 6.21% in 2003 from 6.94% in 2002. The decrease in interest income is likely to reverse when interest rates increase.

During the three and six months ended June 30, 2003 and June 30, 2002, Bancorp increased investment securities as loans refinanced and were subsequently sold.

Interest Expense

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002. Interest expense decreased $0.2 million to $1.8 million from $2.0 million. This was primarily due to the decrease in rates paid on average interest-bearing deposits and FHLB advances. The rate paid on average interest-bearing liabilities decreased to 2.88% from 3.36%.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002. Interest expense decreased $0.5 million to $3.7 million from $4.2 million. This was primarily due to the decrease in rates paid on average interest-bearing deposits and FHLB advances. The rate paid on average interest-bearing liabilities decreased to 2.96% from 3.49%.

During the three and six months ended June 30, 2003 compared to the three and six months ended June 30, 2002, the shift from FHLB borrowings to lower rate deposit accounts also contributed to the decrease in interest expense.

Net Interest Income

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30,

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2002. Net interest income decreased $125,099 to $2.1 million from $2.3 million. This decrease was primarily caused by a decrease in net interest-earning assets to $9.1 million from $11.3 million and a decrease in the net interest margin to 3.31% from 3.56%.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002. Net interest income decreased $0.2 million to $4.3 million from $4.5 million. This decrease was primarily caused by a decrease in net interest-earning assets to $8.4 million from $11.4 million and a decrease in the net interest margin to 3.34% from 3.61%.

During the three and six months ended June 20, 2003 compared to the three and six months ended June 30, 2002, the decrease in market interest rates to historically low levels significantly contributed to the decrease in net interest income, as the portfolio has a positive gap (assets reprice more quickly than liabilities).

Provision for Loan Losses

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002. The provision for loan losses was $710,787 for the quarter ended June 30, 2003 and $235,125 for the quarter ended June 30, 2002.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002. The provision for loan losses was $1,029,476 for the quarter ended June 30, 2003 and $815,257 for the quarter ended June 30, 2002.

The provision for loan losses was based upon management s assessment of relevant factors, including types and amounts of non-performing loans, historical and anticipated loss experience on such types of loans, and current and projected economic conditions. The increases in provision for loan losses during the three and six month periods ended June 30, 2003 compared to the three and six month periods ended June 30, 2002 are primarily due to a single commercial lending relationship. During the three months ended June 30, 2003, Bancorp classified a loan relationship totaling $5.4 million which resulted in an increase in the allowance for loan losses of approximately $700,000.

Noninterest Income

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002. Noninterest income was $1.8 million for the three months ended June 30, 2003 compared to $1.1 million for the three months ended June 30, 2002, an increase of $765,573 or 68.5%. The primary component of noninterest income was mortgage banking activities, which increased to $989,221 in 2003 from $274,659 in 2002. Commission income was $303,179 for the three months ended June 30, 2003 compared to $282,656 for the three months ended June 30, 2002.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002. Noninterest income was $3.4 million for the six months ended June 30, 2003 compared to $2.5 million for the six months ended June 30, 2002, an increase of $872,641 or 34.5%. The primary component of noninterest income was mortgage banking activities, which

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increased to $1,723,700 in 2003 from $859,302 in 2002. Commission income was $542,142 for the six months ended June 30, 2003 compared to $492,653 for the six months ended June 30, 2002.

During the three and six months ended June 30, 2003 compared to the three and six months ended June 30, 2002, the increase in mortgage banking activities is due to the increase in loan sales during 2003 compared to 2002. Management does not expect refinance activity to continue at the current pace. The increases in commission income are due to growth in account relationships at Oakleaf Financial Services, Inc., the Bank s wholly owned investment subsidiary.

Noninterest Expense

Three Months Ended June 30, 2003 Compared to Three Months Ended June 30, 2002. Noninterest expense was $2.5 million for the three months ended June 30, 2003 compared to $2.3 million for the three months ended March 31, 2002, an increase of $235,030. Salaries and employee benefits increased by $163,870 due to staffing changes, salary adjustments and cost of living increases that took effect January 2003 and benefits expense. Service bureau expense increased to $238,800 from $157,206 for the three months ended June 30, 2003 and 2002, respectively.

Six Months Ended June 30, 2003 Compared to Six Months Ended June 30, 2002. Noninterest expense was $4.8 million for the six months ended June 30, 2003 compared to $4.4 million for the six months ended June 30, 2002, an increase of $370,509. Salaries and employee benefits increased by $219,864 due to staffing changes, salary adjustments and cost of living increases that took effect January 2003 and benefit expense. Service bureau expense increased to $444,113 from $315,260 for the six months ended June 30, 2003 and 2002, respectively.

For the three and six months ended June 30, 2003 compared to the three and six months ended June 30, 2002, the increase in service bureau expense was due to conversion in April 2003 to a different service bureau. The conversion to a new service bureau enhances the technological capability and efficiency of the Bank.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information concerning quantitative and qualitative disclosures about market risk contained under the captions Asset/Liability Management and Effect of Interest Rate Fluctuations on pages 13 through 18 (inclusive) of the Bancorp s Annual Report to Stockholders for the year ended December 31, 2002 is incorporated herein by reference. Such Annual Report was previously filed as Exhibit 13.1 to Bancorp s Annual Report on Form 10-K for the year ended December 31, 2002.

Copies of the Bank s historical filings with the FDIC under the Securities Exchange Act of 1934 can be obtained from Sturgis Bank & Trust Company by contacting Eric L. Eishen at Sturgis Bank & Trust Company, 113-125 E. Chicago Road, Sturgis, Michigan

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49091, telephone number (269) 651-9345 or, for a nominal fee, from the FDIC, telephone number (202) 898-8913 or fax number (202) 898-3909. Filings of Bancorp with the Securities and Exchange Commission can be obtained from Bancorp by contacting Eric L. Eishen at Sturgis Bancorp, Inc., 113-125 E. Chicago Road, Sturgis, Michigan 49091, telephone number (269) 651-9345 or through the Securities and Exchange Commission EDGAR System at www.sec.gov. The Bank also maintains a website at www.sturgisbank.com, at which Bancorp s electronic filings with the SEC are freely available.

ITEM 4. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

Bancorp s chief executive officer and chief financial officer have concluded that Bancorp s disclosure controls (as defined in Exchange Act Rule 13a-14(c)) are sufficiently effective to ensure that the information required to be disclosed by Bancorp in the reports it files under the Exchange Act is gathered, analyzed and disclosed with adequate timeliness, accuracy and completeness, based on an evaluation of such controls and procedures conducted within 90 days prior to the date hereof.

CHANGES IN INTERNAL CONTROLS

There have been no significant changes in Bancorp s internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation referred to above.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There are no material legal proceedings other than the ordinary routine proceedings of Bancorp.

ITEM 2. CHANGES IN SECURITIES

The information contained in the section captioned Market Information in the 2002 Annual Report to Stockholders is incorporated herein by reference. Such Annual Report was previously filed as Exhibit 13.1 to Bancorp s Annual Report on Form 10-K for the year ended December 31, 2002. In addition to the information incorporated by reference, the following table shows sales of unregistered securities by Bancorp since December 31, 2002.

Date of Sale	Number of Shares	Exercise Price	Name
01/03/2003	9,000	$ 9.00	Leonard L. Eishen

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

The Annual Meeting of stockholders was held on April 29, 2003. Two matters were voted at the Meeting.

Election of Directors

Mr. Eric L. Eishen and Mr. James A. Goethals were elected to the Board of Directors for three (3) year terms expiring in 2006. The certified shares for the election of Eric L. Eishen were 2,282,332. The certified shares for the election of James A. Goethals were 2,281,657. The other Directors whose terms of office continued after the Meeting were Raymond H. Dresser, Jr., Leonard L. Eishen, Lawrence A. Franks, Donald L. Frost, and Philip G. Ward.

Ratification of the appointment of Independent Public Accountants

The Board of Directors appointed Plante & Moran, PLLC as Independent Public Accountants for the year ending December 31, 2003. The certified shares voted at the Meeting ratified this appointment with 2,301,565 shares voting in favor of the appointment, 45,282 shares voting against, and 124,450 shares abstaining. The appointment was approved.

ITEM 6. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a) Exhibit Listing

Exhibit Number	Description
2.1	Plan of Reorganization and Merger Agreement (1)
2.2	Consolidation Agreement (1)
3.1	Articles of Incorporation of Sturgis Bancorp, Inc. (1)

Exhibit Number	Description
3.2	Bylaws of Sturgis Bancorp, Inc. (1)
10.1	Sturgis Federal Savings Bank Non-Employee Director Stock Option Plan (2)
10.2	Sturgis Federal Savings Bank Director Stock Option Plan (2)
10.3	Sturgis Federal Savings Bank Employee Stock Option Plan (3)
13.1	Annual Report to Stockholders (4)
21	Subsidiaries of Registrant (4)
31.1	Certification of President Chief Executive Officer
31.2	Certification of Chief Financial Officer
99.1	Certification of the CEO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.2	Certification of the CFO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(1) Incorporated by reference to the Proxy Statement dated November 21, 2001 of Sturgis Bank & Trust Company.

(2) Incorporated by reference to 1994 Form 10-KSB of Sturgis Federal Savings Bank, the predecessor of Sturgis Bank & Trust Company.

(3) Incorporated by reference to 1995 Form 10-KSB of Sturgis Federal Savings Bank, the predecessor of Sturgis Bank & Trust Company.

(4) Incorporated by reference to Form 10-K for Sturgis Bancorp, Inc. for the year ended December 31, 2002.

(b) Reports on Form 8-K

On January 16, 2003, Bancorp filed one report on Form 8-K, announcing the resignation of Gary Malloy as a director of Bancorp.

On May 1, 2003, Bancorp filed one report on Form 8-K, announcing the appointments of Eric L. Eishen as President and Chief Executive Officer and Ronald W. Scheske as Vice President effective May 1, 2003.

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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.

	STURGIS BANCORP, INC. (Registrant)
Date August 13, 2003	/s/ Eric L. Eishen
	Eric L. Eishen, President and Chief Executive Officer
Date August 13, 2003	/s/ Brian P. Hoggatt
	Brian P. Hoggatt, Chief Financial Officer

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10-Q EXHIBIT INDEX

EXHIBIT NO.	DESCRIPTION
EX - 31.1	Certification of President Chief Executive Officer
EX - 31.2	Certification of Chief Financial Officer
EX - 32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
EX - 32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002