SLADES FERRY BANCORP
Form 10-Q
August 11, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarter ended June 30, 2006

Commission file number 000-23904

SLADE'S FERRY BANCORP.
(Exact name of registrant as specified in its character)

Massachusetts	04-3061936
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
100 Slade's Ferry Avenue Somerset, Massachusetts	02726
(Address of principal executive offices)	(Zip code)

(508)-675-2121
(Registrant's telephone number, including area code)

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, and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

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

Large Accelerated Filer [ ] Accelerated Filer [ ] Non Accelerated Filer [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

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

Common stock ($0.01 par value) 4,171,990 outstanding shares as of July 31, 2006.

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PART I

ITEM 1

FINANCIAL STATEMENTS

SLADE'S FERRY BANCORP. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	June 30, 2006	Decembe
Assets	(In thousands)	
Cash and due from banks	$ 22,319	$ 1
Interest-bearing demand deposits with other banks	970	
Federal funds sold	6,200	
Cash and cash equivalents	29,489	2

Interest-bearing certificates of deposit with other banks	100	
Securities available for sale	88,744	9
Securities held to maturity (fair value approximates of $26,275 as of June 30, 2006 and $28,858 as of December 31, 2005)	27,235	2
Federal Home Loan Bank stock, at cost	6,304	
Loans, net of allowance for loan losses of $4,366 at June 30, 2006 and $4,333 at December 31, 2005	426,678	40
Premises and equipment, net	5,746	
Goodwill	2,173	
Accrued interest receivable	2,091	
Bank-owned life insurance	12,097	1
Deferred tax assets, net	2,846	
Other assets	1,850	
	$605,353	$58
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest-bearing	$ 80,710	$ 8
Interest-bearing	349,358	33
Total deposits	430,068	41
Short-term borrowings	10,000	
Long-term borrowings	93,043	10
Subordinated debentures	10,310	1
Due to broker	9,509	
Accrued expenses and other liabilities	2,575	
Total liabilities	555,505	53
Stockholders' equity:		
Common stock, par value $0.01 per share; authorized 10,000,000 shares; issued and outstanding 4,164,042 shares at June 30, 2006 and 4,132,200 shares at December 31, 2005	42	
Additional paid-in capital	31,608	3
Retained earnings	19,782	1
Accumulated other comprehensive loss	(1,484)	(
Unearned compensation	(100)	
Total stockholders' equity	49,848	4
	$605,353	$58

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

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SLADE'S FERRY BANCORP. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Six Months Ended June 30,	
	2006	2005
	(In thousands, except per share	

Interest and dividend income:		
Interest and fees on loans	$ 13,120	$ 10,993
Interest and dividends on securities:		
Taxable	2,550	2,430
Tax-exempt	134	175
Interest on federal funds sold	64	157
Other interest	18	11
Total interest and dividend income	15,886	13,766
Interest expense:		
Interest on deposits	4,167	2,616
Interest on Federal Home Loan Bank advances	2,365	1,985
Interest on subordinated debentures	394	291
Total interest expense	6,926	4,892
Net interest and dividend income	8,960	8,874
Provision for loan losses	39	65
Net interest income, after provision for loan losses	8,921	8,809
Noninterest income:		
Service charges on deposit accounts	659	420
Gain on sales of assets	--	51
Gain (loss) on sales and calls of available-for-sale securities, net	(169)	17
Increase in cash surrender value of life insurance policies	213	258
Other income	546	363
Total noninterest income	1,249	1,109
Noninterest expense:		
Salaries and employee benefits	4,398	4,095
Occupancy and equipment expense	983	809
Professional fees	800	614
Marketing expense	187	328
Other expense	1,334	1,091
Total noninterest expense	7,702	6,937
Income before income taxes	2,468	2,981
Provision for income taxes	935	1,033
Net income	$ 1,533	$ 1,948
Earnings per share:		
Basic	$ 0.37	$ 0.48
Diluted	$ 0.37	$ 0.47
Average common shares outstanding:		
Basic	4,151,091	4,094,939
Diluted	4,168,271	4,123,796

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

SLADE'S FERRY BANCORP. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended June 30 2006	2005
	(In thousands, except per share	
Interest and dividend income:		
Interest and fees on loans	$ 6,685	$ 5,727
Interest and dividends on securities:		
Taxable	1,217	1,199
Tax-exempt	65	84
Interest on federal funds sold	53	92
Other interest	10	7
Total interest and dividend income	8,030	7,109
Interest expense:		
Interest on deposits	2,256	1,457
Interest on Federal Home Loan Bank advances	1,209	1,074
Interest on subordinated debentures	170	155
Total interest expense	3,635	2,686
Net interest and dividend income	4,395	4,423
Provision for loan losses	--	15
Net interest income, after provision for loan losses	4,395	4,408
Noninterest income:		
Service charges on deposit accounts	352	212
Gain on sales of assets	--	11
Gain (loss) on sales and calls of available-for-sale securities, net	(172)	15
Increase in cash surrender value of life insurance policies	106	111
Other income	260	191
Total noninterest income	546	540
Noninterest expense:		
Salaries and employee benefits	2,287	2,120
Occupancy and equipment expense	490	400
Professional fees	388	307
Marketing expense	109	229
Other expense	678	566
Total noninterest expense	3,952	3,622
Income before income taxes	989	1,326
Provision for income taxes	363	478
Net income	$ 626	$ 848
Earnings per share:		
Basic	$ 0.15	$ 0.21
Diluted	$ 0.15	$ 0.21

Average common shares outstanding:		
Basic	4,156,481	4,112,969
Diluted	4,170,610	4,132,712

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

SLADE'S FERRY BANCORP. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(Unaudited)

	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulat Other Comprehens Loss
	(In thousands, except per share da				
Balance at December 31, 2005	4,132,200	$ 41	$31,014	$18,998	$(1,198)
Comprehensive income:					
Net income	-	-	-	1,533	-
Other comprehensive loss	-	-	-	-	(286)
Comprehensive income					
Issuance of common stock	16,842	-	302	-	-
Stock options exercised	28,000	1	304	-	-
Tax benefit of stock options exercised	-	-	82	-	-
Stock-based compensation	-	-	136	-	-
Purchase of treasury stock	(13,000)	-	(230)	-	-
Unearned compensation	-	-	-	-	-
Dividends declared ($.18 per share)	-	-	-	(749)	-
Balance at June 30, 2006	4,164,042	$ 42	$31,608	$19,782	$(1,484)

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

SLADE'S FERRY BANCORP. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended June	
	2006	2005

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	(In thousands)	
Cash flows from operating activities:		
Net income	$ 1,533	$ 1,94
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization, net of accretion of securities	65	15
Loss (gain) on sales and calls of available-for-sale securities, net	169	(1
Change in net deferred loan fees	(10)	4
Provision for loan losses	39	6
Deferred tax provision (benefit)	(491)	12
Depreciation and amortization	439	39
Gain on sale of assets	--	(5
Increase in cash surrender value of life insurance	(213)	(24
Stock-based compensation	136	-
Net change in:		
Other assets	67	14
Accrued interest receivable	224	(21
Other liabilities	(463)	51
Net cash provided by operating activities	1,495	2,85
Cash flows from investing activities:		
Activity in available-for-sale securities:		
Purchases	(6,440)	(20,76
Sales	15,196	1,82
Maturities, calls and paydowns	5,611	6,54
Activity in held-to-maturity securities:		
Maturities, calls and paydowns	2,046	4,25
Purchases of Federal Home Loan Bank stock	--	(1,25
Loan principal originations, net	(17,097)	(29,20
Recoveries of loans previously charged off, net	--	5
Capital expenditures	(268)	(1,04
Proceed from sale of property and equipment	--	2
Proceeds from sale of investment real estate	--	65
Redemption of life insurance policy	--	12
Net cash used in investing activities	(952)	(38,78

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

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SLADE'S FERRY BANCORP. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Unaudited)

	Six Months Ended June	
	2006	2005
	(In thousands)	
Cash flows from financing activities:		

Net increase (decrease) in noninterest-bearing deposits	$ 5	$ (2,63
Net increase in interest-bearing deposits	14,217	9,37
Short-term advances from Federal Home Loan Bank	43,000	-
Long-term advances from Federal Home Loan Bank	--	20,00
Payments on Federal Home Loan Bank short-term advances	(40,000)	-
Payments on Federal Home Loan Bank long-term advances	(7,822)	(20
Proceeds from issuance of common stock	302	31
Stock options exercised	305	31
Purchase of treasury stock	(230)	-
Unearned compensation	(100)	-
Dividends paid	(749)	(73
Net cash provided by financing activities	8,928	26,41
Net increase (decrease) in cash and cash equivalents	9,471	(9,50
Cash and cash equivalents at beginning of period	20,018	35,19
Cash and cash equivalents at end of period	$ 29,489	$ 25,68
Supplemental disclosures:		
Interest paid	$ 7,105	$ 4,77
Income taxes paid	$ 475	$ 88
Non-cash disclosure:		
Due to broker	$ 9,509	$ -

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

SLADE'S FERRY BANCORP. AND SUBSIDIARY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
June 30, 2006

NOTE A - BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and the instructions to Form 10-Q and, accordingly, do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of the management of Slade's Ferry Bancorp. (the "Company"), all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six months ended June 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

The year-end consolidated financial data was derived from audited financial statements, but does not include all disclosures required by GAAP. This Form 10-Q should be read in conjunction with the Company's Annual Report filed on Form 10-K for the year ended December 31, 2005.

NOTE B - ACCOUNTING POLICIES

The accounting principles followed by Slade's Ferry Bancorp. and subsidiary and the methods of applying these principles which materially affect the determination of financial position, results of operations, or changes in financial position are consistent with those used for the year ended December 31, 2005, except for the adoption of Statement of Financial Accounting Standards No. 123(R), Share-Based Payment, ("SFAS 123 (R)" or the "Statement") effective January 1, 2006 applicable to the Company's stock-based employee compensation plans. See Note C.

The consolidated financial statements include the accounts of Slade's Ferry Bancorp., its wholly-owned subsidiary, Slade's Ferry Trust Company (the "Bank") and the Bank's wholly-owned subsidiaries. All significant inter-company balances and transactions have been eliminated in consolidation. The Company accounts for its wholly-owned subsidiary, Slade's Ferry Statutory Trust I, using the equity method.

Slade's Ferry Statutory Trust I, a subsidiary of the Company, was formed on March 17, 2004 to sell capital securities to the public through a third party trust pool. In accordance with Financial Accounting Standards Board ("FASB") Interpretation No. 46R, "Consolidation of Variable Interest Entities" ("FIN 46R"), the subsidiary has not been included in the consolidated financial statements.

Slade's Ferry Loan Company was dissolved in early 2005.

NOTE C - STOCK BASED COMPENSATION

The Company adopted Statement of Financial Accounting Standards No. 123(R), Share-Based Payment, ("SFAS 123(R)" or the "Statement") effective January 1, 2006 applicable to the Company's stock-based employee compensation plans. The Company's stock-based compensation plans are described in Note 15 to the Company's consolidated financial statements included in its Form 10-K for the year ended December 31, 2005. No changes have been made to the plans during the six months ended June 30, 2006. In accordance with SFAS No. 123(R), for the six months ended June 30, 2006, the Company has expensed, on a straight line basis, the previously unrecognized compensation costs related to the non-vested portion of awards granted and outstanding as of January 1, 2006 based on the grant-date fair value of those awards as calculated under the original provisions of Statement No. 123. Fair value has been determined using Black-Scholes option-pricing

model. Compensation costs are now being recognized over the period the employee is required to provide services to obtain the award. The impact of adopting SFAS No. 123(R) was a reduction of income before income taxes of $136,000 and a reduction of net income by $98,000 for the six months ended June 30, 2006. Basic and diluted earnings per share were reduced by $0.02 and $0.03 per share, respectively. The impact of adopting SFAS No. 123(R) was a reduction of income before income taxes of $70,000 and a reduction of net income of $51,000 for the three months ended June 30, 2006. Basic and diluted earnings per share were reduced by $0.01 per share.

Prior to the adoption of SFAS No. 123(R), the Company accounted for the plans under the recognition and measurement principles of Accounting Principle Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and related Interpretations. Accordingly, no stock-based employee compensation cost was reflected in net income, as all options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

A summary of the status of the Company's stock option plans (shares in thousands) are presented below:

Options	Shares Available for Grant	Stock Options Outstanding Shares	Weighted-Average Exercise Price
Balance at December 31, 2005	164	255	$15.92
Granted	(8)	8	18.40
Stock options exercised	-	(28)	10.89
Shares vested	-	-	-
Forfeited or expired	-	(4)	14.18
Balance at June 30, 2006	156	231	

The weighted-average grant-date fair value of options granted during the six months ended June 30, 2006 was $18.40. The total intrinsic value of options exercised during the six months ended June 30, 2006 was $325,000.

A summary of options outstanding (shares in thousands) at June 30, 2006 is as follows:

	Stock Options Outstanding	Stock Options Exercisable
Total number of shares	231	203
Weighted average exercise price	$ 18.18	$ 18.03
Aggregate intrinsic value (in thousands)	$ 4,198	$ 3,360
Weighted average remaining contractual term (in months)	11	11

The fair value of each option award is estimated on the date of grant based on a number of factors including volatilities, dividends, and expected terms. Listed below is a summary of the factors we employed:

	June 30, 2006
Expected volatility	24% - 33%
Weighted-average volatility	29%
Expected dividends	1.90%
Expected term (in years)	5 - 10
Risk-free rate	3.98% - 5.22%

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") Statement No. 123(R), "Accounting for Stock-Based Compensation," to stock-based employee compensation for the three and six months ended June 30, 2005.

[OBJECT OMITTED]]

		Three Months Ended June 30, 2005	Six Months Ende June 30, 2005
		(In thousands, except per share data)	
Net income, as reported		$ 848	$1,948
Deduct: stock-based employee compensation expense determined under fair value method, net of related tax effects		26	63
Net income, pro forma		$ 822	$1,885
Earnings per share - basic	As reported	$0.21	$0.48
	Pro forma	$0.20	$0.46
Earnings per share - assuming dilution	As reported	$0.21	$0.47
	Pro forma	$0.20	$0.46

NOTE D - PENSION PLAN

The components of net periodic pension expense (income) are as follows:

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months 2006
		(In thousands)	
Interest cost	$ 16	$ 21	$ 33
Expected return on plan assets	(29)	(37)	(58)
Settlements	133	-	133
Recognized net actuarial loss	8	9	15
Net periodic benefit expense (income)	$128	$ (7)	$123

The Company previously disclosed in its consolidated financial statements for the year ended December 31, 2005 that it expects to make no contributions to the plan in 2006.

ITEM 2

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Slade's Ferry Bancorp., a Massachusetts corporation, is a bank holding company headquartered in Somerset, Massachusetts with consolidated assets of $605.4 million, consolidated net loans and leases of $426.7 million, consolidated deposits of $430.1 million and consolidated shareholders' equity of $49.8 million as of June 30, 2006. We conduct our business principally through our wholly-owned subsidiary, Slade's Ferry Trust Company (referred to herein as the "Bank"), a Massachusetts-chartered trust company. Our common stock is quoted on the Nasdaq Capital Market under the symbol "SFBC."

FORWARD-LOOKING STATEMENTS

This Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including statements regarding the strength of the company's capital and asset quality. Such statements may be identified by words such as "believes," "will," "expects," "project," "may," "could," "developments," "strategic," "launching," "opportunities," "anticipates," "estimates," "intends," "plans," "targets" and similar expressions. These statements are based upon the current beliefs and expectations of Slade's Ferry Bancorp.'s management and are subject to significant risks and uncertainties. Actual results may differ materially from those set forth in the forward-looking statements as a result of numerous factors.

The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in our forward-looking statements:

(1) enactment of adverse government regulation;
(2) competitive pressures among depository and other financial institutions may increase significantly and have an effect on pricing, spending, third-party relationships and revenues;
(3) the strength of the United States economy in general and specifically the strength of the New England economies may be different than expected, resulting in, among other things, a deterioration in overall credit quality and borrowers' ability to service and repay loans, or a reduced demand for credit, including the resultant effect on the our loan portfolio, levels of charge-offs and non-performing loans and allowance for loan losses;
(4) changes in the interest rate environment may reduce interest margins and adversely impact net interest income; and
(5) changes in assumptions used in making such forward-looking statements.

Should one or more of these risks materialize or should underlying beliefs or assumptions prove incorrect, Slade's Ferry Bancorp.'s actual results could differ materially from those discussed.

All subsequent written and oral forward-looking statements attributable to Slade's Ferry Bancorp. or any person acting on its behalf are expressly qualified in their entirety by the cautionary statements set forth above. Slade's Ferry Bancorp. does not intend or undertake any obligation to update any forward-looking statement to reflect circumstances or events that occur after the date the forward-looking statements are made.

As used throughout this report, the terms "we," "our," "us," or the "Company" refer to Slade's Ferry Bancorp. and its consolidated subsidiary, unless the context otherwise requires.

CRITICAL ACCOUNTING POLICIES

Our significant accounting policies are incorporated by reference to Note 1 to our Consolidated Financial Statements filed within Form 10-K for the year ended December 31, 2005. In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and other-than-temporary impairment losses.

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.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

Other than temporary impairment. In estimating other-than-temporary-impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

COMPARISON OF FINANCIAL CONDITION AT JUNE 30, 2006 AND DECEMBER 31, 2005

GENERAL

Total assets increased by $19.5 million, or 3.3%, from $585.9 million at December 31, 2005 to $605.4 million at June 30, 2006. Total net loans increased by $17.1 million, or 4.2%, from $409.6 million to $426.7 million. Deposits increased by $14.2 million, or 3.4%, from $415.8 million to $430.1 million. The increase in deposits was partially offset by a decrease in Federal Home Loan Bank advances of $4.8 million.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents increased by $9.5 million, from $20.0 million at December 31, 2005 to $29.5 million at June 30, 2006. This increase was due primarily to uninvested proceeds from an investment exchange at June 30, 2006 (see "Investment Portfolio", below).

INVESTMENT PORTFOLIO

The main objectives of our investment portfolio are to achieve a competitive rate of return over a reasonable time period and to provide liquidity.

Our total investment portfolio decreased from $129.9 million at December 31, 2005 to $122.3 million at June 30, 2006, a decrease of 5.9%. The decrease is the result of sales, maturities, calls and paydowns of certain state and municipal obligations and mortgage-backed securities. Those funds were used to provide liquidity for current loan growth.

An overriding investment strategy is to allow the investment portfolio to decrease through normal paydowns and maturities and reinvest these funds into higher yielding loans or investments. At June 30, 2006, the portfolio duration was approximately 3.1 years which was within our investment policy limit of 5 years. We do not purchase investments with imbedded derivative characteristics, or free-standing derivative instruments such as swaps, options, or futures.

SECURITIES AVAILABLE FOR SALE

Securities not designated as held-to-maturity are designated as available for sale. Although we do not anticipate the sale of these securities, the designation as available for sale allows the flexibility to alter the investment strategy and sell these securities when conditions warrant. Additionally, marketable equity securities that have no maturity date must be designated as available-for-sale. These securities are carried at fair value. The available-for-sale securities portfolio includes obligations and mortgage-backed securities of government-sponsored enterprises, corporate debt and equity securities. Available-for-sale securities decreased from $94.3 million at December 31, 2005 to $88.7 million at June 30, 2006.

On June 20, 2006, the Board of Directors approved a strategy to restructure the available-for-sale investment portfolio through the sale of approximately $14.5 million of low-yielding obligations of government-sponsored enterprises. Realized losses amounted to $176,000 or 1.2% of the underlying cost basis of these securities. All purchases and sales relating to this reinvestment strategy were reflected in the financial statements as of June 30, 2006.

The following table shows the amortized cost basis and fair value of securities available for sale at June 30, 2006 and December 31, 2005.

	June 30, 2006		December 31, 2005	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
Debt Securities:				
Government-sponsored enterprises	$34,450	$33,504	$50,443	$49,581
Corporate	9,517	9,057	9,564	9,014
Mortgage-backed	42,640	41,867	31,574	31,232

Total debt securities	86,607	84,428	91,581	89,827
Marketable equity securities	3,306	3,151	3,426	3,271
Mutual funds	1,215	1,165	1,205	1,200
Total securities available for sale	$91,128	$88,744	$96,212	$94,298

SECURITIES HELD TO MATURITY

The held-to-maturity portfolio consists of mortgage-backed securities and securities issued by states and municipalities. These securities are carried at amortized cost. Held-to-maturity securities decreased from $29.3 million at December 31, 2005 to $27.2 million at June 30, 2006. Management has designated these mortgage-backed securities to secure advances from the FHLB. We have the positive intent and ability to hold these securities to maturity.

The following table shows the amortized cost basis and fair value of securities held to maturity at June 30, 2006 and December 31, 2005.

	June 30, 2006		December 31, 2005	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In thousands)			
State and municipal obligations	$ 6,098	$ 6,164	$ 6,766	$ 6,892
Mortgage-backed securities	21,137	20,111	22,540	21,966
Total securities held to maturity	$27,235	$26,275	$29,306	$28,858

LOANS

Our loan portfolio consists primarily of residential and commercial real estate loans, construction and land development loans, commercial loans, home equity lines of credit and consumer loans originated primarily in our market area. There are no foreign loans outstanding. Interest rates charged on loans are affected principally by the demand for such loans, the supply of money available for lending purposes and the rates offered by the our competitors. Total net loans were 70.5% of total assets at June 30, 2006, as compared to 69.9% of total assets at December 31, 2005.

MULTI-FAMILY AND COMMERCIAL REAL ESTATE LENDING

We originate multi-family and commercial real estate loans that are generally secured by five or more unit apartment buildings and properties used for business purposes, such as small office buildings, restaurants or retail facilities. Loans secured by multi-family and commercial real estate properties generally involve larger principal amounts and a greater degree of risk than one-to-four family residential mortgage loans. Because payments on loans secured by multi-family and commercial real estate properties are often dependent on successful operation or management of the properties, repayment of such loans may be subject to adverse conditions in the real estate market or the economy. We seek to minimize these risks through our underwriting standards.

Multi-family and commercial real estate loans totaled $211.3 million and comprised 49.0% of the total gross loan portfolio at June 30, 2006. At December 31, 2005, the multi-family and commercial real estate loan portfolio totaled $213.8 million, or 51.6% of total gross loans.

RESIDENTIAL LENDING

We currently offer fixed-rate, one-to-four family mortgage loans with terms from 10 to 30 years and a number of adjustable-rate mortgage ("ARM") loans with terms of up to 30 years and interest rates that adjust every one or three years from the outset of the loan.

We generally underwrite our residential real estate loans to comply with secondary market standards established by the Federal National Mortgage Association. Although loans are underwritten to standards that make them readily saleable, we have not chosen to sell these loans. Rather, we maintain them in our portfolio, consistent with our income and interest rate risk management targets.

Residential real estate loans totaled $127.0 million and comprised 29.4% of the total gross loan portfolio at June 30, 2006. At December 31, 2005, the residential real estate loan portfolio totaled $120.3 million, or 29.1% of total gross loans. Due to competitive pricing, our residential loan portfolio continues to increase.

COMMERCIAL LOANS

Commercial business loans consist of loans and lines predominantly collateralized by inventory, furniture and fixtures, and accounts receivable. In assessing the collateral for this type of loan, we apply a 50% liquidation value to inventories; 25% to furniture, fixtures and equipment; and 70% to accounts receivable less than 90 days of the invoice date.

Commercial loans totaled $50.0 million and comprised 11.6% of the total gross loan portfolio at June 30, 2006. At December 31, 2005, the commercial loan portfolio totaled $38.1 million, or 9.2% of total gross loans. With the implementation of our loan portfolio management team, our commercial loan officers are able to concentrate their efforts on this aspect of business development.

CONSTRUCTION LENDING

Fixed-rate construction loans are originated for the development of one-to-four family residential properties. Although we do not generally make loans secured by raw land, our policies permit the origination of such loans. Construction loan proceeds are disbursed periodically in increments as construction progresses and as inspections by an independent construction specialist warrant.

Construction and land development loans totaled $23.3 million and comprised 5.4% of total gross loan portfolio at June 30, 2006. At December 31, 2005, the construction and land development loans totaled $21.5 million or 5.2% of total gross loans. Again with the implementation of our loan portfolio management team, our commercial loan officers are able to manage their efforts on business development.

HOME EQUITY LINES OF CREDIT

Home equity lines of credit are secured by second mortgages on owner-occupied, one-to-four family residences located in our primary market area. Interest rates on our home equity lines of credit are generally indexed to the Wall Street Journal Prime Rate and adjust on a monthly basis.

Home equity lines of credit totaled $17.1 million and comprised 4.0% of the total gross loan portfolio at June 30, 2006. At December 31, 2005, home equity lines of credit totaled $17.9 million, or 4.3% of total gross loans.

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CONSUMER LENDING

Consumer loans secured by rapidly depreciable assets such as recreational vehicles and automobiles entail greater risks than one-to-four family residential mortgage loans. Consumer loans are typically made based on the borrower's ability to repay the loan through continued financial stability. We endeavor to minimize risk by reviewing the borrower's repayment history on past debts, and assessing the borrower's ability to meet existing obligations on the proposed loan. Consumer loans are both secured and unsecured borrowings. Consumer loans totaled $2.7 million and comprised 0.6% of the total gross loan portfolio at June 30, 2006. At December 31, 2005, the consumer loans totaled $2.6 million, or 0.6% of total gross loans.

The following table summarizes our loan portfolio by category at June 30, 2006 and December 31, 2005.

	June 30, 2006	December 31, 2005	Perc Increase
	(Dollars in thousands)		
Real estate mortgage loans:			
Commercial	$211,280	$213,815	-
Residential	126,943	120,345	
Construction and land development	23,359	21,490	
Home equity lines of credit	17,122	17,915	-
Commercial, financial and agricultural	50,015	38,111	3
Consumer loans	2,671	2,623	
Total loans	431,390	414,299	
Less: Allowance for loan losses	(4,366)	(4,333)	
Net deferred loan fees	(346)	(356)	-
Loans, net	$426,678	$409,610	

The increases in the loan portfolio are the result of the continued demand by small businesses for commercial and industrial loans and the normal origination process for residential loans. These increases were partially offset by a weaker overall general market environment relating to commercial real estate and home equity lines of credit.

The following table presents information with respect to non-performing loans at the dates indicated.

	At June 30, 2006	At Decembe
	(Dollars in thousands	
Non-accrual loans	$ 441	$
Loans 90 days or more past due and still accruing	-	
Total non-performing loans	$ 441	$
Percentage of non-accrual loans to total loans	0.10%	0
Percentage of allowance for loan losses to non-accrual loans	990.02%	478

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The $441,000 in non-accrual loans as of June 30, 2006 consists of $402,000 of commercial real estate loans, $34,000 of residential real estate loans and $5,000 of consumer loans. There were no restructured or impaired loans included in non-accrual loans for the six months ended June 30, 2006.

It is our policy to manage our loan portfolio in order to recognize problem loans at an early stage and thereby minimize loan losses. Loans are considered delinquent when any payment of principal or interest is one month or more past due. We generally commence collection procedures when accounts are 15 days past due. Generally, when a loan becomes past due 90 days or more, management discontinues the accrual of interest and reverses previously accrued interest, unless the credit is well-secured and in process of collection. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. When a loan, or any portion of a loan, is determined to be uncollectible, it is charged off to the Allowance for Loan Losses. If applicable, any real estate securing the loan is acquired through foreclosure, and recorded as Other Real Estate Owned at the then fair market value, and thereby reducing the amount required to be charged against the Allowance for Loan Losses.

Management defines non-performing loans to include non-accrual loans, loans past due 90 days or more and still accruing, and restructured loans not performing in accordance with amended terms.

Statement of Financial Accounting Standards No. 114 "Accounting by Creditors for Impairment of a Loan" ("SFAS No. 114") applies to all loans except large groups of smaller-balance homogeneous loans that are collectively evaluated for impairment. For loans that are classified as impaired an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loans is lower than the carrying value of that loan. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. We do not separately identify consumer loans for impairment disclosures. A loan is considered impaired when, based on current information and events, it is probable that we will be unable to collect the scheduled payments of principle or interest when due according to the contractual terms of the loan agreement.

ANALYSIS OF ALLOWANCE FOR LOAN LOSSES

The table below illustrates the changes in the Allowance for Loan Losses for the periods indicated.

	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005
	(Dollars in thousands)	
Balance at beginning of period	$4,333	$4,101
Charge-offs:		
Real estate mortgage loans:		
Commercial	-	-
Residential	-	-
Home equity lines of credit	-	-
Commercial, financial and agricultural loans	-	-
Consumer	6	-
	6	-
Recoveries:		
Real estate mortgage loans:		
Commercial	-	-
Residential	-	-
Home equity lines of credit	-	16
Commercial, financial and agricultural loans	-	32
Consumer	-	9
	-	57
Net loan recoveries (charge-offs)	(6)	57
Provision for loan losses	39	65
Balance at end of period	$4,366	$4,223
Allowance for loan losses as a percent of loans	1.02%	1.08%
Ratio of net loan recoveries (charge-offs) to average loans outstanding	0.00%	-0.01%

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific, general and unallocated components. For such loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

As the composition of the loan portfolio gradually changes and diversifies from higher credit risk weighted loans, such as commercial real estate and commercial, to residential and home equity loans, a lower overall reserve allowance rate will be required. After thorough review and analysis of the adequacy of the loan loss allowance, management determined a provision for losses of $39,000 was required for the six months ended June 30, 2006 as compared to a provision of $65,000 for the six months ended June 30, 2005. The allowance for loan losses as a percentage of total loans outstanding declined from 1.05% at December 31, 2005 to 1.01% at June 30, 2006. The decline in the provision for loan losses in 2006, as compared to the same period in 2005, was primarily attributable to refinements in calculating the risk components inherent in our loan portfolio. These refinements in the allocated risk factors attributable to all loan pools were finalized in the second quarter of 2006.

This table below shows an allocation of the allowance for loan losses at the dates indicated. The unallocated portion of the allowance for loan losses is reflected in the allocation for real estate mortgage loans.

	June 30, 2006		December 31,	
	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percen in Eac to To
	(Dollars in thousands)			
Commercial	$ 775	11.6%	$ 905	
Real estate construction	247	5.4%	248	
Real estate mortgage	3,157	82.4%	3,056	
Consumer	187	0.6%	124	
	$4,366	100.0%	$4,333	

DEPOSITS

We continue our efforts to competitively price deposit products and develop and maintain relationship banking with our customers. The flow of deposits is influenced significantly by general economic conditions, changes in money market rates, prevailing interest rates and competition from local branches of nationwide and regional banks as well as local banks and credit unions. Our total deposits increased from $415.8 million at December 31, 2005 to $430.1 million at June 30, 2006, an increase of $14.2 million or 3.4%. The increase in total deposits was primarily attributable to increases in term deposits. A $10.0 million certificate of deposit from the Commonwealth of Massachusetts that is to be used to assist in promoting job growth through loans to qualifying small businesses, and other reinvestments from lower-yielding deposit products made up the majority of this increase.

The following table presents deposits by category at June 30, 2006 and December 31, 2005.

	June 30, 2006	December 31, 2005	Percenta Increase/(De
	(Dollars in thousands)		
Demand deposits	$ 80,710	$ 80,705	0.01%
NOW	53,118	55,493	-4.28%
Regular and other savings	82,288	87,146	-5.57%
Money market deposits	27,595	29,835	-7.51%
Total non-certificate accounts	243,711	253,179	-3.74%
Term certificates less than $100,000	120,723	116,861	3.30%
Term certificates of $100,000 or more	65,634	45,806	43.29%
Total certificate accounts	186,357	162,667	14.56%
Total deposits	$430,068	$415,846	3.42%

BORROWINGS

Short- and long-term advances from the Federal Home Loan Bank of Boston totaling $103.0 million at June 30, 2006, as compared to $107.9 million at December 31, 2005, a decrease of $4.8 million or 4.5%. Our strategy is to utilize advances from the Federal Home Loan Bank in conjunction with the investment portfolio runoffs to fund loans as required. There was no change in the balance of our subordinated debentures.

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COMPARISON OF RESULTS OF OPERATIONS FOR THE SIX MONTHS ENDED

JUNE 30, 2006 AND 2005

GENERAL

Net income decreased from $1.9 million or $0.47 per share on a diluted basis, for the six months ended June 30, 2005 to $1.5 million or $0.37 per share on a diluted basis, for the six months ended June 30, 2006, a decrease of 21.30%. Net interest and dividend income increased by $86,000 or 1.00%, from $8.9 million to $9.0 million when comparing the six months ended June 30, 2005 and 2006. Over the same period, the provision for loan losses decreased from $65,000 to $39,000. Non-interest income increased by $140,000 or 12.62% from $1.1 million to $1.2 million for the six months ended June 30, 2005 and 2006. Non-interest expenses increased by $765,000 or 11.03%, from $6.9 million for the six months ended June 30, 2005 to $7.7 million for the six months ended June 30, 2006.

INTEREST INCOME

Our operating performance is dependent on net interest and dividend income, the difference between interest and dividend income earned on loans and investments and interest expense paid on deposits and borrowed funds. The level of net interest income and dividend income is significantly impacted by factors such as economic conditions, interest rates, asset/liability management, and strategic planning.

Interest and dividend income increased by $2.1 million or 15.40%, to $15.9 million for the six months ended June 30, 2006 from $13.8 million for the six months ended June 30, 2005. This increase is attributable to the growth in the loan portfolio and higher yields on loans. The average balance of loans increased by $35.5 million or 9.23% and the yield on the loan portfolio increased from 5.76% for the six months ended June 30, 2005 to 6.30% for the six months ended June 30, 2006. The increase was principally the result of a greater volume and higher rates earned on commercial and real estate loans reflecting current market conditions. Interest and dividends on investments decreased by $29,000, on a fully taxable equivalent basis, for the six months ended June 30, 2006 compared to the six months ended June 30, 2005, respectively. The decrease was due to a combination of higher rates and reduced average balances, and the lack of a second quarter dividend declaration by the Federal Home Loan Bank of Boston. Based on preliminary information from the Federal Home Loan Bank, it is expected that this dividend will be declared in the third quarter of 2006.

INTEREST EXPENSE

Total interest expense increased by $2.0 million or 41.58%, from $4.9 million for the six months ended June 30, 2005 to $6.9 million for the six months ended June 30, 2006. Market interest rates and our own deposit rates have also increased. Interest on deposits increased by $1.6 million or 59.29% when comparing the six months ended June 30, 2006 and 2005. In response to competitive pressures and the rising rate environment, we raised rates on certain deposit products with the most significant increases in certificate of deposit and certain money-market based products. As a result of the rate increases, the weighted average cost of deposits increased from 1.66% for the six months ended June 30, 2005 to 2.49% for the six months ended June 30, 2006. Interest expense associated with the Federal Home Loan Borrowings increased by $380,000 due to a combination of rate increases and volume increases related to the need to fund loan growth. Interest expense associated with subordinated debentures increased by $103,000, the result of increased market interest rates. The debentures carry an adjustable rate of interest tied to the three-month LIBOR rate.

NET INTEREST MARGIN

As a result of the current interest rate environment and our corresponding rate increases on deposit accounts, the net interest margin has compressed 15 basis points from 3.46% for the six months ended June 30, 2005 to 3.31% at June 30, 2006. The compression in net interest margin was mostly due to the rise in short term rates and the prolonged flatness of the yield curve, which has reduced the gap between short and intermediate-term interest rates and the spread between what banks earn on loans and securities and pay on deposits and borrowings.

PROVISION FOR LOAN LOSSES

After thorough review and analysis of the adequacy of the loan loss reserve, management deemed it prudent to provide $39,000 for possible loan losses for the six months ended June 30, 2006 compared to $65,000 for possible loan losses for the six months ended June 30, 2005. The decline in the provision for loan losses in 2006 was attributable to continued improvements in the overall loan quality, combined with the refinements made in the allocated risk factors attributable to all components of our loan portfolio, during the six months ended June 30, 2006, as compared to the same period in 2005.

The following table sets forth our average assets, liabilities, and stockholders' equity, interest income earned and interest paid, average rates earned and paid, net interest spread and the net interest margin for the six months ended June 30, 2006 and 2005. Average balances reported are daily averages.

	Six Months Ended June 30,			
	2006			
	Average Balance	Interest Income/Expense	Average Rate	Average Balance
Assets:			(Dollars in thousands)	
Interest earning assets (2)				
Loans:				
Commercial	$ 44,416	$ 1,658	7.53%	$ 30,272
Commercial real estate	228,745	7,319	6.45%	220,402
Residential real estate	144,352	4,066	5.68%	131,579
Consumer	2,557	77	6.07%	2,312
Total loans	420,070	13,120	6.30%	384,565
Federal funds sold	2,738	64	4.71%	12,606
Taxable debt securities	109,752	2,394	4.40%	106,927
Tax-exempt debt securities (1)	6,260	208	6.69%	8,127
Marketable equity securities	4,355	74	3.43%	4,809
FHLB stock	6,304	82	2.62%	5,485

Other investments	650	18	5.58%	775
Total interest earning assets	550,129	15,960	5.85%	523,294
Allowance for loan losses	(4,358)			(4,163)
Deferred loan fees	(330)			(401)
Cash and due from banks	12,951			18,311
Other assets	26,229			25,575
	$584,621			$562,616
Liabilities and Stockholders' Equity:				
Interest bearing liabilities				
Savings accounts	$ 83,637	$ 529	1.28%	$ 91,619
NOW accounts	56,715	361	1.28%	48,242
Money market accounts	26,898	258	1.93%	37,311
Time deposits	169,791	3,019	3.59%	141,333
FHLB advances	110,998	2,365	4.30%	104,460
Subordinated debt	10,310	394	7.71%	10,310
Total interest bearing liabilities	458,349	6,926	3.05%	433,275
Demand deposits	73,868			79,334
Other liabilities	842			2,594
Total liabilities	533,059			515,203
Total stockholders' equity	51,562			47,413
	$584,621			$562,616
Net interest income		$ 9,034		
Net interest spread			2.80%	
Net interest margin			3.31%	

(1) On a fully taxable basis based on tax rate of 35.0% for 2006 and 2005. Interest income on in income includes a fully taxable equivalent adjustment of $74,000 in 2006 and $96,000 in 2005

(2) Average balance includes non-accruing loans. The effect of including such loans, although no the average rate earned on the Company's loans.

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The following table presents the changes in components of net interest income for the six months ended June 30, 2006 and 2005, which are the result of changes in interest rates and the changes that the result of changes in volume of the underlying asset or liability. Changes that are attributable to the changes in both rate and volume have been allocated equally to rate and volume.

	Six Months Ended June 30, 2006 vs. 2005 Increase (Decrease)		
	Total Change	Due to Volume	Due to Rate
	(In thousands)		
Commercial loans	$ 751	$ 492	$ 259
Commercial real estate	758	255	503

Residential real estate	609	349	260
Consumer loans	9	7	2
Federal funds sold	(93)	(177)	84
Taxable debt securities	159	60	99
Tax-exempt debt securities	(63)	(62)	(1)
Marketable equity securities	(9)	(8)	(1)
FHLB Stock	(30)	14	(44)
Other investments	7	(3)	10
Total interest income	2,098	927	1,171
Savings accounts	61	(46)	107
NOW accounts	130	45	85
Money market accounts	40	(80)	120
Time deposits	1,320	391	929
FHLB advances	380	129	251
Subordinated debt	103	-	103
Total interest expense	2,034	439	1,595
Net interest income	$ 64	$ 488	$ (424)

NON-INTEREST INCOME

Non-interest income increased from $1.1 million for the six months ended June 30, 2005 to $1.2 million for the six months ended June 30, 2006, an increase of $140,000 or 12.6%. Service charges on deposit accounts increased by $239,000 or 56.9% from $420,000 for the six months ended June 30, 2005 to $659,000 for the six months ended June 30, 2006. This was the result of an increase in overdraft fees with the implementation of an overdraft protection program partially offset by a decrease in service charges on checking accounts. For the six months ended June 30, 2006, and in accordance with the previously-mentioned investment portfolio restructuring strategy, we recognized losses on the sale of securities, including certain low-yielding investments in order to acquire higher yielding assets, in the amount of $169,000 when compared to a gain of $17,000 for the six months ended June 30, 2005. Cash surrender value increases pertaining to bank-owned life insurance policies decreased $45,000 to $213,000 for the six months ended June 30, 2006 from $258,000 for the six months ended June 30, 2005. Additionally, other income increased from $363,000 for the six months ended June 30, 2005 to $546,000 for the six months ended June 30, 2006, primarily as a result of increased commissions earned on the sale of non-deposit investment products, combined with increased volumes in official check fees and debit card income.

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NON-INTEREST EXPENSE

Non-interest expense increased from $6.9 million for the six months ended June 30, 2005 to $7.7 million for the six months ended June 30, 2006, an increase of $765,000 or 11.0%. Salaries and employee benefits increased by $303,000 or 7.4%, from $4.1 million for the six months ended June 30, 2005 to $4.4 million for the six months ended June 30, 2006. The increase in salaries and benefits includes the adoption of SFAS 123(R) effective January 1, 2006 applicable to the Company's stock-based employee compensation plan which resulted in the recognition of $136,000 in expense, and settlement accounting recognized on the Bank's defined benefit pension plan totaling $133,000. Occupancy and equipment expense for the six months ended June 30, 2006 increased $174,000 to $983,000 as compared to $809,000 for the six months ended June 30, 2005. The increase was the result of additional depreciation expense incurred from both the Assonet branch that was opened April 2005 and the upgrade in software associated with the modernization of teller and platform systems. Professional fees increased $186,000 due primarily to the outsourcing of our internal audit function commencing January 1, 2006 and consultations regarding accounting and regulatory matters. Marketing expense decreased $141,000 to $187,000 for the six months ended June 30, 2006 from $328,000 for the six months ended June 30, 2005 which is attributable to the timing of certain advertising and community sponsorship initiatives in 2006. Other expense increased $243,000 or 22.3% from $1.1 million for the six months ended June 30, 2005 to $1.3 million for the six months ended June 30, 2006. This increase was due to the increased volume of internet banking and cash management fees, increased postage cost, the outsourcing of our courier service, and the increase of meetings and committee fees for two additional Board members when compared to June 30, 2005.

PROVISION FOR INCOME TAXES

Income before income taxes was $3.0 million for the six months ended June 30, 2005 as compared to $2.5 million for the six months ended June 30, 2006. Provision for income taxes totaled $1.0 million and $935,000 for the six months ended June 30, 2005 and 2006, respectively, representing effective tax rates of 34.65% and 37.88%, respectively. The increase in the overall tax rate was due to a decline in income for the Bank's subsidiaries which are taxed at a lower state tax rate, a decline in federally exempt municipal income and a decrease in cash surrender value of life insurance, which is tax-exempt income, recognized in the six months ended June 30, 2006 compared to 2005.

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COMPARISON OF RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED JUNE 30, 2006 AND 2005

GENERAL

Net income decreased from $848,000 or $0.21 per share on a diluted basis, for the three months ended June 30, 2005 to $626,000 or $0.15 per share on a diluted basis, for the three months ended June 30, 2006, a decrease of 26.2%. Net interest and dividend income remained stable when comparing the three months ended June 30, 2005 and 2006. The provision for loan losses decreased by $15,000 for the three months ended June 30, 2006. Non-interest income increased by $6,000 or 1.1% from $540,000 to $546,000 for the three months ended June 30, 2005 and 2006. Non-interest expense increased by $330,000 or 9.1%, from $3.6 million for the three months ended June 30, 2005 to $4.0 million for the three months ended June 30, 2006.

INTEREST INCOME

Our operating performance is dependent on net interest and dividend income, the difference between interest and dividend income earned on loans and investments and interest expense paid on deposits and borrowed funds. The level of net interest income and dividend income is significantly impacted by factors such as economic conditions, interest rates, asset/liability management, and strategic planning.

Interest and dividend income increased by $921,000 or 13.0%, from $7.1 million for the three months ended June 30, 2005 to $8.0 million for the three months ended June 30, 2006. This increase can be attributed to both the growth in the loan portfolio as well as an increase in yields on loans. The average balance of loans increased by $29.6 million or 7.52% and an increase in yield on the loan portfolio from 5.84% for the three months ended June 30, 2005 to 6.34% for the three months ended June 30, 2006. The increase was the result of a greater volume and higher rates earned on commercial and real estate loans reflecting current market conditions. Interest and dividends on investments decreased by $45,000, on a fully taxable equivalent basis, for the three months ended June 30, 2006 compared to the three months ended June 30, 2005. The decrease was due to a combination of higher rates off set by a reduction in average balances, and the lack of a second quarter dividend declaration by the Federal Home Loan Bank of Boston. Preliminary indications from the Federal Home Loan Bank are that this dividend will be declared in the third quarter of 2006.

INTEREST EXPENSE

Total interest expense increased by $949,000 or 35.33%, from $2.7 million for the three months ended June 30, 2005 to $3.6 million for the three months ended June 30, 2006. In response to competitive pressures and the rising rate environment, we raised rates on certain deposit products with the most significant increases in certificate of deposit and certain money-market based products. As a result of the rate increases, the weighted average cost of deposits increased from 1.82% for the three months ended June 30, 2005 to 2.65% for the three months ended June 30, 2006. The interest expense on Federal Home Loan Bank borrowings increased $135,000 during this same time period due primarily to associated rate increases. Interest expense associated with subordinated debentures increased by $15,000, the result of increased market interest rates. The debentures carry an adjustable rate of interest tied to the three-month LIBOR rate.

NET INTEREST MARGIN

As a result of the current interest rate environment and our corresponding rate increases on deposit accounts, the net interest margin has compressed 14 basis points from 3.36% for the three months ended June 30, 2005 to 3.22% at June 30, 2006. The compression in net interest margin was mostly due to the rise in short term rates and the prolonged flatness of the yield curve, which has reduced the gap between short and intermediate-term interest rates and the spread between what banks earn on loans and securities and pay on deposits and borrowings.

PROVISION FOR LOAN LOSSES

After thorough review and analysis of the adequacy of the loan loss reserve, management deemed it prudent to provide no provision for possible loan losses for the three months ended June 30, 2006 compared to $15,000 for possible loan losses for the three months ended June 30, 2005. The decline in the provision for loan losses in 2006 was attributable to continued improvements in the overall loan quality, combined with refinements made in the allocated risk factors attributable to all components of our loan portfolio, during the three months ended June 30, 2006, as compared to the same period in 2005.

The following table sets forth our average assets, liabilities, and stockholders' equity, interest income earned and interest paid, average rates earned and paid, net interest spread and the net interest margin for the three months ended June 30, 2006 and 2005. Average balances reported are daily averages.

	Three Months Ended June 30,			
	2006			
	Average Balance	Interest Income/Expense	Average Rate	Average Balance
	(Dollars in thousands)			
Assets:				
Interest earning assets (2)				
Loans:				
Commercial	$ 46,111	$ 885	7.70%	$ 32,019
Commercial real estate	228,558	3,710	6.51%	224,863
Residential real estate	145,725	2,051	5.65%	134,281
Consumer	2,565	39	6.10%	2,225
Total loans	422,959	6,685	6.34%	393,388
Federal funds sold	4,387	53	4.85%	13,051
Taxable debt securities	108,068	1,182	4.39%	107,093
Tax-exempt debt securities (1)	6,099	102	6.68%	7,787
Marketable equity securities	4,344	35	3.23%	4,653
FHLB stock	6,304	-	0.00%	5,905
Other investments	650	10	6.17%	799
Total interest earning assets	552,811	8,067	5.85%	532,676
Allowance for loan losses	(4,373)			(4,205)
Deferred loan fees	(310)			(486)
Cash and due from banks	13,932			18,115
Other assets	26,432			25,057
	$ 588,492			$ 571,157
Liabilities and Stockholders' Equity:				
Interest bearing liabilities				
Savings accounts	$ 82,199	$ 272	1.33%	$ 93,492
NOW accounts	57,648	188	1.31%	26,789
Money market accounts	25,709	149	2.32%	56,829
Time deposits	175,539	1,647	3.76%	144,393
FHLB advances	110,802	1,209	4.38%	110,118
Subordinated debt	10,310	170	6.61%	10,310
Total interest bearing liabilities	462,207	3,635	3.15%	441,931
Demand deposits	73,494			79,401
Other liabilities	707			2,388

Total liabilities	536,408		523,720
Total stockholders' equity	52,084		47,437
	$ 588,492		$ 571,157

Net interest income	$ 4,432	
Net interest spread		2.70%
Net interest margin		3.22%

(1) On a fully taxable basis based on tax rate of 35.0% for 2006 and 2005. Interest income on in
income includes a fully taxable equivalent adjustment of $37,000 in 2006 and $45,000 in 2005

(2) Average balance includes non-accruing loans. The effect of including such loans, although no
the average rate earned on the Company's loans.

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The following table presents the changes in components of net interest income for the three months ended June 30, 2006 and 2005, which are the result of changes in interest rates and the changes that the result of changes in volume of the underlying asset or liability. Changes that are attributable to the changes in both rate and volume have been allocated equally to rate and volume.

	Three Months Ended June 30, 2006 vs. 2005 Increase (Decrease)		
	Total Change	Due to Volume	Due to Rate
	(In thousands)		
Commercial loans	$ 395	$ 251	$ 144
Commercial real estate	296	57	239
Residential real estate	265	157	108
Consumer loans	3	5	(2)
Federal funds sold	(39)	(83)	44
Taxable debt securities	69	10	59
Tax-exempt debt securities	(28)	(28)	-
Marketable equity securities	12	(2)	14
FHLB Stock	(63)	2	(65)
Other investments	3	(2)	5
Total interest income	913	367	546
Savings accounts	8	(35)	43
NOW accounts	37	137	(100)
Money market accounts	50	(117)	167
Time deposits	704	233	471
FHLB advances	135	7	128
Subordinated debt	15	-	15

Total interest expense	949	225	724
Net interest income	$ (36)	$ 142	$ (178)

NON-INTEREST INCOME

Non-interest income increased from $540,000 for the three months ended June 30, 2005 to $546,000 for the three months ended June 30, 2006, an increase of $6,000 or 1.11%. Increases in service charges on deposit accounts and increases in the volumes of official check fees and debit card income were offset primarily by recognized losses on the sale of securities, including certain low-yielding investments in order to acquire higher yielding assets, in accordance with the previously-mentioned investment portfolio restructuring strategy.

NON-INTEREST EXPENSE

Non-interest expense increased from $3.6 million for the three months ended June 30, 2005 to $4.0 for the three months ended June 30, 2006, an increase of $330,000 or 9.11%. Salaries and employee benefits increased by $167,000 or 7.88%, from $2.1 million for the three months ended June 30, 2005 to $2.3 million for the three months ended June 30, 2006. The increase in salaries and benefits includes the adoption of SFAS 123(R) effective January 1, 2006 applicable to the Company's stock-based employee compensation plan which resulted in the recognition of $71,000 in expense and settlement accounting recognized on the Bank's defined benefit pension plan totaling $133,000, which were partially offset by other reductions in salary expense with associated benefit costs due to outsourcing initiatives. Occupancy and equipment expense for the three months

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ended June 30, 2006 increased $90,000 to $490,000 as compared to $400,000 for the three months ended June 30, 2005. The increase was the result of additional depreciation expense incurred from both the Assonet branch that was opened April 2005 and the upgrade in software associated with the modernization of teller and platform systems. Professional fees increased $81,000 as a result of outsourcing the internal audit function commencing January 1, 2006. Marketing expense decreased $120,000 to $109,000 for the three months ended June 30, 2006 from $229,000 for the three months ended June 30, 2005 which is attributable to the timing of certain advertising and community sponsorship initiatives in 2006. Other expense increased $112,000 or 19.79% from $566,000 for the three months ended June 30, 2005 to $678,000 for the three months ended June 30, 2006. The increase in other expense was due to the recognition of $42,000 of losses due to implementation of an overdraft protection program combined with expenses attributable to the increased volumes of internet banking and cash management fees, postal cost increases, the outsourcing of our courier service, and the increase of meetings and committee fees for two additional Board of Director members when compared to the three months ended June 30, 2005.

PROVISION FOR INCOME TAXES

Income before income taxes was $1.3 million for the three months ended June 30, 2005 as compared to $1.0 million for the three months ended June 30, 2006. Provision for income taxes totaled $478,000 and $363,000 million for the three months ended June 30, 2005 and 2006, respectively, representing effective tax rates of 36.05% and 36.70%, respectively. The increase in the overall tax rate was due to a decline in income for the Bank's subsidiaries which are taxed at a lower state tax rate, a decline in federally exempt municipal income and a decrease in the cash surrender value of life insurance, which is tax-exempt income, recognized in the three months ended 2006 compared to 2005.

LIQUIDITY

Our principal sources of funds are customer deposits, amortization and payoff of existing loan principal, and sales, amortization or maturities of various investment securities. The Bank is a voluntary member of the Federal Home Loan Bank of Boston (the "FHLB") and as such, may take advantage of the FHLB's borrowing programs to enhance liquidity and leverage its favorable capital position. The Bank also may draw on lines of credit at the FHLB or the Federal Reserve Board (the "FRB"), and enter into repurchase or reverse repurchase agreements with authorized brokers. These various sources of liquidity are used to fund withdrawals, new loans, and investments.

Management seeks to promote deposit growth while controlling the cost of funds. Sales-oriented programs to attract new depositors and the cross-selling of various products to its existing customer base are currently in place. Management reviews, on an ongoing basis, possible new products, with particular attention to products and services, which will aid in retaining our base of lower-costing deposits.

Maturities and sales of investment securities provide us with liquidity. Our policy of purchasing shorter-term debt securities reduces market risk in the bond portfolio while providing significant cash flow. For the six months ended June 30, 2006, cash flow from maturities of securities was $7.7 million and the proceeds from sales of securities totaled $15.1 million. In comparison maturities of securities aggregated $10.8 million, and the proceeds from sales of securities aggregated $1.8 million for the six months ended June 30, 2005. Purchases of securities for the six months ended June 30, 2006 totaled $6.4 million without the due to broker amount reflected on the June 30, 2006 balance sheet as compared to $20.8 million at June 30, 2005.

Amortization and pay-offs of the loan portfolio also provide us with significant liquidity. Traditionally, amortization and pay-offs are reinvested into loans.

We have also used borrowed funds as a source of liquidity. At June 30, 2006, the Bank's outstanding borrowings from the Federal Home Loan Bank of Boston were $103.0 million. The Bank has the capacity to borrow in excess of additional $40.0 million at the Federal Home Loan Bank.

Loan originations for the six months ended June 30, 2006 totaled $58.4 million. Commitments to originate loans at June 30, 2006 were $6.5 million, excluding unadvanced construction funds totaling $16.6 million, unadvanced commercial lines of credit totaling $18.2 million and unadvanced home equity lines totaling $16.7 million. Management believes that adequate liquidity is available to fund loan commitments utilizing deposits, loan amortization, maturities of securities, or borrowings.

Liquidity declined marginally during the six months ended June 30, 2006 due primarily to a greater reliance on Federal Home Loan Bank borrowings.

CAPITAL

At June 30, 2006, our total shareholders' equity was $49.8 million, an increase of $993,000 from $48.9 million at December 31, 2005. Additions to shareholders' equity consisted primarily of net income of $1.5 million for the six months ended June 30, 2006. In addition, there were 16,842 shares issued at a value of $302,000, pursuant to our Dividend Reinvestment Program, in lieu of cash dividends or for optional cash contributions. Furthermore, stock option exercises resulted in the issuance of 28,000 shares common stock at a value of $305,000, including a tax benefit compensation expense of $82,000 and stock-based compensation of $136,000. These additions were offset by dividends declared of $749,000, the purchase of treasury stock of $230,000, the contribution of $100,000 to a trust for the purchase of our common stock and an accumulated other comprehensive loss of $286,000.

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In May 2006, the Board authorized the purchase of 50,000 shares of common stock to be held in trust for future restricted stock awards under the 2004 Equity Incentive Plan. The $100,000, which is reflected on our balance sheet as unearned compensation under stockholder's equity has been contributed to the trust to fund the purchase of some of these shares. No shares have been awarded to date.

Under the requirements for Risk Based and Leverage Capital of the federal banking agencies, a minimum level of capital will vary among banks based on safety and soundness of operations. Risk Based Capital ratios are calculated with reference to risk-weighted assets, which include both on and off balance sheet exposure.

In addition to meeting the required levels, the Company's and the Bank's capital ratios met the criteria of the well-capitalized category established by the federal banking agencies at June 30, 2006 and at December 31, 2005. The Tier I Capital leverage ratio and Tier I Capital to risk weighted assets ratio for Slade's Ferry Bancorp are 10.11% and 14.97%, respectively, at June 30, 2006. Slade's Ferry Bancorp's Tier I Capital leverage ratio and Tier I Capital to risk weighted assets ratio at December 31, 2005 were 10.07% and 14.66%, respectively. The Tier I Capital leverage ratio and Tier I Capital to risk weighted assets ratio for the Bank are 8.73% and 12.00%, respectively, at June 30, 2006. The Bank's Tier I Capital leverage ratio and Tier I Capital to risk weighted assets ratio at December 31, 2005 were 8.56% and 12.51%, respectively.

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OFF-BALANCE SHEET ARRANGEMENTS

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

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ITEM 3

QUANTATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We consider interest rate risk to be a significant market risk as it could potentially have an effect on our financial condition and results of operation. The definition of interest rate risk is the exposure of our earnings to adverse movements in interest rates, arising from the differences in the timing of repricing of assets and liabilities; the differences in the various pricing indices inherent in our assets and liabilities; and the effects of overt and embedded options in our assets and liabilities. Our Asset/Liability Committee, comprised of the executive management, is responsible for managing and monitoring interest rate risk, and reviewing with the Board of Directors, at least quarterly, the interest rate risk positions, the impact changes in interest rates would have on net interest income, and the maintenance of interest rate risk exposure within approved guidelines.

The potentially volatile nature of market interest rates requires us to manage interest rate risk on an active and dynamic basis. Our objective is to reduce and control the volatility of net interest income to within tolerance levels established by the Board of Directors, by managing the relationship of interest-earning assets and interest-bearing liabilities. In order to manage this relationship, the Asset/Liability Committee utilizes an income simulation model to measure the net interest income at risk under differing interest rate scenarios. Additionally, the Committee uses Economic Value of Equity ("EVE") analysis to measure the effects of changing interest rates on the market values of rate-sensitive assets and liabilities, taken as a whole. The Board of Directors and management believe that static measures of timing differences, such as "gap analysis", do not accurately assess the levels of interest rate risk inherent in our balance sheet. Gap analysis does not reflect the effects of overt and embedded options on net interest income, given a shift in interest rates, nor does it take into account basis risk, the risk arising from using various different indices on which to base pricing decisions.

The income simulation model currently utilizes a 200 basis point increase and decrease in interest rate shocks. The interest rate movements used assume an instant and parallel change in interest rates and no implementation of any strategic plans are made in response to the change in rates. Prepayment speeds for loans are based on median dealer forecasts for each interest rate scenario.

The Board of Directors has established a risk limit of a 5.00% change in net interest income for each 100 basis point shift in market interest rates. The limit provides an internal tolerance level to control interest rate risk. We are within our policy-mandated risk limit for net interest income at risk.

The following table reflects our estimated exposure as a percentage of net interest income and the change in basis points for the next twelve months, assuming an immediate change in interest rates set forth below:

Rate Change (Basis Points)	Estimated Exposure as a Percentage of Net Interest Income	Change (Basis Points)
+200	-10.90%	(19)
-200	2.77%	6

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Additionally we use the model to estimate the effects of changes in interest rates on our EVE. EVE represents our theoretical market value, given the rate shocks applied in the model. The Board of Directors has established a risk limit for EVE which provides that the EVE will not fall below 6.00%, the FDIC's minimum capital level to be classified as "well capitalized". We are within our risk limit for EVE.

The following table presents the changes in EVE given rate shocks.

Rate Change (Basis Points)	Economic Value of Equity	Change from Flat Rates
Flat	12.97%	N/A
+200	11.55%	-1.42%
-200	13.07%	0.10%

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ITEM 4

CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as of the end of the period covered by this report, the Company carried out an evaluation under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of June 30, 2006 to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding disclosure. In connection with the rules regarding disclosure and control procedures, we intend to continue to review and document our disclosure controls and procedures, including our internal controls and procedures for financial reporting, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that our systems evolve with our business.

(b) Changes in Internal Controls over Financial Reporting

There were no changes in the Company's internal controls over financial reporting identified in connection with the Company's evaluation of its disclosure controls and procedures that occurred during the Company's last fiscal quarter that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

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PART II

OTHER INFORMATION

ITEM 1

LEGAL PROCEEDINGS

None.

ITEM 1A

RISK FACTORS

There have been no material changes to the risk factors that are included in our Annual Report on Form 10-K for the year ended December 31, 2005 that could affect our business, results of operations or financial condition.

ITEM 2

UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

This table provides certain information with respect to our purchase of our common stock during the three months ended June 30, 2006.

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs
April 1, 2006 through April 30, 2006	-	N/A	-
May 1, 2006 through May 31, 2006	6,000 (2)	$ 17.40	-
June 1, 2006 through June 30, 2006	5,000 (2)	$ 17.01	-
Total	11,000	$ 17.22	-

(1) On July 18, 2006 the Company announced a stock repurchase plan pursuant to which the Company to 208,036 shares of its outstanding common stock. The shares shown in this table were not r to this plan.

(2) These shares were purchased privately negotiated sales.

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ITEM 3

DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4

SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Annual Meeting of the Company's Shareholders was held on May 17, 2006 with the following mater being voted upon and with the indicated results:

ELECTION OF DIRECTORS FOR TERMS EXPIRING IN 2009

Votes

Nominee	For	Withheld
Peter G. Collias	3,008,394	30,212
Melvyn A. Holland	2,995,917	42,689
Jean F. MacCormack	3,010,035	28,571
Shaun O'Hearn, Sr.	2,998,389	40,217
Carl Ribeiro	3,011,199	27,407
William J. Sullivan	2,997,201	41,405

ITEM 5

OTHER INFORMATION

None.

ITEM 6

EXHIBITS

Exhibits: See exhibit index.

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.

SLADE'S FERRY BANCORP.
(Registrant)

August 11, 2006	/s/ Mary Lynn D. Lenz
(Date)	Mary Lynn D. Lenz President and Chief Executive Officer
August 11, 2006	/s/ Deborah A. McLaughlin
(Date)	Deborah A. McLaughlin Executive Vice President Chief Financial Officer and Chief Operations Officer

EXHIBIT INDEX

Exhibit No.	Description
3.1	Amended and Restated Articles of Incorporation of Slade's Ferry Bancorp.
3.2	Amended and Restated Bylaws of Slade's Ferry Bancorp.
3.3	Articles of Amendment to the Amended and Restated Articles of Incorporation of Slade's Ferry Bank
10.1	Slade's Ferry Bancorp. 1996 Stock Option Plan, as amended
10.2	Supplemental Executive Retirement Agreement between Slade's Ferry Bancorp. and Manuel J. Tavares
10.3	Form of Director Supplemental Retirement Program Director Agreement, Exhibit 1 thereto (Slade's Ferry Trust Company Director Supplemental Retirement Program Plan) and Endorsement Method Split Dollar Plan Agreement thereunder.
10.4	Form of Directors' Paid-up Insurance Policy (part of the Director Supplemental Retirement Program).
10.5	Supplemental Executive Retirement Agreement between Slade's Ferry Bancorp. and Mary Lynn D. Lenz
10.6	Employment Agreement between Slade's Ferry Bancorp. and Mary Lynn D. Lenz
10.7	Employment Agreement between Slade's Ferry Bancorp. and Deborah A. McLaughlin
10.8	Employment Agreement between Slade's Ferry Bancorp. and Manuel J. Tavares
10.9	Form Change of Control Agreement
10.10	Severance Pay Plan
10.11	Slade's Ferry Bancorp. 2004 Equity Incentive Plan
11.1	Statement Regarding Computation of Per Share Earnings
14.1	Code of Ethics
31.1	Rule 13a-14(a)/15d-14(a) Certification of the CEO
31.2	Rule 13a-14(a)/15d-14(a) Certification of the CFO
32.1	Section 1350 Certification of the CEO
32.2	Section 1350 Certification of the CFO

(1) Incorporated by reference to the Registrant's Registration Statement on Form SB-2 filed with the Commission on April 14, 1997.
(2) Incorporated by reference to the Registrant's Form 8-K filed with the Commission on June 22, 2006.
(3) Incorporated by reference to the Registrant's Form 8-K filed with the Commission on December 21, 2004.
(4) Incorporated by reference to the Registrant's Form 10-Q/A for the quarter ended June 30, 199
(5) Incorporated by reference to the Registrant's Form 10-K/ASB for the fiscal year ended Decemb 31, 1996.
(6) Incorporated by reference to Exhibit 10 to the Registrant's Form 10-Q/A for the quarter ende March 31, 1999.

(7) Incorporated by reference to Exhibit 10 to the Registrant's Form 10-Q/ASB for the quarter en June 30, 1998.

(8) Incorporated by reference to Exhibit 10.10 to the Registrant's Form 10-Q/A for the quarter ended March 31, 2003.
(9) Incorporated by reference to Exhibit 10.11 to the Registrant's Form 10-Q/A for the quarter ended June 30, 2004.
(10) Incorporated by reference to Exhibit 10.7 to the Registrant's Form 10-Q/A for the quarter en September 30, 2004.
(11) Incorporated by reference to Exhibit 10.8 to the Registrant's Form 10-Q/A for the quarter en September 30, 2004.
(12) Incorporated by reference to the Registrant's Form 8-K filed with the Commission on January 2005.
(13) Incorporated by reference to the Registrant's Form 8-K filed with the Commission on January 2005.
(14) Incorporated by reference to Appendix C to the Registrant's Proxy Statement filed on April 9 2004.
(15) Incorporated by reference to the Registrant's Form 10-K for the fiscal year ended December 3 2003.