

CARVER BANCORP INC
Form 10-Q
August 18, 2009

Table of Contents

**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 quarterly period ended June 30, 2009

OR

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

For the transition period from _____ to _____

Commission File Number: 1-13007

CARVER BANCORP, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or Other Jurisdiction of Incorporation or
Organization)

13-3904174

(I.R.S. Employer Identification No.)

75 West 125th Street, New York, New York

(Address of Principal Executive Offices)

10027

(Zip Code)

Registrant's telephone number, including area code: (718) 230-2900

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large Accelerated Filer Accelerated Filer Non-accelerated Filer Smaller Reporting Company

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

Yes No

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

Common Stock, par value \$0.01

2,470,072

Class

Outstanding at August 14, 2009

TABLE OF CONTENTS

	Page
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	
<u>Consolidated Statements of Financial Condition as of June 30, 2009 (unaudited) and March 31, 2009</u>	2
<u>Consolidated Statements of Income for the Three Months Ended June 30, 2009 and 2008 (unaudited)</u>	3
<u>Consolidated Statement of Changes in Stockholders' Equity and Comprehensive Income (Loss) for the Three Months Ended June 30, 2009 (unaudited)</u>	4
<u>Consolidated Statements of Cash Flows for the Three Months Ended June 30, 2009 and 2008 (unaudited)</u>	5
<u>Notes to Consolidated Financial Statements (unaudited)</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	15
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	25
<u>Item 4. Controls and Procedures</u>	25
PART II. OTHER INFORMATION	
<u>Item 1. Legal Proceedings</u>	26
<u>Item 1A. Risk Factors</u>	26
<u>Item 2. Issuer Purchases of Equity Securities</u>	26
<u>Item 3. Defaults Upon Senior Securities</u>	26
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	27
<u>Item 5. Other Information</u>	27
<u>Item 6. Exhibits</u>	27
<u>SIGNATURES</u>	28
<u>Exhibit 11</u>	
<u>Exhibit 31.1</u>	

Exhibit 31.2

Exhibit 32.1

Exhibit 32.2

Table of Contents

CARVER BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(In thousands, except per share data)

	June 30, 2009	March 31, 2009
	(unaudited)	
ASSETS		
Cash and cash equivalents:		
Cash and due from banks	\$ 17,100	\$ 8,251
Money market investments	952	5,090
 Total cash and cash equivalents	 18,052	 13,341
Securities:		
Available-for-sale, at fair value (including pledged as collateral of \$54,237 and \$59,928 at June 30, 2009 and March 31, 2009, respectively)	54,685	59,973
Held-to-maturity, at amortized cost (including pledged as collateral of \$14,087 and \$14,342 at June 30, 2009 and March 31, 2009, respectively; fair value of \$14,244 and \$14,528 at June 30, 2009 and March 31, 2009, respectively)	14,474	14,808
 Total securities	 69,159	 74,781
 Loans held-for-sale	 21,069	 21,105
Loans receivable:		
Real estate mortgage loans	592,611	581,987
Commercial business loans	64,789	57,398
Consumer loans	1,535	1,674
Allowance for loan losses	(7,369)	(7,049)
 Total loans receivable, net	 651,566	 634,010
 Office properties and equipment, net	 14,888	 15,237
Federal Home Loan Bank of New York stock, at cost	4,945	4,174
Bank owned life insurance	9,561	9,481
Accrued interest receivable	3,591	3,697
Core deposit intangibles, net	342	380
Other assets	16,465	15,222
 Total assets	 \$ 809,638	 \$ 791,428
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Deposits	\$ 605,144	\$ 603,416
Advances from the FHLB-New York and other borrowed money	131,110	115,017
Other liabilities	9,005	8,657

Edgar Filing: CARVER BANCORP INC - Form 10-Q

Total liabilities	745,259	727,090
Stockholders' equity:		
Preferred stock (TARP) (par value \$0.01 per share, 2,000,000 shares authorized; 18,980 shares, with a liquidation preference of \$1,000.00 per share, issued and outstanding as of June 30, 2009 and March 31, 2009)	18,980	18,980
Common stock (par value \$0.01 per share: 10,000,000 shares authorized; 2,524,691 shares issued; 2,470,072 and 2,475,037 shares outstanding at June 30, 2009 and March 31, 2009, respectively)	25	25
Additional paid-in capital	24,219	24,214
Retained earnings	22,096	21,898
Unamortized awards of common stock under ESOP Treasury stock, at cost (49,972 and 49,654 shares at June 30, 2009 and March 31, 2009, respectively)	(696)	(760)
Accumulated other comprehensive loss	(245)	(19)
Total stockholders' equity	64,379	64,338
Total liabilities and stockholders' equity	\$ 809,638	\$ 791,428

See accompanying notes to unaudited consolidated financial statements

Table of Contents**CARVER BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME**

(In thousands, except per share data)

(Unaudited)

	Three Months Ended June 30,	
	2009	2008
Interest Income:		
Loans	\$ 9,100	\$ 10,453
Mortgage-backed securities	743	561
Investment securities	60	66
Money market investments	10	39
Total interest income	9,913	11,119
Interest expense:		
Deposits	2,037	4,139
Advances and other borrowed money	986	722
Total interest expense	3,023	4,861
Net interest income	6,890	6,258
Provision for loan losses	688	169
Net interest income after provision for loan losses	6,202	6,089
Non-interest income:		
Depository fees and charges	717	668
Loan fees and service charges	228	417
Gain on loans	43	247
Other	165	416
Total non-interest income	1,153	1,748
Non-interest expense:		
Employee compensation and benefits	3,119	3,414
Net occupancy expense	987	1,016
Equipment, net	584	615
Consulting fees	207	165
Federal deposit insurance premiums	793	31
Other	1,367	2,094
Total non-interest expense	7,057	7,335
Income before income taxes and minority interest	298	502
Income tax benefit	(396)	(322)

Edgar Filing: CARVER BANCORP INC - Form 10-Q

Minority interest, net of taxes			138
Net income	\$	694	\$ 686
Earnings per common share:			
Basic	\$	0.18	\$ 0.28
Diluted	\$	0.18	\$ 0.27

See accompanying notes to unaudited consolidated financial statements

Table of Contents

CARVER BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY AND
COMPREHENSIVE INCOME (LOSS)

(In thousands)

					Accumulated		
	TARP	Common	Additional	Treasury	Retained	Other	Total
	Preferred	Stock	Paid-In	Stock	Earnings	Comprehensive	Stock-
	Stock		Capital			Loss	Holders
							Equity
Balance March 31, 2009	18,980	25	24,214	(760)	21,898	(19)	64,338
Net income					694		694
Change in net unrealized loss on available-for-sale securities, net of taxes						(226)	(226)
Comprehensive income (loss), net of taxes:					694	(226)	468
Common Dividends paid					(247)		(247)
TARP Preferred Dividends paid					(237)		(237)
Treasury stock activity			5	64			69
Stock based compensation					(12)		(12)
Balance June 30, 2009	18,980	25	24,219	(696)	22,096	(245)	64,379

See accompanying notes to unaudited consolidated financial statements

Table of Contents

CARVER BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Three Months Ended June 30,	
	2009	2008
OPERATIONS		
Net income	\$ 694	\$ 686
Adjustments to reconcile net income to net cash from operating activities:		
Provision for loan losses	688	169
Stock based compensation expense	12	35
Depreciation and amortization expense	483	454
Amortization of premiums and discounts	53	52
Loss from sale of real estate owned	34	12
Gain on loans	(43)	(247)
Originations of loans held-for-sale	(386)	(9,097)
Proceeds from sale of loans held-for-sale	386	9,889
Changes in assets and liabilities:		
Decrease in accrued interest receivable	106	271
Decrease in loan premiums and discounts and deferred charges	33	41
Increase in premiums and discounts securities	158	75
(Increase) decrease in other assets	(1,582)	7,500
Increase (decrease) in other liabilities	348	(749)
Net cash provided by operating activities	984	9,091
INVESTING ACTIVITIES		
Purchase of available-for-sale securities		(12,446)
Proceeds from principal payments, maturities and calls of securities:		
Available-for-sale	4,779	1,490
Held-to-maturity	326	669
Originations of loans held-for-investment	(36,462)	(43,225)
Loans purchased from third parties	(3,163)	
Principal collections on loans	21,562	40,675
(Purchase) redemption of FHLB-NY stock	(771)	(642)
Additions to premises and equipment	(134)	(433)
Proceeds from sale of real estate owned	268	1,061
Net cash used in investing activities	(13,595)	(12,851)
FINANCING ACTIVITIES		
Net increase (decrease) in deposits	1,728	(21,199)
Net borrowing of FHLB advances and other borrowings	16,078	13,993
Common stock repurchased		(101)
Dividends paid	(484)	(248)
Net cash provided by (used in) financing activities	17,322	(7,555)

Edgar Filing: CARVER BANCORP INC - Form 10-Q

Net increase (decrease) in cash and cash equivalents	4,711	(11,315)
Cash and cash equivalents at beginning of period	13,341	27,368
Cash and cash equivalents at end of period	\$ 18,052	\$ 16,053

Supplemental information:

Noncash Transfers-

Change in unrealized loss on valuation of available-for-sale investments, net	\$ (359)	\$ (373)
Cash paid for-		
Interest	\$ 5,617	\$ 4,877
Income taxes	\$	\$ 40

See accompanying notes to unaudited consolidated financial statements

Table of Contents**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)****(1) Organization****Nature of operations**

Carver Bancorp, Inc. (on a stand-alone basis, the Holding Company or Registrant), incorporated in May 1996, is the holding company for Carver Federal Savings Bank (the Bank or Carver Federal). Carver Federal's material subsidiaries include Carver Community Development Corp. (CCDC) and CFSB Realty Corp. The Bank also has a majority owned interest in Carver Asset Corporation, a real estate investment trust formed in February 2004.

The Bank was chartered in 1948 and began operations in 1949 as Carver Federal Savings and Loan Association, a federally chartered mutual savings and loan association. The Bank converted to a federal savings bank in 1986. On October 24, 1994, the Bank converted from mutual to stock form and issued 2,314,275 shares of its common stock, par value \$0.01 per share. On October 17, 1996, the Bank completed its reorganization into a holding company structure (the Reorganization) and became a wholly owned subsidiary of the Holding Company.

Carver Federal was founded to serve African-American communities whose residents, businesses and institutions had limited access to mainstream financial services. Today, Carver Federal is the largest African-American operated bank in the United States. The Bank remains dedicated to expanding wealth enhancing opportunities in the communities it serves by increasing access to capital and other financial services for consumers, businesses and non-profit organizations, including faith-based institutions. The Bank remains headquartered in Harlem, and predominantly all of its nine branches and eight stand-alone 24/7 ATM Centers are located in low- to moderate-income neighborhoods. Many of these historically underserved communities have experienced unprecedented growth and diversification of incomes, ethnicity and economic opportunity, after decades of public and private investment. Carver Federal's principal business consists of attracting deposit accounts through its branches and investing those funds in mortgage loans, small business loans and other investments permitted by federal savings banks.

The Bank formalized its many community focused investments on August 18, 2005, by forming CCDC. CCDC oversees the Bank's participation in local economic development and other community-based initiatives, including financial literacy activities. CCDC is now coordinating the Bank's development of an innovative approach to reach the unbanked customer market in Carver Federal's communities. Importantly, CCDC spearheads the Bank's applications for grants and other resources to help fund these important community activities. In this regard, Carver Federal has successfully competed with large regional and global financial institutions in a number of competitions for government grants and other awards. In June 2006, Carver Federal was selected by the U.S. Department of the Treasury (the Treasury) to receive an award of \$59 million in New Market Tax Credits (NMTC). In May 2009, Carver Federal was selected to receive a second NMTC award in the amount of \$65 million. These credits enable the Bank to invest with community and development partners in economic development projects with attractive terms including, in some cases, below market interest rates, which may have the effect of attracting capital to underserved communities and facilitating revitalization of the community. The NMTC award provides substantive credits to Carver Federal against Federal income taxes when the Bank makes qualified investments. For additional information regarding Carver Federal's NMTC, refer to Item 7, New Market Tax Credit Award.

The Company's subsidiary, Carver Statutory Trust I, is not consolidated with Carver Bancorp, Inc. for financial reporting purposes in accordance with Financial Accounting Standards Board, or FASB, revised interpretation No. 46,

Consolidation of Variable Interest Entities, an interpretation of ARB No. 51, or FIN 46(R). Carver Statutory Trust I was formed in 2003 for the purpose of issuing \$13.0 million aggregate liquidation amount of floating rate Capital Securities due September 17, 2033 (Capital Securities) and \$0.4 million of common securities (which are the only voting securities of Carver Statutory Trust I), which are 100% owned by Carver Bancorp, Inc., and using the proceeds to acquire Junior Subordinated Debentures issued by Carver Bancorp, Inc. Carver Bancorp, Inc. has fully and unconditionally guaranteed the Capital Securities along with all obligations of Carver Statutory Trust I under the trust agreement relating to the Capital Securities.

Table of Contents**(2) A) Basis of Presentation**

The accompanying unaudited consolidated financial statements of the Holding Company have been prepared in accordance with United States generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X promulgated by the Securities and Exchange Commission (SEC). Accordingly, they do not include all of the information and footnotes required by GAAP for complete consolidated financial statements. Certain information and note disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to the rules and regulations of the SEC. In the opinion of management, all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of the financial condition, results of operations, changes in stockholders' equity and cash flows of the Holding Company and its subsidiaries on a consolidated basis as of and for the periods shown have been included.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts in the consolidated financial statements. Amounts subject to significant estimates and assumptions are items such as the allowance for loan losses and lending related commitments, valuation on mortgage servicing rights (MSR), goodwill and intangibles, pensions, assessment of other than temporary impairment and the fair value of financial instruments. The current economic environment has increased the uncertainty inherent in these estimates. Actual results could differ from these estimates. The unaudited consolidated financial statements presented herein should be read in conjunction with the consolidated financial statements and notes thereto included in the Holding Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2009, as previously filed with the SEC. The consolidated results of operations and other data for the three-month period ended June 30, 2009 are not necessarily indicative of results that may be expected for the entire fiscal year ending March 31, 2010 (fiscal 2010).

B) Reclassifications

Certain amounts in the consolidated financial statements presented for the prior year period have been reclassified to conform to the current year presentation.

(3) Earnings Per Share

Basic earnings per share (EPS) is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding. In calculating EPS for the quarter ended June 30, 2009, dividends paid pursuant to the Company's participation in the United States, Department of Treasury Troubled Asset Relief Program, Capital Purchase Program (TARP CPP) reduced the income available to common shareholders, thereby reducing EPS for June 30, 2009 compared to June 30, 2008. Further, income available to common shareholders was reduced by dividend paid to unvested restricted shares granted under the Company's Management Recognition Plan (MRP) which are participating securities in accordance with the FSP EITF 03-6-1, *Determining Whether Instruments Granted In Share-Based Payment Transactions Are Participating Securities*. Diluted earnings per common share includes any additional common shares as if all potentially dilutive common shares were issued (for instance, stock options with an exercise price that is less than the average market price of the common shares for the periods stated). For the purpose of these calculations, unreleased Employee Stock Ownership Program (ESOP) shares are not considered to be outstanding. For the quarters ended June 30, 2009 and 2008, respectively, 19,321 and 37,730 shares of common stock were potentially issuable from the exercise of stock options with an exercise price that is less than the average market price of the common shares and unvested restricted stock grants for the same period. The effects of these potentially dilutive common shares were considered in determining the diluted earnings per common share.

(4) Accounting for Stock Based Compensation

The Company follows Statement of Financial Accounting Standards No. 123R, *Share-Based Payment* (SFAS No. 123R), which requires that all stock-based compensation be recognized as an expense in the financial statements and that such cost be measured at the fair value of the award. This statement was adopted using the modified prospective method of application, which requires the Company to recognize compensation expense on a prospective basis. Therefore, prior period financial statements have not been restated. Under this method, in addition to reflecting compensation expense for new share-based awards, expense is also recognized to reflect the remaining service period

of awards that had been included in pro forma disclosures in prior periods. SFAS No. 123R also requires that excess tax benefits related to stock option exercises be reflected as financing cash inflows instead of operating cash inflows. Stock-based compensation expense and the related tax benefit recognized for the quarter ended June 30, 2009 and June 30, 2008 totaled \$12,000 and \$18,000, respectively.

(5) Benefit Plans

Employee Pension Plan

The Bank has a non-contributory defined benefit pension plan covering all eligible employees. The benefits are based on each employee's term of service. The Bank's policy was to fund the plan with contributions equal to the maximum amount deductible for federal income tax purposes. The pension plan was curtailed and future benefit accruals ceased as of December 31, 2000.

Table of Contents

The Company's pension benefit and post-retirement health and welfare benefit obligations, and the related costs, are calculated using actuarial concepts, within the framework of SFAS No. 87, *Employers' Accounting for Pensions* and SFAS No. 106, *Employers' Accounting for Post-retirement Benefits Other than Pensions*, respectively. The measurement of such obligations and expenses requires that certain assumptions be made regarding several factors, most notably including the discount rate and the expected return on plan assets. The Company evaluates these critical assumptions on an annual basis. Other factors considered by the Company include retirement patterns, mortality, turnover, and the rate of compensation increase.

Under Statement of Financial Accounting Standards No. 158, *Employers' Accounting for Defined Benefits Pension and Other Post-retirement Plans- an amendment of SFAS Statement Nos. 87, 88, 106 and 132(R)*, actuarial gain and losses, prior services cost or credits, and any remaining transition assets or obligations that have not been recognized under previous accounting standards must be recognized in accumulated other comprehensive income or loss, net of taxes effects, until they are amortized as a component of net of periodic benefit cost. In addition, under SFAS No. 158 the measurement date (i.e., the date at which plan assets and the benefit obligation are measured for financial reporting purposes) is required to be the company's fiscal year end. The company had used a December 31 measurement date for its pension, as permitted by SFAS Nos. 87 and 106. In accordance with SFAS No. 158, the Company has adopted a fiscal year-end measurement date on March 31, 2009.

(6) Common Stock Dividend

On August 14, 2009, the Board of Directors of the Holding Company declared, for the quarter ended June 30, 2009, a cash dividend of ten cents \$0.10 per common share outstanding. The dividend is payable on September 14, 2009 to stockholders of record at the close of business on September 1, 2009.

(7) Investment Securities

Effective April 1, 2009, we adopted FASB Staff Position, or FSP, No. FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*, which amends existing other-than-temporary-impairment, or OTTI, guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of OTTI on debt and equity securities in the financial statements. This FSP modifies the existing requirements for recognizing OTTI on debt securities but does not amend existing recognition and measurement guidance related to OTTI of equity securities. This FSP expands and increases the frequency of existing disclosures about OTTI for debt and equity securities and requires new disclosures to help users of financial statements understand the significant inputs used in determining a credit loss, as well as a rollforward of that amount each period. As of June 30, 2009, we have not recognized OTTI on any debt securities. Our adoption of FSP No. 115-2 and FAS 124-2 did not have a material impact on our financial condition or results of operations.

Table of Contents

The following table sets forth the amortized cost and estimated fair value of securities available-for-sale and held-to-maturity at the dates indicated.

	Amortized Cost	Gross Unrealized		Estimated Fair-Value
		Gains	Losses	
Available-for-Sale:				
Mortgage-backed securities:				
Government National Mortgage Association	\$ 36,175	\$ 21	\$ (618)	\$ 35,578
Federal Home Loan Mortgage Corporation	12,836	354	(5)	13,185
Federal National Mortgage Association	5,382	137	(1)	5,518
Other	473	3	(73)	403
Total mortgage-backed securities	54,866	515	(697)	54,684
U.S. Government Agency Securities				
Total available-for-sale	54,866	515	(697)	54,684
	Amortized Cost	Gross Unrealized		Estimated Fair-Value
		Gains	Losses	
Held-to-Maturity:				
Mortgage-backed securities:				
Government National Mortgage Association	458	33		491
Federal Home Loan Mortgage Corporation	9,675	15	(48)	9,642
Federal National Mortgage Association	3,801	42	(270)	3,573

Level 1: Inputs are unadjusted quoted prices in active markets for assets or liabilities identical to those reported at fair value.

Level 2: Inputs other than quoted prices included within Level 1 inputs that are observable either directly or indirectly. These inputs include quoted prices in active or not active markets or inputs derived from or corroborated by observable market data.

Level 3: Inputs are unobservable inputs for an asset or liability. These inputs are used to determine fair value only when observable inputs are not available.

<PAGE> 8

The Company did not make any changes to its valuation techniques during the three months ended March 31, 2008.

The following table summarizes the financial assets measured at fair value on a recurring basis:

(In thousands)	Fair Value Measurements at March 31, 2008 Using			
	March 31, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Available for sale securities	\$342,511	--	\$341,622	\$889

Available for sale securities are reported at fair value primarily utilizing observable inputs (Level 2). The Company obtains fair value measurements from independent pricing services, which base their fair value measurements upon observable inputs such as reported trades of comparable securities, broker quotes, the Treasury yield curve, benchmark interest rates, market spread relationships, historic and consensus prepayment rates, credit information and the security's terms and conditions.

The Company used significant unobservable inputs (Level 3) to value one of its available for sale securities, which is a private placement mezzanine tranche of a collateralized debt obligation backed by trust preferred securities. There is limited trading in this security and in comparable securities. The security was valued based upon market-maker bid level pricing estimates.

The following table shows a reconciliation of the beginning and ending balances for fair value measurements using significant unobservable inputs:

	Fair Value Measurements Using Significant Unobservable Inputs
Available for sale securities	(In thousands)
Balance, January 1, 2008	\$974
Total unrealized losses included in other comprehensive income	(85)
Purchases	--
Sales/Maturities	--
Transfers in and/out of Level 3	--
Balance, March 31, 2008	\$889

The following table summarizes the financial assets measured at fair value on a non-recurring basis.

(In thousands)	Fair Value Measurements at March 31, 2008 Using			
	March 31, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Impaired loans	\$3,653	--	\$3,653	--

Impaired loans, which are measured for impairment using the fair value of the collateral (Level 2) for collateral dependent loans, had a carrying amount of \$4.2 million, with a valuation allowance of \$568,000, resulting in an additional provision for loan losses of \$82,000 for the three months ended March 31, 2008.

<PAGE> 9

In February 2007, the FASB issued SFAS No. 159 ("SFAS 159"), *"The Fair Value Option for Financial Assets and Financial Liabilities."* SFAS 159 provides companies with an option to report selected financial assets and liabilities at fair value and to provide additional information that will help investors and other users of financial statements to understand more easily the effect on earnings of the company's choice to use fair value. It also requires companies to display the fair value of those assets and liabilities for which the company has chosen to use fair value on the face of the balance sheet. The Company did not elect the fair value option for any financial assets or financial liabilities as of January 1, 2008, the effective date of this standard.

In November 2007, the SEC issued SAB No. 109 ("SAB 109"), *"Written Loan Commitments Recorded at Fair Value Through Earnings."* SAB 109 supersedes SAB No. 105, *"Application of Accounting Principles to Loan Commitments,"* and indicates that the expected net future cash flows related to the associated servicing of the loan should be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The guidance in SAB 109 is applied on a prospective basis to derivative loan commitments issued or modified in fiscal quarters beginning after December 15, 2007. The adoption of SAB 109 on January 1, 2008 did not have a material impact on the Company's consolidated financial statements.

(5) Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141 ("SFAS 141R"), *"Business Combinations (Revised 2007)."* SFAS 141R replaces SFAS No. 141, *"Business Combinations,"* and applies to all transactions and other events in which one entity obtains control over one or more other businesses. SFAS 141R requires an acquirer, upon initially obtaining control of another entity, to recognize the assets, liabilities and any non-controlling interest in the acquiree at fair value as of the acquisition date. Contingent consideration is required to be recognized and measured at fair value on the date of acquisition rather than at a later date when the amount of that consideration may be determinable beyond a reasonable doubt. This fair value approach replaces the cost-allocation process required under SFAS 141 whereby the cost of an acquisition was allocated to the individual assets acquired and liabilities assumed based on their estimated fair value. SFAS 141R requires acquirers to expense acquisition-related costs as incurred rather than allocating such costs to the assets acquired and liabilities assumed, as was previously the case under SFAS 141. Under SFAS 141R, the requirements of SFAS No. 146, *"Accounting for Costs Associated with Exit or Disposal Activities,"* would

have to be met in order to accrue for a restructuring plan in purchase accounting. Pre-acquisition contingencies are to be recognized at fair value, unless it is a non-contractual contingency that is not likely to materialize, in which case, nothing should be recognized in purchase accounting and, instead, that contingency would be subject to the probable and estimable recognition criteria of SFAS No. 5, "Accounting for Contingencies." The Company does not anticipate the adoption of SFAS 141R will materially impact its consolidated financial statements upon adoption on January 1, 2009.

<PAGE> 10

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

ITEM 2. Management's Discussion and Analysis

General

The Company's principal subsidiary, Bank Rhode Island, is a commercial bank chartered as a financial institution in the State of Rhode Island. The Bank pursues a community banking mission and is principally engaged in providing banking products and services to individuals and businesses in Rhode Island and nearby areas of Massachusetts. The Bank is subject to competition from a variety of traditional and nontraditional financial service providers both within and outside of Rhode Island. The Bank offers its customers a wide range of business, commercial real estate, consumer and residential loans and leases, deposit products, nondeposit investment products, cash management, private banking and other banking products and services designed to meet the financial needs of individuals and small- to mid-sized businesses. The Bank also offers both commercial and consumer online banking products and maintains a web site at <http://www.bankri.com>. The Company and Bank are subject to the regulations of certain federal and state agencies and undergo periodic examinations by certain of those regulatory authorities. The Bank's deposits are insured by the FDIC, subject to regulatory limits. The Bank is also a member of the Federal Home Loan Bank of Boston ("FHLB"). The Company's common stock is traded on the Nasdaq Global Select MarketSM under the symbol "BARI." The Company's financial reports can be accessed through its website within 24 hours of filing with the SEC.

Critical Accounting Policies

Accounting policies involving significant judgments and assumptions by management, which have, or could have, a material impact on the carrying value of certain assets or net income, are considered critical accounting policies. The preparation of financial statements in accordance with U.S. generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. Actual results could differ from those estimates. As discussed in the Company's 2007 Annual Report on Form 10-K, management has identified the accounting for the allowance for loan and lease losses, review of goodwill for impairment and accounting for income taxes as the Company's most critical accounting policies. There have been no significant changes in the methods or assumptions used in accounting policies that require material estimates or assumptions.

Overview

The primary drivers of the Company's operating income are net interest income, which is strongly affected by the net yield on interest-earning assets ("net interest margin"), and the quality of the Company's assets.

The Company's net interest income represents the difference between interest income and its cost of funds. Interest income depends on the amount of interest-earning assets outstanding during the year and the interest rates earned thereon. Cost of funds is a function of the average amount of deposits and borrowed money

outstanding during the year and the interest rates paid thereon. The net interest margin is calculated by dividing net interest income by average interest-earning assets. Net interest spread is the difference between the average rate earned on interest-earning assets and the average rate paid on interest-bearing liabilities. Net interest margin generally exceeds the net interest spread as a portion of interest-earning assets are funded by various noninterest-bearing sources (primarily noninterest-bearing deposits and shareholders' equity). The increases (decreases) in the components of interest income and interest expense, expressed in terms of fluctuation in average volume and rate, are summarized in the Rate/Volume Analysis tables shown on page 24. Information as to the components of interest income and interest expense and average rates is provided under "*Average Balances, Yields and Costs*" on page 23.

<PAGE> 11

Because the Company's assets are not identical in duration and in repricing dates to its liabilities, the spread between the two is vulnerable to changes in market interest rates as well as the overall shape of the yield curve. These vulnerabilities are inherent to the business of banking and are commonly referred to as "interest rate risk." How to measure interest rate risk and, once measured, how much risk to take are based on numerous assumptions and other subjective judgments. See also discussion under "*Interest Rate Risk*" on page 28.

The quality of the Company's assets also influences its earnings. Loans and leases that are not paid on a timely basis and exhibit other weaknesses can result in the loss of principal and/or interest income. Additionally, the Company must make timely provisions to the allowance for loan and lease losses based on estimates of probable losses inherent in the loan and lease portfolio; these additions, which are charged against earnings, are necessarily greater when greater probable losses are expected. Further, the Company incurs expenses as a result of resolving troubled assets. All of these reflect the "credit risk" that the Company takes on in the ordinary course of business and is further discussed under "*Financial Condition - Asset Quality*" on page 17.

The Company's business strategy has been to concentrate its asset generation efforts on commercial and consumer loans and its deposit generation efforts on checking and savings accounts. These deposit accounts are commonly referred to as "core deposit accounts." This strategy is based on the Company's belief that it can distinguish itself from its larger competitors, and indeed attract customers from them, through a higher level of service and through its ability to set policies and procedures, as well as make decisions, locally. The loan and deposit products referenced also tend to be geared more toward customers who are relationship oriented than those who are seeking stand-alone or single transaction products. The Company believes that its service-oriented approach enables it to compete successfully for relationship-oriented customers. Additionally, the Company is predominantly an urban franchise with a high concentration of businesses, which makes deployment of funds in the commercial lending area practicable. Commercial loans are attractive to the Company, among other reasons, because of their higher yields. Similarly, core deposits are attractive to the Company because of their generally lower interest cost and potential for fee income.

The Company also seeks to leverage business opportunities presented by its customer base, franchise footprint and resources. In 2005, the Bank formed a private banking division and completed the Bank's first acquisition, acquiring the operations of an equipment leasing company located in Long Island, New York ("Macrolease"). The Bank is using the Macrolease platform to generate additional income by originating equipment leases for third parties, as well as increasing the Bank's portfolio of equipment leases.

The deposit market in Rhode Island is highly concentrated. The State's three largest banks have an aggregate market share of approximately 85% in Providence and Kent Counties, the Bank's primary marketplace (based upon June 2007 FDIC statistics, excluding one bank that draws its deposits primarily from the internet). Competition for loans and deposits remains intense. This competition has resulted in considerable advertising and promotional product offerings by competitors, including print, radio and television media.

Edgar Filing: CARVER BANCORP INC - Form 10-Q

For the three months ended March 31, 2008, approximately 78.0% of the Company's revenues (defined as net interest income plus noninterest income) were derived from its level of net interest income. In a continuing effort to diversify its sources of revenue, the Company has sought to expand its sources of noninterest income (primarily fees and charges for products and services the Bank offers). Service charges on deposit accounts remain the largest component of noninterest income, while the Bank has recently seen growth in gains on lease sales.

The future operating results of the Company are dependent upon on its ability to maintain and expand its net interest margin, while minimizing its exposure to credit risk, along with increasing sources of noninterest income, while controlling the growth of noninterest or operating expenses.

<PAGE> 12

Financial Condition - Executive Summary

Selected balance sheet data is presented in the table below as of the dates indicated:

(In thousands)	March 31, 2008	December 31, 2007	September 30, 2007	June 30, 2007	March 31, 2007
Balance sheet data:					
Total assets	\$1,490,720	\$1,477,119	\$1,492,695	\$1,466,715	\$1,483,157
Loans and leases receivable	1,024,901	1,038,132	1,025,875	1,024,235	1,007,448
Securities available for sale	342,512	335,181	330,749	330,304	350,655
Core deposits ^(a)	658,557	640,717	637,290	641,164	638,317
Certificates of deposit	379,673	374,063	381,821	384,543	390,295
Borrowings	317,099	331,703	339,692	313,776	322,336
Total shareholders' equity	114,831	113,108	117,868	115,080	115,357
Core deposit ratio	63.4%	63.1%	62.5%	62.5%	62.1%

(a) Core deposits consist of demand deposit, NOW, money market and savings accounts.

Total assets increased by \$13.6 million since December 31, 2007. Total loans and leases decreased by \$13.2 million during the first quarter of 2008, as the increase in commercial loans of \$3.3 million, or 0.6%, was offset by decreases in the primarily purchased residential mortgage loan portfolio of \$12.2 million, or 4.9% and a decrease in consumer and other loans of \$4.3 million, or 2.0%. Available for sale securities increased \$7.3 million, or 2.2%, since year-end. The Bank increased its core deposits by \$17.8 million, or 2.8%, since year-end. Within this growth, savings accounts grew by \$14.0 million, or 3.5%, and demand deposit accounts increased by \$7.2 million, or 4.2%. Borrowings decreased by \$14.6 million, or 4.4%, primarily from a decrease in customer retail repurchase agreements. Shareholders' equity as a percentage of total assets was 7.7% at March 31, 2008 and December 31, 2007.

The Company's financial position at March 31, 2008 as compared to the prior year quarter-end (March 31, 2007) reflects net growth of \$17.5 million in total loans and leases. This increase reflects the continuing conversion of the balance sheet to a more commercial profile with increases in commercial loans and leases of

\$44.5 million (up 8.4%). Consumer loans declined \$4.6 million (down 2.1%) from the prior year quarter-end. The residential mortgage portfolio declined \$22.4 million (down 8.7%) from March 31, 2007 as repayments exceeded new purchases. Also, available for sale securities at March 31, 2008 declined by \$8.1 million (down 2.3%). Deposits have increased \$9.6 million, or 0.9%, since the prior year quarter-end, with growth centered in savings accounts (up \$39.7 million). This increase was offset by decreases in NOW accounts (down \$17.3 million), certificate of deposit accounts (down \$10.6 million), demand deposit accounts (down \$1.6 million), and money market accounts (down \$525,000). Borrowings have decreased since March 31, 2007 by \$5.2 million, reflecting the Company's redemption of the subordinated deferrable interest debentures held by BRI Statutory Trust II in September 2007.

<PAGE> 13

Financial Condition - Detailed Analysis

Investments

Total investments consists of available for sale securities (investment securities and mortgage-backed securities ("MBSs")), stock in the FHLB and overnight investments. Total investments comprised \$391.3 million, or 26.2% of total assets, at March 31, 2008, compared to \$367.9 million, or 24.9% of total assets, at December 31, 2007, representing an increase of \$23.3 million, or 6.3%. All \$342.5 million of investment securities and MBSs at March 31, 2008 were classified as available for sale and recorded at fair value. These available for sale securities carried a total of \$1.3 million in net unrealized gains at the end of the quarter, compared to \$106,000 of net unrealized losses at December 31, 2007.

The Company's securities in an unrealized loss position were deemed to be not other-than-temporarily impaired after considering that substantially all available for sale securities were rated "investment grade" with unrealized losses primarily caused by market interest rate changes. In addition, the Company has the intent and ability to hold all securities with unrealized losses until recovery or maturity. In making these other-than-temporary impairment determinations, management considers, among other things, the length of time and extent to which the fair value has been less than cost and the credit worthiness and near-term prospects of the issuer. Also, management considers capital adequacy, interest rate risk, liquidity and business plans in assessing the intent and ability to hold all securities with unrealized losses until recovery or maturity.

The Company's available for sale securities are reported at fair value primarily utilizing observable inputs (Level 2 under SFAS 157). The Company obtains fair value measurements from independent pricing services, which base their fair value measurements upon observable inputs such as reported trades of comparable securities, broker quotes, the Treasury yield curve, benchmark interest rates, market spread relationships, historic and consensus prepayment rates, credit information and the security's terms and conditions. The Company validates its valuation techniques by periodically performing procedures such as understanding the models used by pricing sources and obtaining market values from other pricing sources. See also Note 4 - Recently Adopted Accounting Pronouncements in the accompanying notes to unaudited consolidated financial statements on page 8 for further discussion.

The investment portfolio provides the Company a source of short-term liquidity and acts as a counterbalance to loan and deposit flows. During the first quarter of 2008, the Company purchased \$66.1 million of available for sale securities, while maturities/calls and principal repayments totaled \$47.3 million. Additionally, in the first quarter of 2008, the Company sold \$13.1 million of mortgage-backed securities generating gains of \$242,000. Fluctuations in market interest rates led to a large number of calls on the Company's investment holdings in the 2008 first quarter resulting in increased volume of investment and mortgage-backed security purchases compared to the first quarter of 2007.

Loans and Leases

Total loans and leases decreased by \$13.2 million since December 31, 2007 to stand at \$1.02 billion at March 31, 2008. As a percentage of total assets, loans and leases decreased to 68.8% at March 31, 2008, compared to 70.3% at December 31, 2007. The Company attempts to concentrate its asset growth in its loan and lease portfolios to maximize the yield on new assets and to take advantage of demand for both commercial and home equity loan products in its market area. Total loans and leases as of March 31, 2008 is comprised of three broad categories: commercial loans and leases that aggregate \$577.0 million, or 56.3% of the portfolio; residential mortgages that aggregate \$236.5 million, or 23.1% of the portfolio; and consumer and other loans that aggregate \$211.4 million, or 20.6% of the portfolio.

Commercial loans and leases - The commercial loan and lease portfolio (consisting of commercial real estate, business lending, equipment leases, multi-family real estate, construction and small business loans) increased \$3.3 million, or 0.6%, during the first three months of 2008. During this period, the Bank recorded approximately the same amount of new commercial commitments as compared to the first quarter of 2007. However, portfolio growth was largely offset by an increase in prepayments.

<PAGE> 14

The Bank's business lending group originates business loans, also referred to as commercial and industrial loans, including owner-occupied commercial real estate loans, term loans and revolving lines of credit. Within the business lending portfolio, commercial and industrial loans increased \$1.2 million, or 0.9%, while owner-occupied commercial real estate loans decreased by a similar amount of \$1.7 million, or 1.1%, since year-end.

The Bank's commercial real estate ("CRE") group originates nonowner-occupied commercial real estate, multi-family residential real estate and construction loans. These real estate secured commercial loans are offered as both fixed and adjustable-rate products. Since December 31, 2007, CRE loans have increased \$1.7 million, or 0.9%, on a net basis, reflective of the increased repayment activity referred to above.

With the Macrolease platform, the Bank originates equipment leases for its own portfolio, as well as originates leases for third parties as a source of noninterest income. In addition, the Bank historically has purchased equipment leases from originators outside of the Bank. The U.S. Government and its agencies are the principal lessees on the vast majority of these purchased leases. These "government" leases generally have maturities of five years or less and are not dependent on residual collateral values. At March 31, 2008, leases comprised 10.5% of the commercial loan and lease portfolio, with \$47.7 million of Macrolease-generated leases and \$13.1 million of purchased government leases. Included within these amounts were \$1.2 million of leases generated for sale at March 31, 2008.

At March 31, 2008, small business loans were \$46.3 million, compared to \$45.8 million at December 31, 2007, representing 8.0% of the commercial portfolio at each period end. These loans reflect those historically originated by the Bank's small business lending group and branch system and now primarily originated by the Bank's branch system. The Bank utilizes credit scoring and streamlined documentation, as well as traditional review standards in originating these credits.

The Bank is a participant in the U.S. Small Business Administration ("SBA") Preferred Lender Program in both Rhode Island and Massachusetts. SBA guaranteed loans are found throughout the portfolios managed by the Bank's various lending groups.

The Company believes it is well positioned for continued commercial growth. The Bank places particular emphasis on the generation of small- to medium-sized commercial relationships (those with \$10 million or less

in total loan commitments). Additionally, the Bank offers asset-based commercial loan facilities that monitor advances against receivables and inventories on a formula basis.

Residential mortgage loans - During the first three months of 2008, residential mortgage loans decreased \$12.2 million, or down 4.9%. During this period, the Bank did not originate or purchase any mortgages. Comparatively, in the 2007 first quarter, the Bank purchased \$5.7 million of mortgages and did not originate any mortgages for its own portfolio. Since inception, the Bank has concentrated its portfolio lending efforts on commercial and consumer lending opportunities, but originates mortgage loans for its own portfolio on a limited basis. The Bank does not employ any outside mortgage originators, but periodically purchases residential mortgage loans from third-party originators. The Bank may purchase residential mortgage loans to utilize available cash flow as opportunities arise. At March 31, 2008, the Bank did not have any commitments to purchase residential mortgage loans within the next 60 days.

Consumer loans - The consumer loan portfolio decreased \$4.3 million, or 2.0%, during the first three months of 2008 as repayments of \$9.8 million exceeded originations of \$5.5 million. The decline in growth through March 31, 2008 was reflective of the softening of housing prices in the local market area over the past few years. The Company believes the softening prices have reduced consumer appetite for borrowing against the value of their homes. However, the Company continues to promote consumer lending as it believes that these ten- to twenty-year fixed rate products, along with floating rate lines of credit, possess attractive cash flow characteristics in the current interest rate environment.

<PAGE> 15

The following is a summary of loans and leases receivable:

	March 31, 2008	December 31, 2007
	(In thousands)	
Commercial loans and leases:		
Commercial real estate - owner occupied	\$ 155,750	\$ 157,431
Commercial and industrial	133,085	131,927
Commercial real estate - nonowner occupied	101,604	102,990
Small business	46,311	45,778
Multi-family	47,238	42,536
Construction	37,169	38,832
Leases and other ^(a)	60,813	58,702
Subtotal	581,970	578,196
Unearned lease income	(6,378)	(5,742)
Net deferred loan origination costs	1,362	1,214
Total commercial loans and leases	576,954	573,668
Residential mortgage loans:		
One- to four-family adjustable rate	143,833	155,087
One- to four-family fixed rate	91,626	92,485

Edgar Filing: CARVER BANCORP INC - Form 10-Q

Subtotal	235,459	247,572
Premium on loans acquired	1,125	1,198
Net deferred loan origination fees	(41)	(42)
	<hr/>	<hr/>
Total residential mortgage loans	236,543	248,728
	<hr/>	<hr/>
Consumer loans:		
Home equity - term loans	143,494	149,192
Home equity - lines of credit	63,680	62,357
Unsecured and other	2,860	2,774
	<hr/>	<hr/>
Subtotal	210,034	214,323
Net deferred loan origination costs	1,370	1,413
	<hr/>	<hr/>
Total consumer loans	211,404	215,736
	<hr/>	<hr/>
Total loans and leases receivable	\$1,024,901	\$1,038,132
	<hr/>	<hr/>

- (a) Included within commercial loans and leases were leases held for sale of \$1.2 million at March 31, 2008 and \$3.3 million at December 31, 2007, respectively.

Deposits

Total deposits increased by \$23.5 million, or 2.3%, during the first three months of 2008, from \$1.01 billion, or 68.7% of total assets, at December 31, 2007, to \$1.04 billion, or 69.6% of total assets, at March 31, 2008.

The following table sets forth certain information regarding deposits:

	March 31, 2008			December 31, 2007		
	Amount	Percent Of Total	Weighted Average Rate	Amount	Percent of Total	Weighted Average Rate
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
	(In thousands)					
NOW accounts	\$ 61,706	5.9%	0.28%	\$ 65,191	6.4%	0.60%
Money market accounts	6,172	0.6%	1.75%	6,054	0.6%	2.32%
Savings accounts	410,796	39.6%	2.22%	396,838	39.1%	3.01%
Certificate of deposit accounts	379,673	36.6%	4.17%	374,063	36.9%	4.46%
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Total interest bearing deposits	858,347	82.7%	2.94%	842,146	83.0%	3.46%

Edgar Filing: CARVER BANCORP INC - Form 10-Q

Noninterest bearing accounts	179,883	17.3%	--	172,634	17.0%	--
Total deposits	<u>\$1,038,230</u>	<u>100.0%</u>	<u>2.42%</u>	<u>\$1,014,780</u>	<u>100.0%</u>	<u>2.86%</u>

<PAGE> 16

The overall composition of total deposits remained relatively the same during the first three months of the year. At March 31, 2008, core deposit accounts comprised 63.4% of total deposits, up moderately from 63.1% of total deposits at December 31, 2007. The Bank continued its strategy of emphasizing the normally lower cost core deposits over CDs. This strategy resulted in an increase in core deposits since December 31, 2007 of \$17.8 million, or 2.8%.

During the first three months of 2008, competition for deposits remained strong in the Company's market areas. During this period, the Bank increased its total deposits by \$23.5 million as compared to December 31, 2007, with growth in most deposit categories. Savings and CD accounts grew \$14.0 million and \$5.6 million, respectively, over the past three months. By March 31, 2008, demand deposit accounts grew to \$179.9 million, an increase of \$7.2 million from \$172.6 million at December 31, 2007. These increases offset the decline of NOW accounts of \$3.5 million. At March 31, 2008, brokered CDs were \$10.0 million, or 1.0% of total deposits, down from \$20.0 million, or 2.0% of total deposits, at the prior year-end. The Bank may utilize brokered CDs if their rates are attractive compared to wholesale funding.

Borrowings

Overnight and short-term borrowings decreased \$17.9 million during the first three months of 2008 from the December 31, 2007 level of \$66.8 million, with one larger customer retail repurchase agreement comprising the majority of this decline. Through the Bank's membership in the FHLB, the Company has access to a number of different funding structures. FHLB borrowings increased by \$3.2 million from the December 31, 2007 amount of \$241.5 million. Wholesale repurchase agreements remained constant with the December 31, 2007 balance of \$10.0 million. The Bank may utilize wholesale repurchase agreement funding in the future if spreads are favorable compared to FHLB borrowings or for diversification purposes.

On a long-term basis, the Company intends to continue concentrating on increasing its core deposits, and will utilize FHLB borrowings or wholesale repurchase agreements as cash flows dictate, as opportunities present themselves and as part of the Bank's overall strategy to manage interest rate risk.

Asset Quality

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

Nonperforming assets - At March 31, 2008, the Company had nonperforming assets of \$8.6 million, which represented 0.58% of total assets. This compares to nonperforming assets of \$4.1 million, or 0.28% of total assets, at December 31, 2007. Total nonperforming assets at March 31, 2008 consisted of nonaccrual loans and leases with commercial loans and leases aggregating \$5.1 million, residential mortgage loans aggregating \$2.4

million and commercial loans and leases 90 days past due, but still accruing of \$1.1 million. Nonperforming assets at December 31, 2007 were comprised of nonaccrual residential and commercial loans. With respect to loans past due 90 days, but still accruing at March 31, 2008, this balance was comprised of commercial leases to government entities, which were primarily attributable to administrative delays as opposed to underlying credit or cash flow issues. These leases were within commercial loans and leases 60 to 89 days past due of \$3.4 million at December 31, 2007.

Included in nonaccrual loans and leases at March 31, 2008 were \$4.8 million of impaired loans and leases, with specific impairment reserves against these loans of \$568,000. At December 31, 2007, there were \$3.0 million of impaired loans and leases with specific impairment reserves of \$486,000. The increase in nonaccrual loans and leases since year-end relates primarily to a few commercial loans and lease credits.

<PAGE> 17

The Company evaluates the underlying collateral of each nonperforming loan and continues to pursue the collection of interest and principal. Management believes that the current level of nonperforming assets remains low relative to the size of the Company's loan portfolio. As the loan portfolio continues to grow and mature, or if economic conditions worsen, management believes it possible that the level of nonperforming assets may increase, as may its level of charged-off loans.

Delinquencies - At March 31, 2008, loan balances of \$779,000 were 60 to 89 days past due, down from \$3.7 million at December 31, 2007.

The following table sets forth information regarding nonperforming assets and loans 60-89 days past due as of the dates indicated:

	March 31, 2008	December 31, 2007
	(In thousands)	
Loans and leases accounted for on a nonaccrual basis	\$7,449	\$4,012
Restructured loans and leases	34	37
Loans and leases past due 90 days or more, but still accruing	1,138	100
Impaired loans and leases (not included in nonaccrual loans and leases)	--	--
	<hr/>	<hr/>
Total nonperforming loans and leases	8,621	4,149
Other real estate owned	--	--
	<hr/>	<hr/>
Total nonperforming assets	<u>\$8,621</u>	<u>\$4,149</u>
Delinquent loans 60-89 days past due	\$ 779	\$3,702
Nonperforming loans and leases as a percent of total loans and leases	0.84%	0.40%
Nonperforming assets as a percent of total assets	0.58%	0.28%
Delinquent loans and leases 60-89 days past due as a percent of total loans	0.08%	0.36%

Adversely classified assets - The Company's management classifies certain assets as "substandard," "doubtful" or "loss" based on criteria established under banking regulations. An asset is considered substandard if inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the "distinct possibility" that the insured institution will sustain "some loss" if existing deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses present make "collection or liquidation in full," on the basis of currently existing facts, conditions and values, "highly questionable and improbable." Assets classified as loss are those considered "uncollectible" and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted.

At March 31, 2008, the Company had \$10.9 million of assets that were classified as substandard. This compares to \$9.5 million of assets that were classified as substandard at December 31, 2007. The Company had no assets that were classified as doubtful or loss at either date. Performing loans may or may not be adversely classified depending upon management's judgment with respect to each individual loan. At March 31, 2008, included in the assets that were classified as substandard were \$3.4 million of performing loans. This compares to \$5.3 million of adversely classified performing loans as of December 31, 2007. These amounts constitute assets that, in the opinion of management, could potentially migrate to nonperforming or doubtful status. Management believes that the March 31, 2008 level of adversely classified assets is low relative to the size of the Company's loan and lease portfolio. If a significant downturn in the local or regional market occurs or if other economic or market conditions worsen, management believes it possible that the level of adversely classified assets may increase. This in turn may necessitate an increase to the provision for loan losses in future periods.

<PAGE> 18

Allowance for Loan and Lease Losses

During the first three months of 2008, the Company made additions to the allowance for loan and lease losses of \$285,000 and experienced net charge-offs of \$311,000 compared to additions to the allowance for loan and lease losses of \$100,000 and net charge-offs of \$39,000 for the first three months of 2007. The net charge-offs were primarily from commercial real estate and small business portfolios. At March 31, 2008, the allowance for loan and lease losses stood at \$12.6 million and represented 146.1% of nonperforming loans and 1.23% of total loans and leases outstanding. This compares to an allowance for loan and lease losses of \$12.6 million, representing 304.2% of nonperforming loans and 1.22% of total loans and leases outstanding at December 31, 2007.

An analysis of the activity in the allowance for loan and lease losses is as follows:

	Three Months Ended March 31, 2008	Year Ended December 31, 2007
(In thousands)		
Balance at beginning of period	\$12,619	\$12,377
Loans charged-off:		
Commercial loans and leases	(298)	(184)
Residential mortgage loans	--	(248)
Consumer and other loans	(30)	(96)

Total loans charged-off	(328)	(528)
Recoveries of loans previously charged-off:		
Commercial loans and leases	13	32
Residential mortgage loans	--	--
Consumer and other loans	4	38
Total recoveries of loans previously charged-off	17	70
Net charge-offs	(311)	(458)
Provision for loan and lease losses charged against income	285	700
Balance at end of period	\$12,593	\$12,619

The following table represents the allocation of the allowance for loan and lease losses as of the dates indicated:

	March 31, 2008	December 31, 2007
	(In thousands)	
Loan category		
Commercial loans and leases	\$ 8,721	\$ 8,786
Residential mortgage loans	1,118	1,002
Consumer and other loans	1,603	1,637
Unallocated	1,151	1,194
Total	\$12,593	\$12,619

Assessing the appropriateness of the allowance for loan and lease losses involves substantial uncertainties and is based upon management's evaluation of the amounts required to meet estimated charge-offs in the loan and lease portfolio after weighing various factors. Management's methodology to estimate loss exposure includes an analysis of individual loans and leases deemed to be impaired, reserve allocations for various loan types based on payment status or loss experience and an unallocated allowance that is maintained based on management's assessment of many factors including the growth, composition and quality of the loan portfolio, historical loss experiences, general economic conditions and other pertinent

<PAGE> 19

factors. These risk factors are reviewed and revised by management where conditions indicate that the estimates initially applied are different from actual results. Based on this evaluation, management believes that the allowance for loan and lease losses, as of March 31, 2008, is appropriate.

A portion of the allowance for loan and lease losses is not allocated to any specific segment of the loan portfolio. This non-specific allowance, also referred to as unallocated allowance, is maintained for two primary reasons: (i) there exists an inherent subjectivity and imprecision to the analytical processes employed, and (ii) the prevailing business environment, as it is affected by changing economic conditions and various external factors, may impact the portfolio in ways currently unforeseen. Management, therefore, has established and maintains a non-specific allowance for loan and lease losses. The amount of this measurement imprecision allocation was \$1.2 million at both March 31, 2008 and December 31, 2007.

The allocation of the allowance for loan and lease losses at March 31, 2008 remained relatively consistent with the allocation at December 31, 2007. The moderate changes within the allocation were primarily attributable to assessment of risk within each category as well as changes in loan balances.

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

<PAGE> 20

Results of Operations - Executive Overview

Selected income statement and per share data and operating ratios are presented in the table below for the three-month periods indicated:

(In thousands, except per share data)	For the three-month periods ended				
	March 31, 2008	December 31, 2007	September 30, 2007	June 30, 2007	March 31, 2007
Income statement data:					
Net interest income	\$10,304	\$10,459	\$10,265	\$10,292	\$10,228
Noninterest income	2,903	2,703	2,856	2,664	2,562
Noninterest expense	9,460	9,398	9,492	9,624	9,511
Net income	2,326	2,395	2,278	2,194	2,178
Per share data:					
Diluted earnings per share	\$ 0.50	\$ 0.50	\$ 0.46	\$ 0.44	\$ 0.44
Dividends per common share	0.16	0.16	0.16	0.15	0.15
Operating ratios:					
Net interest margin	2.97%	2.98%	2.91%	2.97%	2.97%
Return on average assets	0.64%	0.65%	0.61%	0.60%	0.61%
Return on average equity	8.23%	8.21%	7.79%	7.63%	7.79%
Efficiency ratio	71.63%	71.40%	72.34%	74.28%	74.36%

The Company's 2008 first quarter net income of \$2.3 million decreased by \$69,000, or 2.9%, from the prior quarter (three months ended December 31, 2007). Net income was up \$148,000, or 6.8%, on a comparative quarter basis (as compared to the three months ended March 31, 2007). Diluted earnings per common share ("EPS") was up 0.5% on a linked-quarter basis (as compared to the three months ended December 31, 2007) and increased 14.2% as compared to the same quarter a year ago.

The first quarter 2008 net interest income decreased by \$155,000, or 1.5%, as compared to the fourth quarter of 2007. The yield on earning assets declined 25 basis points ("bps"), while the cost of liabilities fell 31 bps. These decreases were due in large part to the 200 bps reduction of the Federal Funds rate in the first quarter of 2008.

Compared to the first quarter of 2007, net interest income increased by \$76,000, or 0.7%, with decreases in the yield of earning assets of 22 bps being outpaced by decrease in the cost of funds of 30 bps. Available funds from deposit growth, loan repayments and calls of investment securities were redeployed into commercial loan growth and mortgage-backed securities. The Company's disciplined deposit pricing enabled the Company to hold its net interest margin steady on both a linked-quarter and comparative quarter basis despite the reduction in key benchmark interest rates.

Noninterest income for the first quarter of 2008 increased on a linked-quarter basis by \$200,000. The 2008 first quarter benefited from a gain on the sale of available for sale securities of \$242,000 and increases in commissions on nondeposit investment products, which were up \$72,000. Partially offsetting these increases were lower service charges on deposits accounts (down \$53,000) and other income (down \$56,000). In comparison to the 2007 first quarter, noninterest income was up \$341,000 for the 2008 first quarter. Service charges on deposit accounts increased by \$119,000 compared to the first quarter 2007. This increase, as well as available for sale security gains and increases in commissions on nondeposit investment products, more than offset the decline in gains on lease sales and commissions on loans originated for others compared to the same period a year ago.

Noninterest expenses for the current quarter increased moderately on a linked-quarter basis by \$62,000, or 0.7%, with increases in salaries and employee benefits, reflective of timing of payroll taxes, and higher professional services costs. First quarter 2008 noninterest expenses decreased \$51,000, or 0.5%, compared to

<PAGE> 21

the first quarter of 2007. Salaries and employee benefits costs declined \$123,000, or 2.3%, compared to the first quarter a year ago. Additionally, occupancy expense decreased \$41,000, or 4.5%. Within the net decrease in noninterest expenses were increases in loan workout costs of \$147,000 compared to \$9,000 of loan workout costs incurred in the first quarter of 2007.

The Company's key operating ratios (return on average assets, return on average equity, and efficiency ratio) for the first quarter of 2008 were consistent on a linked-quarter basis, while these metrics improved compared to the first quarter of 2007. The Company continues to focus on controlling the growth of expenses as part of its efforts to improve earnings and build shareholder value.

Results of Operations - Comparison of the Three Months Ended March 31, 2008 and 2007

Net Interest Income

Net interest income for the quarter ended March 31, 2008 was up \$76,000, or 0.7%, from the \$10.2 million earned in the first quarter of 2007. The first quarter 2008 net interest margin of 2.97% was equal to the net interest margin for the first quarter of 2007. Average earning assets were \$6.5 million, or 0.5% higher, and

average interest-bearing liabilities were \$13.5 million, or 1.2%, higher, than the comparable period a year earlier.

<PAGE> 22

Average Balances, Yields and Costs - The following table sets forth certain information relating to the Company's average balance sheet and reflects the average yield on assets and average cost of liabilities for the three month periods indicated. Such yields and costs are derived by dividing income or expense by the average balance of assets or liabilities. Average balances are derived from daily balances and include nonperforming loans. Available for sale securities are stated at amortized cost.

(In thousands)

For the three months ended March 31,

Assets	2008			2007		
	Average Balance	Interest Earned/ Paid	Average Yield	Average Balance	Interest Earned/ Paid	Average Yield
Earning assets:						
Overnight investments	\$ 22,766	\$ 197	3.48%	\$ 21,329	\$ 287	5.46%
Investment securities	58,689	701	4.78%	107,614	1,333	4.96%
Mortgage-backed securities	259,215	3,232	4.99%	239,235	2,869	4.80%
Stock in the FHLB	15,671	237	6.08%	15,881	281	7.18%
Loans receivable:						
Commercial loans and leases	575,488	9,806	6.85%	520,279	9,479	7.38%
Residential mortgage loans	243,681	3,296	5.41%	260,714	3,501	5.37%
Consumer and other loans	214,093	3,063	5.75%	218,020	3,352	6.24%
Total earning assets	1,389,603	20,532	5.93%	1,383,072	21,102	6.15%
Cash and due from banks	26,788			23,282		
Allowance for loan and lease losses	(12,686)			(12,391)		
Premises and equipment	13,586			14,757		
Goodwill, net	11,869			11,317		
Accrued interest receivable	5,238			5,685		
Bank-owned life insurance	24,279			23,232		
Prepaid expenses and other assets	6,559			9,428		

Edgar Filing: CARVER BANCORP INC - Form 10-Q

Total assets	\$1,465,236			\$1,458,382		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Deposits:						
NOW accounts	\$ 58,288	68	0.47%	\$ 64,285	101	0.64%
Money market accounts	6,085	29	1.91%	6,660	38	2.29%
Savings accounts	393,259	2,487	2.54%	361,539	2,472	2.77%
Certificate of deposit accounts	373,764	4,108	4.42%	392,144	4,440	4.59%
Overnight and short-term borrowings	62,132	431	2.79%	53,466	667	5.06%
Wholesale repurchase agreements	10,000	135	5.32%	15,778	196	4.97%
FHLB borrowings	245,549	2,720	4.46%	236,584	2,591	4.44%
Subordinated deferrable interest debentures	13,403	250	7.48%	18,558	369	8.02%
Total interest-bearing liabilities	1,162,480	10,228	3.54%	1,149,014	10,874	3.84%
Noninterest-bearing deposits	170,641			180,781		
Other liabilities	18,409			15,234		
Total liabilities	1,351,530			1,345,029		
Shareholders' Equity:	113,706			113,353		
Total liabilities and shareholders' equity	\$1,465,236			\$1,458,382		
Net interest income		\$10,304			\$10,228	
Net interest rate spread			2.39%			2.31%
Net interest rate margin			2.97%			2.97%

Rate/Volume Analysis - The following table sets forth certain information regarding changes in the Company's interest income and interest expense for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in rate (changes in rate multiplied by old average balance) and (ii) changes in volume (changes in average balances multiplied by old rate). The net change attributable to the combined impact of rate and volume was allocated proportionally to the individual rate and volume changes.

(In thousands)	Three Months Ended March 31, 2008 vs. 2007		
	Increase/(decrease) due to		
	Rate	Volume	Total
Interest income:			
Overnight investments	\$ (108)	\$ 18	\$ (90)
Investment securities	(49)	(583)	(632)
Mortgage-backed securities	116	247	363
Stock in the FHLB	(41)	(3)	(44)
Commercial loans and leases	(775)	1,102	327
Residential mortgage loans	26	(231)	(205)
Consumer and other loans	(248)	(41)	(289)
Total interest income	(1,079)	509	(570)
Interest expense:			
NOW accounts	(24)	(9)	(33)
Money market accounts	(6)	(3)	(9)
Savings accounts	(206)	221	15
Certificate of deposit accounts	(154)	(178)	(332)
Overnight and short-term borrowings	(333)	97	(236)
Wholesale repurchase agreements	13	(74)	(61)
FHLB borrowings	1	128	129
Subordinated deferrable interest debentures	(24)	(95)	(119)
Total interest expense	(733)	87	(646)
Net interest income	\$ (346)	\$ 422	\$ 76

Interest Income - Investments - Total investment income (consisting of interest on overnight investments, investment securities and MBSs and dividends on FHLB stock) was \$4.4 million for the quarter ended March 31, 2008, compared to \$4.8 million for the 2007 period. The decrease in total investment income of \$403,000, or 8.4%, was primarily attributable to lower average balances.

The Company intends to redeploy cash flows available from maturing investment securities and MBSs primarily into higher-yielding internally generated assets, such as commercial loans and leases. With respect to

duration and repricing of the Company's available for sale investment portfolio, the majority of the Company's investments are comprised of U.S. Agency securities and MBSs with repricing periods or expected duration of less than five years.

Interest Income - Loans and Leases - Interest from loans and leases was \$16.2 million for the quarter ended March 31, 2008, and represented a yield on total loans and leases of 6.28%. This compares to \$16.3 million of interest, and a yield of 6.60%, for the first quarter of 2007. Interest income decreased \$167,000, or 1.0%, with the decrease in yield on loans and leases of 32 bps partially offset by the increase in the average balance of loans and leases of \$34.2 million, or 3.4%.

The average balance of the various components of the loan and lease portfolio changed from the first quarter of 2007 as follows: commercial loans and leases increased \$55.2 million, or 10.6%, residential mortgage loans decreased \$17.0 million, or 6.5%, while consumer and other loans decreased \$3.9 million, or 1.8%. Changes in the average yields from the first quarter of 2007 were as follows: commercial loans and

<PAGE> 24

leases decreased 53 bps, to 6.85%, and consumer and other loans decreased 49 bps, to 5.75%, while residential mortgage loans increased 4 bps, to 5.41%. Downward repricing of variable rate assets impacted the yields on loans and leases in the first quarter of 2008.

Interest Expense - Deposits and Borrowings - Interest paid on deposits and borrowings decreased \$646,000, or 5.9%, to \$10.2 million for the three months ended March 31, 2008, down from \$10.9 million for the same period during 2007. The overall average cost for interest-bearing liabilities decreased 30 bps to 3.54% for the first quarter of 2008, compared to 3.84% for the first quarter of 2007. The average balance of total interest-bearing liabilities for the three months ended March 31, 2008 was \$1.16 billion, up from \$1.15 billion for the same period during 2007.

The growth in deposit average balances was centered in savings accounts (up \$31.7 million, or 8.8%). The increase was somewhat countered by decreases in CDs (down \$18.4 million, or 4.7%), NOW accounts (down \$6.0 million, or 9.3%) and money market accounts (down \$575,000, or 8.6%).

Borrowings increased as compared to the first quarter of 2007, with increases in customer short-term borrowings (up \$8.7 million, or 16.2%) and FHLB funding (up \$9.0 million, or 3.8%), slightly offset by a decrease in wholesale repurchase agreements (down \$5.8 million, or 36.6%). Additionally, the average balance of subordinated deferrable interest debentures declined \$5.2 million, or 27.8%, resulting from the Company's September 2007 redemption of the subordinated deferrable interest debentures held by BRI Statutory Trust II.

The decrease in deposit and borrowing costs was primarily attributable to the reduction of the Federal Funds rate by 200 bps in the first quarter of 2008. However, market competition from bank and non-bank financial institutions continues to be strong in the Company's market area, as does customer demand for higher-yielding deposit products. These two factors, as well as contractual maturities on borrowings and CDs, partially limit the Company's ability to reduce its deposit and borrowing costs as quickly as benchmark rate decreases.

Overall, the Company's liability costs continue to be dependent upon a number of factors including general economic conditions, national and local interest rates, competition in the local deposit marketplace, interest rate tiers offered and the Company's cash flow needs.

Provision for Loan and Lease Losses

The provision for loan and lease losses was \$285,000 for the quarter ended March 31, 2008, up \$185,000 from the first quarter of 2007. The Bank made additions to the allowance for loan and lease losses during the first quarter of 2008 primarily in response to higher charge-offs compared to the prior year first quarter, increased nonperforming loans since December 31, 2007 and general economic conditions.

Management evaluates several factors including new loan originations, actual and estimated charge-offs and the risk characteristics of the loan and lease portfolio and general economic conditions when determining the provision for each quarter. As the loan portfolio continues to grow and mature, or if economic conditions worsen, management believes it possible that the level of nonperforming assets may increase, which in turn may lead to increases in the provision for loan and lease losses. Also see discussion under "*Allowance for Credit Losses*."

Noninterest Income

Total noninterest income increased \$341,000, or 13.3%, to \$2.9 million for the first quarter of 2008, from \$2.6 million for the first quarter of 2007. The first quarter benefited from gross gains on the sale of available for sale securities of \$242,000, while there were no security sales in the first quarter of 2007. Service charges on deposit accounts also increased compared to the first quarter of 2007, with an increase of \$119,000, or 9.0%, primarily due to an increase in cash management account fees and deposit fee enhancement programs. Commissions on nondeposit investment products also increased by \$90,000, or 75.0%, compared to the first quarter of 2007. These increases were partially offset by lower gains on lease sales and loan commissions,

<PAGE> 25

which were down \$168,000, or 43.4%. In the first quarter of 2008, the Company originated more leases for its own portfolio versus for sale as compared to the same period a year ago.

Noninterest Expense

Noninterest expense for the first quarter of 2008 of \$9.5 million decreased \$51,000, or 0.5%, compared to the first quarter of 2007. This moderate decrease reflected the Company's ongoing initiatives to control expense growth.

Salaries and benefits costs decreased \$123,000, or 2.3%, compared to the first quarter a year ago, with savings in salaries expense due to reallocation of positions in the Company's retail branch network, as well as in its back-office operations area. Additionally, occupancy costs declined by \$41,000, or 4.5%, benefiting in part from the Company's decision to transfer its rights to develop a planned branch site to a third party. The Company also had decreases in loan servicing, equipment, professional services and marketing costs.

Loan workout costs increased in the first quarter of 2008 compared to the same period a year ago by \$147,000, or 1,633.3%, reflective of increased costs. The Company had experienced lower than normal workout costs in the first part of 2007, whereas the current period costs were consistent with costs incurred in the previous quarter, the three months ended December 31, 2007. Data processing costs remained relatively consistent with the \$704,000 incurred in the first quarter of 2007, up only \$15,000, or 2.1%.

Other miscellaneous expenses increased by \$28,000, or 2.6%, compared to the same period a year ago. This net increase was primarily driven by increases in FDIC insurance costs of \$70,000 being partially offset by lower provisions to the reserve for unused commitments of \$50,000. Overall, with the net decrease in noninterest expenses, the Company improved its efficiency ratio in the first quarter of 2008 to 71.63% from 74.36% in the first quarter of 2007.

Income Tax Expense

Income tax expense of \$1.1 million was recorded for the three months ended March 31, 2008, compared to \$1.0 million for the same period during 2007. This represented total effective tax rates of 32.8% and 31.5%, respectively. Tax-favored income from BOLI, along with the Company's utilization of a Rhode Island passive investment company, has reduced the effective tax rate from the 40.9% combined statutory federal and state tax rates.

Liquidity and Capital Resources

Liquidity

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

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

Management is responsible for establishing and monitoring liquidity targets as well as strategies and tactics to meet these targets. In general, the Company seeks to maintain a high degree of flexibility with a liquidity target of 10% to 30% of total assets. At March 31, 2008, overnight investments, investment securities and MBSs available for sale amounted to \$375.6 million, or 25.2% of total assets. This compares to \$352.3 million, or 23.8% of total assets at December 31, 2007. The Bank is a member of the FHLB and, as such, has access to both short- and long-term borrowings. In addition, the Bank maintains a line of credit at the FHLB as well as a line of credit with a correspondent bank. The Bank also has access to funding through

<PAGE> 26

wholesale repurchase agreements. There have been no adverse trends in the Company's liquidity or capital reserves. Management believes that the Company has adequate liquidity to meet its commitments.

Capital Resources

Total shareholders' equity of the Company at March 31, 2008 was \$114.8 million, as compared to \$113.1 million at December 31, 2007. This difference of \$1.7 million was the result of net income of \$2.3 million, proceeds from the exercise of stock options and related tax effects of \$609,000, contingent share payments of \$362,000, increase in accumulated other comprehensive income of \$941,000 (attributable to increases in net unrealized gains on investments and MBSs) and non-cash share-based compensation of \$68,000. Partially offsetting the aforementioned items were dividend payments of \$717,000 and stock repurchases of \$1.9 million.

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

Edgar Filing: CARVER BANCORP INC - Form 10-Q

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

As of March 31, 2008, the Company and the Bank met all applicable minimum capital requirements and were considered "well capitalized" by both the FRB and the FDIC.

The Company's and the Bank's actual and required capital amounts and ratios are as follows:

	Actual		Minimum Required For Capital Adequacy Purposes		Minimum Required To Be Considered "Well Capitalized"	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<u>(Dollars in thousands)</u>						
At March 31, 2008:						
<u>Bancorp Rhode Island, Inc.</u>						
Tier I capital (to average assets)	\$114,938	7.92%	\$58,054	4.00%	\$ 72,568	5.00%
Tier I capital (to risk weighted assets)	114,938	11.35%	40,513	4.00%	60,770	6.00%
Total capital (to risk weighted assets)	127,531	12.59%	81,027	8.00%	101,284	10.00%
<u>Bank Rhode Island</u>						
Tier I capital (to average assets)	\$113,848	7.85%	\$58,030	4.00%	\$ 72,537	5.00%
Tier I capital (to risk weighted assets)	113,848	11.25%	40,481	4.00%	60,721	6.00%
Total capital (to risk weighted assets)	126,441	12.49%	82,962	8.00%	101,202	10.00%
At December 31, 2007:						
<u>Bancorp Rhode Island, Inc.</u>						
Tier I capital (to average assets)	\$114,403	7.87%	\$58,119	4.00%	\$ 72,649	5.00%
Tier I capital (to risk weighted assets)	114,403	11.06%	41,361	4.00%	62,042	6.00%
Total capital (to risk weighted assets)	127,022	12.28%	82,722	8.00%	103,403	10.00%
<u>Bank Rhode Island</u>						
Tier I capital (to average assets)	\$112,323	7.72%	\$58,165	4.00%	\$ 72,706	5.00%

Tier I capital (to risk weighted assets)	112,323	10.87%	41,325	4.00%	61,987	6.00%
Total capital (to risk weighted assets)	124,942	12.09%	82,650	8.00%	103,312	10.00%

<PAGE> 27

BANCORP RHODE ISLAND, INC.
Quantitative and Qualitative Disclosures About Market Risk

ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Risk

The principal market risk facing the Company is interest rate risk. The Company's objective regarding interest rate risk is to manage its assets and funding sources to produce results which are consistent with its liquidity, capital adequacy, growth and profitability goals, while maintaining interest rate risk exposure within established parameters over a range of possible interest rate scenarios.

Interest rate risk management is governed by the Bank's Asset/Liability Committee ("ALCO"). The ALCO establishes exposure limits that define the Company's tolerance for interest rate risk. The ALCO monitors current exposures versus limits and reports results to the Board of Directors. The policy limits and guidelines serve as benchmarks for measuring interest rate risk and for providing a framework for evaluation and interest rate risk management decision making. The primary tools for managing interest rate risk currently are the securities portfolio, purchased mortgages, wholesale repurchase agreements and borrowings from the FHLB.

The Company's interest rate risk position is measured using both income simulation and interest rate sensitivity "gap" analysis. Income simulation is the primary tool for measuring the interest rate risk inherent in the Company's balance sheet at a given point in time by showing the effect on net interest income, over a 24-month period, of 200 bps interest rate ramps. These simulations take into account repricing, maturity and prepayment characteristics of individual products. The ALCO reviews simulation results to determine whether the exposure resulting from changes in market interest rates remains within established tolerance levels over both a 12-month and 24-month horizon, and develops appropriate strategies to manage this exposure. The Company's guidelines for interest rate risk specify that if interest rates were to shift up or down 200 bps over a 12-month and 24-month period, estimated net interest income should decline by no more than 10.0%. As of March 31, 2008, net interest income simulation indicated that the Company's exposure to changing interest rates was within these tolerances. The ALCO reviews the methodology utilized for calculating interest rate risk exposure and may periodically adopt modifications to this methodology.

The following table presents the estimated impact of interest rate ramps on the Company's estimated net interest income over a twenty-four month period beginning April 1, 2008:

Estimated Exposure to Net Interest Income	
Dollar Change	Percent Change
(Dollars in thousands)	

Initial Twelve Month Period:

Up 200 bps	\$ (249)	-0.6%
Down 200 bps	(791)	-1.8%

Subsequent Twelve Month Period:

Up 200 bps	\$ 230	0.5%
Down 200 bps	(4,341)	-9.9%

<PAGE> 28

The Company also uses interest rate sensitivity "gap" analysis to provide a more general overview of its interest rate risk profile. The interest rate sensitivity gap is defined as the difference between interest-earning assets and interest-bearing liabilities maturing or repricing within a given time period. At March 31, 2008, the Company's one year cumulative gap was a positive \$80.9 million, or 5.4% of total assets.

For additional discussion on interest rate risk see the section titled "Asset and Liability Management" on pages 57 through 58 of the Company's 2007 Annual Report on Form 10-K.

ITEM 4. Controls and Procedures

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Company carried out an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. This evaluation was carried out under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer. Based upon that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

There was no significant change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to affect, the Company's internal control over financial reporting. The Company continues to enhance its internal controls over financial reporting, primarily by evaluating and enhancing process and control documentation. Management discusses with and discloses these matters to the Audit Committee of the Board of Directors and the Company's auditors.

<PAGE> 29

BANCORP RHODE ISLAND, INC.
Other Information

PART II. Other Information

Item 1. Legal Proceedings

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

Item 1A. Risk Factors

There have been no material changes from the risk factors as previously disclosed in the Company's 2007 Annual Report on Form 10-K.

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

In 2005, the Company, through its Macrolease subsidiary, purchased substantially all of the operating assets of DWW Leasing Corp. (formerly Macrolease International Corporation) (the "Seller") pursuant to the terms of an Asset Purchase Agreement dated April 29, 2005 among the Company, the Bank, Macrolease, the Seller and certain shareholders of the Seller (the "Agreement"). Pursuant to the terms of the Agreement, on March 27, 2008, the Company issued 10,764 shares of its common stock to the Seller, which shares represented additional consideration contingent upon Macrolease achieving certain performance goals for 2007, which were met. These additional shares were issued in a private placement pursuant to Section 4(2) of the Securities Act of 1933. In addition, the Company has reserved up to 31,728 additional shares of its common stock for issuance to the Seller in the event Macrolease achieves certain performance goals over the four months remaining in a three-year performance period and pursuant to an earn-out through 2010. The Company has filed a registration statement on Form S-3 covering up to 51,532 shares of its common stock issued or reserved for issuance to the Seller, which registration statement was declared effective on July 12, 2005.

The table below summarizes the Company's repurchases of common stock during the quarter ended March 31, 2008:

Period	Total number of shares purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Announced Plan (a)	Maximum number of shares that may yet be purchased under the plan
1/1/08 through 1/31/08	39,600	\$33.53	39,600	0
2/1/08 through 2/29/08	--	--	--	0
3/1/08 through 3/31/08	--	--	--	0

- (a) The Company has maintained a stock repurchase program authorized by the Company's board of directors, which has enabled the Company to proactively manage its capital position. The program, which was initially approved on April 18, 2006, authorized the Company to repurchase up to 245,000 shares of its common stock from time to time through open market or privately negotiated purchases. On November 26, 2007, the Company expanded the stock repurchase program to 345,000 shares and also adopted a written purchase plan pursuant to Rule 10b5-1 of the Securities Exchange Act of 1934, as amended. The Company concluded its repurchase program this quarter. Additionally, in February 2008, the Company's Chief Executive Officer delivered 7,450 shares of the Company's common stock to satisfy the exercise price for 20,000 stock options exercised. The shares delivered were valued at \$33.30 per share. The Chief Executive officer paid the balance of the exercise price and all taxes in cash.

Item 3. Defaults Upon Senior Securities

No defaults upon senior securities have taken place.

<PAGE> 30

Item 4. Submission of Matters to a Vote of the Security Holders

No information to report.

Item 5. Other Information

No information to report.

Item 6. Exhibits

- | | |
|---------|--|
| 10.1(a) | First Amendment to Amended and Restated Executive Employment Agreement between Merrill W. Sherman, Bancorp Rhode Island, Inc. and Bank Rhode Island dated as of March 6, 2008. |
| 31.1 | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
- <PAGE> 31

BANCORP RHODE ISLAND, INC.

SIGNATURES

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

Bancorp Rhode Island, Inc.

May 8, 2008

(Date)

/s/ Merrill W. Sherman

Merrill W. Sherman
President and
Chief Executive Officer

May 8, 2008

(Date)

/s/ Linda H. Simmons

Linda H. Simmons
Chief Financial Officer
and Treasurer

<PAGE> 32