EMCLAIRE FINANCIAL CORP
Form 10QSB
August 13, 2001

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-QSB

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2001

OR

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES ACT OF 1934

For the transition period from ______________ to ______________

Commission file Number: 000-18464

EMCLAIRE FINANCIAL CORP.
(Exact Name of small business issuer as specified in its charter)

PENNSYLVANIA	25-1606091
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)

612 Main Street	
Emlenton, PA	16373
(Address of principal executive offices)	(Zip Code)

Issuer's telephone number, including area code: (724) 867-2311

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ___ No X

As of August 9, 2001, there were 1,332,835 shares outstanding of the issuer's common stock, par value $1.25 per share.

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EMCLAIRE FINANCIAL CORP.
CONSOLIDATED BALANCE SHEET
(Unaudited - dollars in thousands)

	June 30, 2001	Dec
ASSETS		
Cash and due from banks	$ 6,396	$
Federal funds sold	7,960	
Investment securities		
Available for sale	26,882	
Held to maturity (estimated market value		

of $216 and $213)	216	
Loans	153,851	
Less allowance for loan losses	1,464	
Net loans	152,387	
Premises and equipment	3,213	
Accrued interest and other assets	5,085	
TOTAL ASSETS	$ 202,139	$
LIABILITIES		
Deposits		
Noninterest bearing demand	$ 28,621	$
Interest bearing demand	20,750	
Savings	21,196	
Money market	27,334	
Time	82,659	
Total deposits	180,560	
Borrowed funds	--	
Accrued interest and other liabilities	966	
TOTAL LIABILITIES	181,526	
STOCKHOLDERS' EQUITY		
Preferred stock, par value $1.00; 3,000,000 shares authorized; none issued	--	
Common stock, par value $1.25; 12,000,000 shares authorized; 1,395,852 shares issued	1,745	
Additional paid-in capital	10,871	
Retained earnings	8,679	
Accumulated other comprehensive income	289	
Treasury stock at cost (63,017 shares)	(971)	
TOTAL STOCKHOLDERS' EQUITY	20,613	
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 202,139	$

See accompanying notes to the consolidated financial statements.

EMCLAIRE FINANCIAL CORP.
CONSOLIDATED STATEMENT OF INCOME
(Unaudited - dollars in thousands, except per share amounts)

Three Months Ended June 30,	Six

	2001	2000	20
INTEREST INCOME			
Loans, including fees	$ 3,150	$ 3,097	$
Interest bearing deposits in other banks	1	3	
Federal funds sold	88	3	
Investment securities:			
Taxable	325	411	
Exempt from federal income tax	92	83	
Total interest income	3,656	3,597	
INTEREST EXPENSE			
Deposits	1,571	1,375	
Borrowed funds	3	54	
Total interest expense	1,574	1,429	
NET INTEREST INCOME	2,082	2,168	
Provision for loan losses	36	51	
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	2,046	2,117	
OTHER OPERATING INCOME			
Service fees on deposit accounts	247	223	
Other	97	75	
Total other operating income	344	298	
OTHER OPERATING EXPENSE			
Salaries and employee benefits	935	867	
Occupancy, furniture and equipment	268	268	
Other	590	621	
Total other operating expense	1,793	1,756	
Income before income taxes	597	659	
Income taxes	176	199	
NET INCOME	$ 421	$ 460	$
EARNINGS PER SHARE	$ 0.32	$ 0.34	$
DIVIDENDS PER SHARE	0.17	0.15	
AVERAGE SHARES OUTSTANDING	1,332,835	1,348,245	1,33

See accompanying notes to the consolidated financial statements.

EMCLAIRE FINANCIAL CORP.
CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited - dollars in thousands)

	Six Months Ended J
	2001
OPERATING ACTIVITIES	
Net income	$ 812
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization	435
Net amortization of investment security discounts and premiums	1
Provision for loan losses	82
Decrease (increase) in accrued interest receivable	81
Increase (decrease) in accrued interest payable	(25)
Other, net	(130)
Net cash provided by operating activities	1,256
INVESTING ACTIVITIES	
Proceeds from maturities and repayments of investment securities:	
Available for sale	3,951
Held to maturity	3
Purchases of investment securities:	
Available for sale	(4,049)
Net loan originations	(2,228)
Purchases of premises and equipment	(92)
Proceeds from sales of premises and equipment	2
Proceeds from sale of foreclosed assets	21
Net cash used for investing activities	(2,392)
FINANCING ACTIVITIES	
Net increase in deposits	9,435
Increase (decrease) in short-term borrowings	(2,000)
Acquisition of treasury stock	--
Cash dividends paid, including fractional shares	(453)
Net cash provided by provided by financing activities	6,982
Increase (decrease) in cash and cash equivalents	5,846
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	8,510
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 14,356

See accompanying notes to the consolidated financial statements.

EMCLAIRE FINANCIAL CORP.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. GENERAL

The accounting and financial reporting polices of Emclaire Financial Corp. and its wholly-owned subsidiary The Farmers National Bank of Emlenton ("Bank" or "Farmers"), conform to accounting principles generally accepted in the United States of America and to general practice within the banking industry. In the opinion of management, the accompanying unaudited consolidated financial statements of Emclaire Financial Corp. ("Company" or "Emclaire") contain all adjustments, consisting of only normal and recurring adjustments, necessary for the fair presentation of the Company's financial position, results of operations and cash flows for the periods presented. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year.

2. EARNINGS PER SHARE

The Company maintains a simple capital structure; therefore there are no dilutive effects on earnings per share. As such earnings per share computations are based on the weighted average number of shares outstanding of 1,332,835, 1,348,245, and 1,332,835, 1,356,662, for the three and six month periods in 2001 and 2000, respectively.

3. RECLASSIFICATION

Common stocks of the Federal Home Loan Bank and the Federal Reserve Bank have been classified as other assets to conform to the current period presentation. In prior periods these items had been presented as investment securities available for sale.

4. COMPREHENSIVE INCOME

The components of comprehensive income consist exclusively of unrealized gains and losses on securities available for sale. For the six months ended June 30, 2001, this activity is shown under the heading Accumulated Other Comprehensive Income as presented in the Consolidated Statement of Changes in Stockholders' Equity. For the six months ended June 30, 2000, comprehensive net income totaled $377,000. For the three months ended June 30, 2001 and 2000, comprehensive income totaled $414,000 and $514,000, respectively.

5. LOANS

Major classifications of loans are summarized as follows (in thousands):

	June 30, 2001	December 31, 2000

Commercial, industrial and other	$ 20,923	$ 20,084
Real estate mortgages		
Residential	93,986	92,429
Commercial and other	24,561	24,661
Consumer	14,381	14,618
	153,851	151,792
Less allowance for loan losses	1,464	1,460
	$152,387	$150,332

The Bank's primary business activity is with customers located within Venango, Clarion, Butler, Elk, Clearfield and Jefferson Counties. Commercial, residential, personal, and agricultural loans are granted. Although the Bank has a diversified loan portfolio at June 30, 2001 and December 31, 2000, loans outstanding to individuals and businesses are dependent upon the local economic conditions within the immediate trade area.

NOTE 6 - RECENT ACCOUNTING PRONOUNCEMENTS

In July 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 141, Business Combinations, effective for all business combinations initiated after June 30, 2001, as well as all business combinations accounted for by the purchase method that are completed after June 30, 2001. The new statement requires that the purchase method of accounting be used for all business combinations and prohibits the use of the pooling-of-interests method. The adoption of Statement No. 141 is not expected to have a material affect on the Company's financial position or results of operations.

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, effective for fiscal years beginning after December 15, 2001. The new statement changes the accounting for goodwill from an amortization method to an impairment-only approach. Thus, amortization of goodwill, including goodwill recorded in past business combinations, will cease upon adoption of this Statement. At June 30, 2001, the Company had approximately $1,487,000 of identified goodwill from business combinations and branch acquisitions that is currently being amortized on a straight-line basis of $135,000 per year over 13 years. Management is currently reviewing the effect this Statement will have on the Company's financial position and results of operations.

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

Emclaire Financial Corp. ("Emclaire" or the "Company") is the parent holding company for the Farmers National Bank of Emlenton ("Farmers" or the "Bank"). The following discussion and analysis is intended to provide information about the financial condition and results of operation of the Company and should be read in conjunction with the consolidated financial statements and the related notes thereto appearing elsewhere in this quarterly report.

Certain information presented in this report and other statements concerning future performance, developments or events, and expectations for growth and market forecasts constitute forward-looking statements which are subject to a number of risks and uncertainties, including interest rate fluctuations, changes in local or national economic conditions, and government and regulatory actions which might cause actual results to differ materially from stated expectations or estimates. The Company does not undertake, and specifically disclaims any obligation, to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

Comparison of the Three Months Ended June 30, 2001 and 2000

Net Income - Net income for the three months ended June 30, 2001 totaled $421,000 or $.32 per share, as compared to $460,000 or $.34 per share during the same period in 2000. The 2001 quarterly earnings represented a decrease of $39,000 or 8% from the same period in 2000. A decline in net interest income of $86,000 combined with an increase in operating costs, which rose $37,000, was offset by improved fee income of $46,000, resulted in the net earnings decrease. On a per share basis, net income declined 6% to $.32 due to the reduced net earnings for the period.

The net income reported resulted in annualized returns on average assets and average equity of .85% and 8.25% for the quarter ended June 30, 2001, as compared to returns of .95% and 8.96% for the same period in 2000.

Net Interest Income - Tax-equivalent net interest income decreased $89,000 or 4% during the second quarter of 2001 as compared to the same period in 2000. The increase in the volume and rate paid on interest bearing liabilities, particularly certificates of deposit caused interest expense to increase $145,000 or 10% during the second quarter of 2001 as compared to the same period in 2000, as the average cost of funds increased 21 basis points to 4.20%. The increased interest cost exceeded the $56,000 or 2% increase in tax equivalent interest income. Tax equivalent interest income on loans increased $46,000 due largely to the $4.1 million increase in average loan volume, as the average balance on loans totaled $152.6 million for the second quarter of 2001. Deposit growth and maturities of investment securities funded this growth in loan volume. Investment maturities caused tax equivalent investment interest income to fall $73,000 or 14%. Additional liquidity provided by the growth in deposits caused the average volume of federal funds to rise $7.8 million, increasing interest income on federal funds from $85,000 to $88,000. The net tax-equivalent yield on earning assets for the quarter was 4.53%, a 37 basis point decline from the 4.90% yield earned during the same period in 2000.

Average earning assets totaled $188.9 million for the second quarter of 2001 representing 94.0% of total average assets. For the same period in 2000, average earning assets totaled $182.4 million or 93.4% of total average assets.

Tax equivalent interest income rose $56,000 or 1.5% during the second quarter of 2001, as compared to the same period in 2000, due to the increased loan volume that was offset by slightly lower interest rates. The tax-equivalent yield on the loan portfolio for the second quarter of 2001 declined 13 basis points to 8.29%, as compared to the same quarter of 2000. This decrease was due to the trend of rising interest rates during the first half of 2000. This trend ended in 2001 as the Federal Reserve Board has adopted a policy of aggressive interest rate reduction, lowering the federal funds rate 270 basis points since the beginning of 2001. It is reasonable to expect this trend to continue for at least the short-term. This shift in interest rates is expected to have an adverse impact on the yield on earning assets in relation to prior comparative periods during the remainder of 2001.

Interest expense increased $145,000 or 10.1% to $1.57 million during the second quarter of 2001, as compared to the same period in 2000. Increased rates accounted for $55,000 of the increase as the cost of these funds rose to 4.20%. The remainder of the increase resulted from an increase in the volume of average interest-bearing liabilities, which rose $6.1 million to $150.3 million due largely to the increase in time certificates of deposit as deposits were attracted during 2000 through the use of promotional certificates of deposits. The impact of these fixed rate certificates of deposit will remain, in varying degrees, for the next four quarters. During the first quarter of 2001 a premium money market deposit account was introduced, offering a market based interest rate on balances over a specified amount. This product will allow for the downward adjustment of interest rates during periods of declining interest rates.

Provision for Loan Losses - Based upon management's ongoing assessment of the quality of the loan portfolio, the provision for loan losses for the second quarter of 2001 totaled $36,000 as compared to $51,000 during the same period ended in 2000.

Other operating income - Other operating income increased $46,000 or 15% for the second quarter of 2001, due to an increase of approximately $24,000 in overdraft and service fees due to the restructuring of service charges in the second half of 2000. In addition, ATM convenience fees and fees generated from the MasterMoney(TM) debit card increased due to increased customer usage. Combined, these fees accounted for $35,000 of the total increase in other operating income. The cumulative effect of increases in other fees, commissions on accident health and life insurance and other income accounted for the remainder of the increase.

Other Operating Expense - Total other operating expense for the second quarter of 2001 increased $37,000 or 2.1% as compared to the same period in 2000. Increases in employee costs offset a decrease in other operating expense.

Due to the impact of normal, recurring annual salary adjustments, and several staff additions, salaries and employee benefits increased $68,000 or 8% for the second quarter of 2001 as compared to the same period in 2000. For the remainder of 2001 in

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comparison to 2000 the increase in salaries and benefits is expected to rise due to the Company converting its health care coverage to a health maintenance organization during the second quarter of 2000.

Other operating expense totaled $590,000 for the second quarter of 2001, a decrease of $31,000 or 5%, as compared to the same period of 2000. Intangible asset amortization declined $11,000 in the comparative quarters due to the revaluation of intangible assets during the fourth quarter of 2000 and the resulting reduction in monthly amortization. Combined with this reduction were savings of $6,000 related to customer check losses incurred in 2000 that were not repeated in the current quarter.

Income Taxes - Applicable income taxes for the second quarter of 2001 totaled $176,000 and represented 29.5% of pre-tax earnings. This comparable to the $199,000 recorded during the same period in 2000.

Comparison of the Six Months Ended June 30, 2001 and 2000

Net Income - Net income for the six months ended June 30, 2001 totaled $812,000, a decrease of $39,000 or 5% as compared to the first six months of 2000. On a per share basis earnings were $.61 per share, a 3% decrease from the $.63 reported in 2000. A decline in net interest income of $136,000 combined with an increase in operating costs of $89,000, was offset by improved fee income of $152,000, resulting in the net earnings decrease.

Net Interest Income - Net interest income on a tax equivalent basis decreased $145,000 or 3% for the comparative six-month periods due to the increase in time deposits volume as discussed in the quarterly earnings section of this report. For the six months ended June 30, 2001 average time deposits volume was $82.8 million, an increase of $9.3 million or 13% from 2000. During the same period the volume of interest-earning assets rose $6.1 million or 3% to $187.0 million. As discussed earlier, increases in time certificates of deposit were attracted during 2000 through the use of promotional certificates. The net tax equivalent yield for the first six months of 2001 was 4.58% as compared to 4.88% for the same period in 2000.

Other operating income - As previously discussed, increases resulted from the restructuring of service charges in the second half of 2000 and fees generated from increased customer usage of ATM's and the MasterMoney(TM) debit card. For the first half of 2001, other operating income rose $152,000 or 30% to $344,000.

Other Operating Expense - Other operating expense for the first half of 2001 totaled $3.6 million, an increase of $89,000 or 3%. The added salaries and related payroll taxes discussed earlier accounted for $110,000 of the increase. Offsetting this increase was a decrease in intangible asset amortization of $24,000 and a savings of $23,000 related to customer check losses incurred in 2000 that were not repeated in the current six-month period.

Financial Condition

At June 30, 2001 consolidated assets totaled $202.1 million an increase of $8.0 million or 4% from December 31, 2000. Deposits increased $9.4 million or 5% during the first

half of 2001. This increase, which is similar to that experienced throughout the industry, increased liquidity as federal funds sold rose $6.2 million.

The increase in deposits was largely due to the addition of a tiered rate money market account product introduced in February 2001. This account is designed to provide depositors a return on their funds at a level approximating that available from money market accounts offered by brokerages, plus the benefit of applicable federal deposit insurance. During the first half of 2001 money market deposits increased $7.9 million or 40% while certificates of deposit rose $1.2 million or 1.5% respectively. These increases more than offset the decline in NOW accounts of $942,000 or 4% during the first half of the year. A portion of the decline is due to funds migrating from NOW to the new money market account product.

Total loans increased $2.1 million to $153.9 million, primarily resulting from an increase of $1.5 million in other real estate loans and $839,000 in commercial loans from December 31, 2000. Management attributes the increases in other real estate loans and commercial loans to a lower interest rate environment, continued customer referrals and the Company's overall relationship with its customers.

Retained net earnings of $359,000 combined with a net increase in the accumulated other comprehensive income resulted in a net increase in stockholders' equity of $568,000 or 3% during the first half of 2001.

Liquidity

Cash and cash equivalents increased $5.8 million during the first half of 2001 and totaled $14.4 million at June 30, 2001. During the same period in 2000 cash and cash equivalents declined $1.4 million to $7.2 million.

Operating activities consisting principally of net income, depreciation and amortization provided $1,256,000 during the first half of 2001 as compared to $1,482,000 during the same period of 2000. This resulted primarily from a reduction in net income and intangible asset amortization as previously discussed.

Investing activities consist primarily of loan originations and repayments, and investment purchases and maturities. Investing activities during 2001 resulted in a net use of $2.4 million. Investment purchases and loan originations of $4.0 million and $2.2 million, respectively, were offset somewhat by investment repayment and maturities of $4.0 million. During the same period in 2000, investing activities used $5.1 million due largely to $10.7 million in net loan orginations that was offset by $6.0 million in investment repayment and maturities.

Financing activities for the first six months of 2001 provided approximately $7.0 million, due principally to net increase in deposits of $9.4 million that was offset by repayment of a $2.0 million Federal Home Loan Bank borrowing originally taken in 1997 and dividend payments of $453,000. During the same period of 2000, financing activities provided $2.2 million due to principally to an increase in short-term borrowings of $2.2 million and an increase in net deposits of $1.0 million that was offset by the use of $486,000 for the repurchase of common stock and $406,000 for dividend payments.

Aside from liquidity available from customer deposits or through sales and maturities of the investment portfolio, the Company has alternative sources of funds such as a line of credit available from the Federal Home Loan Bank. At June 30, 2001, this short-term revolving credit facility totaling $10 million was available.

Management is not aware of any conditions, including any regulatory recommendations or requirements, which would adversely affect its liquidity or its ability to meet funding needs in the ordinary course of business.

Risk Elements

At June 30, 2001, non-performing loans, including those past due ninety days or more, and loans on non-accrual status totaled approximately $1,154,000.

Of the non-performing loan total, $490,000 is considered to be impaired for financial reporting purposes. These impaired loans consist of four commercial loans to a single borrower, secured by real estate. The borrower continues operating under Chapter 11 bankruptcy protection. As part of management's ongoing assessment of the loan portfolio, $40,000 of the allowance for loan losses at June 30, 2001, has been allocated for these loans. During April 2001, a previous loan to this borrower totaling $50,000 was repaid in full, including non-accrual interest of $16,000. During the first half of 2001, the borrower made payments on the remaining loans totaling $29,000, of which $15,000 was recorded against principal and $14,000 was recorded as interest income. Management believes the underlying collateral, supporting the remaining loans, adequately secures the Company.

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The following table presents the components of non-performing loans and other non-performing assets as of the five most recent quarters ended:

	2001		20	
	June 30,	March 31,	December 31,	September 30,
Non-performing loans				
Loans past due 90 days or more	$ 172	$ 215	$ 158	$ 159
Non-accrual loans	982	698	742	909
Total non-performing loans	1,154	913	900	1,068
Other non-performing assets:				
Real estate acquired through foreclosure	62	65	33	40
Total other non-performing assets	62	65	33	40
Total non-performing assets	$1,216	$ 978	$ 933	$1,108
Non-performing loans as a percentage of total loans	.75%	.60%	.59%	.70%
Non-performing assets to assets	.60	.49	.48	.56

At June 30, 2001, based on the ongoing quarterly review and assessment of credit quality, management is not aware of any trends or uncertainties related to any accounts which might have a material adverse impact on future earnings, liquidity or capital resources. Based on the results of the quarterly internal loan review process, and considering the trend of past loan losses and recoveries, and current risk elements in the loan portfolio, management believes the allowance for loan losses at June 30, 2001 is adequate.

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PART II - OTHER INFORMATION

Item 1. Legal Proceedings

(None)

Item 2. Changes in Securities

(None)

Item 3. Defaults Upon Senior Securities

(None)

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

(a) The annual meeting of stockholders was held May 16, 2000. Of 1,332,835 shares eligible to vote, 1,120,628 or 84.1% were voted in person or by proxy.

(b) The following Class C directors were elected to a three year term expiring in 2003:

NAME	SHARES FOR	SHARES WITHHELD	BROKER NO VOTES
Rodney C. Heeter	1,049,734	70,894	100
J. Michael King	1,027,042	93,586	100
David L. Cox	1,119,380	1,248	100

In addition, to the above listed individuals, the following persons continue to serve as directors:

Ronald L. Ashbaugh
Bernadette H. Crooks
George W. Freeman
Elizabeth C. Smith
Robert L. Hunter
Brian C. McCarrier
John B. Mason

(c) The recommendation of the Board of Directors to ratify the appointment of S. R. Snodgrass, A.C. as the Company's independent auditors, as described in the Proxy Statement for the Annual Meeting, was approved with 1,116,268 shares in favor, and 4,360 shares against, and 100 shares abstaining.

Item 5. Other Information

On August 6, 2001, the Company hired William Marsh as the new Chief Financial Officer.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

(None)

(b) Reports on Form 8-K

On June 5, 2001, a Form 8-K (Item 5) was filed with the Securities and Exchange Commission to disclose the resignation of the Company's Secretary/Treasurer and Principal Accounting Officer.

SIGNATURES

In accordance with the requirements of the Exchange Act, the Registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Emclaire Financial Corp.
(Registrant)

Date: August 10, 2001

By: /s/ David L. Cox
David L. Cox
President and CEO