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FIRSTFED AMERICA BANCORP INC
Form 10-Q
February 14, 2002

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 DECEMBER 31, 2001

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 1-12305

FIRSTFED AMERICA BANCORP, INC.

(Exact name of registrant as specified in its charter)

DELAWARE

04-3331237

(State or other jurisdiction of (I.R.S. Employer Identification No.)
incorporation or organization)

ONE FIRSTFED PARK, SWANSEA, MASSACHUSETTS 02777

(Address of principal executive offices)

Registrant's telephone number, including area code: (508) 679-8181

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange 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 (X) No ()

As of February 1, 2002, there were 6,220,249 shares of the Registrant's Common Stock outstanding.

FIRSTFED AMERICA BANCORP, INC.

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SIGNATURES

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FIRSTFED AMERICA BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(IN THOUSANDS)

| ASSETS | DECEMBER 31, 2001 ---- | MARCH 31, 2001 ---- |
|---|------------------------------|---------------------------|
| | (UNAUDITED) | |
| Cash on hand and due from banks | \$ 26,607 | \$ 23,013 |
| Short-term investments | 36,780 | 200 |
| | ----- | ----- |
| Total cash and cash equivalents | 63,387 | 23,213 |
| Mortgage loans held for sale | 67,280 | 39,103 |
| Investment in trading securities, at fair value | 528 | 815 |
| Investment securities available for sale, at fair value (amortized cost of \$21,330 and \$6,405) | 23,939 | 7,837 |

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| | | |
|---|--------------|--------------|
| Mortgage-backed securities available for sale, at fair value (amortized cost of \$527,463 and \$498,344) | 530,080 | 501,230 |
| Mortgage-backed securities held to maturity (fair value of \$1,254 and \$2,154) | 1,236 | 2,138 |
| Stock in Federal Home Loan Bank of Boston, at cost | 40,369 | 40,369 |
| Loans receivable, net (net of allowance for loan losses of \$14,049 and \$13,233) | 889,604 | 977,174 |
| Accrued interest receivable | 7,128 | 7,928 |
| Mortgage servicing rights | 5,982 | 4,881 |
| Office properties and equipment, net | 22,746 | 24,038 |
| Real estate owned | -- | 175 |
| Bank-Owned Life Insurance | 35,181 | 33,764 |
| Goodwill | 1,087 | 1,145 |
| Prepaid expenses and other assets | 10,210 | 7,255 |
| | ----- | ----- |
| Total assets | \$ 1,698,757 | \$ 1,671,065 |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Liabilities: | | |
| Deposits | \$ 765,287 | \$ 707,416 |
| FHLB advances and other borrowings | 766,139 | 814,764 |
| Advance payments by borrowers for taxes and insurance | 3,571 | 5,868 |
| Accrued interest payable | 3,563 | 5,997 |
| Other liabilities | 38,898 | 25,462 |
| | ----- | ----- |
| Total liabilities | 1,577,458 | 1,559,507 |
| | ----- | ----- |
| Stockholders' equity: | | |
| Common stock | 87 | 87 |
| Additional paid-in capital | 85,859 | 85,585 |
| Retained earnings | 77,549 | 70,048 |
| Accumulated other comprehensive income | 3,133 | 2,551 |
| Unallocated ESOP shares | (3,098) | (3,098) |
| Unearned stock incentive plan | (1,559) | (2,998) |
| Treasury stock | (40,672) | (40,617) |
| | ----- | ----- |
| Total stockholders' equity | 121,299 | 111,558 |
| | ----- | ----- |
| Total liabilities and stockholders' equity | \$ 1,698,757 | \$ 1,671,065 |
| | ===== | ===== |

See accompanying notes to consolidated financial statements.

FIRSTFED AMERICA BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)

FOR THE THREE MONTHS
ENDED DECEMBER 31,

2001 2000

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| | | |
|---|-----------|-------|
| Interest and dividend income: | | |
| Loans | \$ 16,996 | \$ 19 |
| Investment securities | 305 | |
| Mortgage-backed securities | 7,659 | 8 |
| Federal Home Loan Bank stock | 458 | |
| | ----- | ----- |
| Total interest and dividend income | 25,418 | 29 |
| | ----- | ----- |
| Interest expense: | | |
| Deposits | 5,935 | 6 |
| Borrowed funds | 9,959 | 13 |
| | ----- | ----- |
| Total interest expense | 15,894 | 20 |
| | ----- | ----- |
| Net interest income before loan loss provision | 9,524 | 8 |
| Provision for loan losses | 300 | |
| | ----- | ----- |
| Net interest income after loan loss provision | 9,224 | 8 |
| Non-interest income: | | |
| Service charges on deposit accounts | 588 | |
| Loan servicing income | 348 | |
| Insurance commission income | 229 | |
| Trust fee income | 354 | |
| Earnings on Bank-Owned Life Insurance | 513 | |
| Gain on sale of mortgage loans, net | 1,888 | |
| Gain on sale of securities available for sale | -- | |
| Other income | 714 | |
| | ----- | ----- |
| Total non-interest income | 4,634 | 2 |
| | ----- | ----- |
| Non-interest expense: | | |
| Compensation and employee benefits | 4,441 | 4 |
| Office occupancy and equipment | 1,101 | 1 |
| Data processing | 475 | |
| Advertising and business promotion | 196 | |
| Federal deposit insurance premiums | 33 | |
| Other expense | 1,212 | |
| | ----- | ----- |
| Total non-interest expense | 7,458 | 7 |
| | ----- | ----- |
| Income before income tax expense | 6,400 | 3 |
| Income tax expense | 2,402 | |
| | ----- | ----- |
| Net income before cumulative effect of accounting change | 3,998 | 2 |
| Cumulative effect of change in accounting for derivative instruments and hedging activities, net of \$237 tax benefit | -- | |
| | ----- | ----- |
| Net income | \$ 3,998 | \$ 2 |
| | ===== | ===== |
| Basic earnings per share before cumulative effect of accounting change | \$ 0.69 | \$ |
| Cumulative effect of accounting change | -- | |
| | ----- | ----- |
| Basic earnings per share | \$ 0.69 | \$ |
| | ===== | ===== |
| Diluted earnings per share before cumulative effect of accounting change | \$ 0.68 | \$ |
| Cumulative effect of accounting change | -- | |
| | ----- | ----- |
| Diluted earnings per share | \$ 0.68 | \$ |

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| | | |
|---|-----------|-------|
| Weighted average shares outstanding - basic | ===== | ===== |
| | 5,815,449 | 5,795 |
| Weighted average shares outstanding - diluted | ===== | ===== |
| | 5,868,411 | 5,814 |
| | ===== | ===== |

See accompanying notes to consolidated financial statements.

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FIRSTFED AMERICA BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE NINE MONTHS ENDED DECEMBER 31, 2001
(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)
(UNAUDITED)

| | COMMON STOCK | ADDITIONAL PAID-IN CAPITAL | RETAINED EARNINGS | ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS) | UNALLOCATED ESOP SHARES | U ST I P |
|---|-----------------|----------------------------------|----------------------|---|-------------------------------|-------------------|
| Balance at March 31, 2001 | \$87 | \$85,585 | \$70,048 | \$2,551 | \$ (3,098) | \$ |
| Earned SIP stock awards | -- | (155) | -- | -- | -- | |
| Earned ESOP shares charged to expense | -- | 430 | -- | -- | -- | |
| Stock options exercised | -- | (1) | -- | -- | -- | |
| Cash dividends declared and paid (1st quarter at \$0.10 per share; 2nd and 3rd quarters at \$0.14 per share) | -- | -- | (2,365) | -- | -- | |
| Common stock acquired for certain employee benefit plans (3,331 shares at an average price of \$16.34 per share) | -- | -- | -- | -- | -- | |
| Comprehensive income: | | | | | | |
| Net income | -- | -- | 9,866 | -- | -- | |
| Other comprehensive income, net of tax | | | | | | |
| Unrealized holding gains on available for sale securities | -- | -- | -- | 1,911 | -- | |
| Reclassification adjustment for losses (gains) included in net income | -- | -- | -- | (1,003) | -- | |

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| | | | | | |
|------------------------------|------|----------|----------|---------|------------|
| Net unrealized gains | -- | -- | -- | 908 | -- |
| Tax effect | -- | -- | -- | (326) | -- |
| Net-of-tax effect | -- | -- | -- | 582 | -- |
| Total comprehensive income | -- | -- | -- | -- | -- |
| Balance at December 31, 2001 | \$87 | \$85,859 | \$77,549 | \$3,133 | \$ (3,098) |

See accompanying notes to consolidated financial statements.

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FIRSTFED AMERICA BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

| | FOR THE ENDED D |
|---|--------------------|
| | 2001 |
| Cash flows from operating activities: | |
| Net income | \$ 9,866 |
| Adjustments to reconcile net income to net cash used in operating activities: | |
| Amortization (accretion) of: | |
| Premium (discount) on investment and mortgage-backed securities | 256 |
| Deferred loan origination costs | (1,052) |
| Mortgage servicing rights | 2,314 |
| Goodwill | 69 |
| Provision for loan losses | 900 |
| Gains on sales of: | |
| Mortgage loans | (3,349) |
| Investment securities available for sale | (750) |
| Mortgage-backed securities available for sale | (253) |
| Office properties and equipment | (105) |
| Real estate owned | (27) |
| Net proceeds from sales of mortgage loans | 389,083 |
| Origination of mortgage loans held for sale | (418,209) |
| Earnings on Bank-Owned Life Insurance | (1,418) |
| Unrealized (gain) loss on trading securities | 460 |
| Depreciation of office properties and equipment | 1,201 |
| Appreciation in fair value of ESOP shares | 430 |
| Earned SIP shares | 1,284 |
| Increase or decrease in: | |
| Accrued interest receivable | 800 |
| Other assets | (2,388) |
| Accrued interest payable | (2,434) |
| Other liabilities | 13,436 |
| Net cash used in operating activities | (9,886) |
| Cash flows from investing activities: | |

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| | |
|---|-------------|
| Purchase of investment securities available for sale | (14,921) |
| Purchase of trading securities | (173) |
| Purchase of mortgage-backed securities available for sale | (224,094) |
| Payments received on mortgage-backed securities available for sale | 175,147 |
| Proceeds from sale of investment securities available for sale | 753 |
| Proceeds from sale of mortgage-backed securities available for sale | 19,820 |
| Payments received on mortgage-backed securities held to maturity | 900 |
| Purchase of Federal Home Loan Bank stock | -- |
| Net decrease (increase) in loans | 87,695 |
| Purchase of office properties and equipment | (903) |
| Proceeds from sales of office properties and equipment | 1,099 |
| Proceeds from sales of real estate owned | 209 |
| | ----- |
| Net cash provided by (used in) investing activities | 45,532 |
| | ----- |
| Cash flows from financing activities: | |
| | |
| Net increase in deposits | 57,871 |
| Proceeds from FHLB advances and other borrowings | 1,187,690 |
| Repayments on FHLB advances and other borrowings | (1,236,315) |
| Net change in advance payments by borrowers for taxes and insurance | (2,297) |
| Cash dividends paid | (2,365) |
| Payments to acquire common stock for treasury stock and stock options exercised | (56) |
| | ----- |
| Net cash provided by financing activities | 4,528 |
| | ----- |
| Net increase in cash and cash equivalents | 40,174 |
| Cash and cash equivalents at beginning of period | 23,213 |
| | ----- |
| Cash and cash equivalents at end of period | \$ 63,387 |
| | ===== |
| Supplemental disclosures of cash flow information: | |
| Cash paid during the year for: | |
| Interest | \$ 55,504 |
| | ===== |
| Income taxes | \$ 6,031 |
| | ===== |
| Supplemental disclosures of noncash investing activities: | |
| Property acquired in settlement of loans | \$ 27 |
| | ===== |

See accompanying notes to consolidated financial statements.

FIRSTFED AMERICA BANCORP, INC. AND SUBSIDIARIES NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(1) BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements include the accounts of FIRSTFED AMERICA BANCORP, INC. (the "Company"), its wholly-owned subsidiaries, First Federal Savings Bank of America (the "Bank"), FAB FUNDING CORPORATION ("FAB FUNDING") and FIRSTFED INSURANCE AGENCY, LLC (the "Agency"), and its 65% interest in FIRSTFED TRUST COMPANY, N.A. (the "Trust Company"). The remaining 35% interest of the Trust Company is held by M/D Trust, LLC, a minority owner. The Bank includes its wholly-owned subsidiaries, FIRSTFED MORTGAGE CORPORATION, FIRSTFED INVESTMENT CORPORATION, and CELMAC INVESTMENT CORPORATION.

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The interim consolidated financial statements reflect all normal and recurring adjustments which are, in the opinion of management, considered necessary for a fair presentation of the financial condition and results of operations for the periods presented. The results of operations for the three months and nine months ended December 31, 2001 are not necessarily indicative of the results of operations that may be expected for all of fiscal year 2002.

Certain information and note disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission.

These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report to Stockholders on Form 10-K for the fiscal year ended March 31, 2001.

(2) IMPACT OF RECENT ACCOUNTING STANDARDS

On April 1, 2001, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities" and recognized an after-tax loss from the cumulative effect of adoption of \$461,000, or \$0.08 per share, representing the initial adjustment to fair value of certain derivative instruments, including a pre-tax adjustment of \$743,000 related to interest rate swaps designed to reduce its exposure to interest rate changes, partially offset by a pre-tax adjustment of \$45,000 related to commitments to originate and sell mortgage loans for sale that hedge its secondary market activities. Changes to the fair value of derivative instruments are recognized in non-interest income each quarter, and additions to pre-tax income of \$958,000, or approximately \$0.10 per share, and \$891,000, or approximately \$0.10 per share, were recognized for the third quarter and first nine months, respectively, of fiscal year 2002.

In September 2000, the Financial Accounting Standards Board ("FASB") issued SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities - a Replacement of FASB Statement No. 125." Certain disclosure provisions required by SFAS No. 140 were effective immediately, with additional requirements related to SFAS No. 140 effective beginning March 31, 2001. The adoption of SFAS No. 140 had no effect on the Company's consolidated financial position or results of operations.

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In June 2001, the FASB issued SFAS No. 141, "Business Combinations" and SFAS No. 142, "Accounting for Goodwill and Other Intangible Assets." SFAS No. 141 requires business combinations initiated after June 30, 2001 to be accounted for using the purchase method. Under SFAS No. 142 goodwill will no longer be amortized, and will instead be subject to assessment for impairment, and intangible assets with finite useful lives will continue to be amortized over their useful lives. The Company will adopt SFAS No. 142 on April 1, 2002. At December 31, 2001, the Company had \$1.1 million of goodwill on its balance sheet with an annual amortization rate of approximately \$92,000.

(3) PENDING ACQUISITION

On October 1, 2001, the Company and People's Bancshares, Inc. ("People's"), New Bedford, Massachusetts, jointly announced that they had signed a definitive agreement pursuant to which the Company will acquire People's for

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approximately \$72 million in cash and stock. People's reported total assets of \$915.8 million, total deposits of \$561.1 million and total stockholders' equity of \$39.1 million at December 31, 2001. On February 4, 2002, stockholders of both companies voted to approve the merger agreement. Under the terms of the merger agreement, People's stockholders could elect to receive either 1.2644 shares of the Company's common stock (and cash in lieu of any fractional share) or \$22.00 in cash for each share of People's common stock they own. The value of the FIRSTFED common stock will be evaluated during a 20-day measurement period shortly before the closing of the merger. If during this period the average closing price of the FIRSTFED stock declines below \$13.92 (causing the value of 1.2644 shares of FIRSTFED stock to be less than \$17.60), and the market value of FIRSTFED common stock underperforms the "SNL New England Thrift Index" by more than 15%, People's has the right to terminate the merger. FIRSTFED would have the right to cancel the termination by increasing the number of shares of FIRSTFED stock it is to exchange to a specified level. If the average closing price of FIRSTFED common stock during the measurement period increases to \$20.88 or more, the value of the shares of FIRSTFED common stock to be exchanged for each share of People's common stock will be limited to \$26.40. The elections of People's shareholders will be subject to the requirement that 55% of People's shares be exchanged for cash and 45% be exchanged for the Company's common stock. Upon consummation of the merger, former shareholders of People's will own approximately 23% of the Company's outstanding shares. The transaction, which would increase the Company's assets from \$1.7 billion as of December 31, 2001 to approximately \$2.6 billion, is expected to be completed prior to March 31, 2002, subject to certain conditions including approval of the regulators of both companies. In accordance with SFAS No. 141 and SFAS No. 142, the Company will use the purchase method of accounting for the merger, as well as the new accounting standards for goodwill and other intangible assets.

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

GENERAL

The Company's primary business is attracting retail deposits from the general public and investing those deposits and other borrowed funds in loans, mortgage-backed securities, U.S. Government securities and other securities. The Company originates commercial, consumer, and mortgage loans for investment, and mortgage loans for sale in the secondary market. The Company's primary sources of funds are deposits, principal and interest payments on loans and mortgage-backed securities, proceeds from the sale of loans and securities, FHLB advances, and other borrowings.

The Company's results of operations are primarily dependent on net interest income, which is the difference between the income earned on its loan, investment and mortgage-backed securities portfolios, and its cost of funds, consisting of the interest paid on deposits and borrowings. Results of operations are also affected by the Company's provision for loan losses and non-interest income including service charges on deposit accounts, loan servicing income, revenue from the Trust Company and Agency operations, earnings on Bank-Owned Life Insurance ("BOLI"), gains on sale of loans and investment securities, and other income. The Company's non-interest expense consists of compensation and employee benefits, office occupancy and equipment expense, data processing expense, advertising and business promotion, federal deposit insurance premiums, and other expenses. Results of operations of the Company are also significantly affected by general economic and competitive conditions, particularly changes in interest rates, government policies and the actions of regulatory authorities.

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This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and is including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of the Company, are generally identified by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project," or similar expressions. The Company's ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on the operations of the Company and the subsidiaries include, but are not limited to, changes in: interest rates, general economic conditions, legislative/regulatory changes, monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board, the quality or composition of the loan or investment portfolios, demand for loan products, deposit flows, competition, demand for financial services in the Company's market area and accounting principles and guidelines. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Further information on the Company and its business, including additional factors that could materially affect the Company's financial results, is included in the Company's filings with the Securities and Exchange Commission.

Subject to applicable laws and regulations, the Company does not undertake - and specifically disclaims any obligation - to publicly release the result of any revisions which may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

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RESULTS OF OPERATIONS

OVERVIEW

Net income increased \$1.9 million, or 87.7%, to \$4.0 million for the third quarter of fiscal year 2002 from \$2.1 million for the third quarter of fiscal year 2001. Diluted earnings per share ("EPS") increased 83.8% to \$0.68 for the third quarter of fiscal year 2002 from \$0.37 per share for the third quarter of fiscal year 2001. Income before income tax expense increased \$3.3 million, or 106.7%, to \$6.4 million, as a result of increases in net interest income of \$1.1 million and non-interest income of \$2.5 million, partially offset by an increase in non-interest expense of \$316,000.

Year to date net income before the cumulative effect of adoption of SFAS No. 133 was \$10.3 million for the first nine months of fiscal year 2002, an increase of \$3.6 million, or 54.2%, from net income of \$6.7 million for the first nine months of fiscal year 2001. After the cumulative effect of adoption of SFAS No. 133, net income was \$9.9 million for the first nine months of fiscal year 2002, an increase of \$3.2 million, or 47.3%, as compared to the first nine months of fiscal year 2001. Diluted EPS before the cumulative effect of adoption of SFAS No. 133 increased 55.3% to \$1.77 for the first nine months of fiscal year 2002 from \$1.14 for the first nine months of fiscal year 2001. After the cumulative effect of adoption of SFAS No. 133, diluted EPS was \$1.69 for the first nine months of fiscal year 2002, an increase of 48.2% as compared to the first nine months of fiscal year 2001. Income before income tax expense increased \$6.2 million, or 63.6%, to \$15.9 million, as a result of increases in net interest income of \$2.0 million and non-interest income of \$4.5 million, partially offset by an increase in non-interest expense of \$306,000.

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The growth in EPS for the third quarter and year to date periods of fiscal year 2002, compared to the same periods of fiscal year 2001, was caused primarily by the growth in net income. Gain on sale of mortgage loans contributed \$0.20 per share and \$0.37 per share to EPS for the third quarter of fiscal year 2002 and the first nine months of fiscal year 2002, respectively, as compared to \$0.02 per share and \$0.04 per share for the third quarter of fiscal year 2001 and the first nine months of fiscal year 2001, respectively.

Return on average stockholders' equity increased to 12.99% for the third quarter of fiscal year 2002 and 10.95% for the first nine months of fiscal year 2002, compared to 8.04% and 8.56% for the respective periods of fiscal year 2001. Return on average assets increased to 0.93% for the third quarter of fiscal year 2002 and 0.77% for the first nine months of fiscal year 2002, compared to 0.51% and 0.54% for the respective periods of fiscal year 2001.

NET INTEREST INCOME

Net interest income before provision for loan losses increased \$1.1 million, or 13.7%, to \$9.5 million for the third quarter of fiscal year 2002 from \$8.4 million for the third quarter of fiscal year 2001. The net interest rate spread and net interest margin were 2.03% and 2.36% for the third quarter of fiscal year 2002, compared to 1.88% and 2.15%, respectively, for the third quarter of fiscal year 2001.

Year to date net interest income before provision for loan losses increased \$2.0 million, or 7.7%, to \$27.9 million for the first nine months of fiscal year 2002 from \$25.9 million for the first nine months of fiscal year 2001. The net interest rate spread and net interest margin were 1.96% and 2.30% for the first nine months of fiscal year 2002, compared to 1.96% and 2.24%, respectively, for the first nine months of fiscal year 2001.

The increases in net interest income and the average balances of interest-earning assets and interest-bearing liabilities during the third quarter and year to date periods of fiscal year 2002, compared to the same periods of fiscal year 2001, were due to several key factors. Declining market interest rates and related consumer preferences resulted in the Company's shift to origination of fixed-rate mortgages that are generally sold in the secondary

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market, from origination of adjustable-rate mortgages that are generally retained for portfolio. In addition, prepayment speeds on mortgage loans increased due primarily to refinancing activity. This economic environment, combined with the Company's business development and cross-selling efforts, contributed to growth in commercial and consumer loans and deposits. The decline in FHLB advances and other borrowings reflected a greater reliance on deposits for funding balance sheet growth, while borrowing costs also declined. Lastly, the growth in investment and mortgage-backed securities resulted from management's strategy to maintain the Company's leverage in fiscal year 2002.

The following tables set forth certain information relating to the Company for the periods indicated. Net interest income is a function of both the relative amounts of interest-earning assets and interest-bearing liabilities, and the interest rates earned or paid on them. Income from BOLI is excluded from interest income, and the BOLI cash value balances are excluded from interest-earning assets. The average yields and costs are derived by dividing income or expense by the average balance of interest-earning assets or interest-bearing liabilities, respectively, for the periods shown. Average balances are derived from the best available daily or monthly data, which management believes approximates the average balances computed on a daily basis.

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The yields and the costs include fees, premiums and discounts which are considered adjustments to yields.

| | FOR THE THREE MONTHS ENDED DE | | | |
|--|---------------------------------------|-----------|---------------------------|----------------|
| | ----- 2001 ----- | | | |
| | AVERAGE BALANCE | INTEREST | AVERAGE YIELD/ COST | AVERA BALAN |
| | ----- (DOLLARS IN THOUSAN ----- | | | |
| Assets: | | | | |
| Interest-earning assets: | | | | |
| Loans receivable, net and mortgage loans held for sale (1) | \$ 956,329 | \$ 16,996 | 7.11% | \$1,006, |
| Investment securities (2) | 70,564 | 763 | 4.29 | 46, |
| Mortgage-backed securities (3) | 577,329 | 7,659 | 5.31 | 492, |
| | ----- | | | |
| Total interest-earning assets | 1,604,222 | 25,418 | 6.34 | 1,545, |
| | ----- | | | |
| Noninterest-earning assets | 100,441 | | | 99, |
| | ----- | | | |
| Total assets | \$1,704,663 | | | \$1,644, |
| | ===== | | | ===== |
| Liabilities and Stockholders' Equity: | | | | |
| Interest-bearing liabilities: | | | | |
| Deposits (4) | \$ 669,463 | 5,935 | 3.52 | \$ 609, |
| FHLB advances and other borrowings | 794,168 | 9,959 | 4.98 | 845, |
| | ----- | | | |
| Total interest-bearing liabilities | 1,463,631 | 15,894 | 4.31 | 1,455, |
| | ----- | | | |
| Noninterest-bearing liabilities (5) | 118,954 | | | 84, |
| | ----- | | | |
| Total liabilities | 1,582,585 | | | 1,539, |
| Stockholders' equity | 122,078 | | | 105, |
| | ----- | | | |
| Total liabilities and stockholders' equity | \$1,704,663 | | | \$1,644, |
| | ===== | | | ===== |
| Net interest rate spread (6) | | \$ 9,524 | 2.03% | |
| | | ===== | | |
| Net interest margin (7) | | | 2.36% | |
| | | | ===== | |
| Ratio of interest-earning assets to interest- bearing liabilities | 109.61% | | | 106 |
| | ===== | | | ===== |

FOR THE NINE MONTHS ENDED DE

2001

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| | AVERAGE BALANCE | INTEREST | AVERAGE YIELD/ COST | AVERAGE BALANCE |
|--|--------------------|-----------|---------------------------|--------------------|
| | | | (DOLLARS | IN THOUSAN |
| Assets: | | | | |
| Interest-earning assets: | | | | |
| Loans receivable, net and mortgage loans held for sale (1) | \$ 973,917 | \$ 53,924 | 7.38% | \$ 976, |
| Investment securities (2) | 72,085 | 2,650 | 4.88 | 44, |
| Mortgage-backed securities (3) | 562,763 | 24,371 | 5.77 | 514, |
| Total interest-earning assets | 1,608,765 | 80,945 | 6.70 | 1,535, |
| Noninterest-earning assets | 102,525 | | | 99, |
| Total assets | \$1,711,290 | | | \$1,635, |
| Liabilities and Stockholders' Equity: | | | | |
| Interest-bearing liabilities: | | | | |
| Deposits (4) | \$ 654,301 | 19,280 | 3.91 | \$ 608, |
| FHLB advances and other borrowings | 830,424 | 33,790 | 5.40 | 839, |
| Total interest-bearing liabilities | 1,484,725 | 53,070 | 4.74 | 1,447, |
| Noninterest-bearing liabilities (5) | 107,006 | | | 84, |
| Total liabilities | 1,591,731 | | | 1,531, |
| Stockholders' equity | 119,559 | | | 103, |
| Total liabilities and stockholders' equity | \$1,711,290 | | | \$1,635, |
| Net interest rate spread (6) | | \$ 27,875 | 1.96% | |
| Net interest margin (7) | | | 2.30% | |
| Ratio of interest-earning assets to interest-bearing liabilities | 108.35% | | | 106 |

-
- (1) Amount is net of deferred loan origination costs, undisbursed proceeds of construction mortgages in process, allowance for loan losses and includes non-performing loans.
 - (2) Includes short-term investments, investments in trading securities, investment securities available for sale and held to maturity, and FHLB stock.
 - (3) Consists of mortgage-backed securities available for sale and held to maturity.
 - (4) Includes the net effect of payments related to interest rate swaps.
 - (5) Consists primarily of business checking accounts.
 - (6) Net interest rate spread represents the difference between the weighted average yield on interest-earning assets and the weighted average cost of interest-bearing liabilities.
 - (7) Net interest margin represents net interest income as a percentage of average interest-earning assets.

PROVISION FOR LOAN LOSSES

The Company's provision for loan losses remained unchanged at \$300,000 for the third quarters of fiscal years 2002 and 2001, and \$900,000 for the first nine months of fiscal years 2002 and 2001. The allowance for loan losses was \$14.0 million, or 1.55% of loans receivable, at December 31, 2001, compared to \$13.2 million, or 1.34% of loans receivable at March 31, 2001.

The provision for loan losses is based on management's assessment of the loan loss reserve level, the existing loan portfolio, current market conditions, and the volume and mix of new originations. To the extent the Company experiences increases in the overall balance of its loan portfolio or further increases its concentrations of loans which bear a higher degree of risk than one-to-four family loans, the Company anticipates further increases in its allowance for loan losses through continued provisions for loan losses. For additional information on the amount of the allowance and the process for evaluating its adequacy, see "Financial Condition - Asset Quality."

NON-INTEREST INCOME

Non-interest income increased \$2.5 million, or 114.1%, to \$4.6 million for the third quarter of fiscal year 2002 from \$2.1 million for the third quarter of fiscal year 2001. This increase was primarily attributable to increases of \$1.7 million in gain on sale of mortgage loans, net, \$123,000 in service charges on deposit accounts and \$473,000 in other non-interest income.

Year to date non-interest income increased \$4.5 million, or 69.1%, to \$11.0 million for the first nine months of fiscal year 2002 from \$6.5 million for the first nine months of fiscal year 2001. This increase was primarily attributable to increases of \$3.0 million in gain on sale of mortgage loans, net, \$1.0 million in gain on sale of securities available for sale, \$343,000 in trust fee income, and \$314,000 in service charges on deposit accounts, partially offset by a decrease of \$347,000 in loan servicing income.

The quarterly and year-to-date increases in gain on sale of mortgage loans, net, were due primarily to a higher volume of fixed rate loans originated for sale and more favorable loan pricing during fiscal year 2002. Mortgage servicing rights were capitalized totaling \$1.2 million and \$218,000 for the third quarters of fiscal year 2002 and 2001, respectively, and \$3.4 million and \$504,000 for the first nine months of fiscal year 2002 and 2001, respectively. In addition, increases in gain on sale of mortgage loans, net, of \$858,000 for the third quarter of fiscal year 2002 and \$882,000 for the first nine months of fiscal year 2002 were recognized as a result of changes in fair value of derivative instruments utilized in secondary market hedging activities following the adoption of SFAS No. 133 on April 1, 2001. Management of the Company believes that the adoption of SFAS No. 133 has introduced the potential for greater volatility to quarterly earnings due to valuation changes and accelerated recognition of gains or losses in the Company's mortgage banking activities. However, such effects are expected to offset over time as market conditions change.

The year-to-date decrease in loan servicing income was due primarily to a \$240,000 addition to the valuation allowance for mortgage servicing rights during the second quarter of fiscal year 2002, based on estimated impairment due to a combination of faster than previously expected actual payoff experience and faster prepayment forecasts in September 2001 versus June 2001. The balance of the valuation allowance amounted to \$490,000 at December 31, 2001 and \$250,000 at March 31, 2001. Amortization of mortgage servicing rights, including the addition to the valuation allowance, totaled \$2.3 million and \$1.8 million for

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the first nine months of fiscal year 2002 and 2001, respectively.

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The quarterly and year-to-date increases in service charges on deposit accounts were due primarily to a higher fee rate structure. The year-to-date increase in trust fee income was due to continued growth at the Trust Company, which opened in February 2000. The quarterly increase in other non-interest income was due primarily to an increase in the fair value of investments in certain employee benefit plans, which is offset by a corresponding increase in other non-interest expense.

NON-INTEREST EXPENSE

Non-interest expense increased \$316,000, or 4.4%, to \$7.4 million for the third quarter of fiscal year 2002 from \$7.1 million for the third quarter of fiscal year 2001, due primarily to an increase of \$276,000 in other non-interest expense. The increase in other non-interest expense was due primarily to an increase in the fair value of investments in certain employee benefit plans.

Year to date non-interest expense increased \$306,000, or 1.4%, to \$22.1 million for the first nine months of fiscal year 2002 from \$21.8 million for the first nine months of fiscal year 2001, due primarily to increases of \$270,000 in compensation and benefits and \$207,000 in data processing expense, partially offset by a decrease of \$235,000 in advertising and business promotion expense.

INCOME TAXES

Income tax expense increased \$1.4 million, or 148.6%, to \$2.4 million for the third quarter of fiscal year 2002 from \$966,000 for the third quarter of fiscal year 2001. Year to date income tax expense increased \$2.6 million, or 84.3%, to \$5.6 million for the first nine months of fiscal year 2002 from \$3.0 million for the first nine months of fiscal year 2001. These increases were due primarily to increased income before income tax expense. The Company's effective tax rate increased to 35.2% during the first nine months of fiscal year 2002 from 31.3% for the first nine months of fiscal year 2001, due primarily to the effects of an increase in the statutory federal income tax rate based on a higher taxable earnings threshold, increased state taxes and appreciation of FIRSTFED stock contributed to the Company's Employee Stock Ownership Plan.

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FINANCIAL CONDITION

OVERVIEW

Total assets increased \$27.7 million, or 1.7%, to \$1.699 billion at December 31, 2001 from \$1.671 billion at March 31, 2001. This growth was primarily attributable to increases of \$36.6 million in short-term investments, \$28.9 million in mortgage-backed securities available for sale, \$28.2 million in mortgage loans held for sale, and \$16.1 million in investment securities available for sale, partially offset by a decrease of \$87.6 million in loans receivable, net.

The following table sets forth the composition of the Company's loan portfolio in dollar amounts and as a percentage of the portfolio at the dates indicated:

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| | DECEMBER 31, 2001 | | MARCH 31, 2001 | |
|---|------------------------|---------------------|----------------|---------------------|
| | AMOUNT | PERCENT OF TOTAL | AMOUNT | PERCENT OF TOTAL |
| | (DOLLARS IN THOUSANDS) | | | |
| Mortgage Loans: | | | | |
| Residential | \$ 527,001 | 57.26% | \$ 680,527 | 67.49% |
| Commercial real estate | 64,192 | 6.97 | 44,375 | 4.40 |
| Construction and land | 68,455 | 7.44 | 72,225 | 7.16 |
| Total mortgage loans | 659,648 | 71.67 | 797,127 | 79.05 |
| Commercial Loans | 136,141 | 14.79 | 94,681 | 9.39 |
| Consumer Loans: | | | | |
| Home equity lines | 64,770 | 7.04 | 45,191 | 4.48 |
| Second mortgages | 50,227 | 5.45 | 61,759 | 6.12 |
| Other consumer loans | 9,643 | 1.05 | 9,665 | .96 |
| Total consumer loans | 124,640 | 13.54 | 116,615 | 11.56 |
| Total loans receivable | 920,429 | 100.00% | 1,008,423 | 100.00% |
| Less: | | | | |
| Allowance for loan losses | (14,049) | | (13,233) | |
| Undisbursed proceeds of Construction mortgages in process | (18,038) | | (19,445) | |
| Deferred loan origination costs, net | 1,262 | | 1,429 | |
| Loans receivable, net | \$ 889,604 | | \$ 977,174 | |

Balance sheet growth was primarily funded by an increase of \$57.9 million, or 8.2%, in deposit balances, partially offset by a decrease of \$48.6 million, or 6.0%, in FHLB advances and other borrowings during the first nine months of fiscal year 2002. The increase in deposits included increases of \$49.9 million in demand and savings accounts and \$8.0 million in certificate accounts.

Total stockholders' equity increased \$9.7 million, or 8.7%, to \$121.3 million at December 31, 2001, from \$111.6 million at March 31, 2001. The increase is due primarily to \$9.9 million in net income, \$1.3 million in earned Stock-based Incentive Plan awards, and a \$582,000 increase in the fair market value of securities available for sale, net of tax, partially offset by \$2.4 million in dividends paid to stockholders. Stockholders' equity to assets was 7.14% at December 31, 2001, compared to 6.68% at March 31, 2001. Book value per share increased 6.4% to \$20.82 at December 31, 2001 from \$19.57 at March 31, 2001.

At December 31, 2001 and March 31, 2001, mortgage loans sold to others and serviced by the Bank on a fee basis under various agreements amounted to \$1.563 billion and \$1,531 billion, respectively. Loans serviced for others are not included in the Consolidated Balance Sheets.

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The Company's primary sources of funds are deposits, principal and interest payments on loans and mortgage-backed securities, proceeds from the sale of loans and securities, FHLB advances, and other borrowings. While maturities and scheduled amortization of loans are predictable sources of funds, deposit flows and mortgage prepayments are influenced by general interest rates, economic conditions and competition.

The Company's most liquid assets are cash, short-term investments, mortgage loans held for sale, investments in trading securities, investment securities available for sale, and mortgage-backed securities available for sale. The levels of these assets are dependent on the Company's operating, financing, lending and investing activities during any given period. At December 31, 2001, cash, short-term investments, mortgage loans held for sale, investments in trading securities, investment securities available for sale, and mortgage-backed securities available for sale totaled \$685.2 million, or 40.3% of total assets.

The Company has other sources of liquidity if a need for additional funds arises, including a \$25.0 million FHLB secured line of credit, FHLB advances, and other borrowings. At December 31, 2001, the Company had \$766.1 million in advances outstanding from the FHLB and other borrowings, and an additional borrowing capacity from the FHLB of \$134.9 million. The Company uses FHLB advances and other borrowings to fund asset growth and other cash flow needs, and may continue to do so in the future, depending on market conditions, the pricing of deposit products, and the pricing of FHLB advances and other borrowings. At December 31, 2001, the putable advances portfolio totaled \$159.0 million, consisting of eight advances with an average rate of 5.34%, an average life to maturity of 7.2 years and an expected average life of 2.4 years. The expected average life calculated by the Bank may or may not mirror the FHLB's actual decision to exercise its option to terminate the advances.

At December 31, 2001, the Company had commitments to originate loans and unused outstanding lines of credit and undistributed balances of construction loans totaling \$188.5 million. The Company anticipates that it will have sufficient funds available to meet its current loan origination commitments. Certificate of deposit accounts scheduled to mature in less than one year from December 31, 2001 totaled \$288.4 million. Based upon historical experience with deposit retention, the Company expects that it will retain a majority of maturing certificate accounts.

At December 31, 2001, the Bank exceeded all of its regulatory capital requirements. The Bank's tangible capital of \$111.8 million, or 6.63% of total adjusted assets, was above the required level of \$33.7 million or 2.0%; Tier 1 core capital of \$111.8 million, or 6.63% of total adjusted assets, was above the required level of \$67.4 million, or 4.0%; risk-based capital of \$119.2 million, or 13.30% of risk-weighted assets, was above the required level of \$71.7 million or 8.0%, and Tier 1 risk-based capital of \$111.8 million, or 12.05% of risk-weighted assets, was above the required level of \$35.9 million or 4.0%. The Bank is considered a "well capitalized" institution under the OTS prompt corrective action regulations. The Trust Company is subject to similar regulatory capital requirements, and exceeded all of its capital requirements at December 31, 2001.

The Company expects the Bank's Tier 1 core capital ratio to be approximately 5.0% upon consummation of the merger with People's. If the Bank does not maintain a Tier 1 core capital ratio of 5.0%, its regulatory classification would change from "well capitalized" to "adequately capitalized." Although an "adequately capitalized" classification means that First Federal complies with all applicable minimum regulatory capital requirements, reclassification as "adequately capitalized" would have certain adverse consequences such as increased FDIC insurance premiums and a prohibition on

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accepting brokered deposits without prior FDIC approval. Under the current FDIC regulations, institutions which qualify as well capitalized are assessed 0.17 basis points per

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\$100 of deposits, depending on the risk of the institution as compared to 3 to 24 basis points for "adequately capitalized" institutions. The Company expects to fund the cash payment to People's stockholders from its cash and cash equivalents. The Company has obtained a commitment from a third party for an unsecured loan of approximately \$10 million. The loan is expected to close prior to the consummation of the merger. Proceeds from this loan may be used for general corporate purposes including the payment of such funds to the Bank as a capital contribution, thereby raising the Bank's level of Tier 1 capital. The funding of the loan or any other form of capital raising is not a condition to the consummation of the merger under the terms of the merger agreement.

MARKET RISK AND MANAGEMENT OF INTEREST-RATE RISK

The principal market risk affecting the Company is interest-rate risk. The principal objective of the Company's interest rate risk management function is to evaluate the interest rate risk included in certain balance sheet accounts, determine the level of risk appropriate given the Company's business strategy, operating environment, capital and liquidity requirements and performance objectives, and manage the risk consistent with Board of Directors' approved guidelines. Through such management, the Company seeks to reduce the vulnerability of its operations to changes in interest rates. The Company monitors its interest rate risk as such risk relates to its operating strategies. The Company's Board of Directors has established an Asset/Liability Committee, responsible for reviewing its asset/liability policies and interest rate risk position, which meets on a monthly basis and reports trends and interest rate risk position to the Board of Directors on a quarterly basis. The extent of the movement of interest rates is an uncertainty that could have a negative impact on the earnings of the Company.

The Company has primarily utilized the following strategies to manage interest rate risk: (1) emphasizing the origination and retention of adjustable-rate and shorter-term (generally ten years or less) fixed-rate, one-to-four family mortgage loans; (2) selling in the secondary market longer-term, fixed-rate mortgage loans originated while generally retaining the servicing rights on such loans; and (3) investing primarily in adjustable-rate mortgage-backed securities and short-term fixed-rate collateralized mortgage obligations ("CMOs"). In conjunction with its mortgage banking activity, the Company uses forward contracts in order to reduce exposure to interest-rate risk. The amount of forward coverage of the "pipeline" of mortgages is managed on a day-to-day basis by an operating officer, within Board approved policy guidelines, based on the Company's assessment of the general direction of interest rates and levels of mortgage origination activity. In addition, the Company has engaged in interest rate swap agreements to synthetically lengthen its liability maturities.

The matching of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are "interest rate sensitive" and by monitoring a bank's interest rate sensitivity "gap." An asset or liability is said to be interest rate sensitive within a specific time period if it will mature or reprice within that time period. The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within that same time period. At December 31, 2001, the Company's cumulative one-year interest rate gap (which is the difference between the amount of interest-earning assets and the amount of

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interest-bearing liabilities maturing or repricing within one year) as a percentage of total assets was a positive 9.12%. Accordingly, during a period of falling interest rates, the Company's interest-earning assets would be expected to reprice downward at a faster rate than its interest-bearing liabilities, which, consequently, may negatively affect the Company's net interest income. During a period of rising interest rates, the Company's interest-earning assets would be expected to reprice upward at a faster rate than its interest-bearing liabilities, which, consequently, may positively affect the Company's net interest income.

Certain shortcomings are inherent in gap analysis. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain

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assets, such as adjustable-rate loans, have features which restrict changes in interest rates both on a short-term basis and over the life of the asset. Further, in the event of change in interest rates, prepayment and early withdrawal levels would likely deviate significantly from those assumed in calculating the cumulative one year interest rate gap. Finally, the ability of some borrowers to service their adjustable-rate loans may decrease in the event of an interest rate increase.

The Company's interest rate sensitivity is also monitored by management through the use of a model which generates estimates of the change in the Company's net interest income ("NII") and net portfolio value ("NPV") over a range of interest rate scenarios. NPV is the present value of expected cash flows from assets, liabilities, and off-balance sheet contracts. The NPV ratio, under any interest rate scenario, is defined as the NPV in that scenario divided by the estimated market value of assets in the same scenario. The OTS produces a similar analysis for the Bank using its own model, based upon data submitted on the Bank's quarterly Thrift Financial Report, the results of which may vary from the Company's internal model primarily due to differences in assumptions utilized between the Company's internal model and the OTS model, including estimated loan prepayment rates, reinvestment rates and deposit renewal rates.

Certain shortcomings are inherent in the methodology used in the above interest rate risk measurements. Modeling changes in NPV require certain assumptions which may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. In this regard, the Company's NPV model incorporates an assumption that the composition of the Company's interest sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured, and that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or repricing of specific assets and liabilities. Accordingly, although the NPV measurements and net interest income models provide an indication of the Company's interest rate risk exposure at a particular point in time, such measurements are not intended to, and do not, provide a precise forecast of the effect of changes in market interest rates on the Company's net interest income and may differ from actual results.

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ASSET QUALITY

Non-Performing Assets. The following table sets forth information

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regarding non-accrual loans, real estate owned ("REO") and other repossessed assets. The Company ceases to accrue interest on loans 90 days or more past due and charges off all accrued interest. Foregone interest on non-accrual loans was \$58,000 for the three months ended December 31, 2001 and \$108,000 for the nine months ended December 31, 2001.

| | AT DECEMBER 31, 2001 | AT MARCH 31, 2001 |
|--|-------------------------|----------------------|
| | ----- | ----- |
| | (DOLLARS IN THOUSANDS) | |
| Non-accrual loans: | | |
| Mortgage loans: | | |
| One-to-four family | \$ 729 | \$ 431 |
| Construction and land | 1,382 | -- |
| | ----- | ----- |
| Total mortgage loans | 2,111 | 431 |
| | ----- | ----- |
| Commercial loans | 628 | 821 |
| | ----- | ----- |
| Consumer loans: | | |
| Second mortgages | 56 | 56 |
| Other consumer loans | 32 | 24 |
| | ----- | ----- |
| Total consumer loans | 88 | 80 |
| | ----- | ----- |
| Total non-accrual loans | 2,827 | 1,332 |
| Real estate owned, net (1) | -- | 175 |
| Other repossessed assets, net | 20 | -- |
| | ----- | ----- |
| Total non-performing assets | \$ 2,847 | \$ 1,507 |
| | ===== | ===== |
| Allowance for loan losses as a percent of loans (2) | 1.55% | 1.34% |
| Allowance for loan losses as a percent of non-accrual loans (3) | 497% | 993% |
| Non-accrual loans as a percent of loans (2)(3) | 0.31% | 0.13% |
| Non-performing assets as a percent of total assets (4) .. | 0.17% | 0.09% |

- (1) REO balances are shown net of related valuation allowances.
- (2) Loans includes loans receivable, net, excluding allowance for loan losses.
- (3) Non-performing loans consist of all loans 90 days or more past due and other loans which have been identified by the Company as presenting uncertainty with respect to the collectability of interest or principal.
- (4) Non-performing assets consist of non-performing loans, REO and other repossessed assets.

The increase in non-performing assets during the first nine months of fiscal year 2002 is primarily due to an increase of \$1.7 million in non-accrual one-to-four family mortgage loans, including \$1.4 million in the construction and land category.

Allowance for Loan Losses. The allowance for loan losses is based on management's ongoing review and estimate of the credit losses inherent in the loan portfolio. Management's methodology to estimate loss exposure inherent in the portfolio includes analysis of individual loans deemed to be impaired, performance of individual loans in relation to contract terms, and allowance allocations for various loan types based on payment status or loss experience. An unallocated allowance is also maintained within an established range based on management's assessment of many factors including current market conditions,

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trends in loan delinquencies and charge-offs, the volume and mix of new originations, and the current type, mix, changing risk profiles and balance of the portfolio. In addition, the OTS and the FDIC, as an integral part of their examination process, periodically review the

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Company's allowance for loan losses. Such agencies may require the Company to make additional provisions for estimated loan losses based upon judgments different from those of management.

The allowance for loan losses totaled \$14.0 million at December 31, 2001, an increase of \$816,000, or 6.2%, as compared to \$13.2 million at March 31, 2001. The following table sets forth activity in the Company's allowance for loan losses for the periods indicated:

| | FOR THE THREE MONTHS ENDED DECEMBER 31, | | FOR THE NINE MONTHS ENDED DECEMBER 31, | |
|--|--|-----------|---|-----------|
| | 2001 | 2000 | 2001 | 2000 |
| | ----- | | | |
| | (DOLLARS IN THOUSANDS) | | | |
| Balance at beginning of period | \$ 13,725 | \$ 12,783 | \$ 13,233 | \$ 12,275 |
| Provision for loan losses | 300 | 300 | 900 | 900 |
| | ----- | | | |
| Charge-offs: | | | | |
| One-to-four family mortgage loans . | -- | (27) | -- | (42) |
| Commercial loans | -- | -- | (68) | (58) |
| Consumer Loans: | | | | |
| Home equity lines | (4) | (2) | (7) | (4) |
| Second mortgages | -- | (5) | -- | (14) |
| Other consumer | (63) | (16) | (102) | (27) |
| | ----- | | | |
| Total | (67) | (50) | (177) | (145) |
| Recoveries | 91 | 33 | 93 | 36 |
| | ----- | | | |
| Balance at end of period | \$ 14,049 | \$ 13,066 | \$ 14,049 | \$ 13,066 |
| | ===== | | | |
| Ratio of net recoveries (charge-offs) during the period to average loans outstanding during the period | 0.01% | (0.01%) | (0.01%) | (0.01%) |

Management was influenced by several key factors as a basis for maintaining the level of the Company's provisions for loan losses, which resulted in increases in the balance of the allowance for loan losses and as a percent of the total loan portfolio during fiscal year 2002. Although the Company's non-performing loans and charge-offs have remained low, there has been a significant shift in the composition of the loan portfolio during the reporting periods of fiscal year 2002 as compared to fiscal year 2001. The residential mortgage portfolio has decreased due primarily to a low fixed rate environment, which resulted in high refinancing activity, while the commercial and consumer loan portfolios have shown significant growth. Commercial and consumer loans bear a higher degree of risk than the one-to-four family mortgage loans that make up substantially all of the Company's residential portfolio. In addition, management believes that current economic conditions, including rising unemployment rates in its key market area of southeastern New England, could

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have an adverse affect on asset quality and result in higher non-performing loans and charge-offs.

The Company will continue to monitor and modify its allowances for loan losses as conditions dictate. While management believes the Company's allowance for loan losses was sufficient to absorb losses inherent in its loan portfolio at December 31, 2001, no assurances can be given that the Company's level of allowance for loan losses will be sufficient to cover future loan losses incurred by the Company or that future adjustments to the allowance for loan losses will not be necessary if economic and other conditions differ substantially from the economic and other conditions used by management to determine the current level of the allowance for loan losses.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

See the Section of Item 2 captioned, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Market Risk and Management of Interest-Rate Risk" for quantitative and qualitative information about market risk and its potential effect on the Company.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

The Company is not engaged in any legal proceedings of a material nature at the present time. From time to time, the Company is a party to routine legal proceedings within the normal course of business. Such routine legal proceedings in the aggregate are believed by management to be immaterial to the Company's financial condition or results of operations.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS.

Not Applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

Not Applicable.

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

Not Applicable.

ITEM 5. OTHER INFORMATION.

Not Applicable.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

a) Exhibits

- 3.1 Certificate of Incorporation of FIRSTFED AMERICA BANCORP, INC. (1)
- 3.2 Bylaws of FIRSTFED AMERICA BANCORP, INC. (1)
- 4.0 Stock Certificate of FIRSTFED AMERICA BANCORP, INC. (1)

b) Reports on Form 8-K

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A current report of Form 8-K was filed on October 2, 2001, attaching the press release issued on October 1, 2001 announcing the signing of a definitive agreement to acquire People's Bancshares, Inc.

- (1) Incorporated by reference into this document from the Exhibits to Form S-1, Registration Statement, and any amendments thereto, filed on September 27, 1996, Registration No. 333-12855.

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SIGNATURES

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

FIRSTFED AMERICA BANCORP, INC.
Registrant

Date: February 13, 2002

/s/ Robert F. Stoico

Chairman of the Board, President and
Chief Executive Officer
(Principal Executive Officer)

Date: February 13, 2002

/s/ Edward A. Hjerpe III

Executive Vice President, Chief Operating
Officer and Chief Financial Officer
(Principal Accounting and Financial Officer)

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