

MID PENN BANCORP INC  
Form 10-Q  
May 16, 2011  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549  
**FORM 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2011

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 1-13677

**MID PENN BANCORP, INC.**

(Exact Name of Registrant as Specified in its Charter)

**Pennsylvania**  
(State or Other Jurisdiction of

**25-1666413**  
(I.R.S. Employer Identification Number)

Incorporation or Organization)

**349 Union Street**

**Millersburg, Pennsylvania**  
(Address of Principal Executive Offices)

**17061**  
(Zip Code)

Registrant's telephone number, including area code **717.692.2133**

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

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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 definition 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

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

Yes  No

As of May 16, 2011, the registrant had 3,480,738 shares of common stock outstanding.

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<i>Unless the context otherwise requires, the terms "Mid Penn", "we", "us", and "our" refer to Mid Penn Bancorp, Inc. and its consolidated subsidiaries.</i>	

**Table of Contents****MID PENN BANCORP, INC.  
PART I FINANCIAL INFORMATION****Consolidated Balance Sheets (Unaudited)****ITEM 1 Financial Statements**

(Dollars in thousands, except share data)	March 31, 2011	December 31, 2010
<b>ASSETS</b>		
Cash and due from banks	\$ 7,440	\$ 6,779
Interest-bearing balances with other financial institutions	828	884
Federal funds sold	12,888	5,238
<b>Total cash and cash equivalents</b>	<b>21,156</b>	<b>12,901</b>
Interest-bearing time deposits with other financial institutions	61,226	55,041
Available for sale investment securities	95,689	70,702
Loans and leases, net of unearned interest	472,910	467,735
Less: Allowance for loan and lease losses	(7,172)	(7,061)
<b>Net loans and leases</b>	<b>465,738</b>	<b>460,674</b>
Bank premises and equipment, net	13,176	13,185
Restricted investment in bank stocks	3,638	3,828
Foreclosed assets held for sale	643	596
Accrued interest receivable	2,571	2,632
Deferred income taxes	2,866	2,875
Goodwill	1,016	1,016
Core deposit and other intangibles, net	333	351
Cash surrender value of life insurance	7,703	7,638
Other assets	4,537	6,018
<b>Total Assets</b>	<b>\$ 680,292</b>	<b>\$ 637,457</b>
<b>LIABILITIES &amp; SHAREHOLDERS EQUITY</b>		
Deposits:		
Noninterest bearing demand	\$ 63,647	\$ 60,228
Interest bearing demand	52,160	44,578
Money Market	243,170	209,936
Savings	27,276	26,466
Time	213,644	213,774
<b>Total Deposits</b>	<b>599,897</b>	<b>554,982</b>
Short-term borrowings	698	1,561
Long-term debt	22,838	27,883
Accrued interest payable	1,340	1,111
Other liabilities	6,414	3,719
<b>Total Liabilities</b>	<b>631,187</b>	<b>589,256</b>
Shareholders Equity:		
Preferred stock, par value \$1,000; authorized 10,000,000 shares; 5% cumulative dividend; 10,000 shares issued and outstanding at March 31, 2011 and December 31, 2010	10,000	10,000
Common stock, par value \$1 per share; 10,000,000 shares authorized; 3,480,738 shares issued and outstanding at March 31, 2011 and 3,479,780 at December 31, 2010	3,481	3,480
Additional paid-in capital	29,814	29,810

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Retained earnings	5,576	4,875
Accumulated other comprehensive income	234	36
Total Shareholders' Equity	49,105	48,201
Total Liabilities and Shareholders' Equity	\$ 680,292	\$ 637,457

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

**Table of Contents****MID PENN BANCORP, INC.****Consolidated Statements of Operations (Unaudited)**

(Dollars in thousands, except per share data)	Three Months Ended March 31,	
	2011	2010
<b>INTEREST INCOME</b>		
Interest & fees on loans and leases	\$ 6,735	\$ 6,712
Interest on interest-bearing time deposits with financial institutions	162	216
Interest and dividends on investment securities:		
U.S. Treasury and government agencies	222	163
State and political subdivision obligations, tax-exempt	323	257
Other securities	3	3
Interest on federal funds sold and securities purchased under agreements to resell	8	3
<b>Total Interest Income</b>	<b>7,453</b>	<b>7,354</b>
<b>INTEREST EXPENSE</b>		
Interest on deposits	2,195	2,472
Interest on short-term borrowings	2	11
Interest on long-term debt	273	370
<b>Total Interest Expense</b>	<b>2,470</b>	<b>2,853</b>
<b>Net Interest Income</b>	<b>4,983</b>	<b>4,501</b>
<b>PROVISION FOR LOAN AND LEASE LOSSES</b>	<b>200</b>	<b>160</b>
<b>Net Interest Income After Provision for Loan and Lease Losses</b>	<b>4,783</b>	<b>4,341</b>
<b>NONINTEREST INCOME</b>		
Income from fiduciary activities	95	65
Service charges on deposits	183	332
Earnings from cash surrender value of life insurance	65	68
Mortgage banking income	123	70
Other income	292	281
<b>Total Noninterest Income</b>	<b>758</b>	<b>816</b>
<b>NONINTEREST EXPENSE</b>		
Salaries and employee benefits	2,201	2,106
Occupancy expense, net	308	255
Equipment expense	344	358
Pennsylvania Bank Shares tax expense	121	102
FDIC Assessment	314	201
Legal and professional fees	87	138
Director fees and benefits expense	73	76
Marketing and advertising expense	63	68
Computer expense	166	136
Telephone expense	94	87
Loss on sale/write-down of foreclosed assets	(28)	132
Intangible amortization	16	16
Other expenses	541	594
<b>Total Noninterest Expense</b>	<b>4,300</b>	<b>4,269</b>
<b>INCOME BEFORE PROVISION FOR INCOME TAXES</b>	<b>1,241</b>	<b>888</b>

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Provision for (benefit from) income taxes	241	153
NET INCOME	1,000	735
Preferred stock dividends and discount accretion	128	128
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	\$ 872	\$ 607
PER COMMON SHARE DATA:		
Basic Earnings Per Common Share	\$ 0.25	\$ 0.17
Diluted Earnings Per Common Share	\$ 0.25	\$ 0.17
Cash Dividends	\$ 0.05	\$

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

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MID PENN BANCORP, INC.

Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

FOR THE THREE MONTHS ENDED MARCH 31, 2011 AND 2010

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
(Dollars in thousands, except share data)						
<b>Balance, December 31, 2010</b>	\$ 10,000	\$ 3,480	\$ 29,810	\$ 4,875	\$ 36	\$ 48,201
Comprehensive income:						
Net income				1,000		1,000
Change in net unrealized gain on securities available for sale, net of tax effects					197	197
Defined benefit plans, net of tax effects					1	1
Total comprehensive income						1,198
Cash dividends				(174)		(174)
Employee Stock Purchase Plan		1	7			8
Preferred dividends				(125)		(125)
Amortization of warrant cost			(3)			(3)
<b>Balance, March 31, 2011</b>	\$ 10,000	\$ 3,481	\$ 29,814	\$ 5,576	\$ 234	\$ 49,105
<b>Balance, December 31, 2009</b>	\$ 10,000	\$ 3,480	\$ 29,824	\$ 2,627	\$ 773	\$ 46,704
Comprehensive income:						
Net income				735		735
Change in net unrealized loss on securities available for sale, net of tax effects					(173)	(173)
Defined benefit plans, net of tax effects					4	4
Total comprehensive income						566
Preferred dividends				(125)		(125)
Amortization of warrant cost			(3)			(3)
<b>Balance, March 31, 2010</b>	\$ 10,000	\$ 3,480	\$ 29,821	\$ 3,237	\$ 604	\$ 47,142

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

**Table of Contents****MID PENN BANCORP, INC.****Consolidated Statements of Cash Flows (Unaudited)**

(Dollars in thousands)	Three Months Ended March 31,	
	2011	2010
<b>Operating Activities:</b>		
Net Income	\$ 1,000	\$ 735
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan and lease losses	200	160
Depreciation	324	319
Amortization of core deposit and other intangibles	18	13
Net amortization of securities premiums	1,140	42
Earnings on cash surrender value of life insurance	(65)	(68)
(Gain) loss on sale / write-down of foreclosed assets	(28)	132
Deferred income tax (benefit) liability	(90)	28
Decrease in accrued interest receivable	61	129
Decrease in other assets	1,476	59
Increase in accrued interest payable	229	149
Increase (decrease) in other liabilities	2,695	(18)
<b>Net Cash Provided by Operating Activities</b>	<b>6,960</b>	<b>1,680</b>
<b>Investing Activities:</b>		
Net (increase) decrease in interest-bearing balances	(6,185)	875
Proceeds from the maturity of investment securities	4,844	2,411
Purchases of investment securities	(30,672)	(5,602)
Redemptions of restricted investment in bank stock	190	
Net (increase) decrease in loans and leases	(5,513)	5,725
Purchases of bank premises and equipment	(315)	(694)
Proceeds from sale of foreclosed assets	230	178
<b>Net Cash (Used in) Provided by Investing Activities</b>	<b>(37,421)</b>	<b>2,893</b>
<b>Financing Activities:</b>		
Net increase in demand deposits and savings accounts	45,045	54,352
Net decrease in time deposits	(130)	(17,643)
Net decrease in short-term borrowings	(863)	(12,990)
Preferred stock dividend paid	(125)	(125)
Common stock dividend paid	(174)	
Employee Stock Purchase Plan	8	
Long-term debt repayment	(5,045)	(10,043)
<b>Net Cash Provided by Financing Activities</b>	<b>38,716</b>	<b>13,551</b>
Net increase in cash and cash equivalents	8,255	18,124
Cash and cash equivalents, beginning of period	12,901	8,960
Cash and cash equivalents, end of period	\$ 21,156	\$ 27,084
<b>Supplemental Disclosures of Cash Flow Information:</b>		
Interest paid	\$ 2,241	\$ 2,704
Income taxes paid		
<b>Supplemental Noncash Disclosures:</b>		
Transfers to foreclosed assets held for sale	\$ 249	\$ 153

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

**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)****1. Basis of Presentation**

The consolidated financial statements for 2011 and 2010 include the accounts of Mid Penn Bancorp, Inc. ( Mid Penn ), and its subsidiaries Mid Penn Bank (the Bank ) and Mid Penn Investment Corporation (collectively the Corporation ). All material intercompany accounts and transactions have been eliminated in consolidation.

Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission ( SEC ). We believe the information presented is not misleading and the disclosures are adequate. The results of operations for interim periods are not necessarily indicative of operating results expected for the full year. These interim consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in Mid Penn s Annual Report on Form 10-K for the year ended December 31, 2010.

Mid Penn has evaluated events and transactions occurring subsequent to the balance sheet date of March 31, 2011, for items that should potentially be recognized or disclosed in these consolidated financial statements. The evaluation was conducted through the date these consolidated financial statements were issued.

**2. Investment Securities**

Securities to be held for indefinite periods, but not intended to be held to maturity, are classified as available for sale and carried at fair value. Securities held for indefinite periods include securities that management intends to use as part of its asset and liability management strategy and that may be sold in response to liquidity needs, changes in interest rates, resultant prepayment risk, and other factors related to interest rate and resultant prepayment risk changes.

Realized gains and losses on dispositions are based on the net proceeds and the adjusted book value of the securities sold, using the specific identification method. Unrealized gains and losses on investment securities available for sale are based on the difference between book value and fair value of each security. These gains and losses are credited or charged to other comprehensive income, whereas realized gains and losses flow through Mid Penn s results of operations.

Accounting Standards Codification ( ASC ) Topic 320, *Investments – Debt and Equity Securities*, clarifies the interaction of the factors that should be considered when determining whether a debt security is other-than-temporarily impaired. For debt securities, management must assess whether (a) it has the intent to sell the security and (b) it is more likely than not that it will be required to sell the security prior to its anticipated recovery. These steps are done before assessing whether the entity will recover the cost basis of the investment. Previously, this assessment required management to assert it has both the intent and the ability to hold a security for a period of time sufficient to allow for an anticipated recovery in fair value to avoid recognizing other-than-temporary impairment. This change does not affect the need to forecast recovery of the value of the security through either cash flows or market price.

In instances when a determination is made that other-than-temporary impairment exists but the investor does not intend to sell the debt security and it is not more likely than not that it will be required to sell the debt security prior to its anticipated recovery, this guidance changes the presentation and amount of the other-than-temporary impairment recognized in the income statement. The other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

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At March 31, 2011 and December 31, 2010, amortized cost, fair value, and unrealized gains and losses on investment securities are as follows:

<b>(Dollars in thousands)</b>	<b>Amortized Cost</b>	<b>Unrealized Gains</b>	<b>Unrealized Losses</b>	<b>Fair Value</b>
<b>March 31, 2011</b>				
Available-for-sale securities:				
U.S. Treasury and U.S. government agencies	\$ 25,512	\$ 657	\$	\$ 26,169
Mortgage-backed U.S. government agencies	40,432	258	159	40,531
State and political subdivision obligations	28,930	592	774	28,748
Equity securities	250		9	241
	<b>\$ 95,124</b>	<b>\$ 1,507</b>	<b>\$ 942</b>	<b>\$ 95,689</b>

<b>(Dollars in thousands)</b>	<b>Amortized Cost</b>	<b>Unrealized Gains</b>	<b>Unrealized Losses</b>	<b>Fair Value</b>
<b>December 31, 2010</b>				
Available-for-sale securities:				
U.S. Treasury and U.S. government agencies	\$ 16,726	\$ 668	\$	\$ 17,394
Mortgage-backed U.S. government agencies	25,528	144	285	25,387
State and political subdivision obligations	27,932	481	735	27,678
Equity securities	250		7	243
	<b>\$ 70,436</b>	<b>\$ 1,293</b>	<b>\$ 1,027</b>	<b>\$ 70,702</b>

Estimated fair values of debt securities are based on quoted market prices, where applicable. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments, adjusted for differences between the quoted instruments and the instruments being valued.

Included in equity securities is an investment in Access Capital Strategies, an equity fund that invests in low to moderate income financing projects. This investment was purchased in 2004 to help fulfill the Bank's regulatory requirement of the Community Reinvestment Act and at March 31, 2011 and December 31, 2010, is reported at fair value.

Investment securities having a fair value of \$83,018,000 at March 31, 2011, and \$37,259,000 at December 31, 2010, were pledged to secure public deposits and other borrowings.

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The following table presents gross unrealized losses and fair value of investments aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at March 31, 2011 and December 31, 2010.

(Dollars in thousands)	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
March 31, 2011						
Available-for-sale securities:						
Mortgage-backed U.S. government agencies	\$ 10,543	\$ 159	\$	\$	\$ 10,543	\$ 159
State and political subdivision obligations	11,356	756	857	18	12,213	774
Equity securities			241	9	241	9
Total temporarily impaired available for sale securities	\$ 21,899	\$ 915	\$ 1,098	\$ 27	\$ 22,997	\$ 942

(Dollars in thousands)	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2010						
Available-for-sale securities:						
Mortgage-backed U.S. government agencies	\$ 13,032	\$ 285	\$	\$	\$ 13,032	\$ 285
State and political subdivision obligations	11,318	668	808	67	12,126	735
Equity securities			243	7	243	7
Total temporarily impaired available for sale securities	\$ 24,350	\$ 953	\$ 1,051	\$ 74	\$ 25,401	\$ 1,027

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis; and more frequently when economic or market concerns warrant such evaluation. Consideration is given to the length of time and the extent to which the fair value has been less than cost, and the financial condition and near term prospects of the issuer. In addition, for debt securities, Mid Penn considers (a) whether management has the intent to sell the security, (b) it is more likely than not that management will be required to sell the security prior to its anticipated recovery, and (c) whether management expects to recover the entire amortized cost basis. For equity securities, management considers the intent and ability to hold securities until recovery of unrealized losses.

At March 31, 2011, Mid Penn had 26 debt securities with unrealized losses. These securities have depreciated 3.91% from their amortized cost basis. At December 31, 2010, 30 debt securities with unrealized losses had depreciated 3.60% from the amortized cost basis. These securities are issued by either the U.S. Government or other governmental agencies. These unrealized losses were determined principally by reference to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the U.S. Government or its agencies issued the securities, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. Based on the above conditions management has determined that no declines are deemed to be other-than-temporary.

The table below is the maturity distribution of investment securities at amortized cost and fair value at March 31, 2011 and December 31, 2010:

(Dollars in thousands)	March 31, 2011		December 31, 2010	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in 1 year or less	\$ 5,035	\$ 5,059	\$ 7,791	\$ 7,825
Due after 1 year but within 5 years	18,095	18,396	6,319	6,558
Due after 5 years but within 10 years	14,825	15,576	15,245	16,014
Due after 10 years	16,487	15,886	15,303	14,675

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	54,442	54,917	44,658	45,072
Mortgage-backed securities	40,432	40,531	25,528	25,387
Equity securities	250	241	250	243
	\$ 95,124	\$ 95,689	\$ 70,436	\$ 70,702

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Mortgage-backed securities at March 31, 2011 had an average life of 3.1 years compared to an average life of 3.7 years at December 31, 2010. New investment purchases in this category have longer average lives than the portfolio at December 31, 2010.

***3. Loans and Allowance for Loan and Lease Losses***

Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, net of an allowance for loan losses and any deferred fees or costs. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the yield (interest income) of the related loans. These amounts are generally being amortized over the contractual life of the loan. Premiums and discounts on purchased loans are amortized as adjustments to interest income using the effective yield method.

The loan portfolio is segmented into commercial and consumer loans. Commercial loans consist of the following classes: commercial and industrial, commercial real estate, commercial real estate-construction and lease financing. Consumer loans consist of the following classes: residential mortgage loans, home equity loans and other consumer loans.

For all classes of loans, the accrual of interest is discontinued when the contractual payment of principal or interest has become 90 days or more past due or management has serious doubts about further collectability of principal or interest, even though the loan is currently performing. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed and unpaid interest accrued in prior years is charged against the allowance for loan and lease losses. Interest received on nonaccrual loans, including impaired loans, generally is either applied against principal or reported as interest income, according to management's judgment as to the collectability of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt. The past due status of all classes of loans receivable is determined based on contractual due dates for loan payments.

***Commercial and industrial***

Mid Penn originates commercial and industrial loans. Most of the Bank's commercial and industrial loans have been extended to finance local and regional businesses and include short-term loans to finance machinery and equipment purchases, inventory, and accounts receivable. Commercial loans also involve the extension of revolving credit for a combination of equipment acquisitions and working capital in expanding companies.

The maximum term for loans extended on machinery and equipment is based on the projected useful life of such machinery and equipment. Generally, the maximum term on non-mortgage lines of credit is one year. The loan-to-value ratio on such loans and lines of credit generally may not exceed 80% of the value of the collateral securing the loan. The Bank's commercial business lending policy includes credit file documentation and analysis of the borrower's character, capacity to repay the loan, the adequacy of the borrower's capital and collateral as well as an evaluation of conditions affecting the borrower. Analysis of the borrower's past, present, and future cash flows is also an important aspect of the Bank's current credit analysis. Nonetheless, such loans are believed to carry higher credit risk than more traditional investments.

Commercial and industrial loans typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of commercial business loans may be substantially dependent on the success of the business itself, which, in turn, is likely to be dependent upon the general economic environment. Mid Penn's commercial and industrial loans are usually, but not always, secured by business assets and personal guarantees. However, the collateral securing the loans may depreciate over time, may be difficult to appraise, and may fluctuate in value based on the success of the business.

***Commercial real estate and commercial real estate - construction***

Commercial real estate and commercial real estate construction loans generally present a higher level of risk than loans secured by one to four family residences. This greater risk is due to several factors, including the concentration of principal in a limited number of loans and borrowers, the effect of general economic conditions on income producing properties, and the increased difficulty of evaluating and monitoring these types of loans. In addition, the repayment of loans secured by commercial real estate is typically dependent upon the successful operation of the related real estate project. If the cash flow from the project is reduced, the borrower's ability to repay the loan may be impaired.

*Lease financing*

Mid Penn originates leases for select commercial and state and municipal government lessees. The nature of the leased asset is often subject to rapid depreciation in salvage value over a relatively short time frame or may be of an industry specific nature, making appraisal or liquidation of the asset difficult. These factors have led the Bank to severely curtail the origination of new leases to state or municipal government agencies where default risk is extremely limited and to only the most credit-worthy commercial customers. These commercial customers are primarily leasing fleet vehicles for use in their primary line of business, mitigating some of the asset value concerns within the portfolio. Leasing has been a declining percentage of the Mid Penn's portfolio since 2006, declining 59% during that period.

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**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)***Residential mortgage*

Mid Penn offers a wide array of residential mortgage loans for both permanent structures and those under construction. The Bank's residential mortgage originations are secured primarily by properties located in its primary market and surrounding areas. Residential mortgage loans have terms up to a maximum of 30 years and with loan to value ratios up to 100% of the lesser of the appraised value of the security property or the contract price. Private mortgage insurance is generally required in an amount sufficient to reduce the Bank's exposure to at or below the 85% loan to value level. Residential mortgage loans generally do not include prepayment penalties.

In underwriting residential mortgage loans, the Bank evaluates both the borrower's ability to make monthly payments and the value of the property securing the loan. Most properties securing real estate loans made by Mid Penn are appraised by independent fee appraisers. The Bank generally requires borrowers to obtain an attorney's title opinion or title insurance and fire and property insurance (including flood insurance, if necessary) in an amount not less than the amount of the loan. Real estate loans originated by the Bank generally contain a due on sale clause allowing the Bank to declare the unpaid principal balance due and payable upon the sale of the security property.

The Bank underwrites residential mortgage loans to the standards established by the secondary mortgage market, i.e., Fannie Mae, Ginnie Mae, Freddie Mac, or Pennsylvania Housing Finance Agency standards, with the intention of selling the majority of residential mortgages originated into the secondary market. In the event that the facts and circumstances surrounding a residential mortgage application do not meet all underwriting conditions of the secondary mortgage market, the Bank will evaluate the failed conditions and evaluate the potential risk of holding the residential mortgage in the Bank's portfolio rather than rejecting the loan request. In the event that the loan is held in the Bank's portfolio, the interest rate on the residential mortgage would be increased to compensate for the added portfolio risk.

*Consumer, including home equity*

Mid Penn offers a variety of secured consumer loans, including home equity, automobile, and deposit secured loans. In addition, the Bank offers other secured and unsecured consumer loans. Most consumer loans are originated in Mid Penn's primary market and surrounding areas.

The largest component of Mid Penn's consumer loan portfolio consists of fixed rate home equity loans and variable rate home equity lines of credit. Substantially all home equity loans and lines of credit are secured by second mortgages on principal residences. The Bank will lend amounts, which, together with all prior loans, typically may be up to 85% of the appraised value of the property securing the loan. Home equity term loans may have maximum terms up to 20 years while home equity lines of credit generally have maximum terms of five years.

Consumer loan terms vary according to the type and value of collateral, length of contract and creditworthiness of the borrower. The underwriting standards employed by the Bank for consumer loans include an application, a determination of the applicant's payment history on other debts and an assessment of ability to meet existing obligations and payments on the proposed loan. Although creditworthiness of the applicant is a primary consideration, the underwriting process also includes a comparison of the value of the collateral, if any, in relation to the proposed loan amount.

Consumer loans may entail greater credit risk than do residential mortgage loans, particularly in the case of consumer loans which are unsecured or are secured by rapidly depreciable assets, such as automobiles or recreational equipment. In such cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be affected by adverse personal circumstances. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans.

The allowance for credit losses consists of the allowance for loan and lease losses and the reserve for unfunded lending commitments. The allowance for loan and lease losses represents management's estimate of losses inherent in the loan portfolio as of the balance sheet date and is recorded as a reduction to loans. The reserve for unfunded lending commitments represents management's estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated balance sheet. The allowance for loan and lease losses is increased by the provision for loan and lease losses, and decreased by charge-offs, net of recoveries. Loans deemed to be uncollectible are charged against the allowance for loan and lease losses, and subsequent recoveries, if any, are credited to the allowance. All, or part, of the principal balance of loans are charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely. Non-residential consumer loans are generally charged off no later than 120 days past due on a contractual basis, earlier in the event of Bankruptcy, or if there is an amount deemed uncollectible. Because all identified losses are immediately charged off, no portion of the

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allowance for loan and lease losses is restricted to any individual loan or groups of loans, and the entire allowance is available to absorb any and all loan losses.

The allowance for credit losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management performs a monthly evaluation of the adequacy of the allowance. The allowance is based on Mid Penn's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revision as more information becomes available.

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**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)**

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, an allowance is established when the discounted cash flows, collateral value, or observable market price of the impaired loan is lower than the carrying value of that loan. The general component covers pools of loans by loan class including commercial loans not considered impaired, as well as smaller balance homogeneous loans, such as residential real estate, home equity and other consumer loans. These pools of loans are evaluated for loss exposure based upon historical loss rates for each of these categories of loans, adjusted for qualitative factors. These qualitative risk factors include changes in economic conditions, fluctuations in loan quality measures, changes in the experience of the lending staff and loan review systems, growth or changes in the mix of loans originated, and shifting industry or portfolio concentrations.

Each factor is assigned a value to reflect improving, stable or declining conditions based on management's best judgment using relevant information available at the time of the evaluation. Adjustments to the factors are supported through documentation of changes in conditions in a narrative accompanying the allowance for loan loss calculation.

Mid Penn considers a commercial loan (consisting of commercial and industrial, commercial real estate, commercial real estate-construction, and lease financing loan classes) to be impaired when it becomes 90 days or more past due and not in the process of collection. This methodology assumes the borrower cannot or will not continue to make additional payments. At that time the loan would be considered collateral dependent as the discounted cash flow (DCF) method indicates no operating income is available for evaluating the collateral position; therefore, all impaired loans are deemed to be collateral dependent.

In addition, Mid Penn's rating system assumes any loans classified as sub-standard non-accrual to be impaired, and all of these loans are considered collateral dependent; therefore, all of Mid Penn's impaired loans, whether reporting a specific allocation or not, are considered collateral dependent.

Mid Penn evaluates loans for charge-off on a monthly basis. Policies that govern the recommendation for charge-off are unique to the type of loan being considered. Commercial loans rated as nonaccrual or lower will first have a collateral evaluation completed in accordance with the guidance on impaired loans. Once the collateral evaluation has been completed, a specific allocation of allowance is made based upon the results of the evaluation. In the event the loan is unsecured, the loan would have been charged-off at the recognition of impairment. If the loan is secured, it will undergo a 90 day waiting period to ensure the collateral shortfall identified in the evaluation is accurate and then charged down by the specific allocation. Once the charge down is taken, the remaining balance remains a nonperforming loan with the original terms and interest rate intact (not restructured). Commercial loans secured by real estate rated as impaired will also have an initial collateral evaluation completed in accordance with the guidance on impaired loans. An updated real estate valuation is ordered and the collateral evaluation is modified to reflect any variations in value. A specific allocation of allowance is made for any anticipated collateral shortfall and a 90 day waiting period begins to ensure the accuracy of the collateral shortfall. The loan is then charged down by the specific allocation. Once the charge down is taken, the remaining balance remains a nonperforming loan with the original terms and interest rate intact (not restructured). The process of charge-off for residential mortgage loans begins upon a loan becoming delinquent for 90 days and not in the process of collection. The existing appraisal is reviewed and a lien search is obtained to determine lien position and any instances of intervening liens. A new appraisal of the property will be ordered if deemed necessary by management and a collateral evaluation is completed. The loan will then be charged down to the value indicated in the evaluation. Consumer loans (including home equity loans and other consumer loans) are recommended for charge-off after reaching delinquency of 90 days and the loan is not in the process of collection. The entire balance of the consumer loan is recommended for charge-off at this point.

As noted above, Mid Penn assesses a specific allocation for commercial loans prior to charging down or charging off the loan. Once the charge down is taken, the remaining balance remains a nonperforming loan with the original terms and interest rate intact (not restructured). In addition, Mid Penn takes a preemptive step when any commercial loan becomes classified under its internal classification system. A preliminary collateral evaluation in accordance with the guidance on impaired loans is prepared using the existing collateral information in the loan file. This process allows Mid Penn to review both the credit and documentation files to determine the status of the information needed to make a collateral evaluation. This collateral evaluation is preliminary but allows Mid Penn to determine if any potential collateral shortfalls exist.

It is Mid Penn's policy to obtain updated third party valuations on all impaired loans collateralized by real estate within 30 days of the credit being classified as sub-standard non-accrual. Prior to receipt of the updated real estate valuation Mid Penn will use any existing real estate valuation to determine any potential allowance issues; however no allowance recommendation will be made until which time Mid Penn is in receipt of the updated valuation. The credit department employs an electronic tracking system to monitor the receipt of and need for updated appraisals. To date, there have been no significant time lapses noted with the above processes.

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In some instances Mid Penn is not holding real estate as collateral and is relying on business assets (personal property) for repayment. In these circumstances a collateral inspection is performed by Mid Penn personnel to determine an estimated value. The value is based on net book value, as provided by the financial statements, and discounted accordingly based on determinations made by management. Occasionally, Mid Penn will employ an outside service to provide a fair estimate of value based on auction sales or private sales. Management reviews the estimates of these third parties and discounts them accordingly based on management's judgment, if deemed necessary.

For impaired loans with no valuation allowance required, Mid Penn's practice of obtaining independent third party market valuations on the

**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)**

subject property within 30 days of being placed on non-accrual status sometimes indicates that the loan to value ratio is sufficient to obviate the need for a specific allocation in spite of significant deterioration in real estate values in Mid Penn's primary market area. These circumstances are determined on a case by case analysis of the impaired loans.

Mid Penn actively monitors the values of collateral on impaired loans. This monitoring may require the modification of collateral values over time or changing circumstances by some factor, either positive or negative, from the original values. All collateral values will be assessed by management at least every 18 months for possible revaluation by an independent third party.

Mid Penn does not currently, or plan in the future to, use automated valuation methodologies as a method of valuing real estate collateral.

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, Mid Penn does not separately identify individual residential mortgage loans, home equity loans and other consumer loans for impairment disclosures, unless such loans are the subject of a troubled debt restructuring agreement.

Loans whose terms are modified are classified as troubled debt restructurings if the borrowers have been granted concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring generally involve a temporary reduction in interest rate or an extension of a loan's stated maturity date. Non-accrual troubled debt restructurings are restored to accrual status if principal and interest payments, under the modified terms, are current for six consecutive months after modification. Loans classified as troubled debt restructurings are designated as impaired.

The allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower's overall financial condition, repayment sources, guarantors, and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments. Credit quality risk ratings include regulatory classifications of special mention, substandard, doubtful, and loss. Loans criticized as special mention have potential weaknesses that deserve management's close attention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They include loans that are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified doubtful have all the weaknesses inherent in loans classified substandard with the added characteristic that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans classified as a loss are considered uncollectible and are charged to the allowance for loan losses. Any loans not classified as noted above are rated pass.

In addition, Federal regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan and lease losses and may require the Bank to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management. Based on management's comprehensive analysis of the loan portfolio, management believes the current level of the allowance for loan losses is adequate.

The classes of the loan portfolio, summarized by the aggregate pass rating and the classified ratings of special mention, substandard, and doubtful within Mid Penn's internal risk rating system as of March 31, 2011 and December 31, 2010 are as follows:

(Dollars in thousands)

March 31, 2011	Pass	Special Mention	Substandard	Doubtful	Total
Commercial and industrial	\$ 67,264	\$ 1,737	\$ 2,916	\$	\$ 71,917
Commercial real estate	280,407	7,324	15,207		302,938
Commercial real estate - construction	19,419	2,908	1,055		23,382
Lease financing	1,998		254		2,252
Residential mortgage	42,897		79		42,976

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Home equity	20,870	273	365	21,508
Consumer	7,510	427		7,937
	\$ 440,365	\$ 12,669	\$ 19,876	\$ 472,910

**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)**

(Dollars in thousands)

<b>December 31, 2010</b>	<b>Pass</b>	<b>Special Mention</b>	<b>Substandard</b>	<b>Doubtful</b>	<b>Total</b>
Commercial and industrial	\$ 63,195	\$ 1,830	\$ 2,803	\$	\$ 67,828
Commercial real estate	262,743	6,421	16,537		285,701
Commercial real estate - construction	34,495	2,768	1,565		38,828
Lease financing	2,177		277		2,454
Residential mortgage	43,960		106		44,066
Home equity	19,708	308	352		20,368
Consumer	8,058	432			8,490
	\$ 434,336	\$ 11,759	\$ 21,640	\$	\$ 467,735

Impaired loans by loan portfolio class as of March 31, 2011 and December 31, 2010 are summarized as follows:

(Dollars in thousands)

<b>March 31, 2011</b>	<b>Recorded Investment</b>	<b>Unpaid Principal Balance</b>	<b>Related Allowance</b>	<b>Average Recorded Investment</b>	<b>Interest Income Recognized (1)</b>
<b>With no related allowance recorded:</b>					
Commercial and industrial	\$ 639	\$ 975	\$	\$ 853	\$
Commercial real estate	5,794	9,295		7,713	1
Commercial real estate - construction	925	941		1,331	
Lease financing	170	212		182	
Residential mortgage	69	99		84	1
Home equity	111	498		282	
<b>With an allowance recorded:</b>					
Commercial and industrial	\$ 1,094	\$ 2,307	\$ 752	\$ 1,372	\$
Commercial real estate	4,585	6,266	1,194	4,790	
Residential mortgage	10	10	10	10	
Home equity	21	24	21	24	
<b>Total:</b>					
Commercial and industrial	\$ 1,733	\$ 3,282	\$ 752	\$ 2,225	\$
Commercial real estate	10,379	15,561	1,194	12,503	1
Commercial real estate - construction	925	941		1,331	
Lease financing	170	212		182	
Residential mortgage	79	109	10	94	1
Home equity	132	522	21	306	

(1) Represents interest income recognized for the three months ended March 31, 2011

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(Dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized (2)
<b>December 31, 2010</b>					
With no related allowance recorded:					
Commercial and industrial	\$ 766	\$ 1,730	\$	\$ 1,222	\$ 11
Commercial real estate	7,414	10,642		9,317	
Commercial real estate - construction	1,565	1,957		1,858	
Lease financing	169	211		181	
Residential mortgage	96	99		97	
Home equity	113	516		283	
With an allowance recorded:					
Commercial and industrial	\$ 896	\$ 1,518	\$ 685	\$ 938	\$
Commercial real estate	4,218	5,839	1,166	4,384	
Residential mortgage	10	10	10	10	
Home equity	22	113	22	25	
<b>Total:</b>					
Commercial and industrial	\$ 1,662	\$ 3,248	\$ 685	\$ 2,160	\$ 11
Commercial real estate	11,632	16,481	1,166	13,701	
Commercial real estate - construction	1,565	1,957		1,858	
Lease financing	169	211		181	
Residential mortgage	106	109	10	107	
Home equity	135	629	22	308	

(2) Represents interest income recognized for the year ended December 31, 2010

Non-accrual loans by loan portfolio class as of March 31, 2011 and December 31, 2010 are summarized as follows:

(Dollars in thousands)	March 31, 2011	December 31, 2010
Commercial and industrial	\$ 1,910	\$ 1,839
Commercial real estate	10,499	11,878
Commercial real estate - construction	926	1,565
Lease financing	177	219
Residential mortgage	1,176	1,376
Home equity	316	320
Consumer	20	31
	\$ 15,024	\$ 17,228

**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)**

The performance and credit quality of the loan portfolio is also monitored by analyzing the age of the loans receivable as determined by the length of time a recorded payment is past due. The classes of the loan portfolio summarized by the past due status as of March 31, 2011 and December 31, 2010 are summarized as follows:

(Dollars in thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans	Loans Receivable > 90 Days and Accruing
<b>March 31, 2011</b>							
Commercial and industrial	\$ 179	\$ 80	\$ 1,678	\$ 1,937	\$ 69,980	\$ 71,917	\$ 35
Commercial real estate	1,857		5,887	7,744	295,194	302,938	
Commercial real estate - construction			469	469	22,913	23,382	
Lease financing	26		1	27	2,225	2,252	1
Residential mortgage	759		1,097	1,856	41,120	42,976	356
Home equity	11	49	238	298	21,210	21,508	
Consumer	23		19	42	7,895	7,937	
<b>Total</b>	<b>\$ 2,855</b>	<b>\$ 129</b>	<b>\$ 9,389</b>	<b>\$ 12,373</b>	<b>\$ 460,537</b>	<b>\$ 472,910</b>	<b>\$ 392</b>

(Dollars in thousands)	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans	Loans Receivable > 90 Days and Accruing
<b>December 31, 2010</b>							
Commercial and industrial	\$ 112	\$ 186	\$ 1,652	\$ 1,950	\$ 65,878	\$ 67,828	\$
Commercial real estate	1,670	469	4,954	7,093	278,608	285,701	
Commercial real estate - construction			931	931	37,897	38,828	
Lease financing			1	1	2,453	2,454	1
Residential mortgage	823	133	870	1,826	42,240	44,066	
Home equity	330		238	568	19,800	20,368	
Consumer	369	11	49	429	8,061	8,490	18
<b>Total</b>	<b>\$ 3,304</b>	<b>\$ 799</b>	<b>\$ 8,695</b>	<b>\$ 12,798</b>	<b>\$ 454,937</b>	<b>\$ 467,735</b>	<b>\$ 19</b>

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The allowance for loan and lease losses and recorded investment in financing receivables as of March 31, 2011 and December 31, 2010 are as follows:

(Dollars in thousands)	Commercial real estate -									Total
March 31, 2011	Commercial and industrial	Commercial real estate	construction	Lease financing	Residential mortgage	Home equity	Consumer	Unallocated	Total	
<b>Allowance for loan and lease losses:</b>										
Beginning Balance	\$ 2,447	\$ 3,616	\$ 159	\$ 1	\$ 219	\$ 363	\$ 61	\$ 195	\$ 7,061	
Charge-offs		(40)			(32)		(51)		(123)	
Recoveries	9	9		5	1	3	7		34	
Provisions	(14)	248	22	(5)	122	(46)	32	(159)	200	
Ending balance	\$ 2,442	\$ 3,833	\$ 181	\$ 1	\$ 310	\$ 320	\$ 49	\$ 36	\$ 7,172	
Ending balance: individually evaluated for impairment	\$ 752	\$ 1,194	\$	\$	\$ 10	\$ 21	\$	\$	\$ 1,977	
Ending balance: collectively evaluated for impairment	\$ 1,690	\$ 2,639	\$ 181	\$ 1	\$ 300	\$ 299	\$ 49	\$ 36	\$ 5,195	
<b>Loans receivables:</b>										
Ending balance	\$ 71,917	\$ 302,938	\$ 23,382	\$ 2,252	\$ 42,976	\$ 21,508	\$ 7,937	\$	\$ 472,910	
Ending balance: individually evaluated for impairment	\$ 1,733	\$ 10,379	\$ 925	\$ 170	\$ 79	\$ 132	\$	\$	\$ 13,418	
Ending balance: collectively evaluated for impairment	\$ 70,184	\$ 292,559	\$ 22,457	\$ 2,082	\$ 42,897	\$ 21,376	\$ 7,937	\$	\$ 459,492	
<b>Commercial real estate -</b>										
(Dollars in thousands)	Commercial and industrial	Commercial real estate	construction	Lease financing	Residential mortgage	Home equity	Consumer	Unallocated	Total	
<b>December 31, 2010</b>										
<b>Allowance for loan and lease losses:</b>										
Ending balance	\$ 2,447	\$ 3,616	\$ 159	\$ 1	\$ 219	\$ 363	\$ 61	\$ 195	\$ 7,061	
Ending balance: individually evaluated for impairment	\$ 685	\$ 1,166	\$	\$	\$ 10	\$ 22	\$	\$	\$ 1,883	
Ending balance: collectively evaluated for impairment	\$ 1,762	\$ 2,450	\$ 159	\$ 1	\$ 209	\$ 341	\$ 61	\$ 195	\$ 5,178	
<b>Loans receivables:</b>										
Ending balance	\$ 67,828	\$ 285,701	\$ 38,828	\$ 2,454	\$ 44,066	\$ 20,368	\$ 8,490	\$	\$ 467,735	
	\$ 1,662	\$ 11,632	\$ 1,565	\$ 169	\$ 106	\$ 135	\$	\$	\$ 15,269	

Ending balance: individually  
evaluated for impairment

Ending balance: collectively  
evaluated for impairment

\$ 66,166	\$ 274,069	\$ 37,263	\$ 2,285	\$ 43,960	\$ 20,233	\$ 8,490	\$	\$ 452,466
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**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)*****4. Fair Value Measurements***

Fair value measurement and disclosure guidance defines fair value as the price that would be received to sell the asset or transfer the liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. This guidance provides additional information on determining when the volume and level of activity for the asset or liability has significantly decreased. The guidance also includes information on identifying circumstances when a transaction may not be considered orderly.

Fair value measurement and disclosure guidance provides a list of factors that a reporting entity should evaluate to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. When the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability, further analysis of the information from that market is needed and significant adjustments to the related prices may be necessary to estimate fair value in accordance with the fair value measurement and disclosure guidance.

This guidance clarifies that when there has been a significant decrease in the volume and level of activity for the asset or liability, some transactions may not be orderly. In those situations, the entity must evaluate the weight of the evidence to determine whether the transaction is orderly. The guidance provides a list of circumstances that may indicate that a transaction is not orderly. A transaction price that is not associated with an orderly transaction is given little, if any, weight when estimating fair value.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own belief about the assumptions market participants would use in pricing the asset or liability based upon the best information available in the circumstances. Fair value measurement and disclosure guidance establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

**Level 1 Inputs** Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

**Level 2 Inputs** Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability;

**Level 3 Inputs** Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

There were no transfers of assets between fair value Level 1 and Level 2 for the three months ended March 31, 2011. The following table illustrates the financial instruments measured at fair value on a recurring basis segregated by hierarchy fair value levels:

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MID PENN BANCORP, INC.

Notes to Consolidated Financial Statements (Unaudited)

## Fair value measurements at March 31, 2011 using:

(Dollars in thousands)

	Total carrying value at March 31, 2011	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
<b>Assets:</b>				
U.S. Treasury and U.S. government agencies	\$ 26,169	\$	\$ 26,169	\$
Mortgage-backed U.S. government agencies	40,531		40,531	
State and political subdivision obligations	28,748		28,748	
Equity securities	241	241		
	\$ 95,689	\$ 241	\$ 95,448	\$

## Fair value measurements at December 31, 2010 using:

(Dollars in thousands)

	Total carrying value at December 31, 2010	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
<b>Assets:</b>				
U.S. Treasury and U.S. government agencies	\$ 17,394	\$	\$ 17,394	\$
Mortgage-backed U.S. government agencies	25,387		25,387	
State and political subdivision obligations	27,678		27,678	
Equity securities	243	243		
	\$ 70,702	\$ 243	\$ 70,459	\$

Certain financial assets and financial liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis, but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

The following table illustrates the financial instruments measured at fair value on a nonrecurring basis segregated by hierarchy fair value levels:

## Fair value measurements at March 31, 2011 using:

(Dollars in thousands)

	Total carrying value at March 31, 2011	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
<b>Assets:</b>				
Impaired Loans	\$ 3,733	\$	\$	\$ 3,733
Foreclosed Assets Held for Sale	234			234

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Fair value measurements at December 31, 2010 using:

(Dollars in thousands)

Assets:	Total carrying value at December 31, 2010	Quoted prices in active		Significant unobservable inputs (Level 3)
		markets (Level 1)	Significant other observable inputs (Level 2)	
Impaired Loans	\$ 3,263	\$	\$	\$ 3,263
Foreclosed Assets Held for Sale	299			299

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**MID PENN BANCORP, INC.**

**Notes to Consolidated Financial Statements (Unaudited)**

ASC Topic 825, *Financial Instruments*, requires disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements.

The following methodologies and assumptions were used to estimate the fair value of Mid Penn's financial instruments:

***Cash and Cash Equivalents:***

The carrying value of cash and cash equivalents is considered to be a reasonable estimate of fair value.

***Interest-bearing Balances with other Financial Institutions:***

The estimate of fair value was determined by comparing the present value of quoted interest rates on like deposits with the weighted average yield and weighted average maturity of the balances.

***Securities Available for Sale:***

The fair value of securities classified as available for sale is determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or matrix pricing (level 2), which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities but rather relying on the securities' relationship to other benchmark quoted prices.

***Impaired Loans:***

Mid Penn's rating system assumes any loans classified as sub-standard non-accrual to be impaired, and all of these loans are considered collateral dependent; therefore, all of Mid Penn's impaired loans, whether reporting a specific allocation or not, are considered collateral dependent.

It is Mid Penn's policy to obtain updated third party valuations on all impaired loans collateralized by real estate within 30 days of the credit being classified as sub-standard non-accrual. Prior to receipt of the updated real estate valuation Mid Penn will use any existing real estate valuation to determine any potential allowance issues; however no allowance recommendation will be made until which time Mid Penn is in receipt of the updated valuation.

In some instances Mid Penn is not holding real estate as collateral and is relying on business assets (personal property) for repayment. In these circumstances a collateral inspection is performed by Mid Penn personnel to determine an estimated value. The value is based on net book value, as provided by the financial statements, and discounted accordingly based on determinations made by management. Occasionally, Mid Penn will employ an outside service to provide a fair estimate of value based on auction sales or private sales. Management reviews the estimates of these third parties and discounts them accordingly based on management's judgment, if deemed necessary. Mid Penn considers the estimates used in its impairment analysis to be Level 3 inputs.

Mid Penn actively monitors the values of collateral on impaired loans. This monitoring may require the modification of collateral values over time or changing circumstances by some factor, either positive or negative, from the original values. All collateral values will be assessed by management at least every 18 months for possible revaluation by an independent third party.

Mid Penn does not currently, or plan to in the future, use automated valuation methodologies as a method of valuing real estate collateral.

***Loans:***

For variable-rate loans that reprice frequently and which entail no significant changes in credit risk, carrying values approximated fair value. The fair value of other loans are estimated by calculating the present value of the cash flow difference between the current rate and the market rate, for the average maturity, discounted quarterly at the market rate.

***Foreclosed Assets Held for Sale:***

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Assets included in foreclosed assets held for sale are carried at fair value and accordingly is presented as measured on a non-recurring basis. Values are estimated using Level 3 inputs, based on appraisals that consider the sales prices of property in the proximate vicinity.

### ***Accrued Interest Receivable and Payable:***

The carrying amount of accrued interest receivable and payable approximates their fair values.

### ***Restricted Investment in Bank Stocks:***

The carrying amount of required and restricted investment in correspondent bank stock approximates fair value, and considers the limited marketability of such securities.

### ***Deposits:***

The fair value for demand deposits (e.g., interest and noninterest checking, savings, and money market deposit accounts) is by definition, equal to the amount payable on demand at the reporting date (i.e. their carrying amounts). Fair value for fixed-rate certificates of deposit was estimated using a discounted cash flow calculation by combining all fixed-rate certificates into a pool with a weighted average yield and a weighted average maturity for the pool and comparing the pool with interest rates currently being offered on a similar maturity.

**Table of Contents****MID PENN BANCORP, INC.****Notes to Consolidated Financial Statements (Unaudited)****Short-term Borrowings:**

Because of time to maturity, the estimated fair value of short-term borrowings approximates the book value.

**Long-term Debt:**

The estimated fair values of long-term debt were determined using discounted cash flow analysis, based on currently available borrowing rates for similar types of borrowing arrangements.

**Commitments to Extend Credit and Letters of Credit:**

The fair value of commitments to extend credit is estimated using the fees currently charged to enter into similar agreements, taking into account market interest rates, the remaining terms and present credit worthiness of the counterparties. The fair value of guarantees and letters of credit is based on fees currently charged for similar agreements.

The following table summarizes the carrying value and fair value of financial instruments at March 31, 2011 and December 31, 2010.

(Dollars in thousands)	March 31, 2011		December 31, 2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<b>Financial assets:</b>				
Cash and cash equivalents	\$ 21,156	\$ 21,156	\$ 12,901	\$ 12,901
Interest-bearing balances with other financial institutions	63,870	63,870	55,041	55,041
Investment securities	93,045	93,045	70,702	70,702
Net loans and leases	472,910	484,405	460,674	481,248
Restricted investment in bank stocks	3,638	3,638	3,828	3,828
Accrued interest receivable	2,571	2,571	2,632	2,632
<b>Financial liabilities:</b>				
Deposits	\$ 599,897	\$ 605,945	\$ 554,982	\$ 560,843
Short-term borrowings	698	698	1,561	1,561
Long-term debt	22,838	23,891	27,883	28,318
Accrued interest payable	1,340	1,340	1,111	1,111
<b>Off-balance sheet financial instruments:</b>				
Commitments to extend credit	\$	\$	\$	\$
Financial standby letters of credit				

**5. Guarantees**

In the normal course of business, Mid Penn makes various commitments and incurs certain contingent liabilities, which are not reflected in the accompanying consolidated financial statements. The commitments include various guarantees and commitments to extend credit. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Mid Penn evaluates each customer's credit-worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the customer. Standby letters of credit and financial guarantees written are conditional commitments to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. Mid Penn had \$10,480,000 and \$10,048,000 of standby letters of credit outstanding as of March 31, 2011 and December 31, 2010, respectively. Mid Penn does not anticipate any losses because of these transactions. The current amount of the liability as of March 31, 2011 for payment under standby letters of credit issued was not material.



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MID PENN BANCORP, INC.

Notes to Consolidated Financial Statements (Unaudited)

**6. Short-term Borrowings**

Short-term borrowings as of March 31, 2011 and December 31, 2010 consisted of:

(Dollars in thousands)	March 31, 2011	December 31, 2010
Securities sold under repurchase agreements	\$ 245	\$ 578
Treasury, tax and loan notes	453	983
	\$ 698	\$ 1,561

Short-term borrowings are comprised primarily of securities sold under repurchase agreements. Investment securities are pledged in sufficient amounts to collateralize repurchase agreements. Treasury tax and loan notes are open-ended interest bearing notes payable to the U.S. Treasury upon call. All tax deposits accepted by the Bank are placed in the Treasury note option account.

**7. Long-term Debt**

During the three months ended March 31, 2011, the Bank entered into no additional long-term borrowings with the Federal Home Loan Bank of Pittsburgh. During the three months ended March 31, 2010, \$5,000,000 in long-term borrowings, at an interest rate of 5.13%, with the Federal Home Loan Bank of Pittsburgh matured and were not renewed.

**8. Defined Benefit Plans**

Mid Penn has an unfunded noncontributory defined benefit retirement plan for directors. The plan provides defined benefits based on years of service. In addition, Mid Penn sponsors a defined benefit health care plan that provides post-retirement medical benefits and life insurance to qualifying full-time employees. These health care and life insurance plans are noncontributory. A December 31 measurement date for our plans is used.

The components of net periodic benefit costs from these benefit plans are as follows:

(Dollars in thousands)	Three Months Ended March 31,			
	Pension Benefits		Other Benefits	
	2011	2010	2011	2010
Service cost	\$ 6	\$ 6	\$ 5	\$ 5
Interest cost	13	13	11	11
Amortization of prior service cost	5	5		
Amortization of net gain				(3)
Net periodic benefit cost	\$ 24	\$ 24	\$ 16	\$ 13

**9. Comprehensive Income**

Accounting principles generally accepted in the United States of America require that recognized revenue, expenses, gains, and losses be included in net income. Changes in certain assets and liabilities such as unrealized gains (losses) on securities available for sale and the liability associated with defined benefit plans, are reported as a separate component of the shareholders' equity section of the balance sheet. Such items, along with net income, are components of comprehensive income. The components of other comprehensive income and the related tax effects are as follows:



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(Dollars in thousands)	Three Months Ended March 31,	
	2011	2010
Change in unrealized holding gains (losses) on available for sale securities	\$ 299	\$ (262)
Less reclassification adjustment for gains realized in income		
Net unrealized gains (losses)	299	(262)
Change in defined benefit plans	2	6
Other comprehensive income	301	(256)
Income tax effect	(103)	87
Net of tax amount	\$ 198	\$ (169)

The components of accumulated other comprehensive income, net of taxes, are as follows:

(Dollars in thousands)	Unrealized Gain on Securities	Defined Benefit Plan Liability	Accumulated Other Comprehensive Income
Balance March 31, 2011	\$ 373	\$ (139)	\$ 234
Balance December 31, 2010	\$ 176	\$ (140)	\$ 36

**10. Preferred Stock**

On December 19, 2008, Mid Penn entered into and closed a Letter Agreement with the United States Department of the Treasury (the Treasury) pursuant to which the Treasury invested \$10,000,000 in Mid Penn under the Treasury's Capital Purchase Program (the CPP).

Under the CPP, the Treasury received (1) 10,000 shares of Series A Fixed Rate Cumulative Perpetual Preferred Stock, \$1,000 liquidation preference, and (2) Warrants to purchase up to 73,099 shares of Mid Penn's common stock at an exercise price of \$20.52 per share. The \$10,000,000 in new capital is treated as Tier 1 Capital.

The Series A Preferred Stock pays cumulative dividends at a rate of 5% per annum for the first five years and 9% per annum thereafter. Pursuant to the American Recovery and Reinvestment Act of 2009, the Secretary of the Treasury is required to permit, subject to consultation with the appropriate Federal banking agency, Mid Penn to redeem the Series A Preferred Stock. Mid Penn may do so without regard to the source of the funds to be used to redeem the Series A Preferred Stock or any minimum waiting period. If Mid Penn elects to redeem the Series A Preferred Stock prior to February 15, 2012, and receives approval from the Treasury and the Board of Governors of the Federal Reserve System, it must redeem at least \$2,500,000 of the Series A Preferred Stock. Upon redemption of the Series A Preferred Stock, the Secretary of the Treasury must liquidate the warrants associated with Mid Penn's participation in the CPP at the current market price. Upon the appropriate approval, Mid Penn may redeem the Series A Preferred Stock at the original purchase price plus accrued but unpaid dividends, if any. The related Warrants expire in ten years and are immediately exercisable upon their issuance.

To participate in the program, Mid Penn is required to meet certain standards, including; (1) ensuring that incentive compensation for senior executives does not encourage unnecessary and excessive risk that threaten the value of Mid Penn; (2) requiring a clawback of any bonus or incentive compensation paid to a senior executive based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate; (3) prohibiting Mid Penn from making any golden parachute payment to specified senior executives; and (4) agreeing not to deduct for tax purposes executive compensation in excess of \$500,000 for each senior executive.

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Based on the Program term sheet provided by the Treasury, the following are the effects on holders of common stock from the issuance of Senior Preferred stock to the Treasury under the Program:

### ***Restrictions on Dividends***

For as long as any Senior Preferred shares are outstanding, no dividends can be declared or paid on common shares, nor can Mid Penn repurchase or redeem any common shares, unless all accrued and unpaid dividends for all past dividend periods on the Senior Preferred shares have been fully paid. In addition, the consent of the Treasury is required for any increase in the per share dividends on common shares until the third anniversary of the date of the Senior Preferred investment unless prior to such third anniversary, the Senior Preferred shares have been redeemed in whole or the Treasury has transferred all of the Senior Preferred shares to third parties.

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MID PENN BANCORP, INC.

Notes to Consolidated Financial Statements (Unaudited)

**Repurchases**

The Treasury's consent is required for any share repurchases (other than (1) repurchases of the Senior Preferred shares and (2) repurchases of common shares in connection with any benefit plan in the ordinary course of business consistent with past practice) until the third anniversary of the date of this investment unless prior to such third anniversary the Senior Preferred shares have been redeemed in whole or the Treasury has transferred all of the Senior Preferred shares to third parties. In addition, there can be no share repurchases of common shares if prohibited as described under "Restrictions on Dividends" above.

**Voting Rights**

The Senior Preferred shares are non-voting, other than class voting rights on (1) any authorization or issuance of shares ranking senior to the Senior Preferred shares, (2) any amendment to the rights of Senior Preferred, or (3) any merger, exchange or similar transaction which would adversely affect the rights of the Senior Preferred. If dividends on the Senior Preferred shares are not paid in full for six dividend periods, whether or not consecutive, the Senior Preferred shareholder(s) have the right to elect two directors. The right to elect directors would end when full dividends have been paid for four consecutive dividend periods.

**11. Earnings per Common Share**

Earnings per common share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during each of the periods presented giving retroactive effect to stock dividends and stock splits. The following data show the amounts used in computing basic and diluted earnings per common share. As shown in the table that follows, diluted earnings per common share is computed using weighted average common shares outstanding, plus weighted average common shares available from the exercise of all dilutive stock warrants issued to the U.S. Treasury under the provisions of the Capital Purchase Program, based on the average share price of Mid Penn's common stock during the period.

The computations of basic earnings per common share follow:

(Dollars in thousands, except per share data)	Three Months Ended March 31,	
	2011	2010
Net Income	\$ 1,000	\$ 735
Less: Dividends on preferred stock	(125)	(125)
Accretion of preferred stock discount	(3)	(3)
Net income available to common shareholders	\$ 872	\$ 607
Weighted average common shares outstanding	3,480,738	3,479,780
Basic earnings per common share	\$ 0.25	\$ 0.17

The computations of diluted earnings per common share follow:

(Dollars in thousands, except per share data)	Three Months Ended March 31,	
	2011	2010
Net income available to common shareholders	\$ 872	\$ 607
Weighted average number of common shares outstanding	3,480,738	3,479,780
Dilutive effect of potential common stock arising from stock warrants: Exercise of outstanding stock warrants issued to U.S. Treasury under the Capital Repurchase Program		
Adjusted weighted-average common shares outstanding	3,480,738	3,479,780
Diluted earnings per common share	\$ 0.25	\$ 0.17

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As of March 31, 2011, Mid Penn had 73,099 warrants that were anti-dilutive because the fair value of the common stock was below the \$20.52 exercise price of these warrants.

### ***12. Recent Accounting Pronouncements***

**ASU 2010-06:** The FASB has issued ASU 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*. This ASU requires some new disclosures and clarifies some existing disclosure requirements about fair value measurement as set forth in Codification Subtopic 820-10. The FASB's objective is to improve these disclosures and, thus, increase the transparency in financial reporting. Specifically, ASU 2010-06 amends Codification Subtopic 820-10 to now require:

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**MID PENN BANCORP, INC.**

**Notes to Consolidated Financial Statements (Unaudited)**

A reporting entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers; and

In the reconciliation for fair value measurements using significant unobservable inputs, a reporting entity should present separately information about purchases, sales, issuances, and settlements.

In addition, ASU 2010-06 clarifies the requirements of the following existing disclosures:

For purposes of reporting fair value measurement for each class of assets and liabilities, a reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities; and

A reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements.

ASU 2010-06 is effective for interim and annual reporting periods beginning after January 1, 2010, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. Mid Penn adopted the required provisions of ASU 2010-06, with no significant impact on its financial condition or results of operations.

**ASU 2010-28:** The amendments in this ASU modify Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that impairment may exist. The qualitative factors are consistent with the existing guidance and examples in paragraph 350-20-35-30, which requires that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount.

These amendments eliminate an entity's ability to assert that a reporting unit is not required to perform Step 2 because the carrying amount of the reporting unit is zero or negative despite the existence of qualitative factors that indicate the goodwill is more likely than not impaired. As a result, goodwill impairments may be reported sooner than under current practice.

For public entities, the amendments in this ASU are effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. Early adoption is not permitted. For nonpublic entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Nonpublic entities may early adopt the amendments using the effective date for public entities.

Upon adoption of the amendments, an entity with reporting units that have carrying amounts that are zero or negative is required to assess whether it is more likely than not that the reporting units' goodwill is impaired. If the entity determines that it is more likely than not that the goodwill of one or more of its reporting units is impaired, the entity should perform Step 2 of the goodwill impairment test for those reporting unit(s). Any resulting goodwill impairment should be recorded as a cumulative-effect adjustment to beginning retained earnings in the period of adoption. Any goodwill impairments occurring after the initial adoption of the amendments should be included in earnings as required by Section 350-20-35. The Corporation does not expect the adoption will have a significant impact on the Corporation's financial condition or results of operations.

**ASU 2010-29:** The objective of this ASU is to address diversity in practice about the interpretation of the pro forma revenue and earnings disclosure requirements for business combinations.

Paragraph 805-10-50-2(h) requires a public entity to disclose pro forma information for business combinations that occurred in the current reporting period. The disclosures include pro forma revenue and earnings of the combined entity for the current reporting period as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual reporting period. If comparative financial statements are presented, the pro forma revenue and earnings of the combined entity for the comparable prior reporting

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period should be reported as though the acquisition date for all business combinations that occurred during the current year had been as of the beginning of the comparable prior annual reporting period.

In practice, some preparers have presented the pro forma information in their comparative financial statements as if the business combination that occurred in the current reporting period had occurred as of the beginning of each of the current and prior annual reporting periods. Other preparers have disclosed the pro forma information as if the business combination occurred at the beginning of the prior annual reporting period only, and carried forward the related adjustments, if applicable, through the current reporting period.

The amendments in this ASU specify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only.

The amendments in this ASU also expand the supplemental pro forma disclosures under ASC Topic 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma

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**MID PENN BANCORP, INC.**

**Notes to Consolidated Financial Statements (Unaudited)**

revenue and earnings.

The amendments in this ASU are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. Early adoption is permitted. The Corporation does not expect the adoption will have a significant impact on the Corporation's financial condition or results of operations.

**ASU 2011-02:** The FASB has issued this ASU to clarify the accounting principles applied to loan modifications, as defined by FASB ASC Subtopic 310-40, Receivables—Troubled Debt Restructurings by Creditors. This guidance was prompted by the increased volume in loan modifications prompted by the recent economic downturn. The ASU clarifies guidance on a creditor's evaluation of whether or not a concession has been granted, with an emphasis on evaluating all aspects of the modification rather than a focus on specific criteria, such as the effective interest rate test, to determine a concession. The ASU goes on to provide guidance on specific types of modifications such as changes in the interest rate of the borrowing, and insignificant delays in payments, as well as guidance on the creditor's evaluation of whether or not a debtor is experiencing financial difficulties.

For public entities, the amendments in the ASU are effective for the first interim or annual periods beginning on or after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. The entity should also disclose information required by ASU 2010-20, Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses, which had previously been deferred by ASU 2011-01, Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20, for interim and annual periods beginning on or after June 15, 2011. Nonpublic entities are required to adopt the amendments in this Update for annual periods ending on or after December 15, 2012. Early adoption is permitted. The Corporation does not expect the adoption will have a significant impact on the Corporation's financial condition or results of operations.

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**MID PENN BANCORP, INC.**

**Management's Discussion and Analysis**

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

The following is Management's Discussion of Consolidated Financial Condition as of March 31, 2011, compared to year-end 2010, and the Results of Operations for the three months ended March 31, 2011, compared to the same period in 2010.

This discussion should be read in conjunction with the financial tables, statistics, and the audited financial statements and notes thereto included in Mid Penn's Annual Report on Form 10-K for the year ended December 31, 2010. The results of operations for interim periods are not necessarily indicative of operating results expected for the full year.

Certain of the matters discussed in this document and in documents incorporated by reference herein, including matters discussed under the caption Management's Discussion and Analysis of Financial Condition and Results of Operations, may constitute forward-looking statements for purposes of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, and as such may involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Mid Penn to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements. The words "expect", "anticipates", "intend", "plan", "believe", "estimate", and similar expressions are intended to identify such forward-looking statements.

Mid Penn's actual results may differ materially from the results anticipated in these forward-looking statements due to a variety of factors, including, without limitation:

The effects of future economic conditions on Mid Penn and its customers;

Governmental monetary and fiscal policies, as well as legislative and regulatory changes, including the effects of the recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act;

The effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Financial Accounting Standards Board and other accounting standard setters;

The risks of changes in interest rates on the level and composition of deposits, loan demand, and the values of loan collateral, securities and interest rate protection agreements, as well as interest rate risks;

The effects of economic deterioration on current customers, specifically the effect of the economy on loan customers' ability to repay loans;

The effects of competition from other commercial banks, thrifts, mortgage banking firms, consumer finance companies, credit unions, securities brokerage firms, insurance companies, money market and other mutual funds and other financial institutions operating in Mid Penn's market area and elsewhere, including institutions operating locally, regionally, nationally and internationally, together with such competitors offering banking products and services by mail, telephone, computer and the internet;

The costs and effects of litigation and of unexpected or adverse outcomes in such litigation;

Technological changes;

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Acquisitions and integration of acquired businesses;

The failure of assumptions underlying the establishment of reserves for loan and lease losses and estimations of values of collateral and various financial assets and liabilities;

Acts of war or terrorism;

Volatilities in the securities markets; and

Deteriorating economic conditions.

Mid Penn undertakes no obligation to publicly revise or update these forward-looking statements to reflect events or circumstances that arise after the date of this report. Readers should carefully review the risk factors described in the documents that we periodically file with the SEC, including Mid Penn's Annual Report on Form 10-K for the year ended December 31, 2010.

### ***Critical Accounting Estimates***

Mid Penn's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and conform to general practices within the banking industry. Application of these principles involves significant judgments and estimates by management that have a material impact on the carrying value of certain assets and liabilities. The judgments and estimates that we used are based on historical experiences and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and estimates that we have made, actual results could differ from these judgments and estimates, which could have a material impact on the carrying values of assets and liabilities and the results of our operations.

Management of the Corporation considers the accounting judgments relating to the allowance for loan and lease losses, the evaluation of the Corporation's investment securities for other-than-temporary impairment, and the assessment of goodwill for impairment to be the accounting areas that require the most subjective and complex judgments.

The allowance for loan and lease losses represents management's estimate of probable incurred credit losses inherent in the loan and lease portfolio. Determining the amount of the allowance for loan and lease losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan and lease portfolio also represents the largest asset type on the consolidated balance sheet. Throughout the remainder of this report, the terms "loan" or "loans" refers to both loans and leases.

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Valuations for the investment portfolio are determined using quoted market prices, where available. If quoted market prices are not available, investment valuation is based on pricing models, quotes for similar investment securities, and observable yield curves and spreads. In addition to valuation, management must assess whether there are any declines in value below the carrying value of the investments that should be considered other than temporary or otherwise require an adjustment in carrying value and recognition of the loss in the consolidated statement of operations.

Accounting Standards Codification (ASC) Topic 350, *Intangibles-Goodwill and Other*, requires that goodwill is not amortized to expense, but rather that it be tested for impairment at least annually. Impairment write-downs are charged to results of operations in the period in which the impairment is determined. The Corporation did not identify any impairment on its outstanding goodwill from its most recent testing, which was performed as of December 31, 2010. If certain events occur which might indicate goodwill has been impaired, the goodwill is tested when such events occur.

**Results of Operations***Overview*

Net income available to common shareholders was \$872,000, \$0.25 per common share, for the quarter ended March 31, 2011, as compared to net income available to common shareholders of \$607,000, or \$0.17 per common share, for the quarter ended March 31, 2010.

Net interest income increased \$482,000, or 10.7%, to \$4,983,000 for the quarter ended March 31, 2011 from \$4,501,000 during the quarter ended March 31, 2010. This increase has been spurred by a moderating cost of funds and increasing levels of average earning assets.

The provision for loan and lease losses in the first quarter of 2011 was \$200,000, compared to \$160,000 in the first quarter of 2010.

Net income as a percent of average assets (return on average assets or ROA) and shareholders' equity (return on average equity or ROE) were as follows on an annualized basis:

	<b>Three Months Ended March 31,</b>	
	<b>2011</b>	<b>2010</b>
Return on average assets	0.62%	0.49%
Return on average equity	8.34%	6.32%

Total assets increased to \$680,292,000 at March 31, 2011, from \$637,457,000 at December 31, 2010. This asset increase was driven by strong core deposit growth through the first quarter of 2011 with total deposits of \$599,897,000 at March 31, 2011, compared to \$554,982,000 at December 31, 2010, an increase of approximately \$45 million. This growth in core deposits led to an increase in federal funds sold, and is being deployed to replace maturing long-term borrowings, and into investments and loans to maximize the return on these new funds.

The funding side of Mid Penn has continued the transformation begun in 2009. Deposit growth remained strong, as noted above, during the first three months of 2011. This increase in deposits was primarily the result of an attractive money market rate, and the building of relationship-based core deposit accounts from the extensive portfolio of commercial real estate borrowers. In addition to the ongoing efforts to place these funds into loans and investments, during the first three months of 2011, \$5,000,000 of long-term FHLB debt has matured and been replaced with core deposits at a more advantageous rate structure. These strategies have improved the cost of funds and overall net interest margin despite continued downward pressure on asset yields.

*Net Interest Income/Funding Sources*

Net interest income, Mid Penn's primary source of revenue, is the amount by which interest income on loans and investments exceeds interest incurred on deposits and borrowings. The amount of net interest income is affected by changes in interest rates and changes in the volume and mix of interest-sensitive assets and liabilities. Net interest income and corresponding yields are presented in the analysis below on a taxable-equivalent basis. Income from tax-exempt assets, primarily loans to or securities issued by state and local governments, is adjusted by an amount equivalent to the federal income taxes which would have been paid if the income received on these assets was taxable at the statutory rate of 34%. The following table includes average balances, rates, interest income and expense, interest rate spread, and net interest margin:



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