

PATAPSCO BANCORP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2008 and 2007

A reconciliation of the income tax provision and the amount computed by multiplying income before income taxes by the statutory Federal income tax rate of 34% is as follows for the years ended June 30:

<i>(In thousands)</i>	2008	2007
Tax at statutory rate	\$732	\$650
State income taxes, net of Federal income tax benefit	69	114
Other	(26)	(37)
Income tax provision	\$775	\$727
Effective tax rate	36.00%	38.00%

The Company has qualified under provisions of the Internal Revenue Code which permit it to deduct from taxable income a provision for bad debts based on actual bad debt experience. Therefore, the provision for bad debts deducted from taxable income for Federal income tax purposes was based on the experience method.

Effective July 1, 2007, the Company adopted the provision of FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes". The Interpretation provides clarification on accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB No. 109, "Accounting for Income Taxes." The Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. As a result of the Company's evaluation of the implementation of FIN 48, no significant income tax uncertainties were identified. Therefore, the Company recognized no adjustment for unrecognized income tax benefits for the year ended June 30, 2008. Our policy is to recognize interest and penalties on unrecognized tax benefits in income taxes expense in the Consolidated Statement of Income. The Company did not recognize any interest and penalties for the year ended June 30, 2008. The tax years subject to examination by the taxing authorities are the years ended June 30, 2007, 2006, 2005, and 2004.

In May 2007, the FASB issued FASB Staff Position (UFSP) FIN 48-1 "Definition of Settlement in FASB Interpretation No. 48" (FSP FIN 48-1). FSP FIN 48-1 provides guidance on how to determine whether a tax position is effectively settled for purpose of recognizing previously unrecognized tax benefits. FSP FIN 48-1 is effective retroactively to July 1, 2007 for the Company. The implementation of this standard did not have a material impact on our consolidated financial position or results of operation.

(9) Regulatory Matters

The Federal Deposit Insurance Corporation (FDIC) insures deposits of account holders up to \$100,000. Patapsco pays an annual premium to provide for this insurance. Patapsco is also a member of the Federal Home Loan Bank System and is required to maintain an investment in the stock of the Federal Home Loan Bank of Atlanta (FHLBA) equal to at least 4.50% of the outstanding borrowings from the FHLBA plus the lesser of 0.20% of total assets or \$25 million. The investment in the FHLBA stock is reported in the balance sheet as investment securities required by law. Purchases and sales of stock are made directly with Patapsco at par value.

Pursuant to regulations of the Federal Reserve Board, all FDIC-insured depository institutions must maintain average daily reserves against their transaction accounts. No reserves are required to be maintained on the first \$9.3 million of transaction accounts, reserves equal to 3% must be maintained on the next \$34.6 million of transaction accounts, and a reserve of 10% must be maintained against all remaining transaction accounts. These reserve requirements are subject to adjustments by the Federal Reserve Board. Because required reserves must be maintained in the form of vault cash or in a non-interest bearing account at a Federal Reserve Bank, the effect of the reserve requirement is to reduce the amount of the institution's interest-earning assets. At June 30, 2008 and 2007, the Bank met its reserve requirements of \$461,000 and \$533,000, respectively.

The Company, as the holding company for the Bank, has an annual cash requirement of approximately \$850,000 for the payment of common stock dividends and debt service on the subordinated debentures. The only source of internal funds for the holding company is dividends from the Bank. The amount of dividends that can be paid to the Company from the Bank is limited by the retained earnings of the Bank in the current calendar year and the prior

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two calendar years. However, dividends paid by the Bank to the Company would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements.

Patapsco is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory - and possibly additional discretionary - actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, Patapsco must meet specific capital guidelines that involve quantitative measures of Patapsco's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. Patapsco's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. In addition, the Bank must maintain minimum capital and other requirements of regulatory authorities when declaring or paying dividends. The Bank has complied with such capital requirements.

Quantitative measures established by regulation to ensure capital adequacy require Patapsco to maintain minimum amounts and ratios (as defined in the regulations and as set forth in the table below, as defined) of total and Tier I capital (as defined) to risk-weighted assets (as defined), and of Tier I capital to average assets (as defined). Management believes, as of June 30, 2008 and 2007, that Patapsco meets all capital adequacy requirements to which it is subject.

As of June 30, 2008, the most recent notification from banking regulators categorized Patapsco as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well or adequately capitalized Patapsco must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in tables below. There are no conditions or events since that notification that management believes have changed the institution's category.

At June 30, 2008 the Bank exceeded all regulatory minimum capital requirements. The table below presents certain information relating to the Bank's regulatory compliance at June 30, 2008.

	<u>Actual</u>		<u>For Capital Adequacy Purposes</u>		<u>To Be Well Capitalized Under Prompt Corrective Action Provisions</u>	
	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>
	(Dollars in thousands)					
Total Capital (to Risk Weighted Assets) ..	\$21,585	10.45%	\$16,532	8.00%	\$20,665	10.00%
Tier 1 Capital (to Risk Weighted Assets) ..	19,752	9.56%	8,266	4.00%	12,399	6.00%
Tier 1 Leverage Ratio ..	19,752	7.63%	10,352	4.00%	12,940	5.00%

At June 30, 2007, the Bank exceeded all regulatory minimum capital requirements. The table below presents certain information relating to the Bank's regulatory compliance at June 30, 2007.

	<u>Actual</u>		<u>For Capital Adequacy Purposes</u>		<u>To Be Well Capitalized Under Prompt Corrective Action Provisions</u>	
	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>	<u>Amount</u>	<u>Ratio</u>
	(Dollars in thousands)					
Total Capital (to Risk Weighted Assets) .	\$20,091	10.26%	\$15,665	8.00%	\$19,582	10.00%
Tier 1 Capital (to Risk Weighted Assets) ..	18,981	9.69%	7,833	4.00%	11,749	6.00%
Tier 1 Leverage Ratio .	18,981	7.57%	10,030	4.00%	12,537	5.00%

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(10) Stockholders' Equity and Related Matters

In 1995, the Bank converted from a federally chartered mutual savings association to a capital stock savings bank. Simultaneously, the Bank consummated the formation of a holding company, Patapsco Bancorp, Inc., of which the Bank is a wholly-owned subsidiary. In connection with the Conversion, the Company publicly issued 362,553 shares of its common stock.

Federal regulations required that, upon conversion from mutual to stock form of ownership, a "liquidation account" be established by restricting a portion of net worth for the benefit of eligible savings account holders who maintain their savings accounts with Patapsco after conversion. In the event of complete liquidation (and only in such event), each savings account holder who continues to maintain his savings account shall be entitled to receive a distribution from the liquidation account after payment to all creditors, but before any liquidation distribution with respect to capital stock. This account will be proportionately reduced for any subsequent reduction in the eligible holders' savings accounts. At conversion the liquidation account totaled approximately \$6,088,000. In addition to the foregoing, certain bad debt reserves of approximately \$2,561,000 deducted from income for federal income tax purposes and included in retained earnings of Patapsco, are not available for the payment of cash dividends or other distributions to stockholders without payment of taxes at the then-current tax rate by Patapsco, on the amount removed from the reserves for such distributions. The unrecorded deferred income tax liability on the above amount was approximately \$989,000.

(11) Benefit Plans

Employee Stock Ownership Plan

Patapsco had previously established an Employee Stock Ownership Plan (ESOP) for its employees. All ESOP shares contained a "Put Option" which required the Company to repurchase the share at the then fair market value subject to the availability of retained earnings.

The ESOP shares have been fully allocated, the Plan terminated and as of June 30, 2008 all shares subject to put option have been repurchased.

For the years ended June 30, 2008 and 2007 there was no compensation expense recognized related to the ESOP.

2004 Stock Incentive Plan

In October 2004, the shareholders' of the Company approved the 2004 Stock Incentive Plan. Under this plan, 90,000 shares of common stock are available for issuance under a variety of awards. An additional 40,146 shares were made available for issuance to settle past deferred compensation obligations. This new plan replaced the Director's retirement plan that became effective in September 1995. At the time of adoption, the directors had the option to reallocate their deferred compensation assets.

As of June 30, 2008, there are 54,893 deferred shares under this plan of which 12,906 are issued and outstanding. These deferred shares are allocated in lieu of cash compensation to Directors of the Company. These shares are included in shares outstanding for the purposes of computing earnings per share. Additionally, as of June 30, 2008 there are 12,649 non-vested shares outstanding under this plan.

Compensation expense recognized in connection with these plans during the years ended June 30, 2008 and 2007 was \$60,000 and \$67,000, respectively.

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A summary of the status of the Company's non-vested shares as of June 30, 2008 is presented below:

	Common Shares	Weighted Average Grant-Date Fair Value
Non-Vested as of June 30, 2007	14,453	\$ 13.71
Vested		\$
Forfeited	1,804	\$ 13.71
Non-vested at June 30, 2008	12,649	\$ 13.71

As of June 30, 2008, there was \$70,000 of total unrecognized compensation costs related to non-vested share-based compensation. The cost is expected to be recognized over a weighted average period of 13 months. At grant date, vesting of the shares was "cliff" vesting at the end of either a two or three year period.

Stock Options

The Company's 1996 **Stock Options and Incentive Plan (Plan)** was approved by the stockholders at the 1996 annual meeting. The Plan provides for the granting of options to acquire common stock to directors and key employees. Option prices are equal or greater than the estimated fair market value of the common stock at the date of the grant. In October 1996 the Company granted options to purchase 137,862 shares at \$4.60 per share.

The Company's 2000 Stock Option and Incentive Plan was approved by the stockholders at the 2000 annual meeting. The Plan provides for the granting of options to acquire common stock to directors and key employees. Option prices are equal or greater than the estimated fair market value of the common stock at the date of the grant.

The Plan provides for one-fifth of the options granted to be exercisable on each of the first five anniversaries of the date of grant. Under this plan, in August 2001 the Company granted options to purchase 99,975 shares at \$6.29 per share.

The following table summarizes the status of and changes in the Company's stock option plans during the past two years.

	Options	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercise Price	Aggregate Intrinsic Value(OO0s)
Outstanding, June 30, 2006	138,495	\$ 5.62	122,877	\$ 5.51	
Granted					
Exercised	(90,623)	5.41			
Cancelled					
Outstanding, June 30, 2007	47,872	6.02	47,872	\$ 6.02	\$ 801
Granted					
Exercised	(27,040)	5.82			
Cancelled					
Outstanding, June 30, 2008	20,832	\$ 6.29	20,832	\$ 6.29	\$ 19

The following table summarizes information about stock options outstanding at June 30, 2008.

Exercise Price of All Options	Number Outstanding	Remaining Contractual Ufe	Number Exercisable
6.29	20,832	3.14 years	20,832

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401(K) Retirement Savings Plan

The Company has a 401(k) Retirement Savings Plan. Employees may contribute a percentage of their salary subject to limitations established by the Internal Revenue Service. The Company is obligated to contribute 3% of each employee's salary, whether or not the employee contributes their own money. All employees who have completed six months of service with the Company in which they have worked more than 500 hours, and are at least 21 years old, are eligible to participate. The Company's contribution to this plan was \$88,000 and \$91,000 for the years ended June 30, 2008 and 2007, respectively. Additionally, since the ESOP is fully allocated, the Compensation Committee of the Board of Directors has approved a discretionary profit sharing component to the 401K plan. The accrual for this component of the plan for the years ended June 30, 2008 and 2007 was \$108,000 and \$113,000, respectively.

(12) Fair Value of Financial Instruments

Statement of Financial Accounting Standards No. 107, *Disclosures about Fair Value of Financial Instruments* (SFAS 107) requires the Company to disclose estimated fair values for certain on- and off-balance sheet financial instruments. Fair value estimates, methods, and assumptions are set forth below for the Company's financial instruments as of June 30, 2008 and 2007.

Fair value estimates are made at a specific point in time, based on relevant market information and information about financial instruments. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect estimates.

The carrying amount and estimated fair value of financial instruments is summarized as follows at June 30:

<i>(In thousands)</i>	2008		2007	
	Carrying amount	Fair value	Carrying amount	Fair value
Assets:				
Cash and interest-bearing deposits	\$ 6,720	\$ 6,720	\$ 5,215	\$ 5,215
Federal funds sold	2,473	2,473	2,255	2,255
Investment securities available for sale	9,601	9,601	13,147	13,147
Loans receivable, net	227,514	231,277	220,239	217,376
Investment securities required by law	2,649	2,649	2,599	2,599
Accrued interest receivable	1,198	1,198	1,063	1,063
Liabilities:				
Deposits	197,886	198,623	189,712	183,343
Long-term debt	42,300	42,750	43,800	43,032
Accrued interest payable	666	666	472	472
Off balance sheet instruments:				
Commitments to extend credit				

Cash and Due from Banks, Interest Bearing Deposits with Banks and Federal Funds Sold

The statement of financial condition carrying amounts for cash and due from banks, interest bearing deposits with banks and federal funds sold approximate the estimated fair values of such assets.

PATAPSCO BANCORP, INC. AND SUBSIDIARIES

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June 30, 2008 and 2007

Securities

The fair value of securities is based on quoted market values.

Loans Receivable

Loans receivable were segmented into portfolios with similar financial characteristics. Loans were also segmented by type such as residential and nonresidential, construction and land, second mortgage loans, commercial, and consumer. Each loan category was further segmented by fixed and adjustable rate interest terms.

The fair value of loans was calculated by discounting anticipated cash flows based on weighted average contractual maturity, weighted average coupon and current loan origination rates.

Accrued Interest Receivable

The carrying amount of accrued interest receivable approximates its fair value.

Securities required by Law

The carrying amount of securities required by law approximates its fair value.

Deposits

Under SFAS 107, the fair value of deposits with no stated maturity, such as non-interest bearing deposits, interest bearing NOW accounts and statement savings accounts, is equal to the carrying amounts. The fair value of certificates of deposit was based on the discounted value of contractual cash flows. The discount rate for certificates of deposit was estimated using the rate currently offered for deposits of similar remaining maturities.

Long-Term Debt

The fair value of long-term debt was based on the discounted value of contractual cash flows, using rates currently available.

Accrued Interest Payable

The carrying amount of accrued interest payable approximates its fair value.

Off-Balance Sheet Financial Instruments and Standby Letters of Credit

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business, including mortgage loan commitments, undisbursed lines of credit on commercial business loans and standby letters of credit. These instruments involve, to various degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated statements of financial condition. The fair values of such commitments are immaterial.

The disclosure of fair value amounts does not include the fair values of any intangibles, including core deposit intangibles. Core deposit intangibles represent the value attributable to total deposits based on an expected duration of customer relationships.

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(13) Condensed Financial Information (Parent Company Only)

Summarized financial information for the Company is as follows as of and for the years ended June 30:

(In thousands)

Statements of Financial Condition	2008	2007
Cash	\$ 327	\$ 1,671
Loans	1,375	
Equity in net assets of the bank	22,815	22,369
Other assets	209	251
Total Assets	\$24,726	\$24,291
Accrued expenses and other liabilities	\$ 335	\$ 375
Subordinated Debentures	5,000	5,000
Stockholders' equity	19,391	18,916
Total Liabilities & Stockholders Equity	\$24,726	\$24,291

(In thousands)

Statements of Income	2008	2007
Total Interest Income	\$ 67	\$ 5
Total Interest Expense	324	323
Non-interest Income	2,000	2
Non-interest Expense	14	11
Income(loss) before equity in net income of subsidiary and income taxes	1,729	(327)
Net income of subsidiary	292	1,399
Income before income tax provision	2,021	1,072
Income tax provision (benefit)	644	(113)
Net income	\$1,377	\$1,185

PATAPSCO BANCORP, INC. AND SUBSIDIARIES
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(in thousands)

Statements of Cash Flows	2008	2007
Operating activities:		
Net income	\$1,377	\$ 1,185
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in net income of subsidiary	(292)	(1,399)
Termination fee earned, not collected	(2,000)	
Increase in other assets	(34)	(51)
Increase in accrued expenses and other liabilities	45	172
Net cash used in operating activities	(904)	(93)
Investing activities:		
Purchase of equity securities		(20)
Proceeds from sale of equity security		92
Additional investment in subsidiary stock		(300)
Dividend received from subsidiary	625	
Net cash provided by/(used in) investing activities	625	(228)
Financing activities:		
Payment to purchase common stock	(659)	(690)
Cash received in exercise of stock options	114	338
Cash dividend paid	(520)	(490)
Net cash used in financing activities	(1,065)	(842)
Decrease in cash and cash equivalents	(1,344)	0,163)
Cash and cash equivalents, beginning of year	1,671	2,834
Cash and cash equivalents, end of year	\$ 327	\$ 1,671

Non-cash Transaction: A portion of a loan in the amount of \$625,000 was contributed to a Subsidiary.



REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
Patapsco Bancorp, Inc.
Dundalk, Maryland

We have audited the accompanying consolidated statements of financial condition of Patapsco Bancorp, Inc. and subsidiaries as of June 30, 2007 and 2006, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended June 30, 2007. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Patapsco Bancorp, Inc. and subsidiaries as of June 30, 2007 and 2006, and the consolidated results of their operations and their cash flows for each of the three years in the period ended June 30, 2007, in conformity with accounting principles generally accepted in the United States of America.

Beard Miller Company LLP

Beard Miller Company LLP
Baltimore, Maryland
September 6, 2007

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\$ 4,308	\$ 4,839
907	968
<u>2,255</u>	<u>2,381</u>
7,470	8,188
	605
13,147	16,667
220,239	190,589
2,599	2,416
4,474	2,175
3,303	3,354
4,226	4,076
<hr/>	<hr/>
\$ 255,458	\$ 228,070

\$ 11,753	\$ 13,186
<u>177,959</u>	<u>153,647</u>
189,712	166,833
5,000	5,000
38,800	35,050
3,030	2,899
236,542	209,782

Commitments and contingencies

Temporary equity - ESOP shares subject to put option

935	1,121
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Stockholders' equity

Common stock \$0.01 par value; authorized 4,000,000 shares; issued and outstanding 1,864,985 and 1,813,925 shares at June 30, 2007 and 2006 respectively

18	18
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Additional paid-in capital

6,937	6,950
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Deferred compensation contra

(18)	(78)
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Obligation under deferred compensation

423	395
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Retained earnings, substantially restricted

10,994	10,317
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Accumulated other comprehensive loss, net of taxes

(313)	(435)
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Total Stockholders' Equity - Permanent

17,981	17,167
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Total Stockholders' Equity - including Temporary Equity

18,916	18,288
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Total Liabilities and Stockholders' Equity

<u>\$255,458</u>	<u>\$228,070</u>
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See accompanying notes to consolidated financial statements.

PATAPSCO BANCORP, INC. AND SUBSIDIARIES

Consolidated Statements of Income

Years Ended June 30, 2007, 2006 and 2005

<i>(in thousands except for per share data)</i>	2007	2006	2005
Interest income:			
Loans receivable	\$15,461	\$12,501	\$10,613
Investment securities	502	941	1,046
Federal funds sold and other investments	163	114	152
Total interest income	16,426	13,556	11,811
Interest expense:			
Deposits	5,455	3,486	2,818
Short-term debt	37	140	
Long term debt and junior subordinated debentures	2,008	1,323	936
Total interest expense	7,503	4,949	3,754
Net interest income	\$9,23	\$8,607	\$8,057
Provision for loan losses	430	65	225
		8,542	7,832
Non-interest income:			
Fees and service charges	730	656	525
Gain on sale of securities available for sale		64	
Gain on sale of office building	14		
Loss on sale of other repossessed assets	(9)		
Other	131	149	159
Total non-interest income		871	684
Non-interest expenses:			
Compensation and employee benefits	4,382	4,490	3,773
Professional fees	591	241	287
Equipment expenses	331	326	284
Net occupancy costs	565	552	306
Advertising	110	86	178
Data processing	304	285	244
Amortization of core deposit intangible	51	51	51
Telephone, postage and delivery	250	271	276
Other	863	900	1,012
Total non-interest expenses	7,447	7,202	6,411
Income before income taxes	1,912	2,211	2,105
Income tax provision	72	823	759
	1,185	1,388	1,346
Preferred dividends declared		123	177
Net income available to common stockholders	\$ 1,185	\$ 1,265	\$ 1,169
Basic earnings per share	\$ 0.62	\$ 0.80	\$ 0.81
Diluted earnings per share	\$ 0.61	\$ 0.72	\$ 0.70
Cash dividends declared per common share	\$ 0.27	\$ 0.25	\$ 0.23

PATAPSCO BANCORP, INC. AND SUBSIDIARIES
 Consolidated Statements of Stockholders' Equity
 Years Ended June 30, 2007, 2006 and 2005

2005
 10,613
 1,946
 152
 11,811
 2,818
 936
 3,754
 8,057
 225
 7,832
 525
 159
 684
 3,773
 287
 284
 306
 178
 244
 51
 276
 1,012
 6,411
 2,105
 759
 1,346
 177
 169
 0.81
 0.70
 0.23

PATAPSCO BANCORP, INC. AND SUBSIDIARIES

Consolidated Statements of Stockholders' Equity

Years Ended June 30, 2007, 2006 and 2005

(dollars in thousands except for per share data)

	Preferred Stock	Additional Paid-In Capital Preferred	Common Stock	Additional Paid-In Capital Common	Temp. Equity ESOP Shares Subject to Put	Obligation Under Deferred Compensation	Retained Earnings	Accumulated Other Comprehensive Income (Loss), Net of Taxes	Total Stockholders' Equity
Balance at July 1, 2004	\$ 1	\$ 2,454	\$ 14	\$ 4,098	\$ 1,404	\$ 172	\$ 8,592	\$ (355)	\$ 16,380
Comprehensive income:									
Net income							1,346	-	1,346
Change in unrealized gains (losses) on									
Securities available-for-sale, net of taxes of \$116								184	184
Comprehensive income									1,530
Preferred stock dividends (\$1.875 per share)							(177)		(177)
Common stock dividends (\$.23 per share)							(323)		(323)
Options exercised and related tax benefit, 22,635 shares									184
Shares surrendered in exercise of stock options 4,387 shares									(92)
Purchase of shares under ESOP put option, 7,755 shares									(105)
Transfer from temporary equity									
Obligation under deferred compensation									190
Conversion of Preferred to Common									
Balance at June 30, 2005									\$ 17,587
Comprehensive income:									
Net income									1,388
Change in unrealized gains (losses) on									
Securities available-for-sale, net of taxes of \$166									(263)
Reclassification adjustment for gains included in net income, net of tax of \$0.6									(1)
Comprehensive income									1,124
Preferred stock dividends (\$1.41 per share)									(123)
Common stock dividends (\$0.25 per share)									(386)
Compensation under stock-based benefit plan					89	(72)			17
Options exercised and related tax benefit, 36,353 shares					189				189
Shares surrendered in exercise of stock options, 5,649 shares					(59)				(59)
Purchase of shares under ESOP put option, 1,938 shares					(23)				(23)
Transfer from temporary equity					145	(145)			
Obligation under deferred compensation							27		27
Conversion of Preferred to Common	(1)	(2,280)	4	2,277					

(continued on next page)

Conversion of Preferred stock to cash		(65)	-	-	-	-	-	-	(65)
Balance at June 30, 2006	\$	\$	\$ 18	\$ 6,950	\$ 1,121	\$ 317	\$ 10,317	\$ (435)	\$ 18,288
Balance at June 30, 2006	\$	\$	\$ 18	\$ 6,950	\$ 1,121	\$ 317	\$ 10,317	\$ (435)	\$ 18,288
Comprehensive income:									
Net income							1,185		1,185
Change in unrealized gains (losses) on									
Securities available for sale, net of taxes of \$76	-	-	-	-	-	-	-	122	122
Comprehensive income									1,307
Common stock dividends (\$0.27 per share)	-	-	-	-	-	-	(508)	-	(508)
Compensation under stock-based benefit plan	-	-	-	105	-	-	-	-	105
Options exercised and related tax benefit, 90,623 shares	-	-	-	538	-	-	-	-	538
Shares surrendered in exercise of stock options, 13,831 shares	-	-	-	(152)	-	-	-	-	(152)
Purchase of shares under ESOP put option, 29,992 shares	-	-	-	(690)	-	-	-	-	(690)
Transfer from temporary equity	-	-	-	186	(186)	-	-	-	-
Obligation under deferred compensation	-	-	-	-	-	28	-	-	28
Balance at June 30, 2007	\$	\$	\$ 18	\$ 6,937	\$ 935	\$ 345	\$ 10,994	\$ (313)	\$ 18,916

See accompanying notes to consolidated financial statements.

PATAPSCO BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows

Years ended June 30, 2007, 2006 and 2005

<u>(in thousands)</u>	2007	2006	2005
	\$ 1,185	\$ 1,388	\$ 1,346
	316	312	271
	430	65	225
	116	59	48
	48	9	45
	51	51	51
	42	28	(5)
	(68)	(59)	(59)
	(34)	(43)	(105)
	(2)	(2)	(2)
	(14)	(64)	(64)
	9	9	9
	(165)	24	80
	156	327	(371)
Net cash provided by operating activities	\$ 2,072	\$ 2,095	\$ 1,526
Cash flows from investing activities:			
Proceeds from maturing time deposit investments	600	600	293
Purchase of securities available for sale	(20)	(10)	(2,006)
Proceeds from sale of securities available for sale	92	302	302
Proceeds from maturing securities available for sale and principal payments on mortgage-backed securities available for sale	3,612	7,356	6,653
Loan principal disbursements, net of repayments	(28,498)	(26,838)	(9,825)
Purchase of consumer loans	(1,577)	(2,726)	(2,726)
Proceeds from sale of repossessed assets	15	15	15
(Increase) decrease in investments required by law	(183)	(739)	83
Cash received in sale of property and equipment	50	154	154
Purchases of property and equipment	(2,651)	(992)	(241)
Net cash used in investing activities	\$ (28,560)	\$ (23,493)	\$ (5,043)
	\$ 22,905	\$ 2,603	\$ (3,627)
	(43)	6	(127)
	8,000	20,000	2,000
	(4,250)	(5,183)	(4,667)
	5,000	5,000	5,000
	338	121	47
	(690)	(23)	(105)
	(490)	(521)	(500)
	(65)	(65)	(65)
Net increase (decrease) in cash and cash equivalents	(718)	8,188	8,188
Cash and cash equivalents at beginning of year	8,188	8,188	8,188
Cash and cash equivalents at end of year	\$ 7,470	\$ 7,470	\$ 7,470

Supplemental cash flow information:

Interest paid	\$ 7,351	\$ 4,940	\$ 3,735
Income taxes paid	837	790	656
Non-cash equity transactions:			
Conversion of 91,297 preferred shares to 363,878 common shares and 4,345 preferred shares to 17,348 common shares in the years ended June 30, 2006 and 2005, respectively		2,281	109

See accompanying notes to consolidated financial statements.

PATAPSCO BANCORP, INC. AND SUBSIDIARIES'
Notes to Consolidated Financial Statements
June 30, 2007, 2006 and 2005

(1) Basis of Presentation and Summary of Significant Accounting Policies

Description of Business

Patapsco Bancorp, Inc. (the Company) is the holding company of The Patapsco Bank (Patapsco). Patapsco owns 100% of Prime Business Leasing, Inc. (Prime Leasing) and Patapsco Financial Services, Inc. (Financial). The primary business of Patapsco is to attract deposits from individual and corporate customers and to originate residential and commercial mortgage loans, commercial loans and consumer loans, primarily in the Greater Baltimore Metropolitan area. Patapsco is subject to competition from other financial and mortgage institutions in attracting and retaining deposits and in making loans. Patapsco is subject to the regulations of certain agencies of the federal government and undergoes periodic examination by those agencies. The primary business of Prime Leasing is the origination and servicing of commercial finance leases. The primary business of Financial is the sale of consumer investment products.

Announced Transaction

As announced on March 19, 2007, Patapsco Bancorp, Inc. executed a definitive merger agreement with Bradford Bancorp, Inc. whereby the Company will be merged with and into Bradford Bancorp. The transaction is expected to be completed in the fourth calendar quarter of 2007 and is subject to the approval of the members of Bradford Bank MHC, the shareholders of Patapsco Bancorp and regulatory authorities.

In connection with the merger, Bradford Bank's current mutual holding company, Bradford Bank MHC, which owns 100% of Bradford Bancorp's outstanding shares, will undergo a full mutual-to-stock conversion and stock offering. Under the terms of the transaction, shareholders of Patapsco Bancorp will be entitled to receive either \$23.00 in cash or 2.3 shares of Bradford Bancorp common stock (assuming a \$10.00 per share initial public offering price) in exchange for each share of Patapsco Bancorp common stock. Based upon the \$23.00 per share price, the consideration is approximately 278% of tangible book value, 229% of book value and 30 times trailing twelve months earnings, computed as of the day of the announcement.

Basis of Presentation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Patapsco, Prime Leasing and Financial. All significant intercompany accounts and transactions have been eliminated in consolidation.

In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the statements of financial condition and income and expenses for the periods then ended. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses.

Management believes that the allowance for loan losses is adequate. While management uses and considers available information in making the required estimates, additional provisions for losses may be necessary based on changes in economic conditions, particularly in Baltimore and the State of Maryland. In addition, various regulatory agencies, as an integral part of their examination process, periodically review Patapsco's allowance for loan losses. Such agencies may require Patapsco to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

Significant concentrations of credit risk

Most of the Company's activities are with customers in the Greater Baltimore Metropolitan Area. Note 2 discusses the types of securities the Company invests in. Note 3 discusses the types of lending that the Company engages in. The Company's largest lending relationship is \$2.7 million.

PATAPSCO BANCORP, INC. AND SUBSIDIARIES
Notes to Consolidated Financial Statements

June 30, 2007, 2006 and 2005

The Company's residential lending operations are focused in the State of Maryland, primarily the Baltimore Metropolitan area. While residential lending is generally considered to involve less risk than other forms of lending, payment experience on these loans is dependent to some extent on economic and market conditions in the Company's primary lending area.

Cash and Cash Equivalents

Cash equivalents include short-term investments, with an original maturity of 90 days or less, which consist of federal funds sold and interest bearing deposits in other financial institutions.

Securities

Debt securities that the Company has the positive intent and ability to hold to maturity are classified as held-to-maturity and recorded at amortized cost. As the Company does not engage in securities trading, the balance of its debt and equity securities are classified as available-for-sale and recorded at fair value with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity, net of tax effects. All of the Company's securities are classified as available-for sale at June 30, 2007 and 2006.

If a decline in value of an individual security classified as held-to-maturity or available-for-sale is judged to be other than temporary, the cost basis of that security is reduced to its fair value and the amount of the write-down is included in earnings. Fair value is determined based on bid quotations received from securities dealers. In estimating other-than-temporary impairment losses, management considers the length of time and extent to which fair value has been less than cost, the financial condition and near term prospects of the issuer and the intent and ability of the Company to hold the securities until the earlier of market price recovery or maturity. For purposes of computing realized gains or losses on the sales of securities, cost is determined using the specific identification method. Premiums and discounts on securities are amortized over the term of the security using the interest method.

Investment Securities Required by Law

Investment securities required by law represent Federal Reserve Bank of Richmond and Federal Home Loan Bank of Atlanta stock, which are considered restricted as to marketability.

Loans Held For Sale

Loans held for sale are carried at the lower of aggregate cost or fair value. Fair value is determined based on outstanding investor commitments or, in the absence of such commitments, based on current investor yield requirements. Gains and losses on loan sales are determined using the specific identification method.

There were no loans held for sale at June 30, 2007 and 2006.

Loans Receivable

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 adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance.

The accrual of interest is generally discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectibility 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 losses. Interest received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectibility of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual

PATAPSCO BANCORP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2007, 2006 and 2005

terms for a reasonable period of time and the ultimate collectibility of the total contractual principal and interest is no longer in doubt.

Loan Fees

Loan origination fees are deferred and amortized to income over the contractual lives of the related loans using the interest method. Certain incremental direct loan origination costs are deferred and recognized over the contractual lives of the related loans using the interest method as a reduction of the loan yield. Deferred fees and costs are combined where applicable and the net amount is amortized.

Allowance for Loan Losses

The allowance for loan losses ("allowance") represents an amount, that in the judgment of management, will be adequate to absorb probable losses on outstanding loans and leases that may become uncollectible. The allowance represents an estimate made based upon two principles of accounting: (1) Statement of Financial Accounting Standards ("SFAS") No. 5, "Accounting for Contingencies", that requires losses to be accrued when their occurrence is probable and estimable, and (2) SFAS No. 144 "Accounting by Creditors for Impairment of a Loan", that requires losses be accrued when it is probable that the lender will not collect all principal and interest when due under the original term of the loan. The adequacy of the allowance is determined through careful evaluation of the loan portfolio. This determination is inherently subjective and requires significant estimates, including estimated losses on pools of homogeneous loans based on historical loss experience and consideration of the current economic environment that may be subject to change. Loans and leases deemed uncollectible are charged against the allowance and recoveries of previously charged-off amounts are credited to it. The level of the allowance is adjusted through the provision for loan losses that is recorded as a current period expense.

The methodology for assessing the appropriateness of the allowance includes a specific allowance, a formula allowance and a nonspecific allowance. The specific allowance is for risk rated credits on an individual basis. The formula allowance reflects historical losses by credit category. The nonspecific allowance captures losses whose impact on the portfolio have occurred but have yet to be recognized in either the specific allowance or the formula allowance. The factors used in determining the nonspecific allowance include trends in delinquencies, trends in volumes and terms of loans, the size of loans relative to the allowance, concentration of credits, the quality of the risk identification system and credit administration, and local and national economic trends.

A loan is determined to be impaired when, based on current information and events, it is probable that Patapsco will be unable to collect all amounts when due according to the contractual terms of the loan agreement. A loan is not considered impaired during a period of insignificant delay in payment if Patapsco expects to collect all amounts due, including past-due interest. Patapsco generally considers a period of insignificant delay in payment to include delinquency up to and including 90 days. Impairment is measured through a comparison of the loan's carrying amount to the present value of its expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller-balance homogeneous loans are evaluated collectively for impairment. Accordingly, the Company does not separately identify individual residential first and second mortgage loans and consumer installment loans for impairment disclosures, unless such loans are the subject of a restructuring agreement. Impaired loans are therefore generally comprised of commercial, commercial mortgage, real estate development, and certain restructured residential loans. In addition, impaired loans are generally loans which management has placed in nonaccrual status since loans are placed in nonaccrual status on the earlier of the date that management determines that the collection of principal and/or interest is in doubt or the date that principal or interest is 90 days or more past due.

Patapsco recognized interest income for impaired loans consistent with its method for nonaccrual loans. Specifically, interest payments received are recognized as interest income or, if the ultimate collectibility of principal is in doubt, are applied to principal.

PATAPSCO BANCORP, INC. AND **SUBSIDIARIES**
 Notes to Consolidated Financial Statements
 June 30, 2007, 2006 and 2005

Property and Equipment

Land is carried at cost. Property and equipment are stated at cost less accumulated depreciation computed by use of the straight-line method over the estimated useful lives of the related assets. Additions and betterments are capitalized and costs of repairs and maintenance are expensed when incurred. The related costs and accumulated depreciation are eliminated from the accounts when an asset is sold or retired and the resultant gain or loss is credited or charged to income.

Foreclosed Real Estate and Other Repossessed Assets

Foreclosed real estate and other repossessed assets are initially recorded at the estimated fair value, net of estimated selling costs, and subsequently at the lower of carrying cost or fair value less estimated costs to sell. Costs relating to holding such property are charged against income in the current period, while costs relating to improving such real estate are capitalized until a salable condition is reached. At June 30, 2007, the Company had no foreclosed real estate and other repossessed assets of \$5,000. There were no foreclosed real estate or other repossessed assets at June 30, 2006.

Deferred Income Taxes

Deferred income taxes are recognized, with certain exceptions, for temporary differences between the financial reporting basis and income tax basis of assets and liabilities based on enacted tax rates expected to be in effect when such amounts are realized or settled. Deferred tax assets are recognized only to the extent that it is more likely than not that such amounts will be realized based on consideration of available evidence, including tax planning strategies and other factors. The effects of changes in tax laws or rates on deferred tax assets and liabilities are recognized in the period that includes the enactment date.

Earnings per Share of Common Stock

Basic earnings per share amounts are based on the weighted average shares of common stock outstanding. Diluted earnings per share assume the conversion, exercise or issuance of all potential common stock instruments such as options, warrants and convertible securities, unless the effect is to reduce a loss or increase earnings per share. No adjustments were made to net income (numerator) for all periods presented.

(in thousands, except per share data)	Year Ended					
	June 30, 2007		June 30, 2006		June 30, 2005	
	Basic	Diluted	Basic	Diluted	Basic	Diluted
Net income	\$1,185	\$1,185	\$1,388	\$1,388	\$1,346	\$1,346
Preferred Stock Dividends			123		177	
Net Income Available to Common Stock	\$1,185	\$1,185	\$1,265	\$1,388	\$1,169	\$1,346
Weighted average common shares outstanding	1,906	1,906	1,573	1,573	1,441	1,441
Diluted securities:						
Convertible preferred stock				265		374
Stock options		48		81		108
Adjusted weighted average shares	1,906	1,954	1,573	1,919	1,441	1,923
Per share amount	\$0.62	\$0.61	\$0.80	\$0.72	\$0.81	\$0.70

PATAPSCO BANCORP, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
June 30, 2007, 2006 and 2005'

Stock-Based Compensation

In December 2004, the FASB issued SFAS No. 123 (revised), "Share-Based Payment" ("SFAS 123(R)"). SFAS 123(R) replaces SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). SFAS 123(R) requires compensation costs related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides services in exchange for the award. The Company adopted effective July 1, 2006, the new standard using the modified prospective method. Under the modified prospective method, companies are required to record compensation cost for new and modified awards over the related vesting period of such awards prospectively, and to record compensation cost prospectively on the non-vested portion, at the date of adoption, of previously issued and outstanding awards over the remaining vesting period of such awards. No change to prior periods presented is permitted under the modified prospective method. The Company recognized a pre-tax expense of approximately \$5,600 in the year ended June 30, 2007 for the expense related to the final scheduled vesting of all outstanding stock option awards. There were no stock options granted in the year ended June 30, 2007. Any additional impact of adopting the new accounting standard will be determined by share-based payments granted in future periods.

Prior to revision, Statement 123 allowed companies to account for stock-based compensation either under the new provisions of Statement 123 or under the provisions of Accounting Principles Board Opinion No. 25 (APB 25), Accounting for Stock Issued to Employees, but required pro forma disclosure in the footnotes to the financial statements as if the measurement provisions of Statement 123 had been adopted. The Company accounted for its stock-based compensation in accordance with APB 25 through June 30, 2006. Accordingly, no stock option based employee compensation cost is reflected in net income for the years ended June 30, 2006 and 2005, as all options granted under these plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the company had applied the fair value recognition provisions of Statement 123.

	Year Ended June 30,	
	2006	2005
(in thousands except for per share data)		
Net Income as reported	\$ 1,388	\$ 1,346
Amounts recognized as expense in financial statements, net of related tax effects	22	30
Deduct: Total stock option based employee compensation expense determined under fair value method for all awards, net of related tax effects	(28)	(57)
Proforma Net Income	\$ 1,382	\$ 1,319
Earnings per share		
Basic - as reported	\$ 0.80	\$ 0.81
Basic - pro forma	\$ 0.80	\$ 0.79
Diluted - as reported	\$ 0.72	\$ 0.70
Diluted - pro forma	\$ 0.72	\$ 0.69

Comprehensive Income:

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the statement of financial condition, such items, along with net income are components of comprehensive income.

PATAPSCO BANCORP, INC. AND SUBSIDIARIES
 Notes to Consolidated Financial Statements
 June 30, 2007, 2006 and 2005

Goodwill and Intangible Assets

Goodwill is not amortized, but rather it is tested for impairment on an annual basis at the reporting unit level; which is either at the same level or one level below an operating segment. Other acquired intangible assets with finite lives, such as purchased customer accounts, are required to be amortized over their estimated lives. The Company amortizes such assets using the straight-line method over estimated useful lives of 10 years. The Company periodically assesses whether events or changes in circumstances indicate that the carrying amounts of goodwill and other intangible assets may be impaired.

Amortizable intangible assets were composed of the following:

(Dollars in Thousands)	June 30, 2007		June 30, 2006	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortizable intangible assets:				
acquisition of deposit accounts	\$516	\$168	\$516	\$116

Amortization expense was \$51,000 for the year ended June 30, 2007, 2006 and 2005 and is scheduled to be \$51,600 for each of the next five years.

Advertising Costs:

The Company expenses advertising costs as they are incurred.

Segment Reporting

The Company acts as an independent community financial services provider, and offerstraditional banking and related financial services to individual, business and government customers. Through its branch and automated teller machine networks, the Bank offers a full array of commercial and retail financial services, including taking of time, savings and demand deposits; the making of commercial, consumer and mortgage loans; and the providing of other financial services.

Reclassification

Certain prior year's amounts have been reclassified to conform to the current year's presentation.

Off Balance Sheet Credit Related Financial Instruments

In the ordinary course of business, the Company has entered into commitments to extend credit, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded when funded.

New Accounting Pronouncements

In February 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments." SFAS No. 155 amends FASB Statement No. 133 and FASB Statement No. 140, and improves the financial reporting of certain hybrid financial instruments by requiring more consistent accounting that eliminates exemptions and provides a means to simplify the accounting for these instruments. Specifically, SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that