

MALVERN BANCORP, INC.
Form 10-Q
February 09, 2016

UNITED STATES OF AMERICA
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended December 31, 2015

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: 000-54835

MALVERN BANCORP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Pennsylvania **45-5307782**
(State or Other Jurisdiction of (IRS Employer

Incorporation or Organization) Identification No.)

42 Lancaster Avenue, Paoli, Pennsylvania 19301

(Address of Principal Executive Offices) (Zip Code)

(610) 644-9400

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or 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):

Non-accelerated filer

Large accelerated filer Accelerated filer (Do not check if smaller reporting company
reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

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

Common Stock, par value \$0.01:	6,560,713 shares
(Title of Class)	(Outstanding as of February 8, 2016)

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PART I – FINANCIAL INFORMATION

The following unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X, and, accordingly, do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. However, in the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three months ended December 31, 2015 are not necessarily indicative of the results that may be expected for the full year ending September 30, 2016, or for any other interim period. The Malvern Bancorp, Inc. 2015 Annual Report on Form 10-K should be read in conjunction with these financial statements.

Item 1. Financial Statements**MALVERN BANCORP, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

(in thousands, except for share and per share data)	December 31, 2015 (unaudited)	September 30, 2015
ASSETS		
Cash and due from depository institutions	\$ 16,334	\$ 16,026
Interest bearing deposits in depository institutions	40,036	24,237
Total cash and cash equivalents	56,370	40,263
Investment securities available for sale, at fair value	116,767	128,354
Investment securities held to maturity at cost (fair value of \$53,931 and \$56,825)	54,914	57,221
Restricted stock, at cost	4,762	4,765
Loans receivable, net of allowance for loan losses of \$4,576 and \$4,667, respectively	461,491	391,307
Other real estate owned	1,168	1,168
Accrued interest receivable	2,722	2,484
Property and equipment, net	6,486	6,535
Deferred income taxes, net	2,874	2,874
Bank-owned life insurance	18,033	17,905
Other assets	1,561	2,814
Total assets	\$ 727,148	\$ 655,690
LIABILITIES		
Deposits:		
Non-interest bearing	\$ 28,260	\$ 27,010
Interest-bearing	506,441	438,512
Total deposits	534,701	465,522
FHLB Advances	103,000	103,000
Advances from borrowers for taxes and insurance	2,790	1,806
Accrued interest payable	398	396
Other liabilities	3,601	3,575
Total liabilities	644,490	574,299
SHAREHOLDERS' EQUITY		
Preferred stock, \$0.01 par value, 10,000,000 shares, authorized, none issued	—	—
Common stock, \$0.01 par value, authorized 40,000,000 shares authorized, issued and outstanding: 6,558,473 shares at December 31, 2015 and September 30, 2015	66	66
Additional paid in capital	60,387	60,365
Retained earnings	25,158	23,814
Unearned Employee Stock Ownership Plan (ESOP) shares	(1,739)	(1,775)

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Accumulated other comprehensive loss	(1,214)	(1,079)
Total shareholders' equity	82,658		81,391	
Total liabilities and shareholders' equity	\$ 727,148		\$ 655,690	

See accompanying notes to unaudited consolidated financial statements.

MALVERN BANCORP, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

(in thousands, except for per share data) (unaudited)	Three Months Ended December 31,	
	2015	2014
Interest and Dividend Income		
Loans, including fees	\$ 4,545	\$ 4,202
Investment securities, taxable	875	514
Investment securities, tax-exempt	195	37
Dividends, restricted stock	54	37
Interest-bearing cash accounts	18	23
Total Interest and Dividend Income	5,687	4,813
Interest Expense		
Deposits	964	859
Borrowings	512	393
Total Interest Expense	1,476	1,252
Net interest income	4,211	3,561
Provision for Loan Losses	—	90
Net Interest Income after Provision for Loan Losses	4,211	3,471
Other Income		
Service charges and other fees	211	270
Rental income-other	50	64
Net gains on sales of investments	131	26
Net gains on sale of loans	34	19
Earnings on bank-owned life insurance	132	132
Total Other Income	558	511
Other Expense		
Salaries and employee benefits	1,499	1,728
Occupancy expense	423	424
Federal deposit insurance premium	200	167
Advertising	30	85
Data processing	297	302
Professional fees	400	343
Other real estate owned (income) expenses, net	(1)	(36)
Other operating expenses	577	648
Total Other Expense	3,425	3,661
Income before income tax expense	1,344	321
Income tax expense	—	—
Net Income	\$ 1,344	\$ 321
Basic Earnings Per Share	\$ 0.21	\$ 0.05
Dividends Declared Per Share	\$ 0.00	\$ 0.00

See accompanying notes to unaudited consolidated financial statements.

MALVERN BANCORP, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited)**

(in thousands)	Three Months Ended December 31,	
	2015	2014
Net Income	\$ 1,344	\$ 321
Other Comprehensive (Loss) Income, Net of Tax:		
Unrealized holding (losses) gains on available-for-sale securities	(482)	1,163
Tax effect	164	(395)
Net of tax amount	(318)	768
Reclassification adjustment for net gains arising during the period ⁽¹⁾	(131)	(26)
Tax effect	45	8
Net of tax amount	(86)	(18)
Accretion of unrealized holding losses on securities transferred from available-for-sale to held-to-maturity ⁽²⁾	2	—
Tax effect	(1)	—
Net of tax amount	1	—
Fair value adjustments on derivatives	403	—
Tax effect	(135)	—
Net of tax amount	268	—
Total other comprehensive (loss) income	(135)	750
Total comprehensive income	\$ 1,209	\$ 1,071

⁽¹⁾ Amounts are included in net gain on sales of securities on the Consolidated Statements of Operations in total other income.

⁽²⁾ Amounts are included in interest and dividends on investment securities on the Consolidated Statements of Operations.

See accompanying notes to unaudited consolidated financial statements.

MALVERN BANCORP, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY****(Unaudited)**

	Common Stock	Additional Paid-In Capital	Retained Earnings	Unearned ESOP Shares	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	(in thousands, except share data)					
Balance, October 1, 2014	\$66	\$ 60,317	\$ 20,116	\$ (1,922)	) \$ (1,805)	) \$ 76,772
Net Income	—	—	321	—	—	321
Other comprehensive income	—	—	—	—	750	750
Committed to be released ESOP shares (3,600 shares)	—	5	—	37	—	42
Balance, December 31, 2014	\$66	\$ 60,322	\$ 20,437	\$ (1,885)	) \$ (1,055)	) \$ 77,885
Balance, October 1, 2015	\$66	\$ 60,365	\$ 23,814	\$ (1,775)	) \$ (1,079)	) \$ 81,391
Net Income	—	—	1,344	—	—	1,344
Other comprehensive loss	—	—	—	—	(135)	) (135)
Committed to be released ESOP shares (3,600 shares)	—	22	—	36	—	58
Balance, December 31, 2015	\$66	\$ 60,387	\$ 25,158	\$ (1,739)	) \$ (1,214)	) \$ 82,658

See accompanying notes to unaudited consolidated financial statements.

MALVERN BANCORP, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

(in thousands)	Three Months Ended December	
	31, 2015	2014
Cash Flows from Operating Activities		
Net income	\$ 1,344	\$ 321
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation expense	158	159
Provision for loan losses	—	90
Deferred income taxes benefit	(230)	(430)
ESOP expense	58	42
Amortization (accretion) of premiums and discounts on investment securities, net	328	(2,596)
Amortization of loan origination fees and costs	552	136
Amortization of mortgage service rights	13	20
Net gain on sale of investment securities available-for-sale	(131)	(26)
Net gain (loss) on sale of secondary market loans	34	(19)
Proceeds on sale of secondary market loans	1,441	982
Originations of secondary market loans	(1,475)	(963)
Gain on sale of other real estate owned	—	(53)
Write down of other real estate owned	—	19
Earnings on bank-owned life insurance	(132)	(132)
Increase in accrued interest receivable	(238)	(301)
Increase in accrued interest payable	2	102
Increase in other liabilities	129	671
(Increase) decrease in other assets	(424)	310
Net Cash Provided by (Used in) Operating Activities	1,429	(1,668)
Cash Flows from Investing Activities		
Investment securities available-for-sale:		
Purchases	(2,115)	(57,169)
Sales	12,500	21,051
Maturities, calls and principal repayments	1,664	5,034
Investment securities held-to-maturity:		
Maturities, calls and principal repayments	2,259	—
(Loan originations) and principal collections, net	(70,736)	2,459
Proceeds from sale of other real estate owned	—	503
Additions to mortgage servicing rights	—	(8)
Proceeds from death benefit of bank-owned life insurance	1,049	—
Net increase (decrease) in restricted stock	3	(302)
Purchases of property and equipment	(109)	(55)
Net Cash Used in Investing Activities	(55,485)	(28,487)

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Cash Flows from Financing Activities		
Net increase in deposits	69,179	27,672
Proceeds from long-term borrowings	15,000	30,000
Repayment of long-term borrowings	(15,000)	—
Increase in advances from borrowers for taxes and insurance	984	1,348
Net Cash Provided by Financing Activities	70,163	59,020
Net Increase in Cash and Cash Equivalents	16,107	28,865
Cash and Cash Equivalent – Beginning	40,263	19,187
Cash and Cash Equivalent – Ending	\$ 56,370	\$ 48,052
Supplementary Cash Flows Information		
Interest paid	\$ 1,474	\$ 1,150

See accompanying notes to unaudited consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 – Basis of Presentation

The consolidated financial statements of Malvern Bancorp, Inc. (the “Company” or “Malvern Bancorp”) include the accounts of the Company and its wholly-owned subsidiary, Malvern Federal Savings Bank (“Malvern Federal Savings” or the “Bank”) and the Bank’s subsidiary, Strategic Asset Management Group, Inc. All significant intercompany accounts and transactions have been eliminated from the accompanying consolidated financial statements.

The Bank is a federally chartered stock savings bank which was originally organized in 1887. The Bank operates from its headquarters in Paoli, Pennsylvania and through its seven full service financial center offices in Chester and Delaware Counties, Pennsylvania.

We continue to execute on our business plans and are positioning the Company to take advantage of the growth activity we are achieving in our markets, which includes our two new private banking / loan production offices in Villanova, PA and Morristown, New Jersey.

In preparing the consolidated financial statements, management has made estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the consolidated statements of condition and that affect the results of operations for the periods presented. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to change in the near term relate to the determination of the allowance for loan losses, other real estate owned, the evaluation of deferred tax assets and the other-than-temporary impairment evaluation of securities.

The consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (“U.S. GAAP”).

Note 2 – Recent Accounting Pronouncements

In January 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2016-01, “Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets

and Financial Liabilities.” The new guidance is intended to improve the recognition and measurement of financial instruments. The ASU affects public and private companies, not-for-profit organizations, and employee benefit plans that hold financial assets or owe financial liabilities. ASU No. 2016-01 is effective for interim and annual reporting periods beginning after December 15, 2017. The Company is currently evaluating the effect that the standard will have on its consolidated financial statements and related disclosures.

In November 2015, the FASB issued ASU No. 2015-17, “Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes.” The FASB is issuing the amendments in this Update as part of its initiative to reduce complexity in accounting standards (the Simplification Initiative). The objective of the Simplification Initiative is to identify, evaluate, and improve areas of generally accepted accounting principles (“GAAP”) for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements. To simplify the presentation of deferred income taxes, the amendments in this Update require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The amendments in this Update apply to all entities that present a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in this Update. ASU No. 2015-17 is effective for interim and annual reporting periods beginning after December 15, 2016. Early adoption is permitted, including adoption in an interim period. All other amendments will be effective upon the issuance of this Update. The Company has evaluated the standard and determined that it has no effect on the Company’s consolidated financial statements and related disclosures.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 3 – Earnings Per Share**

Basic earnings per common share is computed based on the weighted average number of shares outstanding reduced by unearned ESOP shares. Diluted earnings per share is computed based on the weighted average number of shares outstanding and common stock equivalents (“CSEs”) that would arise from the exercise of dilutive securities reduced by unearned ESOP shares. As of December 31, 2015 and for the three months ended December 31, 2015 and 2014, the Company had not issued and did not have any outstanding CSEs.

The following table sets forth the composition of the weighted average shares (denominator) used in the earnings per share computations.

(in thousands, except for share data)	Three Months Ended December 31,	
	2015	2014
Net Income	\$ 1,344	\$ 321
Weighted average shares outstanding	6,558,473	6,558,473
Average unearned ESOP shares	(156,141)	(170,541)
Weighted average shares outstanding – basic	6,402,332	6,387,932
Earnings per share – basic	\$ 0.21	\$ 0.05

Note 4 – Employee Stock Ownership Plan

The Company established an employee stock ownership plan (“ESOP”) for substantially all of its full-time employees. The current ESOP trustee is Bell Rock Capital, LLC. Shares of the Company’s common stock purchased by the ESOP are held until released for allocation to participants. Shares released are allocated to each eligible participant based on the ratio of each such participant’s base compensation to the total base compensation of all eligible plan participants. As the unearned shares are committed to be released and allocated among participants, the Company recognizes compensation expense equal to the fair value of the ESOP shares during the periods in which they become committed to be released. To the extent that the fair value of the ESOP shares released differs from the cost of such shares, the difference is charged or credited to additional paid-in capital. During the period from May 20, 2008 to September 30, 2008, the ESOP purchased 241,178 shares of the common stock for approximately \$2.6 million, an average price of \$10.86 per share, which was funded by a loan from Malvern Federal Bancorp, Inc. (the Company’s predecessor). The ESOP loan is being repaid principally from the Bank’s contributions to the ESOP. The loan, which bears an interest

rate of 5%, is being repaid in quarterly installments through 2026. Shares are released to participants proportionately as the loan is repaid. During the three months ended December 31, 2015 and 2014, there were 3,600 and 3,600 shares, respectively, committed to be released. At December 31, 2015, there were 154,365 unallocated shares and 104,853 allocated shares held by the ESOP which had an aggregate fair value of approximately \$2.7 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 - Investment Securities

The Company's investment securities are classified as available-for-sale or held-to-maturity at December 31, 2015 and at September 30, 2015. Investment securities available-for-sale are reported at fair value with unrealized gains or losses included in equity, net of tax. Accordingly, the carrying value of such securities reflects their fair value at the balance sheet date. Fair value is based upon either quoted market prices, or in certain cases where there is limited activity in the market for a particular instrument, assumptions are made to determine their fair value.

Transfers of debt securities from the available-for-sale category to the held-to-maturity category are made at fair value at the date of transfer. The unrealized holding gain or loss at the date of transfer remains in accumulated other comprehensive income and in the carrying value of the held-to-maturity investment security. Premiums or discounts on investment securities are amortized or accreted using the effective interest method over the life of the security as an adjustment of yield. Unrealized holding gains or losses that remain in accumulated other comprehensive income are amortized or accreted over the remaining life of the security as an adjustment of yield, offsetting the related amortization of the premium or accretion of the discount.

The following tables present information related to the Company's investment securities at December 31, 2015 and September 30, 2015.

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Investment Securities Available-for-Sale:				
U.S. government agencies	\$787	\$ —	\$ (8)	) \$779
State and municipal obligations	37,434	240	(140)	) 37,534
Single issuer trust preferred security	1,000	—	(151)	) 849
Corporate debt securities	65,030	—	(1,329)	) 63,701
	104,251	240	(1,628)	) 102,863
Mortgage-backed securities:				
Federal National Mortgage Association (FNMA), fixed-rate	8,443	—	(218)	) 8,225
Federal Home Loan Mortgage Company (FHLMC), fixed-rate	5,809	—	(130)	) 5,679
	14,252	—	(348)) 13,904
Total	\$118,503	\$ 240	\$ (1,976)) \$116,767
Investment Securities Held-to-Maturity:				

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U.S. government agencies	\$13,301	\$ —	\$ (124) \$13,177
State and municipal obligations	10,013	34	(61) 9,986
Corporate debt securities	3,988	—	(117	) 3,871
Mortgage-backed securities:				
Collateralized mortgage obligations, fixed-rate	27,612	3	(718	) 26,897
Total	\$54,914	\$ 37	\$ (1,020	) \$53,931
Total investment securities	\$173,417	\$ 277	\$ (2,996	) \$170,698

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 - Investment Securities – (continued)

	September 30, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Investment Securities Available-for-Sale:				
U.S. government agencies	\$816	\$ —	\$ (1)	) \$815
State and municipal obligations	42,007	192	(116)	) 42,083
Single issuer trust preferred security	1,000	—	(150)	) 850
Corporate debt securities	70,874	34	(926)	) 69,982
	114,697	226	(1,193)	) 113,730
Mortgage-backed securities:				
Federal National Mortgage Association (FNMA), fixed-rate	8,797	—	(105)	) 8,692
Federal Home Loan Mortgage Company (FHLMC), fixed-rate	5,986	—	(54)	) 5,932
	14,783	—	(159)	) 14,624
Total	\$129,480	\$ 226	\$ (1,352)	) \$128,354
Investment Securities Held-to-Maturity:				
U.S. government agencies	\$14,301	\$ 8	\$ (13)	) \$14,296
State and municipal obligations	10,075	23	(75)	) 10,023
Corporate debt securities	4,011	—	(55)	) 3,956
Mortgage-backed securities:				
Collateralized mortgage obligations, fixed-rate	28,834	55	(339)	) 28,550
Total	\$57,221	\$ 86	\$ (482)	) \$56,825
Total investment securities	\$186,701	\$ 312	\$ (1,834)	) \$185,179

During the year ended September 30, 2015, the Company transferred at fair value approximately \$57.5 million in available-for-sale investment securities to the held-to-maturity category. The net unrealized loss at date of transfer amounted to \$115,000 which is being amortized over the remaining life of the securities as an adjustment of yield, offsetting the related amortization of the premium or accretion of the discount on the transferred securities. No gains or losses were recognized at the time of transfer. Management considers the held-to-maturity classification of these investment securities to be appropriate as the Company has the positive intent and ability to hold these securities to maturity.

For the three months ended December 31, 2015, proceeds of available-for-sale investment securities sold amounted to approximately \$12.5 million. Gross realized gains on investment securities sold amounted to approximately \$131,000, while there were no gross realized losses for the period. For the three months ended December 31, 2014, proceeds of

investment securities sold amounted to approximately \$21.1 million. Gross realized gains on investment securities sold amounted to approximately \$99,000, while gross realized losses amounted to approximately \$73,000, for the period.

The varying amount of sales from the available-for-sale portfolio over the past few years, reflect the significant volatility present in the market. Given the historic low interest rates prevalent in the market, it is necessary for the Company to protect itself from interest rate exposure. Securities that once appeared to be sound investments can, after changes in the market, become securities that the Company has the flexibility to sell to avoid losses and mismatches of interest-earning assets and interest-bearing liabilities at a later time.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 - Investment Securities – (continued)

The following tables indicate gross unrealized losses not recognized in income and fair value, aggregated by investment category and the length of time individual securities have been in a continuous unrealized loss position at December 31, 2015 and September 30, 2015:

	December 31, 2015					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair value	Unrealized Losses
	(In thousands)					
Investment Securities Available-for-Sale:						
U.S. government agencies	\$—	\$ —	\$779	\$ (8	) \$779	\$ (8)
State and municipal obligations	14,727	(140)	—	—	14,727	(140)
Single issuer trust preferred security	—	—	849	(151)	849	(151)
Corporate debt securities	63,702	(1,329)	—	—	63,702	(1,329)
Mortgage-backed securities:						
FNMA, fixed-rate	5,141	(125)	3,085	(93)	8,226	(218)
FHLMC, fixed-rate	3,152	(72)	2,527	(58)	5,679	(130)
Total	\$86,722	\$ (1,666)	\$7,240	\$ (310)	\$93,962	\$ (1,976)
Investment Securities Held-to-Maturity:						
U.S. government agencies	13,178	(124)	—	—	13,178	(124)
State and municipal obligations	8,001	(61)	—	—	8,001	(61)
Corporate debt securities	3,871	(117)	—	—	3,871	(117)
Mortgage-backed securities:						
CMO, fixed-rate	25,952	(718)	—	—	25,952	(718)
Total	51,002	(1,020)	—	—	51,002	(1,020)
Total investment securities	\$137,724	\$ (2,686)	\$7,240	\$ (310)	\$144,964	\$ (2,996)

	September 30, 2015					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair value	Unrealized Losses
	(In thousands)					
Investment Securities Available-for-Sale:						
U.S. government agencies	\$—	\$ —	\$815	\$ (1) \$815	\$ (1)
State and municipal obligations	18,223	(116)	—	—	18,223	(116)

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Single issuer trust preferred security	—	—	850	(150)	850	(150)
Corporate debt securities	58,064	(926)	—	—	58,064	(926)
Mortgage-backed securities:						
FNMA, fixed-rate	5,459	(53)	3,233	(52)	8,692	(105)
FHLMC, fixed-rate	3,280	(25)	2,652	(29)	5,932	(54)
Total	\$85,026	\$ (1,120)	\$7,550	\$ (232)	\$92,576	\$ (1,352)
Investment Securities Held-to-Maturity:						
U.S. government agencies	4,792	(13)	—	—	4,792	(13)
State and municipal obligations	6,917	(75)	—	—	6,917	(75)
Corporate debt securities	3,957	(55)	—	—	3,957	(55)
Mortgage-backed securities:						
CMO, fixed-rate	22,734	(339)	—	—	22,734	(339)
Total	38,400	(482)	—	—	38,400	(482)
Total investment securities	\$123,426	\$ (1,602)	\$7,550	\$ (232)	\$130,976	\$ (1,834)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 5 - Investment Securities – (continued)**

As of December 31, 2015, the estimated fair value of the securities disclosed above was primarily dependent upon the movement in market interest rates, particularly given the negligible inherent credit risk associated with these securities. These investment securities are comprised of securities that are rated investment grade by at least one bond credit rating service. Although the fair value will fluctuate as market interest rates move, management believes that these fair values will recover as the underlying portfolios mature and are reinvested in market rate yielding investments. As of December 31, 2015, the Company held 15 U.S. government agency securities, 19 municipal bonds, 30 corporate securities, 45 mortgage-backed securities and one single issuer trust preferred security which were in an unrealized loss position. The Company does not intend to sell and expects that it is not more likely than not that it will be required to sell these securities until such time as the value recovers or the securities mature. Management does not believe any individual unrealized loss as of December 31, 2015 represents other-than-temporary impairment.

At December 31, 2015 and September 30, 2015 the Company had no securities pledged to secure public deposits.

The following table presents information for investment securities at December 31, 2015, based on scheduled maturities. Actual maturities can be expected to differ from scheduled maturities due to prepayment or early call options of the issuer.

	December 31, 2015	
	Amortized Cost	Fair Value
	(in thousands)	
Investment Securities Available-for-Sale:		
Due in one year or less	\$—	\$—
Due after one year through five years	14,170	14,011
Due after five years through ten years	72,047	70,893
Due after ten years	32,286	31,863
Total	\$118,503	\$116,767
Investment Securities Held-to-Maturity:		
Due after one year through five years	\$13,301	\$13,177
Due after five years through ten years	5,939	5,856
Due after ten years	35,674	34,898
Total	\$54,914	\$53,931
Total investment securities	\$173,417	\$170,698

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 6 - Loans Receivable and Related Allowance for Loan Losses**

Loans receivable in the Company's portfolio consisted of the following at the dates indicated below:

	December 31, 2015	September 30, 2015
	(in thousands)	
Residential mortgage	\$211,302	\$ 214,958
Construction and Development:		
Residential and commercial	6,007	5,677
Land	6,804	2,142
Total Construction and Development	12,811	7,819
Commercial:		
Commercial real estate	142,981	87,686
Multi-family	10,549	7,444
Other	25,975	13,380
Total Commercial	179,505	108,510
Consumer:		
Home equity lines of credit	23,207	22,919
Second mortgages	35,533	37,633
Other	2,299	2,359
Total Consumer	61,039	62,911
Total loans	464,657	394,198
Deferred loan fees and cost, net	1,410	1,776
Allowance for loan losses	(4,576)	(4,667)
Total loans receivable, net	\$461,491	\$ 391,307

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)

The following tables summarize the primary classes of the allowance for loan losses (“ALLL”), segregated into the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment as of December 31, 2015 and September 30, 2015. Activity in the allowance is presented for the three months ended December 31, 2015 and 2014 and the year ended September 30, 2015, respectively.

	Three Months Ended December 31, 2015										Total	
	Residential Mortgage	Residential and Commercial	Land Development	Commercial Real Estate	Multi- family	Other	Consumer Home Equity Lines of Credit	Second Mortgages	Other	Unallocated		
	(In thousands)											
Allowance for loan losses:												
Beginning balance	\$1,486	\$30	\$35	\$1,235	\$104	\$108	\$139	\$761	\$24	\$745	\$4,667	
Charge-offs	(9)	-	-	(98)	-	-	-	(197)	-	-	(304)	
Recoveries	-	188	-	2	-	1	-	21	1	-	213	
Provisions	(180)	(172)	71	702	(11)	58	(11)	75	(7)	(525)	-	
Ending Balance	\$1,297	\$46	\$106	\$1,841	\$93	\$167	\$128	\$660	\$18	\$220	\$4,576	
Ending balance: individually evaluated for impairment	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	
Ending balance: collectively evaluated for impairment	\$1,297	\$46	\$106	\$1,841	\$93	\$167	\$128	\$660	\$18	\$220	\$4,576	

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Loans receivable: Ending balance	\$211,302	\$6,007	\$6,804	\$142,981	\$10,549	\$25,975	\$23,207	\$35,533	\$2,299	\$464,657
Ending balance: individually evaluated for impairment	\$609	\$121	\$-	\$1,475	\$-	\$-	\$20	\$154	\$-	\$2,379
Ending balance: collectively evaluated for impairment	\$210,693	\$5,886	\$6,804	\$141,506	\$10,549	\$25,975	\$23,187	\$35,379	\$2,299	\$462,278

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)

Three Months Ended December 31, 2014											
	Construction and Development			Commercial			Consumer			Unallocated	
	Residential Mortgage	Residential and Commercial	Land	Commercial Real Estate	Multi-family	Other	Home Equity Lines of Credit	Second Mortgages	Other		Total
(In thousands)											
Allowance for loan losses:											
Beginning balance	\$1,672	\$291	\$13	\$1,248	\$29	\$50	\$168	\$1,033	\$23	\$62	\$4,589
Charge-offs	-	(1)	-	(48)	-	-	-	(31)	(17)	-	(97)
Recoveries	1	-	-	2	-	1	-	12	2	-	18
Provisions	(25)	73	(13)	(120)	123	(2)	(14)	(98)	21	145	90
Ending Balance	\$1,648	\$363	\$-	\$1,082	\$152	\$49	\$154	\$916	\$29	\$207	\$4,600
Ending balance: individually evaluated for impairment	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-
Ending balance: collectively evaluated for impairment	\$1,648	\$363	\$-	\$1,082	\$152	\$49	\$154	\$916	\$29	\$207	\$4,600
Loans receivable:											
Ending balance	\$229,507	\$6,039	\$-	\$67,274	\$5,450	\$5,603	\$24,430	\$45,051	\$2,675		\$386,029
Ending balance: individually evaluated	\$962	\$143	\$-	\$609	\$-	\$898	\$20	\$708	\$-		\$3,340

for
impairment
Ending
balance:
collectively
evaluated
for
impairment

\$228,545	\$5,896	\$-	\$66,665	\$5,450	\$4,705	\$24,410	\$44,343	\$2,675	\$382,689
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)

	Year Ended September 30, 2015										
	Residential Mortgage	Construction and Development Residential and Commercial Land Commercial	Commercial Real Estate	Commercial Multi- family	Other	Consumer Home Equity Lines of Credit	Second Mortgages	Other	Unallo-	Total	
	(In thousands)										
Allowance for loan losses:											
Beginning balance	\$1,672	\$291	\$13	\$1,248	\$29	\$50	\$168	\$1,033	\$23	\$62	\$4,589
Charge-offs	-	(1)	-	(48)	-	-	-	(138)	(34)	-	(221)
Recoveries	17	98	-	9	-	3	2	69	11	-	209
Provisions	(203)	(358)	22	26	75	55	(31)	(203)	24	683	90
Ending Balance	\$1,486	\$30	\$35	\$1,235	\$104	\$108	\$139	\$761	\$24	\$745	\$4,667
Ending balance: individually evaluated for impairment	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-	\$-
Ending balance: collectively evaluated for impairment	\$1,486	\$30	\$35	\$1,235	\$104	\$108	\$139	\$761	\$24	\$745	\$4,667
Loans receivable:											
Ending balance	\$214,958	\$5,677	\$2,142	\$87,686	\$7,444	\$13,380	\$22,919	\$37,633	\$2,359		\$394,198
Ending balance: individually evaluated	\$599	\$121	\$-	\$1,571	\$-	\$-	\$20	\$179	\$-		\$2,490

for
impairment
Ending
balance:
collectively
evaluated
for
impairment

\$214,359	\$5,556	\$2,142	\$86,115	\$7,444	\$13,380	\$22,899	\$37,454	\$2,359	\$391,708
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)

The following table presents impaired loans in portfolio by class, segregated by those for which a specific allowance was required and those for which a specific allowance was not necessary as of December 31, 2015 and September 30, 2015.

	Impaired Loans With Specific Allowance		Impaired Loans With No Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	Unpaid Principal Balance
	(in thousands)				
December 31, 2015:					
Residential mortgage	\$—	\$ —	\$ 609	\$ 609	\$ 723
Construction and Development:					
Residential and commercial	—	—	121	121	253
Commercial:					
Commercial real estate	—	—	1,475	1,475	1,658
Consumer:					
Home equity lines of credit	—	—	20	20	36
Second mortgages	—	—	154	154	320
Total impaired loans	\$—	\$ —	\$ 2,379	\$ 2,379	\$ 2,990
September 30, 2015:					
Residential mortgage	\$—	\$ —	\$ 599	\$ 599	\$ 696
Construction and Development:					
Residential and commercial	—	—	121	121	253
Commercial:					
Commercial real estate	—	—	1,571	1,571	1,807
Consumer:					
Home equity lines of credit	—	—	20	20	36
Second mortgages	—	—	179	179	342
Total impaired loans	\$—	\$ —	\$ 2,490	\$ 2,490	\$ 3,134

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)**

The following table presents the average recorded investment in impaired loans in portfolio and related interest income recognized for three months ended December 31, 2015 and 2014.

(in thousands)	Three Months Ended December 31, 2015	
	Average Impaired Loans	Interest Income Recognized on Impaired Loans
Residential mortgage	\$ 586	\$ —
Construction and Development:		
Residential and commercial	121	1
Commercial:		
Commercial real estate	1,536	55
Consumer:		
Home equity lines of credit	20	—
Second mortgages	189	—
Total	\$ 2,452	\$ 56

(in thousands)	Three Months Ended December 31, 2014	
	Average Impaired Loans	Interest Income Recognized on Impaired Loans
Residential mortgage	\$ 918	\$ —
Construction and Development:		
Residential and commercial	179	1
Commercial:		
Commercial real estate	523	—
Other	899	12
Consumer:		
Home equity lines of credit	35	—
Second mortgages	729	—
Total	\$ 3,283	\$ 13

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)

The following table presents the classes of the loan portfolio summarized by loans considered to be rated as pass and the categories of special mention, substandard and doubtful within the Company's internal risk rating system as of December 31, 2015 and September 30, 2015.

	December 31, 2015				
	Pass	Special Mention	Substandard	Doubtful	Total
	(in thousands)				
Residential mortgage	\$210,324	\$ 128	\$ 850	\$ —	\$211,302
Construction and Development:					
Residential and commercial	5,886	—	121	—	6,007
Land	6,804	—	—	—	6,804
Commercial:					
Commercial real estate	133,865	4,557	4,559	—	142,981
Multi-family	10,276	273	—	—	10,549
Other	24,985	269	721	—	25,975
Consumer:					
Home equity lines of credit	23,087	—	120	—	23,207
Second mortgages	34,727	132	674	—	35,533
Other	2,285	14	—	—	2,299
Total	\$452,239	\$ 5,373	\$ 7,045	\$ —	\$464,657

	September 30, 2015				
	Pass	Special Mention	Substandard	Doubtful	Total
	(in thousands)				
Residential mortgage	\$214,146	\$ 130	\$ 682	\$ —	\$214,958
Construction and Development:					
Residential and commercial	5,450	106	121	—	5,677
Land	2,142	—	—	—	2,142
Commercial:					
Commercial real estate	78,207	4,791	4,688	—	87,686
Multi-family	7,166	278	—	—	7,444
Other	12,387	272	721	—	13,380
Consumer:					
Home equity lines of credit	22,801	—	118	—	22,919
Second mortgages	36,834	133	666	—	37,633

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Other	2,345	14	—	—	2,359
Total	\$381,478	\$ 5,724	\$ 6,996	\$ —	\$394,198

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)**

The following table presents loans that are no longer accruing interest by portfolio class.

	December 31, 2015	September 30, 2015
	(in thousands)	
Residential mortgage	\$ 609	\$ 599
Construction and Development:		
Residential and commercial	12	12
Commercial:		
Commercial real estate	—	589
Consumer:		
Home equity lines of credit	20	20
Second mortgages	154	179
Total non-accrual loans	\$ 795	\$ 1,399

Under the Bank's loan policy, once a loan has been placed on non-accrual status, we do not resume interest accruals until the loan has been brought current and has maintained a current payment status for not less than six consecutive months. Interest income that would have been recognized on nonaccrual loans had they been current in accordance with their original terms was \$9,000 and \$29,000 for the three months ended December 31, 2015 and 2014, respectively. There were no loans past due 90 days or more and still accruing interest at December 31, 2015 or September 30, 2015.

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by whether a loan payment is "current," that is, it is received from a borrower by the scheduled due date, or the length of time a scheduled payment is past due. The following table presents the classes of the loan portfolio summarized by the aging categories as of December 31, 2015 and September 30, 2015.

	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or More Past Due	Total Past Due	Total Loans Receivable
(In thousands)					

December 31, 2015:

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Residential mortgage	\$206,109	\$ 4,313	\$ 271	\$ 609	\$ 5,193	\$ 211,302
Construction and Development:						
Residential and commercial	5,995	—	—	12	12	6,007
Land	6,804	—	—	—	—	6,804
Commercial:						
Commercial real estate	141,309	277	1,395	—	1,672	142,981
Multi-family	10,549	—	—	—	—	10,549
Other	25,895	—	80	—	80	25,975
Consumer:						
Home equity lines of credit	23,060	127	—	20	147	23,207
Second mortgages	34,453	482	444	154	1,080	35,533
Other	2,284	10	5	—	15	2,299
Total	\$456,458	\$ 5,209	\$ 2,195	\$ 795	\$ 8,199	\$ 464,657

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)

September 30, 2015:						
Residential mortgage	\$213,253	\$913	\$193	\$599	\$1,705	\$214,958
Construction and Development:						
Residential and Commercial	5,665	—	—	12	12	5,677
Land	2,142	—	—	—	—	2,142
Commercial:						
Commercial real estate	86,119	485	493	589	1,567	87,686
Multi-family	7,444	—	—	—	—	7,444
Other	13,380	—	—	—	—	13,380
Consumer:						
Home equity lines of credit	22,899	—	—	20	20	22,919
Second mortgages	37,010	345	99	179	623	37,633
Other	2,329	30	—	—	30	2,359
Total	\$390,241	\$1,773	\$785	\$1,399	\$3,957	\$394,198

Restructured loans deemed to be TDRs are typically the result of extension of the loan maturity date or a reduction of the interest rate of the loan to a rate that is below market, a combination of rate and maturity extension, or by other means including covenant modifications, forbearance and other concessions. However, the Company generally only restructures loans by modifying the payment structure to require payments of interest only for a specified period or by reducing the actual interest rate. Once a loan becomes a TDR, it will continue to be reported as a TDR during the term of the restructure.

The Company had five loans classified as TDRs with an aggregate outstanding balance of \$1.6 million at December 31, 2015 and September 30, 2015, respectively. At December 31, 2015, these loans were also classified as impaired. All of the TDR loans continue to perform under the restructured terms through December 31, 2015 and we continued to accrue interest on such loan through such date. Two commercial loans to one borrower, with an aggregate balance of \$492,000 were returned to accruing status at December 31, 2015. At September 30, 2015, these two commercial loans to one borrower with a balance of \$492,000 were non-accruing. All of such loans have been classified as TDRs since we modified the payment terms and in some cases interest rate from the original agreements and allowed the borrowers, who were experiencing financial difficulty, to make interest only payments for a period of time in order to relieve some of their overall cash flow burden. Some loan modifications classified as TDRs may not ultimately result in the full collection of principal and interest, as modified, and result in potential incremental losses. These potential incremental losses have been factored into our overall estimate of the allowance for loan losses. The level of any defaults will likely be affected by future economic conditions. A default on a troubled debt restructured loan for purposes of this disclosure occurs when the borrower is 90 days past due or a foreclosure or repossession of the applicable collateral has occurred.

TDRs may arise in which, due to financial difficulties experienced by the borrower, the Company obtains through physical possession one or more collateral assets in satisfaction of all or part of an existing credit. Once possession is obtained, the Company reclassifies the appropriate portion of the remaining balance of the credit from loans to OREO, which is included within other assets in the Consolidated Statements of Condition. For any residential real estate property collateralizing a consumer mortgage loan, the Company is considered to possess the related collateral only if legal title is obtained upon completion of foreclosure, or the borrower conveys all interest in the residential real estate property to the Company through completion of a deed in lieu of foreclosure or similar legal agreement. Excluding OREO, the Company had \$987,000 and \$1.2 million of residential real estate properties in the process of foreclosure at December 31, 2015 and September 30, 2015, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Loans Receivable and Related Allowance for Loan Losses – (continued)

The following table presents our TDR loans as of December 31, 2015 and September 30, 2015.

	Total Troubled Debt Restructurings	Number of Recorded Investment Loans	Troubled Debt Restructured Loans That Have Defaulted on Modified Terms Within The Past 12 Months	Number of Loans	Recorded Investment
At December 31, 2015:					
Construction and Development:					
Residential and commercial	1 \$ 109		—		\$ —
Commercial:					
Commercial real estate	4 1,475		—		—
Total	5 \$ 1,584		—		\$ —
At September 30, 2015:					
Construction and Development:					
Residential and commercial	1 \$ 109		—		\$ —
Commercial:					
Commercial real estate	4 1,474		2		982
Total	5 \$ 1,583		2		\$ 982

The following table reports the performing status all of TDR loans. The performing status is determined by the loans compliance with the modified terms.

	December 31, 2015		September 30, 2015	
	Performing	Non-Performing	Performing	Non-Performing
(in thousands)				
Construction and Development:				
Residential and commercial	\$ 109	\$ —	\$ 109	\$ —
Commercial:				
Commercial real estate	1,475	—	982	492
Total	\$ 1,584	\$ —	\$ 1,091	\$ 492

There was no new TDR activity for the three months ended December 31, 2015 and 2014.

Note 7 - Regulatory Matters

The Bank 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 Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk-weightings and other factors.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 7 - Regulatory Matters – (continued)

In July of 2013 the respective U.S. federal banking agencies issued final rules implementing Basel III and the Dodd-Frank Act capital requirements to be fully phased in on a global basis on January 1, 2019. The new regulations establish a new tangible common equity capital requirement, increase the minimum requirement for the current Tier 1 risk-weighted asset (“RWA”) ratio, phase out certain kinds of intangibles treated as capital and certain types of instruments and change the risk weightings of certain assets used to determine required capital ratios. The new common equity Tier 1 capital component requires capital of the highest quality – predominantly composed of retained earnings and common stock instruments. For community banks such as Malvern Federal Savings Bank, a common equity Tier 1 capital ratio 4.5% became effective on January 1, 2015. The new capital rules also increased the current minimum Tier 1 capital ratio from 4.0% to 6.0% beginning on January 1, 2015. In addition, in order to make capital distributions and pay discretionary bonuses to executive officers without restriction, an institution must also maintain greater than 2.5% in common equity attributable to a capital conservation buffer to be phased in from January 1, 2016 until January 1, 2019. The new rules also increase the risk weights for several categories of assets, including an increase from 100% to 150% for certain acquisition, development and construction loans and more than 90-day past due exposures. The new capital rules maintain the general structure of the prompt corrective action rules, but incorporate the new common equity Tier 1 capital requirement and the increased Tier 1 RWA requirement into the prompt corrective action framework.

The Bank remains well capitalized under the implementation of Basel III, which was effective January 1, 2015.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of tangible and core capital (as defined in the regulations) to total adjusted tangible assets (as defined) and of risk-based capital (as defined) to risk-weighted assets (as defined). The Office of the Comptroller of the Currency recently advised the Bank that, as of January 21, 2016, it no longer is required to satisfy the individual minimum capital ratios (“IMCRs”) previously imposed.

Management believes, as of December 31, 2015, that the Bank met all capital adequacy requirements to which it was subject.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 7 - Regulatory Matters – (continued)**

The Bank's actual capital amounts and ratios are also presented in the table:

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions			
	Amount	Ratio	Amount	Ratio	Amount	Ratio		
	(Dollars in thousands)							
As of December 31, 2015:								
Core Capital (to adjusted tangible assets)	\$70,435	10.43%	\$ ≥27,003	4.00	% \$ ≥33,753	5.00	%	
Common equity Tier 1 (to risk-weighted assets)	70,435	13.94	≥22,743	4.50	≥32,850	6.50		
Tier 1 Capital (to risk-weighted assets)	70,435	13.94	≥30,323	6.00	≥40,431	8.00		
Total risk-based Capital (to risk-weighted assets)	75,072	14.85	≥40,431	8.00	≥50,539	10.00		
As of September 30, 2015:								
Core Capital (to adjusted tangible assets)	\$69,030	10.80%	\$ ≥25,573	4.00	% \$ ≥31,966	5.00	%	
Common equity Tier 1 (to risk-weighted assets)	69,030	15.90	≥19,538	4.50	≥28,222	6.50		
Tier 1 Capital (to risk-weighted assets)	69,030	15.90	≥26,051	6.00	≥34,734	8.00		
Total risk-based Capital (to risk-weighted assets)	73,759	16.99	≥34,734	8.00	≥43,418	10.00		

Note 8 – Derivatives and Hedging Activities

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risks, including interest rate, liquidity, and credit risk primarily by managing the amount, sources, and duration of its debt funding and the use of derivative financial instruments. Specifically, the Company enters into derivative financial instruments to manage exposures that arise from business activities that result in the payment of future uncertain cash amounts, the value of which are determined by interest rates.

The Company's objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in Accumulated Other Comprehensive Income and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. At December 31, 2015, such derivatives were used to hedge the variable cash flows associated with FHLB advances. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. The Company's derivatives did not have any hedge ineffectiveness recognized in earnings during the three months ended December 31, 2015.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 8 – Derivatives and Hedging Activities – (continued)**

Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest expense as interest payments are made on the Company's variable-rate debt. During the next twelve months, the Company estimates approximately \$144,000 to be reclassified to earnings in interest expense. The Company is hedging its exposure to the variability in future cash flows for forecasted transactions over a maximum period of twenty months (excluding forecasted transactions related to the payment of variable interest on existing financial instruments).

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the Balance Sheet as of December 31, 2015 and September 30, 2015:

	December 31, 2015			
	Notional	Fair	Balance Sheet	Expiration
	Amount	Value	Location	Date
	(Dollars in thousand)			
Derivatives designated as hedging instruments				
Interest rate swaps by effective date:				
August 3, 2015	\$15,000	\$ 103	Other liabilities	August 3, 2020
	September 30, 2015			
	Notional	Fair	Balance Sheet	Expiration
	Amount	Value	Location	Date
	(Dollars in thousand)			
Derivatives designated as hedging instruments				
Interest rate swaps by effective date:				
August 3, 2015	\$15,000	\$ 348	Other liabilities	August 3, 2020

The table below presents the net gains (losses) recorded in accumulated other comprehensive income and the Consolidate Statements of Income relating to the cash flow derivative instruments for the three months ended December 31, 2015. There were no derivatives held by the Company at or for the three months ended December 31, 2014.

For the Three Months Ended December 31, 2015

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	Amount of Gain (Loss) Recognized in OCI (Effective Portion) (In thousands)	Amount of Gain (Loss) Reclassified from OCI to Interest Expense	Amount of Gain (Loss) Recognized in Other Non-Interest Income (Ineffective Portion)
Interest Rate Contracts	\$ 152	\$ (56)	\$ —

The company has agreements with each of its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then the company could also be declared in default on its derivative obligations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 8 – Derivatives and Hedging Activities – (continued)

At December 31, 2015, the fair value of derivatives in a net liability position, which includes accrued interest but excludes any adjustment for nonperformance risk, related to these agreements was \$140,000. As of December 31, 2015, the Company has minimum collateral posting thresholds with certain of its derivative counterparties and has posted collateral of \$600,000 against its obligations under these agreements. If the Company had breached any of these provisions at December 31, 2015, it could have been required to settle its obligations under the agreements at the termination value and would have been required to pay any additional amounts due in excess of amounts previously posted as collateral with the respective counterparty.

At September 30, 2015, the fair value of derivatives in a net liability position, which includes accrued interest but excludes any adjustment for nonperformance risk, related to these agreements was \$195,000. At September 30, 2015, the Company has minimum collateral posting thresholds with certain of its derivative counterparties and has posted collateral of \$600,000 against its obligations under these agreements. If the Company had breached any of these provisions at September 30, 2015, it could have been required to settle its obligations under the agreements at the termination value and would have been required to pay any additional amounts due in excess of amounts previously posted as collateral with the respective counterparty.

Note 9 - Fair Value Measurements

The Company follows FASB ASC Topic 820 “Fair Value Measurement,” to record fair value adjustments to certain assets and to determine fair value disclosures for the Company’s financial instruments. Investment and mortgage-backed securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans, real estate owned and certain other assets. These nonrecurring fair value adjustments typically involve application of lower-of-cost-or-market accounting or write-downs of individual assets.

The Company groups its assets at fair value in three levels, based on the markets in which the assets are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1—Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2—Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3—Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company's own estimates of assumptions that market participants would use in pricing the asset.

The Company bases its fair values on 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. It is our policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements, in accordance with the fair value hierarchy.

Fair value measurements for assets where there exists limited or no observable market data and, therefore, are based primarily upon the Company's or other third-party's estimates, are often calculated based on the characteristics of the asset, the economic and competitive environment and other factors. Therefore, the results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset. Additionally, there may be inherent weaknesses in any calculation technique, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, could significantly affect the results of current or future valuations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**Note 9 – Fair Value Measurements – (continued)**

FASB ASC Topic 825 “Financial Instruments” provides an option to elect fair value as an alternative measurement for selected financial assets and financial liabilities not previously recorded at fair value. The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation.

The Company monitors and evaluates available data to perform fair value measurements on an ongoing basis and recognizes transfers among the levels of the fair value hierarchy as of the date event or a change in circumstances that affects the valuation method chosen. There were no changes in valuation technique or transfers between levels at December 31, 2015 or September 30, 2015.

The table below presents the balances of assets measured at fair value on a recurring basis:

	December 31, 2015			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
Assets:				
Investment securities available-for-sale:				
Debt securities:				
U.S. government agencies	\$779	\$ —	\$779	\$ —
State and municipal obligations	37,534	—	37,534	—
Single issuer trust preferred security	849	—	849	—
Corporate debt securities	63,701	—	63,701	—
Total investment securities available-for-sale	102,863	—	102,863	—
Mortgage-backed securities available-for-sale:				
FNMA, fixed-rate	8,225	—	8,225	—
FHLMC, fixed-rate	5,679	—	5,679	—
Total mortgage-backed securities available-for-sale	13,904	—	13,904	—
Total investments securities available for sale	\$116,767	\$ —	\$116,767	\$ —
Liabilities:				
Derivative instruments	\$103	\$ —	\$103	\$ —

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9 - Fair Value Measurements – (continued)

	September 30, 2015			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
Assets:				
Investment securities available-for-sale:				
Debt securities:				
U.S. government agencies	\$815	\$ —	\$815	\$ —
State and municipal obligations	42,083	—	42,083	—
Single issuer trust preferred security	850	—	850	—
Corporate debt securities	69,982	—	69,982	—
Total investment securities available-for-sale	113,730	—	113,730	—
Mortgage-backed securities available-for-sale:				
FNMA, fixed-rate	8,692	—	8,692	—
FHLMC, fixed-rate	5,932	—	5,932	—
Total mortgage-backed securities available-for-sale	14,624	—	14,624	—
Total investments securities available for sale	\$128,354	\$ —	\$128,354	\$ —
Liabilities:				
Derivative instruments	\$348	\$ —	\$348	\$ —

For assets measured at fair value on a nonrecurring basis that were still held at the end of the period, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related individual assets or portfolios at December 31, 2015 and September 30, 2015:

	December 31, 2015			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
Impaired loans ^{(1) (2)}	\$ 21	\$ —	\$ —	\$ 21
Total	\$ 21	\$ —	\$ —	\$ 21

December 31, 2015		Unobservable Input	Range/(Weighted Average)
Fair Value	Valuation Technique		
at			
December			
31,			

	2015			
	(Dollars in thousands)			
Impaired loans ^{(1) (2)}	\$21	Appraisal of collateral ⁽³⁾	Collateral discounts ⁽⁴⁾	28%/(0.4%)
Total	\$21			

(1) At December 31, 2015, consisted of one loan with an aggregate balance of \$21,000 and there was no specific loan loss allowance.

(2) Includes assets directly charged-down to fair value during the year-to-date period.

(3) Fair value is generally determined through independent appraisals of the underlying collateral primarily using comparable sales.

(4) Appraisals may be adjusted by management for qualitative factors such as time, changes in economic conditions and estimated liquidation expense.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9 - Fair Value Measurements – (continued)

	September 30, 2015			
	Total	Level 1	Level 2	Level 3
	(In thousands)			
Impaired loans ^{(1) (2)}	\$48	\$ —	\$ —	\$ 48
Mortgage servicing rights	30	—	30	—
Total	\$78	\$ —	\$ 30	\$ 48

	September 30, 2015			
	Fair Value	at September 30, 2015	Valuation Technique	Unobservable Input
	(Dollars in thousands)			
Impaired loans ^{(1) (2)}	\$48	Appraisal of collateral ⁽³⁾	Collateral discounts ⁽⁴⁾	65 – 80%/(74%)
Total	\$48			

(1) At September 30, 2015, consisted of two loans with an aggregate balance of \$48,000 and there were no specific loan loss allowance.

(2) Includes assets directly charged-down to fair value during the year-to-date period.

(3) Fair value is generally determined through independent appraisals of the underlying collateral primarily using comparable sales.

(4) Appraisals may be adjusted by management for qualitative factors such as time, changes in economic conditions and estimated liquidation expense.

The following table shows active information regarding significant techniques and inputs used at December 31, 2015 and September 30, 2015 for measures in a non-recurring basis using unobservable inputs (Level 2):

	Fair Value at December 31, 2015 (in thousands)	Valuation Technique	Unobservable Input	Method or Value as of December 31, 2015
Mortgage servicing rights	\$—	Discounted rate	Discount rate	11.00 – 12.00 % Rate used through modeling per
			Loan prepayment speeds	14.22 % Weighted-average CPR
			Servicing fees	0.25 % Of loan balance
			Servicing costs	\$6.25 Monthly servicing cost per acco
				\$300 – 500 Additional monthly servicing co
				per loan on loans more than 30 c
				delinquent

	Fair Value at September 30, 2015 (in thousands)	Valuation Technique	Unobservable Input	Method or Value as of September 30, 2015
Mortgage servicing rights	\$30	Discounted rate	Discount rate	11.00 – 12.00 % Rate used through modeling p
			Loan prepayment speeds	14.73 % Weighted-average CPR
			Servicing fees	0.25 % Of loan balance
			Servicing costs	\$6.25 Monthly servicing cost per acco
				\$300 – 500 Additional monthly servicing o
				per loan on loans more than 30
				delinquent

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9 - Fair Value Measurements – (continued)

The following disclosure of the estimated fair value of financial instruments is made in accordance with the requirements of FASB ASC 825. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methods. However, considerable judgment is necessarily required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company would realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. FASB ASC 825 excludes certain financial instruments and all non-financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

The fair value estimates presented herein are based on pertinent information available to management as of December 31, 2015 and September 30, 2015. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since December 31, 2015 and September 30, 2015 and, therefore, current estimates of fair value may differ significantly from the amounts presented herein

The following assumptions were used to estimate the fair value of the Company's financial instruments:

Cash and Cash Equivalents—These assets are carried at historical cost. The carrying amount is a reasonable estimate of fair value because of the relatively short time between the origination of the instrument and its expected realization.

Investment Securities—Investment and mortgage-backed securities available for sale (carried at fair value) and held to maturity (carried at amortized cost) are measured at fair value on a recurring basis. Fair value measurements for these securities are typically obtained from independent pricing services that we have engaged for this purpose. When available, we, or our independent pricing service, use quoted market prices to measure fair value. If market prices are not available, fair value measurement is based upon models that incorporate available trade, bid and other market information and for structured securities, cash flow and, when available, loan performance data. Because many fixed income securities do not trade on a daily basis, our independent pricing service's applications apply available information through processes such as benchmark curves, benchmarking of like securities, sector groupings and matrix pricing to prepare evaluations. For each asset class, pricing applications and models are based on information from market sources and integrate relevant credit information. All of our securities available for sale are valued using either of the foregoing methodologies to determine fair value adjustments recorded to our financial statements. The

Company had no Level 1 or Level 3 securities as of December 31, 2015 or September 30, 2015.

Loans Receivable—We do not record loans at fair value on a recurring basis. As such, valuation techniques discussed herein for loans are primarily for estimating fair value for FASB ASC 825 disclosure purposes. However, from time to time, we record nonrecurring fair value adjustments to loans to reflect partial write-downs for impairment or the full charge-off of the loan carrying value. The valuation of impaired loans is discussed below. The fair value estimate for FASB ASC 825 purposes differentiates loans based on their financial characteristics, such as product classification, loan category, pricing features and remaining maturity. Prepayment and credit loss estimates are evaluated by loan type and rate. The fair value of loans is estimated by discounting contractual cash flows using discount rates based on current industry pricing, adjusted for prepayment and credit loss estimates.

Impaired Loans—Impaired loans are valued utilizing independent appraisals that rely upon quoted market prices for similar assets in active markets. These appraisals include adjustments to comparable assets based on the appraisers' market knowledge and experience. The appraisals are adjusted downward by management, as necessary, for changes in relevant valuation factors subsequent to the appraisal date and are considered level 3 inputs.

Accrued Interest Receivable—This asset is carried at historical cost. The carrying amount is a reasonable estimate of fair value because of the relatively short time between the origination of the instrument and its expected realization.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9 - Fair Value Measurements – (continued)

Restricted Stock—Although restricted stock is an equity interest in the FHLB, it is carried at cost because it does not have a readily determinable fair value as its ownership is restricted and it lacks a market. The estimated fair value approximates the carrying amount.

Other Real Estate Owned—Assets acquired through foreclosure or deed in lieu of foreclosure are recorded at estimated fair value less estimated selling costs when acquired, thus establishing a new cost basis. Fair value is generally based on independent appraisals. These appraisals include adjustments to comparable assets based on the appraisers' market knowledge and experience, and are considered level 3 inputs. When an asset is acquired, the excess of the loan balance over fair value, less estimated selling costs, is charged to the allowance for loan losses. If the estimated fair value of the asset declines, a write-down is recorded through expense. The valuation of foreclosed assets is subjective in nature and may be adjusted in the future because of, among other factors, changes in the economic conditions.

Deposits—Deposit liabilities are carried at cost. As such, valuation techniques discussed herein for deposits are primarily for estimating fair value for FASB ASC 825 disclosure purposes. The fair value of deposits is discounted based on rates available for borrowings of similar maturities. A decay rate is estimated for non-time deposits. The discount rate for non-time deposits is adjusted for servicing costs based on industry estimates.

Long-Term Borrowings—Advances from the FHLB are carried at amortized cost. However, we are required to estimate the fair value of long-term debt under FASB ASC 825. The fair value is based on the contractual cash flows discounted using rates currently offered for new notes with similar remaining maturities.

Derivatives— The fair value of derivatives are based on valuation models using observable market data as of the measurement date (level 2). Our derivatives are traded in an over-the-counter market where quoted market prices are not always available. Therefore, the fair values of derivatives are determined using quantitative models that utilize multiple market inputs. The inputs will vary based on the type of derivative, but could include interest rates, prices and indices to generate continuous yield or pricing curves, prepayment rate, and volatility factors to value the position. The majority of market inputs are actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services.

Accrued Interest Payable—This liability is carried at historical cost. The carrying amount is a reasonable estimate of fair value because of the relatively short time between the origination of the instrument and its expected realization.

Commitments to Extend Credit and Letters of Credit—The majority of the Company's commitments to extend credit and letters of credit carry current market interest rates if converted to loans. Because commitments to extend credit and letters of credit are generally unassignable by either the Bank or the borrower, they only have value to the Company and the borrower. The estimated fair value approximates the recorded deferred fee amounts, which are not significant.

Mortgage Servicing Rights—The fair value of mortgage servicing rights is based on observable market prices when available or the present value of expected future cash flows when not available. Assumptions, such as loan default rates, costs to service, and prepayment speeds significantly affect the estimate of future cash flows. Mortgage servicing rights are carried at the lower of cost or fair value.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9 - Fair Value Measurements – (continued)

The carrying amount and estimated fair value of the Company's financial instruments as of December 31, 2015 and September 30, 2015 are presented below:

	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
	(In thousands)				
December 31, 2015:					
Financial assets:					
Cash and cash equivalents	\$56,370	\$56,370	\$56,370	\$—	\$—
Investment securities available-for-sale	116,767	116,767	—	116,767	—
Investment securities held-to-maturity	54,914	53,931	—	53,931	—
Loans receivable, net	461,491	469,133	—	—	469,133
Accrued interest receivable	2,722	2,722	—	2,722	—
Restricted stock	4,762	4,762	—	4,762	—
Mortgage servicing rights (included in Other Assets)	388	417	—	417	—
Financial liabilities:					
Savings accounts	45,312	45,312	—	45,312	—
Checking and NOW accounts	114,268	114,268	—	114,268	—
Money market accounts	133,608	133,608	—	133,608	—
Certificates of deposit	241,513	243,812	—	243,812	—
FHLB advances	103,000	103,839	—	103,839	—
Derivatives	103	103	—	103	—
Accrued interest payable	398	398	—	398	—
September 30, 2015:					
Financial assets:					
Cash and cash equivalents	\$40,263	\$40,263	\$40,263	\$—	\$—
Investment securities available-for-sale	128,354	128,354	—	128,354	—
Investment securities held-to-maturity	57,221	56,825	—	56,825	—
Loans receivable, net	391,307	400,305	—	—	400,305
Accrued interest receivable	2,484	2,484	—	2,484	—
Restricted stock	4,765	4,765	—	4,765	—
Mortgage servicing rights	401	416	—	416	—
Financial liabilities:					
Savings accounts	45,189	45,189	—	45,189	—
Checking and NOW accounts	109,907	109,907	—	109,907	—
Money market accounts	108,706	108,706	—	108,706	—
Certificates of deposit	201,720	203,257	—	203,257	—

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FHLB advances	103,000	104,889	—	104,889	—
Derivatives	348	348	—	348	—
Accrued interest payable	396	396	—	396	—

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 10 – Income Taxes

Deferred income taxes at December 31, 2015 and September 30, 2015 were as follows:

	December 31, 2015	September 30, 2015	
	(in thousands)		
Deferred Tax Assets:			
Unrealized loss on investments available-for-sale	\$590	\$ 383	
Allowance for loan losses	2,985	2,985	
Non-accrual interest	86	98	
Write-down of real estate owned	106	106	
Alternative minimum tax (AMT) credit carryover	147	128	
Low-income housing tax credit carryover	337	337	
Supplement Employer Retirement Plan	409	455	
Charitable contributions	49	36	
Depreciation	—	205	
Federal net operating loss	5,985	6,375	
Other	382	338	
Total Deferred Tax Assets	11,076	11,446	
Valuation allowance for DTA	(7,824)	(8,043)	
Total Deferred Tax Assets, Net of Valuation Allowance	3,252	3,403	
Deferred Tax Liabilities:			
State net operating income	—	(187)	
Depreciation	(11)	—	
Mortgage servicing rights	(132)	(136)	
Other	(235)	(206)	
Total Deferred Tax Liabilities	(378)	(529)	
Deferred Tax Assets, Net	\$2,874	\$ 2,874	

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 11 – Comprehensive Income (Loss)

The components of accumulated other comprehensive (loss) included in shareholders' equity are as follows:

December 31, 2015	September 30, 2015
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