CAPITOL FEDERAL FINANCIAL
Form 10-Q
February 04, 2010

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

Form 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2009

or

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

Commission file number: 000-25391

Capitol Federal Financial
(Exact name of registrant as specified in its charter)

United States	48-1212142
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
700 Kansas Avenue, Topeka, Kansas	66603
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code:
(785) 235-1341

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 requirements for the past 90 days. Yes þ 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 a smaller reporting company. See definition of "accelerated filer, large accelerated filer, and smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer ¨	Non-accelerated filer ¨ (do not check if a smaller reporting company)	Smaller 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 þ

As of January 25, 2010, there were 73,971,687 shares of Capitol Federal Financial Common Stock outstanding.

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PART I -- FINANCIAL INFORMATION
Item 1. Financial Statements
CAPITOL FEDERAL FINANCIAL AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands except per share data and amounts)

	December 31, 2009	September 30, 2009
ASSETS:	(Unaudited)	
Cash and cash equivalents (includes interest-earning deposits of $80,895 and $32,319)	$ 105,128	$ 41,154
Investment securities:		
Available-for-sale ("AFS") at estimated fair value (amortized cost of $234,500 and $235,185)	234,001	234,784
Held-to-maturity ("HTM") at amortized cost (estimated fair value of $419,352 and $248,929)	417,942	245,920
Mortgage-backed securities ("MBS"):		
AFS, at estimated fair value (amortized cost of $1,254,958 and $1,334,357)	1,305,096	1,389,211
HTM, at amortized cost (estimated fair value of $594,365 and $627,829)	572,873	603,256
Loans receivable, net of allowance for loan losses ("ALLL") of $12,207 and $10,150	5,423,923	5,603,965
Bank-owned life insurance ("BOLI")	53,777	53,509
Capital stock of Federal Home Loan Bank ("FHLB"), at cost	134,064	133,064
Accrued interest receivable	31,048	32,640
Premises and equipment, net	39,901	37,709
Real estate owned ("REO"), net	6,637	7,404
Prepaid federal insurance premium	25,735	--
Other assets	24,637	21,064
TOTAL ASSETS	$ 8,374,762	$ 8,403,680
LIABILITIES:		
Deposits	$ 4,227,252	$ 4,228,609
Advances from FHLB	2,394,214	2,392,570
Other borrowings, net	713,609	713,609
Advance payments by borrowers for taxes and insurance	21,339	55,367
Income taxes payable	13,881	6,016
Deferred income tax liabilities, net	31,740	30,970
Accounts payable and accrued expenses	30,728	35,241
Total liabilities	7,432,763	7,462,382
STOCKHOLDERS' EQUITY:		
Preferred stock ($0.01 par value) 50,000,000 shares authorized; none issued	--	--
Common stock ($0.01 par value) 450,000,000 shares authorized, 91,512,287 shares issued; 74,023,577 and 74,099,355 shares outstanding as of December 31, 2009 and September 30, 2009, respectively	915	915
Additional paid-in capital	453,975	452,872
Unearned compensation, Employee Stock Ownership Plan ("ESOP")	(7,561)	(8,066)
Unearned compensation, Recognition and Retention Plan ("RRP")	(260)	(330)
Retained earnings	785,914	781,604

Accumulated other comprehensive income, net of tax	30,875	33,870
Less shares held in treasury (17,488,710 and 17,412,932 shares as of		
December 31, 2009 and September 30, 2009, respectively, at cost)	(321,859)	(319,567)
Total stockholders' equity	941,999	941,298
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$8,374,762	$8,403,680

See accompanying notes to consolidated financial statements.

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CAPITOL FEDERAL FINANCIAL AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)
(Dollars and share counts in thousands except per share data)

	For the Three Months Ended December 31,	
	2009	2008
INTEREST AND DIVIDEND INCOME:		
Loans receivable	$74,526	$76,716
MBS	20,754	26,402
Investment securities	2,559	1,326
Capital stock of FHLB	1,001	780
Cash and cash equivalents	47	49
Total interest and dividend income	98,887	105,273
INTEREST EXPENSE:		
FHLB advances	24,819	29,545
Deposits	22,105	26,785
Other borrowings	7,109	7,725
Total interest expense	54,033	64,055
NET INTEREST AND DIVIDEND INCOME	44,854	41,218
PROVISION FOR LOAN LOSSES	3,115	549
NET INTEREST AND DIVIDEND INCOME AFTER PROVISION FOR LOAN LOSSES	41,739	40,669
OTHER INCOME:		
Retail fees and charges	4,723	4,530
Insurance commissions	582	491
Loan fees	581	569
Income from BOLI	268	384
Gains on securities and loans receivable, net	6,472	24
Other, net	505	644
Total other income	13,131	6,642
OTHER EXPENSES:		
Salaries and employee benefits	10,532	11,164
Occupancy of premises	3,942	3,722
Federal insurance premium	1,814	166
Advertising	1,644	1,742
Deposit and loan transaction costs	1,380	1,303
Regulatory and outside services	1,448	1,149
Office supplies and related expenses	625	713
Other, net	1,364	2,228
Total other expenses	22,749	22,187
INCOME BEFORE INCOME TAX EXPENSE	32,121	25,124
INCOME TAX EXPENSE	11,141	9,272
NET INCOME	$20,980	$15,852

Basic earnings per common share	$0.29	$0.22
Diluted earnings per common share	$0.29	$0.22
Dividends declared per public share	$0.79	$0.61
Basic weighted average common shares	73,281	73,085
Diluted weighted average common shares	73,287	73,176

See accompanying notes to consolidated financial statements.

CAPITOL FEDERAL FINANCIAL AND SUBSIDIARY
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(Unaudited)
(Dollars in thousands)

	Common Stock	Additional Paid-In Capital	Unearned Compensation ESOP	Unearned Compensation RRP	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Total Stockholders' Equity
Balance at October 1, 2009	$ 915	$ 452,872	$ (8,066)	$ (330)	$ 781,604	$ 33,870	$ (319,567)	$ 941,298
Comprehensive income:								
Net income					20,980			20,980
Changes in unrealized gain/losses on								
securities AFS, net of deferred								
income taxes of $1,819						(2,995)		(2,995)
Total comprehensive income								17,985
ESOP activity, net		1,039	505					1,544
RRP activity, net		3						3
Stock based compensation - stock options and RRP		61		70				131
Acquisition of treasury stock							(2,292)	(2,292)
Dividends on common stock to								
stockholders ($0.79 per public share)					(16,670)			(16,670)
Balance at December 31, 2009	$ 915	$ 453,975	$ (7,561)	$ (260)	$ 785,914	$ 30,875	$ (321,859)	$ 941,999

See accompanying notes to consolidated financial statements.

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CAPITOL FEDERAL FINANCIAL AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in thousands)

	For the Three Months Ended December 31,	
	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$20,980	$15,852
Adjustments to reconcile net income to net cash provided by		
operating activities:		
FHLB stock dividends	(1,000)	(780)
Provision for loan losses	3,115	549
Originations of loans receivable held-for-sale (“LHFS”)	(1,701)	(738)
Proceeds from sales of LHFS	575	1,508
Amortization and accretion of premiums and discounts on MBS		
and investment securities	1,453	220
Depreciation and amortization of premises and equipment	1,272	1,156
Amortization of deferred amounts related to FHLB advances, net	1,644	(165)
Common stock committed to be released for allocation - ESOP	1,544	2,170
Stock based compensation - stock options and RRP	131	177
Gain on the sale of trading securities received in the loan swap transaction	(6,454)	--
Prepaid federal insurance premium	(25,735)	--
Other, net	(537)	66
Changes in:		
Accrued interest receivable	1,592	1,280
Other assets	(387)	1,303
Income taxes payable/receivable	10,457	5,855
Accounts payable and accrued expenses	(5,257)	(1,327)
Net cash provided by operating activities	1,692	27,126
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of trading securities received in the loan swap transaction	199,144	--
Proceeds from maturities or calls of investment securities AFS	23	28
Proceeds from maturities or calls of investment securities HTM	1,010	37,400
Purchases of investment securities HTM	(173,431)	(886)
Principal collected on MBS AFS	78,991	49,459
Principal collected on MBS HTM	33,389	40,735
Purchases of MBS HTM	(2,990)	--
Proceeds from the redemption of capital stock of FHLB	--	2,958
Purchases of capital stock of FHLB	--	(9,002)
Loan originations and purchases, net of principal collected	(18,233)	(138,149)
Net deferred fee activity	(925)	(35)
Purchases of premises and equipment	(3,473)	(3,088)
Proceeds from sales of REO	3,124	2,131
Net cash used in investing activities	116,629	(18,449)

(Continued)

	For the Three Months Ended December 31, 2009	2008
CASH FLOWS FROM FINANCING ACTIVITIES:		
Dividends paid	(16,670)	(12,737)
Deposits, net of withdrawals	(1,357)	(56,579)
Proceeds from advances/line of credit from FHLB	--	312,682
Repayments on advances/line of credit from FHLB	--	(162,682)
Change in advance payments by borrowers for taxes and insurance	(34,028)	(33,883)
Acquisitions of treasury stock	(2,292)	(859)
Stock options exercised and excess tax benefits from stock options	--	1,377
Net cash (used in)/provided by financing activities	(54,347)	47,319
NET INCREASE IN CASH AND CASH EQUIVALENTS	63,974	55,996
CASH AND CASH EQUIVALENTS:		
Beginning of period	41,154	87,138
End of period	$105,128	$143,134
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Income tax payments	$682	$3,417
Interest payments, net of interest credited to deposits	$30,004	$36,542
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Loans transferred to REO	$2,196	$1,846
Swap of loans for trading securities	$193,889	$--

(Concluded)

See accompanying notes to consolidated financial statements.

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Notes to Consolidated Financial Statements (Unaudited)

1. Basis of Financial Statement Presentation

The accompanying consolidated financial statements of Capitol Federal Financial ("CFFN") and subsidiary (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. These statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2009, filed with the Securities and Exchange Commission ("SEC"). Interim results are not necessarily indicative of results for a full year. In preparing these financial statements, we have evaluated events occurring subsequent to December 31, 2009 through February 4, 2010, the date our financial statements were filed with the SEC, for potential recognition and disclosure. There have been no material events or transactions which would require adjustments and/or disclosures to the consolidated financial statements at December 31, 2009.

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting periods. Significant estimates include the ALLL, other-than-temporary declines in the fair value of securities, and fair value measurements. Actual results could differ from those estimates. See "Item 2- Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies."

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Capitol Federal Savings Bank (the "Bank"). The Bank has a wholly-owned subsidiary, Capitol Funds, Inc. Capitol Funds, Inc. has a wholly-owned subsidiary, Capitol Federal Mortgage Reinsurance Company. All intercompany accounts and transactions have been eliminated.

2. Recent Accounting Pronouncements

Effective October 1, 2009, the Company adopted new authoritative accounting guidance under Accounting Standards Codification ("ASC") 260, Earnings Per Share, which provides that unvested share-based payment awards containing nonforfeitable rights to dividends or dividend equivalents are participating securities and should be included in the computation of earnings per share pursuant to the two-class method. The Company determined that its unvested RRP awards are participating securities. Accordingly, effective October 1, 2009, earnings per common share is computed using the two-class method prescribed under ASC 260, and prior periods were adjusted retrospectively to conform with the provisions of this guidance. Earnings per share for the years ended September 30, 2009, 2008 or 2007, or any of the related interim periods, did not change due to the retrospective application of ASC 260.

3. Earnings Per Share ("EPS")

The Company accounts for the 3,024,574 shares acquired by its ESOP and the shares awarded pursuant to its RRP in accordance with ASC 260, which requires that our unvested RRP awards that contain nonforfeitable rights to dividends be treated as participating securities in the computation of EPS pursuant to the two-class method. The two-class method is an earnings allocation that determines EPS for each class of common stock and participating security. Shares acquired by the ESOP are not considered in the basic average shares outstanding until the shares are committed for allocation or vested to an employee's individual account. The following table is a computation of our basic and diluted EPS under the two-class method for the periods indicated.

	For the Three Months Ended December 31,	
	2009	2008
	(in thousands, except share and per share data)	
Net income	$20,980	$15,852
Less: income allocable to unvested RRP awards	(4)	(5)
Net income available to common stockholders	$20,976	$15,847
Average common shares outstanding	73,266,128	73,062,337
Average unvested RRP shares outstanding	14,328	22,428
Average committed ESOP shares outstanding	548	548
Total basic average common shares outstanding	73,281,004	73,085,313
Effect of dilutive stock options	5,833	90,443
Total diluted average common shares outstanding	73,286,837	73,175,756
Net EPS:		
Basic	$0.29	$0.22
Diluted	$0.29	$0.22
Antidilutive stock options, excluded from the diluted average common shares outstanding calculation	241,350	25,500

4. Fair Value of Financial Instruments

Fair Value Measurements - ASC 820, Fair Value Measurements and Disclosures, defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The Company uses fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. The Company did not have any liabilities that were measured at fair value at December 31, 2009. The Company's AFS securities 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 or liabilities on a non-recurring basis, such as REO and impaired loans. These non-recurring fair value adjustments involve the application of lower-of-cost-or-fair value accounting or write-downs of individual assets.

In accordance with ASC 820, 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 or liability. Valuation techniques include the use of option pricing models, discounted cash flow models, and similar techniques. The results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset or liability.

The Company bases its fair values on the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. As required by ASC 820, the Company maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value.

The following is a description of valuation methodologies used for assets measured at fair value on a recurring basis.

AFS Securities
The Company's AFS securities portfolio is carried at estimated fair value, with any unrealized gains and losses, net of taxes, reported as accumulated other comprehensive income/loss in stockholders' equity. The Company's major security types based on the nature and risks of the securities are included in the table below. The majority of the securities within the AFS portfolio are issued by U.S. government sponsored enterprises. The fair values for all AFS securities are based on quoted prices for similar securities. Various modeling techniques are used to determine pricing for the Company's securities, including option pricing and discounted cash flow models. The inputs to these models may include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, benchmark securities, bids, offers and reference data. There are some AFS securities in the AFS portfolio that have significant unobservable inputs requiring the independent pricing services to use some judgment in pricing the related securities. These AFS securities are classified as Level 3. All other AFS securities are classified as Level 2.

The following table provides the level of valuation assumption used to determine the carrying value of the Company's assets measured at fair value on a recurring basis, which consists of AFS securities, at December 31, 2009.

	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3) (1)

	(Dollars in thousands)							
U.S. government-sponsored enterprises	$	228,840	$	--	$	228,840	$	--
Municipal bonds		2,753		--		2,753		--
Trust preferred securities		2,408		--		--		2,408
MBS		1,305,096		--		1,305,096		--
	$	1,539,097	$	--	$	1,536,689	$	2,408

(1) The Company's Level 3 AFS securities were not significant at December 31, 2009 and had no material activity during the period ended December 31, 2009.

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The following is a description of valuation methodologies used for significant assets measured at fair value on a non-recurring basis.

Loans Receivable
Loans which meet certain criteria are evaluated individually for impairment. A loan is considered impaired when, based upon current information and events, it is probable the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the loan agreement. Impaired loans at December 31, 2009 were $47.4 million. Substantially all of the Bank's impaired loans at December 31, 2009 are secured by residential real estate. These impaired loans are individually assessed to ensure that the carrying value of the loan is not in excess of the fair value of the collateral, less estimated selling costs. Fair value is estimated through current appraisals, real estate brokers or listing prices. Fair values may be adjusted by management to reflect current economic and market conditions and, as such, are classified as Level 3. Based on this evaluation, the Company maintained an ALLL of $4.0 million at December 31, 2009 for such impaired loans.

REO
REO represents real estate acquired as a result of foreclosure or by deed in lieu of foreclosure and is carried at the lower of cost or fair value less estimated selling costs. Fair value is estimated through current appraisals, real estate brokers or listing prices. As these properties are actively marketed, estimated fair values may be adjusted by management to reflect current economic and market conditions and, as such, are classified as Level 3. REO at December 31, 2009 was $6.6 million. During the three months ended December 31, 2009, charge-offs to the ALLL related to loans that were transferred to REO were $437 thousand. Write downs related to REO that were charged to other expense were $173 thousand for the three months ended December 31, 2009.

The following table provides the level of valuation assumption used to determine the carrying value of the Company's assets measured at fair value on a non-recurring basis at December 31, 2009.

	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(Dollars in thousands)		
Impaired loans	$ 47,427	$ --	$ --	$ 47,427
REO	6,637	--	--	6,637
	$ 54,064	$ --	$ --	$ 54,064

Fair Value Disclosures
The Company determined estimated fair value amounts using available market information and a selection from a variety of valuation methodologies. However, considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented are not necessarily indicative of the amount the Company could realize in a current market exchange. The use of different market assumptions and estimation methodologies may have a material effect on the estimated fair value amounts. The fair value estimates presented herein are based on pertinent information available to management as of December 31, 2009 and September 30, 2009. 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 those dates.

The estimated fair values of the Company's financial instruments as of December 31, 2009 and September 30, 2009 are as follows.

	At December 31, 2009		At September 30, 2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(Dollars in thousands)			
Financial assets:				
Cash and cash equivalents	$105,128	$105,128	$41,154	$41,154
Investment securities:				
AFS	234,001	234,001	234,784	234,784
HTM	417,942	419,352	245,920	248,929
MBS:				
AFS	1,305,096	1,305,096	1,389,211	1,389,211
HTM	572,873	594,365	603,256	627,829
Loans receivable	5,423,923	5,589,283	5,603,965	5,801,724
BOLI	53,777	53,777	53,509	53,509
Capital stock of FHLB	134,064	134,064	133,064	133,064
Financial liabilities:				
Deposits	4,227,252	4,282,549	4,228,609	4,294,454
Advances from FHLB	2,394,214	2,528,034	2,392,570	2,554,206
Other borrowings	713,609	738,653	713,609	742,301

The following methods and assumptions were used to estimate the fair value of the financial instruments:

Cash and Cash Equivalents - The carrying amounts of cash and cash equivalents are considered to approximate their fair value due to the nature of the financial asset.

Investment Securities and MBS - Estimated fair values of securities are based on one of three methods: 1) quoted market prices where available, 2) quoted market prices for similar instruments if quoted market prices are not available, 3) unobservable data that represents the Bank's assumptions about items that market participants would consider in determining fair value where no market data is available. AFS securities are carried at estimated fair value. HTM securities are carried at amortized cost.

Loans Receivable - Fair values are estimated for portfolios with similar financial characteristics. Loans are segregated by type, such as one- to four-family residential mortgages, multi-family residential mortgages, nonresidential and installment loans. Each loan category is further segmented into fixed and adjustable interest rate categories. Market pricing sources are used to approximate the estimated fair value of fixed and adjustable-rate one- to four-family residential mortgages. For all other loan categories, future cash flows are discounted using the LIBOR curve plus a margin at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturity.

BOLI - The carrying value of BOLI is considered to approximate its fair value due to the nature of the financial asset.

Capital Stock of FHLB - The carrying value of FHLB stock equals cost. The fair value is based on redemption at par value.

Deposits - The estimated fair value of demand deposits, savings and money market accounts is the amount payable on demand at the reporting date. The estimated fair value of fixed-maturity certificates of deposit is estimated by discounting the future cash flows using a margin to the LIBOR curve.

Advances from FHLB - The estimated fair value of advances from FHLB is determined by discounting the future cash flows of each advance using a margin to the LIBOR curve.

Other Borrowings - Other borrowings consists of repurchase agreements and Junior Subordinated Deferrable Interest Debentures ("the debentures"). The estimated fair value of the repurchase agreements is determined by discounting the future cash flows of each agreement using a margin to the LIBOR curve. The debentures have a variable rate structure, with the ability to redeem at par; therefore, the carrying value of the debentures approximates their estimated fair value.

5. Securities

The following tables reflect the amortized cost, estimated fair value, and gross unrealized gains and losses of AFS and HTM securities at December 31, 2009 and September 30, 2009. The majority of the security portfolio is composed of securities issued by U.S. government-sponsored enterprises.

	December 31, 2009			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(Dollars in thousands)			
AFS:				
U.S. government-sponsored enterprises	$228,075	$766	$1	$228,840
Municipal bonds	2,663	103	13	2,753
Trust preferred securities	3,762	--	1,354	2,408
MBS	1,254,958	50,339	201	1,305,096
	1,489,458	51,208	1,569	1,539,097
HTM:				
U.S. government-sponsored enterprises	348,623	245	628	348,240
Municipal bonds	69,319	1,893	100	71,112
MBS	572,873	21,628	136	594,365
	990,815	23,766	864	1,013,717
	$2,480,273	$74,974	$2,433	$2,552,814

	September 30, 2009			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(Dollars in thousands)			
AFS:				
U.S. government-sponsored enterprises	$228,743	$1,132	$--	$229,875
Municipal bonds	2,668	131	--	2,799
Trust preferred securities	3,774	--	1,664	2,110
MBS	1,334,357	55,552	698	1,389,211
	1,569,542	56,815	2,362	1,623,995
HTM:				

U.S. government-sponsored enterprises	175,394	535	--	175,929
Municipal bonds	70,526	2,514	40	73,000
MBS	603,256	24,645	72	627,829
	849,176	27,694	112	876,758
	$2,418,718	$84,509	$2,474	$2,500,753

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The following table presents the taxable and non-taxable components of interest income on investment securities for the three months ended December 31, 2009 and 2008:

	For the Three Months Ended December 31,	
	2009	2008
	(Dollars in thousands)	
Taxable	$ 2,024	$ 841
Non-taxable	535	485
	$ 2,559	$ 1,326

The following tables summarize the estimated fair value and gross unrealized losses of those securities on which an unrealized loss at December 31, 2009 and September 30, 2009 was reported and the continuous unrealized loss position for the twelve months prior to December 31, 2009 and September 30, 2009 or for a shorter period of time, as applicable.

	December 31, 2009					
		Less Than 12 Months			Equal to or Greater Than 12 Months	
	Count	Estimated Fair Value	Unrealized Losses	Count	Estimated Fair Value	Unrealized Losses
AFS:			(Dollars in thousands)			
U.S. government-sponsored enterprises	1	$25,025	$1	--	$--	$--
Municipal bonds	1	412	13	--	--	--
Trust preferred securities	--	--	--	1	2,408	1,354
MBS	44	87,014	181	11	2,063	20
	46	$112,451	$195	12	$4,471	$1,374
HTM:						
U.S. government-sponsored enterprises	4	$97,495	$627	--	$--	$--
Municipal bonds	8	3,336	36	2	1,316	65
MBS	5	28,943	135	1	54	1
	17	$129,774	$798	3	$1,370	$66

	September 30, 2009					
		Less Than 12 Months			Equal to or Greater Than 12 Months	
	Count	Estimated Fair Value	Unrealized Losses	Count	Estimated Fair Value	Unrealized Losses
AFS:			(Dollars in thousands)			
Trust preferred securities	--	$--	$--	1	$2,110	$1,664
MBS	16	57,157	600	37	15,804	98
	16	$57,157	$600	38	$17,914	$1,762
HTM:						
Municipal bonds	4	$1,930	$36	1	$495	$4
MBS	3	5,563	26	4	11,043	46
	7	$7,493	$62	5	$11,538	$50

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On a quarterly basis, management conducts a formal review of securities for the presence of an other-than-temporary impairment ("OTTI"). Management assesses whether an OTTI is present when the fair value of a security is less than its amortized cost basis at the balance sheet date. For such securities, OTTI is considered to have occurred if the Company intends to sell the security, if it is more likely than not the Company will be required to sell the security before recovery of its amortized cost basis, or if the present values of expected cash flows is not sufficient to recover the entire amortized cost.

The unrealized losses are primarily a result of increases in market yields from the time of purchase. In general, as market yields rise, the fair value of securities will decrease; as market yields fall, the fair value of securities will increase. Management generally views changes in fair value caused by changes in interest rates as temporary; therefore, these securities have not been classified as other-than-temporarily impaired. Additionally, the impairment is also considered temporary because scheduled coupon payments have been made, it is anticipated that the entire principal balance will be collected as scheduled, and management neither intends to sell the securities and it is not more likely than not that the Company will be required to sell the securities before the recovery of the remaining amortized cost amount.

The amortized cost and estimated fair value of securities by remaining contractual maturity without consideration for call features or pre-refunding dates as of December 31, 2009 are shown below. Actual maturities of MBS may differ from contractual maturities because borrowers have the right to prepay obligations, generally without penalty. Maturities of MBS depend on the repayment characteristics and experience of the underlying financial instruments. Issuers of certain investment securities have the right to call and prepay obligations with or without prepayment penalties. As of December 31, 2009, the amortized cost of the securities in our portfolio which are callable or have pre-refunding dates within one year totaled $534.2 million.

	AFS		HTM	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
	(Dollars in thousands)			
One year or less	$ 25,740	$ 25,999	$ 1,506	$ 1,536
One year through five years	202,918	203,434	367,861	368,044
Five years through ten years	105,593	111,744	353,048	367,809
Ten years and thereafter	1,155,207	1,197,920	268,400	276,328
	$ 1,489,458	$ 1,539,097	$ 990,815	$ 1,013,717

As of December 31, 2009 and September 30, 2009, the Bank has pledged AFS and HTM MBS with an amortized cost of $734.3 million and $764.4 million, respectively, and an estimated fair value of $765.3 million and $797.0 million, respectively, as collateral for repurchase agreements. The securities pledged as collateral for the repurchase agreements can be repledged by the counterparties. As of December 31, 2009 and September 30, 2009, the Bank also had pledged AFS and HTM MBS with an amortized cost of $198.6 million and $193.6 million, respectively, and an estimated fair value of $207.3 million and $202.8 million, respectively, as collateral for public unit depositors, and discount window borrowings and treasury, tax, and loan requirements at the Federal Reserve Bank.

During the quarter, the Bank swapped $194.8 million of originated fixed-rate mortgage loans with the Federal Home Loan Mortgage Corporation ("FHLMC") for MBS ("loan swap transaction"). The MBS received in the loan swap transaction were classified as trading securities prior to the sale. Proceeds from the sale of these securities were $199.1 million, resulting in a gross realized gain of $6.5 million. The gain is included in gains on securities and loans receivable, net in the consolidated statements of income for the quarter.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The Company and its wholly-owned subsidiary, the Bank, may from time to time make written or oral "forward-looking statements," including statements contained in documents filed or furnished by the Company with the SEC. These forward-looking statements may be included in this Quarterly Report on Form 10-Q and the exhibits attached to it, in the Company's reports to stockholders, and in other communications by the Company, which are made in good faith by us pursuant to the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements include statements about our beliefs, plans, objectives, goals, expectations, anticipations, estimates and intentions, that are subject to significant risks and uncertainties, and are subject to change based on various factors, some of which are beyond our control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan" and similar expressions are intended to identify forward-looking statements. The following factors, among others, could cause our future results to differ materially from the plans, objectives, goals, expectations, anticipations, estimates and intentions expressed in the forward-looking statements:

- our ability to continue to maintain overhead costs at reasonable levels;
- our ability to continue to originate a significant volume of one- to four-family mortgage loans in our market area;
- our ability to acquire funds from or invest funds in wholesale or secondary markets;
- the future earnings and capital levels of the Bank and the continued waiver by its primary regulator, the Office of Thrift Supervision (the "OTS"), to distribute capital from the Bank to the Company, which could affect the ability of the Company to pay dividends in accordance with its dividend policies;
- fluctuations in deposit flows, loan demand, and/or real estate values, as well as unemployment levels, which may adversely affect our business;
- the credit risks of lending and investing activities, including changes in the level and direction of loan delinquencies and write-offs and changes in estimates of the adequacy of the ALLL;
- results of examinations of the Bank by the OTS, including the possibility that the OTS may, among other things, require the Bank to increase its ALLL;
- the strength of the U.S. economy in general and the strength of the local economies in which we conduct operations;
- the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System;
- the effects of, and changes in, foreign and military policies of the United States Government;
- inflation, interest rate, market and monetary fluctuations;
- our ability to access cost-effective funding;
- the timely development of and acceptance of our new products and services and the perceived overall value of these products and services by users, including the features, pricing and quality compared to competitors' products and services;
- the willingness of users to substitute competitors' products and services for our products and services;
- our success in gaining regulatory approval of our products and services and branching locations, when required;
- the impact of changes in financial services laws and regulations, including laws concerning taxes, banking securities and insurance and the impact of other governmental initiatives affecting the financial services industry;
- implementing business initiatives may be more difficult or expensive than anticipated;
- technological changes;
- acquisitions and dispositions;
- changes in consumer spending and saving habits; and
- our success at managing the risks involved in our business

This list of important factors is not all inclusive. We do not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company or the Bank.

As used in this Form 10-Q, unless we specify otherwise, “the Company,” “we,” “us,” and “our” refer to Capitol Federal Financial, a United States corporation. “Capitol Federal Savings,” and “the Bank,” refer to Capitol Federal Savings Bank, a federal savings bank and the wholly-owned subsidiary of Capitol Federal Financial. “MHC” refers to Capitol Federal Savings Bank MHC, a mutual holding company and majority-owner of Capitol Federal Financial.

The following discussion and analysis is intended to assist in understanding the financial condition and results of operations of the Company. It should be read in conjunction with the consolidated financial statements and notes presented in this report. The discussion includes comments relating to the Bank, since the Bank is wholly-owned by the Company and comprises the majority of its assets and is the principal source of income for the Company. This discussion and analysis should be read in conjunction with the management discussion and analysis included in the Company's 2009 Annual Report on Form 10-K filed with the SEC.

Executive Summary

The following summary should be read in conjunction with our Management's Discussion and Analysis of Financial Condition and Results of Operations in its entirety.

Our principal business consists of attracting deposits from the general public and investing those funds primarily in permanent loans secured by first mortgages on owner-occupied, one- to four-family residences. We also originate consumer loans, loans secured by first mortgages on non-owner-occupied one- to four-family residences, construction loans secured by one- to four-family residences, commercial real estate loans, and multi-family real estate loans. While our primary business is the origination of one- to four-family loans funded through retail deposits, we also purchase whole loans and invest in certain investment securities and MBS, and use FHLB advances, repurchase agreements and other borrowings as additional funding sources.

The Company is significantly affected by prevailing economic conditions including federal monetary and fiscal policies and federal regulation of financial institutions. Deposit balances are influenced by a number of factors, including interest rates paid on competing personal investment products, the level of personal income, and the personal rate of savings within our market areas. Lending activities are influenced by the demand for housing and other loans, changing loan underwriting guidelines, as well as interest rate pricing competition from other lending institutions. The primary sources of funds for lending activities include deposits, loan repayments, investment income, borrowings, and funds provided from operations.

The Company's results of operations are primarily dependent on net interest income, which is the difference between the interest earned on loans, MBS, investment securities and cash, and the interest paid on deposits and borrowings. On a weekly basis, management reviews deposit flows, loan demand, cash levels, and changes in several market rates to assess all pricing strategies. We generally price our loan and deposit products based upon an analysis of our competition and changes in market rates. The Bank generally prices its first mortgage loan products based on secondary market and competitor pricing. Generally, deposit pricing is based upon a survey of competitors in the Bank's market areas, and the need to attract funding and retain maturing deposits. The majority of our loans are fixed-rate products with maturities up to 30 years, while the majority of our deposits have maturity or reprice dates of less than two years.

During the first quarter of fiscal year 2010, the economy began to show signs of recovery, as evidenced by an increase in consumer spending and stabilization of the labor market, the housing sector, and financial markets. However, unemployment levels remained elevated, housing prices remained depressed and demand for housing was weak, due to distressed sales and tightened lending standards. In an effort to support mortgage lending and housing market recovery, and to help improve credit conditions overall, the Federal Open Market Committee of the Federal Reserve maintained the overnight lending rate between zero and 25 basis points during the first quarter of fiscal year 2010. The Federal Reserve has announced its intention to purchase up to $1.25 trillion of agency MBS by March 2010.

The Company recognized net income of $21.0 million for the quarter ended December 31, 2009, compared to net income of $15.9 million for the quarter ended December 31, 2008. The $5.1 million increase in net income between the periods was primarily due to a decrease of $10.1 million in interest expense and an increase of $6.5 million in other income, partially offset by a $6.4 million decrease in interest and dividend income, a $2.6 million increase in the provision for loan losses, and a $1.8 million increase in income taxes due to higher earnings. The decrease in interest expense was due to a decrease in the rate on our FHLB advances due to the refinance of $875.0 million of advances during the second and third quarters of fiscal year 2009 and a decrease in interest expense on deposits due to the continued decline in the cost of our certificate of deposit and money market portfolios as a result of lower short-term market rates. The $6.5 million increase in other income was primarily due to the gain on the sale of trading securities received in conjunction with a loan swap transaction during the current quarter. The decrease in interest and dividend income was primarily a result of a decrease in the average yield of the MBS and loans receivable portfolios due to prepayments of MBS and mortgage loans with higher yields than the average portfolio yield, to adjustable-rate MBS and mortgage loans adjusting to lower market rates on their reprice dates, refinances and modifications of mortgage loans, and the origination of new mortgage loans at rates lower than the overall portfolio rate. The $2.6 million increase in the provision for loan losses primarily reflects increases in the level of certain qualitative factors in our general valuation allowance model to account for lingering negative economic conditions.

During the quarter, the Bank swapped $194.8 million of originated fixed-rate mortgage loans with FHLMC for trading MBS. The trading MBS were sold at a gain of $6.5 million and the proceeds were reinvested into assets with an average life shorter than that of the Bank's remaining assets in an effort to reduce future interest rate risk sensitivity that could occur as a result of the high volume of refinances and modifications and likely increases in interest rates. Since December 2008, mortgage interest rates have been historically low, prompting increased demand for refinances, and loan modifications.

The Bank has opened two new branches in our Kansas City market area since the beginning of fiscal year 2010, and will open a new branch in the Wichita market area in the second quarter of 2010. The Bank continues to consider expansion opportunities in all its market areas.

Available Information

Financial and other Company information, including press releases, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and all amendments to those reports can be obtained free of charge from our investor relations website, http://ir.capfed.com. SEC filings are available on our website immediately after they are electronically filed with or furnished to the SEC, and are also available on the SEC's website at www.sec.gov.

Critical Accounting Policies

Our most critical accounting policies are the methodologies used to determine the ALLL, other-than-temporary declines in the value of securities and fair value measurements. These policies are important to the presentation of our financial condition and results of operations, involve a high degree of complexity, and require management to make difficult and subjective judgments that may require assumptions or estimates about highly uncertain matters. The use of different judgments, assumptions, and estimates could cause reported results to differ materially. These critical accounting policies and their application are reviewed at least annually by our audit committee. The following is a description of our critical accounting policies and an explanation of the methods and assumptions underlying their application.

Allowance for Loan Losses. Management maintains an ALLL to absorb known and inherent losses in the loan portfolio based upon ongoing quarterly assessments of the loan portfolio. Our methodology for assessing the appropriateness of the ALLL consists of a formula analysis for general valuation allowances and specific valuation allowances for identified problem and impaired loans. The ALLL is maintained through provisions for loan losses which are charged to income. The methodology for determining the ALLL is considered a critical accounting policy by management because of the high degree of judgment involved, the subjectivity of the assumptions used, and the potential for changes in the economic environment that could result in changes to the amount of the recorded ALLL.

Our primary lending emphasis is the origination and purchase of one- to four-family mortgage loans on residential properties, and, to a lesser extent, home equity and second mortgages on one- to four-family residential properties resulting in a loan concentration in residential first mortgage loans. As a result of our lending practices, we also have a concentration of loans secured by real property located primarily in Kansas and Missouri. At December 31, 2009, approximately 70% and approximately 15% of the Bank's loans were secured by real property located in Kansas and Missouri, respectively. Based on the composition of our loan portfolio, we believe the primary risks inherent in our portfolio are the continued weakened economic conditions due to the recent U.S. recession, continued high levels of unemployment or underemployment, the potential for rising mortgage interest rates in the markets we lend and a continuing decline in real estate values. Any one or a combination of these events may adversely affect borrowers' ability to repay their loans, resulting in increased delinquencies, non-performing assets, loan losses and future levels of loan loss provisions. Although management believes that the Bank has established and maintained the ALLL at appropriate levels, additions may be necessary if future economic and other conditions differ substantially from the current operating environment.

Management considers quantitative and qualitative factors when determining the appropriateness of the ALLL. Such factors include changes in underwriting standards, the trend and composition of delinquent and non-performing loans, results of foreclosed property and short sale transactions, historical charge-offs, the current status and trends of local and national economies; specifically levels of unemployment, changes in mortgage interest rates, and loan portfolio growth and concentrations. Since our loan portfolio is primarily concentrated in one- to four-family real estate, we monitor one- to four-family real estate market value trends in our local market areas and geographic sections of the U.S. by reference to various industry and market reports, economic releases and surveys, and our general and specific knowledge of the real estate markets in which we lend, in order to determine what impact, if any, such trends may have on the level of our ALLL. We also use ratio analyses as a supplemental tool for evaluating the overall reasonableness of the ALLL. We consider the observed trends in the ratios, taking into consideration the composition of our loan portfolio compared to our peers, in combination with our historical loss experience. We also review the actual performance and charge-off history of our portfolio and compare that to our previously determined allowance coverage percentages and specific valuation allowances. In addition, the OTS reviews the adequacy of the Company’s ALLL during its examination process. We consider any comments from the OTS when assessing the appropriateness of our ALLL. Reviewing these quantitative and qualitative factors assists management in evaluating the overall reasonableness of the ALLL and whether changes need to be made to our assumptions. Our ALLL methodology is applied in a consistent manner; however, the methodology can be modified in response to changing conditions.

Each quarter, the loan portfolio is segregated into categories in the formula analysis based on certain risk characteristics such as loan type (one- to four-family, multi-family, etc.), interest payments (fixed-rate, adjustable-rate), loan source (originated or purchased), loan-to-value ratios, borrower’s credit score and payment status (i.e. current or number of days delinquent). Consumer loans, such as second mortgages and home equity lines of credit, with the same underlying collateral as a one- to four-family loan are combined with the one- to four-family loan in the formula analysis to calculate a combined loan-to-value ratio. Loss factors are assigned to each category in the formula analysis based on management’s assessment of the potential risk inherent in each category. The greater the risks associated with a particular category, the higher the loss factor. Loss factors increase as individual loans become classified or delinquent, the foreclosure process begins or as economic and market conditions and trends warrant. All loans that are not impaired are included in a formula analysis. Impaired loans are defined as non-accrual loans and troubled debt restructurings (“TDRs”) that have not been performing under the restructured terms for 12 consecutive months.

The loss factors applied in the formula analysis are reviewed quarterly by management to assess whether the factors adequately cover probable and estimable losses inherent in the loan portfolio. The review considers such qualitative and quantitative factors as the trends and composition of delinquent and non-performing loans, the results of foreclosed property and short sale transactions, and the status and trends of the local and national economies and housing markets. Our ALLL methodology permits modifications to any loss factor used in the computation of the formula analysis in the event that, in management’s judgment, significant factors which affect the collectibility of the portfolio or any category of the loan portfolio, as of the evaluation date, are not reflected in the current loss factors. Management’s evaluation of the qualitative factors with respect to these conditions is subject to a higher degree of uncertainty because they are not identified with a specific problem loan or portfolio segments. During the current quarter, management increased the level of certain qualitative factors in our formula analysis to account for lingering negative economic conditions.

Specific valuation allowances are established in connection with individual loan reviews of specifically identified problem and impaired loans. Since the majority of our loan portfolio is composed of one- to four-family real estate, determining the estimated fair value of the underlying collateral is critical in evaluating the amount of specific valuations required for problem and impaired loans. Estimated fair value of the underlying collateral is based on current appraisals, real estate broker values or listing prices. It sometimes takes several months for a loan to work through the foreclosure process. For purchased loans, the estimated fair values received from servicers when a loan becomes 90 days delinquent is not always an accurate representation of the fair value once the collateral has been sold, due to the continued decline in real estate values between the two points in time. To account for the declines in fair value on purchased loans, management applies a market value adjustment to non-performing purchased loans to more accurately estimate the fair values of the underlying collateral. The adjustments are determined based on the geographic location of the underlying collateral, recent losses recognized on foreclosed property and short sale transactions and trends of non-performing purchased loans entering foreclosure in the various geographic areas. Specific valuation allowances are established if the adjusted estimated fair value, less estimated selling costs, is less than the current loan balance.

Loans with an outstanding balance of $1.5 million or more are individually reviewed annually if secured by property in one of the following categories: multi-family (five or more units) property, unimproved land, other improved commercial property, acquisition and development of land projects, developed building lots, office building, single-use building, or retail building. Specific valuation allowances are established if the individual loan review determines a quantifiable impairment.

Securities Impairment. Management monitors the securities portfolio for OTTI on an ongoing basis and performs a formal review quarterly. The process involves monitoring market events and other items that could impact issuers' ability to perform. The evaluation includes, but is not limited to such factors as: the nature of the investment, the length of time the security has had a fair value less than the amortized cost basis, the cause(s) and severity of the loss, expectation of an anticipated recovery period, recent events specific to the issuer or industry including the issuer's financial condition and the current ability to make future payments in a timely manner, external credit ratings and recent downgrades in such ratings, the Company's intent to sell and whether it is more likely than not the Company would be required to sell prior to recovery for debt securities.

Management determines whether OTTI losses should be recognized for impaired securities by assessing all known facts and circumstances surrounding the securities. If the Company intends to sell an impaired security or if it is more likely than not that the Company will be required to sell an impaired security before recovery of its amortized cost basis, an OTTI will be recognized and the difference between amortized cost and fair value will be recognized as a loss in earnings. At December 31, 2009, no securities had been identified as other-than-temporarily impaired.

Fair Value Measurements. The Company uses fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures, per the provisions of ASC 820, Fair Value Measurements and Disclosures. The Company's AFS securities are recorded at fair value on a recurring basis. Changes in the fair value of AFS securities are recorded, net of tax, in accumulated other comprehensive income, which is a component of stockholders' equity. The Company did not have any liabilities that were measured at fair value at December 31, 2009. Additionally, from time to time, the Company may be required to record at fair value other assets or liabilities on a non-recurring basis, such as REO and impaired loans. These non-recurring fair value adjustments involve the application of lower-of-cost-or-fair value accounting or write-downs of individual assets.

In accordance with ASC 820, 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 underlying assumptions used to determine fair value, with Level 1 (quoted prices for identical assets in an active market) being considered the most reliable, and Level 3 having the most unobservable inputs and therefore being considered the least reliable. The Company bases its fair values on the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. As required by ASC 820, the Company maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value.

Financial Condition

Total assets and total liabilities both decreased slightly from September 30, 2009 to December 31, 2009. Management may continue to maintain interest-earning assets at current levels or below until market conditions provide profitable growth opportunities that are consistent with interest rate risk management policies.

The following table presents selected balance sheet data for the Company at the dates indicated.

	Balance at				
	December 31, 2009	September 30, 2009	June 30, 2009	March 31, 2009	December 31, 2008
	(Dollars in thousands, except per share amounts)				
Total assets	$8,374,762	$8,403,680	$8,319,292	$8,269,881	$8,157,324
Cash and cash equivalents	105,128	41,154	74,101	52,025	143,134
Investment securities	651,943	480,704	322,166	214,410	105,965
MBS	1,877,969	1,992,467	2,100,998	2,204,369	2,176,302
Loans receivable, net	5,423,923	5,603,965	5,541,731	5,377,699	5,456,569
Capital stock of FHLB	134,064	133,064	132,071	131,278	131,230
Deposits	4,227,252	4,228,609	4,175,251	4,116,514	3,867,304
Advances from FHLB	2,394,214	2,392,570	2,410,949	2,411,560	2,596,964
Other borrowings	713,609	713,609	713,609	713,609	713,595
Stockholders' equity	941,999	941,298	922,634	916,391	897,435
Accumulated other comprehensive income	30,875	33,870	23,512	24,622	14,263
Equity to total assets at end of period	11.2 %	11.2 %	11.1 %	11.1 %	11.0 %
Book value per share	12.86	12.85	12.60	12.52	12.27
Bank tangible equity ratio (1)	10.1 %	10.0 %	9.8 %	9.9 %	10.0 %

(1) See tangible equity to GAAP equity reconciliation in “Liquidity and Capital Resources – Regulatory Capital.”

Loans Receivable. The loans receivable portfolio decreased $180.0 million from $5.60 billion at September 30, 2009 to $5.42 billion at December 31, 2009. The decrease in the portfolio was a result of the loan swap transaction that took place during the quarter, where $194.8 million of originated fixed-rate mortgage loans were swapped for MBS as a means of reducing future interest rate risk sensitivity. The Bank will continue to service these loans. The MBS were classified as trading securities and sold during the current quarter for a gain. The proceeds from the sale were primarily reinvested into investment securities with terms shorter than that of the loans swapped.

The Bank purchased $37.6 million of loans from nationwide lenders during the quarter, the majority of which were adjustable-rate. These loans had an average credit score of 725 and a weighted average LTV ratio of 46% at the time of purchase. At December 31, 2009, loans purchased from nationwide lenders represented 13% of our loan portfolio and were secured by properties located in 47 of the continental United States and Washington, D.C. As of December 31, 2009, the average balance of a purchased nationwide mortgage loan was approximately $350 thousand, the average balance of a purchased correspondent loan was approximately $250 thousand, and the average balance of an originated mortgage loan was approximately $125 thousand. By purchasing loans from nationwide lenders, the Bank is able to attain some geographic diversification in its loan portfolio, and help mitigate the Bank's interest rate risk exposure as the purchased loans are predominately adjustable-rate or 15-year fixed-rate loans. Although at the time these loans were purchased, they met our underwriting standards; as a result of the continued elevated levels of unemployment rates and the declines in real estate values in some of the states where we have purchased loans, we have experienced an increase in non-performing purchased loans. See additional discussion regarding non-performing purchased loans in "Asset Quality – Loans and REO."

Included in the loan portfolio at December 31, 2009 were $243.7 million of interest-only adjustable-rate mortgage ("ARM") loans, the majority of which were purchased from nationwide lenders during fiscal year 2005. These loans do not typically require principal payments during their initial term, and have initial interest-only terms of either five or ten years. The interest-only loans purchased had an average credit score of 737 and an average LTV ratio of 80% or less at the time of purchase. The Bank has not purchased any interest-only ARM loans since 2006 and discontinued offering the product in its local markets during 2008 to reduce future credit risk. At December 31, 2009, $233.3 million, or 96%, of interest-only loans were still in their interest-only payment term. As of December 31, 2009, $110.7 million will begin to amortize principal within two years, $16.4 million will begin to amortize principal within two-to-five years, $89.7 million will begin to amortize principal within five-to-seven years, and the remaining $16.4 million will begin amortizing in seven-to-ten years. At December 31, 2009, $15.7 million or approximately 50% of non-performing loans were interest-only and $2.8 million was reserved in the ALLL for these loans. Non-performing interest-only loans represent approximately 6% of the total interest-only portfolio at December 31, 2009. See additional discussion regarding non-performing loans in "Asset Quality – Loans and REO."

The following table presents loan origination, refinance and purchase activity for the periods indicated. Loan originations, purchases and refinances are reported together. The fixed-rate one- to four-family loans less than or equal to 15 years have an original maturity at origination of less than or equal to 15 years, while fixed-rate one- to four-family loans greater than 15 years have an original maturity at origination of greater than 15 years. The adjustable-rate one- to four-family loans less than or equal to 36 months have a term to first reset of less than or equal to 36 months at origination and adjustable-rate one- to four-family loans greater than 36 months have a term to first reset of greater than 36 months at origination.

	For the Three Months Ended December 31, 2009			For the Three Months Ended December 31, 2008		
	Amount	Rate	% of Total	Amount	Rate	% of Total
	(Dollars in thousands)					
Fixed-Rate:						
One- to four-family						
<= 15 years	$56,955	4.60 %	21.9 %	$28,017	5.47 %	9.0 %
> 15 years	117,783	5.10	45.4	107,145	5.79	34.4
Other real estate	--	--	--	5,965	5.88	1.9
Home Equity	1,500	7.45	0.6	2,851	7.45	0.9
Other	418	8.86	0.2	433	8.52	0.1
Total fixed-rate	176,656	4.97	68.1	144,411	5.77	46.3
Adjustable-Rate:						
One- to four-family						
<= 36 months	32,945	3.34	12.7	88,076	5.00	28.2
> 36 months	26,870	4.36	10.3	55,922	5.32	17.9
Other real estate	--	--	--	--	--	--
Home Equity	21,810	4.86	8.4	22,749	5.08	7.3
Other	1,190	4.73	0.5	754	5.49	0.3
Total adjustable-rate	82,815	4.09	31.9	167,501	5.12	53.7
Total originations, refinances and purchases	$259,471	4.69 %	100.0 %	$311,912	5.42 %	100.0 %
Purchased loans included above:						
Fixed-Rate:						
Correspondent	$17,811	5.09 %		$13,749	5.79 %	
Nationwide	2,338	5.05		256	4.38	
Adjustable-Rate:						
Correspondent	9,697	4.49		6,249	5.76	
Nationwide	35,233	3.47		125,815	5.05	
Total purchased loans	$65,079	4.12 %		$146,069	5.15 %	

Loan modification activity is not included in the tables above because a new loan is not generated at the time of modification. During the three months ended December 31, 2009 and 2008, the Bank modified $139.7 million and $24.8 million loans, respectively, with a weighted average rate decrease of 83 basis points and 3 basis points, respectively.

The Bank generally prices its one- to four-family loan products based upon prices available in the secondary market. During the three months ended December 31, 2009, the average rate offered on the Bank's 30-year fixed-rate one- to four-family loans, with no points paid by the borrower, was approximately 160 basis points above the average

10-year Treasury rate, while the average rate offered on the Bank's 15-year fixed-rate one- to four-family loans were approximately 100 basis points above the average 10-year Treasury rate.

The following table summarizes the activity in the loan portfolio for the periods indicated, excluding changes in loans in process, deferred fees and ALLL. Loans that were paid-off as a result of refinances are included in "repayments." Purchased loans include purchases from correspondent and nationwide lenders. Loan modification activity is not included in the activity in the following table because a new loan is not generated at the time of modification. See modification activity for the three months ended December 31, 2009 on the previous page. The modified balance and rate are included in the ending loan portfolio balance and rate.

	For the Three Months Ended							
	December 31, 2009		September 30, 2009		June 30, 2009		March 31, 2009	
	Amount	Rate	Amount	Rate	Amount	Rate	Amount	Rate
	(Dollars in thousands)							
Beginning balance	$5,646,950	5.29 %	$5,587,130	5.36 %	$5,422,798	5.50 %	$5,506,352	5.63 %
Originations and refinances:								
Fixed	156,507	4.95	255,441	5.07	325,640	4.96	276,888	5.06
Adjustable	37,885	4.57	37,948	4.75	32,652	4.78	25,269	4.83
Purchases:								
Fixed	20,149	5.09	24,670	5.08	37,912	5.11	33,226	5.18
Adjustable	44,930	3.69	11,662	4.82	9,544	5.04	70,349	4.90
Repayments	(245,838)		(266,362)		(322,104)		(311,733)	
Transfer of loans to LHFS (1)	(194,759)		--		81,190		(175,862)	
Other (2)	(2,080)		(3,539)		(502)		(1,691)	
Ending balance	$5,463,744	5.23 %	$5,646,950	5.29 %	$5,587,130	5.36 %	$5,422,798	5.50 %

(1) "Transfer of loans to LHFS" in the December 31, 2009 quarter includes loans with a principal balance of $194.8 million related to the loan swap transaction.

(2) "Other" consists of transfers to REO and modification fees advanced.

The following table presents the Company's loan portfolio at the dates indicated.

	December 31, 2009			September 30, 2009		
	Amount	Average Rate	% of Total	Amount	Average Rate	% of Total
	(Dollars in thousands)					
Real Estate Loans:						
One- to four-family	$5,155,773	5.21 %	94.4 %	$5,321,935	5.26 %	94.2 %
Multi-family and commercial	71,395	6.18	1.3	80,493	6.01	1.4
Construction	33,403	5.15	0.6	39,535	5.20	0.7
Total real estate loans	5,260,571	5.22	96.3	5,441,963	5.27	96.3
Consumer and Other Loans:						
Home equity	193,987	5.60	3.5	195,557	5.63	3.5
Other	9,186	6.00	0.2	9,430	6.11	0.2
Total consumer and other loans	203,173	5.62	3.7	204,987	5.65	3.7
Total loans receivable	5,463,744	5.23 %	100.0 %	5,646,950	5.29 %	100.0 %
Less:						
Undisbursed loan funds	17,089			20,649		
Unearned loan fees and deferred costs	10,525			12,186		
ALLL	12,207			10,150		
Total loans receivable, net	$5,423,923			$5,603,965		

The following table presents the contractual maturity of our loan portfolio at December 31, 2009. Loans which have adjustable or renegotiable interest rates are shown as maturing in the period during which the contract is due. The table does not reflect the effects of possible prepayments or enforcement of due on sale clauses.

	One- to Four-Family		Real Estate Multi-family and Commercial		Construction (2)		Home Equity (3)		Other		Total
	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount	Weighted Average Rate	Amount
	(Dollars in thousands)										
Amounts due:											
Within one year (1)	$2,131	6.00%	$22	7.00%	$17,673	5.18%	$4,024	4.14%	$1,478	5.59%	$25,328
After one year:											
Over one to two	5,117	5.57	--	--	15,730	5.11	1,456	4.64	1,083	8.10	23,386
Over two to three	8,508	5.53	996	5.72	--	--	2,004	5.23	1,092	6.56	12,600
Over three to five	45,562	5.30	34	8.50	--	--	3,580	5.42	5,136	5.36	54,312
Over five to ten	479,433	5.18	6,867	5.87	--	--	32,187	5.11	368	8.62	518,855
Over 10 to 15	856,233	5.00	13,098	6.40	--	--	60,379	4.87	29	6.50	929,739
After 15 years	3,758,789	5.25	50,378	6.17	--	--	90,357	6.37	--	--	3,899,524
Total due after one year	5,153,642	5.21	71,373	6.18	15,730	5.11	189,963	5.64	7,708	6.07	5,438,416
Total loans	$5,155,773	5.21%	$71,395	6.18%	$34,403	5.15%	$193,987	5.60%	$9,186	6.00%	5,463,744
Less:											
Undisbursed loan funds											17,089
Unearned loan fees and deferred costs											10,525
ALLL											12,207
Total loans receivable, net											$5,423,923

(1) Includes demand loans, loans having no stated maturity, and overdraft loans.

(2) Construction loans are presented based upon the term to complete construction.

(3) For home equity loans, the maturity date calculated assumes the customer always makes the required minimum payment. The majority of interest-only home equity lines of credit assume a balloon payment of unpaid principal at 120 months. All other home equity lines of credit generally assume a term of 240 months.

The following table presents, as of December 31, 2009, the amount of loans, net of undisbursed loan funds, due after December 31, 2010, and whether these loans have fixed or adjustable interest rates.

	Fixed	Adjustable	Total
		(Dollars in thousands)	
Real Estate Loans:			
One- to four-family	$ 4,096,494	$ 1,057,148	$ 5,153,642
Multi-family and commercial	68,902	2,471	71,373
Construction	15,185	545	15,730
Consumer and Other Loans:			
Home equity	53,203	136,760	189,963
Other	3,780	3,928	7,708
Total	$ 4,237,564	$ 1,200,852	$ 5,438,416

Asset Quality – Loans and REO

The Bank's traditional underwriting guidelines have provided the Bank with generally low delinquencies and low levels of non-performing assets compared to national levels. Of particular importance is the complete documentation required for each loan the Bank originates and purchases. This allows the Bank to make an informed credit decision based upon a thorough assessment of the borrower's ability to repay the loan compared to underwriting methodologies that do not require full documentation. See additional discussion regarding underwriting standards in "Lending Practices and Underwriting Standards" in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2009.

For one- to four-family loans and home equity loans, when a borrower fails to make a loan payment 15 days after the due date, a late charge is assessed and a notice is mailed. All delinquent balances are reviewed by collection personnel once the loan is 16 or more days past due. Attempts to contact the borrower occur by personal letter and, if no response is received, by telephone, with the purpose of establishing repayment arrangements for the borrower to bring the loan current. Repayment arrangements may be approved by a designated bank officer. Once a loan becomes 90 days delinquent, a demand letter is issued requiring the loan to be brought current or foreclosure procedures will be implemented. Once a loan becomes 120 days delinquent, and an acceptable repayment plan has not been established, the loan is forwarded to legal counsel to initiate foreclosure. We also monitor whether mortgagors who filed for bankruptcy are meeting their obligation to pay the mortgage debt in accordance with the terms of the bankruptcy petition.

We monitor delinquencies on our purchased loan portfolio with reports we receive from the servicers. We monitor these servicer reports to ensure that the servicer is upholding the terms of the servicing agreement. The reports generally provide total principal and interest due and length of delinquency, and are used to prepare monthly management reports and perform delinquent loan trend analysis. Management also utilizes information from the servicers to monitor property valuations and identify the need to record specific valuation allowances. The servicers handle collection efforts per the terms of the servicing agreement. In the event of a foreclosure, the servicer obtains our approval prior to initiating foreclosure proceedings, and handles all aspects of the repossession and disposition of the repossessed property, which is also governed by the terms of the servicing agreement.

The following matrix shows the balance of one-to four-family mortgage loans as of December 31, 2009 cross-referenced by LTV ratio and credit score. The LTV ratios used in the matrix were based on the current loan balance and the most recent bank appraisal available, or the lesser of the purchase price or original appraisal. In most cases, the most recent appraisal was obtained at the time of origination. The LTV ratios based upon appraisals obtained at the time of origination may not necessarily indicate the extent to which we may incur a loss on any given loan that may go into foreclosure as the value of the underlying collateral may have declined since the time of origination. Credit scores were updated in March 2009 for loans originated by the Bank and in September 2009 for purchased loans. Management will continue to update credit scores as deemed necessary based upon economic conditions. Per the matrix, the greatest concentration of loans fall into the "751 and above" credit score category and have a LTV ratio of less than 70%. The loans falling into the "less than 660" credit score category and having LTV ratios of more than 80% comprise the lowest concentration. The average LTV ratio and credit score for our one-to four-family purchased loans at December 31, 2009 was approximately 67% and 758, respectively. The average LTV ratio and credit score for our one-to four-family originated loans at December 31, 2009 was approximately 59% and 742, respectively.

	Credit Score									
	Less than 660		661 to 700		701 to 750		751 and above		Total	
LTV ratio	Amount	% of total	Amount	% of total	Amount	% of total	Amount	% of total	Amount	% of total
	(Dollars in thousands)									
Less than 70%	$121,923	2.4 %	$158,508	3.1 %	$427,621	8.3 %	$1,891,927	36.7 %	$2,599,979	50.5 %
70% to 80%	114,771	2.2	125,766	2.4	406,457	7.9	1,152,435	22.3	1,799,429	34.8
More than 80%	71,345	1.4	77,532	1.5	211,548	4.1	395,940	7.7	756,365	14.7
Total	$308,039	6.0 %	$361,806	7.0 %	$1,045,626	20.3 %	$3,440,302	66.7 %	$5,155,773	100.0%

Delinquent and non-performing loans and REO

The following tables present the Company's 30 to 89 day delinquent loans, non-performing loans, and REO at the dates indicated. Purchased loans include loans purchased from nationwide lenders. Non-performing loans are non-accrual loans that are 90 or more days delinquent or are in the process of foreclosure. Non-performing assets include non-performing loans and REO.

	December 31, 2009		September 30, 2009		June 30, 2009		March 31, 2009		December 31, 2008	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
	(Dollars in thousands)									
30 to 89 days delinquent										
One- to four-family:										
Originated	184	$ 19,468	159	$ 15,488	140	$ 12,981	115	$ 13,459	147	$ 15,089
Purchased	44	11,464	41	10,556	49	13,225	43	9,698	42	9,359
Multi-family and commercial	1	5	--	--	--	--	--	--	--	--
Construction	--	--	--	--	--	--	--	--	--	--
Consumer and Other Loans:										
Home equity	49	1,021	40	708	38	746	33	611	36	496
Other	24	114	15	89	15	98	9	50	16	106
	302	$ 32,072	255	$ 26,841	242	$ 27,050	200	$ 23,818	241	$ 25,050
30 to 89 days delinquent loans as a percentage of total loans		0.59%		0.48%		0.49%		0.44%		0.46%

	December 31, 2009		September 30, 2009		June 30, 2009		March 31, 2009		December 31, 2008	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
	(Dollars in thousands)									
Non-performing loans:										
One- to four-family:										
Originated	104	$10,040	99	$9,248	108	$11,332	96	$9,748	95	$9,231
Purchased	70	21,912	70	21,259	59	17,270	45	12,158	32	9,625
Multi-family and commercial	--	--	--	--	--	--	--	--	--	--
Construction	--	--	--	--	--	--	--	--	--	--
Consumer and Other Loans:										
Home equity	32	516	22	367	29	448	26	407	18	275
Other	6	9	8	45	7	60	6	58	11	101
	212	32,477	199	30,919	203	29,110	173	22,371	156	19,232
Non-performing loans as a percentage of total loans		0.60 %		0.55 %		0.53 %		0.42 %		0.35 %
REO:										
One- to four-family:										
Originated (1)	55	4,726	51	5,702	36	3,950	48	4,119	38	2,833
Purchased	9	1,911	8	1,702	5	1,127	10	1,705	6	1,644
Multi-family and commercial	--	--	--	--	--	--	--	--	--	--
Construction	--	--	--	--	--	--	--	--	--	--
Consumer and Other Loans:										
Home equity	--	--	--	--	--	--	--	--	--	--
Other	--	--	--	--	--	--	--	--	--	--
	64	6,637	59	7,404	41	5,077	58	5,824	44	4,477
Total non-performing assets	276	$39,114	258	$38,323	244	$34,187	231	$28,195	200	$23,709
Non-performing assets as a percentage of total assets		0.47 %		0.46 %		0.41 %		0.34 %		0.29 %

(1) Real estate related consumer loans are included in the one- to four-family category as the underlying collateral is one- to four-family property.

Loans 30 to 89 days delinquent increased $5.3 million from $26.8 million at September 30, 2009 to $32.1 million at December 31, 2009. We believe the increase in the 30 to 89 day delinquent balance during the quarter was due to the continued elevated level of unemployment. The following table presents the average percentage of one-to four-family loans, by principal balance, that entered the 30-89 days delinquent category during the past 12 months that paid off, returned to performing status, stayed 30-89 days delinquent, or progressed to the non-performing or REO categories. Purchased loans include loans purchased from nationwide lenders.

30-89 Day Delinquent Loan Trend Analysis

	Paid Off	Performing	30-89 Days Delinquent	Non-Performing	REO	Total
Originated	5.7 %	38.1 %	34.1 %	18.0 %	4.1 %	100.0 %
Purchased	3.7 %	20.9 %	35.6 %	37.6 %	2.2 %	100.0 %
Total Portfolio Average	4.8 %	30.9 %	35.3 %	25.9 %	3.1 %	100.0 %

Non-performing loans increased $1.6 million from $30.9 million at September 30, 2009 to $32.5 million at December 31, 2009. The balance of non-performing loans continues to remain at historically high levels due to the continued elevated level of unemployment coupled with the decline in real estate values, particularly in some of the states in which we have purchased loans. At December 31, 2009, one-to four-family non-performing loans with LTV ratios greater than 80% comprised approximately 15% of total non-performing loans. Of these loans, 71% have PMI which reduces or eliminates the Bank's exposure to loss. The balance of one-to four-family non-performing loans with LTV ratios greater than 80% with no PMI was $1.4 million at December 31, 2009. At origination, these loans generally had LTV ratios less than 80%, but as a result of updating the appraisals, the LTV ratios are now in excess of 80%.

The following table presents the top twelve states where our one- to four-family mortgages are located, and the corresponding balance of 30-89 day delinquent loans, non-performing loans and the weighted average LTV ratios for non-performing loans at December 31, 2009. The LTV ratios were based on the current loan balance and the most recent appraisal available, or the lesser of the purchase price or original appraisal.

	One- to Four-Family		Loans 30 to 89 Days Delinquent		Non-Performing Loans		
State	Balance	% of Total	Balance	% of Total	Balance	% of Total	Average LTV
			(Dollars in thousands)				
Kansas	$3,717,625	72.1 %	$14,290	46.2 %	$8,442	26.4 %	76 %
Missouri	749,956	14.6	5,177	16.7	1,598	5.0	92
Illinois	78,757	1.5	1,008	3.2	2,129	6.7	67
Texas	51,295	1.0	753	2.4	58	0.2	74
New York	50,282	1.0	875	2.8	846	2.6	75
Florida	48,407	0.9	113	0.4	3,649	11.4	71
Colorado	35,069	0.7	204	0.7	415	1.3	79
Arizona	33,442	0.6	1,227	4.0	4,181	13.1	75
Virginia	31,185	0.6	1,816	5.9	444	1.4	71
Connecticut	31,016	0.6	--	--	151	0.5	68
Minnesota	28,835	0.6	676	2.2	129	0.4	70
New Jersey	27,560	0.5	327	1.1	360	1.1	59
Other states	272,344	5.3	4,466	14.4	9,550	29.9	71

$5,155,773	100.0	%	$30,932	100.0	%	$31,952	100.0	%	74	%

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Impaired loans

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the loan agreement. Impaired loans totaled $47.4 million at December 31, 2009, compared to $41.4 million at September 30, 2009. All TDRs that have not been performing under the new terms for 12 consecutive months and non-accrual loans are considered to be impaired loans.

A TDR is the situation where, due to a borrower's financial difficulties, the Bank grants a concession to the borrower that the Bank would not otherwise have considered. The majority of the Bank's TDRs involve a restructuring of loan terms such as a temporary reduction in the payment amount to require only interest and escrow (if required) and extending the maturity date of the loan. TDRs are not reported as non-performing loans, unless the restructured loans are more than 90 days delinquent. At December 31, 2009, the balance of TDRs included in the impaired loan balance at December 31, 2009 was $15.2 million, of which 93%, or $14.3 million, were originated loans. Of the $15.2 million, $623 thousand was greater than 90 days delinquent and was included in the non-performing loan balance at December 31, 2009. Loans are removed from the TDR classification after 12 consecutive months of satisfactory repayment performance under the new loan terms.

Classified assets

In accordance with our asset classification policy, we regularly review the problem assets in our portfolio to determine whether any assets require classification in accordance with applicable regulations. The following table sets forth the balance of assets, less specific valuation allowances, classified as special mention, substandard, or doubtful at December 31, 2009. Purchased loans and purchased REO represent loans purchased from nationwide lenders.

	Special Mention		Substandard		Doubtful	
	Number	Amount	Number	Amount	Number	Amount
			(Dollars in thousands)			
Real Estate Loans:						
One- to four-family:						
Originated	57	$9,546	131	$15,068	--	$--
Purchased	1	262	70	18,691	--	--
Multi-family and commercial	1	8,167	--	--	--	--
Construction	--	--	--	--	--	--
Consumer and Other Loans:						
Home equity	6	71	38	836	--	--
Other	--	--	8	51	--	--
Total loans	65	18,046	247	34,646	--	--
REO:						
Originated	--	--	55	4,727	--	--
Purchased	--	--	9	1,911	--	--
Total REO	--	--	64	6,638	--	--
Trust preferred securities	--	--	1	2,408	--	--
Total classified assets	65	$18,046	312	$43,692	--	$--

Allowance for loan losses

The following table presents the Company's activity for the ALLL and related ratios at the dates and for the periods indicated. Charge-offs represent losses on loans transferred to REO and losses on short sales. Recoveries represent amounts recovered after a loan has been charged-off. Once a loan enters REO, any future write downs or recoveries are reported in REO operations in other expenses on the consolidated statement of income; therefore, recoveries of charge-offs are rare.

	For the Three Months Ended		
	December 31, 2009	September 30, 2009	December 31, 2008
	(Dollars in thousands)		
Balance at beginning of period	$10,150	$10,242	$5,791
Charge-offs:			
One- to four-family loans--originated	39	169	10
One- to four-family loans--purchased	856	540	182
Multi-family and commercial loans	--	--	--
Construction	--	--	--
Home equity	23	1	--
Other loans	5	5	11
Total charge-offs	923	715	203
Recoveries	--	--	--
Net charge-offs	923	715	203
ALLL on loans in the loan swap transaction	(135)	--	--
Provision for loan losses	3,115	623	549
Balance at end of period	$12,207	$10,150	$6,137
Ratio of net charge-offs during the period to average loans outstanding during the period (1)	0.02 %	0.01 %	-- %
Ratio of net charge-offs during the period to average non-performing assets	2.39 %	1.97 %	0.95 %