MALVERN FEDERAL BANCORP INC
Form 10-Q
February 14, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)
x Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended: December 31, 2011
or
o 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: 001-34051

MALVERN FEDERAL BANCORP, INC.
(Exact name of Registrant as specified in its charter)

United States (State or Other Jurisdiction of Incorporation or Organization)	38-3783478 (I.R.S. Employer Identification Number)
42 E. Lancaster Avenue, Paoli, Pennsylvania (Address of Principal Executive Offices)	19301 (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 and (2) has been subject to such filing requirements for the past 90 days. YES x NO o

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 x NO o

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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer o
Non-accelerated filer o Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES o NO x

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's class of common stock, as of the latest practicable date: As of February 14, 2012, 6,102,500 shares of the Registrant's common stock were issued and outstanding.

MALVERN FEDERAL BANCORP, INC.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Consolidated Statements of Financial Condition (Unaudited)

	December 31, 2011	September 30, 2011
	(Dollars in thousands, except per share data)	
Assets		
Cash and due from depository institutions	$ 8,550	$ 13,490
Interest bearing deposits in depository institutions	49,291	20,006
Cash and Cash Equivalents	57,841	33,496
Investment securities available for sale, at fair value	81,164	74,389
Investment securities held to maturity (fair value of $3,796 and $4,024 respectively)	3,569	3,797
Restricted stock, at cost	5,081	5,349
Loans receivable, net of allowance for loan losses of $9,015 and $10,101, respectively	477,528	506,019
Other real estate owned	6,431	8,321
Accrued interest receivable	1,805	1,897
Property and equipment, net	8,068	8,165
Deferred income taxes, net	6,970	7,465
Bank-owned life insurance	14,894	14,760
Other assets	2,940	2,910
Total Assets	$ 666,291	$ 666,568
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Deposits-noninterest-bearing	$ 20,707	$ 19,833
Deposits-interest-bearing	530,574	534,622
Total Deposits	551,281	554,455
FHLB advances	48,846	49,098
Advances from borrowers for taxes and insurance	2,306	651
Accrued interest payable	254	233
Other liabilities	1,947	1,847
Total Liabilities	604,634	606,284
Commitments and Contingencies	-	-
Shareholders' Equity		
Preferred stock, $0.01 par value, 10,000,000 shares authorized, none issued	-	-
Common stock, $0.01 par value, 40,000,000 shares authorized, issued and outstanding: 6,102,500	62	62

Additional paid-in capital		25,873			25,889	
Retained earnings		37,888			36,637	
Treasury stock—at cost, 50,000 shares		(477	)		(477	)
Unearned Employee Stock Ownership Plan (ESOP) shares		(2,142	)		(2,178	)
Accumulated other comprehensive income		453			351	
Total Shareholders' Equity		61,657			60,284	
Total Liabilities and Shareholders' Equity	$	666,291		$	666,568	

See notes to unaudited consolidated financial statements.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Consolidated Statements of Operations (Unaudited)

	Three Months Ended December 31, 2011	2010
	(Dollars in thousands, except per share data)	
Interest and Dividend Income		
Loans, including fees	$ 6,427	$ 7,345
Investment securities, taxable	432	336
Investment securities, tax-exempt	4	7
Interest-bearing cash accounts	9	12
Total Interest and Dividend Income	6,872	7,700
Interest Expense		
Deposits	1,853	2,451
Long-term borrowings	434	452
Total Interest Expense	2,287	2,903
Net Interest Income	4,585	4,797
(Credit) Provision for Loan Losses	(300)	1,900
Net Interest Income after (Credit) Provision for Loan Losses	4,885	2,897
Other Income		
Service charges and other fees	277	241
Rental income	66	63
Gain on sale of investments, net	455	-
Gain (loss) on sale of other real estate owned, net	38	(26)
Earnings on bank-owned life insurance	134	143
Total Other Income	970	421
Other Expense		
Salaries and employee benefits	1,589	1,515
Occupancy expense	508	537
Federal deposit insurance premium	232	383
Advertising	186	194
Data processing	294	291
Professional fees	455	387
Other real estate owned expense	293	697
Other operating expenses	487	499
Total Other Expenses	4,044	4,503

Income (Loss) before income tax expense (benefit)		1,811		(1,185	)
Income tax expense (benefit)		560		(446	)
Net Income (Loss)	$	1,251	$	(739	)
Basic Earnings (Loss) Per Share	$	0.21	$	(0.13	)
Dividends Declared Per Share	$	0.00	$	0.03	

See notes to unaudited consolidated financial statements.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended December 31, 2011	Three Months Ended December 31, 2010
	(Dollars in thousands)	
Net Income (Loss)	$1,251	$(739)
Other Comprehensive Income (Loss):		
Changes in net unrealized gains on securities available for sale	609	(1,140)
Gains realized in net income	(455)	-
	154	(1,140)
Deferred income tax effect	(52)	388
Total other comprehensive income (loss)	102	(752)
Total comprehensive income (loss)	$1,353	$(1,491)

See notes to unaudited consolidated financial statements.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

	Common Stock	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Unearned ESOP Shares	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	(Dollars in thousands, except share and per share data)						
Balance, October 1, 2010	$ 62	$ 25,912	$ 42,830	$ (477)	$ (2,299)	$ 179	$ 66,207
Comprehensive Loss:							
Net Loss	-	-	(739)	-	-	-	(739)
Net change in unrealized loss on securities available for sale, net of taxes	-	-	-	-	-	(752)	(752)
Total Comprehensive Loss	-	-	-	-	-	-	(1,491)
Cash dividends declared ($0.03 per share)	-	-	(81)	-	-	-	(81)
Committed to be released ESOP shares (3,351 shares)	-	(16)	-	-	12	-	(4)
Balance, December 31, 2010	$62	$25,896	$42,010	$(477)	$(2,287)	$ (573)	$ 64,631
Balance, October 1, 2011	$ 62	$ 25,889	$ 36,637	$ (477)	$ (2,178)	$ 351	$ 60,284
Comprehensive Income:							
Net Income	-	-	1,251	-	-	-	1,251
Net Change in unrealized gain on securities available for sale, net of taxes	-	-	-	-	-	102	102
Total Comprehensive Income	-	-	-	-	-	-	1,353
Committed to be released ESOP shares (3,351 shares)	-	(16)	-	-	36	-	20

Balance, December 31, 2011	$62	$25,873	$37,888	$(477)	$(2,142)	$ 453	$ 61,657

See notes to unaudited consolidated financial statements.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited)

	Three Months Ended December 31, 2011	Three Months Ended December 31, 2010
	(Dollars in thousands)	
Cash Flows from Operating Activities		
Net income (loss)	$1,251	$(739)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation expense	186	216
(Credit) provision for loan losses	(300)	1,900
Deferred income taxes expense (benefit)	442	(244)
ESOP expense	20	(4)
(Accretion) of premiums and discounts on investment securities, net	(71)	(68)
Amortization (accretion) of mortgage servicing rights	11	(21)
Net gain on sale of investment securities available for sale	(455)	-
(Gain) loss on sale of other real estate owned	(38)	26
Write down of other real estate owned	111	430
Amortization of loan origination fees and costs	(338)	(306)
Decrease (increase) in accrued interest receivable	92	(9)
Increase (decrease) in accrued interest payable	21	(28)
Increase (decrease) in other liabilities	100	(77)
Earnings on bank-owned life insurance	(134)	(143)
(Increase) decrease in other assets	(263)	71
Decrease in prepaid FDIC assessment	222	368
Net Cash Provided by Operating Activities	857	1,372
Cash Flows from Investing Activities		
Proceeds from maturities and principal collections:		
Investment securities held to maturity	255	442
Investment securities available for sale	8,181	5,610
Proceeds from sales of investment securities available for sale	13,928	-
Purchases of investment securities available for sale	(17,560)	(41,680)
Loan purchases	(5,632)	(3,424)
Loan originations and principal collections, net	23,981	16,308
Proceeds from sale of other real estate owned	1,926	2,960
Net decrease in restricted stock	268	328
Purchases of property and equipment	(88)	(152)
Net Cash Provided by (Used in) Investing Activities	25,259	(19,608)
Cash Flows from Financing Activities		
Net decrease in deposits	(3,174)	(23,010)
Repayment of long-term borrowings	(252)	(5,485)
Increase in advances from borrowers for taxes and insurance	1,655	1,074
Cash dividends paid	-	(81)
Net Cash Used in Financing Activities	(1,771)	(27,502)

Net Increase (Decrease) in Cash and Cash Equivalents	24,345	(45,738)
Cash and Cash Equivalents - Beginning	33,496	81,395
Cash and Cash Equivalents - Ending	$57,841	$35,657
Supplementary Cash Flows Information		
Interest paid	$2,266	$2,931
Income taxes paid	$-	$-
Non-cash transfer of loans to other real estate owned	$109	$1,578
Non-cash transfer of loans to investment securities available for sale	$10,671	$-

See notes to unaudited consolidated financial statements.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)

Note 1 – Organizational Structure and Nature of Operations

Malvern Federal Bancorp, Inc. (the "Company") and its subsidiaries, Malvern Federal Holdings, Inc., a Delaware investment company, and Malvern Federal Savings Bank (the "Bank") and the Bank's subsidiaries, Strategic Asset Management Group, Inc. ("SAMG") and Malvern Federal Investments, Inc., a Delaware investment company, provide various banking services, primarily the accepting of deposits and the origination of residential and commercial mortgage loans and consumer loans and other loans through the Bank's eight full-service branches in Chester and Delaware Counties, Pennsylvania. SAMG owns 50% of Malvern Insurance Associates, LLC. Malvern Insurance Associates, LLC offers a full line of business and personal lines of insurance products. As of December 31, 2011 and September 30, 2011, SAMG's total assets were $42,000 and $42,000, respectively. There was no income reported for SAMG for the three months ended December 31, 2011. For the three months ended December 31, 2010 the net income for SAMG was $ $8,000. The Company is subject to competition from various other financial institutions and financial services companies. The Company is also subject to the regulations of certain federal and state agencies and, therefore, undergoes periodic examinations by those regulatory agencies.

On January 17, 2012, the Company, the Bank and the Mutual Holding Company announced that they had adopted a Plan of Conversion and Reorganization pursuant to which the Bank will reorganize from the two-tier mutual holding company structure to the stock holding company structure.

In accordance with the subsequent events topic of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification (the "Codification" or the "ASC"), the Company evaluates events and transactions that occur after the statement of financial condition date for potential recognition and disclosure in the consolidated financial statements. The effect of all subsequent events that provide additional evidence of conditions that existed at the balance sheet date are recognized in the unaudited consolidated financial statements as of December 31, 2011.

Note 2 – Summary of Significant Accounting Policies

Basis of Presentation and Consolidation

The consolidated financial statements at December 31, 2011, and September 30, 2011 and for the three months ended December 31, 2011 and 2010 include the accounts of Malvern Federal Bancorp, Inc. and its subsidiaries. All significant intercompany transactions and balances have been eliminated.

The accompanying unaudited consolidated financial statements were prepared in accordance with the instructions to Form 10-Q, and therefore, do not include all the information or footnotes necessary for a complete presentation of financial condition, operations, changes in shareholders' equity, and cash flows in conformity with accounting principles generally accepted in the United States of America. However, all normal recurring adjustments that, in the opinion of management, are necessary for a fair presentation of the consolidated financial statements have been included. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements of Malvern Federal Bancorp, Inc. and the accompanying notes thereto for the year ended September 30, 2011, which are included in the Company's Annual Report on Form 10-K for the year ended September 30, 2011. The results for the three months ended December 31, 2011 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2012, or any other period.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management 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 the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of deferred tax assets, the evaluation of other-than-temporary impairment of investment securities and fair value measurements.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)

Note 2 – Summary of Significant Accounting Policies (Continued)

Significant Group Concentrations of Credit Risk

Most of the Company's activities are with customers located within Chester and Delaware Counties, Pennsylvania. Note 5 discusses the types of investment securities that the Company invests in. Note 6 discusses the types of lending that the Company engages in. The Company does not have any significant concentrations to any one industry or customer. Although the Company has a diversified portfolio, its debtor's abilities to honor their contracts is influenced by, among other factors, the region's economy.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from depository institutions and interest bearing deposits.

The Company maintains cash deposits in other depository institutions that occasionally exceed the amount of deposit insurance available. Management periodically assesses the financial condition of these institutions and believes that the risk of any possible credit loss is minimal.

Investment Securities

Debt securities held to maturity are securities that the Company has the positive intent and the ability to hold to maturity; these securities are reported at amortized cost and adjusted for unamortized premiums and discounts. Securities held for trading are securities that are bought and held principally for the purpose of selling in the near term; these securities are reported at fair value, with unrealized gains and losses reported in current earnings. At December 31, 2011 and September 30, 2011, the Company had no investment securities classified as trading. Debt securities that will be held for indefinite periods of time and equity securities, including securities that may be sold in response to changes in market interest or prepayment rates, needs for liquidity and changes in the availability of and the yield of alternative investments are classified as available for sale. Realized gains and losses are recorded on the trade date and are determined using the specific identification method. Securities held as available for sale are reported at fair value, with unrealized gains and losses, net of tax, reported as a component of accumulated other comprehensive income ("AOCI"). Management determines the appropriate classification of investment securities at the time of purchase.

Securities are evaluated on a quarterly basis, and more frequently when market conditions warrant such an evaluation, to determine whether declines in their value are other-than-temporary. To determine whether a loss in value is other-than-temporary, management utilizes criteria such as the reasons underlying the decline, the magnitude and duration of the decline and whether or not management intends to sell or expects that it is more likely than not that it will be required to sell the security prior to an anticipated recovery of the fair value. The term "other-than-temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value for a debt security is determined to be other-than-temporary, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

Loans Receivable

The Company, through the Bank, grants mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by residential and commercial mortgage loans secured by properties located throughout Chester County, Pennsylvania and surrounding areas. The ability of the Company's debtors to honor their contracts is dependent upon, among other factors, the real estate and general economic conditions in this area.

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Malvern Federal Bancorp, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)

Note 2 – Summary of Significant Accounting Policies (Continued)

Loans receivable that management has the intent and ability to hold until maturity or payoff are stated at their outstanding unpaid principal balances, net of an allowance for loan losses and any deferred fees and costs. Interest income is accrued on the unpaid principal balance. Loan origination fees and costs are deferred and recognized as an adjustment of the yield (interest income) of the related loans using the interest method. The Company is amortizing these amounts over the contractual lives of the loans.

The loans receivable portfolio is segmented into residential loans, construction and development loans, commercial loans and consumer loans. The residential loan segment has one class, one- to four-family first lien residential mortgage loans. The construction and development loan segment consists of the following classes: residential and commercial and land loans. Residential construction loans are made for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built. Commercial construction loans are made for the purpose of acquiring, developing and constructing a commercial structure. The commercial loan segment consists of the following classes: commercial real estate loans, multi-family real estate loans, and other commercial loans, which are also generally known as commercial and industrial loans or commercial business loans. The consumer loan segment consists of the following classes: home equity lines of credit, second mortgage loans and other consumer loans, primarily unsecured consumer lines of credit.

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

In addition to originating loans, the Company purchases consumer and mortgage loans from brokers in our market area. Such purchases are reviewed for compliance with our underwriting criteria before they are purchased, and are generally purchased without recourse to the seller. Premiums and discounts on purchased loans are amortized as adjustments to interest income using the effective yield method.

Allowance for Loan Losses

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

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

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Malvern Federal Bancorp, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)

Note 2 – Summary of Significant Accounting Policies (Continued)

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers pools of loans by loan class that are not considered impaired. These pools of loans are evaluated for loss exposure based upon historical loss rates for each of these classes of loans, as adjusted for qualitative factors. These qualitative risk factors include:

1. Lending policies and procedures, including underwriting standards and collection, charge-off, and recovery practices.
2. National, regional, and local economic and business conditions as well as the condition of various market segments, including the value of underlying collateral for collateral dependent loans.
3. The nature and volume of the loan portfolio and terms of loans.
4. The experience, ability, and depth of lending management and staff.
5. The volume and severity of past due, classified and nonaccrual loans as well as and other loan modifications.
6. The quality of the Company’s loan review system, and the degree of oversight by the Company’s Board of Directors.
7. The existence and effect of any concentrations of credit and changes in the level of such concentrations.
8. The effect of external factors, such as competition and legal and regulatory requirements.

The qualitative factors are applied to the historical loss rates for each class of loan. In addition, while not reported as a separate factor, changes in the value of underlying collateral (for regional property values) for collateral dependent loans is considered and addressed within the economic trends factor. A quarterly calculation is made adjusting the reserve allocation for each factor within a risk weighted range as it relates to each particular loan type, collateral type and risk rating within each segment. Data is gathered and evaluated through internal, regulatory, and government sources quarterly for each factor.

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

In addition, the allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower’s overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments, for commercial and consumer loans. Credit quality risk ratings include categories of “pass,” “special mention,” “substandard” and “doubtful.” Assets which do not currently expose the insured institution to sufficient risk to warrant classification as substandard or doubtful but possess certain identified weaknesses are required to be designated “special mention.” If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. An asset is considered “substandard” if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. “Substandard” assets include those characterized by the “distinct possibility” that the insured institution will sustain “some loss” if the deficiencies are not corrected. Assets classified as “doubtful” have all of the weaknesses inherent in those classified “substandard” with the added characteristic that the weaknesses present make “collection or liquidation in full,” on the basis of currently existing facts, conditions, and values, “highly questionable and improbable.”

Residential Lending. Residential mortgage originations are secured primarily by properties located in the Company’s primary market area and surrounding areas. We currently originate fixed-rate, fully amortizing mortgage loans with maturities of 15 to 30 years. We also offer adjustable rate mortgage (“ARM”) loans where the interest rate either adjusts on an annual basis or is fixed for the initial one, three or five years and then adjusts annually. However, due to local market conditions, we have not originated a significant amount of ARM loans in recent years.

Malvern Federal Bancorp, Inc. and Subsidiaries
Notes to Consolidated Financial Statements (Unaudited)

Note 2 – Summary of Significant Accounting Policies (Continued)

We underwrite one- to four-family residential mortgage loans with loan-to-value ratios of up to 95%, provided that the borrower obtains private mortgage insurance on loans that exceed 80% of the appraised value or sales price, whichever is less, of the secured property. We also require that title insurance, hazard insurance and, if appropriate, flood insurance be maintained on all properties securing real estate loans. We require that a licensed appraiser from our list of approved appraisers perform and submit to us an appraisal on all properties secured by a first mortgage on one- to four-family first mortgage loans.

In underwriting one- to four-family residential mortgage loans, the Company evaluates both the borrower's ability to make monthly payments and the value of the property securing the loan. Most properties securing real estate loans made by the Company are appraised by independent fee appraisers approved by the Board of Directors. The Company generally requires borrowers to obtain an attorney's title opinion or title insurance, and fire and property insurance (including flood insurance, if necessary) in an amount not less than the amount of the loan. Real estate loans originated by the Company generally contain a "due on sale" clause allowing the Company to declare the unpaid principal balance due and payable upon the sale of the security property. The Company has not engaged in sub-prime residential mortgage loan originations. Our single-family residential mortgage loans generally are underwritten on terms and documentation conforming to guidelines issued by Freddie Mac and Fannie Mae.

Construction and Development Loans. During fiscal 2010, the Company generally ceased originating any new construction and development loans. Previously, we originated construction loans for residential and, to a lesser extent, commercial uses within our market area. We generally limited construction loans to builders and developers with whom we had an established relationship, or who were otherwise known to officers of the Bank. Our construction and development loans currently in the portfolio typically have variable rates of interest tied to the prime rate which improves the interest rate sensitivity of our loan portfolio.

Construction and development loans generally are considered to involve a higher level of risk than one-to four-family residential lending, due to the concentration of principal in a limited number of loans and borrowers and the effect of economic conditions on developers, builders and projects. Additional risk is also associated with construction lending because of the inherent difficulty in estimating both a property's value at completion and the estimated cost (including interest) to complete a project. The nature of these loans is such that they are more difficult to evaluate and monitor. In addition, speculative construction loans to a builder are not pre-sold and thus pose a greater potential risk than construction loans to individuals on their personal residences. In order to mitigate some of the risks inherent to construction lending, we inspect properties under construction, review construction progress prior to advancing funds, work with builders with whom we have established relationships, require annual updating of tax returns and other financial data of developers and obtain personal guarantees from the principals.

Commercial Lending. During fiscal 2010, the Company generally ceased originating new commercial or multi-family real estate mortgage loans and we are no longer purchasing whole loans or participation interests in commercial real estate or multi-family loans from other financial institutions. Commercial and multi-family real estate loans generally present a higher level of risk than loans secured by one- to four-family residences. This greater risk is due to several factors, including the concentration of principal in a limited number of loans and borrowers, the effect of general economic conditions on income producing properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by commercial and multi-family real estate is typically dependent upon the successful operation of the related real estate project. If the cash flow from the project is reduced (for example, if leases are not obtained or renewed, or a bankruptcy court modifies a lease term, or a major tenant is unable to fulfill its lease obligations), the borrower’s ability to repay the loan may be impaired.

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Note 2 – Summary of Significant Accounting Policies (Continued)

Most of the Company's commercial business loans have been extended to finance local and regional businesses and include short-term loans to finance machinery and equipment purchases, inventory and accounts receivable. The commercial business loans which we originated may be either a revolving line of credit or for a fixed term of generally 10 years or less. Interest rates are adjustable, indexed to a published prime rate of interest, or fixed. Generally, equipment, machinery, real property or other corporate assets secure such loans. Personal guarantees from the business principals are generally obtained as additional collateral.

Consumer Lending Activities. The Company currently originates most of its consumer loans in its primary market area and surrounding areas. The Company originates consumer loans on both a direct and indirect basis. Consumer loans generally have higher interest rates and shorter terms than residential mortgage loans; however, they have additional credit risk due to the type of collateral securing the loan or in some case the absence of collateral. As a result of the declines in the market value of real estate and the deterioration in the overall economy, we are continuing to evaluate and monitor the credit conditions of our consumer loan borrowers and the real estate values of the properties securing our second mortgage loans as part of our on-going efforts to assess the overall credit quality of the portfolio in connection with our review of the allowance for loan losses.

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

Once all factor adjustments are applied, general reserve allocations for each segment are calculated, summarized and reported on the ALLL summary. ALLL final schedules, calculations and the resulting evaluation process are reviewed quarterly by the Bank's Asset Classification Committee and the Bank's Board of Directors.

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

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed.

An allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of substantially all of the Company's impaired loans are measured based on the estimated fair value of the loan's collateral.

For commercial loans secured by real estate, estimated fair values are determined primarily through third-party appraisals. When a real estate secured loan becomes impaired, a decision is made regarding whether an updated appraisal of the real estate is necessary. This decision is based on various considerations, including the age of the most recent appraisal, the loan-to-value ratio based on the original appraisal and the condition of the property. Appraised values are discounted to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

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Note 2 – Summary of Significant Accounting Policies (Continued)

For commercial and industrial loans secured by non-real estate collateral, such as accounts receivable, inventory and equipment, estimated fair values are determined based on the borrower's financial statements, inventory reports, accounts receivable aging or equipment appraisals or invoices. Indications of value from these sources are generally discounted based on the age of the financial information or the quality of the assets.

Loan Servicing

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. Capitalized servicing rights are reported in other assets and are amortized into non-interest expense in proportion to, and over the period of, the estimated future net servicing income of the underlying financial asset.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. If the Company later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income.

Troubled Debt Restructurings

Loans whose terms are modified are classified as troubled debt restructurings ("TDRs") if the Company grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring typically consist of concessions such as extending the maturity date of the loan, reducing the interest rate on the loan to a rate which is below market, a combination of rate adjustments and maturity extensions, or by other means including covenant modifications, forbearances or other concessions. However, the Company generally only restructures loans by modifying the payment structure to require payments of interest only for a specified period of time or by reducing the actual interest rate. We do not accrue interest on loans that were non-accrual prior to the troubled debt restructuring until they have performed in accordance with their restructured terms for a period of at least six months. We continue to accrue interest on troubled debt restructurings which were performing in accordance with their terms prior to the restructure and continue to perform in accordance with their restructured terms. Management evaluates the ALLL with respect to TDRs under the same policy and guidelines as all other performing loans are evaluated with respect to the ALLL.

Other Real Estate Owned

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of the previously established carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in other expenses from other real estate owned.

Malvern Federal Bancorp, Inc. and Subsidiaries
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Note 2 – Summary of Significant Accounting Policies (Continued)

Restricted Stock

Restricted stock represents required investments in the common stock of a correspondent bank and is carried at cost. As of December 31, 2011 and September 30, 2011, restricted stock consists solely of the common stock of the Federal Home Loan Bank of Pittsburgh (“FHLB”).

Management’s evaluation and determination of whether this investment is impaired is based on their assessment of the ultimate recoverability of their cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of an investment’s cost is influenced by criteria such as (1) the significance of the decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, and (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the FHLB.

Property and Equipment

Property and equipment are carried at cost. Depreciation is computed using the straight-line and accelerated methods over estimated useful lives ranging from 3 to 39 years beginning when assets are placed in service. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is reflected in income for the period. The cost of maintenance and repairs is charged to income as incurred.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Bank-Owned Life Insurance

The Company invests in bank owned life insurance (“BOLI”) as a source of funding for employee benefit expenses. BOLI involves the purchasing of life insurance by the Bank on a chosen group of employees. The Bank is the owner and beneficiary of the policies. This life insurance investment is carried at the cash surrender value of the underlying policies. Earnings from the increase in cash surrender value of the policies are included in other income on the statement of income.

Advertising Costs

The Company follows the policy of charging the costs of advertising to expense as incurred.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. These calculations are based on many complex factors including estimates of the timing of reversals of temporary differences, the interpretation of federal income tax laws and a determination of the differences between the tax and the financial reporting basis of assets and liabilities. Actual results could differ significantly from the estimates and interpretations used in determining the current and deferred income tax assets and liabilities.

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Note 2 – Summary of Significant Accounting Policies (Continued)

A valuation allowance is required to be recognized if it is “more likely than not” that a portion of the deferred tax assets will not be realized. The Company’s policy is to evaluate the deferred tax asset on a quarterly basis and record a valuation allowance for our deferred tax asset if we do not have sufficient positive evidence indicating that it is more likely than not that some or all of the deferred tax asset will be realized.

Commitments and Contingencies

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the statement of financial condition when they are funded.

Segment Information

The Company has one reportable segment, “Community Banking.” All of the Company’s activities are interrelated, and each activity is dependent and assessed based on how each of the activities of the Company supports the others. For example, lending is dependent upon the ability of the Company to fund itself with deposits and other borrowings and manage interest rate and credit risk. Accordingly, all significant operating decisions are based upon analysis of the Company as one segment or unit.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale investment securities, are reported as a separate component of the shareholders’ equity section of the statement of financial condition, such items, along with net income, are components of comprehensive income. The Company early adopted Financial Accounting Standards Board (“FASB”) Accounting Standards Update (“ASU”) No. 2011-05, “Comprehensive Income (ASC Topic 220): Presentation of Comprehensive Income,” (“ASU 2011-05”) as of December 31, 2011. ASU No. 2011-05 amended prior comprehensive income guidance.

Reclassifications

Certain reclassifications have been made to the previous years’ financial statements to conform to the current year’s presentation. These reclassifications had no effect on the Company’s results of operations.

Recent Accounting Pronouncements

In June 2011, the FASB issued ASU No. 2011-05, “Comprehensive Income (ASC Topic 220): Presentation of Comprehensive Income,” (“ASU 2011-05”) which amends current comprehensive income guidance. This accounting update eliminates the option to present the components of other comprehensive income as part of the statement of shareholders’ equity. Instead, the Company must report comprehensive income in either a single continuous statement of comprehensive income which contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. ASU 2011-05 will be effective for public companies during the interim and annual periods beginning after December 15, 2011 with early adoption permitted. The Company adopted ASU 2011-05 as of December 31, 2011. The early adoption of ASU 2011-05 did not have an impact on the Company’s statements of operations, financial condition or cash flows as it only requires a change in the format of the current presentation.

In May 2011 the FASB issued ASU No. 2011-04, “Fair Value Measurements (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and International Financial Reporting Standards (“IFRS”). ASU 2011-04 represents the converged guidance of the FASB and the IASB (the “Boards”) on fair value measurements. The collective efforts of the Boards and their staffs, reflected in ASU 2011-04, have resulted in common requirements for measuring fair value and for disclosing information about fair value measurements, including a consistent meaning of the term “fair value.” The Boards have concluded the common requirements will result in greater comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with GAAP and IFRS. The amendments in this ASU are required to be applied prospectively, and are effective for interim and annual periods beginning after December 15, 2011. The Company does not expect that the adoption of ASU 2011-04 will have a significant impact on the Company’s statements of operations and financial condition.

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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, 2011 and for the three months ended December 31, 2011 and 2010 the Company had not issued and did not have any outstanding CSEs and at the present time, the Company's capital structure has no potential dilutive securities.

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

	Three Months Ended December 31,	
	2011	2010
	(Dollars in thousands, except per share amounts)	
Net Income (Loss)	$ 1,251	$ (739)
Average common shares outstanding	6,102,500	6,102,500
Average unearned ESOP shares	(194,820)	(208,206)
Weighted average shares outstanding – basic	5,907,680	5,894,294
Earnings (Loss) per share – basic	$ 0.21	$ (0.13)

Note 4 – Employee Stock Ownership Plan

The Company established an employee stock ownership plan ("ESOP") for substantially all of its full-time employees. Certain senior officers of the Bank have been designated as Trustees of the ESOP. 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 Company's 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 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, 2011 and 2010, there were 3,351 and 3,351 shares committed to be released, respectively. At December 31, 2011, there were 193,149 unallocated shares held by the ESOP which had an aggregate fair value of approximately $1.1 million.

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Note 5 - Investment Securities

At December 31, 2011 and September 30, 2011, all of the Company's mortgage-backed securities consisted of securities backed by residential mortgage loans.

Investment securities available for sale at December 31, 2011 and September 30, 2011 consisted of the following:

	December 31, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. government obligations	$4,998	$11	$-	$5,009
U.S. government agencies	20,878	141	(1)	21,018
FHLB notes	4,193	11	-	4,204
State and municipal obligations	952	29	(20)	961
Single issuer trust preferred security	1,000	-	(315)	685
Corporate debt securities	1,505	28	-	1,533
	33,526	220	(336)	33,410
Mortgage-backed securities:				
FNMA:				
Adjustable-rate	1,456	73	-	1,529
Fixed-rate	791	53	-	844
FHLMC:				
Adjustable-rate	587	20	-	607
GNMA, adjustable-rate	144	3	-	147
CMO, fixed-rate	43,974	654	(1)	44,627
	46,952	803	(1)	47,754
	$80,478	$1,023	$(337)	$81,164

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Note 5 - Investment Securities (Continued)

	September 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. government obligations	$4,998	$12	$-	$5,010
U.S. government agencies	23,874	98	(26)	23,946
FHLB notes	4,498	5	(7)	4,496
State and municipal obligations	952	31	(20)	963
Single issuer trust preferred security	1,000	-	(210)	790
Corporate debt securities	2,185	29	-	2,214
	37,507	175	(263)	37,419
Mortgage-backed securities:				
FNMA:				
Adjustable-rate	2,500	135	-	2,635
Fixed-rate	897	57	-	954
FHLMC:				
Adjustable-rate	643	21	-	664
Fixed-rate	325	27	-	352
GNMA, adjustable-rate	147	4	-	151
CMO, fixed-rate	31,838	425	(49)	32,214
	36,350	669	(49)	36,970
	$73,857	$844	$(312)	$74,389

Proceeds from sales of securities available for sale during the first quarter of fiscal 2012 were $13.9 million. Gross gains of $455,000 were realized on these sales. There were no sales of securities during fiscal 2011.

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Note 5 - Investment Securities (Continued)

Investment securities held to maturity at December 31, 2011 and September 30, 2011 consisted of the following:

	December 31, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
Mortgage-backed securities:				
GNMA, Adjustable-rate	$220	$8	$-	$228
GNMA, Fixed-rate	1	-	-	1
FNMA, Fixed-rate	3,348	219	-	3,567
	$3,569	$227	$-	$3,796

	September 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
Mortgage-backed securities:				
GNMA, Adjustable-rate	$231	$9	$-	$240
GNMA, Fixed-rate	1	-	-	1
FNMA, Fixed-rate	3,565	218	-	3,783
	$3,797	$227	$-	$4,024

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Note 5 - Investment Securities (Continued)

The following tables summarize the aggregate investments at December 31, 2011 and September 30, 2011 that were in an unrealized loss position.

	December 31, 2011					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)					
Investment Securities Available for Sale:						
U.S. government obligations and agencies	$999	$(1)	$-	$-	$999	$(1)
State and municipal obligations	20	(20)	-	-	20	(20)
Single issuer trust preferred security	-	-	685	(315)	685	(315)
Mortgage-backed securities:						
CMO, fixed-rate	889	(1)	-	-	889	(1)
	$1,908	$(22)	$685	$(315)	$2,593	$(337)

	September 30, 2011					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)					
Investment Securities Available for Sale:						
U.S. government agencies	$6,971	$(26)	$-	$-	$6,971	$(26)
FHLB notes	994	(5)	997	(2)	1,991	(7)
State and municipal obligations	20	(20)	-	-	20	(20)
Single issuer trust preferred security	-	-	790	(210)	790	(210)
Mortgage-backed securities:						
CMO, fixed-rate	6,077	(49)	-	-	6,077	(49)
	$14,062	$(100)	$1,787	$(212)	$15,849	$(312)

As of December 31, 2011, 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 the 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, 2011, the Company held one U.S. government agency securities, one tax-free municipal bond, three 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, 2011 represents other-than-temporary impairment.

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Note 5 - Investment Securities (Continued)

During the quarter ended December 31, 2011, the gross unrealized loss of the single issuer trust preferred security declined by $105,000 from an unrealized loss at September 30, 2011 of $210,000 to an unrealized loss of $315,000 as of December 31, 2011. The historic changes in the economy and interest rates have caused the pricing of agency securities, mortgage-backed securities, and trust preferred securities to widen dramatically over U.S. Treasury securities into the December 2011 quarter, but slight signs of improvement have recently occurred that have slightly stabilized the market. On a quarterly basis, management reviews the credit rating and performance of the issuer, as well as the impact that the overall economy is expected to have on those measurements and the fair value of this security.

At December 31, 2011 and September 30, 2011 the Company had no securities pledged to secure public deposits.

The amortized cost and fair value of debt securities by contractual maturity at December 31, 2011 follows:

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in thousands)			
Within 1 year	$ 24,331	$ 24,090	$ -	$ -
Over 1 year through 5 years	9,200	9,345	-	-
After 5 years through 10 years	(5)	(25)	-	-
Over 10 years	-	-		
	33,526	33,410	-	-
Mortgage-backed securities	46,952	47,754	3,569	3,796
	$ 80,478	$ 81,164	$ 3,569	$ 3,796

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Note 6 - Loans Receivable and Related Allowance for Loan Losses

Loans receivable consisted of the following for the periods indicated below:

	December 31, 2011	September 30, 2011
	(Dollars in thousands)	
Residential mortgage	$ 218,846	$ 229,330
Construction and Development:		
Residential and commercial	23,201	26,005
Land	632	2,722
Total Construction and Development	23,833	28,727
Commercial:		
Commercial real estate	131,283	131,225
Multi-family	639	5,507
Other	9,162	10,992
Total Commercial	141,084	147,724
Consumer:		
Home equity lines of credit	21,942	20,735
Second mortgages	77,254	85,881
Other	885	788
Total Consumer	100,081	107,404
Total loans	483,844	513,185
Deferred loan costs, net	2,699	2,935
Allowance for loan losses	(9,015)	(10,101)
Total loan receivable, net	$ 477,528	$ 506,019

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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, and September 30, 2011. Activity in the allowance is presented for the three months ended December 31, 2011 and 2010 and the year ended September 30, 2011, respectively.

		Construction and Development		Commercial			Consumer				
	Residential Mortgage	Residential and Commercial	Land	Commercial Real Estate	Multi-family	Other	Home Equity Lines of Credit	Second Mortgages	Other	Unallocated	Total
	(Dollars in thousands)										
Three Months Ended December 31, 2011:											
Allowance for loan losses:											
Beginning balance	$1,458	$1,627	$49	$4,176	$49	$317	$220	$2,154	$16	$35	$10,101
Charge-offs	(475)	(412)	-	(494)	-	(88)	(36)	(456)	(16)	-	(1,977)
Recoveries	-	1,139	-	-	-	1	-	50	1	-	1,191
Provision	356	(1,531)	(38)	937	(44)	30	(14)	(87)	17	74	(300)
Ending Balance	$1,339	$823	$11	$4,619	$5	$260	$170	$1,661	$18	$109	$9,015
Ending balance: individually evaluated for impairment	$-	$104	$-	$1,067	$-	$-	$-	$19	$-	$-	$1,190
Ending balance: collectively evaluated for impairment	$1,339	$719	$11	$3,552	$5	$260	$170	$1,642	$18	$109	$7,825
Loans receivable:											
Ending balance	$218,846	$23,201	$632	$131,283	$639	$9,162	$21,942	$77,254	$885		$483,844
Ending balance: individually evaluated for impairment	$1,178	$3,431	$-	$7,689	$-	$176	$-	$479	$-		$12,953
Ending balance: collectively evaluated for	$217,668	$19,770	$632	$123,594	$639	$8,986	$21,942	$76,775	$885		$470,891

impairment

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

		Construction and Development		Commercial			Consumer				
	Residential Mortgage	Residential and Commercial	Land	Commercial Real Estate	Multi-family	Other	Home Equity Lines of Credit	Second Mortgages	Other	Unallocated	To
	(Dollars in thousands)										
Three Months Ended December 31, 2010:											
Allowance for loan losses:											
Beginning balance	$1,555	$689	$63	$2,741	$191	$303	$284	$2,264	$22	$45	$8,1
Charge-offs	(429)	(107)	-	(284)	(164)	-	(99)	(1,448)	-	-	(2,5
Recoveries	-	-	-	1	1	1	-	17	3	-	23
Provision	445	125	1	221	(1)	35	40	1,055	(7)	(14)	1,9
Ending Balance	$1,571	$707	$64	$2,679	$27	$339	$225	$1,888	$18	$31	$7,5
Ending balance: individually evaluated for impairment	$757	$-	$-	$327	$-	$-	$55	$355	$-	$-	$1,4
Ending balance: collectively evaluated for impairment	$814	$707	$64	$2,352	$27	$339	$170	$1,533	$18	$31	$6,0
Loans receivable:											
Ending balance	$220,966	$29,191	$2,991	$142,027	$5,416	$12,452	$20,811	$101,030	$918		$535
Ending balance: individually evaluated for impairment	$1,928	$1,393	$-	$6,839	$-	$-	$62	$675	$-		$10,
Ending balance: collectively evaluated for impairment	$219,038	$27,798	$2,991	$135,188	$5,416	$12,452	$20,749	$100,355	$918		$524

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Malvern Federal Bancorp, Inc. and Subsidiaries
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Note 6 – Loans Receivable and Related Allowance for Loan Losses (Continued)

		Construction and Development		Commercial			Consumer				
	Residential Mortgage	Residential and Commercial	Land	Commercial Real Estate	Multi-family	Other	Home Equity Lines of Credit	Second Mortgages	Other	Unallocated	T
	(Dollars in thousands)										
Year Ended September 30, 2011:											
Allowance for loan losses:											
Beginning balance	$1,555	$689	$63	$2,741	$191	$303	$284	$2,264	$22	$45	$8,
Charge-offs	(2,478)	(1,307)	-	(2,460)	(164)	(278)	(166)	(3,691)	(6)	-	(1
Recoveries	1	-	-	1	1	5	3	82	9	-	10
Provision	2,380	2,245	(14)	3,894	21	287	99	3,499	(9)	(10)	12
Ending Balance	$1,458	$1,627	$49	$4,176	$49	$317	$220	$2,154	$16	$35	$10
Ending balance: individually evaluated for impairment	$296	$870	$-	$751	$-	$20	$61	$356	$-	$-	$2,
Ending balance: collectively evaluated for impairment	$1,162	$757	$49	$3,425	$49	$297	$159	$1,798	$16	$35	$7,
Loans receivable:											
Ending balance	$229,330	$26,005	$2,722	$131,225	$5,507	$10,992	$20,735	$85,881	$788		$51
Ending balance: individually evaluated for impairment	$1,651	$5,201	$-	$6,996	$-	$195	$60	$757	$-		$14
Ending balance: collectively evaluated for impairment	$227,679	$20,804	$2,722	$124,229	$5,507	$10,797	$20,675	$85,124	$788		$49

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

The following table presents impaired loans 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, 2011 and September 30, 2011.

	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
	(Dollars in thousands)				
December 31, 2011:					
Residential mortgage	$-	$-	$1,178	$1,178	$2,806
Construction and Development:					
Residential and commercial	1,810	104	1,621	3,431	4,947
Commercial:					
Commercial real estate	5,422	1,067	2,267	7,689	11,182
Other	-	-	176	176	176
Consumer:					
Second mortgages	479	19	-	479	479
Total impaired loans	$7,711	$1,190	$5,242	$12,953	$19,590
September 30, 2011:					
Residential mortgage	$1,627	$296	$24	$1,651	$2,813
Construction and Development:					
Residential and commercial	2,033	870	3,168	5,201	9,306
Commercial:					
Commercial real estate	5,005	751	1,991	6,996	9,999
Other	20	20	175	195	195
Consumer:					
Home equity lines of credit	60	61	-	60	60
Second mortgages	440	356	317	757	757
Total impaired loans	$9,185	$2,354	$5,675	$14,860	$23,130

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

The following table presents the average recorded investment in impaired loans and related interest income recognized for three months ended December 31, 2011 and 2010.

	Average Impaired Loans	Interest Income Recognized on Impaired Loans	Cash Basis Collection on Impaired Loans
	(Dollars in thousands)		
Three Months Ended December 31, 2011:			
Residential mortgage	$ 1,567	$ 3	$ 8
Construction and development:			
Residential and commercial	4,316	-	-
Commercial:			
Commercial real estate	6,972	73	84
Other	192	1	1
Consumer:			
Home equity lines of credit	42	-	-
Second mortgages	570	-	-
Other	5	-	-
Total	$ 13,664	$ 77	$ 93
Three Months Ended December 31, 2010:			
Residential mortgage	$ 2,282	$ -	$ -
Construction and development:			
Residential and commercial	1,398	-	35
Commercial:			
Commercial real estate	7,985	-	-
Multi-family	546	54	54
Consumer:			
Home equity lines of credit	158	-	-
Second mortgages	2,618	-	-
Total	$ 14,987	$ 54	$ 89

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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, 2011 and September 30, 2011.

	Pass	Special Mention	Substandard	Doubtful	Total
			(Dollars in thousands)		
December 31, 2011:					
Residential mortgage	$214,973	$709	$3,164	$-	$218,846
Construction and Development:					
Residential and commercial	13,568	2,728	6,905	-	23,201
Land	-	632	-	-	632
Commercial:					
Commercial real estate	109,089	4,683	16,845	666	131,283
Multi-family	639	-	-	-	639
Other	7,484	900	778	-	9,162
Consumer:					
Home equity lines of credit	21,905	-	37	-	21,942
Second mortgages	75,913	5	1,336	-	77,254
Other	879	6	-	-	885
Total	$444,450	$9,663	$29,065	$666	$483,844
September 30, 2011:					
Residential mortgage	$225,498	$197	$3,635	$-	$229,330
Construction and Development:					
Residential and commercial	15,514	2,579	7,042	870	26,005
Land	662	900	1,160	-	2,722
Commercial:					
Commercial real estate	108,267	6,645	16,088	225	131,225
Multi-family	4,910	-	597	-	5,507
Other	9,190	1,004	798	-	10,992
Consumer:					
Home equity lines of credit	20,621	16	98	-	20,735
Second mortgages	82,425	1,335	2,121	-	85,881
Other	779	9	-	-	788
Total	$467,866	$12,685	$31,539	$1,095	$513,185

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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, 2011		September 30, 2011
		(Dollars in thousands)		
Non-accrual loans:				
Residential mortgage	$	2,562	$	2,866
Construction and Development:				
Residential and commercial		4,841		6,617
Commercial:				
Commercial real estate		1,694		1,765
Other		209		229
Consumer:				
Home equity lines of credit		37		61
Second mortgages		1,065		1,377
Total non-accrual loans	$	10,408	$	12,915

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 six consecutive months. Interest income that would have been recognized on nonaccrual loans had they been current in accordance with their original terms was $178,000 and $282,000 for the three months ended December 31, 2011 and 2010, respectively. There were no loans past due 90 days or more and still accruing interest at December 31, 2011 and September 30, 2011

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

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, 2011and September 30, 2011.

	Current	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Total Loans Receivable
	(Dollars in thousands)					
December 31, 2011:						
Residential mortgage	$214,876	$534	$874	$2,562	$3,970	$218,846
Construction and Development:						
Residential and commercial	18,360	-	-	4,841	4,841	23,201
Land	632	-	-	-	-	632
Commercial:						
Commercial real estate	126,419	-	3,170	1,694	4,864	131,283
Multi-family	639	-	-	-	-	639
Other	8,953	-	-	209	209	9,162
Consumer:						
Home equity lines of credit	21,885	-	20	37	57	21,942
Second mortgages	75,007	759	423	1,065	2,247	77,254
Other	878	-	7	-	7	885
Total	$467,649	$1,293	$4,494	$10,408	$16,195	$483,844
September 30, 2011:						
Residential mortgage	$225,705	$341	$418	$2,866	$3,625	$229,330
Construction and Development:						
Residential and commercial	19,388	-	-	6,617	6,617	26,005
Land	2,722	-	-	-	-	2,722
Commercial:						
Commercial real estate	129,265	-	195	1,765	1,960	131,225
Multi-family	5,507	-	-	-	-	5,507
Other	10,741	22	-	229	251	10,992
Consumer:						
Home equity lines of credit	20,658	-	16	61	77	20,735
Second mortgages	82,803	1,074	627	1,377	3,078	85,881
Other	772	-	16	-	16	788
Total	$497,561	$1,437	$1,272	$12,915	$15,624	$513,185

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

As a result of adopting the amendments in ASU No. 2011-02 in the fourth quarter of fiscal 2011, the Company reassessed all restructured loans that occurred on or after October 1, 2010 and for which the borrower was determined to be troubled, for identification as troubled debt restructurings ("TDRs"). Upon identifying those receivables as TDRs, the Company identified them as impaired under the guidance in Section 310-10-35 of the Accounting Standards Codification. The amendments in ASU No. 2011-02 require prospective application of the impairment measurement guidance in Section 450-20 for those receivables newly identified as impaired.

Restructured loans deemed to be TDRs atypically are 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, 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 $10.1 million and $10.3 million of TDRs at December 31, 2011 and September 30, 2011, respectively. Ten loans deemed TDRs with an aggregate balance of $7.1 million at December 31, 2011 were classified as impaired; however, they were performing prior to the restructure and continued to perform under their restructured terms as of December 31, 2011. During the quarter ended December 31, 2011 we charged-off $37,000 with respect to one home equity line of credit loan which was deemed a TDR. In addition we modified two non-accruing construction and development loans in the aggregate amount of $1.8 million, which were deemed non-accruing TDRs at December 31, 2011, with no additional allowance for loan losses. 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. No defaults on troubled debt restructured loans occurred during the quarter ended December 31, 2011 on loans modified as a TDR within the previous 12 months. The following table shows information on the troubled debt restructurings by type of loan portfolio as of December 31, 2011 and September 30, 2011.

	December 31, 2011			September 30, 2011		
	Number of Contracts	Pre-Modifications Outstanding Recorded Investments	Post-Modifications Outstanding Recorded Investments	Number of Contracts	Pre-Modifications Outstanding Recorded Investments	Post-Modifications Outstanding Recorded Investments
			(Dollars in thousands)			

Troubled Debt Restructurings:						
Residential mortgage	4	$ 1,061	$ 882	4	$ 1,061	$ 1,049
Construction and Development:						
Residential and commercial	2	1,810	1,810	-	-	-
Land loans	2	1,169	1,157	2	1,169	1,160
Commercial:						
Commercial real estate	7	7,986	7,897	7	7,986	7,919
Other	1	175	175	1	175	175
Consumer:						
Home equity lines of credit	-	-	-	1	37	37
Total troubled debt restructurings	16	$ 12,201	$ 11,921	15	$ 10,428	$ 10,340

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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.

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).

Management believes, as of December 31, 2011, that the Bank met all capital adequacy requirements to which it was subject.

As of December 31, 2011, the most recent notification from the regulators categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. To be categorized as well-capitalized, the Bank must maintain minimum tangible, core, and risk-based ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the Bank's category.

Until recently, the Bank, the Company and the Mutual Holding Company were regulated by the Office of Thrift Supervision (the "OTS"). As a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the OTS was eliminated and, as of July 21, 2011, the regulatory oversight functions and authority of the OTS related to the Bank were transferred to the Office of the Comptroller of the Currency (the "OCC") and the regulatory oversight functions and authority of the OTS related to the Holding Company and Mutual Holding Company, which are savings and loan holding companies, were transferred to the Board of Governors of the Federal Reserve System (the "Federal Reserve Board" or the "FRB").

In October 2010, the Bank and the Company and the Mutual Holding Company entered into Supervisory Agreements (the "Agreement") with the OTS (now, the OCC) that required compliance with certain items within specified timeframes as outlined in the Agreements. The Company and the Bank operated in compliance with the Supervisory Agreements in all material respects during the quarter ended December 31, 2011.

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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, 2011:						
Tangible Capital (to tangible assets)	$52,996	8.09 %	$≥ 9,831	≥1.50 %	N/A	
Core Capital (to adjusted tangible assets)	52,996	8.09	≥26,215	≥4.00	$≥32,769	≥ 5.00 %
Tier 1 Capital (to risk-weighted assets)	52,996	11.88	≥17,836	≥4.00	≥26,755	≥ 6.00
Total risk-based Capital (to risk-weighted assets)	58,613	13.14	≥35,673	≥8.00	≥44,591	≥ 10.00
As of September 30, 2011:						
Tangible Capital (to tangible assets)	$49,681	7.54 %	$≥ 9,878	≥ 1.50 %	N/A	
Core Capital (to adjusted tangible assets)	49,681	7.54	≥ 26,342	≥ 4.00	$≥ 32,928	≥ 5.00 %
Tier 1 Capital (to risk-weighted assets)	49,681	10.76	≥ 18,476	≥ 4.00	≥ 27,714	≥ 6.00
Total risk-based Capital (to risk-weighted assets)	55,493	12.01	≥ 36,952	≥ 8.00	≥ 46,190	≥ 10.00

During the quarter ended December 31, 2011, the Company made a $3.2 million capital infusion to the Bank.

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Note 8 - Fair Value Measurements

The Company follows FASB ASC Topic 820 “Fair Value Measurements,” 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.

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.

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Note 8 - Fair Value Measurements (Continued)

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

	December 31, 2011			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Investment securities available for sale:				
Debt securities:				
U.S. government obligations	$5,009	$5,009	$-	$-
U.S. government agencies	21,018	-	21,018	-
FHLB notes	4,204	-	4,204	-
State and municipal obligations	961	-	961	-
Single issuer trust preferred security	685	-	685	-
Corporate debt securities	1,533	-	1,533	-
Total investment securities available for sale	33,410	5,009	28,401	-
Mortgage-backed securities available for sale:				
FNMA:				
Adjustable-rate	1,529	-	1,529	-
Fixed-rate	844	-	844	-
FHLMC:				
Adjustable-rate	607	-	607	-
GNMA, adjustable-rate	147	-	147	-
CMO, fixed-rate	44,627	-	44,627	-
Total mortgage-backed securities available for sale	47,754	-	47,754	-
Total	$81,164	$5,009	$76,155	$-

	September 30, 2011			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Investment securities available for sale:				
Debt securities:				
U.S. government obligations	$5,010	$5,010	$-	$-
U.S. government agencies	23,946	-	23,946	-
FHLB notes	4,496	-	4,496	-
State and municipal obligations	963	-	963	-
Single issuer trust preferred security	790	-	790	-
Corporate debt securities	2,214	-	2,214	-
Total investment securities available for sale	37,419	5,010	32,409	-

Mortgage-backed securities available for sale:				
FNMA:				
Adjustable-rate	2,635	-	2,635	-
Fixed-rate	954	-	954	-
FHLMC:				
Adjustable-rate	664	-	664	-
Fixed-rate	352	-	352	-
GNMA, adjustable-rate	151	-	151	-
CMO, fixed-rate	32,214	-	32,214	-
Total mortgage-backed securities available for sale	36,970	-	36,970	-
Total	$74,389	$5,010	$69,379	$-

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Note 8 - Fair Value Measurements (Continued)

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, 2011 and September 30, 2011:

	December 31, 2011			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Other real estate owned	$761	$-	$-	$761
Impaired loans	6,537	-	-	6,537
Total	$7,298	$-	$-	$7,298

	September 30, 2011			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Other real estate owned	$3,382	$-	$-	$3,382
Impaired loans	6,831	-	-	6,831
Total	$10,213	$-	$-	$10,213

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, 2011 and September 30, 2011. 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, 2011 and September 30, 2011 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, 2011 or September 30, 2011.

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Note 8 - Fair Value Measurements (Continued)

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 evaluated and valued at the time the loan is identified as impaired, at the lower of cost or fair value. Fair value is measured based on the value of the collateral securing these loans and is classified at Level 3 in the fair value hierarchy. Collateral may be real estate and/or business assets including equipment, inventory and/or accounts receivable and is determined based on appraisals by qualified licensed appraisers hired by the Company. Appraised and reported values may be discounted based on management's historical knowledge, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client's business. Impaired loans are reviewed and evaluated on a monthly basis for additional impairment and adjusted accordingly, based on the same factors identified above.

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.

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— Other real estate owned includes foreclosed properties securing commercial, residential and construction loans. Real estate properties acquired through foreclosure are initially recorded at the fair value of the property at the date of foreclosure. After foreclosure, valuations are periodically performed by management and the real estate is carried at the lower of cost or fair value less estimated costs to sell. Fair value is generally based upon independent market prices or appraised value of the collateral. Our appraisals are typically performed by independent third party appraisers. For appraisals of commercial and construction properties, comparable properties within the area may not be available. In such circumstances, our appraisers will rely on certain judgments in determining how a specific property compares in value to other properties that are not identical in design or in geographic area. Our current portfolio of other real estate owned is comprised of such properties and, accordingly, we classify other real estate owned as Level 3 on a non-recurring basis.

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.

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Note 8 - Fair Value Measurements (Continued)

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.

The carrying amount and estimated fair value of the Company's financial instruments as of December 31, 2011 and September 30, 2011 are presented below:

	December 31, 2011		September 30, 2011	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:	(Dollars in thousands)			
Cash and cash equivalents	$57,841	$57,841	$33,496	$33,496
Investment securities available for sale	81,164	81,164	74,389	74,389
Investment securities held to maturity	3,569	3,796	3,797	4,024
Loans receivable, net	477,528	494,069	506,019	527,628
Accrued interest receivable	1,805	1,805	1,897	1,897
Restricted stock	5,081	5,081	5,349	5,349
Mortgage servicing rights	117	117	128	128
Financial liabilities:				
Savings accounts	43,982	43,982	45,067	45,067
Checking and NOW accounts	112,557	112,557	108,555	108,555
Money market accounts	88,105	88,105	86,315	86,315
Certificates of deposit	306,637	315,956	314,518	323,634
FHLB advances	48,846	53,655	49,098	53,643
Accrued interest payable	254	254	233	233

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Note 9 – Income Taxes

The following is reconciliation between the statutory federal income tax rate of 34% and the effective income tax rate on income before income taxes:

	Three Months Ended December 31, 2011	2010
	(Dollars in thousands)	
At federal statutory rate	$ 616	$ (403)
Adjustments resulting from:		
Tax-exempt interest	(2)	(2)
Low-income housing credit	(11)	(10)
Earnings on bank-owned life insurance	(46)	(49)
Other	3	18
	$ 560	$ (446)

The Company's effective tax rate was 30.93% and (37.65%) for the three months ended December 31, 2011 and 2010, respectively.

Deferred income taxes at December 31, 2011 and September 30, 2011 were as follows:

	December 31, 2011	September 30, 2011
	(Dollars in thousands)	
Deferred Tax Assets:		
Allowance for loan losses	$ 3,065	$ 3,434
Nonaccrual interest	408	431
Write-down of real estate owned	232	298
AMT credit carryover	196	84
Low-income housing tax credit carryover	205	191
Supplement Employer Retirement Plan	359	352
Charitable contributions	247	247
State net operating loss	296	296
Net operating loss	2,548	2,702
Other	144	137
Total Deferred Tax Assets	7,700	8,172
Valuation allowance for state net operating loss	(296)	(296)
Total Deferred Tax Assets, Net of Valuation Allowance	$ 7,404	$ 7,876
Deferred Tax Liabilities:		
Unrealized gain on investments available for sale	(233)	(180)

Depreciation		-		(28)
Mortgage servicing rights		(40)		(43)
Other		(161)		(160)
Total Deferred Tax Liabilities		(434)		(411)
Deferred Tax Assets, Net	$	6,970	$	7,465

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

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains certain forward looking statements (as defined in the Securities Exchange Act of 1934 and the regulations thereunder). Forward looking statements are not historical facts but instead represent only the beliefs, expectations or opinions of Malvern Federal Bancorp, Inc. and its management regarding future events, many of which, by their nature, are inherently uncertain. Forward looking statements may be identified by the use of such words as: "believe", "expect", "anticipate", "intend", "plan", "estimate", or words of similar meaning, or f or conditional terms such as "will", "would", "should", "could", "may", "likely", "probably", or "possibly." Forwarc statements include, but are not limited to, financial projections and estimates and their underlying assumptions; statements regarding plans, objectives and expectations with respect to future operations, products and services; and statements regarding future performance. Such statements are subject to certain risks, uncertainties and assumptions, many of which are difficult to predict and generally are beyond the control of Malvern Federal Bancorp, Inc. and its management, that could cause actual results to differ materially from those expressed in, or implied or projected by, forward looking statements. The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in the forward looking statements: (1) economic and competitive conditions which could affect the volume of loan originations, deposit flows and real estate values; (2) the levels of non-interest income and expense and the amount of loan losses; (3) competitive pressure among depository institutions increasing significantly; (4) changes in the interest rate environment causing reduced interest margins; (5) general economic conditions, either nationally or in the markets in which Malvern Federal Bancorp, Inc. is or will be doing business, being less favorable than expected; (6) political and social unrest, including acts of war or terrorism; or (7) legislation or changes in regulatory requirements adversely affecting the business in which Malvern Federal Bancorp, Inc. is engaged. Malvern Federal Bancorp, Inc. undertakes no obligation to update these forward looking statements to reflect events or circumstances that occur after the date on which such statements were made.

As used in this report, unless the context otherwise requires, the terms "we," "our," "us," or the "Company" refer to Malverr Federal Bancorp, Inc., a Federal corporation, and the term the "Bank" refers to Malvern Federal Savings Bank, a federally chartered savings bank and wholly owned subsidiary of the Company. In addition, unless the context otherwise requires, references to the operations of the Company include the operations of the Bank.

General

In 2008, Malvern Federal Savings Bank ("Malvern Federal Savings" or the "Bank") completed its reorganization to the mutual holding company form of organization and formed Malvern Federal Bancorp, Inc. (the "Company") to serve as the stock holding company for the Bank. In connection with the reorganization, the Company sold 2,645,575 shares of its common stock to certain members of the Bank and the public at a purchase price of $10.00 per share. In addition, the Company issued 3,383,875 shares, or 55% of the outstanding shares, of its common stock to Malvern Federal Mutual Holding Company, a federally chartered mutual holding company (the "Mutual Holding Company"), and contributed 123,050 shares (with a value of $1.2 million), or 2.0% of the outstanding shares, to the Malvern Federal Charitable Foundation, a newly created Delaware charitable foundation.

On January 17, 2012, the Company, the Bank and the Mutual Holding Company announced that they had adopted a Plan of Conversion and Reorganization pursuant to which the Bank will reorganize from the two-tier mutual holding company structure to the stock holding company structure.

The Company is a federally chartered corporation which owns all of the issued and outstanding shares of the Bank's common stock, the only shares of equity securities which the Bank has issued. Malvern Federal Bancorp does not own or lease any property, but instead uses the premises, equipment and furniture of the Bank. At the present time, the Company employs only persons who are officers of Malvern Federal Savings to serve as officers of the Company. The Company also uses the Bank's support staff from time to time. These persons are not separately compensated by Malvern Federal Bancorp.

Malvern Federal Savings is a federally chartered community-oriented savings bank which was originally organized in 1887 and is headquartered in Paoli, Pennsylvania. The Bank currently conducts its business from its headquarters and eight additional financial centers.

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The Bank is primarily engaged in attracting deposits from the general public and using those funds to invest in loans and investment securities. The Bank's principal sources of funds are deposits, repayments of loans and investment securities, maturities of investments and interest-bearing deposits, other funds provided from operations and wholesale funds borrowed from outside sources such as the Federal Home Loan Bank of Pittsburgh (the "FHLB"). These funds are primarily used for the origination of various loan types including single-family residential mortgage loans, commercial real estate mortgage loans, construction and development loans, home equity loans and lines of credit and other consumer loans. The Bank derives its income principally from interest earned on loans, investment securities and, to a lesser extent, from fees received in connection with the origination of loans and for other services. Malvern Federal Savings' primary expenses are interest expense on deposits and borrowings and general operating expenses. Funds for activities are provided primarily by deposits, amortization of loans, loan prepayments and the maturity of loans, securities and other investments and other funds from operations.

Until recently, the Bank, the Company and the Mutual Holding Company were regulated by the Office of Thrift Supervision (the "OTS"). As a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the OTS was eliminated and, as of July 21, 2011, the regulatory oversight functions and authority of the OTS related to the Bank were transferred to the Office of the Comptroller of the Currency (the "OCC") and the regulatory oversight functions and authority of the OTS related to the Holding Company and Mutual Holding Company, which are savings and loan holding companies, were transferred to the Board of Governors of the Federal Reserve System (the "Federal Reserve Board" or the "FRB").

In October 2010, the Company, the Bank and the Mutual Holding Company entered into Supervisory Agreements (the "Supervisory Agreement(s)") with the OTS which primarily addressed the issues identified in the OTS' reports of examination of the Company's, the Bank's, and the Mutual Holding Company's operations and financial condition in 2010. See "Item 1. Business" in our Annual Report on Form 10-K for the fiscal year ended September 30, 2011 for more information. As discussed above, the regulatory functions of the OTS have been transferred to the OCC, in the case of the Bank, and the FRB in the case of the Company and the Mutual Holding Company.

Critical Accounting Policies

In reviewing and understanding financial information for Malvern Federal Bancorp, Inc., you are encouraged to read and understand the significant accounting policies used in preparing our consolidated financial statements. These policies are described in Note 2 of the notes to our consolidated financial statements included elsewhere. The accounting and financial reporting policies of Malvern Federal Bancorp conform to accounting principles generally accepted in the United States of America ("U.S. GAAP") and to general practices within the banking industry. Accordingly, the consolidated financial statements require certain estimates, judgments, and assumptions, which are believed to be reasonable, based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of income and expenses during the periods presented. The following accounting policies comprise those that management believes are the most critical to aid in fully understanding and evaluating our reported financial results. These policies require numerous estimates or economic assumptions that may prove inaccurate or may be subject to variations which may affect our reported results and financial condition for the period or in future periods.

Allowance for Loan Losses. The allowance for credit losses consists of the allowance for loan losses and the reserve for unfunded lending commitments. The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the statement of financial condition date and is recorded as a reduction to loans. The reserve for unfunded lending commitments represents management's estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated statement of financial condition. The allowance for loan losses ("ALLL") is increased by the provision for loan losses, and decreased by charge-offs, net of recoveries. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance. All, or part, of the principal balance of loans receivable are charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely. Non-residential consumer loans are generally charged off no later than when they become 120 days past due on a contractual basis or earlier in the event of the borrower's bankruptcy, or if there is an amount deemed uncollectible. Because all identified losses are immediately charged off, no portion of the allowance for loan losses is restricted to any individual loan or groups of loans, and the entire allowance is available to absorb any and all loan losses.

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

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers pools of loans by loan class including commercial loans not considered impaired, as well as smaller balance homogeneous loans, such as residential real estate, home equity and other consumer loans. These pools of loans are evaluated for loss exposure based upon historical loss rates for each of these categories of loans, as adjusted for qualitative factors.

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. Once all factor adjustments are applied, general reserve allocations for each segment are calculated, summarized and reported on the ALLL summary. ALLL final schedules, calculations and the resulting evaluation process are reviewed quarterly by the Asset Classification Committee and the Board of Directors.

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

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and industrial loans, commercial real estate loans and commercial construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent.

The allowance is adjusted for other significant factors that affect the collectibility of the loan portfolio as of the evaluation date including changes in lending policy and procedures, loan volume and concentrations, seasoning of the portfolio, loss experience in particular segments of the portfolio, and bank regulatory examination results. Other factors include changes in economic and business conditions affecting our primary lending areas and credit quality trends. Loss factors are reevaluated each reporting period to ensure their relevance in the current economic environment. We review key ratios such as the allowance for loan losses to total loans receivable and as a percentage of non-performing loans; however, we do not try to maintain any specific target range for these ratios.

While management uses the best information available to make loan loss allowance evaluations, adjustments to the allowance may be necessary based on changes in economic and other conditions or changes in accounting guidance. Historically, our estimates of the allowance for loan losses have not required significant adjustments from management's initial estimates. In addition, the OCC (and, previously, the OTS), as an integral part of its examination processes, periodically reviews our allowance for loan losses. The OCC may require the recognition of adjustments to the allowance for loan losses based on their judgment of information available to them at the time of their examinations. To the extent that actual outcomes differ from management's estimates, additional provisions to the allowance for loan losses may be required that would adversely impact earnings in future periods.

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Fair Value Measurements. The Company uses fair value measurements to record fair value adjustments to certain assets to determine fair value disclosures. 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.

Under FASB ASC Topic 820, Fair Value Measurements, 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.

Under FASB ASC Topic 820, 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 in FASB ASC Topic 820.

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 such 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, that could significantly affect the results of current or future valuations. At December 31, 2011, the Company had $7.3 million of assets that were measured at fair value on a recurring basis using Level 3 measurements.

Income Taxes. We make estimates and judgments to calculate some of our tax liabilities and determine the recoverability of some of our deferred tax assets, which arise from temporary differences between the tax and financial statement recognition of revenues and expenses. We also estimate a reserve for deferred tax assets if, based on the available evidence, it is more likely than not that some portion or all of the recorded deferred tax assets will not be realized in future periods. These estimates and judgments are inherently subjective. Historically, our estimates and judgments to calculate our deferred tax accounts have not required significant revision to our initial estimates.

In evaluating our ability to recover deferred tax assets, we consider all available positive and negative evidence, including our past operating results and our forecast of future taxable income. In determining future taxable income, we make assumptions for the amount of taxable income, the reversal of temporary differences and the implementation of feasible and prudent tax planning strategies. These assumptions require us to make judgments about our future taxable income and are consistent with the plans and estimates we use to manage our business. Any reduction in estimated future taxable income may require us to record a valuation allowance against our deferred tax assets. An increase in the valuation allowance would result in additional income tax expense in the period and could have a significant impact on our future earnings.

Realization of a deferred tax asset requires us to exercise significant judgment and is inherently uncertain because it requires the prediction of future occurrences. Our net deferred tax asset amounted to $7.0 million at December 31, 2011. We have not established a valuation allowance against our net deferred tax asset as we believe it is more likely than not that the entire amount of the asset will be realized. In evaluating the need for a valuation allowance, we must estimate our taxable income in future years. Our deferred tax asset may be reduced in the future if estimates of future income or our tax planning strategies do not support the amount of the deferred tax asset. If it is determined that a valuation allowance with respect to our deferred tax asset is necessary, we may incur a charge to earnings and a reduction to regulatory capital for the amount included therein.

Other-Than-Temporary Impairment of Securities – Securities are evaluated on a quarterly basis, and more frequently when market conditions warrant such an evaluation, to determine whether declines in their value are other-than-temporary. To determine whether a loss in value is other-than-temporary, management utilizes criteria such as the reasons underlying the decline, the magnitude and duration of the decline and whether or not management intends to sell or expects that it is more likely than not that it will be required to sell the security prior to an anticipated recovery of the fair value. The term “other-than-temporary” is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value for a debt security is determined to be other-than-temporary, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

Comparison of Financial Condition at December 31, 2011 and September 30, 2011

The Company’s total assets amounted to $666.3 million at December 31, 2011 compared to $666.6 million at September 30, 2011. The primary reason for the $277,000 decrease in assets during first three months of fiscal 2012 was a decrease of $28.5 million in net loans receivable, a $1.9 million decrease in other real estate owned (“REO”), a $495,000 decrease in deferred taxes and a $268,000 decrease in restricted stock at December 31, 2011 compared to September 30, 2011. These decreases were partially offset by an aggregate $24.3 million increase in cash and cash equivalents and a $6.5 million increase in investment securities. The decrease in loans receivable was due to a $10.7 million loan sale securitization during the first quarter of fiscal 2012, as well as decreased demand from consumers, the internal lending restrictions we adopted early in fiscal 2010, and the restrictions imposed by the Supervisory Agreement that the Bank entered into with the OTS in October 2010. The $1.9 million decrease in REO at December 31, 2011 compared to September 30, 2011, was due to $1.9 million of net sales in REO properties, at a net gain of $38,000, and $111,000 in reductions to REO fair values, which are reflected as REO expense during the first quarter of fiscal 2012. The Company’s total REO amounted to $6.4 million at December 31, 2011 compared to $8.3 million at September 30, 2011.

Our total liabilities at December 31, 2011, amounted to $604.6 million compared to $606.3 million at September 30, 2011. The $1.7 million, or 0.3% decrease in total liabilities was due primarily to a decrease in total deposits of $3.2 million, which was partially offset by $1.6 million increase in total escrow advances for taxes and insurance in the first quarter of fiscal 2011. Our total deposits amounted to $551.3 million at December 31, 2011 compared to $554.5 million at September 30, 2011. There was a $252,000 decrease in our FHLB advances during the three months ended December 31, 2011.

Shareholders’ equity increased by $1.4 million to $61.7 million at December 31, 2011 compared to $60.3 million at September 30, 2011 primarily due to an increase in retained earnings and the effect of an increase in our accumulated other comprehensive income at December 31, 2011. Retained earnings increased by $1.3 million to $37.9 million at December 31, 2011 primarily as a result of the $1.3 million net income during the first quarter of fiscal 2012. Our ratio of equity to assets was 9.25% at December 31, 2011.

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Asset Quality

The table below sets forth the amounts and categories of loans delinquent more than 30 days but less than 90 days at the dates indicated.

	December 31, 2011	September 30, 2011	December 31, 2010
		(Dollars in thousands)	
Loans 31-89 days delinquent:			
Residential mortgage	$ 1,408	$ 759	$ 2,753
Construction and Development:			
Residential and commercial	-	-	-
Commercial:			
Commercial real estate(1)	3,170	195	6,363
Other	-	22	-
Consumer:			
Home equity lines of credit	20	16	-
Second mortgages	1,182	1,701	1,779
Other	7	16	6
Total	$ 5,787	$ 2,709	$ 10,901

(1) At December 31, 2011, includes two TDRs in the aggregate amount of $1.8 million which were more than 60 days but less than 90 days past due.

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The table below sets forth our non-performing assets and performing troubled debt restructurings which were in accruing status at the dates indicated. Loans are generally placed on non-accrual status when they are 90 days or more past due as to principal or interest or when the collection of principal and/or interest becomes doubtful. There were no loans past due 90 days or more and still accruing interest at any of the dates of the table below.

	December 31, 2011	September 30, 2011	December 31, 2010
		(Dollars in thousands)	
Non-accruing loans:			
Residential mortgage	$ 2,562	$ 2,866	$ 8,865
Construction or development:			
Residential and commercial(1)	4,841	6,617	1,393
Commercial:			
Commercial real estate	1,694	1,765	4,548
Other	209	229	209
Consumer:			
Home equity lines of credit	37	61	396
Second mortgages	1,065	1,377	3,207
Other	-	-	1
Total non-accruing loans	10,408	12,915	18,619
Other real estate owned and other foreclosed assets:			
Residential mortgage	2,489	3,872	1,203
Construction or development:			
Residential and commercial	-	-	1,085
Commercial:			
Commercial real estate	3,908	4,415	585
Multi-family	-	-	550
Other	34	34	54
Total	6,431	8,321	3,477
Total non-performing assets	16,839	21,236	22,096
Performing troubled debt restructurings:			
Residential mortgage	882	1,049	2,150
Construction or development:			
Land	1,157	1,160	1,167
Commercial:			
Commercial real estate(2)	7,897	7,919	7,665
Multi-family	-	-	609
Other	175	175	176
Consumer:			
Home equity lines of credit	-	37	-
Second mortgages	-	-	113
Total	10,111	10,340	11,880
Total non-performing assets and performing troubled debt restructurings	$ 26,950	$ 31,576	$ 33,976
Ratios:			
Total non-accrual loans as a percent of gross loans	2.15 %	2.52 %	3.47 %
Total non-performing assets as a percent of total assets	2.53 %	3.19 %	3.20 %
Total non-performing assets and performing troubled	4.04 %	4.74 %	4.91 %

debt restructurings as a percent of total assets

(1) At December 31, 2011, includes two loans classified as TDRs in the aggregate amount of $1.8 million.
(2) At December 31, 2011, includes two TDRs in the aggregate amount of $1.8 million which were more than 60 days but less than 90 days past due.

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At December 31, 2011, our total non-performing assets amounted to $16.8 million, a decrease of $4.4 million compared to total non-performing assets at September 30, 2011. At December 31, 2011, the Company's total non-accruing loans amounted to $10.4 million, or 2.15% of total loans, compared to $12.9 million of non-accruing loans, or 2.52% of total loans at September 30, 2011. Included in our non-performing assets at December 31, 2011 were 12 non-accruing single family residential mortgage loans with an aggregate outstanding balance of $2.6 million at such date, and 14 non-accruing second mortgage loans and one non-accruing home equity loan, with an aggregate outstanding balance of $1.1 million. Our non-performing loans at December 31, 2011, also included the following significant items.

A $3.0 million participation interest in two construction and development loans for the construction of 64 units of a proposed 198 unit age-restricted condominium community located in Delaware County, Pennsylvania. Since the loan was originated in December 2007, a total of 64 units have been built of which 35 have been sold, with 29 units being marketed for sale. This loan was placed on non-accrual status in June 2011 and was 245 days past due at December 31, 2011. During the fiscal year ended September 30, 2011, we recorded a partial charge-off in the amount of $800,000 based on an updated appraisal, and we received principal repayments in the amount of $400,000, reducing our carrying value to $1.8 million at December 31, 2011. The borrower recently pledged additional real estate collateral as part of a loan modification plan which was signed by all parties during the December 2011 quarter. Based on the terms of the agreement, these loans have been classified as troubled debt restructurings ("TDRs"), although they remained on non-accruing and non-performing status as of December 31, 2011. These loans were performing according to the terms of the restructuring agreement at December 31, 2011, and may be returned to accruing, performing status in the event that they continue to perform in accordance with the restructured terms for a period of at least six months.

A $2.4 million participation interest in a $14.3 million construction and development loan for the development of commercial and mixed use facilities on approximately 40 acres located in Mount Laurel, New Jersey. This loan was placed on non-accrual status in June 2011 and was 276 days past due at December 31, 2011. We recorded a partial charge-off in the amount of $400,000 based on an updated appraisal during fiscal 2011. During the quarter ended December 31, 2011, we recorded an additional partial charge-off in the amount of $412,000 reducing our loan carrying value to $1.6 million. We have recently entered into a forbearance agreement with the borrower and other participants which is expected to result in the disposition of such loan during the first half of calendar year 2012 at no additional loss to us.

A $1.3 million commercial real estate loan on a mixed use (warehouse and self-storage rental units) property located in Chester County, Pennsylvania, which was placed on non-accrual status in February 2011. This loan is expected to become current during fiscal year 2012 as the borrower continues to make additional payments to bring this loan current.

For the three months ended December 31, 2011 and 2010, additional gross interest income which would have been recorded had all of our non-accruing loans been current in accordance with their original terms amounted to $178,000 and $282,000, respectively. The amount that was included in interest income on such loans was $30,000 for the three months ended December 31, 2011.

Our non-performing assets include REO in addition to non-performing loans. At December 31, 2011, our total REO amounted to $6.4 million, a decrease of $1.9 million compared to total REO at September 30, 2011. The $1.9 million decrease in REO at December 31, 2011 compared to September 30, 2011, was due to $1.9 million of sales of REO, at a net gain of $38,000, and $111,000 in reductions to REO fair values which are reflected in other REO expense during the first quarter of fiscal 2012. Our REO at December 31, 2011 included the following significant items.

Nine separate properties located in the greater Philadelphia market area which were acquired as REO in July 2011 and which previously secured three separate commercial real estate loans to one borrower with an aggregate carrying value of $3.4 million at the time of foreclosure (which was net of $658,000 in charge-offs to the ALLL taken on the loans prior to foreclosure). The properties consist of various types and usages and include an industrial building in Philadelphia used to process and fabricate marble and granite, three mixed-use (retail space and apartments) buildings in Philadelphia, one building with six retail units in Philadelphia and one mixed-use (eight apartment units and one office) in Norristown, Pennsylvania. We recorded an aggregate of $420,000 in write-downs on these properties during fiscal 2011. During the quarter ended December 31, 2011, we recorded $111,000 in additional write-downs as other real owned expense. The aggregate carrying value of these properties was $3.0 million at December 31, 2011. We are marketing these properties for sale and have sold and settled on two of such properties at no additional loss and with an aggregate sales price of $259,000, during January 2012.

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Ten separate single-family residential rental properties which previously secured loans to one borrower were acquired as real estate owned in September 2011. These properties had an aggregate carrying value in the amount of $1.5 million at December 31, 2011 Five of these properties are located in Chester, Pennsylvania, three properties are located in Claymont, Delaware, one is located in Wilmington, Delaware, and one property is located in Morgantown, Pennsylvania. These properties are in the process of being marketed for sale.

Two parcels of mixed-use real estate located in Franklin County, Pennsylvania and woodworking equipment on site was acquired as real estate owned in September 2011. This property had a carrying value $585,000 at December 31, 2011 and is expected to be sold during the March 2012 quarter at no additional loss.

While not considered non-performing, our performing troubled debt restructurings are closely monitored as they consist of loans that have been modified where the borrower is experiencing financial difficulty. Troubled debt restructurings ("TDRs") may be deemed to have a higher risk of loss than loans which have not been restructured. At December 31, 2011 our total performing troubled debt restructurings amounted to $10.1 million compared to $10.3 million of performing troubled debt restructurings at September 30, 2011. However two commercial real estate loans to the same borrower in the amount of $1.8 million and deemed to be TDRs were more than 60-days past due as of December 31, 2011. Our performing troubled debt restructurings at December 31, 2011 included the following significant items.

A total of five loans to one borrower with an aggregate outstanding balance of $786,000 at December 31, 2011 collateralized by single-family residential rental properties located primarily in Chester and Delaware Counties which were restructured during the quarter ended September 30, 2010 to require payments of interest only for six months as well as a modification to the interest rate. All of these loans have remained current under their restructured terms. During the first quarter of fiscal 2012, all of these loans resumed normal amortization of principal and interest payments under their original terms and interest rates.

Four loans to one borrower with an aggregate outstanding balance of $3.0 million at December 31, 2011 collateralized by first mortgages on commercial real estate and approved lots. Two of these loans, with an aggregate outstanding balance of $1.9 million, are secured by owner occupied commercial real estate located in Montgomery County, Pennsylvania and the other two loans, with an aggregate outstanding balance of $1.0 million, are secured by 23 acres of approved lots located in Chester County, Pennsylvania. The four loans were restructured during the quarter ended March 31, 2010 to require payments of interest only for six months and they have been performing in accordance with their terms since October 2010. The borrower is currently seeking financing at another financial institution and the Bank expects that all four loans will be repaid in full during the March 2012 quarter.

Two loans with an aggregate outstanding balance of $1.8 million at December 31, 2011 collateralized by first mortgages on four commercial real estate properties located in Pottstown, Pennsylvania. As a result of reduced net cash flows on the property due to increased vacancies, on December 1, 2010 the Bank restructured the loans to require payment of interest only until January 1, 2012, when the payments will convert to principal and interest. At December 31, 2011, these two loans were 61 days past due, however, the collateral securing the $1.3 million loan is under agreement of sale with the proceeds from the sale expected to repay the $1.3 million loan and bring the other loan current. Settlement on this sale is expected during the June 2012 quarter.

One loan to one borrower with an outstanding balance in the amount of $1.4 million at December 31, 2011 on a commercial real estate mixed use (warehouse and office space) property located in Delaware County, Pennsylvania. As a result of slow sales, the borrower was experiencing financial difficulties and on April 1, 2011 the Bank agreed to restructure the loan from its original terms to require payments of interest only until October

1, 2011. The borrower has been paying as agreed under the terms of the restructuring and began making principal and interest payments in October 2011. The borrower is expected to continue to pay as agreed.

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One commercial real estate loan to one borrower with an outstanding balance in the amount of $2.8 million at December 31, 2011 secured by a first mortgage on a 420 unit self-storage facility on approximately four acres located in Delaware County, Pennsylvania. This loan was restructured in March 2011 to require payments of interest only, at a reduced rate, for six months. A 2011 appraisal indicated that the outstanding loan balance exceeded the value of the collateral property securing this loan. We have specifically allocated $397,000 of our allowance for loan losses to this loan at December 31, 2011. Since the project was completed in April 2010, a total of 275 units have been rented, with 145 units being marketed for rent. The borrower has been paying as agreed under the terms of the restructuring of interest only payments and will convert to principal and interest payments starting April 1, 2012.

We made a credit to provision for loan losses of $300,000 for the quarter ended December 31, 2011 compared to a $1.9 million expense for the quarter ended December 31, 2010. During the quarter ended December 31, 2011, our total net charge-offs to the allowance for loan losses amounted to $786,000. Total charge-offs were $1.9 million and were offset by a $1.1 million recovery. Our charge-offs and recoveries during the December 31, 2011 quarter include the following significant items.

One $1.1 million recovery recorded upon receipt of a $2.5 million payment in full satisfaction of a $1.4 million participation interest in a construction and development loan on a retirement community located in Montgomery County, Pennsylvania.

A $428,000 partial charge-off on a $3.2 million commercial real estate loan to one borrower secured by a first mortgage on a 420 unit self-storage facility on approximately four acres located in Delaware County, Pennsylvania, reducing the carrying value of this loan at December 31, 2011 to $2.8 million Since the project was completed in April 2010, a total of 275 units have been rented, with 145 units being marketed for rent. The borrower has been paying as agreed under the terms of the restructuring of interest only payments and will convert to principal and interest payments starting April 1, 2012.

A $412,000 partial charge-off on a $2.4 million participation interest in a non-performing construction and development loan for the development of commercial and mixed use facilities on approximately 40 acres located in Mount Laurel, New Jersey, reducing our loan carrying value to $1.6 million at December 31, 2011. The lead lender and participants are continuing to work with the developer towards a satisfactory resolution of this loan. We have recently entered into a forbearance agreement which is expected to result in the disposition of such loan during the first half of calendar year 2012 at no additional loss.

In addition to the above-described items, we charged-off an aggregate of $456,000 of consumer second mortgage loans during the quarter ended December 31, 2011. The primary reason for these charge-offs, which related to a total of eight loans and which also included some short sales, was the decline in the ability of the borrower to continue to make payments and reduced property values in collateral securing these loans.

We will continue to monitor and modify our allowance for loan losses as conditions dictate. No assurances can be given that our level of allowance for loan losses will cover all of the inherent losses on our loans or that future adjustments to the allowance for loan losses will not be necessary if economic and other conditions differ substantially from the economic and other conditions used by management to determine the current level of the allowance for loan losses.

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Comparison of Operating Results for the Three Months Ended December 31, 2011 and 2010

General. Our net income was $1.3 million for the three months ended December 31, 2011 compared to net loss of $739,000 for the three months ended December 31, 2010. On a per share basis, the net income was $0.21 per share for the quarter ended December 31, 2011, compared to net loss of $0.13 per share for the quarter ended December 31, 2010. The primary reason for the $2.0 million difference in our results of operations in the first quarter of fiscal 2012 compared to the first quarter in fiscal 2011 was a decrease in the provision of loan losses of $2.2 million. Our interest rate spread of 2.86% and net interest margin of 2.96% for the three months ended December 31, 2011 improved when compared to a net interest spread of 2.83% and a net interest margin of 2.94% for the three months ended December 31, 2010.

Average Balances, Net Interest Income, and Yields Earned and Rates Paid. The following tables show for the periods indicated the total dollar amount of interest from average interest-earning assets and the resulting yields, as well as the interest expense on average interest-bearing liabilities, expressed both in dollars and rates, and the net interest margin. Tax-exempt income and yields have not been adjusted to a tax-equivalent basis. All average balances are based on monthly balances. Management does not believe that the monthly averages differ significantly from what the daily averages would be.

	Three Months Ended December 31,					
	2011			2010		
	Average Balance	Interest	Average Yield/Rate	Average Balance	Interest	Average Yield/Rate
	(Dollars in Thousands)					
Interest Earning Assets:						
Loans receivable (1)	$496,717	$6,427	5.18 %	$542,959	$7,345	5.41 %
Investment securities	83,827	436	2.08	70,970	343	1.93
Deposits in other banks	33,105	9	0.11	31,959	12	0.15
FHLB stock	5,160	-	0.00	6,345	-	0.00
Total interest-earning assets	618,809	6,872	4.44	652,233	7,700	4.72
Non-interest-earning assets	45,636			50,246		
Total assets	$664,445			$702,479		
Interest Bearing Liabilities:						
Demand and NOW accounts	$88,868	78	0.35	$87,320	171	0.78
Money market accounts	87,340	173	0.79	85,329	233	1.09
Savings accounts	44,845	12	0.11	40,932	19	0.19
Time deposits	308,364	1,590	2.06	348,288	2,028	2.33
Total deposits	529,417	1,853	1.40	561,869	2,451	1.74
FHLB borrowings	48,972	434	3.54	51,064	452	3.54
Total interest-bearing liabilities	578,389	2,287	1.58	612,933	2,903	1.89
Non-interest-bearing liabilities	24,803			23,106		
Total liabilities	603,192			636,039		
Shareholders' Equity	61,253			66,440		
Total liabilities and shareholders' equity	$664,445			$702,479		
Net interest-earning assets	$40,420			$39,300		
Net interest income; average		$4,585	2.86 %		$4,797	2.83 %

interest rate spread				
Net interest margin (2)		2.96 %		2.94 %
Average interest-earning assets to average interest-bearing liabilities	106.99 %		106.41 %	

(1) Includes non-accrual loans during the respective periods. Calculated net of deferred fees and discounts and allowance for loan losses.
(2) Equals net interest income divided by average interest-earning assets.

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Interest and Dividend Income. Our interest and dividend income decreased for the three months ended December 31, 2011 by $828,000 or 10.8% over the comparable 2011 period to $6.9 million. Interest income decreased in the three months ended December 31, 2011 over the prior comparable period in fiscal 2011 due primarily to a $918,000, or 12.5%, decrease in interest earned on loans. The decrease in interest earned on loans in the first quarter of fiscal 2012 was due primarily to both a $46.2 million, or 8.5%, decrease in the average balance of our outstanding loans and an 23 basis point decrease in the average yield earned on our loan portfolio in the first quarter of fiscal 2012 compared to the first quarter of fiscal 2011. Our interest earned on deposits in other institutions decreased by $3,000 to $9,000 in the first quarter of fiscal 2012 compared to $12,000 in the first quarter of fiscal 2011. The primary reason for the decrease in the first quarter of fiscal 2012 was a four basis point decrease in the average yield earned on deposits in other banks. Interest income on investment securities increased by $93,000, or 27.1%, in the first quarter of fiscal 2012 compared to the comparable prior fiscal year period. The increase in interest income on investment securities in the first quarter of fiscal 2012 was due to a $12.9 million, or 18.1%, increase in the average balance of our investment securities portfolio. The average yield on investment securities increased to 2.08% for the three months ended December 31, 2011 from 1.93% for the same period ended 2010.

Interest Expense. Our interest expense for the three month period ended December 31, 2011 was $2.3 million, a decrease of $616,000 from the three month period ended December 31, 2010. The reason for the decrease in interest expense in the first quarter of fiscal 2012 compared to the first quarter of fiscal 2011 was a 34 basis point decrease in average rate paid on total deposits. The average balance of our total deposits decreased by $32.5 million, or 5.8%, in the first quarter of fiscal 2012 compared to the first quarter of fiscal 2011 due primarily to a $39.9 million decrease in the average balance of certificates of deposit. The average rate paid on total deposits decreased to 1.40% for the first quarter of fiscal 2012 from 1.74% for the first quarter of fiscal 2011. Our expense on borrowings amounted to $434,000 in the first quarter of fiscal 2012 compared to $452,000 in the first quarter of fiscal 2011. The average balance of our borrowings decreased by $2.1 million in the first quarter of fiscal 2012 compared to the first quarter of fiscal 2011. The average rate paid on borrowed funds of 3.54% in the first quarter of fiscal 2012 was unchanged when compared to the first quarter of fiscal 2011.

Provision for Loan Losses. We recorded a credit of $300,000 to the provision for loan losses for the three months ended December 31, 2011 compared to a $1.9 million expense for the three months ended December 31, 2010. The $2.2 million difference in the provision for loan losses in fiscal 2012 was due primarily to a $1.1 million recovery recorded upon receipt of a $2.5 million payment in full satisfaction of a $1.4 million participation interest in a construction and development loan on a retirement community located in Montgomery County, Pennsylvania, as well as an overall improvement in the trend of our level of problem assets. Our net charge-offs to the allowance for loan losses for the three months ended December 31, 2011 amounted to approximately $786,000 compared to $2.5 million during the first quarter of fiscal 2011. At December 31, 2011, the Company's total non-performing assets and performing troubled debt restructurings totaled $27.0 million compared to $31.6 million at September 30, 2011. As of December 31, 2011, the balance of the allowance for loan losses was $9.0 million, or 1.86% of gross loans and 86.62% of non-accruing loans, compared to an allowance for loan losses of $10.1 million or 1.97% of gross loans and 78.21% of non-accruing loans at September 30, 2011. The $300,000 credit to the provision for loan losses made in the first quarter of fiscal 2012 reflected management's assessment, based on the information available at the time, of the inherent level of estimable losses in our loan portfolio.

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The following table sets forth an analysis of our allowance for loan losses for the periods indicated.

	For the three Months Ended December 31, 2011	For the three Months Ended December 31, 2010	For the Year Ended September 30, 2011
	(Dollars in Thousands)		
Balance at beginning of period	$ 10,101	$ 8,157	$ 8,157
(Credit) provision for loan losses	(300)	1,900	12,392
Charge-offs:			
Residential mortgage	475	429	2,478
Construction and development			
Residential and commercial	412	107	1,307
Commercial:			
Commercial real estate	494	284	2,460
Multi-family	-	164	164
Other	88	-	278
Consumer:			
Home equity lines of credit	36	99	166
Second mortgages	456	1,448	3,691
Other	16	-	6
Total charge-offs	1,977	2,531	10,550
Recoveries:			
Residential mortgage	-	-	1
Construction and development			
Residential and commercial	1,139	-	-
Commercial:			
Commercial real estate	-	1	1
Multi-family	-	1	1
Other	1	1	5
Consumer:			
Home equity lines of credit	-	-	3
Second mortgages	50	17	82
Other	1	3	9
Total recoveries	1,191	23	102
Net charge-offs	786	2,508	10,448
Balance at end of period	$ 9,015	$ 7,549	$ 10,101
Ratios:			
Ratio of allowance for loan losses to non-accrual loans	86.62 %	40.54 %	78.21 %
Ratio of net charge-offs to average loans outstanding, Annualized for the three-month periods ended December 31, 2011 and 2010	0.64 %	1.84 %	1.97 %
Ratio of net charge-offs to total allowance for loan losses (annualized for the three-month periods ended	34.88 %	132.88 %	103.43 %

December 31, 2011 and 2010)

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Other Income. Our other, or non-interest, income increased by $549,000, or 130.4%, to $970,000 for the three months ended December 31, 2011 compared to $421,000 for the three months ended December 31, 2010. The increase in other income during the first quarter of fiscal 2012 was due primarily to a $415,000 gain recorded on the securitization and sale of $10.7 million of long-term, fixed-rate residential mortgage loans. In addition, we recorded a net gain on the sale of other real estate owned in the amount of $38,000 in the quarter ended December 31, 2011, an improvement of $64,000 over the $26,000 net loss recorded in the fiscal 2011 quarter.

Other Expenses. Our other, or non-interest, expenses decreased by $459,000, or 10.2%, to $4.0 million in the quarter ended December 31, 2011 compared to $4.5 million for the three months ended December 31, 2010. The decrease in other operating expenses in the first quarter of fiscal 2012 compared to the first quarter of fiscal 2011 was due primarily to a $404,000 decrease in other real estate owned expense and a $151,000 decrease in federal deposit insurance premiums, due to a lower deposit base in fiscal 2012. These decreases were partially offset by a $74,000 increase in salaries and employee benefits in the December 31, 2011 compared to the quarter ended December 31, 2010.

Income Tax Expense. Our income tax expense was $560,000 for the three months ended December 31, 2011 compared to income tax benefit of $446,000 for the three months ended December 31, 2010. The increased income tax expense for the quarter ended December 31, 2011 was primarily due to a $3.0 increase in pre-tax income during the quarter ended December 31, 2011. Our effective Federal tax rate was 30.9% and 37.7% for the three months ended December 31, 2011 and 2010, respectively.

As of December 31, 2011, after careful analysis, management determined that the net deferred tax asset, more likely than not, was realizable, and therefore no additional valuation allowance was required aside from the $296,000 state net operating loss allowance as of September 30, 2011. In reaching this conclusion positive and negative evidence were both carefully considered. It is management's belief that the net losses reported for fiscal year end 2010 and 2011 are temporary and were a direct result of the poor economy and are not reflective our ability to be profitable in current and future periods, provided there is stability its asset values. The Company has shown improvement for the first quarter fiscal year 2012, reporting net income for the quarter.

Liquidity and Capital Resources

Our primary sources of funds are from deposits, FHLB borrowings, amortization of loans, loan prepayments and the maturity of loans, mortgage-backed securities and other investments, and other funds provided from operations. While scheduled payments from the amortization of loans and mortgage-backed securities and maturing investment securities are relatively predictable sources of funds, deposit flows and loan prepayments can be greatly influenced by general interest rates, economic conditions and competition. We also maintain excess funds in short-term, interest-bearing assets that provide additional liquidity. At December 31, 2011, our cash and cash equivalents amounted to $57.8 million. In addition, at such date our available for sale investment securities amounted to $81.2 million.

In addition to cash flow from loan and securities payments and prepayments as well as from sales of available for sale securities, we have significant borrowing capacity available to fund liquidity needs. In recent years we have utilized borrowings as a cost efficient addition to deposits as a source of funds. Our borrowings consist primarily of advances from the Federal Home Loan Bank of Pittsburgh, of which we are a member. Under terms of the collateral agreement with the Federal Home Loan Bank, we pledge residential mortgage loans and mortgage-backed securities as well as our stock in the Federal Home Loan Bank as collateral for such advances.

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We use our liquidity to fund existing and future loan commitments, to fund maturing certificates of deposit and demand deposit withdrawals, to invest in other interest-earning assets, and to meet operating expenses. At December 31, 2011, we had certificates of deposit maturing within the next 12 months amounting to $85.1 million. Based upon historical experience, we anticipate that a significant portion of the maturing certificates of deposit will be remaining with us. For the three months ended December 31, 2011, the average balance of our outstanding FHLB advances was $49.0 million. At December 31, 2011, we had $48.8 million in outstanding long-term FHLB advances and we had $318.2 million in potential FHLB advances available to us. In addition, at December 31, 2011, we had $50.0 million available pursuant to an existing line of credit with the FHLB.

The following table summarizes our contractual cash obligations at December 31, 2011.

	Payments Due by Period				
	To One Year	After One to Three Years	After Three to Five Years	After Five Years	Total
	(Dollars in Thousands)				
Long-term debt obligations	$-	$846	$-	$48,000	$48,846
Certificates of deposit	85,117	144,059	37,119	40,342	306,637
Operating lease obligations	279	558	431	4,714	5,982
Total contractual obligations	$85,396	$145,463	$37,550	$93,056	$361,465

We anticipate that we will continue to have sufficient funds and alternative funding sources to meet our current commitments.

Impact of Inflation and Changing Prices

The financial statements, accompanying notes, and related financial data of the Company presented herein have been prepared in accordance with generally accepted accounting principles, which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of operations. Most of our assets and liabilities are monetary in nature; therefore, the impact of interest rates has a greater impact on our performance than the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

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Item 3 - Quantitative and Qualitative Disclosures About Market Risk

For a discussion of the Company's asset and liability management policies as well as the methods used to manage its exposure to the risk of loss from adverse changes in market prices and rates market, see Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations – How We Manage Market Risk" in the Company's Annual Report on Form 10-K for the year ended September 30, 2011. There has been no material change in the Company's asset and liability position since September 30, 2011.

Item 4. Controls and Procedures

Our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and regulations and are operating in an effective manner.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) or 15(d)-15(f) under the Securities Exchange Act of 1934) occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1 - Legal Proceedings

On January 12, 2012, Stilwell Value Partners VI, L.P., withdrew the lawsuit it had previously filed against the Company, the Mutual Holding Company and each of their directors pursuant to a Praecipe to Discontinue filed in the Court of Common Pleas of Chester County, Pennsylvania. Stilwell Value Partners VI, L.P. v. Hughes, et al.

Item 1A - Risk Factors

See Item 1A, "Risk Factors" in the Company's Annual Report on Form 10-K for the year ended September 30, 2011. There have been no material changes from the risk factors previously disclosed in the Company's Annual Report on Form 10-K for the year ended September 30, 2011.

Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds

(a)	Not applicable
(b)	Not applicable
(c)	Purchases of Equity Securities

Not applicable

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Item 3 - Defaults Upon Senior Securities

There are no matters required to be reported under this item.

Item 4 - Mine Safety Disclosure

There are no matters required to be reported under this item.

Item 5 - Other Information

There are no matters required to be reported under this item.

Item 6 - Exhibits

31.1	Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Section 302 Certification of the Chief Financial Officer
32.1	Section 1350 Certification

The following Exhibits are being furnished* as part of this report:

No.	Description
101.INS	XBRL Instance Document.*
101.SCH	XBRL Taxonomy Extension Schema Document.*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.*
101.DEF	XBRL Taxonomy Extension Definitions Linkbase Document.*

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*These interactive data files are being furnished as part of this Quarterly Report, and, in accordance with Rule 402 of Regulation S-T, shall not be deemed filed for purposes of Section 11 or 12 of the Securities Act of 1933, as amended, or Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to liability under those sections.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

	MALVERN FEDERAL BANCORP, INC.
February 14, 2012	By: /s/ Ronald Anderson Ronald Anderson President and Chief Executive Officer
February 14, 2012	By: /s/ Dennis Boyle Dennis Boyle Senior Vice President and Chief Financial Officer