PRUDENTIAL BANCORP INC OF PENNSYLVANIA
Form 10-Q
May 15, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 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 March 31, 2013

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: 000-51214

Prudential Bancorp, Inc. of Pennsylvania
(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| Pennsylvania | 68-0593604 |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification No.) |
| 1834 Oregon Avenue<br>Philadelphia, Pennsylvania<br>(Address of Principal Executive Offices) | 19145<br>Zip Code |

(215) 755-1500
(Registrant's Telephone Number, Including Area Code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

| | |
|---|---|
| Large accelerated filer o | Accelerated filer o |
| Non-accelerated filer o (Do not check if a smaller | Smaller reporting company x |

reporting company)

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practical date: as of May 1, 2013, 10,023,495 shares were issued and outstanding.

PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA

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PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

| | March 31, 2013 | September 30, 2012 |
|---|---|---|
| | (Dollars in Thousands) | |
| ASSETS | | |
| Cash and amounts due from depository institutions | $2,445 | $ 3,001 |
| Interest-bearing deposits | 31,167 | 78,272 |
| Total cash and cash equivalents | 33,612 | 81,273 |
| Investment and mortgage-backed securities available for sale (amortized cost—March 31, 2013, $61,330; September 30, 2012, $64,030) | 62,715 | 65,975 |
| Investment and mortgage-backed securities held to maturity (estimated fair value—March 31, 2013, $90,182; September 30, 2012, $66,401) | 87,976 | 63,110 |
| Loans receivable—net of allowance for loan losses (March 31, 2013, $2,512; September 30, 2012, $1,881) | 278,237 | 260,684 |
| Accrued interest receivable | 1,833 | 1,661 |
| Real estate owned | 1,258 | 1,972 |
| Federal Home Loan Bank stock—at cost | 1,659 | 2,239 |
| Office properties and equipment—net | 1,565 | 1,688 |
| Bank owned life insurance | 7,022 | 6,919 |
| Prepaid expenses and other assets | 1,258 | 2,234 |
| Deferred tax asset-net | 1,968 | 2,749 |
| TOTAL ASSETS | $479,103 | $ 490,504 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| LIABILITIES: | | |
| Deposits: | | |
| Noninterest-bearing | $3,116 | $ 3,711 |
| Interest-bearing | 412,981 | 421,891 |
| Total deposits | 416,097 | 425,602 |
| Advances from Federal Home Loan Bank | 340 | 483 |
| Accrued interest payable | 747 | 2,382 |
| Advances from borrowers for taxes and insurance | 1,266 | 1,273 |
| Accounts payable and accrued expenses | 473 | 933 |
| Total liabilities | 418,923 | 430,673 |
| STOCKHOLDERS' EQUITY: | | |
| Preferred stock, $.01 par value, 10,000,000 shares authorized, none issued | - | - |
| Common stock, $.01 par value, 40,000,000 shares authorized, issued 12,563,750; outstanding - 10,023,495 at March 31, 2013 and September 30, 2012 | 126 | 126 |
| Additional paid-in capital | 54,932 | 54,610 |
| Unearned ESOP shares | (2,676 ) | (2,787 ) |
| Treasury stock, at cost: 2,540,255 shares at March 31, 2013 and September 30, 2012 | (31,625 ) | (31,625 ) |

| | | |
|---|---|---|
| Retained earnings | 38,510 | 38,224 |
| Accumulated other comprehensive income | 913 | 1,283 |
| Total stockholders' equity | 60,180 | 59,831 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | $479,103 | $ 490,504 |

See notes to unaudited consolidated financial statements.

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PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

| | Three Months Ended March 31, | | Six Months Ended March 31, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (Dollars in Thousands Except Per Share Amounts) | | (Dollars in Thousands Except Per Share Amounts) | |
| INTEREST INCOME: | | | | |
| Interest on loans | $ 3,135 | $ 3,251 | $ 6,388 | $ 6,519 |
| Interest on mortgage-backed securities | 544 | 975 | 1,178 | 2,019 |
| Interest and dividends on investments | 552 | 558 | 1,028 | 1,203 |
| Interest on interest-bearing assets | 22 | 29 | 56 | 55 |
| Total interest income | 4,253 | 4,813 | 8,650 | 9,796 |
| INTEREST EXPENSE: | | | | |
| Interest on deposits | 1,139 | 1,492 | 2,359 | 3,005 |
| Interest on borrowings | - | 1 | - | 2 |
| Total interest expense | 1,139 | 1,493 | 2,359 | 3,007 |
| NET INTEREST INCOME | 3,114 | 3,320 | 6,291 | 6,789 |
| PROVISION FOR LOAN LOSSES | - | 100 | - | 250 |
| NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES | 3,114 | 3,220 | 6,291 | 6,539 |
| NON-INTEREST INCOME: | | | | |
| Fees and other service charges | 98 | 107 | 195 | 223 |
| Gain on sale of securities available for sale | - | - | 16 | - |
| Total other-than-temporary impairment losses | (5) | (6) | (25) | (150) |
| Portion of loss recognized in other comprehensive income, before taxes | (1) | (60) | 5 | 47 |
| Net impairment losses recognized in earnings | (6) | (66) | (20) | (103) |
| Other | 107 | 92 | 223 | 186 |
| Total non-interest income | 199 | 133 | 414 | 306 |
| NON-INTEREST EXPENSE: | | | | |
| Salaries and employee benefits | 1,499 | 1,579 | 2,958 | 3,098 |
| Data processing | 114 | 112 | 223 | 220 |
| Professional services | 261 | 351 | 444 | 571 |
| Office occupancy | 95 | 100 | 192 | 199 |

| | | | | |
|---|---|---|---|---|
| Depreciation | 86 | 87 | 172 | 171 |
| Payroll taxes | 117 | 103 | 188 | 167 |
| Director compensation | 74 | 88 | 172 | 195 |
| Deposit insurance | 157 | 164 | 319 | 326 |
| Real estate owned expense | 273 | 79 | 386 | 231 |
| Advertising | 69 | 27 | 156 | 92 |
| Other | 368 | 306 | 672 | 593 |
| Total non-interest expense | 3,113 | 2,996 | 5,882 | 5,863 |
| INCOME BEFORE INCOME TAXES | 200 | 357 | 823 | 982 |
| INCOME TAXES: | | | | |
| Current (benefit) expense | (488) | 94 | (435) | 505 |
| Deferred expense (benefit) | 674 | 179 | 972 | (11) |
| Total income tax expense | 186 | 273 | 537 | 494 |
| NET INCOME | $ 14 | $ 84 | $ 286 | $ 488 |
| BASIC EARNINGS PER SHARE | $ 0.00 | $ 0.01 | $ 0.03 | $ 0.05 |
| DILUTED EARNINGS PER SHARE | $ 0.00 | $ 0.01 | $ 0.03 | $ 0.05 |

See notes to unaudited consolidated financial statements.

PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| | Three months ended March 31, | | Six months ended March 31, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (Dollars in Thousands) | | (Dollars in Thousands) | |
| Net income | $ 14 | $ 84 | $ 286 | $ 488 |
| Unrealized holding loss on available-for-sale securities | (222) | (12) | (564) | (115) |
| Tax effect | 76 | 4 | 192 | 39 |
| Reclassification adjustment for net gains realized in net income | - | - | (16) | - |
| Tax effect | - | - | 5 | - |
| Reclassification adjustment for other than temporary impairment losses on debt securities | 6 | 66 | 20 | 103 |
| Tax effect | (2) | (22) | (7) | (35) |
| Total Other Comprehensive (Loss) Income | (142) | 36 | (370) | (8) |
| Comprehensive (Loss) Income | $ (128) | $ 120 | $ (84) | $ 480 |

See notes to unaudited consolidated financial statements

PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

| | Common Stock | Additional Paid-In Capital | Unearned ESOP Shares | Treasury Stock | Retained Earnings | Accumulated Other Comprehensive Income | Total Stockholders' Equity |
|---|---|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | | | |
| BALANCE, OCTOBER 1, 2012 | $ 126 | $ 54,610 | $ (2,787 ) | $ (31,625 ) | $ 38,224 | $ 1,283 | $ 59,831 |
| Net income | | | | | 286 | | 286 |
| Other comprehensive loss | | | | | | (370 ) | (370 ) |
| Excess tax benefit from stock compensation plans | | 43 | | | | | 43 |
| Stock option expense | | 116 | | | | | 116 |
| Recognition and Retention Plan expense | | 195 | | | | | 195 |
| ESOP shares committed to be released (11,310 shares) | | (32 ) | 111 | | | | 79 |
| BALANCE, March 31, 2013 | $ 126 | $ 54,932 | $ (2,676 ) | $ (31,625 ) | $ 38,510 | $ 913 | $ 60,180 |

| | Common Stock | Additional Paid-In Capital | Unearned ESOP Shares | Treasury Stock | Retained Earnings | Accumulated Other Comprehensive Income | Total Stockholders' Equity |
|---|---|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | | | |
| BALANCE, OCTOBER 1, 2011 | $ 126 | $ 54,078 | $ (3,011 ) | $ (31,625 ) | $ 35,631 | $ 2,253 | $ 57,452 |
| Net income | | | | | 488 | | 488 |
| Other comprehensive loss | | | | | | (8 ) | (8 ) |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Excess tax benefit from stock compensation plans | | 9 | | | | | 9 |
| Stock option expense | | 110 | | | | | 110 |
| Recognition and Retention Plan expense | | 197 | | | | | 197 |
| ESOP shares committed to be released (11,310 shares) | | (52 ) | 112 | | | | 60 |
| BALANCE, March 31, 2012 | $ 126 | $ 54,342 | $ (2,899 ) | $ (31,625 ) | $ 36,119 | $ 2,245 | $ 58,308 |

See notes to unaudited consolidated financial statements

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PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Six Months Ended March 31, 2013 | 2012 |
|---|---|---|
| | (Dollars in Thousands) | |
| OPERATING ACTIVITIES: | | |
| Net income | $ 286 | $ 488 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Provision for loan losses | - | 250 |
| Depreciation | 172 | 171 |
| Net accretion of premiums/discounts | (67) | (188) |
| Net accretion of deferred loan fees and costs | (53) | (102) |
| Impairment charge on investment and mortgage-backed securities | 20 | 103 |
| Gain on sale of investment and mortgage-backed securities | (16) | - |
| Share-based compensation expense | 354 | 316 |
| Loss on sale of real estate owned | 16 | 123 |
| Compensation expense of ESOP | 79 | 60 |
| Deferred income tax benefit (expense) | 973 | (11) |
| Changes in assets and liabilities which used cash: | | |
| Accrued interest receivable | (172) | 236 |
| Prepaid expenses and other assets | 1,136 | 310 |
| Accrued interest payable | (1,635) | (1,404) |
| Accounts payable and accrued expenses | (460) | (1,463) |
| Net cash provided by (used in) operating activities | 633 | (1,111) |
| INVESTING ACTIVITIES: | | |
| Purchase of investment and mortgage-backed securities held to maturity | (33,454) | (33,962) |
| Purchase of investment and mortgage-backed securities available for sale | (7,968) | (18,897) |
| Loans originated or acquired | (43,497) | (26,537) |
| Principal collected on loans | 16,521 | 28,470 |
| Principal payments received on investment and mortgage-backed securities: | | |
| Held-to-maturity | 8,606 | 45,721 |
| Available-for-sale | 10,407 | 11,770 |
| Proceeds from redemptiom of FHLB stock | 580 | 281 |
| Proceeds from sale of investment and mortgage-backed securities | 304 | - |
| Proceeds from sale of loans | 9,240 | - |
| Proceeds from sale of real estate owned | 628 | 186 |
| Purchases of equipment | (49) | (144) |
| Net cash (used in) provided by investing activities | (38,682) | 6,888 |
| FINANCING ACTIVITIES: | | |
| Net increase (decrease) in demand deposits, NOW accounts, and savings accounts | 1,689 | (2,083) |
| Net (decrease) increase in certificates of deposit | (11,194) | 4,432 |
| Repayment of advances from Federal Home Loan Bank | (143) | (19) |
| Decreases in advances from borrowers for taxes and insurance | (7) | (54) |
| Excess tax benefit related to stock compensation plans | 43 | 9 |
| Net cash (used in) provided by financing activities | (9,612) | 2,285 |

| | | |
|---|---|---|
| NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS | (47,661 ) | 8,062 |
| CASH AND CASH EQUIVALENTS—Beginning of period | 81,273 | 53,829 |
| CASH AND CASH EQUIVALENTS—End of period | $ 33,612 | $ 61,891 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION: | | |
| Interest paid on deposits and advances from Federal Home Loan Bank | $ 3,994 | $ 4,411 |
| Income taxes paid | $ - | $ 1,305 |
| SUPPLEMENTAL DISCLOSURES OF NONCASH ITEMS: | | |
| Real estate acquired in settlement of loans | $ 236 | $ 199 |

See notes to unaudited consolidated financial statements.

PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation –The accompanying unaudited consolidated financial statements were prepared pursuant to the rules and regulations of the United States Securities and Exchange Commission ("SEC") for interim information and therefore do not include all the information or footnotes necessary for a complete presentation of financial condition, results of operations, changes in equity and cash flows in conformity with accounting principles generally accepted in the United States of America ("GAAP"). However, all normal recurring adjustments that, in the opinion of management, are necessary for a fair presentation of the financial statements have been included. The results for the six months ended March 31, 2013 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2013, or any other period. These financial statements should be read in conjunction with the audited consolidated financial statements of Prudential Bancorp, Inc. of Pennsylvania (the "Company") and the accompanying notes thereto for the year ended September 30, 2012 included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2012.

Use of Estimates in the Preparation of Financial Statements—The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the 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. The most significant estimates and assumptions in the Company's consolidated financial statements are recorded in the allowance for loan losses, deferred income taxes, other-than-temporary impairment, and the fair value measurement for financial instruments. Actual results could differ from those estimates.

Employee Stock Ownership Plan – The Company maintains an employee stock ownership plan ("ESOP") for substantially all of its full-time employees. The ESOP purchased 452,295 shares of the Company's common stock for an aggregate cost of approximately $4.5 million in fiscal 2005. Shares of the Company's common stock purchased by the ESOP are held in a suspense account until released for allocation to participants. Shares are allocated to each eligible participant based on the ratio of each such participant's compensation, as defined in the ESOP, to the total compensation of all eligible plan participants. As the unearned shares are released from the suspense account, 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 equity as additional paid-in capital. As of March 31, 2013, the Company had allocated a total of 175,305 shares from the suspense account to participants and committed to release an additional 5,655 shares. For the six months ended March 31, 2013, the Company recognized $79,000 in compensation expense related to the ESOP.

Share-Based Compensation – The Company accounts for stock-based compensation issued to employees, and where appropriate, non-employees, at fair value. Under fair value provisions, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the appropriate vesting period using the straight-line method. The amount of stock-based compensation recognized at any date must at least equal the portion of the grant date fair value of the award that is vested at that date and as a result it may be necessary to recognize the expense using a ratable method. Determining the fair value of stock-based awards at the date of grant requires judgment, including estimating the expected term of the stock options and the expected volatility of the Company's stock. In addition, judgment is required in estimating the amount of stock-based awards that are expected to be forfeited. If actual results differ significantly from these estimates or different key assumptions were used, it could have a material effect on the Company's consolidated financial statements.

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Dividends with respect to non-vested share awards are held by the Company's Recognition and Retention Plan ("Plan") Trust (the "Trust") for the benefit of the recipients and are paid out proportionately by the Trust to the recipients of stock awards granted pursuant to the Plan as soon as practicable after the stock awards are earned.

Treasury Stock – Stock held in treasury by the Company is accounted for using the cost method, which treats stock held in treasury as a reduction to total stockholders' equity. The average cost per share of the approximately 2.5 million shares which have been repurchased by the Company was $12.45 for purchases through March 31, 2013. The repurchased shares are available for general corporate purposes. As of March 31, 2013, Prudential Mutual Holding Company ("the MHC") had purchased 568,000 shares at an average cost of $10.30 per share. These shares remain issued and outstanding. As of March 31, 2013, 7,478,062 shares were owned by the MHC, 2,540,255 shares had been repurchased by the Company and were held as treasury stock with the remaining 2,545,433 shares owned by public shareholders.

FHLB Stock – FHLB stock is classified as a restricted equity security because ownership is restricted and there is not an established market for its resale. FHLB stock is carried at cost and is evaluated for impairment when certain conditions warrant further consideration.

The Company is a member of the Federal Home Loan Bank of Pittsburgh and as such, is required to maintain a minimum investment in stock of the Federal Home Loan Bank that varies with the level of advances outstanding from the Federal Home Loan Bank. The stock is bought from and sold to the Federal Home Loan Bank based upon its $100 par value. The FHLB stock does not have a readily determinable fair value and as such is classified as restricted stock, carried at cost and evaluated for impairment by management. The stock's value is determined by the ultimate recoverability of the par value rather than by recognizing temporary declines. The determination of whether the par value will ultimately be recovered is influenced by criteria such as the following: (a) the significance of the decline in net assets of the Federal Home Loan Bank as compared to the capital stock amount and the length of time this situation has persisted; (b) commitments by the Federal Home Loan Bank to make payments required by law or regulation and the level of such payments in relation to the operating performance; (c) the impact of legislative and regulatory changes on the customer base of the Federal Home Loan Bank; and (d) the liquidity position of the Federal Home Loan Bank.

While the Federal Home Loan Banks have been negatively impacted by the current economic conditions, the Federal Home Loan Bank of Pittsburgh reported profits for 2012, remains in compliance with regulatory capital and liquidity requirements and makes redemptions at the par value. With consideration given to these factors, management concluded that the FHLB stock was not impaired at March 31, 2013.

Recent Accounting Pronouncements

In February 2013, the FASB issued ASU 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. The amendments in this Update require an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. For public entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2012. For nonpublic entities, the amendments are effective prospectively for reporting periods beginning after December 15, 2013. Early adoption is permitted. The Unaudited Consolidated Statement of Comprehensive Income is included in the financial statements presented herein.

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2. EARNINGS PER SHARE

Basic earnings per common share is computed by dividing net income available to common shareholders by the weighted average number of shares of common stock outstanding, net of any treasury shares, during the period. Diluted earnings per share is calculated by dividing net income available to common shareholders by the weighted average number of shares of common stock outstanding, net of any treasury shares, after consideration of the potential dilutive effect of common stock equivalents, based upon the treasury stock method using an average market price for the period.

The calculated basic and diluted earnings per share are as follows:

| | Quarter Ended March 31, | | | |
|---|---|---|---|---|
| | 2013 | | 2012 | |
| | Basic | Diluted | Basic | Diluted |
| | (Dollars in Thousands Except Per Share Data) | | | |
| Net income | $ 14 | $ 14 | $ 84 | $ 84 |
| Weighted average shares outstanding | 9,661,894 | 9,661,894 | 9,603,916 | 9,603,916 |
| Effect of common stock equivalents | - | 93,609 | - | 8,733 |
| Adjusted weighted average shares used in earnings per share computation | 9,661,894 | 9,755,503 | 9,603,916 | 9,612,649 |
| Earnings per share - basic and diluted | $ 0.00 | $ 0.00 | $ 0.01 | $ 0.01 |

| | Six Months Ended March 31, | | | |
|---|---|---|---|---|
| | 2013 | | 2012 | |
| | Basic | Diluted | Basic | Diluted |
| | (Dollars in Thousands Except Per Share Data) | | | |
| Net income | $ 286 | $ 286 | $ 488 | $ 488 |
| Weighted average shares outstanding | 9,642,156 | 9,642,156 | 9,584,075 | 9,584,075 |
| Effect of common stock equivalents | - | 92,389 | - | 11,363 |
| Adjusted weighted average shares used in earnings per share computation | 9,642,156 | 9,734,545 | 9,584,075 | 9,595,438 |
| Earnings per share - basic and diluted | $ 0.03 | $ 0.03 | $ 0.05 | $ 0.05 |

At March 31, 2013 and 2012, there were anti-dilutive shares of 554,596 and 442,400, respectively. The exercise price for the stock options representing the anti-dilutive shares ranged from $7.25 to $11.17.

3. ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table presents the changes in accumulated other comprehensive income by component net of tax for the six months ended March 31, 2013:

| | Unrealized gains on available for sale securities (a) |
|---|---|
| Balance as of September 30, 2012 | $ 1,945 |
| Other comprehensive loss before reclassification | (564) |
| Amount reclassified from accumulated other comprehensive income | 4 |
| Total other comprehensive loss | (560) |
| Balance as of March 31, 2013 | $ 1,385 |

(a) All amounts are net of tax. Amounts in parentheses indicate debits.

The following table presents significant amounts reclassified out of each component of accumulated other comprehensive income for the six months ended March 31, 2013:

| Details about other comprehensive income | Amount Reclassified from Accumulated Other Comprehensive Income (a) | Affected Line Item in the Statement Where Net Income is Presented |
|---|---|---|
| Unealized gains on available for sale securities | | |
| | $ 16 | Gain on sale of securities avaiable for sale |
| | (5) | Income taxes |
| | (20) | Net impairment losses recognized in earnings |
| | 7 | Income taxes |
| | $ (2) | Net of tax |

(a) Amounts in parentheses indicate debits to net income

4. INVESTMENT AND MORTGAGE-BACKED SECURITIES

The amortized cost and fair value of investment and mortgage-backed securities, with gross unrealized gains and losses, are as follows:

| | March 31, 2013 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| | | (Dollars in Thousands) | | |
| Securities Available for Sale: | | | | |
| U.S. government and agency obligations | $ 19,985 | $ 69 | $ (97 ) | $ 19,957 |
| Mortgage-backed securities - U.S. government agencies | 37,632 | 1,355 | (39 ) | 38,948 |
| Mortgage-backed securities - non-agency | 3,707 | 215 | (130 ) | 3,792 |
| Total debt securities available for sale | 61,324 | 1,639 | (266 ) | 62,697 |
| FHLMC preferred stock | 6 | 12 | - | 18 |
| Total securities available for sale | $ 61,330 | $ 1,651 | $ (266 ) | $ 62,715 |
| Securities Held to Maturity: | | | | |
| U.S. government and agency obligations | $ 71,932 | $ 1,064 | $ (364 ) | $ 72,632 |
| Mortgage-backed securities - U.S. government agencies | 16,044 | 1,511 | (5 ) | 17,550 |
| Total securities held to maturity | $ 87,976 | $ 2,575 | $ (369 ) | $ 90,182 |

| | September 30, 2012 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| | | (Dollars in Thousands) | | |
| Securities Available for Sale: | | | | |
| U.S. government and agency obligations | $ 13,994 | $ 110 | $ (1 ) | $ 14,103 |
| Mortgage-backed securities - U.S. government agencies | 45,722 | 2,040 | - | 47,762 |
| Mortgage-backed securities - non-agency | 4,308 | 137 | (342 ) | 4,103 |
| Total debt securities available for sale | 64,024 | 2,287 | (343 ) | 65,968 |
| FHLMC preferred stock | 6 | 1 | - | 7 |
| Total securities available for sale | $ 64,030 | $ 2,288 | $ (343 ) | $ 65,975 |
| Securities Held to Maturity: | | | | |
| U.S. government and agency obligations | $ 44,475 | $ 1,333 | $ (9 ) | $ 45,799 |
| Mortgage-backed securities - U.S. government agencies | 18,635 | 1,967 | - | 20,602 |
| Total securities held to maturity | $ 63,110 | $ 3,300 | $ (9 ) | $ 66,401 |

The following table shows the gross unrealized losses and related fair values of the Company's investment securities, aggregated by investment category and length of time that individual securities had been in a continuous loss position at March 31, 2013:

| | Less than 12 months | | More than 12 months | | Total | |
|---|---|---|---|---|---|---|
| | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value |
| | | | (Dollars in Thousands) | | | |
| Securities Available for Sale: | | | | | | |
| U.S. government and agency obligations | $ (97 ) | $ 8,894 | $ - | $ - | $ (97 ) | $ 8,894 |
| Mortgage-backed securities - U.S. government agencies | (39 ) | 1,941 | - | - | (39 ) | 1,941 |
| Mortgage-backed securities - non-agency | (4 ) | - | (126 ) | 867 | (130 ) | 867 |
| Total securities available for sale | $ (140 ) | $ 10,835 | $ (126 ) | $ 867 | $ (266 ) | $ 11,702 |
| Securities Held to Maturity: | | | | | | |

| | | | | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| U.S. government and agency obligations | $ | (364 | ) | $ | 36,597 | $ | - | | $ | - | $ | (364 | ) | $ | 36,597 |
| Mortgage-backed securities - U.S. government agencies | | (5 | ) | | 2,471 | | - | | | - | | (5 | ) | | 2,471 |
| Total securities held to maturity | $ | (369 | ) | $ | 39,068 | $ | - | | $ | - | $ | (369 | ) | $ | 39,068 |
| Total | $ | (509 | ) | $ | 49,903 | $ | (126 | ) | $ | 867 | $ | (635 | ) | $ | 50,770 |

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The following table shows the gross unrealized losses and related fair values of the Company's investment securities, aggregated by investment category and length of time that individual securities had been in a continuous loss position at September 30, 2012:

| | Less than 12 months | | More than 12 months | | Total | |
|---|---|---|---|---|---|---|
| | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value |
| | | | (Dollars in Thousands) | | | |
| Securities Available for Sale: | | | | | | |
| U.S. government and agency obligations | $ (1 ) | $ 2,999 | $ - | $ - | $ (1 ) | $ 2,999 |
| Mortgage-backed securities - non-agency | (21 ) | 144 | (321 ) | 2,343 | (342 ) | 2,487 |
| Total securities available for sale | $ (22 ) | $ 3,143 | $ (321 ) | $ 2,343 | $ (343 ) | $ 5,486 |
| Securities Held to Maturity: | | | | | | |
| U.S. government and agency obligations | $ (9 ) | $ 10,982 | $ - | $ - | $ (9 ) | $ 10,982 |
| Total securities held to maturity | $ (9 ) | $ 10,982 | $ - | $ - | $ (9 ) | $ 10,982 |
| Total | $ (31 ) | $ 14,125 | $ (321 ) | $ 2,343 | $ (352 ) | $ 16,468 |

Management evaluates securities for other-than-temporary impairment ("OTTI") at least once each quarter, and more frequently when economic or market concerns warrant such evaluation. The Company determines whether the unrealized losses are temporary. The evaluation is based upon factors such as the creditworthiness of the issuers/guarantors, the underlying collateral, if applicable, and the continuing performance of the securities. Management also evaluates other facts and circumstances that may be indicative of an OTTI condition. This includes, but is not limited to, an evaluation of the type of security, the length of time and extent to which the fair value of the security has been less than cost, and the near-term prospects of the issuer.

The Company assesses whether a credit loss existed with respect to a security by considering whether (1) the Company has the intent to sell the security, (2) it is more likely than not that it will be required to sell the security before recovery, or (3) it does not expect to recover the entire amortized cost basis of the security. The Company bifurcates the OTTI impact on impaired securities where impairment in value was deemed to be other than temporary between the component representing credit loss and the component representing loss related to other factors. The portion of the fair value decline attributable to credit loss must be recognized through a charge to earnings. The credit component is determined by comparing the present value of the cash flows expected to be collected, discounted at the rate in effect before recognizing any OTTI, with the amortized cost basis of the debt security. The Company uses the cash flow expected to be realized from the security, which includes assumptions about interest rates, timing and severity of defaults, estimates of potential recoveries, the cash flow distribution from the bond indenture and other factors, then applies a discount rate equal to the effective yield of the security. The difference between the present value of the expected cash flows and the amortized book value is considered a credit loss.  The fair market value of the security is determined using the same expected cash flows; the discount rate is a rate the Company determines from open market and other sources as appropriate for the particular security.  The difference between the fair market value and the security's remaining amortized cost is recognized in other comprehensive income.

The following is a rollforward for the six months ended March 31, 2013 of the amounts recognized in earnings related to credit losses on securities which the Company has recorded OTTI charges through earnings and comprehensive income.

| | (Dollars in Thousands) | |
|---|---|---|
| Credit component of OTTI as of October 1, 2012 | $ | 2,103 |
| Additions for credit-related OTTI charges on previously unimpaired securities | | - |
| Additional increases as a result of impairment charges recognized on investments for which an OTTI was previously recognized | | 20 |
| Credit component of OTTI as of March 31, 2013 | $ | 2,123 |

U.S. Government Agency Obligations - The Company's investments reflected in the tables above in U.S. Government sponsored enterprise notes consist of debt obligations of the FHLB and Federal Farm Credit System ("FFCS"). These securities are typically rated AAA by one of the internationally recognized credit rating services. At March 31, 2013, U.S. Government and agency obligations in a gross unrealized loss for less than twelve months consisted of 18 securities having an aggregate depreciation of $461,000 or 0.5% from the Company's amortized cost basis. There were no securities in a gross unrealized loss for more than twelve months at such date. The unrealized losses on these debt securities relates principally to the changes in market interest rates and a lack of liquidity currently in the financial markets and are not as a result of projected shortfall of cash flows. In addition, the Company does not intend to sell these securities and it is more likely than not that the Company will not be required to sell the securities. As such, the Company anticipates it will recover the entire amortized cost basis of the securities. As a result, the Company does not consider these investments to be other-than-temporarily impaired at March 31, 2013.

U.S. Agency Issued Mortgage-Backed Securities - At March 31, 2013, the gross unrealized loss in U.S. agency issued mortgage-backed securities in the category of experiencing a gross unrealized loss for less than 12 months was $44,000 or 0.08% from the Company's amortized cost basis and consisted of two securities. There were no securities in a gross unrealized loss position in the category of experiencing a gross unrealized loss for more than 12 months. These securities represent asset-backed issues that are issued or guaranteed by a U.S. Government sponsored agency or carry the full faith and credit of the United States through a government agency and are currently rated AAA by at least one bond credit rating agency. In September 2008, the U.S. Department of the Treasury announced the establishment of the Government Sponsored Enterprise Credit Facility to ensure credit availability to Fannie Mae and Freddie Mac. The U.S. Department of the Treasury also entered into senior preferred stock purchase agreements, which ensure that each entity maintains a positive net worth and effectively support the holders of debt and mortgage-backed securities issued or guaranteed by Fannie Mae and Freddie Mac. The preferred stock agreements enhance market stability by providing additional security to debt holders, senior and subordinated, thereby alleviating the concern of the credit driven impairment of the securities.

Non-Agency Issued Mortgage-Backed Securities and Collateralized Mortgage Obligations - This portfolio was acquired through the redemption-in-kind during 2008 of the Company's entire investment in a mutual fund and includes 50 collateralized mortgage obligations ("CMO") and mortgage-backed securities issued by large commercial financial institutions. For the six months ended March 31, 2013, management recognized an OTTI charge related to a portion of the portfolio securities in the amount of $25,000 on a pre-tax basis due to the fact that, in management's judgment, the credit quality of the collateral pool underlying such securities had deteriorated during recent periods to the point that full recovery of the entire amortized cost of the investment was considered to be uncertain. This portfolio consists primarily of securities with underlying collateral consisting of Alt-A loans and those collateralized by home equity lines of credit and other receivables as well as whole loans with more significant exposure to depressed real estate markets in the United States. For the overall portfolio of the securities, there was exposure to the declining real estate markets such as California, Nevada, Arizona and Florida and consequently, an additional OTTI charge was deemed to be warranted as of March 31, 2013. Of the recorded charge, a total of $20,000 was concluded to be credit related and recognized currently in earnings and $5,000 was concluded to be attributable to other factors and recognized in accumulated other comprehensive income.

As of March 31, 2013, with the exception of securities discussed above, there are no securities for which the Company currently believes it is not probable that it will collect all amounts due according to the contractual terms of the investment. Management concluded that an other-than-temporary impairment did not exist and the decline in value was attributed to the illiquidity in the financial markets. With respect to the $130,000 in gross unrealized losses related to this part of the portfolio, 13 securities had been in a loss position for longer than 12 months while 1 security had been in a loss position for less than 12 months. However, the Company does not intend to sell these securities and it is more likely than not that the Company will not be required to sell these securities.

The amortized cost and fair value of debt securities, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

| | March 31, 2013<br>Held to Maturity | | Available for Sale | |
|---|---|---|---|---|
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | (Dollars in Thousands) | | | |
| Due within one year | $ 3,000 | $ 3,021 | $ - | $ - |
| Due after one through five years | 2,000 | 2,007 | - | - |
| Due after five through ten years | 11,498 | 12,028 | 2,998 | 3,062 |
| Due after ten years | 55,434 | 55,576 | 16,987 | 16,895 |
| Total | $ 71,932 | $ 72,632 | $ 19,985 | $ 19,957 |

The maturity table above excludes mortgage-backed securities because the contractual maturities are not indicative of actual maturities due to significant prepayments.

5. LOANS RECEIVABLE

Loans receivable consist of the following:

| | March 31, 2013 | September 30, 2012 |
|---|---|---|
| | (Dollars in Thousands) | |
| One-to-four family residential | $ 241,968 | $ 222,793 |
| Multi-family residential | 4,751 | 5,051 |
| Commercial real estate | 18,599 | 19,333 |
| Construction and land development | 14,800 | 14,873 |
| Commercial business | 593 | 632 |
| Consumer | 421 | 523 |
| Total loans | 281,132 | 263,205 |
| Undisbursed portion of loans-in-process | (1,872 ) | (1,629 ) |
| Deferred loan fees, net | 1,489 | 989 |
| Allowance for loan losses | (2,512 ) | (1,881 ) |
| Net loans | $ 278,237 | $ 260,684 |

The following table summarizes the loans individually evaluated for impairment by loan segment at March 31, 2013:

| | One- to four-family residential | Multi-family residential | Commercial real estate | Construction and land development | Commercial business | Consumer | Total |
|---|---|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | | | |
| Individually evaluated for impairment | $ 15,959 | $ 906 | $ 2,623 | $ 1,518 | $ - | $ - | $ 21,006 |
| Collectively evaluated for impairment | 226,009 | 3,845 | 15,976 | 13,282 | 593 | 421 | 260,126 |
| Total loans | $ 241,968 | $ 4,751 | $ 18,599 | $ 14,800 | $ 593 | $ 421 | $ 281,132 |

The following table summarizes the loans individually evaluated for impairment by loan segment at September 30, 2012:

| | One- to four-family residential | Multi-family residential | Commercial real estate | Construction and land development | Commercial business | Consumer | Total |
|---|---|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | | | |
| Individually evaluated for impairment | $ 25,440 | $ 916 | $ 1,679 | $ 2,573 | $ - | $ - | $ 30,608 |
| Collectively evaluated for impairment | 197,353 | 4,135 | 17,654 | 12,300 | 632 | 523 | 232,597 |
| Total loans | $ 222,793 | $ 5,051 | $ 19,333 | $ 14,873 | $ 632 | $ 523 | $ 263,205 |

The loan portfolio is segmented at a level that allows management to monitor risk and performance. Management evaluates all construction loans, commercial real estate and commercial business loans and all loans 90 plus days delinquent as to principal and/or interest for potential impairment. Loans are considered to be 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.

Once the determination is made that a loan is impaired, the determination of whether a specific allocation of the allowance is necessary is generally measured by comparing the recorded investment in the loan to the fair value of the loan using one of the following three methods: (a) the present value of the expected future cash flows discounted at the loan's effective interest rate; (b) the loan's observable market price; or (c) the fair value of the collateral less selling costs. Management primarily utilizes the fair value of collateral method as a practically expedient alternative. On collateral based loans, any portion deemed uncollectible is charged-off against the loan loss allowance.

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 March 31, 2013:

| | Impaired Loans with Specific Allowance (Dollars in Thousands) | | Impaired Loans with No Specific Allowance | Total Impaired Loans | |
|---|---|---|---|---|---|
| | Recorded Investment | Related Allowance | Recorded Investment | Recorded Investment | Unpaid Principal Balance |
| One-to-four family residential | $ - | $ - | $ 15,959 | $ 15,959 | $ 15,959 |
| Mult-family residential | - | - | 906 | 906 | 906 |
| Commercial real estate | - | - | 2,623 | 2,623 | 2,623 |
| Construction and land development | - | - | 1,518 | 1,518 | 1,518 |
| Total Loans | $ - | $ - | $ 21,006 | $ 21,006 | $ 21,006 |

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 September 30, 2012:

| | Impaired Loans with Specific Allowance | | Impaired Loans with No Specific Allowance | Total Impaired Loans | |
|---|---|---|---|---|---|
| | | (Dollars in Thousands) | | | |
| | Recorded Investment | Related Allowance | Recorded Investment | Recorded Investment | Unpaid Principal Balance |
| One-to-four family residential | $ - | $ - | $ 25,440 | $ 25,440 | $ 25,440 |
| Multi-family residential | - | - | 916 | 916 | 916 |
| Commercial real estate | - | - | 1,679 | 1,679 | 1,679 |
| Construction and land development | - | - | 2,573 | 2,573 | 2,573 |
| Total Loans | $ - | $ - | $ 30,608 | $ 30,608 | $ 30,608 |

The following table presents the average recorded investment in impaired loans and related interest income recognized for the periods indicated:

| | Three Months Ended March 31, 2013 | | |
|---|---|---|---|
| | Average Recorded Investment | Income Recognized on Accrual Basis | Income Recognized on Cash Basis |
| | (Dollars in Thousands) | | |
| One-to four-family residential | $ 21,771 | $ 159 | $ - |
| Multi-family residential | 912 | 17 | - |
| Commercial real estate | 1,621 | 11 | 12 |
| Construction and Land Development | 1,941 | 28 | - |
| Total loans | $ 26,245 | $ 215 | $ 12 |

| | Six Months Ended March 31, 2013 | | |
|---|---|---|---|
| | Average Recorded Investment | Income Recognized on Accrual Basis | Income Recognized on Cash Basis |
| | (Dollars in Thousands) | | |
| One-to four-family residential | $ 18,865 | $ 325 | $ 69 |
| Multi-family residential | 909 | 33 | - |
| Commercial real estate | 1,569 | 30 | 12 |
| Construction and Land Development | 1,730 | 63 | - |
| Total loans | $ 23,073 | $ 451 | $ 81 |

| | Three Months Ended March 31, 2012 | | |
|---|---|---|---|
| | Average Recorded Investment | Income Recognized on Accrual Basis | Income Recognized on Cash Basis |
| | (Dollars in Thousands) | | |
| One-to four-family residential | $ 9,884 | $ 102 | $ 95 |
| Commercial real estate | 713 | 8 | - |
| Construction and Land Development | 2,333 | 20 | - |
| Total loans | $ 12,930 | $ 130 | $ 95 |

| | Six Months Ended March 31, 2012 | | |
|---|---|---|---|
| | Average Recorded Investment | Income Recognized on Accrual Basis | Income Recognized on Cash Basis |
| | | (Dollars in Thousands) | |
| One-to four-family residential | $ 11,295 | $ 102 | $ 161 |
| Commercial real estate | 852 | 8 | - |
| Construction and Land Development | 2,878 | 29 | - |
| Total loans | $ 15,025 | $ 139 | $ 161 |

Federal regulations and our policies require that the Company utilize an internal asset classification system as a means of reporting problem and potential problem assets. The Company has incorporated an internal asset classification system, consistent with Federal banking regulations, as a part of its credit monitoring system. Management currently classifies problem and potential problem assets as “special mention”, “substandard,” “doubtful” or “loss” assets. 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.” Assets classified as “loss” are those considered “uncollectible” and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. Assets which do not currently expose the insured institution to sufficient risk to warrant classification in one of the aforementioned categories but possess weaknesses are required to be designated “special mention.”

The following table presents the classes of the loan portfolio in which a formal risk weighting system is utilized summarized by the aggregate “Pass” and the criticized category of “special mention”, and the classified categories of “substandard” and “doubtful” within the Company’s risk rating system. The Company had no loans classified as “doubtful” or “loss” at either of the dates presented.

| | March 31, 2013 | | | | |
|---|---|---|---|---|---|
| | Pass | Special Mention | Substandard | Doubtful | Total Loans |
| | | | (Dollars in Thousands) | | |
| Multi-family residential | $ 3,845 | $ - | $ 906 | $ - | $ 4,751 |
| Commercial real estate | 15,976 | - | 2,623 | - | 18,599 |
| Construction and land development | 13,282 | - | 1,518 | - | 14,800 |
| Commercial business | 593 | - | - | - | 593 |
| Total loans | $ 33,696 | $ - | $ 5,047 | $ - | $ 38,743 |

| | September 30, 2012 | | | | |
|---|---|---|---|---|---|
| | Pass | Special Mention | Substandard | Doubtful | Total Loans |
| | (Dollars in Thousands) | | | | |
| Multi-family residential | $ 4,135 | $ - | $ 916 | $ - | $ 5,051 |
| Commercial real estate | 17,654 | - | 1,679 | - | 19,333 |
| Construction and land development | 12,300 | - | 2,573 | - | 14,873 |
| Commercial business | 632 | - | - | - | 632 |
| Total loans | $ 34,721 | $ - | $ 5,168 | $ - | $ 39,889 |

The following table represents loans in which a formal risk rating system is not utilized, but loans are segregated between performing and non-performing based primarily on delinquency status:

| | March 31, 2013 | | |
|---|---|---|---|
| | Performing | Non-Performing | Total Loans |
| | (Dollars in Thousands) | | |
| One-to-four family residential | $ 237,840 | $ 4,128 | $ 241,968 |
| Consumer | 421 | - | 421 |
| Total loans | $ 238,261 | $ 4,128 | $ 242,389 |

| | September 30, 2012 | | |
|---|---|---|---|
| | Performing | Non-Performing | Total Loans |
| | (Dollars in Thousands) | | |
| One-to-four family residential | $ 209,889 | $ 12,904 | $ 222,793 |
| Consumer | 523 | - | 523 |
| Total loans | $ 210,412 | $ 12,904 | $ 223,316 |

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is due. The following table presents the loan categories of the loan portfolio summarized by the aging categories of performing and delinquent loans and nonaccrual loans:

| | March 31, 2013 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Current | 30-89 Days Past Due | 90 Days + Past Due | 90 Days+ Past Due and Accruing | Total Past Due and Accruing | Total Loans | Non-Accrual |
| | (Dollars in Thousands) | | | | | | |
| One-to-four family residential | $ 237,711 | $ 129 | $ 4,128 | $ - | $ 129 | $ 241,968 | $ 4,128 |
| Multi-family residential | 4,751 | - | - | - | - | 4,751 | - |
| Commercial real estate | 17,538 | 331 | 730 | - | 331 | 18,599 | 2,050 |
| Construction and land development | 14,800 | - | - | - | - | 14,800 | - |
| Commercial business | 593 | - | - | - | - | 593 | - |
| Consumer | 411 | 10 | - | - | 10 | 421 | - |
| Total loans | $ 275,804 | $ 470 | $ 4,858 | $ - | $ 470 | $ 281,132 | $ 6,178 |

| | September 30, 2012 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Current | 30-89 Days Past Due | 90 Days + Past Due | 90 Days+ Past Due and Accruing | Total Past Due and Accruing | Total Loans | Non-Accrual |
| | (Dollars in Thousands) | | | | | | |
| One-to-four family residential | $ 217,061 | $ 1,108 | $ 4,624 | $ - | $ 1,108 | $ 222,793 | $ 12,904 |
| Multi-family residential | 5,051 | - | - | - | - | 5,051 | - |
| Commercial real estate | 18,859 | 233 | 241 | - | 233 | 19,333 | 597 |
| Construction and land development | 14,356 | - | 517 | - | - | 14,873 | 517 |
| Commercial business | 632 | - | - | - | - | 632 | - |
| Consumer | 522 | 1 | - | - | 1 | 523 | - |
| Total loans | $ 256,481 | $ 1,342 | $ 5,382 | $ - | $ 1,342 | $ 263,205 | $ 14,018 |

The allowance for loan losses is established through a provision for loan losses charged to expense. The Company maintains the allowance at a level believed to cover all known and inherent losses in the portfolio that are both probable and reasonable to estimate at each reporting date. Management reviews the allowance for loan losses no less than quarterly in order to identify these inherent losses and to assess the overall collection probability for the loan portfolio in view of these inherent losses. For each primary type of loan, a loss factor is established reflecting an estimate of the known and inherent losses in such loan type using both a quantitative analysis as well as consideration of qualitative factors. The evaluation process includes, among other things, an analysis of delinquency trends, non-performing loan trends, the level of charge-offs and recoveries, prior loss experience, total loans outstanding, the volume of loan originations, the type, size and geographic concentration of our loans, the value of collateral securing the loans, the borrowers' ability to repay and repayment performance, the number of loans requiring heightened management oversight, local economic conditions and industry experience.

Commercial real estate loans entail significant additional credit risks compared to one-to four-family residential mortgage loans, as they generally involve large loan balances concentrated with single borrowers or groups of related borrowers. In addition, the payment experience on loans secured by income-producing properties typically depends on the successful operation of the related real estate project and/or business operation of the borrower who is also the primary occupant, and thus may be subject to a greater extent to the effects of adverse conditions in the real estate market and in the economy in general. Commercial business loans typically involve a higher risk of default than residential loans of like duration since their repayment is generally dependent on the successful operation of the borrower's business and the sufficiency of collateral, if any. Land acquisition, development and construction lending exposes us to greater credit risk than permanent mortgage financing. The repayment of land acquisition, development and construction loans depends upon the sale of the property to third parties or the availability of permanent financing upon completion of all improvements. These events may adversely affect the borrowers and the value of the collateral property.

The following table summarizes the primary segments of the allowance for loan losses, segmented into the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment. Activity in the allowance is presented for the three and six month periods ended March 31, 2013 and 2012:

Three Months Ended March 31, 2013

| | One- to four-family residential | Multi-family residential | Commercial real estate | Construction and land development | Commercial business | Consumer | Unallocated | Total |
|---|---|---|---|---|---|---|---|---|
| | | | | (Dollars in Thousands) | | | | |
| ALLL balance at December 31, 2012 | $ 905 | $ 7 | $ 125 | $ 859 | $ 3 | $ 1 | $ 181 | $ 2,081 |
| Charge-offs | (154 ) | - | - | - | - | - | - | (154 ) |
| Recoveries | 25 | - | - | 560 | - | - | - | 585 |
| Provision (recovery) | 25 | - | 50 | (122 ) | - | - | 47 | - |
| ALLL balance at March 31, 2013 | $ 801 | $ 7 | $ 175 | $ 1,297 | $ 3 | $ 1 | $ 228 | $ 2,512 |
| Individually evaluated for impairment | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - |
| Collectively evaluated for impairment | 801 | 7 | 175 | 1,297 | 3 | 1 | 228 | 2,512 |

Six Months Ended March 31, 2013

| | One- to four-family residential | Multi-family residential | Commercial real estate | Construction and land development | Commercial business | Consumer | Unallocated | Total |
|---|---|---|---|---|---|---|---|---|
| | | | | (Dollars in Thousands) | | | | |
| ALLL balance at September 30, 2012 | $ 830 | $ 7 | $ 125 | $ 745 | $ 3 | $ 1 | $ 170 | $ 1,881 |
| Charge-offs | (154 ) | - | - | - | - | - | - | (154 ) |
| Recoveries | 25 | - | - | 760 | - | - | - | 785 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Provision (recovery) | 100 | - | 50 | (208 ) | - | - | 58 | - |
| ALLL balance at March 31, 2013 | $ 801 | $ 7 | $ 175 | $ 1,297 | $ 3 | $ 1 | $ 228 | $ 2,512 |
| Individually evaluated for impairment | $ - | $ - | $ - | $ - | $ - | $ - | $ - | $ - |
| Collectively evaluated for impairment | 801 | 7 | 175 | 1,297 | 3 | 1 | 228 | 2,512 |

| | Three Months Ended March 31, 2012 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | One- to four-family residential | Multi-family residential | Commercial real estate | Construction and land development | Commercial business | Consumer | Unallocated | Total |
| | (Dollars in Thousands) | | | | | | | |
| ALLL balance at December 31, 2011 | $ 2,138 | $ 8 | $ 59 | $ 1,085 | $ 2 | $ 1 | $ 120 | $ 3,413 |
| Charge-offs | (160 ) | - | - | (303 ) | - | - | - | (463 ) |
| Recoveries | - | - | - | - | - | - | - | - |
| Provision (recovery) | (401 ) | 93 | 110 | 140 | 2 | - | 156 | 100 |
| ALLL balance at March 31, 2012 | $ 1,577 | $ 101 | $ 169 | $ 922 | $ 4 | $ 1 | $ 276 | $ 3,050 |
| Individually evaluated for impairment | $ 957 | $ - | $ - | $ - | $ - | $ - | $ - | $ 957 |
| Collectively evaluated for impairment | 620 | 101 | 169 | 922 | 4 | 1 | 276 | 2,093 |

| | Six Months Ended March 31, 2012 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | One- to four-family residential | Multi-family residential | Commercial real estate | Construction and land development | Commercial business | Consumer | Unallocated | Total |
| | (Dollars in Thousands) | | | | | | | |
| ALLL balance at September 30, 2011 | $ 1,651 | $ 7 | $ 221 | $ 1,481 | $ 3 | $ 1 | $ - | $ 3,364 |
| Charge-offs | (261 ) | - | - | (303 ) | - | - | - | (564 ) |
| Recoveries | - | - | - | - | - | - | - | - |
| Provision (recovery) | 187 | 94 | (52 ) | (256 ) | 1 | - | 276 | 250 |
| ALLL balance at March 31, 2012 | $ 1,577 | $ 101 | $ 169 | $ 922 | $ 4 | $ 1 | $ 276 | $ 3,050 |
| Individually evaluated for impairment | $ 957 | $ - | $ - | $ - | $ - | $ - | $ - | $ 957 |
| Collectively evaluated for impairment | 620 | 101 | 169 | 922 | 4 | 1 | 276 | 2,093 |

The following table summarizes information regarding troubled debt restructurings for both the three and six months ended March 31, 2013:

| | Number of | Pre-modification Outstanding Recorded | Post-modification Outstanding Recorded |
|---|---|---|---|

| | Contracts | Investment (Dollars in Thousands) | Investments |
|---|---|---|---|
| One-to-four family residential | - | - | - |
| Multi-family residential | - | - | - |
| Commercial real estate | 1 | $ 1,321 | $ 1,321 |
| Construction and land development | - | - | - |
| Commercial business | - | - | - |
| Consumer | - | - | - |

In January 2013, the Bank completed the sale of five one-to-four family residential loans classified as troubled debt restructurings related to a 133-unit condominium project located in Philadelphia in which the Bank was the lead lender and held a $9.2 million investment. In connection with the closing of the loan sale, the Bank and the other loan participants extended a loan to an affiliate of the borrower, the proceeds of which were used to reduce the principal balance due on the project. The Bank's portion of such loan is approximately $1.3 million. The new loan is being reported as a troubled debt restructuring during the quarter ending March 31, 2013. The Bank did not incur any additional losses upon completion of the sale of the loans beyond the $968,000 loss already recognized in prior periods. There were no other troubled debt restructuring modifications approved during the six months ended March 31, 2013 or 2012 except for the new loan described above. In addition, no troubled debt restructurings defaulted during the six months ended March 31, 2013 or 2012.

## 6. DEPOSITS

Deposits consist of the following major classifications:

| | March 31, 2013 | | September 30, 2012 | |
|---|---|---|---|---|
| | Amount | Percent | Amount | Percent |
| | | (Dollars in Thousands) | | |
| Money market deposit accounts | $ 68,861 | 16.5 % | $ 69,735 | 16.4 % |
| Interest-bearing checking accounts | 35,640 | 8.6 | 33,659 | 7.9 |
| Non-interest bearing checking accounts | 3,116 | 0.7 | 3,711 | 0.9 |
| Passbook, club and statement savings | 72,260 | 17.4 | 71,083 | 16.7 |
| Certificates maturing in six months or less | 89,095 | 21.4 | 71,173 | 16.7 |
| Certificates maturing in more than six months | 147,125 | 35.4 | 176,241 | 41.4 |
| Total | $ 416,097 | 100.0 % | $ 425,602 | 100.0 % |

Certificates of $100,000 and over totaled $90.7 million as of March 31, 2013 and $96.2 million as of September 30, 2012.

7. INCOME TAXES

Items that gave rise to significant portions of deferred income taxes are as follows:

| | March 31, 2013 | September 30, 2012 |
|---|---|---|
| Deferred tax assets: | (Dollars in Thousands) | |
| Deposit premium | $ - | $ 20 |
| Allowance for loan losses | 1,962 | 2,302 |
| Real estate owned expenses | 222 | 301 |
| Nonaccrual interest | 119 | 196 |
| Accrued vacation | 94 | 95 |
| Capital loss carryforward | 1,718 | 1,262 |
| Impairment loss | 1,113 | 1,562 |
| Split dollar life insurance | 22 | 22 |
| Post-retirement benefits | 133 | 135 |
| Employee benefit plans | 352 | 386 |
| Total deferred tax assets | 5,735 | 6,281 |
| Valuation allowance | (2,274 ) | (2,046 ) |
| Total deferred tax assets, net of valuation allowance | 3,461 | 4,235 |
| Deferred tax liabilities: | | |
| Unrealized gain on available for sale securities | 470 | 661 |
| Property | 517 | 526 |
| Deferred loan fees | 506 | 299 |
| Total deferred tax liabilities | 1,493 | 1,486 |
| Net deferred tax asset | $ 1,968 | $ 2,749 |

The Company establishes a valuation allowance for deferred tax assets when management believes that the use of the deferred tax assets is not likely to be realized either through a carry back to taxable income in prior years, future reversals of existing taxable temporary differences, and, to a lesser extent, future taxable income. The tax deduction generated by the redemption of the shares of the mutual fund and the subsequent impairment charge on the assets acquired through the redemption in kind are considered a capital loss and can only be utilized to the extent of capital gains over a five year period, resulting in the establishment of a valuation allowance for the carryforward period which expires beginning in 2013. The valuation allowance totaled $2.3 million at March 31, 2013. The gross deferred tax assets related to impairment losses and capital loss carryforwards increased in the aggregate by $7,000 during the six months ended March 31, 2013 while the corresponding valuation allowance related to these two assets increased by $228,000, resulting in an increase in income tax expense of $221,000 corresponding to the decrease in the fair value of available for sale mortgage-backed securities at March 31, 2013 which may be sold in the future to generate capital gains.

There is currently no liability for uncertain tax positions and no known unrecognized tax benefits. The Company recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the Consolidated Statements of Operations as a component of income tax expense. As of March 31, 2013, the Internal Revenue Service conducted an audit of the Company's tax returns for the year ended September 30, 2010, and no adverse findings were reported. The Company's federal and state income tax returns for taxable years through

September 30, 2008 have been closed for purposes of examination by the Internal Revenue Service and the Pennsylvania Department of Revenue.

8. STOCK COMPENSATION PLANS

The Company maintains a Recognition and Retention Plan ("RRP") which is administered by a committee of the Board of Directors. The RRP provides for the grant of shares of common stock of the Company to certain officers, employees and directors of the Company. In order to fund the grant of shares under the RRP, the RRP Trust purchased 226,148 shares of the Company's common stock in the open market for approximately $2.5 million at an average price per share of $10.85. The Company made sufficient contributions to the RRP Trust to fund these purchases. No additional purchases are expected to be made by the RRP Trust under the RRP. As of March 31, 2013, all the shares had been awarded as part of the RRP. Shares subject to awards under the RRP generally vest at the rate of 20% per year over five years. As of March 31, 2013, 141,975 shares had become fully vested and 3,900 shares had been forfeited. The forfeited shares are available for future awards.

Compensation expense related to the shares subject to restricted stock awards granted is recognized ratably over the five-year vesting period in an amount which totals the share price at the grant date multiplied by the number of shares subject to the grant. During the three and six months ended March 31, 2013, 128,000 and $225,000, respectively, was recognized in compensation expense for the RRP. A tax benefit of $30,000 was recognized for the three months ended March 31, 2013 while income tax expense of $3,000 was recognized for the six months ended March 31, 2013. During the three months and six months ended March 31, 2012, $97,000 and $195,000, respectively, was recognized in compensation expense for the RRP. Tax expense of $36,000 and $2,000 was recognized during the three and six months ended March 31, 2012, respectively. At March 31, 2013, approximately $623,000 in additional compensation expense for the shares awarded related to the RRP remained unrecognized.

A summary of the Company's nonvested stock award activity for the six months ended March 31, 2013 is presented in the following table:

| | Six Months Ended March 31, 2013 | |
|---|---|---|
| | Number of Shares | Weighted Average Grant Date Fair Value |
| Nonvested stock awards at October 1, 2012 | 72,684 | $ 11.10 |
| Issued | 47,266 | 7.38 |
| Forfeited | (3,900 ) | 8.96 |
| Vested | (35,776 ) | 11.12 |
| Nonvested stock awards at the March 31, 2013 | 80,274 | $ 9.00 |

The Company also maintains a Stock Option Plan. The Stock Option Plan authorizes the grant of stock options to officers, employees and directors of the Company to acquire shares of common stock with an exercise price at least equal to the market value of the common stock on the grant date. Options will generally become vested and exercisable at the rate of 20% per year over five years and are generally exercisable for a period of ten years after the grant date. A total of 565,369 shares of common stock are available for issuance pursuant to the Stock Option Plan. As of March 31, 2013, all of the options had been awarded under the Plan. As of March 31, 2013, 351,093 options were vested and 10,773 had been forfeited.

A summary of the status of the Company's stock options under the Stock Option Plan as of March 31, 2013 and changes during the six month period ended March 31, 2013 are presented below:

| | Six Months Ended March 31, 2013 | | |
|---|---|---|---|
| | Number of Shares | | Weighted Average Exercise Price |
| Outstanding at October 1, 2012 | 442,400 | $ | 11.12 |
| Granted | 122,969 | | 7.37 |
| Exercised | - | | - |
| Forfeited | (10,773 ) | | 8.90 |
| Outstanding at March 31, 2013 | 554,596 | $ | 10.33 |
| Exercisable at March 31, 2013 | 351,093 | $ | 11.13 |

The weighted average remaining contractual term was approximately 6.6 years for options outstanding as of March 31, 2013.

The estimated fair value of options granted during fiscal 2009 was $2.81 per share, $2.76 for options granted during fiscal 2010 and $3.15 for options granted during 2013. The fair value was estimated on the date of grant using the Black-Scholes pricing model. No options were granted in fiscal years 2011 and 2012.

During the three and six months ended March 31, 2013, 68,000 and $129,000, respectively, was recognized in compensation expense for the Stock Option Plan. A tax benefit of $7,000 and $13,000, respectively, were recognized for the three and six months ended March 31, 2013. During the three months and six months ended March 31, 2012, $61,000 and $122,000, respectively, was recognized in compensation expense. A tax benefit of $6,000 and $12,000, respectively, was recognized during the three and six months ended March 31, 2012. At March 31, 2013, approximately $533,000 in additional compensation expense for awarded options remained unrecognized. The weighted average period over which this expense will be recognized is approximately 1.6 years.

## 9. COMMITMENTS AND CONTINGENT LIABILITIES

At March 31, 2013, the Company had $7.5 million in outstanding commitments to originate fixed and variable-rate loans with market interest rates ranging from 2.50% to 6.00%. At September 30, 2012, the Company had $14.1 million in outstanding commitments to originate fixed and variable-rate loans with market interest rates ranging from 2.75% to 6.00%.

The aggregate undisbursed portion of loans-in-process amounted to $1.9 million and $1.6 million, respectively, at March 31, 2013 and September 30, 2012.

The Company also had commitments under unused lines of credit of $6.1 million and $6.5 million, respectively, at March 31, 2013 and September 30, 2012 and letters of credit outstanding of $187,000 and $167,000, respectively, at March 31, 2013 and September 30, 2012.

Among the Company's contingent liabilities are exposures to limited recourse arrangements with respect to the Company's sales of whole loans and participation interests. At March 31, 2013, the exposure, which represents a portion of credit risk associated with the interests sold, amounted to $64,000. This exposure is for the life of the related loans and payables, on our proportionate share, as actual losses are incurred.

The Company is involved in various legal proceedings occurring in the ordinary course of business. Management of the Company, based on discussions with litigation counsel, believes that such proceedings will not have a material adverse effect on the financial condition, operations or cash flows of the Company. There can be no assurance that any of the outstanding legal proceedings to which the Company is a party will not be decided adversely to the Company’s interests and have a material adverse effect on the financial condition and operations of the Company.

## 10. FAIR VALUE MEASUREMENT

The fair value estimates presented herein are based on pertinent information available to management as of March 31, 2013 and September 30, 2012, respectively. Although management is not aware of any factors that would significantly affect the fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

Generally accepted accounting principles used in the United States establish a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value.

The three broad levels of hierarchy are as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Those assets as of March 31, 2013 which are to be measured at fair value on a recurring basis are as follows:

| | Category Used for Fair Value Measurement | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| | (Dollars in Thousands) | | | |
| Securities available for sale: | | | | |
| U.S. Government and agency obligations | $ - | $ 19,957 | $ - | $ 19,957 |
| Mortgage-backed securities - U.S. Government agencies | - | 38,948 | - | 38,948 |
| Mortgage-backed securities - Non-agency | - | 3,792 | - | 3,792 |
| FHLMC preferred stock | 18 | - | - | 18 |
| Total | $ 18 | $ 62,697 | $ - | $ 62,715 |

Those assets as of September 30, 2012 which are measured at fair value on a recurring basis are as follows:

| | Category Used for Fair Value Measurement | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| | (Dollars in Thousands) | | | |
| Assets: | | | | |
| Securities available for sale: | | | | |
| U.S. Government and agency obligations | $ - | $ 14,103 | $ - | $ 14,103 |
| Mortgage-backed securities - U.S. Government agencies | - | 47,762 | - | 47,762 |
| Mortgage-backed securities - Non-agency | - | 4,103 | - | 4,103 |
| FHLMC preferred stock | 7 | - | - | 7 |
| Total | $ 7 | $ 65,968 | $ - | $ 65,975 |

Certain assets are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The Company measures impaired loans and real estate owned at fair value on a non-recurring basis.

Impaired Loans

The Company considers loans to be impaired when it becomes more likely than not that the Company will be unable to collect all amounts due in accordance with the contractual terms of the loan agreements. Collateral dependent impaired loans are based on the fair value of the collateral which is based on appraisals and would be categorized as Level 2 measurement. In some cases, adjustments are made to the appraised values for various factors including the age of the appraisal, age of the comparables included in the appraisal, and known changes in the market and in the collateral. These adjustments are based upon unobservable inputs, and therefore, the fair value measurement has been categorized as a Level 3 measurement. These loans are reviewed for impairment and written down to their net realizable value by charges against the allowance for loan losses. The collateral underlying these loans had a fair value of $21.0 million at March 31, 2013.

Real Estate Owned

Once an asset is determined to be uncollectible, the underlying collateral is repossessed and reclassified to foreclosed real estate (real estate owned) and repossessed assets. These assets are carried at the lower of cost or fair value of the collateral, based on independent appraisals, less cost to sell, and would be categorized as Level 2 measurement. In some cases, adjustments are made to the appraised values for various factors including age of the appraisal, age of the comparables included in the appraisal, and known changes in the market and in the collateral. Thus the evaluations are based upon unobservable inputs, and therefore, the fair value measurement of these assets have been categorized as a Level 3 measurement.

Summary of Non-Recurring Fair Value Measurements

At March 31, 2013
(Dollars in Thousands)

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Impaired loans | $ - | $ - | $ 21,006 | $ 21,006 |
| Real estate owned | - | - | 1,258 | $ 1,258 |
| Total | $ - | $ - | $ 22,264 | $ 22,264 |

At September 30, 2012
(Dollars in Thousands)

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Impaired loans | $ - | $ - | $ 30,608 | $ 30,608 |
| Real estate owned | - | - | 1,972 | $ 1,972 |
| Total | $ - | $ - | $ 32,580 | $ 32,580 |

The following table provides information describing the valuation processes used to determine nonrecurring fair value measurements categorized within level 3 of the fair value hierarchy:

At March 31, 2013
(Dollars in Thousands)

| | Fair Value | Valuation Technique | Unobservable Input | Range |
|---|---|---|---|---|
| Impaired loans | $ 21,006 | Property appraisals | Management discount for selling costs, property type and market volatility | 10% - 20% discount |
| Real estate owned | $ 1,258 | Property appraisals | Management discount for selling costs, property type and market volatility | 10% - 20% discount |

At September 30, 2012
(Dollars in Thousands)

| | Fair Value | Valuation Technique | Unobservable Input | Range |
|---|---|---|---|---|
| Impaired loans | $ 30,608 | Property appraisals | Management discount for selling costs, property type and market volatility | 10% - 20% discount |
| Real estate owned | $ 1,972 | Property appraisals | Management discount for selling costs, property type and market volatility | 10% - 20% discount |

The fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. 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 could 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.

| | | | Fair Value Measurements at March 31, 2013 | | |
|---|---|---|---|---|---|
| | Carrying Amount | Fair Value | (Level 1) | (Level 2) | (Level 3) |
| | (Dollars in Thousands) | | | | |
| Assets: | | | | | |
| Cash and cash equivalents | $33,612 | $33,612 | $33,612 | $- | $- |
| Investment and mortgage-backed securities available for sale | 62,715 | 62,715 | 18 | 62,697 | - |
| Investment and mortgage-backed securities held to maturity | 87,976 | 90,182 | - | 90,182 | - |
| Loans receivable, net | 278,237 | 283,817 | - | - | 283,817 |
| Accrued interest receivable | 1,833 | 1,833 | 1,833 | - | - |
| Federal Home Loan Bank stock | 1,659 | 1,659 | 1,659 | - | - |
| Bank owned life insurance | 7,022 | 7,022 | 7,022 | - | - |
| | | | | | |
| Liabilities: | | | | | |
| Checking accounts | 38,756 | 38,756 | 38,756 | - | - |
| Money market deposit accounts | 68,861 | 68,861 | 68,861 | - | - |
| Passbook, club and statement savings accounts | 72,260 | 72,260 | 72,260 | - | - |
| Certificates of deposit | 236,220 | 240,855 | - | 240,855 | - |
| Advances from Federal Home Loan Bank | 340 | 340 | 340 | - | - |
| Accrued interest payable | 747 | 747 | 747 | - | - |
| Advances from borrowers for taxes and insurance | 1,266 | 1,266 | 1,266 | - | - |

| | Carrying Amount | Fair Value | Fair Value Measurements at September 30, 2012 (Level 1) | (Level 2) | (Level 3) |
|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | |
| Assets: | | | | | |
| Cash and cash equivalents | $ 81,273 | $ 81,273 | $ 81,273 | $ - | $ - |
| Investment and mortgage-backed securities available for sale | 65,975 | 65,975 | 7 | 65,968 | - |
| Investment and mortgage-backed securities held to maturity | 63,110 | 66,401 | - | 66,401 | - |
| Loans receivable, net | 260,684 | 266,699 | - | - | 266,699 |
| Accrued interest receivable | 1,661 | 1,661 | 1,661 | - | - |
| Federal Home Loan Bank stock | 2,239 | 2,239 | 2,239 | - | - |
| Bank owned life insurance | 6,919 | 6,919 | 6,919 | - | - |
| Liabilities: | | | | | |
| Checking accounts | 37,370 | 37,370 | 37,370 | - | - |
| Money market deposit accounts | 69,735 | 69,735 | 69,735 | - | - |
| Passbook, club and statement savings accounts | 71,083 | 71,083 | 71,083 | - | - |
| Certificates of deposit | 247,414 | 252,479 | - | 252,479 | - |
| Advances from Federal Home Loan Bank | 483 | 484 | 484 | - | - |
| Accrued interest payable | 2,382 | 2,382 | 2,382 | - | - |
| Advances from borrowers for taxes and insurance | 1,273 | 1,273 | 1,273 | - | - |

Cash and Cash Equivalents—For cash and cash equivalents, the carrying amount is a reasonable estimate of fair value.

Investments and Mortgage-Backed Securities—The fair value of investment securities and mortgage-backed securities is based on quoted market prices, dealer quotes, and prices obtained from independent pricing services.

Loans Receivable—The fair value of loans is estimated based on present value using the current market rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The carrying value that fair value is compared to is net of the allowance for loan losses and other associated premiums and discounts. Due to the significant judgment involved in evaluating credit quality, loans are classified within Level 3 of the fair value hierarchy.

Accrued Interest Receivable – For accrued interest receivable, the carrying amount is a reasonable estimate of fair value.

Federal Home Loan Bank (FHLB) Stock—Although FHLB stock is an equity interest in an 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.

Bank Owned Life Insurance—The fair value of bank owned life insurance is based on the cash surrender value obtained from an independent advisor that is derivable from observable market inputs.

Checking Accounts, Money Market Deposit Accounts, Passbook Accounts, Club Accounts, Statement Savings Accounts, and Certificates of Deposit—The fair value of passbook accounts, club accounts, statement savings accounts, checking accounts, and money market deposit accounts is the amount reported in the financial statements. The fair value of certificates of deposit is based on market rates currently offered for deposits of similar remaining maturity.

Advances from Federal Home Loan Bank—The fair value of advances from FHLB is the amount payable on demand at the reporting date.

Accrued Interest Payable – For accrued interest payable, the carrying amount is a reasonable estimate of fair value.

Advances from borrowers for taxes and insurance – For advances from borrowers for taxes and insurance, the carrying amount is a reasonable estimate of fair value.

Commitments to Extend Credit and Letters of Credit—The majority of the Bank'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 Bank and the borrower. The estimated fair value approximates the recorded deferred fee amounts, which are not significant.

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

The following discussion should be read in conjunction with our unaudited consolidated financial statements included elsewhere in this Form 10-Q and with our Annual Report on Form 10-K for the year ended September 30, 2012 (the "Form 10-K").

Overview. Prudential Bancorp, Inc. of Pennsylvania (the "Company") was formed by Prudential Savings Bank (the "Bank") in connection with the Bank's reorganization into the mutual holding company form of organization in 2005. The Company's results of operations are primarily dependent on the results of the Bank, which is a wholly owned subsidiary of the Company. The Company's results of operations depend to a large extent on net interest income, which primarily is the difference between the income earned on its loan and securities portfolios and the cost of funds, which is the interest paid on deposits and borrowings. Results of operations are also affected by our provisions for loan losses, non-interest income (which includes impairment charges) and non-interest expense. Non-interest expense principally consists of salaries and employee benefits, office occupancy, depreciation, data processing expense, payroll taxes and other expense. Our results of operations are also significantly affected by general economic and competitive conditions, particularly changes in interest rates, government policies and actions of regulatory authorities. Future changes in applicable laws, regulations or government policies may materially impact our financial condition and results of operations. The Bank is subject to regulation by the Federal Deposit Insurance Corporation ("FDIC") and the Pennsylvania Department of Banking (the "Department"). The Bank's main office is in Philadelphia, Pennsylvania, with six additional banking offices located in Philadelphia and Delaware Counties in Pennsylvania. The Bank's primary business consists of attracting deposits from the general public and using those funds together with borrowings to originate loans and to invest primarily in U.S. Government and agency securities and mortgage-backed securities. In November 2005, the Bank formed PSB Delaware, Inc., a Delaware corporation, as a subsidiary of the Bank. In March 2006, all mortgage-backed securities then owned by the Company were transferred to PSB Delaware, Inc. PSB Delaware, Inc.'s. activities are included as part of the consolidated financial statements.

Critical Accounting Policies. In reviewing and understanding financial information for Prudential Bancorp, you are encouraged to read and understand the significant accounting policies used in preparing our financial statements. These policies are described in Note 1 of the notes to our consolidated financial statements included in Item 1 hereof as well as in Note 2 to our audited consolidated financial statements included in Form 10-K. The accounting and financial reporting policies of the Company 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 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 as well as contingent assets and contingent liabilities at the date of the 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 significantly affect our reported results and financial condition for the period or in future periods.

Allowance for Loan Losses. The allowance for loan losses is established through a provision for loan losses charged to expense. Losses are charged against the allowance for loan losses when management believes that the collectability in full of the principal of a loan is unlikely. Subsequent recoveries are added to the allowance. The allowance for loan losses is maintained at a level that management considers adequate to provide for estimated losses and impairments based upon an evaluation of known and inherent losses in the loan portfolio that are both probable and reasonable to estimate. Loan impairment is evaluated based on the fair value of collateral or estimated net realizable value. It is the policy of management to provide for losses on unidentified loans in its portfolio in addition to criticized and classified loans.

Management monitors its allowance for loan losses at least quarterly and makes adjustments to the allowance through the provision for loan losses as economic conditions and other pertinent factors indicate. The quarterly review and adjustment of the qualitative factors employed in the allowance methodology and the updating of historic loss experience allow for timely reaction to emerging conditions and trends. In this context, a series of qualitative factors are used in a methodology as a measurement of how current circumstances are affecting the loan portfolio. Included in these qualitative factors are:

- Levels of past due, classified, criticized and non-accrual loans, troubled debt restructurings and loan modifications;
- Nature and volume of loans;
- Changes in lending policies and procedures, underwriting standards, collections, charge-offs and recoveries and for commercial loans, the level of loans being approved with exceptions to lending policy;
- Experience, ability and depth of management and staff;
- National and local economic and business conditions, including various market segments;
- Quality of the Company's loan review system and degree of Board oversight;
- Concentrations of credit and changes in levels of such concentrations; and
- Effect of external factors on the level of estimated credit losses in the current portfolio.

In determining the allowance for loan losses, management has established both specific and general pooled allowances. Values assigned to the qualitative factors and those developed from historic loss experience provide a dynamic basis for the calculation of reserve factors for both pass-rated loans (general pooled allowance) and those for criticized and classified loans. The amount of the specific allowance is determined through a loan-by-loan analysis of certain large dollar commercial real estate loans. Loans not individually reviewed are evaluated as a group using reserve factor percentages based on historical loss experience and the qualitative factors described above. In determining the appropriate level of the general pooled allowance, management makes estimates based on internal risk ratings, which take into account such factors as debt service coverage, loan-to-value ratios and external factors.

Estimates are periodically measured against actual loss experience.

This evaluation is inherently subjective as it requires material estimates including, among others, exposure at default, the amount and timing of expected future cash flows on impaired loans, value of collateral, estimated losses on our commercial, construction and residential loan portfolios and historical loss experience. All of these estimates may be susceptible to significant change.

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. In addition, the Department and the FDIC, as an integral part of their examination processes, periodically review our allowance for loan losses. The Department and the FDIC 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 affect earnings in future periods.

Investment and mortgage-backed securities available for sale. Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated using quoted prices of securities with similar characteristics or discounted cash flows and are classified within Level 2 of the fair value hierarchy. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy, although there were no securities with that classification as of March 31, 2013 or September 30, 2012.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. The Company determines whether the unrealized losses are temporary in accordance with U.S. GAAP. The evaluation is based upon factors such as the creditworthiness of the issuers/guarantors, the underlying collateral, if applicable, and the continuing performance of the securities. In addition the Company also considers the likelihood that the security will be required to be sold by a regulatory agency, our internal intent not to dispose of the security prior to maturity and whether the entire cost basis of the security is expected to be recovered. In determining whether the cost basis will be recovered, management evaluates other facts and circumstances that may be indicative of an other-than-temporary impairment condition. This includes, but is not limited to, an evaluation of the type of security, length of time and extent to which the fair value has been less than cost, and near-term prospects of the issuer.

In addition, certain assets are measured at fair value on a non-recurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The Company measures impaired loans, FHLB stock and loans transferred into real estate owned at fair value on a non-recurring basis.

Valuation techniques and models utilized for measuring financial assets and liabilities are reviewed and validated by the Company at least quarterly.

Income Taxes. The Company accounts for income taxes in accordance with U.S. GAAP. The Company records deferred income taxes that reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Management exercises significant judgment in the evaluation of the amount and timing of the recognition of the resulting tax assets and liabilities. The judgments and estimates required for the evaluation are updated based upon changes in business factors and the tax laws. If actual results differ from the assumptions and other considerations used in estimating the amount and timing of tax recognized, there can be no assurance that additional expenses will not be required in future periods.

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 an additional 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.

U.S. GAAP prescribes a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. The Company recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the consolidated income statement.  Assessment of uncertain tax positions requires careful consideration of the technical merits of a position based on management's analysis of tax regulations and interpretations.  Significant judgment may be involved in the assessment of the tax position.

Forward-looking Statements. In addition to historical information, this Quarterly Report on Form 10-Q includes certain “forward-looking statements” based on management’s current expectations. The Company’s actual results could differ materially, as such term is defined in the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, from management’s expectations. Such forward-looking statements include statements regarding management’s current intentions, beliefs or expectations as well as the assumptions on which such statements are based. These forward-looking statements are subject to significant business, economic and competitive uncertainties and contingencies, many of which are not subject to the Company’s control. You are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and that actual results may differ materially from those contemplated by such forward-looking statements. Factors that could cause future results to vary from current management expectations include, but are not limited to, general economic conditions, legislative and regulatory changes, monetary and fiscal policies of the federal government, changes in tax policies, rates and regulations of federal, state and local tax authorities, changes in interest rates, deposit flows, the cost of funds, demand for loan products, demand for financial services, competition, changes in the quality or composition of the Company’s loan and investment portfolios, changes in accounting principles, policies or guidelines and other economic, competitive, governmental and technological factors affecting the Company’s operations, markets, products, services and fees.

The Company undertakes no obligation to update or revise any forward-looking statements to reflect changed assumptions, the occurrence of unanticipated events or changes to future operating results that occur subsequent to the date such forward-looking statements are made unless required by law or regulations.

Market Overview. The economy has shown improvements during 2012 and 2013, but we still view the current environment as challenging.

The Company continues to focus on the credit quality of its customers – closely monitoring the financial status of borrowers throughout the Company’s markets, gathering information, working on early detection of potential problems, taking pre-emptive steps where necessary and performing the analysis required to maintain adequate reserves for loan losses.

Despite the current market and economic conditions, the Company continues to maintain capital well in excess of regulatory requirements.

The following discussion provides further details on the financial condition of the Company at March 31, 2013 and September 30, 2012, and the results of operations for the three and six month periods ended March 31, 2013 and 2012.

COMPARISON OF FINANCIAL CONDITION AT MARCH 31, 2013 AND SEPTEMBER 30, 2012

At March 31, 2013, the Company had total assets of $479.1 million, a decrease of $11.4 million from $490.5 million at September 30, 2012. The decrease was attributable to a decrease in cash and cash equivalents of $47.7 million. This decrease was substantially offset by increases of $21.6 million and $17.6 million in the investment and mortgage-backed securities portfolio and loan portfolio, respectively, reflecting the Company’s deployment of its cash and cash equivalents to purchase securities and originate loans in order to improve the Company’s earnings.

Total liabilities decreased $11.8 million to $418.9 million at March 31, 2013 from $430.7 million at September 30, 2012. The decrease was due to a $9.5 million decrease in deposits and a $1.6 million decrease in accrued interest related to certificates of deposit as interest accrued on such deposits is generally distributed at the end of the calendar year. Allowing the runoff of higher costing certificates of deposit as part of the Company’s asset-liability management strategy led to the reduction in total assets described above as the cash and cash equivalents were used, in part, to fund such deposit outflows.

Stockholders' equity increased by $349,000 to $60.2 million at March 31, 2013. The increase primarily reflected equity increases associated with stock benefit plan expenses of $433,000. Also contributing to the increase was net income of $286,000 for the first six months of fiscal 2013, offset partially by a decline in the unrealized gain on available for sale securities.

COMPARISON OF RESULTS OF OPERATIONS FOR THE THREE AND SIX MONTHS ENDED MARCH 31, 2013 AND 2012

Net income. Net income amounted to $14,000 for the quarter ended March 31, 2013 as compared to $84,000 for the comparable period in 2012. For the six months ended March 31, 2013, the Company recognized net income of $286,000 as compared to net income of $488,000 for the comparable period in 2012. The decreased level of earnings for the 2013 periods primarily reflected decreases in net interest income combined with the effects of an increase in the valuation allowance related to a deferred tax asset.

Net interest income. Net interest income decreased $206,000 or 6.2% to $3.1 million for the three months ended March 31, 2013 as compared to $3.3 million for the same period in 2012. The decrease was due to a $560,000 or 11.6% decrease in interest income partially offset by a $354,000 or 23.7% decrease in interest expense. The decrease in interest income resulted from a 35 basis point decrease to 3.66% in the weighted average yield earned on interest-earning assets combined with a $14.8 million or 3.1% decrease in the average balance of interest-earning assets for the three months ended March 31, 2013, as compared to the same period in 2012. The decrease in the weighted average yield earned was primarily due to the reinvestment of the proceeds from called investment securities and the origination of new loans both at lower current market rates. The decrease in the average balance reflected the use of assets to fund the outflow of higher costing deposits, primarily certificates of deposit. The decrease in interest expense resulted primarily from a 28 basis point decrease to 1.09% in the weighted average rate paid on interest-bearing liabilities, reflecting the continued repricing downward of interest-bearing liabilities during the year combined with a $19.2 million or 4.4% decrease in the average balance of interest-bearing liabilities, primarily certificates of deposit, for the three months ended March 31, 2013, as compared to the same period in 2012. The decline in the weighted average rate paid reflected the continued effect of the low interest rate environment on the Bank's cost of funds as deposits repriced downward as well as the Bank's continued implementation of its asset/liability strategies designed to reduce its use of higher costing certificates of deposit as a funding source.

For the six months ended March 31, 2013, net interest income decreased $498,000 or 7.3% to $6.3 million as compared to $6.8 million for the same period in 2012. The decrease was due to a $1.1 million or 11.7% decrease in interest income partially offset by a $648,000 or 21.5% decrease in interest expense. The decrease in interest income resulted from a 39 basis point decrease to 3.70% in the weighted average yield earned on interest-earning assets combined with an $11.8 million or 2.5% decrease in the average balance of interest-earning assets for the six months ended March 31, 2013, as compared to the same period in 2012. The decrease in the weighted average yield earned was primarily due to the reinvestment of the proceeds from called investment securities and the origination of new loans at lower current market rates. The decrease in the average balance reflected the use of assets to fund the outflow of higher costing deposits, primarily certificates of deposit. The decrease in interest expense resulted primarily from a 26 basis point decrease to 1.12% in the weighted average rate paid on interest-bearing liabilities, reflecting the continued repricing downward of interest-bearing liabilities during the year combined with a $15.1 million or 3.5% decrease in the average balance of interest-bearing liabilities, primarily certificates of deposit, for the six months ended March 31, 2013, as compared to the same period in 2012. The decline in the weighted average rate paid reflected the continued effect of the low interest rate environment on the Bank's cost of funds as deposits repriced downward as well as the Bank's continued implementation of its asset/liability strategies designed to reduce its use of higher costing certificates of deposit as a funding source.

For the quarter ended March 31, 2013, the net interest margin was 2.68%, as compared to 2.77% for the same period in 2012. For the six months ended March 31, 2013, the net interest margin was 2.69%, as compared to 2.83% for the same period in 2012. The decrease in the net interest margin was consistent with the decline in net interest income as the yields on interest-earning assets declined to a greater degree than the rates paid on interest-bearing liabilities due to the already low level of the Bank's cost of funds.

Average Balances, Net Interest Income, and Yields Earned and Rates Paid. The following table shows for the periods indicated the total dollar amount of interest earned from average interest-earning assets and the resulting yields, as well as the interest expense on average interest-bearing liabilities and the resulting costs, expressed both in dollars and rates, and the net interest margin.  Average yields and rates have been annualized.  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 March 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2013 | | | 2012 | | |
| | Average Balance | Interest | Average Yield/Rate | Average Balance | Interest | Average Yield/Rate |
| | (Dollars in Thousands) | | | | | |
| Interest-earning assets: | | | | | | |
| Investment securities | $89,131 | $552 | 2.48 % | $83,345 | $558 | 2.68 % |
| Mortgage-backed securities | 61,140 | 544 | 3.56 | 90,334 | 975 | 4.32 |
| Loans receivable(1) | 272,891 | 3,135 | 4.60 | 240,076 | 3,251 | 5.42 |
| Other interest-earning assets | 42,206 | 22 | 0.21 | 66,443 | 29 | 0.17 |
| Total interest-earning assets | 465,368 | 4,253 | 3.66 | 480,198 | 4,813 | 4.01 |
| Cash and non-interest-bearing balances | 2,395 | | | 2,788 | | |
| Other non-interest-earning assets | 16,315 | | | 18,013 | | |
| Total assets | $484,078 | | | $500,999 | | |
| Interest-bearing liabilities: | | | | | | |
| Savings accounts | $71,579 | 59 | 0.33 | $69,630 | 111 | 0.64 |
| Money market deposit and NOW accounts | 103,463 | 88 | 0.34 | 104,073 | 131 | 0.50 |
| Certificates of deposit | 240,553 | 991 | 1.65 | 261,162 | 1,249 | 1.91 |
| Total deposits | 415,595 | 1,138 | 1.10 | 434,865 | 1,491 | 1.37 |
| Advances from Federal Home Loan Bank | 340 | - | 0.00 | 554 | 1 | 0.72 |
| Advances from borrowers for taxes and insurance | 1,989 | 1 | 0.20 | 1,692 | 1 | 0.24 |
| Total interest-bearing liabilities | 417,924 | 1,139 | 1.09 | 437,111 | 1,493 | 1.37 |
| Non-interest-bearing liabilities: | | | | | | |
| Non-interest-bearing demand accounts | 3,208 | | | 3,696 | | |
| Other liabilities | 2,706 | | | 2,038 | | |
| Total liabilities | 423,838 | | | 442,845 | | |
| Stockholders’ equity | 60,240 | | | 58,154 | | |
| Total liabilities and stockholders’ equity | $484,078 | | | $500,999 | | |
| Net interest-earning assets | $47,444 | | | $43,087 | | |
| Net interest income; interest rate spread | | $3,114 | 2.57 % | | $3,320 | 2.64 % |
| Net interest margin(2) | | | 2.68 % | | | 2.77 % |

| | | |
|---|---|---|
| Average interest-earning assets to average interest-bearing liabilities | 111.35 % | 109.86 % |

(1) Includes non-accrual loans. Calculated net of unamortized deferred fees, undisbursed portion of loans-in-process and the allowance for loan losses.

(2) Equals net interest income divided by average interest-earning assets.

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| | Six Months Ended March 31, | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2013 | | | | 2012 | | | |
| | Average Balance | Interest | Average Yield/Rate | | Average Balance | Interest | Average Yield/Rate | |
| | (Dollars in Thousands) | | | | | | | |
| Interest-earning assets: | | | | | | | | |
| Investment securities | $81,182 | $1,028 | 2.53 | % | $88,556 | $1,203 | 2.72 | % |
| Mortgage-backed securities | 64,883 | 1,178 | 3.63 | | 89,369 | 2,019 | 4.52 | |
| Loans receivable(1) | 270,611 | 6,388 | 4.72 | | 238,958 | 6,519 | 5.46 | |
| Other interest-earning assets | 51,035 | 56 | 0.22 | | 62,598 | 55 | 0.18 | |
| Total interest-earning assets | 467,711 | 8,650 | 3.70 | | 479,481 | 9,796 | 4.09 | |
| Cash and non-interest-bearing balances | 2,558 | | | | 2,822 | | | |
| Other non-interest-earning assets | 17,527 | | | | 18,094 | | | |
| Total assets | $487,796 | | | | $500,397 | | | |
| Interest-bearing liabilities: | | | | | | | | |
| Savings accounts | $71,314 | 119 | 0.33 | | $69,601 | 224 | 0.64 | |
| Money market deposit and NOW accounts | 104,512 | 181 | 0.35 | | 104,431 | 274 | 0.52 | |
| Certificates of deposit | 242,528 | 2,057 | 1.70 | | 259,583 | 2,504 | 1.93 | |
| Total deposits | 418,354 | 2,357 | 1.13 | | 433,615 | 3,002 | 1.38 | |
| Advances from Federal Home Loan Bank | 359 | - | 0.00 | | 559 | 2 | 0.72 | |
| Advances from borrowers for taxes and insurance | 1,853 | 2 | 0.22 | | 1,528 | 3 | 0.39 | |
| Total interest-bearing liabilities | 420,566 | 2,359 | 1.12 | | 435,702 | 3,007 | 1.38 | |
| Non-interest-bearing liabilities: | | | | | | | | |
| Non-interest-bearing demand accounts | 3,317 | | | | 3,925 | | | |
| Other liabilities | 3,818 | | | | 2,830 | | | |
| Total liabilities | 427,701 | | | | 442,457 | | | |
| Stockholders' equity | 60,095 | | | | 57,940 | | | |
| Total liabilities and stockholders' equity | $487,796 | | | | $500,397 | | | |
| Net interest-earning assets | $47,145 | | | | $43,779 | | | |
| Net interest income; interest rate spread | | $6,291 | 2.58 | % | | $6,789 | 2.71 | % |
| Net interest margin(2) | | | 2.69 | % | | | 2.83 | % |
| Average interest-earning assets to average interest-bearing liabilities | | 111.21 % | | | | 110.05 % | | |

(1) Includes non-accrual loans.  Calculated net of unamortized deferred fees, undisbursed portion of loans-in-process and allowance for loan losses.

(2) Equals net interest income divided by average interest-earning assets.

Provisions for loan losses.  The allowance is maintained at a level sufficient to provide for estimated probable losses in the loan portfolio at each reporting date.  At least quarterly, management performs an analysis to identify the inherent risk of loss in the Company’s loan portfolio. This analysis includes a qualitative evaluation of concentrations of credit, past loss experience, current economic conditions, amount and composition of the loan portfolio (including loans being specifically monitored by management), estimated fair value of underlying collateral, delinquencies, and other factors.

The Company's methodology for assessing the adequacy of the allowance establishes both specific and general pooled allocations of the allowance. Loans are assigned ratings, either individually for larger credits or in homogeneous pools, based on an internally developed grading system. The resulting determinations are reviewed and approved by senior management.

The Company did not establish a provision for loan loss for the three or six month periods ended March 31, 2013, while the Company established a provision for loan losses of $100,000 for the quarter ended March 31, 2012 and $250,000 for the six month period ended March 31, 2012. No provisions were deemed necessary for the 2013 periods as recoveries of $585,000 and $785,000 were recognized during the three and six month periods ended March 31, 2013, respectively, on a previously fully charged-off construction loan which led to an increase in the loan loss allowance sufficient to address the inherent risk and known losses associated with the loan portfolio. At March 31, 2013, the Company's non-performing assets totaled $7.4 million or 1.6% of total assets as compared to $16.0 million or 3.3% of total assets at September 30, 2012. Non-performing assets included $6.2 million in non-performing loans of which $4.1 million consisted of one-to-four family residential loans and $2.1 million were commercial real estate loans. Non-performing assets also included six one-to-four family residential real estate owned properties totaling $1.3 million. The decrease in non-performing assets during the six months ended March 31, 2013 was primarily due to the January 2013 sale of a group of loans related to a condominium project located in Philadelphia in which the Bank was the lead lender and held a $9.2 million investment. In connection with the closing of the loan sale, the Bank and the other loan participants extended a loan to an affiliate of the borrower, the proceeds of which were used to reduce the principal balance due on the project. The Bank's portion of such loan is approximately $1.3 million. The new loan was classified as a troubled debt restructuring and is included in the $7.4 million of non-performing assets described above. The new loan is performing in accordance with its terms. The Bank did not incur any additional losses upon completion of the sale of the loans beyond the $968,000 loss already recognized in prior periods. The allowance for loan losses totaled $2.5 million, or 0.9% of total loans and 40.7% of non-performing loans at March 31, 2013 as compared to $1.9 million, or 0.7% of total loans and 13.4% of non-performing loans at September 30, 2012.

Non-interest income. Non-interest income amounted to $199,000 and $414,000 for the three and six month periods ended March 31, 2013, compared with $133,000 and $306,000 for the same periods in 2012. The fluctuation in the periods primarily related to decreases in the other than temporary impairment ("OTTI") charges related to non-agency mortgage-backed securities received by the Company as a result of its redemption in kind of an investment in a mutual fund.

Non-interest expenses. For the quarter ended March 31, 2013, non-interest expense increased $117,000 compared to the same period in the prior year, while non-interest expense increased $19,000 for the six month period ended March 31, 2013 compared to the same period in the prior year. The increases for the 2013 periods primarily related to increased writedowns due to declines in the value of real estate owned properties under agreement of sale for the quarter ending June 30, 2013. The increases were partially offset by decreases in professional services expense.

Income tax expense. The Company recorded income tax expense for the quarter and six months ended March 31, 2013 of $186,000 and $537,000, respectively, compared to income tax expense of $273,000 and $494,000, respectively, for the quarter and six months ended March 31, 2012. The tax expense was adversely impacted by the decline in available unrealized capital gains resulting in an increase in the valuation allowance recognized in the 2012 and 2013 periods related to the deferred tax asset for the capital loss carryforward created in connection with the redemption in kind referenced above.

LIQUIDITY AND CAPITAL RESOURCES

The Company's liquidity, represented by cash and cash equivalents, is a product of its operating, investing and financing activities. Our primary sources of funds are from deposits, scheduled principal and interest payments on 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 and securities prepayments can be greatly influenced by market rates of interest, economic conditions and competition. We also maintain excess funds in short-term, interest-bearing assets that provide additional liquidity. At March 31, 2013, our cash and cash equivalents amounted to $33.6 million. In addition, our available for sale investment and mortgage-backed securities amounted to an aggregate of $62.7 million at such date.

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 March 31, 2013, the Company had $7.5 million in outstanding commitments to originate fixed and variable-rate loans, not including loans in process. The Company also had commitments under unused lines of credit of $6.1 million and letters of credit outstanding of $187,000 at March 31, 2013. Certificates of deposit at March 31, 2013 maturing in one year or less totaled $141.4 million. Based upon historical experience, we anticipate that a significant portion of the maturing certificates of deposit will be redeposited with us.

In addition to cash flows 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 should the need arise. Our borrowings consist solely of advances from the Federal Home Loan Bank of Pittsburgh ("FHLB"), of which we are a member. Under terms of the collateral agreement with the FHLB, we pledge residential mortgage loans as well as our stock in the FHLB as collateral for such advances. However, use of FHLB advances has been modest. At March 31, 2013, we had $340,000 in outstanding FHLB advances and had the ability to obtain an additional $135.0 million in FHLB advances. Additional borrowing capacity with the FHLB could be obtained with the pledging of certain investment securities. The Bank has also obtained approval to borrow from the Federal Reserve Bank discount window.

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

The following table summarizes the Company's and Bank's regulatory capital ratios as of March 31, 2013 and September 30, 2012 and compares them to current regulatory guidelines.

| | Actual Ratio | | Required for Capital Adequacy Purposes | | To Be Well Capitalized Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| March 31, 2013: | | | | | | |
| Tier 1 capital (to average assets) | | | | | | |
| The Company | 12.24 | % | 4.0 | % | N/A | |
| The Bank | 11.47 | % | 4.0 | % | 5.0 | % |
| Tier 1 capital (to risk-weighted assets) | | | | | | |
| The Company | 26.74 | % | 4.0 | % | N/A | |
| The Bank | 25.06 | % | 4.0 | % | 6.0 | % |
| Total capital (to risk-weighted assets) | | | | | | |
| The Company | 27.87 | % | 8.0 | % | N/A | |
| The Bank | 26.19 | % | 8.0 | % | 10.0 | % |
| September 30, 2012: | | | | | | |
| Tier 1 capital (to average assets) | | | | | | |
| Company | 11.73 | % | 4.0 | % | N/A | |
| Bank | 10.95 | % | 4.0 | % | 5.0 | % |
| Tier 1 capital (to risk-weighted assets) | | | | | | |
| Company | 27.51 | % | 4.0 | % | N/A | |
| Bank | 25.69 | % | 4.0 | % | 6.0 | % |
| Total capital (to risk-weighted assets) | | | | | | |
| Company | 28.39 | % | 8.0 | % | N/A | |
| Bank | 26.57 | % | 8.0 | % | 10.0 | % |

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 changes in the relative purchasing power of money over time due to inflation.

Unlike most industrial companies, substantially all of the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution's performance than the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the price of goods and services, since such prices are affected by inflation to a larger extent than interest rates. In the current interest rate environment, liquidity and the maturity structure of the Company's assets and liabilities are critical to the maintenance of acceptable performance levels.

How We Manage Market Risk. Market risk is the risk of loss from adverse changes in market prices and rates. Our market risk arises primarily from interest rate risk which is inherent in our lending, investment and deposit gathering activities. To that end, management actively monitors and manages interest rate risk exposure. In addition to market risk, our primary risk is credit risk on our loan portfolio. We attempt to manage credit risk through our loan underwriting and oversight policies.

The principal objective of our interest rate risk management function is to evaluate the interest rate risk embedded in certain balance sheet accounts, determine the level of risk appropriate given our business strategy, operating environment, capital and liquidity requirements and performance objectives, and manage the risk consistent with approved guidelines. We seek to manage our exposure to risks from changes in interest rates while at the same time trying to improve our net interest spread. We monitor interest rate risk as such risk relates to our operating strategies. We have established an Asset/Liability Committee which is comprised of our President and Chief Executive Officer, Chief Financial Officer, Chief Lending Officer, Treasurer and Controller. The Asset/Liability Committee meets on a regular basis and is responsible for reviewing our asset/liability policies and interest rate risk position. Both the extent and direction of shifts in interest rates are uncertainties that could have a negative impact on future earnings.

In recent years, we primarily have reduced our investment in longer term fixed rate callable agency bonds and increased our portfolio of step-up callable agency bonds and agency issued mortgage-backed securities. However, notwithstanding the foregoing steps, we remain subject to a significant level of interest rate risk in a low interest rate environment due to the high proportion of our loan portfolio that consists of fixed-rate loans as well as our decision to invest a significant amount of our assets in long-term, fixed-rate investment and mortgage-backed securities.

Gap Analysis. The matching of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are “interest rate sensitive” and by monitoring a Company’s interest rate sensitivity “gap.” An asset or liability is said to be interest rate sensitive within a specific time period if it will mature or reprice within that time period. The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within that same time period. A gap is considered positive when the amount of interest rate sensitive assets exceeds the amount of interest rate sensitive liabilities. A gap is considered negative when the amount of interest rate sensitive liabilities exceeds the amount of interest rate sensitive assets. During a period of rising interest rates, a negative gap would tend to affect adversely net interest income while a positive gap would tend to result in an increase in net interest income. Conversely, during a period of falling interest rates, a negative gap would tend to result in an increase in net interest income while a positive gap would tend to affect adversely net interest income.

The following table sets forth the amounts of our interest-earning assets and interest-bearing liabilities outstanding at March 31, 2013, which we expect, based upon certain assumptions, to reprice or mature in each of the future time periods shown (the “GAP Table”). Except as stated below, the amounts of assets and liabilities shown which reprice or mature during a particular period were determined in accordance with the earlier of term to repricing or the contractual maturity of the asset or liability. The table sets forth an approximation of the projected repricing of assets and liabilities at March 31, 2013, on the basis of contractual maturities, anticipated prepayments, and scheduled rate adjustments within a three-month period and subsequent selected time intervals. The loan amounts in the table reflect principal balances expected to be redeployed and/or repriced as a result of contractual amortization and anticipated prepayments of adjustable-rate loans and fixed-rate loans, and as a result of contractual rate adjustments on adjustable-rate loans. Annual prepayment rates for variable-rate and fixed-rate single-family and multi-family residential and commercial mortgage loans are assumed to range from 10.4% to 31.1%. The annual prepayment rate for mortgage-backed securities is assumed to range from 0.4% to 25.0%. For savings accounts, checking accounts and money markets, the decay rates vary on annual basis over a ten year period.

| | 3 Months or Less | More than 3 Months to 1 Year | More than 1 Year to 3 Years | More than 3 Years to 5 Years | More than 5 Years | Total Amount |
|---|---|---|---|---|---|---|
| | | | (Dollars in Thousands) | | | |
| Interest-earning assets(1): | | | | | | |
| Investment and mortgage-backed securities(2) | $ 6,412 | $ 17,755 | $ 16,951 | $ 10,528 | $ 97,662 | $ 149,308 |
| Loans receivable(3) | 32,029 | 48,342 | 93,750 | 46,702 | 58,437 | 279,260 |
| Other interest-earning assets(4) | 32,826 | - | - | - | - | 32,826 |
| Total interest-earning assets | $ 71,267 | $ 66,097 | $ 110,701 | $ 57,230 | $ 156,099 | $ 461,394 |
| Interest-bearing liabilities: | | | | | | |
| Savings accounts | $ 1,923 | $ 5,110 | $ 9,869 | $ 9,049 | $ 47,278 | $ 73,229 |
| Money market deposit and NOW accounts | 3,957 | 11,871 | 23,657 | 17,765 | 46,282 | 103,532 |
| Certificates of deposit | 55,226 | 86,199 | 53,103 | 41,692 | - | 236,220 |
| Advances from Federal Home Loan Bank | - | - | 340 | - | - | 340 |
| Advances from borrowers for taxes and insurance | 1,266 | - | - | - | - | 1,266 |
| Total interest-bearing liabilities | $ 62,372 | $ 103,180 | $ 86,969 | $ 68,506 | $ 93,560 | $ 414,587 |
| Interest-earning assets less interest-bearing liabilities | $ 8,895 | ($ 37,083 ) | $ 23,732 | ($ 11,276 ) | $ 62,539 | $ 46,807 |
| Cumulative interest-rate sensitivity gap (5) | $ 8,895 | ($ 28,188 ) | ($ 4,456 ) | ($ 15,732 ) | $ 46,807 | |
| Cumulative interest-rate gap as a percentage of total assets at March 31, 2013 | 1.86 % | -5.88 % | -0.93 % | -3.28 % | 9.77 % | |
| Cumulative interest-earning assets as a percentage of cumulative interest-bearing liabilities at Marech 31, 2013 | 114.26 % | 82.97 % | 98.24 % | 95.10 % | 111.29 % | |

(1) Interest-earning assets are included in the period in which the balances are expected to be redeployed and/or repriced as a result of anticipated prepayments, scheduled rate adjustments and contractual maturities.

(2) For purposes of the gap analysis, investment securities are stated at amortized cost.

(3) For purposes of the gap analysis, loans receivable includes non-performing loans and is gross of the allowance for loan losses and unamortized deferred loan fees, but net of the undisbursed portion of loans-in-process.

(4) Includes FHLB stock.

(5) Cumulative interest-rate sensitivity gap represents the difference between interest-earning assets and interest-bearing liabilities.

Certain shortcomings are inherent in the method of analysis presented in the foregoing table. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain assets, such as variable-rate loans, have features which restrict changes in interest rates both on a short-term basis and over the life of the asset. Further, in the event of a change in interest rates, prepayment and early withdrawal levels would likely deviate significantly from those assumed in calculating the table. Finally, the ability of many borrowers to service their variable-rate loans may be adversely affected in the event of an interest rate increase.

Net Portfolio Value Analysis.  Our interest rate sensitivity also is monitored by management through the use of a model which generates estimates of the changes in our net portfolio value ("NPV") over a range of interest rate scenarios.  NPV is the present value of expected cash flows from assets, liabilities and off-balance sheet contracts.  The NPV ratio, under any interest rate scenario, is defined as the NPV in that scenario divided by the market value of assets in the same scenario.  The "Sensitivity Measure" is the decline in the NPV ratio, in basis points, caused by a 2% increase or decrease in rates, whichever produces a larger decline.  The following table sets forth our NPV as of March 31, 2013 and reflects the changes to NPV as a result of immediate and sustained changes in interest rates as indicated.

| Change in Interest Rates In Basis Points (Rate Shock) | Net Portfolio Value | | | NPV as % of Portfolio Value of Assets | |
|---|---|---|---|---|---|
| | Amount | $ Change | % Change | NPV Ratio | Change |
| | (Dollars in Thousands) | | | | |
| 300 | $48,130 | $(32,171) | (40.06)% | 11.29% | (5.21)% |
| 200 | 59,451 | (20,850) | (25.96)% | 13.32% | (3.18)% |
| 100 | 71,057 | (9,244) | (11.51)% | 15.20% | (1.30)% |
| Static | 80,301 | - | - | 16.50% | - |
| (100) | 79,887 | (414) | (0.52)% | 16.10% | (0.40)% |
| (200) | 80,366 | 65 | 0.08% | 15.95% | (0.55)% |
| (300) | 87,379 | 7,078 | 8.81% | 17.04% | 0.54% |

At September 30, 2012, the Company's NPV was $78.3 million or 15.69% of the market value of assets.  Following a 200 basis point increase in interest rates, the Company's "post shock" NPV would be $69.0 million or 14.67% of the market value of assets.

As is the case with the GAP Table, certain shortcomings are inherent in the methodology used in the above interest rate risk measurements.  Modeling changes in NPV requires the making of certain assumptions which may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates.  In this regard, the models presented assume that the composition of our interest sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured and also assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or repricing of specific assets and liabilities.  Accordingly, although the NPV model provides an indication of interest rate risk exposure at a particular point in time, such model is not intended to and does not provide a precise forecast of the effect of changes in market interest rates on net interest income and will differ from actual results.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

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 Rule 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 as of the end of period covered by this report, 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 Rule 13a-15(f) or 15d-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

### Item 1. Legal Proceedings

The Company is involved in various legal proceedings occurring in the ordinary course of business. Management of the Company, based on discussions with litigation counsel, does not believe that such proceedings will have a material adverse effect on the financial condition or operations of the Company. There can be no assurance that any of the outstanding legal proceedings to which the Company is a party will not be decided adversely to the Company's interests and have a material adverse effect on the financial condition and operations of the Company.

### Item 1A. Risk Factors

Not applicable

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

| | |
|---|---|
| (a) | Not applicable |
| (b) | Not applicable |

(c) There were no repurchases of common stock by the Company or purchases of common stock by the MHC during the quarter ended March 31, 2013.

### Item 3. Defaults Upon Senior Securities

Not applicable

### Item 4. Mine Safety Disclosures

Not applicable

### Item 5. Other Information

Not applicable

### Item 6. Exhibits

| Exhibit No. | Description |
|---|---|
| 31.1 | Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer |
| 32.0 | Section 1350 Certifications |

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The following Exhibits are being furnished* as part of this quarterly 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.* |

* 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.

SIGNATURES

Pursuant to the requirements 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.

PRUDENTIAL BANCORP, INC. OF PENNSYLVANIA

| | |
|---|---|
| Date: May 15, 2013 | By: /s/<br>Thomas A. Vento<br>Chairman, President and Chief Executive Officer |
| Date: May 15, 2013 | By: /s/<br>Joseph R. Corrato<br>Executive Vice President and Chief Financial Officer |