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Home Federal Bancorp, Inc.
Form 10-Q
August 07, 2009
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2009

or

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

For the transition period from _____ to _____

Commission File Number: 001-33795

HOME FEDERAL BANCORP, INC.
(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of
incorporation
or organization)

68-0666697
(I.R.S. Employer
I.D. Number)

500 12th Avenue South, Nampa, Idaho
(Address of principal executive offices)

83651
(Zip Code)

Registrant's telephone number, including area code: (208) 466-4634

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

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company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting
company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date: Common Stock, \$.01 par value per share, 16,698,168 shares outstanding as of August 5, 2009.

HOME FEDERAL BANCORP, INC.

FORM 10-Q
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Item 1. Financial Statements

| HOME FEDERAL BANCORP, INC. AND SUBSIDIARY CONSOLIDATED BALANCE SHEETS (In thousands, except share data) (Unaudited) | June 30, 2009 | September 30, 2008 |
|---|-------------------|-----------------------|
| ASSETS | | |
| Cash and amounts due from depository institutions | \$ 26,778 | \$ 23,270 |
| Certificate of deposit in correspondent bank | - | 5,000 |
| Mortgage-backed securities available for sale, at fair value | 169,716 | 188,787 |
| Loans receivable, net of allowance for loan losses of \$8,266 and \$4,579 | 418,198 | 459,813 |
| Loans held for sale | 5,064 | 2,831 |
| Accrued interest receivable | 2,209 | 2,681 |
| Property and equipment, net | 17,057 | 15,246 |
| Mortgage servicing rights, net | - | 1,707 |
| Bank owned life insurance | 11,906 | 11,590 |
| Federal Home Loan Bank of Seattle ("FHLB") stock, at cost | 9,591 | 9,591 |
| Real estate and other property owned | 8,614 | 650 |
| Deferred tax asset | 1,853 | 1,770 |
| Other assets | 1,757 | 2,134 |
| TOTAL ASSETS | \$ 672,743 | \$ 725,070 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| LIABILITIES | | |
| Deposit accounts: | | |
| Noninterest-bearing demand deposits | \$ 39,931 | \$ 41,398 |
| Interest-bearing demand deposits | 131,202 | 127,714 |
| Savings deposits | 35,880 | 26,409 |
| Certificates of deposit | 168,983 | 177,404 |
| Total deposit accounts | 375,996 | 372,925 |
| Advances by borrowers for taxes and insurance | 589 | 1,386 |
| Interest payable | 370 | 552 |
| Deferred compensation | 5,219 | 5,191 |
| FHLB advances and other borrowings | 88,891 | 136,972 |
| Other liabilities | 3,030 | 2,857 |
| Total liabilities | 474,095 | 519,883 |
| STOCKHOLDERS' EQUITY | | |
| Serial preferred stock, \$.01 par value; 10,000,000 authorized; | | |
| Issued and outstanding, none | - | - |
| Common stock, \$.01 par value; 90,000,000 authorized; | | |
| Issued and outstanding: | 167 | 174 |
| June 30, 2009 – 17,445,311 issued, 16,698,168 outstanding | | |
| Sept. 30, 2008 – 17,412,449 issued, 17,374,161 outstanding | | |
| Additional paid-in capital | 150,391 | 157,205 |
| Retained earnings | 55,643 | 59,813 |
| Unearned shares issued to employee stock ownership plan ("ESOP") | (9,926) | (10,605) |

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| | | |
|---|-------------------|-------------------|
| Accumulated other comprehensive income (loss) | 2,373 | (1,400) |
| Total stockholders' equity | 198,648 | 205,187 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 672,743 | \$ 725,070 |

See accompanying notes.

1

HOME FEDERAL BANCORP, INC.
AND SUBSIDIARY
CONSOLIDATED STATEMENTS
OF OPERATIONS

(In thousands, except share data)
(Unaudited)

| | Three Months Ended June 30, | | Nine Months Ended June 30, | |
|--|--------------------------------|------------|-------------------------------|---------------|
| | 2009 | 2008 | 2009 | 2008 |
| Interest and dividend income: | | | | |
| Loan interest | \$ 6,418 | \$ 7,544 | \$ 20,337 | \$ 23,390 |
| Mortgage-backed security interest | 1,983 | 2,372 | 6,311 | 6,463 |
| Other interest and dividends | 9 | 177 | 20 | 1,001 |
| Total interest and dividend income | 8,410 | 10,093 | 26,668 | 30,854 |
| Interest expense: | | | | |
| Deposits | 1,629 | 2,429 | 5,389 | 8,515 |
| FHLB advances and other borrowings | 1,068 | 1,752 | 3,861 | 5,594 |
| Total interest expense | 2,697 | 4,181 | 9,250 | 14,109 |
| Net interest income | 5,713 | 5,912 | 17,418 | 16,745 |
| Provision for loan losses | 3,450 | 652 | 8,085 | 1,317 |
| Net interest income after provision for loan losses | 2,263 | 5,260 | 9,333 | 15,428 |
| Noninterest income: | | | | |
| Service charges and fees | 2,008 | 2,396 | 6,009 | 6,731 |
| Gain on sale of loans | 416 | 213 | 1,013 | 560 |
| Increase in cash surrender value of bank owned life insurance | 107 | 106 | 317 | 314 |
| Loan servicing fees | - | 116 | 54 | 369 |
| Mortgage servicing rights, net | - | (63) | (31) | (206) |
| Other | 80 | (33) | 55 | 75 |
| Total noninterest income | 2,611 | 2,735 | 7,417 | 7,843 |
| Noninterest expense: | | | | |
| Compensation and benefits | 3,594 | 3,840 | 10,948 | 11,592 |
| Occupancy and equipment | 804 | 771 | 2,303 | 2,242 |
| Data processing | 654 | 615 | 1,773 | 1,668 |
| Advertising | 211 | 241 | 656 | 786 |
| Postage and supplies | 126 | 147 | 409 | 468 |
| Professional services | 236 | 130 | 870 | 533 |
| Insurance and taxes | 783 | 158 | 1,244 | 383 |
| Other | 606 | 272 | 1,416 | 809 |
| Total noninterest expense | 7,014 | 6,174 | 19,619 | 18,481 |
| Income (loss) before income taxes | (2,140) | 1,821 | (2,869) | 4,790 |
| Income tax expense (benefit) | (894) | 702 | (1,298) | 1,779 |
| NET INCOME (LOSS) | \$ (1,246) | \$ 1,119 | \$ (1,571) | \$ 3,011 |
| Earnings (loss) per share: | | | | |
| Basic | \$ (0.08) | \$ 0.07 | \$ (0.10) | \$ 0.19(1) |
| Diluted | (0.08) | 0.07 | (0.10) | 0.19(1) |
| Weighted average number of shares outstanding: | | | | |
| Basic | 15,352,714 | 16,007,599 | 15,742,102 | 16,237,911(1) |
| Diluted | 15,352,714 | 16,043,435 | 15,742,102 | 16,255,548(1) |

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| | | | | | | | | |
|-------------------------------|----|-------|----|-------|----|-------|----|----------|
| Dividends declared per share: | \$ | 0.055 | \$ | 0.055 | \$ | 0.165 | \$ | 0.158(1) |
|-------------------------------|----|-------|----|-------|----|-------|----|----------|

(1) Earnings (loss) per share, average shares outstanding, and dividends per share have been adjusted to reflect the impact of the second-step conversion and reorganization of Home Federal Bancorp, Inc., which occurred on December 19, 2007.

See accompanying notes.

2

HOME FEDERAL BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY AND COMPREHENSIVE
INCOME

(In thousands, except share data) (Unaudited)

| | Common Stock | | Additional Paid-In | Retained | Unearned Shares Issued to Employee Stock Ownership Plan | Accumulated Other Comprehensive Income (Loss) | Total |
|---|--------------|--------|-----------------------|-----------|---|---|------------|
| | Shares | Amount | Capital | Earnings | | | |
| Balance at Sept. 30, 2007 | 15,232,243 | \$ 152 | \$ 59,613 | \$ 58,795 | \$ (3,698) | \$ (2,225) | \$ 112,637 |
| Second Step Conversion(1) | 2,073,619 | 21 | 95,938 | | (8,160) | | 87,799 |
| Dissolution of Mutual Holding Company | | | 50 | | | | 50 |
| Restricted stock issued, net of forfeitures | 13,502 | | | | | | - |
| ESOP shares committed to be released | | | (23) | | 1,253 | | 1,230 |
| Exercise of stock options | 54,797 | 1 | 605 | | | | 606 |
| Share-based compensation | | | 1,022 | | | | 1,022 |
| Dividends paid (\$0.213 per share) (2) (3) | | | | (2,987) | | | (2,987) |
| Comprehensive income: | | | | | | | |
| Net income | | | | 4,005 | | | 4,005 |
| Other comprehensive income: | | | | | | | |
| Change in unrealized holding loss on securities available for sale, net of taxes | | | | | | 825 | 825 |
| | | | | | | | 4,830 |

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| | | | | | | | | |
|--|------------|--------|------------|-----------|------------|----------|------------|-------|
| Comprehensive income | | | | | | | | |
| Balance at Sept. 30, 2008 | 17,374,161 | 174 | 157,205 | 59,813 | (10,605) | (1,400) | 205,187 | |
| Restricted stock issued, net of forfeitures | 159,115 | 2 | (2) | | | | - | |
| ESOP shares committed to be released | | | 12 | | 679 | | 691 | |
| Exercise of stock options | 32,862 | | 353 | | | | 353 | |
| Share-based compensation | | | 730 | | | | 730 | |
| Treasury shares purchased | (867,970) | (9) | (7,886) | | | | (7,895) | |
| Dividends paid (\$0.165 per share) | | | | | (2,599) | | (2,599) | |
| Tax adjustment | | | (21) | | | | (21) | |
| Comprehensive income: | | | | | | | | |
| Net loss | | | | | (1,571) | | (1,571) | |
| Other comprehensive income: | | | | | | | | |
| Change in unrealized holding loss on securities available for sale, net of taxes | | | | | | | | |
| Adjustment for realized gains, net of taxes of \$20 | | | | | | | 3,804 | 3,804 |
| Adjustment for realized gains, net of taxes of \$20 | | | | | | | (31) | (31) |
| Comprehensive income | | | | | | | | |
| Balance at June 30, 2009 | 16,698,168 | \$ 167 | \$ 150,391 | \$ 55,643 | \$ (9,926) | \$ 2,373 | \$ 198,648 | |

- (1) The total effect on equity accounts from the second-step conversion has changed from the December 31, 2007 reported numbers due to adjustments such as the effect of fractional shares and payment of additional expenses related to the second-step conversion.
- (2) Home Federal MHC waived its receipt of dividends on the 8,979,246 shares that it owned.
- (3) Dividends per share have been adjusted to reflect the impact of the second-step conversion of Home Federal Bancorp, Inc., which occurred on December 19, 2007.

See accompanying notes.

3

| HOME FEDERAL BANCORP, INC. AND SUBSIDIARY CONSOLIDATED STATEMENTS OF CASH FLOWS (In thousands) (Unaudited) | Nine Months Ended June 30, | |
|--|-------------------------------|----------|
| | 2009 | 2008 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income (loss) | \$ (1,571) | \$ 3,011 |
| Adjustments to reconcile net income (loss) to cash provided by operating activities: | | |
| Depreciation and amortization | 1,294 | 1,247 |
| Net amortization (accretion) of premiums and discounts on investments | 9 | (18) |
| Loss on sale of fixed assets and repossessed assets | 82 | 119 |
| Gain on sale of securities available for sale | (51) | - |
| ESOP shares committed to be released | 691 | 423 |
| Equity compensation expense | 730 | 779 |
| Provision for loan losses | 8,085 | 1,317 |
| Valuation allowance on other real estate owned | 552 | - |
| Accrued deferred compensation expense, net | 28 | 513 |
| Net deferred loan fees | (77) | 54 |
| Deferred income tax benefit | (2,598) | (598) |
| Net gain on sale of loans | (1,013) | (560) |
| Proceeds from sale of loans held for sale | 56,151 | 38,579 |
| Originations of loans held for sale | (57,371) | (37,193) |
| Net decrease in value of mortgage servicing rights | 31 | 207 |
| Loss on sale of mortgage servicing rights | 74 | - |
| Net increase in value of bank owned life insurance | (316) | (314) |
| Change in assets and liabilities: | | |
| Interest receivable | 472 | 5 |
| Other assets | 368 | 158 |
| Interest payable | (182) | (151) |
| Other liabilities | 154 | (903) |
| Net cash provided by operating activities | 5,542 | 6,675 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from maturities of mortgage-backed securities available for sale | 26,931 | 23,976 |
| Proceeds from sales of mortgage-backed securities available for sale | 1,203 | - |
| Purchases of mortgage-backed securities available for sale | (2,734) | (56,257) |
| Maturity of (Investment in) certificate of deposit | 5,000 | (5,000) |
| Sale of mortgage servicing rights | 1,602 | - |
| Purchases of property and equipment | (3,088) | (3,218) |
| Net decrease in loans | 23,910 | 9,720 |
| Proceeds from sale of fixed assets and repossessed assets | 1,090 | 501 |
| Net cash provided (used) by investing activities | 53,914 | (30,278) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Net increase (decrease) in deposits | 3,071 | (22,267) |
| Net decrease in advances by borrowers for taxes and insurance | (797) | (948) |
| Proceeds from FHLB advances | 18,000 | 59,715 |
| Repayment of FHLB advances | (67,582) | (94,863) |

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| | | |
|--|------------------|------------------|
| Proceeds from other borrowings | 1,501 | - |
| Net proceeds from stock issuance and exchange pursuant to second step conversion | - | 88,336 |
| Proceeds from exercise of stock options | 353 | 328 |
| Repurchases of common stock | (7,895) | - |
| Dividends paid | (2,599) | (2,099) |
| Net cash (used) provided by financing activities | (55,948) | 28,202 |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 3,508 | 4,599 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 23,270 | 20,588 |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 26,778 | \$ 25,187 |

(Continued)

See accompanying notes.

4

| HOME FEDERAL BANCORP, INC. AND SUBSIDIARY CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued) (In thousands) (Unaudited) | Nine Months Ended June 30, | |
|--|-------------------------------|-----------|
| | 2009 | 2008 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION: | | |
| Cash paid during the period for: | | |
| Interest | \$ 9,433 | \$ 14,259 |
| Income taxes | 2,545 | 2,610 |
| NONCASH INVESTING AND FINANCING ACTIVITIES: | | |
| Acquisition of real estate and other assets in settlement of loans | \$ 9,682 | \$ 1,137 |
| Fair value adjustment to securities available for sale, net of taxes | 3,804 | 117 |

See accompanying notes.

5

HOME FEDERAL BANCORP, INC. AND SUBSIDIARY
SELECTED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 - Basis of Presentation

The consolidated financial statements presented in this quarterly report include the accounts of Home Federal Bancorp, Inc., a Maryland corporation (the “Company”), and its wholly-owned subsidiary, Home Federal Bank (the “Bank”). The financial statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America for interim financial information and are unaudited. In preparing these financial statements, the Company has evaluated events and transactions for potential recognition or disclosure through August 6, 2009, the date the financial statements were available to be issued. All significant intercompany transactions and balances have been eliminated. In the opinion of the Company’s management, all adjustments consisting of normal recurring adjustments necessary for a fair presentation of the financial condition and results of operations for the interim periods included herein have been made. Operating results for the three and nine month periods ended June 30, 2009, are not necessarily indicative of the results that may be expected for the year ending September 30, 2009.

The Company was formed as the new stock holding company for the Bank in connection with the Bank’s conversion from the mutual holding company structure to the stock holding company structure, which was completed on December 19, 2007 (the “Conversion”). Prior to the completion of the Conversion, the Bank was the subsidiary of Home Federal Bancorp, Inc., a federally-chartered stock mid-tier holding company (“Old Home Federal”), and Old Home Federal was a subsidiary of Home Federal MHC, a federally-chartered mutual holding company. The Bank formed the mutual holding company structure in December 2004. As a result of the Conversion, Home Federal MHC and Old Home Federal ceased to exist and were replaced by the Company as the successor to Old Home Federal.

Certain information and note disclosures normally included in the Company’s annual consolidated financial statements have been condensed or omitted. Therefore, these consolidated financial statements and notes thereto should be read in conjunction with the audited financial statements and notes included in the Annual Report on Form 10-K for the year ended September 30, 2008 (“2008 Form 10-K”), filed with the Securities and Exchange Commission (“SEC”) on December 15, 2008.

Note 2 - Critical Accounting Estimates and Related Accounting Policies

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Changes in these estimates and assumptions are considered reasonably possible and may have a material impact on the consolidated financial statements, and thus actual results could differ from the amounts reported and disclosed herein. The Company considers the allowance for loan losses, deferred income taxes and valuation of real estate owned to be critical accounting estimates.

Allowance for loan losses. The procedures for assessing the adequacy of the allowance for loan losses reflect evaluation of credit risk after careful consideration and interpretation of relevant information. In developing this assessment, management must rely on estimates and exercise judgment regarding matters where the ultimate outcome is unknown, such as economic factors, developments affecting companies in specific industries and issues with respect to single borrowers. The allowance for loan losses is maintained at a level that management believes to be the best estimate of probable incurred losses inherent in the loan portfolio at the balance sheet dates presented. Depending on changes in circumstances, future assessments of credit risk may yield materially different results, which may require an increase or a decrease in the allowance for loan losses.

Deferred income taxes. Deferred income taxes are computed using the asset and liability approach as prescribed in Statement of Financial Accounting Standards (“SFAS”) No. 109, Accounting for Income Taxes. Under this method, a deferred tax asset or liability is determined based on the currently enacted tax rates applicable to the period in which the differences between the financial statement carrying amounts and tax basis of the existing assets and liabilities are expected to be reported in the Company’s income tax returns.

Real Estate Owned. Real estate properties acquired through, or in lieu of, loan foreclosure are initially recorded at the lesser of the outstanding loan balance or the fair value at the date of foreclosure minus estimated costs to sell. Any valuation adjustments required at the time of foreclosure are charged to the allowance for loan losses. After foreclosure, the properties are carried at the lower of carrying value or fair value less estimated costs to sell. Any subsequent valuation adjustments, operating expenses or income, and gains and losses on disposition of such properties are recognized in current operations. The valuation allowance is established based on our historical realization of losses and adjusted for current market trends.

Note 3 - Earnings (Loss) Per Share

Earnings (Loss) per share (“EPS”) is computed using the basic and diluted weighted average number of common shares outstanding during the period as applicable. Basic EPS is computed by dividing the Company’s net income or loss by the weighted average number of common shares outstanding for the period. Diluted EPS is computed by dividing net income by the diluted weighted average shares outstanding, which include common stock equivalent shares outstanding using the treasury stock method, unless such shares are anti-dilutive. Common stock equivalents arise from assumed conversion of outstanding stock options and vesting of restricted stock awards. ESOP shares are not considered outstanding for earnings per share purposes until they are committed to be released.

The following table presents the computation of basic and diluted EPS for the periods indicated:

| | Three Months Ended | | Nine Months Ended | |
|---|--------------------|------------|-------------------|------------|
| | June 30, | | June 30, | |
| | 2009 | 2008 | 2009 | 2008 |
| (in thousands, except share and per share data) | | | | |
| Basic EPS: | | | | |
| Net income (loss) | \$ (1,246) | \$ 1,119 | \$ (1,571) | \$ 3,011 |
| Weighted-average common shares outstanding | 15,352,714 | 16,007,599 | 15,742,102 | 16,237,911 |
| Basic EPS | \$ (0.08) | \$ 0.07 | \$ (0.10) | \$ 0.19 |
| Diluted EPS: | | | | |
| Net income (loss) | \$ (1,246) | \$ 1,119 | \$ (1,571) | \$ 3,011 |
| Weighted-average common shares outstanding | 15,352,714 | 16,007,599 | 15,742,102 | 16,237,911 |
| Net effect of dilutive stock options | - | 2,986 | - | - |
| Net effect of dilutive restricted stock | - | 32,850 | - | 17,637 |
| Weighted-average common shares outstanding and common stock equivalents | 15,352,714 | 16,043,435 | 15,742,102 | 16,255,548 |
| Diluted EPS | \$ (0.08) | \$ 0.07 | \$ (0.10) | \$ 0.19 |

For the nine months ended June 30, 2008, earnings (loss) per share and average shares outstanding have been adjusted to reflect the impact of the second-step conversion and reorganization of Home Federal Bancorp, Inc., which occurred on December 19, 2007.

Note 4 - Mortgage-Backed Securities

Mortgage-backed securities available for sale consisted of the following:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|-------------------|------------------------------|-------------------------------|-------------------|
| (in thousands) | | | | |
| June 30, 2009 | | | | |
| Issued by U.S. Government sponsored enterprises | \$ 162,472 | \$ 4,275 | \$ - | \$ 166,747 |
| Other | 3,290 | - | (321) | 2,969 |
| Total | \$ 165,762 | \$ 4,275 | \$ (321) | \$ 169,716 |
| September 30, 2008 | | | | |
| Issued by U.S. Government sponsored enterprises | \$ 187,730 | \$ 669 | \$ (2,669) | \$ 185,730 |
| Other | 3,390 | - | (333) | 3,057 |
| Total | \$ 191,120 | \$ 669 | \$ (3,002) | \$ 188,787 |

The fair value of impaired securities, the amount of unrealized losses and the length of time these unrealized losses existed as of June 30, 2009 were as follows:

| | Less than 12 months | | 12 months or longer | | Total | |
|--|---------------------|----------------------|---------------------|----------------------|---------------|----------------------|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| (in thousands) | | | | | | |
| Mortgage-backed securities, available for sale | \$ - | \$ - | \$2,969 | \$(321) | \$2,969 | \$(321) |

Management has evaluated these securities and has determined that the decline in fair value is not other than temporary. These securities have contractual maturity dates and, at June 30, 2009, management believes it is reasonably probable that principal and interest balances on these securities will be collected based on the performance, underwriting, credit support and vintage of the loans underlying the securities. However, continued deteriorating economic conditions may result in degradation in the performance of the loans underlying these securities in the future. The Company has the ability and intent to hold these securities for a reasonable period of time for a forecasted recovery of the amortized cost.

As of June 30, 2009, the Bank had pledged mortgage-backed securities with an amortized cost of \$70.3 million and a fair value of \$72.1 million as collateral for FHLB advances. Mortgage-backed securities with an amortized cost of \$3.4 million and a fair value of \$3.5 million at June 30, 2009, were pledged as collateral for a commercial repurchase agreement. Mortgage-backed securities with an amortized cost of \$4.8 million and a fair value of \$5.0 million at June 30, 2009, were pledged to the Federal Reserve Bank as collateral for treasury tax and loan funds held by the Bank and for borrowings from the discount window. As of June 30, 2009, and September 30, 2008, there was no balance owed by the Bank through the Federal Reserve Bank discount window.

Note 5 - Loans Receivable

Loans receivable are summarized as follows:

| | June 30, 2009 | | September 30, 2008 | |
|----------------------------------|---------------|---------------------|--------------------|---------------------|
| | Balance | Percent of Total | Balance | Percent of Total |
| (dollars in thousands) | | | | |
| Real Estate: | | | | |
| One- to four-family residential | \$ 176,038 | 41.21% | \$ 210,302 | 45.22% |
| Multi-family residential | 10,092 | 2.36 | 8,477 | 1.82 |
| Commercial | 154,209 | 36.10 | 151,733 | 32.62 |
| Total real estate | 340,339 | 79.67 | 370,512 | 79.66 |
| Real Estate Construction: | | | | |
| One- to four-family residential | 9,710 | 2.27 | 13,448 | 2.89 |
| Multi-family residential | - | - | 920 | 0.20 |
| Commercial and land development | 21,349 | 5.00 | 18,674 | 4.01 |
| Total real estate construction | 31,059 | 7.27 | 33,042 | 7.10 |
| Consumer: | | | | |
| Home equity | 48,404 | 11.33 | 52,954 | 11.38 |
| Automobile | 1,353 | 0.32 | 1,903 | 0.41 |
| Other consumer | 1,217 | 0.29 | 1,370 | 0.29 |
| Total consumer | 50,974 | 11.94 | 56,227 | 12.08 |
| Commercial business | 4,803 | 1.12 | 5,385 | 1.16 |
| | 427,175 | 100.00% | 465,166 | 100.00% |
| Premium on purchased loans | 184 | | 199 | |
| Deferred loan fees | (895) | | (973) | |
| Allowance for loan losses | (8,266) | | (4,579) | |
| Loans receivable, net | \$ 418,198 | | \$ 459,813 | |

Note 6 – Allowance for Loan Losses

Activity in the allowance for loan losses for the three and nine month periods ended June 30, 2009 and 2008, was as follows:

| | Three Months Ended June 30, | | Nine Months Ended June 30, | |
|---------------------------------|--------------------------------|----------|-------------------------------|----------|
| | 2009 | 2008 | 2009 | 2008 |
| (in thousands) | | | | |
| Beginning balance | \$ 7,333 | \$ 3,307 | \$ 4,579 | \$ 2,988 |
| Provision for loan losses | 3,450 | 652 | 8,085 | 1,317 |
| Losses on loans charged-off | (2,616) | (168) | (4,524) | (528) |
| Recoveries on loans charged-off | 99 | 10 | 126 | 24 |

| | | | | | | | | |
|----------------|----|-------|----|-------|----|-------|----|-------|
| Ending balance | \$ | 8,266 | \$ | 3,801 | \$ | 8,266 | \$ | 3,801 |
|----------------|----|-------|----|-------|----|-------|----|-------|

Note 7 – Fair Value Measurement

SFAS No. 157 defines fair value, establishes a consistent framework for measuring fair value and expands disclosure requirements about fair value measurements. SFAS No. 157, among other things, requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices for identical instruments in active markets.
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.
- Level 3 – Instruments whose significant value drivers are unobservable.

The following table summarized the Company's financial instruments that were measured at fair value on a recurring basis at June 30, 2009:

| | June 30, 2009 | | | |
|-------------------------------|----------------|---------|-----------|---------|
| | Total | Level 1 | Level 2 | Level 3 |
| | (in thousands) | | | |
| Securities available for sale | \$169,716 | - | \$169,716 | - |

Additionally, certain assets are measured at fair value on a non-recurring basis. These adjustments to fair value generally result from the application of lower-of-cost-or-market accounting or write-downs of individual assets due to impairment. The following table summarizes the Company's financial instruments that were measured at fair value on a non-recurring basis at June 30, 2009:

| | June 30, 2009 | | | |
|-------------------|----------------|---------|---------|---------|
| | Total | Level 1 | Level 2 | Level 3 |
| | (in thousands) | | | |
| Impaired loans | \$7,424 | - | - | \$7,424 |
| Real estate owned | 8,614 | - | - | 8,614 |

Impaired loans, which are measured for impairment using the fair value of the collateral at June 30, 2009, had a carrying amount of \$9.9 million, net of valuation allowances totaling \$2.4 million, resulting in an additional provision for loan losses of \$1.6 million during the third quarter of fiscal 2009.

The Company used the following methods and significant assumptions to estimate fair value:

Securities: The Company's securities available for sale primarily consist of mortgage-backed securities issued by U.S. Government sponsored enterprises and trade in active markets. These securities are included under Level 2 because there may or may not be daily trades in each of the individual securities and because the valuation of these securities may be based on instruments that are not exactly identical to those owned by the Company.

Impaired loans: A loan is considered impaired when, based upon currently known information, it is deemed probable that the Company will be unable to collect all amounts due as scheduled according to the original terms of the agreement. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, based on the loan's observable market price or the fair value of collateral, if the loan is collateral dependent. Impaired loans that are collateral dependent are included in the table above.

Real estate owned: Fair value for real estate owned is determined by obtaining appraisals on the properties. The fair value under such appraisals is determined by using an income, cost or comparable sales valuation technique. The fair value is then reduced by management's estimate for the direct costs expected to be incurred in order to sell the property. Holding costs or maintenance expenses are recorded as period costs when occurred and are not included in the fair value estimate

Note 8 – Fair Value of Financial Instruments

The estimated fair values of the Company's financial instruments are as follows:

| | June 30, 2009 | |
|--|--------------------|----------------------------|
| | Carrying Amount | Estimated Fair Value |
| | (in thousands) | |
| Financial Assets: | | |
| Cash and cash equivalents | \$ 26,778 | \$ 26,778 |
| Mortgage-backed securities available for sale | 169,716 | 169,716 |
| Loans held for sale | 5,064 | 5,064 |
| Loans receivable, gross | 427,359 | 443,895 |
| FHLB stock | 9,591 | 9,591 |
| Financial Liabilities: | | |
| Demand and savings deposits | 207,013 | 207,013 |
| Certificates of deposit | 168,983 | 171,079 |
| FHLB advances and other borrowings | 88,891 | 94,972 |

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

Cash and cash equivalents:

The carrying amount approximates fair value.

Mortgage-backed securities available for sale:

The fair values of mortgage-backed securities are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans held for sale:

The carrying amount approximates fair value.

Loans receivable:

Fair values for loans are estimated using a discounted cash flow analysis, utilizing interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for loans that are classified as substandard or doubtful under the Bank's asset classification guidelines are estimated using a similar methodology as that employed in computing the appropriate loan loss reserve for classified loans. Fair value of impaired loans is discussed in Note 7.

FHLB stock:

The carrying value of FHLB stock approximates fair value based on the respective redemption provisions.

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Deposits:

The fair value of demand deposits, savings accounts and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated by discounted cash flow analysis using the rates currently offered for deposits of similar remaining maturities.

FHLB advances and other borrowings:

The fair value of the borrowings is estimated by discounting the future cash flows using the current rate at which similar borrowings with similar remaining maturities could be made.

Off-balance-sheet instruments:

Fair values of off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the borrower's credit standing. The fair value of the fees at June 30, 2009 were insignificant.

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

Forward-Looking Statements

This report contains forward-looking statements, which can be identified by the use of words such as "believes," "intends," "expects," "anticipates," "estimates" or similar expressions. Forward-looking statements include, but are not limited to:

- statements of our goals, intentions and expectations;
- statements regarding our business plan, prospects, growth and operating strategies;
 - statements regarding the quality of our loan and investment portfolios; and,
 - estimates of our risks and future costs and benefits.

These forward-looking statements are subject to significant risks and uncertainties. Actual results may differ materially from those contemplated by the forward-looking statements as a result of, among others, the following factors:

- general economic conditions, including real estate values, either nationally or in the Company's market area continue to decline;
- changes in the interest rate environment that reduce the Company's interest margins or reduce the fair value of financial instruments;
- the credit risk of lending activities, including risks related to construction and land development lending and commercial and small business banking;
 - changes in the level and trend of loan delinquencies and write-offs;
 - results of examinations by banking regulators;
 - increased competitive pressures among financial services companies;
 - changes in consumer spending, borrowing and savings habits;
 - our ability to successfully manage our growth;
- legislative or regulatory changes that adversely affect the Company's business, including restrictions or limitations on permissible lending activities for thrifts and savings banks;
 - our ability to integrate the operations from any acquisition we may make;
 - adverse changes in the securities markets; and
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Public Company Accounting Oversight Board or the Financial Accounting Standards Board.

These factors should be considered in evaluating the forward-looking statements, and undue reliance should not be placed on such statements. The Company undertakes no obligation to publish revised forward-looking statements to reflect the occurrence of unanticipated events or circumstances after the date hereof.

Background and Overview

Home Federal Bank (the “Bank”) was founded in 1920 as a building and loan association and reorganized as a federal mutual savings and loan association in 1936. On December 6, 2004, the Bank converted to stock form and reorganized into the two-tiered mutual holding company form of organization and formed Home Federal MHC and Home Federal Bancorp, Inc. (“Old Home Federal”). In connection with that transaction, Old Home Federal sold 40.00% of its outstanding shares of common stock (6,083,500 shares) to the public and issued 59.04% of its outstanding shares of common stock (8,979,246 shares) to Home Federal MHC, the mutual holding company parent of Old Home Federal. In connection with that transaction, Old Home Federal also established and capitalized the Home Federal Foundation (“Foundation”) for the purpose of supporting charitable organizations and activities that enhance the quality of life for residents within the Bank’s market area. The Foundation was capitalized with a \$1.8 million one-time contribution, which consisted of 146,004 shares of its common stock and \$365,010 in cash.

On May 11, 2007, the Boards of Directors of Old Home Federal, Home Federal MHC and the Bank adopted a Plan of Conversion and Reorganization (the “Plan”) pursuant to which the Bank reorganized from the mutual holding company structure to the stock holding company structure. As a result of that transaction, Home Federal Bank formed a new stock holding company, Home Federal Bancorp, Inc. (“we”, “us”, the “Company”), that serves as the holding company for Home Federal Bank. Home Federal Bancorp, Inc., is a Maryland corporation. The Conversion was completed on December 19, 2007.

Pursuant to the terms of the Plan, shares of outstanding common stock of Old Home Federal were exchanged for 1.136 shares of the Company’s common stock. Cash was paid in lieu of fractional shares. The Conversion was approved by the Bank’s members, the Company’s stockholders (including the approval of a majority of the shares held by persons other than Home Federal MHC) and regulatory agencies. The Company’s common stock is traded on the NASDAQ Global Select Market under the symbol “HOME” and is included in the U.S. Russell 2000® Index.

The Bank is a community-oriented financial institution dedicated to serving the financial service needs of consumers and businesses within its market area. The Bank’s primary business is attracting deposits from the general public and using these funds to originate loans. The Bank emphasizes the origination of commercial business loans, commercial real estate loans, construction and residential development loans, consumer loans and loans secured by first mortgages on owner-occupied residential real estate. As a result of a comprehensive and continuing review of its strategic business plan, the Company continues to expand its commercial and small business banking programs, including a variety of loan and deposit products.

The Bank serves the Treasure Valley region of southwestern Idaho, which includes Ada, Canyon, Elmore and Gem counties, through its 15 full-service banking offices and one loan center. Nearly 40% of the state’s population lives and works in the four counties served by Home Federal Bank. Ada County has the largest population and includes the city of Boise, the state capital. Home Federal Bank maintains its largest branch presence in Ada County with eight locations, followed by Canyon County with five branches, including the Company’s corporate headquarters in Nampa. The two remaining branches are located in Elmore and Gem Counties.

The following items summarize the key factors affecting performance of the Company and the key strategic initiatives undertaken by management during the Company’s third quarter of fiscal year 2009:

- Economic conditions in the Treasure Valley continued to deteriorate as a result of rising unemployment, bankruptcies and foreclosures and declining real estate values, which resulted in rising levels of nonperforming assets and the need for an additional provision for loan losses;

- The Company’s total assets declined and maturing borrowings were repaid with excess cash;

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Total loans declined reflecting a decrease in lending opportunities to good credit customers in Southwestern Idaho and management's strategy to reduce 1-4 family residential loan exposure;

Core deposits increased and certificates of deposit decreased as management continued to focus on low-cost relationship accounts;

The Bank launched a new checking account product that is expected to increase core deposit balances and generate interchange income;

While nonperforming loans increased during the quarter, loans delinquent less than 90 days declined compared to March 31, 2009;

Deteriorating asset quality and foreclosed asset valuations resulted in increased operating expenses through additional valuation allowances and maintenance and property tax expense;;
The Bank accrued \$250,000 related to a special assessment levied by the Federal Deposit Insurance Corporation (“FDIC”) to be paid in September 2009; and
The Bank maintained its strong capital position with a total risk-based capital ratio of 33.6% at June 30, 2009.

The current economic and interest rate environments continue to challenge management’s growth plans. Total assets declined during the third quarter of fiscal year 2009 as a lack of demand for loans, or more importantly a diminished supply of creditworthy lending opportunities, and residential loan refinancing, limited the Company’s ability to increase outstanding loan balances. Alternative investments are also unattractive as investment securities offer very low yields within management’s credit and interest rate risk tolerances. As competitor financial institutions continue to struggle with liquidity, some are offering deposit rates that exceed the Company’s wholesale borrowing costs. Therefore, certificate of deposit balances have declined as some customers chose to move their maturing certificate of deposit balances to competitors in search of higher returns.

Consistent with its business strategy, the Company reduced fixed-term borrowing balances with the Federal Home Loan Bank of Seattle (“FHLB”) and management of the Bank continued to focus on growing core deposits, defined as non-maturity deposits such as checking, savings and money market accounts, which management believes will increase the franchise value of the Company and improve profitability by reducing interest rate sensitivity and high-cost borrowing balances. Core deposit relationships should also increase revenue through service and interchange fee income. In response to recent declines in nonsufficient fund and interchange income and to execute the strategy of increasing core deposit balances, the Bank launched a new checking account, the “Ultimate Checking Account,” during the third quarter of fiscal 2009. Management believes this will result in higher checking account balances and provide an incentive for customers to use their check cards more frequently, which should result in higher interchange income.

While balances on loans delinquent less than 90 days declined at June 30, 2009, compared to March 31, 2009, nonperforming assets increased during the third quarter of fiscal 2009. Commercial real estate loans are now being pressured as property vacancies continue to climb in the Treasure Valley and the slowdown in consumer spending is causing many independent and national retailers to close stores or reduce inventory. The Bank’s Credit Administration Department is also spending considerable time reviewing home equity lines of credit and, in some cases, suspending lines at their current balances in order to mitigate future loan losses.

Micron Technology, Inc., one of the larger employers headquartered in our market area, recently announced a plan to eliminate 2,000 jobs in the Treasure Valley during calendar 2009. The unemployment rate in the Treasure Valley has increased significantly over the last 12 months as total employment in the Boise-Nampa metropolitan statistical area fell 7.3% in June 2009 to 255,000 nonfarm employees from 275,000 in June 2008.

Nonetheless, management is optimistic about the long-term outlook for the Company as capital levels remain very high compared to peers and the level of liquidity in the balance sheet provides flexibility to execute several strategies to weather this economic recession.

Critical Accounting Estimates and Related Accounting Policies

Allowance for Loan Losses. Management recognizes that losses may occur over the life of a loan and that the allowance for loan losses must be maintained at a level necessary to absorb specific losses on impaired loans and probable losses inherent in the loan portfolio. Management assesses the allowance for loan losses on a quarterly basis by analyzing several factors including delinquency rates, charge-off rates and the changing risk profile of the Bank’s

loan portfolio, as well as local economic conditions such as unemployment rates, bankruptcies and vacancy rates of business and residential properties.

The Company believes that the accounting estimate related to the allowance for loan losses is a critical accounting estimate because it is highly susceptible to change from period to period, requiring management to make assumptions about probable incurred losses inherent in the loan portfolio at the balance sheet date. The impact of a

sudden large loss could deplete the allowance and require increased provisions to replenish the allowance, which would negatively impact earnings.

The Company's methodology for analyzing the allowance for loan losses consists of specific allocations on significant individual credits and a general allowance amount, including a range of losses. The specific allowance component is determined when management believes that the collectibility of an individually reviewed loan has been impaired and a loss is probable. The general allowance component relates to assets with no well-defined deficiency or weakness and takes into consideration losses that are inherent within the portfolio but have not been identified. The general allowance is determined by applying a historical loss percentage to various types of loans with similar characteristics and classified loans that are not analyzed specifically. Adjustments are made to historical loss percentages to reflect current economic and internal environmental factors, such as changes in underwriting standards and management turnover, which may increase or decrease those loss factors. As a result of the imprecision in calculating inherent and potential losses, a range is added to the general allowance to estimate an allowance for loan losses that is adequate to cover losses that may arise as a result of changing economic conditions and other qualitative factors that may alter historical loss experience. Additionally, future events may evidence additional losses that were unknown at the time management estimated the allowance, which may require an increase in the allowance for loan losses in future periods.

The allowance is increased by the provision for loan losses, which is charged against current period operating results and decreased by the amount of actual loan charge-offs, net of recoveries.

The Company also estimates a reserve related to unfunded loan commitments. In assessing the adequacy of the reserve, the Company uses a similar approach used in the development of the allowance for loan losses. The reserve for unfunded loan commitments is included in other liabilities on the Consolidated Balance Sheets. The provision for unfunded commitments is charged to noninterest expense.

Deferred Income Taxes. Deferred income taxes are reported for temporary differences between items of income or expense reported in the financial statements and those reported for income tax purposes. Deferred taxes are computed using the asset and liability approach as prescribed in SFAS No. 109, Accounting for Income Taxes. Under this method, a deferred tax asset or liability is determined based on the enacted tax rates that will be in effect when the differences between the financial statement carrying amounts and tax basis of existing assets and liabilities are expected to be reported in an institution's income tax returns. The deferred tax provision for the year is equal to the net change in the net deferred tax asset from the beginning to the end of the year, less amounts applicable to the change in value related to investments available for sale. The effect on deferred taxes of a change in tax rates is recognized as income in the period that includes the enactment date. The primary differences between financial statement income and taxable income result from depreciation expense, mortgage servicing rights, loan loss reserves, deferred compensation, mark to market adjustments on our available for sale securities, and dividends received from the Federal Home Loan Bank of Seattle. Deferred income taxes do not include a liability for pre-1988 bad debt deductions allowed to thrift institutions that may be recaptured if the institution fails to qualify as a bank for income tax purposes in the future.

Real Estate Owned. Real estate properties acquired through, or in lieu of, loan foreclosure are initially recorded at the lesser of the outstanding loan balance or the fair value at the date of foreclosure minus estimated costs to sell. Any valuation adjustments required at the time of foreclosure are charged to the allowance for loan losses. After foreclosure, the properties are carried at the lower of carrying value or fair value less estimated costs to sell. Any subsequent valuation adjustments, operating expenses or income, and gains and losses on disposition of such properties are recognized in current operations. The valuation allowance is established based on our historical realization of losses and adjusted for current market trends.

Comparison of Financial Condition at June 30, 2009 and September 30, 2008

For the nine months ended June 30, 2009, total assets decreased \$52.3 million. The changes in total assets were primarily concentrated in the following asset categories:

| | Increase/(Decrease) | | | |
|---|--------------------------------|-------------------------------------|-------------|---------|
| | Balance at June 30, 2009 | Balance at September 30, 2008 | Amount | Percent |
| | (dollars in thousands) | | | |
| Mortgage-backed securities, at fair value | \$ 169,716 | \$ 188,787 | \$ (19,071) | (10.1)% |
| Loans receivable, net | 418,198 | 459,813 | (41,615) | (9.1) |
| Real estate and other property owned | 8,614 | 650 | 7,964 | 1,225 |

Cash. Cash and amounts due from depository institutions increased \$3.5 million to \$26.8 million at June 30, 2009, from \$23.3 million at September 30, 2008. The increase was primarily attributable to principal repayments on one- to four-family residential mortgages and mortgage backed securities offset by maturing borrowings from the Federal Home Loan Bank of Seattle (the "FHLB"). Management has been maintaining higher than optimal levels of cash to provide liquidity in the event of material degradation in the economy and flexibility for strategic initiatives. Additionally, \$9.3 million of FHLB borrowings with an average rate of 5.00% are scheduled to mature in September 2009, which will be repaid with excess cash if alternative, more profitable, investments are not available at that time.

Securities. Mortgage-backed securities decreased \$19.1 million to \$169.7 million at June 30, 2009, from \$188.8 million at September 30, 2008. The decrease was the net of principal repayments and the increase in the value of the mortgage backed securities portfolio during the nine months ended June 30, 2009. At June 30, 2009, the unrealized gain on the portfolio was \$4.0 million compared to an unrealized loss of \$2.3 million at September 30, 2008. Principal reduction totaled \$25.4 million for the nine months ended June 30, 2009 and is occurring at an accelerating rate due to the historically-low rates available on residential mortgages, which is increasing refinancing activity.

Nearly all of the Company's mortgage-backed securities are issued by U.S. Government sponsored enterprises, primarily Fannie Mae and Freddie Mac. While the U.S. Government has affirmed its support for government sponsored enterprises and the mortgage-backed securities they issued, significant deterioration in the financial strength of Fannie Mae, Freddie Mac or mortgage-backed security insurers may have a material effect on the valuation and performance of the Company's mortgage-backed securities portfolio in future periods.

Non-agency, also referred to as "private label," mortgage-backed securities had a fair value of \$3.0 million at June 30, 2009, compared to their amortized cost of \$3.3 million. The securities carried a rating of 'AAA' by Moody's and Standard & Poor's at that date. However, one of these securities was downgraded by Moody's in July 2009 from AAA to A1. Management has reviewed the delinquency status, credit support and collateral coverage of the loans pooled in the private label securities portfolio and has concluded the securities were not other than temporarily impaired at June 30, 2009, or after the ratings downgrade in July 2009. However, continued deterioration in the economy and rapid increases in unemployment may result in a change in the performance expectation for these securities in the future, which may negatively impact the Company's earnings. At June 30, 2009, the Company did not own collateralized debt obligations or trust preferred securities.

FHLB Stock. At June 30, 2009, the Bank held \$9.6 million of common stock in the FHLB. This security is reported at par value, which represents the Bank's cost. The FHLB recently announced that it would report a risk-based capital

deficiency under the regulations of the Federal Housing Finance Agency (the "FHFA"), its primary regulator. As a result, the FHLB has stopped paying a dividend and stated that it would suspend the repurchase and redemption of outstanding common stock until its retained earnings deficiency was reclaimed.

The FHLB has communicated to the Company that it believes the calculation of risk-based capital under the current rules of the FHFA significantly overstates the market and credit risk of the FHLB's private-label mortgage-backed securities in the current market environment and that they have enough capital to cover the risks reflected in the FHLB's balance sheet. As a result, the Company has not recorded an "other than temporary impairment" on its investment in FHLB stock. However, continued deterioration in the FHLB's financial position may result in

impairment in the value of those securities, or the requirement that the Bank contribute additional funds to recapitalize the FHLB, or reduce the Bank's ability to borrow funds from the FHLB, which would impair the Bank's ability to meet liquidity demands.

Loans. Net loans receivable decreased \$41.6 million to \$418.2 million at June 30, 2009, from \$459.8 million at September 30, 2008. One- to four-family residential mortgage loans decreased \$34.3 million as mortgage rates remained at historically low levels through the third quarter of fiscal 2009, which led to significantly higher levels of mortgage loan refinancing. Additionally, the Bank originates conventional one- to four-family residential loans for sale in the secondary market. As a result, the residential loan portfolio will likely continue to decline as new loans are not added to the portfolio. Consumer loans decreased \$5.3 million to \$51.0 million as of June 30, 2009. Commercial real estate, multifamily and acquisition and development loans increased \$1.5 million to \$200.2 million at June 30, 2009 from \$198.6 million at September 30, 2008. The Company plans to continue its emphasis on commercial and small business banking products.

Asset Quality. Net charge-offs totaled \$2.5 million during the quarter ended June 30, 2009. Loans delinquent 30 to 89 days totaled \$3.8 million at June 30, 2009, compared to \$11.6 million at March 31, 2009, and \$6.5 million at September 30, 2008. The following table summarizes loans delinquent 30 to 89 days:

| | June 30, 2009 | March 31, 2009 | September 30, 2008 |
|---|------------------|-------------------|--------------------------|
| | (in thousands) | | |
| Land acquisition and development | \$ 623 | \$ 133 | \$ 1,150 |
| One- to four-family construction | 245 | 760 | 241 |
| Commercial real estate | 1,357 | 5,313 | 3,094 |
| One- to four-family residential | 1,300 | 5,242 | 1,836 |
| Other | 256 | 193 | 190 |
| Total loans delinquent 30 to 89 days | \$ 3,781 | \$ 11,641 | \$ 6,511 |

Nonperforming assets, which includes all loans on nonaccrual status, impaired loans and real estate owned, totaled \$25.1 million at June 30, 2009, compared to \$19.1 million at March 31, 2009, and \$10.6 million at September 30, 2008. The allowance for loan losses was \$8.3 million, or 1.93%, of gross loans at June 30, 2009, compared to \$7.3 million, or 1.64% of gross loans at March 31, 2009, and \$4.6 million, or 0.98% of gross loans at September 30, 2008.

When a loan becomes 90 days delinquent, the Bank places the loan on nonaccrual status. A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Generally, an impaired loan is also placed on nonaccrual status, regardless of delinquency. As a result, some loans that are not 90 days or more past due may be in nonaccrual status if it is considered impaired.

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The delinquency table above includes \$1.5 million, \$1.2 million, and \$5.1 million of loans that were placed on nonaccrual status at June 30, 2009, March 31, 2009 and September 30, 2008, respectively, which are also included in the table below that summarizes total nonperforming loans (including nonaccrual and impaired loans) and real estate owned:

| | June 30, 2009 | | March 31, 2009 | | September 30, 2008 | |
|--|----------------|--------------|----------------|--------------|--------------------|--------------|
| | (in thousands) | | | | | |
| | Balance | Loss Reserve | Balance | Loss Reserve | Balance | Loss Reserve |
| Land acquisition and development | \$ 3,734 | \$ 1,352 | \$ 5,266 | \$ 1,029 | \$ 3,975 | \$ 916 |
| One- to four-family construction | 3,478 | 390 | 2,307 | 286 | 4,239 | 596 |
| Commercial real estate | 4,000 | 256 | 3,074 | 220 | - | - |
| One- to four-family residential | 5,169 | 816 | 3,943 | 441 | 1,701 | 219 |
| Other | 81 | 6 | - | - | 30 | 2 |
| Total nonperforming and impaired loans | \$ 16,462 | 2,820 | \$ 14,590 | 1,976 | \$ 9,945 | 1,733 |
| General loss reserve | | 5,446 | | 5,357 | | 2,846 |
| Total allowance for loan losses | | \$ 8,266 | | \$ 7,333 | | \$ 4,579 |
| Real estate owned, net | \$ 8,614 | | \$ 4,478 | | \$ 650 | |
| Total nonperforming assets | \$ 25,076 | | \$ 19,068 | | \$ 10,595 | |

Troubled debt restructurings that are not included in the delinquency or nonperforming asset tables above totaled \$1.1 million and \$654,000 and \$812,000 at June 30, 2009, March 31, 2009 and September 30, 2008, respectively.

Real estate owned increased \$4.1 million during the third quarter of fiscal 2009 to \$8.6 million at June 30, 2009, and was comprised of \$4.3 million of land development and speculative one- to four-family construction projects, \$3.9 million of commercial real estate and \$383,000 of one- to four-family residential properties.

Nearly all of the Company's loans are secured by collateral located in the Treasure Valley or southern Idaho. The Bank's commercial real estate and construction and land development loans are secured by properties in the following locations in Idaho: approximately 61% and 19% Ada and Canyon counties, respectively, approximately 6% in eastern Idaho, 5% in Valley County, and 3% in the Twin Falls and Ketchum areas.

In 2005, the Bank purchased approximately \$38.8 million of residential real estate loans from Countrywide Financial, now Bank of America, who continues to service the loans. Balances on the portfolio totaled \$22.4 million at June 30, 2009. Approximately 92% of the portfolio balance is secured by properties outside of the state of Idaho and delinquencies and foreclosures are rising quickly in that portfolio. At June 30, 2009, this portfolio had \$3.1 million of nonperforming loans that are reported in the table above. The total reserve allocated to loans in this loan portfolio was \$1.1 million at June 30, 2009, or 5% of the balance of loans outstanding on that date.

At June 30, 2009, nearly all of the Company's home equity lines of credit ("HELOC") were directly originated through the Bank's branch network. However, approximately \$924,000 of HELOCs, or 3% of the HELOC portfolio at June 30, 2009, were referred to the Bank through broker relationships. While nearly all of these loans are secured by properties

in southern Idaho, management ceased indirect origination of HELOCs in fiscal 2008.

The Treasure Valley economy continues to deteriorate as unemployment rose quickly from 4.80% in September 2008 to an estimated 10.1% in June 2009. New home and commercial real estate construction has nearly come to a standstill as excess inventory in the residential and commercial real estate markets continues to reduce property

values. The pending closure of retail locations as a result of reduced consumer spending will exacerbate this problem.

Management believes the Treasure Valley is at the beginning of a downturn in the commercial real estate market. As a result of this uncertainty, management recorded a significant provision for loan losses during the nine months ended June 30, 2009, in order to increase the general reserve component of the allowance for loan losses. While the \$2.4 million provision for loan losses for the full fiscal year of 2008 and the \$8.1 million provision recorded for the first nine months of fiscal 2009 exceeds the level of net charge-offs during those periods, management believes such an increase in the allowance for loan losses is prudent and appropriate and that the allowance for loan losses reflects management's best estimate of probable, known and estimable losses inherent in the loan portfolio at June 30, 2009. However, additional information may later come to management's attention, evidencing losses in excess of the amounts estimated, which may negatively affect earnings in the future.

Deposits. Deposits increased \$3.1 million, or 0.8%, to \$376.0 million at June 30, 2009, from \$372.9 million at September 30, 2008, primarily as a result of savings accounts. Savings account balances have been steadily increasing throughout fiscal 2009. The decrease in certificates of deposit was due to choosing not to match rates offered by local competitors that in many cases exceeded the Bank's cost of alternative funding sources. The Bank had no brokered deposits at June 30, 2009, or September 30, 2008.

The following table details the composition of the deposit portfolio and changes in deposit balances:

| | Increase (decrease) | | | |
|-------------------------------------|--------------------------------|-------------------------------------|------------|---------|
| | Balance at June 30, 2009 | Balance at September 30, 2008 | Amount | Percent |
| | (dollars in thousands) | | | |
| Noninterest-bearing demand deposits | \$ 39,931 | \$ 41,398 | \$ (1,467) | (3.5)% |
| Interest-bearing demand deposits | 131,202 | 127,714 | 3,488 | 2.7 |
| Savings deposits | 35,880 | 26,409 | 9,471 | 35.9 |
| Certificates of deposit | 168,983 | 177,404 | (8,421) | (4.7) |
| Total deposit accounts | \$ 375,996 | \$ 372,925 | \$ 3,071 | 0.8% |

Approximately 74% of the certificates of deposit portfolio at June 30, 2009, is scheduled to mature within 12 months. While this presents an opportunity to reduce the cost of interest bearing deposits in the current low interest rate environment, the significant level of maturities of certificates also places a burden on the Company's liquidity if management is unable to retain the maturing balances.

Borrowings. FHLB advances decreased \$48.1 million, or 35.1%, to \$88.9 million at June 30, 2009, from \$137.0 million at September 30, 2008. Excess cash and principal payment proceeds from mortgage-backed securities and residential loan portfolios were used to repay FHLB advances as they matured. The Bank uses FHLB advances as an alternative funding source to deposits, manage funding costs, reduce interest rate risk, and, from time to time, to leverage the balance sheet.

Deferred Income Tax Asset/Liability. The Company had a deferred tax asset of \$1.9 million at June 30, 2009 versus a deferred tax asset of \$1.8 million at September 30, 2008. There are three major components to the change. There was a \$2.5 million shift from an unrealized loss on the Company's mortgage-backed securities' portfolio as of September 30, 2008 to an unrealized gain as of June 30, 2009, as interest rates fell and spreads narrowed, increasing the value of the securities portfolio during the quarter. There was a \$1.5 million increase in deferred tax assets due to an \$8.1 million provision for loan loss recorded during the nine month period ended June 30, 2009. Lastly, deferred tax

liability decreased \$710,000 due to the sale of mortgage servicing rights completed in December 2008.

Equity. Stockholders' equity decreased \$6.5 million, or 3%, to \$198.7 million at June 30, 2009, compared to \$205.2 million at September 30, 2008. The execution of the entire share repurchase program during the quarter ended March 31, 2009, was the primary cause for the decrease in stockholders' equity. Dividends and a year-to-date loss from operations in fiscal 2009 reduced retained earnings while a lower interest rate environment at June 30, 2009

increased the unrealized gain on securities by \$3.8 million, net of tax, compared to September 30, 2008. The Company's book value per share as of June 30, 2009 was \$11.90 per share based upon 16,698,168 outstanding shares of common stock.

Comparison of Operating Results for the Three Months Ended June 30, 2009 and June 30, 2008

Net loss for the three months ended June 30, 2009 was \$1.2 million, or \$0.08 per diluted share, compared to net income of \$1.1 million, or \$0.07 per diluted share, for the three months ended June 30, 2008. Total revenue for the quarter ended June 30, 2009, which consisted of net interest income before the provision for loan losses plus noninterest income, decreased \$323,000 or 3.7% to \$8.3 million from \$8.6 million for the same period of the prior year. Total revenue for the third quarter of fiscal 2009 was unchanged at \$8.3 million compared to the linked second quarter of fiscal 2009. The Company's efficiency ratio increased to 84.26% for the quarter ended June 30, 2009, compared to 71.40% for the same quarter a year ago due to higher expenses and lower revenue in the 2009 period.

Net Interest Income. Net interest income decreased \$199,000, or 3.4%, to \$5.7 million for the three months ended June 30, 2009, from \$5.9 million for the three months ended June 30, 2008. The decrease in net interest income is primarily attributable to approximately \$307,000 in interest income reversed due to nonaccrual loans.

The Company's net interest margin increased 24 basis points to 3.53% for the quarter ended June 30, 2009, from 3.29% for the same quarter last year. The improvement in the net interest margin is primarily attributable to the decrease in interest expense between the two periods.

The following table sets forth the impacts to the Company's net interest income from changes in balances of interest earning assets and interest bearing liabilities as well as changes in interest rates. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). Changes attributable to both rate and volume, which cannot be segregated, are allocated proportionately to the changes in rate and volume.

| | Three Months Ended June 30, 2009 Compared to Three Months Ended June 30, 2008 | | |
|---|---|----------|------------|
| | Increase (Decrease) | | |
| | Due to | | |
| | Rate | Volume | Total |
| | (in thousands) | | |
| Interest-earning assets: | | | |
| Loans receivable, net | \$ (513) | \$ (617) | \$ (1,130) |
| Loans held for sale | (11) | 15 | 4 |
| Interest-bearing deposits in other banks | (93) | (15) | (108) |
| Mortgage-backed securities | (78) | (311) | (389) |
| FHLB stock | (60) | - | (60) |
| Total net change in income on interest-earning assets | \$ (755) | \$ (928) | \$ (1,683) |
| Interest-bearing liabilities: | | | |
| Savings deposits | \$ (4) | \$ 16 | \$ 12 |
| Interest-bearing demand deposits | (12) | 4 | (8) |
| Money market accounts | (108) | (50) | (158) |
| Certificates of deposit | (527) | (119) | (646) |
| Total deposits | (651) | (149) | (800) |

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| | | | |
|---|----------|----------|------------|
| FHLB advances | (121) | (563) | (684) |
| Total net change in expense on interest-bearing liabilities | \$ (772) | \$ (712) | \$ (1,484) |
| Total decrease in net interest income | | | \$ (199) |

Interest and Dividend Income. Total interest and dividend income for the three months ended June 30, 2009, decreased \$1.7 million, or 16.7%, to \$8.4 million, from \$10.1 million for the three months ended June 30, 2008.

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The decrease during the quarter was attributable to a decrease on yields earned on interest earning assets, a decrease in interest earning assets as well as due to the reversal of interest income on nonaccrual loans.

The following table compares detailed average earning asset balances, associated yields, and resulting changes in interest and dividend income:

| | Three Months Ended June 30, | | | | |
|--|-----------------------------|-------|--------------------|-------|--|
| | 2009 | | 2008 | | Increase/ (Decrease) in Interest and Dividend Income from 2008 |
| | Average Balance | Yield | Average Balance | Yield | |
| (dollars in thousands) | | | | | |
| Interest-bearing deposits in other banks | \$ 20,252 | 0.18% | \$ 23,698 | 1.97% | \$ (108) |
| Mortgage-backed securities | 175,522 | 4.52 | 202,904 | 4.68 | (389) |
| Loans receivable, net | 437,762 | 5.82 | 478,806 | 6.26 | (1,130) |
| Loans held for sale | 4,372 | 4.84 | 3,208 | 6.06 | 4 |
| FHLB stock | 9,591 | - | 9,591 | 2.50 | (60) |
| Total interest-earning assets | \$ 647,499 | 5.20% | \$ 718,207 | 5.71% | \$ (1,683) |

The decline in the yield on interest-bearing deposits in other banks reflects the significantly lower short-term interest rate environment in the third quarter of fiscal 2009 compared to the third quarter of fiscal 2008.

The yield on loans fell to 5.82% in the third quarter of fiscal 2009 also as a result of the decrease in short-term interest rates. For example, the Wall Street Journal Prime rate was 3.25% for the third fiscal quarter of 2009 compared to an average of 5.09% during the same quarter last year. Loans on nonaccrual status during the third quarter of 2009 reduced interest income by approximately \$307,000.

Interest Expense. Interest expense decreased \$1.5 million, or 35.5%, to \$2.7 million for the three months ended June 30, 2009 from \$4.2 million for the three months ended June 30, 2008. The average balance of total interest-bearing liabilities decreased \$63.6 million, or 12.6%, to \$441.0 million for the three months ended June 30, 2009 from \$504.7 million for the three months ended June 30, 2008. The decrease in interest expense in 2009 was mainly due to a reduction in the outstanding balance of FHLB advances and a lower rate paid on certificates of deposit.

The following table details average balances, cost of funds and the change in interest expense:

| | Three Months Ended June 30, | | | | |
|------------------------|-----------------------------|-------|--------------------|-------|---|
| | 2009 | | 2008 | | Increase/ (Decrease) in Interest Expense from 2008 |
| | Average Balance | Cost | Average Balance | Cost | |
| (dollars in thousands) | | | | | |
| Savings deposits | \$ 35,173 | 0.67% | \$ 25,337 | 0.74% | \$ 12 |

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| | | | | | |
|------------------------------------|------------|-------|------------|-------|------------|
| Interest-bearing demand deposits | 83,319 | 0.48 | 80,634 | 0.54 | (8) |
| Money market deposits | 49,731 | 1.09 | 61,902 | 1.90 | (158) |
| Certificates of deposit | 172,146 | 3.10 | 183,791 | 4.31 | (646) |
| FHLB advances | 100,667 | 4.24 | 153,016 | 4.58 | (684) |
| Total interest-bearing liabilities | \$ 441,036 | 2.45% | \$ 504,680 | 3.31% | \$ (1,484) |

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The slight increase in total interest expense of savings deposits was due to the significant growth of the product over the past year. The decline in the cost of all other interest-bearing deposits reflects the significantly lower interest rate environment in the third quarter of fiscal 2009 compared to the third quarter of fiscal 2008.

Provision for Loan Losses. A provision for loan losses of \$3.5 million was recorded as a result of management's analysis of the loan portfolio for the quarter ended June 30, 2009, compared to a provision for loan losses of \$652,000 for the same quarter of the prior year. The provision reflects increases in specific reserves on nonperforming loans. Additionally, the estimated loss rates have been adjusted upward based on recent charge-off experience and the deterioration in the Treasure Valley economy.

While management believes the estimates and assumptions used in its determination of the adequacy of the allowance are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, or that the actual amount of future provisions will not exceed the amount of past provisions or that any increased provision that may be required will not adversely impact the Company's financial condition and results of operations. In addition, the determination of the amount of the allowance for loan losses is subject to review by bank regulators, as part of the routine examination process, which may result in the establishment of additional reserves based upon their judgment of information available to them at the time of their examination.

The provision for loan losses is impacted by the types of loans and the risk factors associated with each loan type in the Bank's portfolio. As the Bank increases its commercial loan portfolio, the Bank anticipates it will increase its allowance for loan losses based upon the higher risk characteristics associated with commercial loans compared with one- to four- family residential loans, which have historically comprised the majority of the Bank's loan portfolio.

The following table details selected activity associated with the allowance for loan losses:

| | At or For the Three Months Ended June 30, | |
|---|---|------------|
| | 2009 | 2008 |
| | (dollars in thousands) | |
| Provision for loan losses | \$ 3,450 | \$ 652 |
| Net charge-offs | 2,517 | 158 |
| Allowance for loan losses | 8,266 | 3,801 |
| Allowance for loan losses as a percentage of gross loans receivable | 1.93% | 0.81% |
| Nonperforming loans | \$ 16,462 | \$ 3,462 |
| Allowance for loan losses as a percentage of nonperforming loans | 50.21% | 109.79% |
| Nonperforming loans as a percentage of gross loans receivable | 3.85 | 0.73 |
| Loans receivable, net | \$ 418,198 | \$ 468,343 |

Noninterest Income. Noninterest income decreased \$124,000, or 4.5%, to \$2.6 million for the three months ended June 30, 2009 from \$2.7 million for the three months ended June 30, 2008. The decrease was primarily attributable to decreases of \$388,000 and \$116,000 in service charges and fees and loan servicing fees, respectively, offset somewhat by an increase in gain on sale of loans of \$203,000. The decreases in service charges and fees reflect the continuing slowdown in consumer spending, which has reduced nonsufficient fund fees from the previous year period. However, nonsufficient fund fees and interchange income increased \$123,000 and \$54,000, respectively, from the second fiscal quarter of 2009. The decrease in loan servicing fees is due to the sale of loan servicing rights completed in the first quarter of fiscal 2009. The increase in gain on sale of loans is attributed to the historically low rates available on residential mortgages during the third quarter of fiscal 2009.

The following table provides a detailed analysis of the changes in components of noninterest income:

| | Three Months Ended | | Increase (decrease) | |
|--|------------------------|-----------------|---------------------|---------------|
| | June 30, | | | |
| | 2009 | 2008 | Amount | Percent |
| | (dollars in thousands) | | | |
| Service fees and charges | \$ 2,008 | \$ 2,396 | \$ (388) | (16.2)% |
| Gain on sale of loans | 416 | 213 | 203 | 95.3 |
| Increase in cash surrender value of bank owned life insurance | 107 | 106 | 1 | 0.9 |
| Loan servicing fees | - | 116 | (116) | (100.0) |
| Mortgage servicing rights, net | - | (63) | 63 | (100.0) |
| Other | 80 | (33) | 113 | (342.4) |
| Total noninterest income | \$ 2,611 | \$ 2,735 | \$ (124) | (4.5)% |

Noninterest Expense. Noninterest expense increased \$840,000, or 13.6%, to \$7.0 million for the three months ended June 30, 2009 from \$6.2 million for the three months ended June 30, 2008. The following table provides a detailed analysis of the changes in components of noninterest expense:

| | Three Months Ended | | Increase (decrease) | |
|----------------------------------|------------------------|-----------------|---------------------|--------------|
| | June 30, | | | |
| | 2009 | 2008 | Amount | Percent |
| | (dollars in thousands) | | | |
| Compensation and benefits | \$ 3,594 | \$ 3,840 | \$ (246) | (6.4)% |
| Occupancy and equipment | 804 | 771 | 33 | 4.3 |
| Data processing | 654 | 615 | 39 | 6.3 |
| Advertising | 211 | 241 | (30) | (12.5) |
| Insurance and taxes | 783 | 158 | 625 | 395.6 |
| Other | 968 | 549 | 419 | 76.3 |
| Total noninterest expense | \$ 7,014 | \$ 6,174 | \$ 840 | 13.6% |

Compensation and benefits declined \$246,000 or 6.4% in the third quarter of 2009 compared to the year-ago period mainly due to the reduction of annual incentives based on payout projections and lower expense related to the Bank's ESOP. Insurance and taxes increased primarily due to a one-time special assessment by the Federal Deposit Insurance Corporation of \$250,000 as well as approximately \$219,000 in past due property taxes paid on recently foreclosed properties. Other expenses increased during the third quarter of fiscal 2009 compared to 2008 primarily as a result of a \$367,000 provision for the decline in the value of foreclosed properties.

Income Tax Expense (Benefit). The Company recorded an income tax benefit of \$894,000 for the three months ended June 30, 2009. Net loss before income taxes was \$2.1 million for the three months ended June 30, 2009 compared to net income before taxes of \$1.8 million for the three months ended June 30, 2008.

Comparison of Operating Results for the Nine Months Ended June 30, 2009 and June 30, 2008

Net loss for the nine months ended June 30, 2009 was (\$1.6) million, or (\$0.10) per diluted share, compared to net income of \$3.0 million, or \$0.19 per diluted share, for the nine months ended June 30, 2008. Earnings per share for

the prior period have been adjusted to reflect the impact of the second-step conversion and reorganization of the Company, which occurred on December 19, 2007. Total revenue for the nine months ended June 30, 2009, which consisted of net interest income before the provision for loan losses plus noninterest income, increased \$247,000 or 1.0% to \$24.8 million compared to \$24.6 million for the same period of the prior year. The Company's efficiency ratio increased to 79.0% for the nine months ended June 30, 2009, compared to 75.2% for the same period of the prior year.

Net Interest Income. Net interest income increased \$673,000, or 4.0%, to \$17.4 million for the nine months ended June 30, 2009, from \$16.7 million for the nine months ended June 30, 2008. The increase was mainly attributable to a decrease in interest expense. Lower interest rates as well as lower outstanding borrowings in the current year period than in the same period a year ago were the main reasons for the decrease.

The Company's net interest margin increased 35 basis points to 3.49% for the nine months ended June 30, 2009, from 3.14% for the same period last year. The improvement in the net interest margin is primarily attributable to the decrease in interest expense between the two periods.

The following table sets forth the impacts to the Company's net interest income from changes in balances of interest earning assets and interest bearing liabilities as well as changes in interest rates. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). Changes attributable to both rate and volume, which cannot be segregated, are allocated proportionately to the changes in rate and volume.

| | Nine Months Ended June 30, 2009 Compared to Nine Months Ended June 30, 2008 | | |
|---|---|------------|------------|
| | Increase (Decrease) Due to | | |
| | Rate | Volume | Total |
| | (in thousands) | | |
| Interest-earning assets: | | | |
| Loans receivable, net | \$ (1,924) | \$ (1,149) | \$ (3,073) |
| Loans held for sale | (2) | 22 | 20 |
| Interest-bearing deposits in other banks | (486) | (352) | (838) |
| Mortgage-backed securities | (146) | (6) | (152) |
| FHLB stock | (143) | - | (143) |
| Total net change in income on interest-earning assets | \$ (2,701) | \$ (1,485) | \$ (4,186) |
| Interest-bearing liabilities: | | | |
| Savings deposits | \$ 6 | \$ 41 | \$ 47 |
| Interest-bearing demand deposits | (71) | (2) | (73) |
| Money market accounts | (575) | (97) | (672) |
| Certificates of deposit | (1,630) | (798) | (2,428) |
| Total deposits | (2,270) | (856) | (3,126) |
| FHLB advances | (172) | (1,561) | (1,733) |
| Total net change in expense on interest-bearing liabilities | \$ (2,442) | \$ (2,417) | \$ (4,859) |
| Total increase in net interest income | | | \$ 673 |

Interest and Dividend Income. Total interest and dividend income for the nine months ended June 30, 2009 decreased \$4.2 million, or 13.6%, to \$26.7 million, from \$30.9 million for the nine months ended June 30, 2008. The decrease during the period was attributable to both a decrease in the average balance of interest-earning assets of \$45.5 million and a drop in yields earned on interest-earning assets of 44 basis points.

The following table compares detailed average earning asset balances, associated yields, and resulting changes in interest and dividend income:

| | Nine Months Ended June 30, | | | | Increase/ (Decrease) in Interest and Dividend Income from 2008 |
|--|----------------------------|--------|--------------------|-------|--|
| | 2009 | | 2008 | | |
| | Average Balance | Yield | Average Balance | Yield | |
| (dollars in thousands) | | | | | |
| Interest-bearing deposits in other banks | \$ 13,630 | 0.52% | \$ 35,301 | 3.37% | \$ (838) |
| Mortgage-backed securities | 181,898 | 4.63 | 182,080 | 4.73 | (152) |
| Loans receivable, net | 455,969 | 5.90 | 480,477 | 6.46 | (3,073) |
| Loans held for sale | 3,585 | 5.47 | 2,716 | 6.22 | 20 |
| FHLB stock | 9,591 | (0.46) | 9,591 | 1.53 | (143) |
| Total interest-earning assets | \$ 664,673 | 5.35% | \$ 710,165 | 5.79% | \$ (4,186) |

Interest Expense. Interest expense decreased \$4.9 million, or 34.4%, to \$9.3 million for the nine months ended June 30, 2009 from \$14.1 million for the nine months ended June 30, 2008. The average balance of total interest-bearing liabilities decreased \$68.5 million, or 13.1%, to \$453.6 million for the nine months ended June 30, 2009 from \$522.1 million for the nine months ended June 30, 2008. Decreases in the average balances of certificates of deposit and FHLB advances of \$25.4 million and \$46.6 million respectively were primarily responsible for the decrease in interest bearing liabilities.

The following table details average balances, cost of funds and the change in interest expense:

| | Nine Months Ended June 30, | | | | Increase/ (Decrease) in Interest Expense from 2008 |
|------------------------------------|----------------------------|-------|--------------------|-------|---|
| | 2009 | | 2008 | | |
| | Average Balance | Cost | Average Balance | Cost | |
| (dollars in thousands) | | | | | |
| Savings deposits | \$ 31,024 | 0.73% | \$ 23,570 | 0.70% | \$ 47 |
| Interest-bearing demand deposits | 80,434 | 0.51 | 79,065 | 0.64 | (73) |
| Money market deposits | 52,532 | 1.26 | 57,793 | 2.69 | (672) |
| Certificates of deposit | 173,765 | 3.39 | 199,179 | 4.58 | (2,428) |
| FHLB advances | 115,833 | 4.44 | 162,471 | 4.59 | (1,733) |
| Total interest-bearing liabilities | \$ 453,588 | 2.72% | \$ 522,078 | 3.60% | \$ (4,859) |

Provision for Loan Losses. A provision for loan losses of \$8.1 million was recorded as a result of our analysis of the loan portfolio for the nine months ended June 30, 2009, compared to a provision for loan losses of \$1.3 million for the same period of the prior year.

The following table details selected activity associated with the allowance for loan losses:

| | At or For the Nine Months Ended June 30, | |
|---|---|------------|
| | 2009 | 2008 |
| | (dollars in thousands) | |
| Provision for loan losses | \$ 8,085 | \$ 1,317 |
| Net charge-offs | 4,398 | 505 |
| Allowance for loan losses | 8,266 | 3,801 |
| Allowance for loan losses as a percentage of gross loans receivable | 1.93% | 0.80% |
| Nonperforming loans | \$ 16,462 | \$ 3,462 |
| Allowance for loan losses as a percentage of nonperforming loans | 50.21% | 109.79% |
| Nonperforming loans as a percentage of gross loans receivable | 3.85 | 0.73 |
| Loans receivable, net | \$ 418,198 | \$ 468,343 |

Noninterest Income. Noninterest income decreased \$426,000, or 5.4%, to \$7.4 million for the nine months ended June 30, 2009 from \$7.8 million for the nine months ended June 30, 2008. The decrease was primarily attributable to decreases of \$722,000 and \$315,000 in service charges and fees and loan servicing fees offset by an increase in gain on sale of loans of \$453,000. The decreases in service charges and fees reflect the continuing slowdown in consumer spending and the decrease in loan servicing fees is due to the sale of loan servicing rights completed in the first quarter of fiscal 2009. The increase in gain on sale of loans is attributed to the historically low rates available on residential mortgages during the first nine months of fiscal 2009.

The following table provides a detailed analysis of the changes in components of noninterest income:

| | Nine Months Ended June 30, | | Increase (decrease) | |
|--|-------------------------------|----------|---------------------|---------|
| | 2009 | 2008 | Amount | Percent |
| | (dollars in thousands) | | | |
| Service fees and charges | \$ 6,009 | \$ 6,731 | \$ (722) | (10.7)% |
| Gain on sale of loans | 1,013 | 560 | 453 | 80.9 |
| Increase in cash surrender value of bank owned life insurance | 317 | 314 | 3 | 1.0 |
| Loan servicing fees | 54 | 369 | (315) | (85.4) |
| Mortgage servicing rights, net | (31) | (206) | 175 | 85.0 |
| Other | 55 | 75 | (20) | (26.7) |
| Total noninterest income | \$ 7,417 | \$ 7,843 | \$ (426) | (5.4)% |

Noninterest Expense. Noninterest expense increased \$1.1 million, or 6.2%, to \$19.6 million for the nine months ended June 30, 2009 from \$18.5 million for the nine months ended June 30, 2008. Compensation and benefits declined \$644,000 or 5.6% from the year ago period. This reduction is mainly attributable to the absence of accruals in the current year for incentive awards due to the Company's financial results to date. The increase in insurance and taxes is mainly due to a one-time FDIC assessment of approximately \$250,000 as well as property tax expense incurred on foreclosed properties. The increase in other expense is mainly attributable to write-downs in the value of real estate owned.

The following table provides a detailed analysis of the changes in components of noninterest expense:

| | Nine Months Ended | | Increase (decrease) | |
|---------------------------|------------------------|-----------|---------------------|---------|
| | June 30, | | Amount | Percent |
| | 2009 | 2008 | | |
| | (dollars in thousands) | | | |
| Compensation and benefits | \$ 10,948 | \$ 11,592 | \$ (644) | (5.6)% |
| Occupancy and equipment | 2,303 | 2,242 | 61 | 2.7 |
| Data processing | 1,773 | 1,668 | 105 | 6.3 |
| Advertising | 656 | 786 | (130) | (16.5) |
| Insurance and taxes | 1,244 | 383 | 861 | 224.8 |
| Other | 2,695 | 1,810 | 885 | 48.9 |
| Total noninterest expense | \$ 19,619 | \$ 18,481 | \$ 1,138 | 6.2% |

Income Tax Expense (Benefit). The Company recorded an income tax benefit of \$1.3 million for the nine months ended June 30, 2009. Net loss before income taxes was \$2.9 million for the nine months ended June 30, 2009 compared to net income before taxes of \$4.8 million for the nine months ended June 30, 2008.

Liquidity, Commitments and Capital Resources

Liquidity. The Company actively analyzes and manages the Bank's liquidity with the objectives of maintaining an adequate level of liquidity and to ensure the availability of sufficient cash flows to support loan growth, fund deposit withdrawals, fund operations and satisfy other financial commitments. See the "Consolidated Statements of Cash Flows" contained in Item 1 - Financial Statements, included herein.

The primary sources of funds are customer deposits, loan repayments, loan sales, maturing investment securities, and FHLB advances. These sources of funds are used to make loans, acquire investment securities and other assets, and fund continuing operations. While maturities and the scheduled amortization of loans are a predictable source of funds, deposit flows and mortgage prepayments are greatly influenced by the level of interest rates, economic conditions and competition. Management believes the Company's current liquidity position and anticipated operating results are sufficient to fund the Bank's known existing commitments and activity levels.

Liquidity is essential to the Company's business. An inability to raise funds through deposits, borrowings, the sale of loans and other sources could have a substantial negative effect on liquidity. The Company's access to funding sources in amounts adequate to finance the Bank's activities on acceptable terms could be impaired by factors that affect the Company and the Bank specifically or within the financial services industry or economy in general. Factors that could detrimentally impact the Company's access to liquidity sources include adverse regulatory action, a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry in light of the recent turmoil faced by banking organizations and the continued deterioration in credit markets.

At June 30, 2009, certificates of deposit were \$169.0 million, or 44.9% of total deposits, including \$124.5 million that are scheduled to mature by June 30, 2010. Historically, the Bank has been able to retain a significant amount of deposits as they mature. However, recent disruptions in the credit markets have resulted in a highly price-competitive market for certificates of deposit. These rates currently exceed alternative costs of borrowings and are high compared to historical spreads to U.S. Treasury note rates. Additionally, since loan demand continues to slow, management has

been reluctant to offer rates in excess of wholesale borrowing costs. This has resulted in some deposit runoff as customers are moving their maturing balances to competitors at a higher pace than the Bank has historically experienced.

At June 30, 2009, the Bank maintained a line of credit with the FHLB of Seattle equal to 40% of total assets to the extent the Bank provides qualifying collateral and holds sufficient FHLB stock. At June 30, 2009, the Bank was in compliance with the collateral requirements and \$169.7 million of the line of credit was available. The Bank is highly dependent on the FHLB of Seattle to provide the primary source of wholesale funding for immediate liquidity

and borrowing needs. The failure of the FHLB of Seattle or the FHLB system in general, may materially impair the Company's ability to meet our growth plans or to meet short and long-term liquidity demands. However, the Company's mortgage backed securities are marketable and could be sold to obtain cash to meet liquidity demands should access to FHLB funding be impaired. Additionally, the Bank could access funding from the Discount Window at the Federal Reserve Bank of San Francisco or through the origination of out of market brokered deposits.

During the second quarter of fiscal year 2009, the Bank was notified by a correspondent bank that the Bank's \$10.0 million unsecured federal funds purchased line was suspended due to the increase in the Bank's nonperforming assets. This line was available on a secured-borrowing basis at June 30, 2009. The Bank had no balances drawn on the line of credit and management does not believe this has a material impact on the Bank's liquidity position or on the ability of management to execute the Company's strategic growth plan.

Off-Balance Sheet Arrangements. The Bank is party to financial instruments with off-balance sheet risk in the normal course of business in order to meet the financing needs of the Bank's customers. These financial instruments generally include commitments to originate mortgage, commercial and consumer loans, and involve to varying degrees, elements of credit and interest rate risk in excess of amounts recognized in the consolidated balance sheets. The Bank's maximum exposure to credit loss in the event of nonperformance by the borrower is represented by the contractual amount of those instruments. Because some commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The same credit policies are used in making commitments as are used for on-balance sheet instruments. Collateral is required in instances where deemed necessary.

Undisbursed balances of loans closed include funds not disbursed but committed for construction projects. Unused lines of credit include funds not disbursed, but committed for, home equity, commercial and consumer lines of credit.

Commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. Those guarantees are primarily used to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

The following is a summary of commitments and contingent liabilities with off-balance sheet risks as of June 30, 2009:

| | Contract or Notional Amount |
|--|-----------------------------------|
| | (in thousands) |
| Commitments to originate loans: | |
| Fixed rate | \$ 8,109 |
| Adjustable rate | 3,713 |
| Undisbursed balance of loans closed | 6,919 |
| Unused lines of credit | 35,291 |
| Commercial letters of credit | 137 |
| Total | \$ 54,169 |

Capital. Consistent with the Bank's goal to operate a sound and profitable financial organization, efforts are ongoing to actively seek to maintain a "well capitalized" institution in accordance with regulatory standards. The Bank's total regulatory capital was \$140.1 million at June 30, 2009, or 21.9%, of total assets on that date. As of June 30, 2009, the Bank exceeded all regulatory capital requirements. The Bank's regulatory capital ratios at June 30, 2009 were as follows: Tier 1 capital 21.9%; Tier 1 (core) risk-based capital 32.3%; and total risk-based capital 33.6%. The applicable regulatory capital requirements to be considered well capitalized are 5%, 6% and 10%, respectively.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Company's Board of Directors has established an asset and liability management policy to guide management in maximizing net interest spread by managing the differences in terms between interest-earning assets and interest-bearing liabilities while maintaining acceptable levels of liquidity, capital adequacy, interest rate sensitivity, credit risk and profitability. The Asset/Liability Management Committee, consisting of certain members of senior management, communicate, coordinate and manage asset/liability positions consistent with the business plan and Board-approved policies, as well as to price savings and lending products, and to develop new products.

One of the Bank's primary financial objectives is to generate ongoing profitability. The Bank's profitability depends primarily on its net interest income, which is the difference between the income it receives on its loan and investment portfolio and its cost of funds, which consists of interest paid on deposits and borrowings. The rates the Company earns on assets and pays on liabilities generally are established contractually for a period of time. Market interest rates change over time. The Bank's loans generally have longer maturities than the deposits. Accordingly, the Company's results of operations, like those of other financial institutions, are affected by changes in interest rates and the interest rate sensitivity of assets and liabilities. The Bank measures its interest rate sensitivity on a quarterly basis using an internal model.

Management employs various strategies to manage the Company's interest rate sensitivity including: (1) selling long-term fixed-rate mortgage loans in the secondary market; (2) borrowing intermediate to long-term funds at fixed rates from the FHLB; (3) originating commercial and consumer loans at shorter maturities or at variable rates; (4) originating adjustable rate mortgage loans; (5) appropriately modifying loan and deposit pricing to capitalize on the then current market opportunities; and (6) increasing lower cost core deposits, such as savings and checking accounts. At March 31, 2009, the Company had no off-balance sheet derivative financial instruments, and the Bank did not maintain a trading account for any class of financial instruments or engage in hedging activities or purchase high risk derivative instruments. Furthermore, the Company is not subject to foreign currency exchange rate risk or commodity price risk.

There has not been any material change in the market risk disclosures contained in the Company's 2008 Form 10-K.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures.

An evaluation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")) was carried out under the supervision and with the participation of the Company's Chief Executive Officer, Chief Financial Officer, and other members of the Company's management team as of the end of the period covered by this quarterly report. The Company's Chief Executive Officer and Chief Financial Officer concluded that as of June 30, 2009, the Company's disclosure controls and procedures were effective in ensuring that the information required to be disclosed by the Company in the reports it files or submits under the Act is (i) accumulated and communicated to the Company's management (including the Chief Executive Officer and Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms.

(b) Changes in Internal Controls.

There have been no changes in the Company's internal control over financial reporting (as defined in 13a-15(f) of the Exchange Act) that occurred during the quarter ended June 30, 2009, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. A number of internal control

procedures were, however, modified during the quarter in conjunction with the Bank's internal control testing. The Company also continued to implement suggestions from its internal auditor and independent auditors to strengthen existing controls.

The Company intends to continually review and evaluate the design and effectiveness of its disclosure controls and procedures and to improve its controls and procedures over time and to correct any deficiencies that it may discover in the future. The goal is to ensure that senior management has timely access to all material financial and non-

financial information concerning the Company's business. While the Company believes the present design of its disclosure controls and procedures is effective to achieve its goal, future events affecting its business may cause the Company to modify its disclosure controls and procedures. The Company does not expect that its disclosure controls and procedures and internal control over financial reporting will prevent every error or instance of fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns in controls or procedures can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, the Company is engaged in legal proceedings in the ordinary course of business, none of which are currently considered to have a material impact on the Company's financial position or results of operations.

Item 1A. Risk Factors

The Company believes there have been no significant changes in risk factors compared to the factors identified in the Company's Annual Report on Form 10-K for the year ended September 30, 2009, and Form 10-Q for the period ended March 31, 2009

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

(a) Not applicable.

(b) Not applicable.

(c) Not applicable.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5. Other Information

Not applicable.

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Item 6. Exhibits

- 2.1 Plan of Conversion and Reorganization (1)
- 3.1 Articles of Incorporation of the Registrant (2)
- 3.2 Bylaws of the Registrant (2)
- 10.1 Amended Employment Agreement entered into by Home Federal Bancorp, Inc. with Len E. Williams(8)
- 10.2 Amended Severance Agreement with Eric S. Nadeau(8)
- 10.3 Amended Severance Agreement with Steven D. Emerson(8)
- 10.4 Amended Severance Agreement with Steven K. Eyre(8)
- 10.5 Form of Home Federal Bank Employee Severance Compensation Plan (3)
- 10.6 Form of Director Indexed Retirement Agreement entered into by Home Federal Savings and Loan Association of Nampa with each of its Directors (2)
- 10.7 Form of Director Deferred Incentive Agreement entered into by Home Federal Savings and Loan Association of Nampa with each of its Directors (2)
- 10.8 Form of Executive Deferred Incentive Agreement, and amendment thereto, entered into by Home Federal Savings and Loan Association of Nampa with Daniel L. Stevens, Robert A. Schoelkoph, and Lynn A. Sander (2)
- 10.9 Form of Amended and Restated Salary Continuation Agreement entered into by Home Federal Savings and Loan Association of Nampa with Daniel L. Stevens (2)
- 10.10 Amended and Restated Salary Continuation Agreement entered into by Home Federal Savings and Loan Association of Nampa with Len E. Williams(8)
- 10.11 Amended and Restated Salary Continuation Agreement entered into by Home Federal Savings and Loan Association of Nampa with Eric S. Nadeau(8)
- 10.12 Amended and Restated Salary Continuation Agreement entered into by Home Federal Savings and Loan Association of Nampa with Steven D. Emerson(8)
- 10.13 Amended and Restated Salary Continuation Agreement entered into by Home Federal Savings and Loan Association of Nampa with Steven K. Eyre(8)
- 10.14 2005 Stock Option and Incentive Plan approved by stockholders on June 23, 2005 and Form of Incentive Stock Option Agreement and Non-Qualified Stock Option Agreement (4)
- 10.15 2005 Recognition and Retention Plan approved by stockholders on June 23, 2005 and Form of Award Agreement (4)
- 10.15 Form of new Director Retirement Plan entered into by Home Federal Bank with each of its Directors (5)
- 10.16 Transition Agreement with Daniel L. Stevens (6)
- 10.17 2008 Equity Incentive Plan (7)
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act *
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act *
- 32 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act *

(1) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated May 11, 2007

(2) Filed as an exhibit to the Registrant's Registration Statement on Form S-1 (333-146289)

(3) Filed as an exhibit to the Registrant's Quarterly Report on Form 10-Q for the quarter ended December 31, 2008

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- (4) Filed as an exhibit to the Registrant's Registration Statement on Form S-8 (333-127858)
- (5) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated October 21, 2005
- (6) Filed as an exhibit to the Registrant's Current Report on Form 8-K dated August 21, 2006
- (7) Filed as an exhibit to the Registrant's Registration Statement on Form S-8 (333-157540)
- (8) Filed as an exhibit to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2009

* Filed herewith

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.

Home Federal Bancorp, Inc.

Date: August 7, 2009

/s/Len E. Williams
Len E. Williams
President and
Chief Executive Officer
(Principal Executive Officer)

Date: August 7, 2009

/s/Eric S. Nadeau
Eric S. Nadeau
Executive Vice President and
Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act
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